Insights from Investors: Key Performance Indicators for SaaS Companies

SaaSOPTICS® FULCRUM EQUITY PARTNERS

Introduction

Traditional financial metrics and legacy ERP systems don't provide adequate insights into the performance and growth of SaaS businesses. That's because these metrics and systems were created for companies selling "one-time" products and simply don't work for a recurring revenue business model.

We understand — we've spent the last 10 years building our subscription management platform to help SaaS businesses better manage the recurring relationships with their subscribers and streamline the entire customer life cycle.

We teamed up with our Series A lead, Fulcrum Equity Partners, to give you a 360-degree view of the key SaaS metrics. Fulcrum is a growth equity firm focused on providing expansion capital, operating expertise and relationships to rapidly growing companies. Fulcrum invests in SaaS businesses — as far back as the early 2000s when they were called ASPs — partners with other SaaS funds and has sold companies to top strategics, including IBM and Oracle.

Together, we're leveraging our combined experience to share insights on the key performance indicators to scale a SaaS business. The journey to reliable SaaS financial operations and future investment capital starts with measuring what matters most.

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Part 1:

Revenue Growth Performance Metrics

Revenue growth performance metrics provide visibility into the health of your business and its potential for growth. You're likely familiar with these, but we'll recap what they are just in case.

Foundational metrics you should know:

- **MRR and ARR**
- **ACV**
- **CAC, CLV and CAC Payback**

MRR or ARR

Monthly Recurring Revenue **(MRR) or** Annual Recurring Revenue (ARR) **is the value of the contracted recurring revenue components of your term** subscriptions normalized to a one-month or annual period.

We break ARR/MRR down into the following categories:

- **New ARR/MRR –** new sales to new customers.
- **Expansion ARR/MRR –** existing customers who expanded their subscriptions or licensed additional products or modules.
- **Contracted ARR/MRR –** existing customers who downgraded their subscription and/or reduced their consumption.
- **Canceled ARR/MRR –** existing customers who canceled their subscription.

These components are frequently measured in both absolute value and relative value and are often presented in the context of incremental changes from period to period.

Average Contract Value

Average Contract Value (ACV) is a measure of the average revenue generated per customer and is usually calculated on an annual basis.

A growing or contracting ACV is a good indicator of the value you are providing to customers. This metric is also a critical input for your sales and marketing plan and provides visibility into how many leads (MQLs) and opportunities (SQLs) are needed to achieve your plan's goals.

$$\text{ACV} = \frac{\textbf{Current ARR}}{\textbf{Current \# of Customers}}$$

Customer Acquisition Costs

These metrics help you make important decisions about how you allocate sales and marketing spend and are valuable in understanding how much your company is making from each new customer and how long it takes to surpass the money you spent to acquire that customer.

- **Customer Acquisitions Costs (CAC) –** total sales and marketing resources associated with acquiring a new customer.
- **Customer Lifetime Value (CLV) –** average revenue or profit a customer will generate before they churn.
- **CAC Payback –** the time it takes in months to recoup the cost of acquiring a customer.

You can also measure your CLV against CAC, which will tell you what you can expect to net for every dollar you spend to acquire a customer.

The Investor’s Point of View:
Revenue Growth Performance Metrics

MRR or ARR

Quarter-over-quarter bookings growth provides valuable insights into the momentum and velocity of the business and growth investors consider it to be one of the best leading indicators of overall business performance.

Average Contract Value

Tracking ACV over time is valuable to understand evolving customer behaviors. It helps drive decision making for sales and marketing strategies, customer success and retention strategies and your product road map.

ACV is also a useful metric to measure the success of land-and-expand growth strategies, upsell initiatives and a company’s ability to deliver more and more value to customers.

Customer Acquisition Costs

CAC, CLV and CAC payback are used to track and measure the performance of sales and marketing teams and are also extremely valuable in understanding the efficiency of a company’s growth model.

Investors will spend a significant amount of time in diligence analyzing the scalability of your sales and marketing organization, and these metrics are great validations that additional investment in sales and marketing activities will drive value creation.

Part 2:

Momentum and Velocity Metrics

- How many leads are we adding to the top of the funnel?
- Where are my leads coming from?
- What does the pipeline look like over time?
- What are my funnel conversion rates?
- How productive is my sales team in closing deals?

The answers to these questions will provide management teams and investors with higher predictability of future performance and help build more accurate forecasts.

Foundational metrics you should know:

- **Lead Generation**
- **Pipeline Conversion**
    - **MQLs**
    - **SQLs**

Lead Generation

Lead generation is the process of attracting quality prospects and moving them into the top of your funnel.

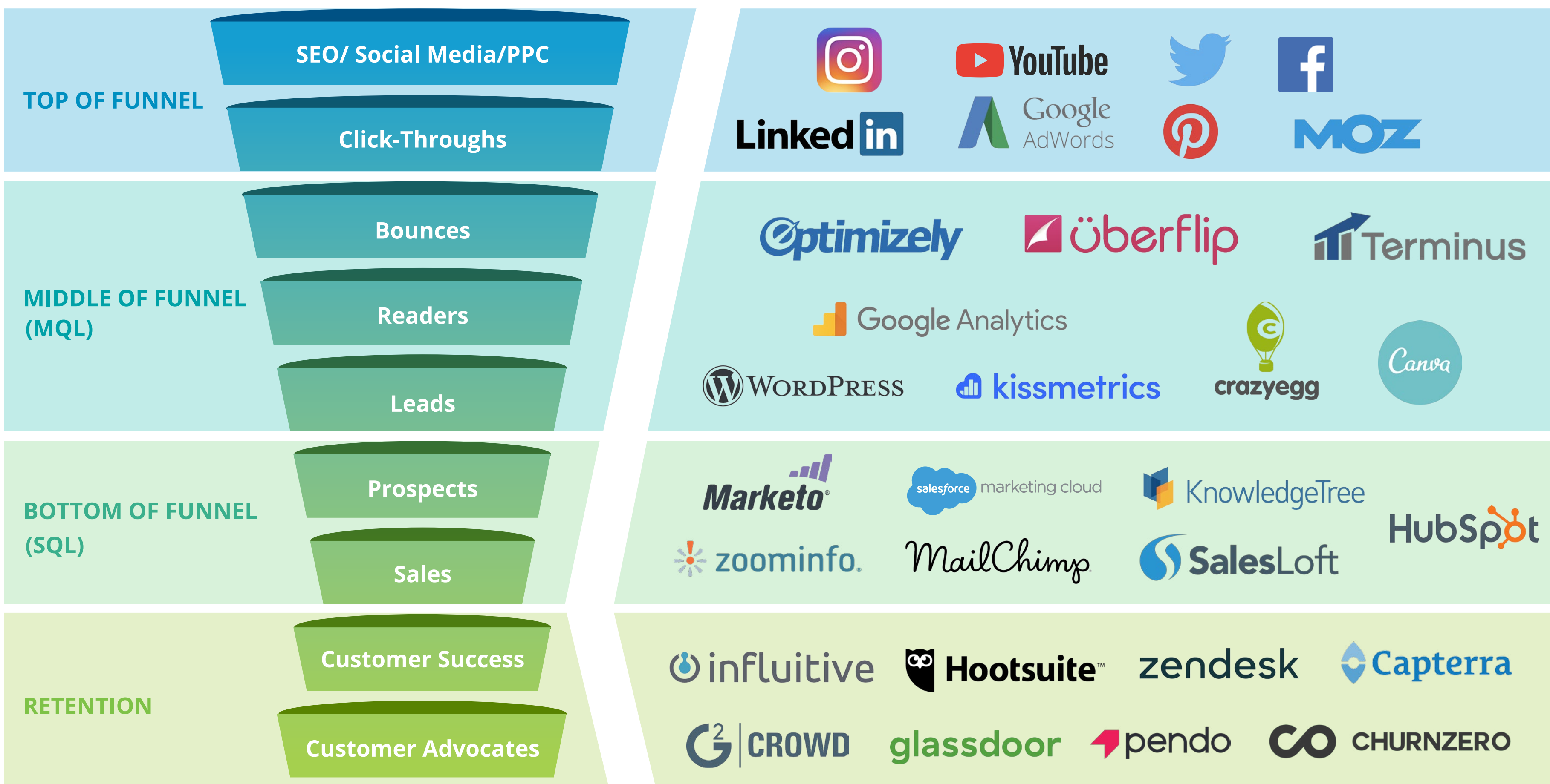
Consistently generating marketing qualified leads (MQLs) and sales qualified leads (SQLs) is essential for growing your SaaS companies. A true marketing “mix” will have a variety of different methods for acquiring new leads.

Tracking which methods and demand generation activities are producing the best results is important so you can weed out programs that aren’t working and continually replace them with more effective ones.

Pipeline Conversion

Once you're generating leads, you'll need to convert them into customers. A strong sales and marketing technology stack, sales process and content generation engine to engage and nurture buyers at every step of their buying process is critical for pipeline conversion.

Building agile sales and marketing teams that can test, iterate and refine your marketing and sales funnel tactics to drive increased conversion is critical.



The Investor’s Point of View:
Momentum and Velocity Metrics

Lead Generation and Pipeline Conversion

Accelerating rapid growth in a SaaS business involves lead generation, CRM, marketing automation and a strong understanding of your conversion metrics. Having an infrastructure in place to produce and track your pipeline of prospects and a history of converting those prospects into customers is critically important in raising capital.

Investors are looking for businesses that truly understand their sales and marketing funnel with strong lead generation and pipeline conversion rates that provide visibility, comfort and high predictability of future revenue growth.

Part 3:

Customer Success Metrics

As a subscription business, establishing positive relationships with your customers is vital. From onboarding and implementation to adoption and support, every touch point can impact whether or not you retain that customer over time. Measuring customer success and setting goals around those metrics is instrumental in growing your SaaS business.

These metrics are indicators for measuring the health of your customer base:

- **Churn and Retention**
- **Expansion Revenue**
- **Cohort Analysis**

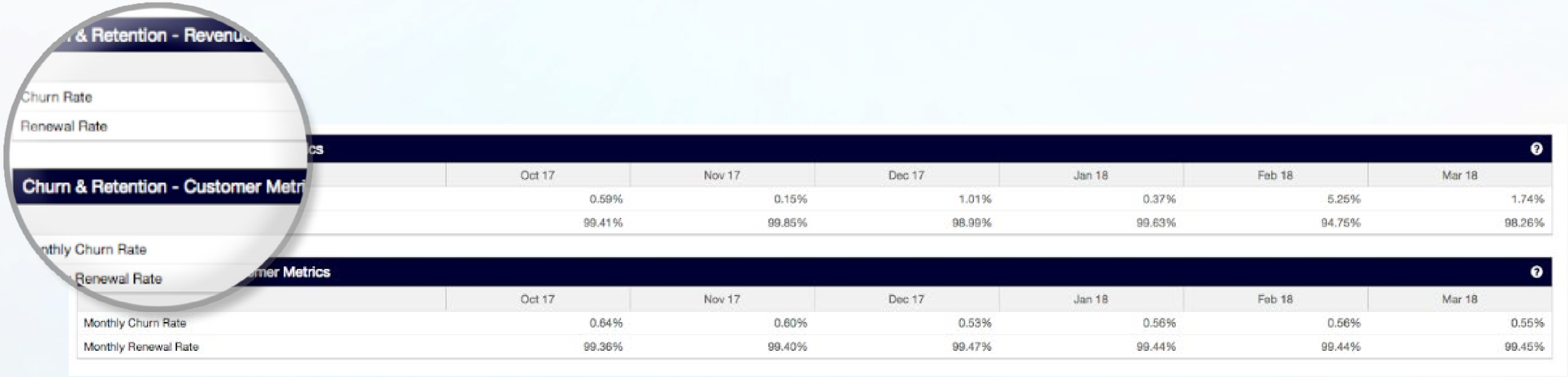
Churn and Retention

Churn can happen for a multitude of reasons, but as one of the most important indicators of the health of your business, you need to understand why. As your company expands and the size of your subscription base grows, the revenue lost to churn can also grow, requiring more bookings from new customers to replace what was lost. This can be a significant drag on growth. Here are two formulas commonly used to calculate churn.

$$\text{Net Churn} = \frac{\text{Sum of churn and contracted MRR - Sum of expansion MRR}}{\text{MRR at start of period}}$$

$$\text{Gross Churn} = \frac{\text{Sum of churn and contracted MRR}}{\text{MRR at start of period}}$$

Another common metric for analyzing retention is logo churn by replacing MRR in the formula above with number of customers. High churn usually indicates your product isn't meeting customer needs and expectations. With insight into the factors driving churn, you can take action, such as improving customer engagement and onboarding or making product tweaks that can improve customer retention.



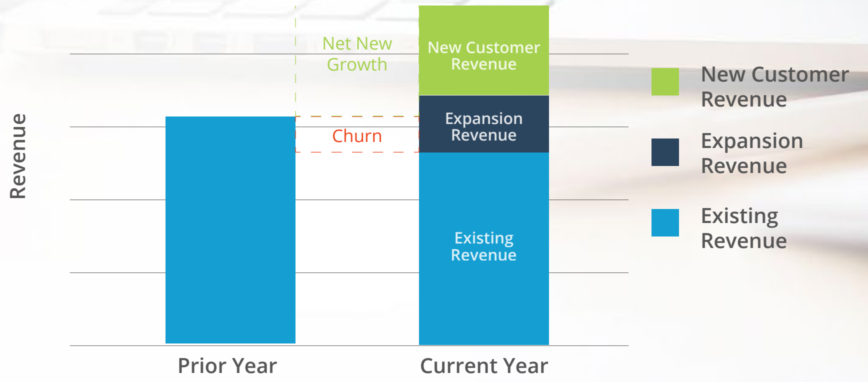
	Oct 17	Nov 17	Dec 17	Jan 18	Feb 18	Mar 18
	0.59%	0.15%	1.01%	0.37%	5.25%	1.74%
	99.41%	99.85%	98.99%	99.63%	94.75%	98.26%

mer Metrics	Oct 17	Nov 17	Dec 17	Jan 18	Feb 18	Mar 18
Monthly Churn Rate	0.64%	0.60%	0.53%	0.56%	0.56%	0.55%
Monthly Renewal Rate	99.36%	99.40%	99.47%	99.44%	99.44%	99.45%

Expansion/Upsell Revenue

Generating revenue from existing customers is a good indicator of whether they are receiving value from your product and expanding their use. Expansion revenue includes customers who upgrade to a more robust plan or those who pay for additional users or features.

When expansion revenue outpaces lost revenue from existing customers, you'll reach net negative churn—also known as the holy grail of SaaS. At that point, your recurring revenue is expanding without adding new customers.



Cohort Analysis

Grouping customers by product, vertical, sales channel, deal size, etc., also known as cohort analysis helps uncover trends in specific customer groups.

For example, if a large number of customers are churning in the first or second month, you may need to address your onboarding process. Emerging SaaS companies typically have customers that vary in size, so cohort analysis by deal size can highlight which "group" has the lowest churn rates.

oduct Heat Map

Item: Name

Astonish Enterpise

Astonish Nano

Astonish Platform

Maintenance

	Jan 17	Feb 17	Mar 17	Apr 17	May 17	Jun 17	Jul 17	Aug 17	Sep 17	Oct 17	Nov 17	Dec 17
A	320,800	100%	107%	100%	101%	95%	127%	203%	192%	157%	148%	112%
Astonish	55,452	88%	94%	105%	90%	94%	100%	356%	203%	154%	163%	111%
Astonish Platform	224,000	94%	105%	102%	99%	95%	136%	220%	234%	160%	136%	117%
Maintenance									600	1,500%	211%	174%
Totals	600,252	580,928	612,240	619,344	617,528	586,036	753,924	1,640,636	3,438,982	5,451,112	7,842,570	8,955,057

The Investor’s Point of View:
Customer Success Metrics

Churn and Retention

Investors pay very close attention to churn because customer retention is 95+ percent of your revenue. Everything is amortized over two- to three-year contracts in a SaaS business.

High retention and strong renewal rates are key value drivers and are crucial to increasing CLV, and it’s an area investors spend a lot of time focusing on during diligence.

Expansion/Upsell Revenue

It takes significantly more time and resources to acquire and onboard a new customer than it does to retain and upsell existing ones.

Investors look closely at expansion and upsell revenue metrics and ascribe high value to businesses that can grow organically by expanding existing customer relationships.

Cohort Analysis

Analyzing customer behavior across various cohorts provides valuable insights into how different segments of your customers are interacting with your product, sales and marketing teams.

Customers have different needs, and understanding these needs across cohorts can help improve customer relationships, go-to-market messaging, predict upsell/expansion opportunities and combat churn.

Next Steps:

Moving Forward and Measuring What Matters

Whether you're motivated by growth or by making more informed decisions about your business, the journey to reliable SaaS financial operations starts with measuring what matters.

We know how challenging this journey can be because we've been in your shoes.

That's the reason we built SaaSOptics. We offer total subscription management, from order to invoice, to cash and renewal, and we are the only platform that can scale and deliver in-depth financial metrics and analysis, including MRR, ARR, ACV, CAC, cohort and CLV. SaaSOptics is everything you need to run and grow your SaaS business, all in one place.

Call us today at 678.710.8260 or email us at info@saasoptics.com for more information.

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Additional Resources

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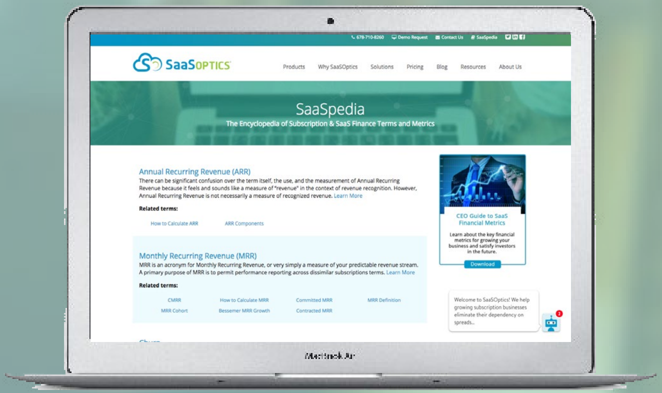

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