Customer Churn: So much data, So few insights.

If you are a member of the leadership team of a SaaS company, you know there are a few key metrics that your board of directors, investors, and industry analysts will monitor to determine the value of your business. In addition to Annual Recurring Revenue (ARR) and Monthly Recurring Revenue (MRR), three of the more critical metrics include:

- Cost to acquire a customer (CAC)
- Lifetime value of the customer (LTV)
- Customer Churn

Many venture capitalists and financial analysts focus on the ratio between LTV and CAC to identify strong performers. Simply stated, investors are interested in companies that can create a stream of revenue that is at least 3x their cost of acquiring a customer.

Still, even when organizations generate positive LTV, CAC, and other metrics, there is one item that has the capability to negatively affect all these outcomes: Customer Churn.

The Impact of Customer Churn

The beauty of the SaaS business model is the continuous monthly stream of revenue from the clients using your products. The risk of this business model is that clients are merely renting your software, and if you fail to deliver on the promised value, they can simply walk away. This act of unsatisfied clients walking away from your business is what experts refer to as customer churn.

According to a recent Key Bank Survey of 385 SaaS companies, the median customer churn is 21%, which is not promising for companies attempting to capitalize on existing relationships over time.

Customer churn impacts revenue—including ARR and MRR—as well as CAC and LTV metrics. From this standpoint, churn is essentially negative revenue, because when the client leaves, they take their MRR and ARR with them. What's more, depending on how soon quickly they choose to terminate their contract after signing, they may not provide enough lifetime value to even cover your cost of sales, let alone provide you with the desired 3X return on investment. This results in unexpected costs that must be put into replacing the revenue you already had, thus negatively impacting your CAC and compounding the impact of the churn.

Managing The Negative Impact

Customer churn can make a large impact on an organization, and when it is at an above average rate, it can send shockwaves through your company. For that reason, unless you implement a structured approach to understanding customer churn, you run the risk of creating a scenario where members of your management team assign responsibility or "blame" for lost customers based on opinions and theories instead of assigning ownership based on facts. This undermines management team cohesion and delays addressing the real issues that are causing the churn to begin with.

The Role of Cohort Analysis in Customer Churn

One way of examining customer churn is through Cohort Analysis. Cohort analysis is the process of examining your customer data in order to identify patterns associated with churned customers. It involves comparing those patterns with trends of similar customers that have not churned, in order to help you understand the root cause of the loss.

While cohort analysis can certainly provide basic insights into your churn, the real value comes from engaging directly with lost clients in order to get at the underlying issues driving their departure.

The Value of Personal Analysis

While derived data from cohort analysis can provide some direction, a person-to-person conversation is the best way to formulate a deeper understanding of the root cause behind your customer's decision to stop using your products.

The Benefit of Outsourcing These Tough Conversations

Since the feedback is likely to identify one or more of your operating groups as a contributing factor in the churn, it is best to outsource this customer insight work to an independent, third-party firm. Consider long-time veterans of the Customer Experience Analysis world for this outsourced objectivity, such as Marlborough Street Partners or Blue Lemon Partners, which both specialize in conducting this type of customer-facing research.

There are many benefits to utilizing a consultant in your business, but when it comes to discussions of churn, an external team with the proper training, language, and the right amount of distance from you and your customers is really the only method for developing a truly unbiased assessment of the situation at hand. In addition, external consulting organizations can also provide an impartial point of view as you share the gathered feedback with your team, a practice equally as vital to this overall discussion as the time spent interviewing customers themselves. Groups that are trained to handle these types of difficult feedback conversations are actually equipped with the skills and expertise to translate the difficult truths or data into actionable insights that feel less like a discussion of loss and blame, and more like a conversation of potential for the future.

A Customer's Perspective

When John Murdoch took over the role of CEO at Centage, one of his first priorities was to better understand the most important issues that he and his management team should focus upon in order to minimize churn. As he says:

> "Like most SaaS businesses we put a high focus on customer retention. When we started the process of defining a strategy to minimize churn, there were differing opinions among the management team with regard to the root causes. While our cohort analysis provided valuable insight, the majority of our data was internally generated by our staff. We lacked the customer's direct voice to isolate the underlying issues leading to their choice to churn. We engaged MSP/Blue Lemon Partners to understand churn from our customer's perspective. The process provided valuable insights that validated some of our opinions and uncovered areas for us to improve. In addition, the simple process of engaging with our clients on how to improve our service resulted in several clients engaging with us again. I feel we got tremendous value from this process, and understand our customers better."

Defining The Issues at Hand

There is seldom just one issue impacting churn. In my experience—which includes a role as President and Chief Operating Officer of a SaaS payments and attribution business, as well as a number of other C-level roles across a variety of other industries—the potential issues contributing to churn can be quite varied, and can include:

- An unorganized or otherwise unsatisfactory customer onboarding process
- Issues with product usability and features
- Problems with business terms and pricing
- Unrealistic expectations set in the sales process

Yet, as diverse as these issues are, they all have one thing in common: They can't be addressed until they are identified and the only real way to do that is by engaging your customers.

Many organizations suffer from an inwardly focused culture but those organizations that are truly driven to become world class SaaS businesses know that, at the end of the day, it is the customer's voice that matters most.

By factoring your customer's voice into your strategy to minimize customer churn, you will greatly improve your ability to address the real issues affecting your SaaS business.

—by Mike DiFranza, Principal

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