BUSINESS GUIDE

How CFOs Can Reverse Customer Churn

Changing buying habits are eroding customer lifetime value. Here's how to fix it.

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CFOs, Churn and CLV: A Survival Story

We all know it's more expensive to acquire new customers than to keep current clients. Experts agree it'll cost anywhere from five to 15 times more, depending on the competitiveness of your industry. Improving customer retention rates by just 5% increases profits by 25% to 95%.

Plus, the more customers you lose, the harder marketing and sales must work to meet goals.

And churn doesn't just impact revenue. A higher net retention rate hikes the valuation of your company compared with competitors with similar annual growth. Lots of investors use churn rates to evaluate the overall health of an organization and its chances of thriving. All else being equal, which would you invest in: Company A that loses 10% of its customers annually or Company B that sheds 25%?

High churn rates are just bad news all around. So it's no wonder smart companies devote time, money and thought to keeping current clients. But what can CFOs do to help? After all, you're likely not directly involved in the day-to-day building and maintaining of customer relationships and may not be in a position to pick up on early warning signs of problems.

The answer: Help department leads track the right metrics, conduct the right analyses to predict churn and hold their teams accountable to the right KPIs.

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CHAPTER 1

The CFO Churn Challenge

Finance professionals are in a position to translate raw churn rates into KPIs that provide empirical indicators teams can act on. For CFOs new to this idea, the best way to set an initial churn benchmark is in aggregate, calculated on a monthly, quarterly or annual basis.

The formula for calculating basic monthly customer churn is:

$$\text{Monthly Customer Churn} = \frac{\text{Lost Customers in Month}}{\text{Previous Month's Customer Balance}}$$

So if you began the month with 100 customers and lost 10 of them, your churn ratio is 10%. To smooth out seasonal or other fluctuations, it may be more valuable to track churn over the trailing twelve months in a year-over-year approach:

$$\text{TTM Customer Churn} = \frac{\text{Sum of Lost Customers Over Trailing 12 Months}}{\text{Customer Balance Prior to 12 Months}}$$

You can perform this calculation at any time during the year by taking the number of customers you had 12 months ago and dividing by the total number lost through the current date. But keep in mind that there are factors in play when it comes to calculating churn, and TTM analysis may be skewed if you released significant new features, signed up a bunch of new customers and thus raised your customer count or moved into new geographies or verticals. The point is to get a sense of how your customer base as a whole is reacting to your current products, so don't focus too much on TTM if your offerings or focus changed significantly in the past 12 months.

Especially in software-as-a-service (SaaS) or other contracted or subscribed services, where monthly recurring revenue (MRR)/annual recurring revenue (ARR) is the primary source of income, it may be more useful to measure churn in terms of dollars rather than number of customers.

The ARR formula is:

$$\text{Monthly Dollar Churn} = \frac{\text{Lost ARR in Month}}{\text{Previous Month's ARR Balance}}$$

And for ARR, the trailing twelve months version is:

$$\text{TTM Dollar Churn} = \frac{\text{Sum of Lost ARR Over Trailing 12 Months}}{\text{ARR Balance Prior to 12 Months}}$$

Churn tells you which way your business is going: A monthly churn rate of just 4% means you're shedding about half your clients per year. You need to know why so you can take action.

No change in total customers could mean you're doing a great job at retention. Or, you could be shedding clients about as fast as sales signs on new ones. If you lose as many customers as you bring on, you have a major problem.

CHAPTER 2

Three Comparative Cohorts

To understand why customers quit you, CFOs can use data to segment leavers by characteristics. By creating and comparing cohorts, you may help your colleagues spot patterns and commonalities. Here are some examples, though this list is certainly not exhaustive. You can slice the leaver pie in as many pieces as makes sense.

Salesperson

This gotcha might not be immediately obvious, but it's fairly common. Retention is usually a function of the quality and usefulness of service delivered. High churn may mean you have a salesperson who is exaggerating or mischaracterizing the results customers can expect just to make a sale. By calculating churn for each salesperson, you may find that a team member is overpromising and thus your product is under-delivering — a main reason customers cancel.

Acquisition Date

Segmenting by customer longevity may provide insights. If many customers cancel after a similar period of time, say three or six months, that suggests they aren't realizing value as quickly as expected. Maybe a large number of customers signed up for your service immediately after a public event, such as the announcement of a data breach or natural disaster, in the case of a data protection company, then dropped after the hype wore off.

Or take the real-world case of Netflix, whose subscriber base exploded during the pandemic as millions of people were stuck at home watching television. Its recent earnings report revealed the loss of 1 million subscribers in its latest quarter, and the company has seen a 66% decline in its stock price this year as the world gets back to being outside the home.

Related, if you can zero in on campaigns or events that drove sales spikes, then see that many of those buyers dropped, you may be able to spot opportunities to add features to increase retention.

Learn More About CRM

- **CRM 101: The Ultimate Guide:** CRM technology provides a single source of information that helps salespeople, marketers and customer service groups drive more revenue, increase productivity, keep track of the health of the business and, most importantly, build lasting customer relationships.
- **CEM vs. CRM:** Adopting a consumer-centric approach is paramount to the success of your business. It leads to happier customers, who, in turn, become more loyal to your brand, delivering increased revenue.
- **CRM Dashboard: KPIs, Examples and Template:** Here's how CRM dashboards can help a business's sales, marketing and customer service departments contribute to bottom-line business growth.

Behavioral

Take a look at exactly how customers use your product. Are there features they rarely take advantage of? Is there a lag between when they sign up and when they actually start using the product? Does usage drop off at a specific time point after onboarding? Are they paying for unused licenses or seats, indicating a lack of uptake?

Analyzing how customers use your product or service can illuminate why they aren't renewing. But to characterize feature use, you have to track it.

You may not identify causal relationships between specific behaviors or characteristics and customer retention until you combine insights. For instance, say a big, headline-making security breach in the supply chain industry led to lots of new inquiries. Those leads filtered through certain salespeople, who used the breach as a conversation starter. Then those clients used, or didn't, your hallmark features to improve their security postures. It becomes a Venn diagram that yields insights, if you have enough data.

If you don't have a solid system to monitor your customers' behavior, from onboarding to renewal (or lack thereof), you're missing insights into the reasons for churn.

One place to start: your customer relationship management (CRM) platform. The trick is to fully use its capabilities after the sale rather than just to track prospects.

CHAPTER 3

Not All Revenue Is Good Revenue

Some customers aren't a profitable fit for your business model. A good customer is one that pays a reasonable fee for the value of services rendered. An accounting or IT services firm, for example, that offers bundles of services for a monthly fee may find that some customers take advantage by regularly demanding work in excess of what they're paying for.

This can happen no matter how well you train your sales teams and solution architects. A customer may have unique needs that fit within the definition of your agreement but cause you to spend more to service them than they've paid you. For a one-time incident that won't likely recur, it may prove worthwhile to keep that customer aboard. When you go beyond the call of duty, they will appreciate it and hopefully reward you further down the road.

But if incidents prove to be a consistent, repeating, intentional pattern of behavior, you have a bad customer. Ideally, your standard contract allows you to "fire" clients, or at least to not renew agreements with the same terms. Alternatively, letting them churn is a viable route to increased profits. No one wants to expend time and energy on a losing bet. Do your analysis, and drop customers that cost you money.

3 Customer Lifetime Value Considerations

CFOs can assist in calculating what it costs to acquire a customer versus how much you can expect to earn. That's a reasonably straightforward calculation, as we'll discuss. But there are three factors ARR/MRR companies need to consider.

1. **70%+ of a buyer's journey** is completed before a prospect makes contact with a salesperson, so include marketing spend, such as Google AdWords, social media and content marketing. If you use a sales channel like AWS Marketplace, is that cost taken into account?
2. **If your product or service is 'white glove,'** how much on average do you spend for your sales force to hobnob with prospects? This includes time, not just line expenditures.
3. **Do you deploy pre-sales engineers** or the equivalent to seal the deal? That's another customer acquisition cost.

CHAPTER 4

The Quality Connection

The only way to reliably retain and increase your revenue from customers is to provide the value promised by sales and an ongoing stellar experience. Many call this likelihood a customer will renew or even increase spend “stickiness.”

The “stickier” you are, the more desirable it is to stay, the higher your customer lifetime value (CLV) and the lower your churn.

Of course, customer satisfaction may come with increased overhead. Do you employ automated software to handle first-level support calls? That’s a cost. Do you have an engineer dedicated to customer requests for features and benefits? That’s a cost. What about your marketing department? If you’re working smart, your marketing people spend time on upsell and cross-sell efforts, all of which come with a cost. Don’t forget your account management teams, customer success teams and other service departments.

CLV encompasses more line items with subscription-based companies than in other forms of commerce.

Once you have all your inputs, CLV is fairly simple to calculate: Total up the loaded cost of the goods and services you sold to a customer and subtract that from what you were paid. This calculation tells you if a client is profitable. Taken in aggregate, it can show you how much ROI (positive or negative) your marketing, sales and customer success teams deliver.

Formulas useful to the CFO include:

$$\textbf{CLV} = \frac{\text{ARPA}}{\text{Churn Rate}}$$

*For the above, make sure that both average revenue per account and churn rate are calculated for the same time period, usually monthly, quarterly or annually.

and

$$\textbf{CLV} = \frac{(\text{ARPA} \times \text{Gross Margin \%})}{\text{Revenue Churn Rate}}$$

Don’t forget that CLV can differ from product to product or service to service, since those all come in at different price points. To get even more granular, calculate your CLV across multiple cohorts so you have a clear idea of how valuable each type of customer is to your business.

CHAPTER 5

Revenue Retention

As a CFO, the filter through which you look at churn is the inflow or outflow of cash. Investors and analysts like retention and may not even look at the actual number of customers. They're far more interested in the predictability of your growth.

While they are also, more often than not, interested in total revenue movement from period to period, you need to look at your change in revenue as the sum of four discrete sales motions:

- Sales to new customers: You've created a new customer and generated revenue.
- Expansions and upsells: Existing customers increase their consumption of your services and generate more revenue.
- Downgrades: Existing customers use less of your services, often due to their own business downturns or changing needs.
- Churn (lost customers): Customers who no longer consume your services, representing revenue last month, quarter or year, but not going forward.

Arrive at your net revenue increase or decrease by adding new and expansion revenue and subtracting lost revenue from downgrades and churn. As you calculate this month by month, you'll see a trend emerging, which is your average customer value, or ACV. At minimum, you must keep this number above zero. Ideally, it will always be moving upward.

CHAPTER 6

Look to the Customer Lifecycle to Minimize Churn

Fortunately, opportunities to reduce churn exist at every stage of the customer lifecycle. For purposes of this article, we begin when a prospect becomes a customer, as opposed to calculating pre-sales marketing metrics.

Deployment and Implementation

After a sale comes the heavy lifting. How easy is it to do business with you? The first experience customers have is when you or they install your product. If they have to troubleshoot, if it takes an uncharacteristically long time or if they have to reconfigure too many other systems or processes to make it work, you'll turn them off. One fix can be creating adoption guides, working with implementation partners and offering professional services to ensure success.

Onboarding and Adoption

There are many reasons a customer's employees may not even open your product, and all of them are your concern. Track average time to implement, feature sets used and similar metrics to identify when a customer isn't getting the experience they should be. Are seats or licenses a customer pays for sitting idle? If so, why? Simply taking the time to ask and offer some education can decrease churn.

Early-Stage Support Calls

Track the number of customers that call in for support within the first few weeks after purchase. If it's high, it's a sign that something is incomplete, incorrect or confusing about your onboarding process. Who is responsible for user implementation success? If you're not sure, churn may be higher than it needs to be.

Quality onboarding requires just as much planning and development as product design and deployment do.

Ongoing Tech Support

The more proactive your technical support team is, the happier customers will be. Just because they adopt readily doesn't mean they won't hit roadblocks. Stay in front of that. Users all too often keep silent about their dissatisfaction and just push on. Expose those frustrations and resolve them and, again, end users become your best salespeople with their management.

Account Management

Suppose for a moment you're a SaaS provider or reseller that has installed a system for a customer. You've completed deployment smoothly. User training went well and adoption was immediately high.

As the quarter proceeds, you notice log-ins dropping off, and you aren't sure why. When it comes time to renew but the customer chooses to leave, you won't have any insight into what went wrong.

This is completely avoidable. We advise monthly or quarterly business reviews (QBRs) to reduce churn. Beyond providing a common measuring stick and keeping your SLA fulfillment success top of mind for customers, each meeting represents an excellent opportunity to expand your share of wallet. QBRs also put your people in front of their people and cement the relationship, helping to assure renewal and expansion.

There's no better way to strengthen your customer relationships than regular QBR meetings. If your company isn't a candidate for regular reviews, at least take time to ask customers how they feel about your offerings.

CHAPTER 7

Other Ways to Track Customer Satisfaction

Particularly for subscription services, nothing matters more in minimizing churn than customer satisfaction. But you'll only learn how happy clients are by asking (see: QBRs).

Here are other ways to drill down into why customers stay or leave.

Gap Surveys

You may be really great at providing documentation. What you may not realize, however, is that customers don't use your documentation, nor do they care about it.

You're really good at something they don't care about.

"Gap" surveys start by asking how important a given issue is to the buyer. Then they ask how you performed on that issue. Now you know what's really important to your customer, which is hugely valuable, and you also know how well they feel you did on what's important to them.

Net Promoter Score (NPS)

Borrowing a page from sales management here, we teach salespeople that the most valuable thing they get from a sale is not the commission, it's a referral to the next customer — though the commission is good, too.

The equivalent here in terms of measuring whether current customers are happy is the Net Promoter Score (NPS), which is a simple two-question survey. The first is, "How likely are you to recommend our product to a friend or colleague?" scored 0-10, and the second is, "Why?"

NPS promoters score 9 or 10, passives score 7 or 8 and detractors score 6 or below.

Net Promoter Score (NPS) = Percentage of Promoters − The Percentage of Detractors

As CFO, you'll be most interested in the distribution of customer end users among these three categories. If a greater percentage are recommenders, you should see that reflected in their loyalty, customer satisfaction ratings and spending. If the majority are detractors, it's time for a management meeting to figure out what's wrong so you can correct it before churn increases.

In fact, identifying detractors may be even more valuable than identifying your promoters. It helps you focus your attention and prevent churn by reversing negative momentum.

Corrective action may be as simple as outreach to detractor customers. What about your service is not to their satisfaction? What would they like to see done differently?

Learn More

5 Ways to Improve Your Net Promoter Score. NPS is only one customer success metric you should track. Here are KPIs that help you evaluate your customers' satisfaction with your products or services — and likeliness to churn.

CHAPTER 8

What the CFO Brings to the Table

The Heiselberg Uncertainty Principle tells us that the fact that a thing is being measured affects the thing being measured. In this case, the actions of the CFO to share insights from analyzing churn metrics should impact the performance of those who manage customer relationships and service delivery.

There is, after all, no more impactful metric than money. Everybody in a company knows they are measured, directly or indirectly, by how much they positively increase revenue and earnings.

Armed with churn calculations, both accounts and revenue, along with the company's satisfaction ratings and Net Promoter Scores, CFOs can guide department leaders to translate what's most important to the enterprise to what's important to every employee of that enterprise. This is among the most difficult challenges any leadership team faces: aligning employee priorities with those of the company and its stakeholders.

As CFO, churn metrics are a valuable tool for keeping everyone's attention fixed on customer retention, which is the best way to assure continuing revenue and profit growth.

Learn More

- **Customer Attrition (Churn) Explained.** Monitoring customer attrition is a best practice for any business. It can help organizations understand a particularly relevant form of ROI, or return on investment — return on customer acquisition investment (ROCAI).
- **Customer Churn Analysis: Why It's Important and How to Do It.** Understanding why customers do — or don't — purchase more goods or services is essential to success for any company. Gaining this insight begins with analyzing how many clients are taking their business elsewhere. Then, you can dig in to find commonalities among leavers, identify opportunities to improve and avoid losing additional customers.
- **The Starter Guide to Using Data Analysis in Your Business.** Every company is a data company, or so the saying goes. Businesses of varying sizes and across industries have differing needs and levels of data analysis proficiency.

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