lighter CAPITAL

THE BEST SAAS STARTUP GROWTH METRICS

8 KPIs to Show Investors Your Startup is Primed for Success

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INTRODUCTION

Business professionals differ about how best to measure startup success. The consensus holds, though, that entrepreneurs must demonstrate to potential investors, lenders, employees and other partners that their business is healthy and growing.

Investors and lenders will review your financial reporting, of course, but they'll also want to gauge crucial performance metrics to determine whether your enterprise is a good investment.

This guide explains the eight essential SaaS metrics and how to track each one.

Together, they validate your company's revenue stream, product/market fit and, most important, your ability to achieve profitability.

SUMMARY OF THE IMPORTANT METRICS

METRIC	WHAT IS IT?	WHY IS IT IMPORTANT?
Monthly Recurring Revenue (MRR)	Measures the total monthly revenue (subscription or recurring) that is highly likely to continue.	Demonstrates whether you're gaining traction or starting to stall.
Committed Monthly Recurring Revenue (CMRR)	A deeper evaluation of MRR that considers potential changes in revenue.	Helps provide a better picture of the company's current and future financial status.
Average Revenue Per Customer (ARPC)	The average revenue generated from each customer per paying period (month or per year).	Helps identify upsell opportunities within accounts and contracts.
Customer Churn (CC)	The percentage of existing customers canceling subscriptions or no longer actively using the product within a given period.	A leading indicator that reveals how well you're meeting—or not meeting—your customers' needs.
Monthly Recurring Revenue Churn (MRRC)	Revenue lost or not realized from canceled contracts during the prior month.	Gauges the impact of lost customers on revenue and if the losses are manageable. It can be considered an early warning system for the future health of your SaaS business.
Customer Acquisition Cost Ratio (CAC)	Provides insights into how long it takes to recoup sales and marketing investments to acquire new customers.	Shows how quickly new customers will increase your profitability.
Customer Lifetime Value (LTV)	The total amount of average revenue forecasted to be earned per customer.	Knowing the value of newly acquired customers over the long run can assist with fundraising and valuation estimations.
Life Time Value/ Customer Acquisition Cost Ratio (LTV/CAC)	Summarizes and provides key insights into your potential valuation.	A high or low ratio can indicate the potential for fast or slow growth, which can drive higher or lower valuations.

DEMONSTRATING REVENUE POTENTIAL

To investors, present is prologue: They see your current performance as predictive of future performance. Unlike one-time deals or one-off services, recurring revenues (e.g., subscription income) are appealing to investors and lenders because they represent sticky future income streams and can be a baseline indicator for future revenue growth.

METRIC #1 :: MONTHLY RECURRING REVENUE (MRR)

What is MRR?

As the name suggests, MRR measures the total monthly revenue that's subscription-based or recurring in nature and highly likely to continue. This number excludes non-recurring payments, such as implementation or professional service fees, hardware and discounts.

On a yearly basis, this metric is known as Annual Recurring Revenue (ARR).

WHY IS MRR IMPORTANT TO ENTREPRENEURS?

Growth in bookings is the revenue performance standard for traditional industry. However, using bookings to measure growth in SaaS businesses is misleading and easily manipulated. Subscription terms can vary wildly — from month-to-month contracts to multiyear arrangements — and once you factor in upgrades, downgrades and renewals over a contract term, it becomes hard to accurately gauge the company's true performance.

MRR normalizes that recurring revenue into one time period, providing an accurate benchmark for business momentum.

Successful SaaS companies track MRR to measure their growth and momentum, and as a tool for financial forecasting and planning.

Measuring MRR month over month demonstrates whether you'regaining traction or starting to stall.

For financial planning purposes, MRR is relatively stable and predictable. Over time you can use it to forecast and plan.

Remember, MRR is not actual cash flow. Even if you're getting all payments upfront, you're still incurring costs to service the contract over its life — without additional cash inflow.

All the data needed to calculate your MRR can be found in your accounting software. To calculate your MRR, you need to make sure you track your recurring and non-recurring revenue separately.

HOW TO CALCULATE MRR

Number of customers x Average monthly subscription value per customer = MRR

- Start by aligning your current customers with their monthly subscription values.
- For multi-month subscriptions, divide those contract values by the number of months in the subscription.
- Last, add up the subscription values to determine your MRR.

MRR EXAMPLE CALCULATION

SaaS Co., a social networking platform for SaaS entrepreneurs, has 2,000 customers — half on its basic plan ($10/month) and the rest on its premium plan ($180/year, paid upfront). To calculate its MRR, SaaS Co would take the 1,000 customers on the monthly plan and add it to the 1,000 customers on the annual plan (dividing total revenue of the annual plan by 12):

$$(1{,}000 \times \$10) + \frac{(1{,}000 \times \$180)}{12} = \$25{,}000$$

Next month, if they add 500 customers with the same 50/50 split and lost no customers, the MRR would be $31,250:

$$\$25{,}000 + (250 \times 10) + \frac{(250 \times 180)}{12} = \$31{,}250$$

The company's total revenue for that month might have been significantly different if it had any non-recurring payments, such as one-time installation fees for new customers or additional charges on top of the monthly contract value for use or data overages. That's because MRR measures not cash flow or receipts, but how quickly and efficiently it's growing the top line. In this case, it's 25% month over month.

HOW DIFFERENT INVESTORS MAY USE MMR

	EQUITY INVESTORS	TRADITIONAL LENDERS	LIGHTER
STARTUP IS GAINING TRACTION	MRR provides insight into the core growth of the business. Investors like to see MRR grow by at least 100% per year.		MRR provides insight into the core growth of the business.
DOWNSIDE PROTECTION		Consistent recurring revenue means increased likelihood of making payments than when revenue is lumpy.	Depending on the type of funding you are seeking (revenue, term, or contract based financing) a percentage of your monthly revenue may be used as your repayment source.
PRICING MECHANISM			Understanding the core baseline and growth in the core business enables us to price the loan more accurately (which means better pricing for the borrower!)
FLEXIBILITY			As MRR grows, Lighter Capital can continue to provide additional financings in line with growth

METRIC #2 :: COMMITTED MRR (CMRR)

What is CMRR?

CMRR looks at current MRR, but adds income from new contracts and subtracts likely revenue decreases within that period.

WHY IS CMRR IMPORTANT TO ENTREPRENEURS

Unlike MRR, which is limited in scope, CMRR (committed MRR) considers potential changes, providing a fuller forecast.

Knowing your CMRR and how it's trending over time helps you predict revenue and provides a better picture of the company's current and future financial status.

The terms to define CMRR are defined as:

- **New Business MRR:** MRR associated with leads that convert to paid customers in a given time period.
- **Expansion MRR:** Increases in MRR from existing customers in a given time period as a result of customers' adding subscriptions, upgrading, etc.
- **Contraction MRR:** Decreases in MRR from existing customers in a given time period as a result of downgrading to a lower plan, adding or increasing a discount, etc.
- **MRR Churn:** MRR from customers who cancel or fail to renew their subscription in each period.

HOW TO CALCULATE CMRR

CMRR = MRR + Signed Contracts – Expected Churn

There is no one industry definition for CMRR measurement. What's essential—for you and for potential investors and lenders—is consistency within your own calculations.

Your MRR data are tracked in your accounting software, but the information on signed contracts and expected churn probably lives in your CRM. You might have to create a spreadsheet pulling from both sources to connect the two types of data; you might prefer to invest in third-party software.

	Detailed MRR	Customers	CMRR	Customers	Notes
End of Q1	**$750K**	**100**	**$750K**	**100**	
New Business	$50K	1	$50K	1	New customer
	$40K	1	$50K	1	New customer
			$50K	1	Contract signed, not yet billed
			$40K	1	Contract signed, not yet billed
Subtotal	**$90K**	**2**	**$190K**	**4**	
Churned	- $100K	-1	- $100K	-1	Lost to competitor
	- $20K	-1	- $20K	-1	No longer wants service
	- $10K	-1	- $10K	-1	Lost to competitor
Subtotal	**- $130K**	**-3**	**- $130K**	**-3**	
Contraction	- $5K		- $5K		Discount on renewal
	- $5K		-$5K		Reducing users
Subtotal	**- $10K**		**- $10K**		
Expected Churn			$30K	-1	Not returning calls for renewal
			$10K	-1	Not returning calls for renewal
Subtotal	**$0**	**0**	**$40K**	**-2**	
Expansion	$50K		$50K		Increasing users
	$20K		$20K		Adding recurring service package
Subtotal	**$70K**		**$70K**	**-2**	
End of Q2	**$770K**	**99**	**$910K**	**97**	

Factoring in signed contracts going into production—along with expected churn—shows more than simple MRR can. In this example, CMRR has a more positive outlook than MRR. In some cases, though, CMRR can show the converse, especially if expected churn is much higher than new contracts entering production.

HOW DIFFERENT INVESTORS MAY USE CMMR

	EQUITY INVESTORS	TRADITIONAL LENDERS	LIGHTER
STARTUP IS GAINING TRACTION	CMRR allows for a forecast of the likely revenues of the business.		CMRR allows for a forecast of the likely revenues of the business.
PRICING MECHANISM		The amount of revolving credit extended to SaaS companies is often based on a variation of CMRR.	
DOWNSIDE PROTECTION		Using CMRR allows the credit line to grow or shrink based on the performance of the company, ensuring that the lender is not taking an outsized risk.	Understanding the core baseline, including signed contracts, helps us to price the loan more accurately (which means better pricing for the borrower).

METRIC #3 :: AVERAGE REVENUE PER CUSTOMER (ARPC)

What is ARPC?

ARPC is the average revenue generated from each customer per month (or per year). For more specificity, consider customer segment (such as enterprise-level clients) or product type.

WHY IS ARPC IMPORTANT TO ENTREPRENEURS?

ARPC gives entrepreneurs deeper insights into what's taking place within their business, and where there may be opportunity to potentially increase revenue either across all product lines and customer types or within specific product lines or customer types.

ARPC may vary by product line

SaaS Co. offers a mix of products and services with the following ARPCs:

Product/Service	ARPC
Product A	$50/mo
Product B	$200/mo
Service	$150 OTF (One Time Fee)

Product B is the cash cow. Assuming products A and B have similar expenses, the focus should be on growing the Product B customer base.

In addition, knowing the ARPC of all products and services helps SaaS businesses identify upsell opportunities. Expanding on the previous example, let's add a pricing column for different products and services.

Product A has an upsell opportunity of $20/customer/month ($50 to $70). Product B has an upsell opportunity of $300. The company should emphasize upselling customers of Product B.

Product/Service	ARPC	Pricing
Product A	$50/mo	$20 to $70/mo
Product B	$200/mo	$150 to $500/mo
Service	$150 OTF	$150 OTF

HOW TO CALCULATE ARPC

Calculating the ARPC is done as follows:

$$\text{ARPC} = \frac{\text{Total Revenue}}{\text{Customer Count}}$$

Total Revenue can be based on customer segments or product types. Regardless of which you choose, the source for your Customer Count must match the source you are using for Total Revenue.

Monitor the evolution of your products' ARPC.

For example, look at Product A's ARPC figures over the last 6 months versus the last 12 months.

Perhaps more informative, the analysis could be pegged to pivotal events (such as shipment of a key upgrade of Product A, or completion of a major marketing campaign) to see how customers have responded.

You can get the ARPC of your products and services from your accounting software or from third-party software.

HOW DIFFERENT INVESTORS MAY USE ARPC

	EQUITY INVESTORS	TRADITIONAL LENDERS	LIGHTER
STARTUP IS GAINING TRACTION	ARPC data show investors whether you are betting on the right products to generate increasing revenues.		ARPC provides a guideline for how much upsell you may be able to do going forward, potentially increasing your revenues.
DOWNSIDE PROTECTION			Understanding the value of individual offerings can allow you to focus on the most profitable products in tough economic times.

GETTING TO PRODUCT-MARKET FIT

Many factors contribute to the success of your startup, but none may be more important than ensuring your product is a viable market fit. To an investor, product-market fit is one of the critical pillars in assessing if your company is on track for long-term viability or if it still requires additional capital or time to achieve market fit. Demonstrating that your product meets or exceeds your customer's needs is essential to your success.

METRIC #4 :: CUSTOMER CHURN?

What is Customer Churn?

Customer Churn is the percentage of customers canceling subscriptions in a given time period.

WHY IS CUSTOMER CHURN IMPORTANT TO ENTREPRENEURS?

Customer Churn helps entrepreneurs monitor how well they are meeting or not meeting their customers needs. It can reveal if you have the ability to grow your revenue or if you need to focus more efforts on retaining customers

SaaS businesses rely heavily on gaining and retaining customers to attain and sustain revenue. The key SaaS metrics are customer churn rate and MRR churn.

Customer Churn reveals how well you're meeting—or not meeting—your customers' needs.

Early growth figures can be deceiving—especially if they belie a lack of repeat business. When you're first reaching out to your potential customer base, your revenues and total number of customers might be growing, yet you could be hemorrhaging a large percentage of existing customers every month.

If customers bail out after a first or second taste of your product or service, that's a major problem. Long-term repeat business is the lifeblood of any successful enterprise. Your potential audience is finite, after all, and winning back a departed customer is a herculean task.

To tell whether there's an underlying problem with customer satisfaction, step away from overall revenue and total number of customers and look at Customer Churn.

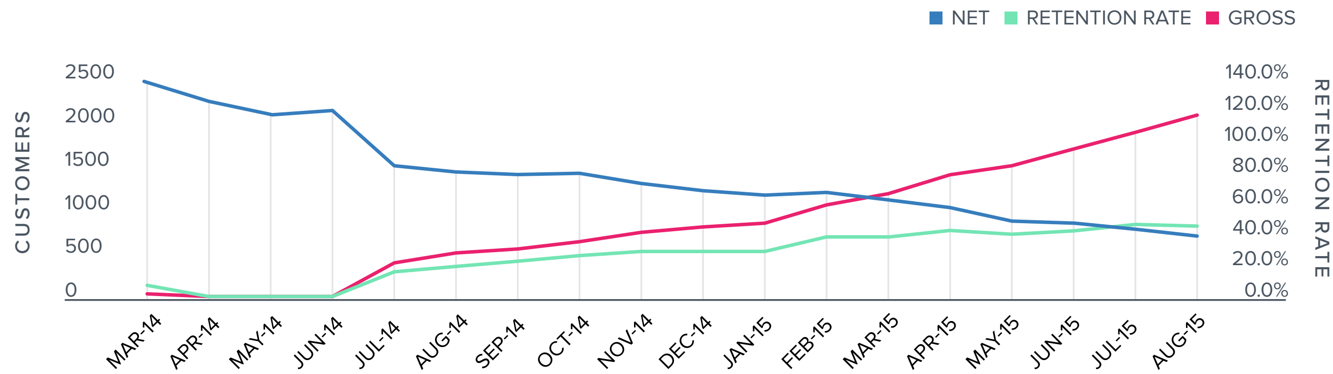

Figure 1. This chart shows how total customer count can be deceptive. The net number of customers isn't as healthy as the gross number, and the retention trend line is highly problematic. The company probably won't see even modest growth in its net customer base, because the Customer Churn is high and increasing.

HOW TO CALCULATE CUSTOMER CHURN

Customer Churn = Number of existing customers who left during a given period/ Total customers at the start of that period.

Customer Churn is measured monthly, quarterly or annually.

Mathematically, it's the inverse of customer retention, as noted in the chart above.

This ratio doesn't account for the gross customer accounts at the end of the period, nor the value you had been getting from each lost customer.

Ideally, a company's customer churn rate would be well under 10%, but this figure can vary depending on industry competition, end customer type, and the maturity of your product or service. For companies serving primarily SMBs, customer churn isn't as relevant, as small businesses often go out of business.

Inevitably, some customers will leave, but make sure you look at trends that reveal sustainability. If your business has a high customer churn rate, it's important to understand the underlying drivers of the exodus—and to take measures to stem the flow quickly.

Cohort Analysis

To understand Customer Churn, conduct a cohort analysis, which allows you to detect or forecast trends. For example, the cohort of customers of longer than six months might churn at a lower rate than those that have been with you for a month.

Such insights can be crucial for B2C businesses or younger businesses seeing high churn; you can show that the longer customers stay with you, the more likely you can retain them long term. This casts a spotlight on improving the initial experience; early adoption and satisfaction translates to brand loyalty (just as it would for dish soap or ice cream), because if you can get customers to adopt your product, they're going to stick around. That loyalty parlays into the Lifetime Value (LTV) of the customer.

Your CRM software can give you insights into your Customer Churn Rate. You can also determine this rate by looking in your accounting software for revenue streams from customers that go to zero in a given month.

CUSTOMER CHURN EXAMPLE CALCULATION

SaaS Co. had 2,000 customers on the first of the month. During the month, 480 customers leave. For that month, SaaS Co. had a monthly customer churn rate of 24%.

$$\frac{480}{2{,}000} = 0.24$$

WHY CUSTOMER CHURN MATTERS TO INVESTORS AND LENDERS

	EQUITY INVESTORS	TRADITIONAL LENDERS	LIGHTER
APPROACHING PRODUCT/MARKET FIT	Want to see if people like your product and how close you are to product/market fit. Will consider customer churn rate for different products to see if you are targeting the right customers.	Included in MRR line calculations.	Will consider customer churn for different products to see if you are targeting the right customers.
SUCCESS/FAILURE	In general, enterprises that have a higher churn rate are more likely to go out of business than companies with a lower churn rate.	The amount of revolving credit extended to SaaS companies is often based on a variation of CMRR.	Evaluate the long-term prospects of the business: Do you have a low Customer Churn that positions you well for growth? If not, does it affect the viability of your company?
DOWNSIDE PROTECTION		What will happen if you get no new sales? At what point will revenues approach zero with the current customer churn?	Look at Cohort Analysis to understand what the life cycle of the customer is.

METRIC #5 :: MRR CHURN

What is MRR Churn?

MRR Churn is the monthly revenue lost from canceled contracts during that month, and the MRR Churn Rate is the MRR Churn compared with the MRR at the start of the month.

A more accurate picture of MRR Churn can be calculated by including the revenue lost through contract contraction, as well the MRR gained through contract expansion and reactivation.

Related to customer churn, MRR churn delivers more crucial insights.

WHY IS MRR CHURN IMPORTANT TO ENTREPRENEURS?

Understanding MRR Churn can help you gauge the impact of lost customers on your revenue, including whether those losses are manageable, especially in the context of MRR from new customers. As your business grows, it can even help you forecast revenue performance.

MRR Churn can also be an early-warning system for your SaaS business. Just as with customer churn, MRR growth can be deceiving if you're in three-steps-forward, two-steps-back mode. It might seem like you're moving ahead, but it's not a sustainable formula for success.

Again, if you're not delivering a product that customers want, eventually the product/market gap will widen and swallow your business whole. By tracking MRR Churn early on, you can identify problems that might elude you if you're tracking only MRR. Such vigilance will give you time to pivot or adjust before your company goes bust.

HOW TO CALCULATE MRR CHURN

First, let's look at potential customer scenarios:

- Do nothing, and leave the purchase the same as before (MRR)
- Buy the product for the first time – New Customer (New MRR)
- Increase the purchase – Upgrades (MRR Upsell)
- Decrease the purchase – Downgrades (MRR Decrease)
- Stop buying altogether – Lost Customer (MRR Lost)

Now let's look at how these five scenarios contribute to MRR levels.
MRR analysis is done over time: month over month, quarter over quarter, or year over year.

Here, we'll examine month over month.
On Jan. 1, our sample company had 100 customers with a total purchase volume of $100,000. During January, 10 new customers purchased our product at $3,000 per month ($30,000 in new MRR). Four of our current customers increased their monthly purchase amount by $2,500 each (a total upgrade of $10,000). Two customers decreased their monthly purchase amounts by $2,500 each (a total downgrade of $5,000). Three customers went out of business and therefore stopped buying our product altogether. Their purchase was typically $2,500 per month, resulting in $5,000 in lost MRR. There were no other changes.

We end up with the following:

- Beginning MRR: $100K
- New Customers (10): +$30K MRR
- Upsell MRR (4): +10K
- Decrease MRR (2): -$5K
- MRR Lost (4): -$10K
- Ending MRR: $125K

TRACKING YOUR MRR

Now let's look at the percentage change for each respective area.

- New MRR Percentage: $30,000/$100,000 = +30%
- Upsell MRR Percentage: $10,000/$100,000 = +10%
- Decrease MRR Percentage: $5,000/$100,000 = -5%
- Lost MRR Percentage: $10,000/$100,000

By combining all the above numbers, we can look at the Net MRR Increase/Decrease. This can be done by summing all the above percentages or working from the original values.

- Net MRR Increase/Decrease: +30% + 10% - 5% - 10% = +25%
- Net MRR Increase/Decrease:

$$\frac{(\$30{,}000 + \$10{,}000 - \$5{,}000 - \$10{,}000)}{\$100{,}000} = +25\%$$

Like with MRR, the data you need to calculate MRR Churn should be recorded in your accounting software.

WHY MRR CHURN MATTERS TO INVESTORS AND LENDERS

	EQUITY INVESTORS	TRADITIONAL LENDERS	LIGHTER
APPROACHING PRODUCT/MARKET FIT	Want to see if people like your product and how close you are to product/market fit. Want to see that the products that are most popular also contribute significantly to your bottom line.	Included in MRR line calculations.	Will consider MRR churn rate for different products to see if you are targeting the most profitable markets.
STARTUP IS GAINING TRACTION	An indicator of your growth trend and traction, and a predictor of future revenue. Want to see you adding more users with existing customers than you are losing.		An indicator of your growth trend and traction, and a predictor of future revenue. Want to see you adding more users with existing customers than you are losing. Are you hitting your stride with existing customers? Are they increasing your MRR by adding users?
DOWNSIDE PROTECTION		One of the metrics that helps project the minimum revenue lenders can expect to receive over the next year(s).	One of the metrics that helps project the minimum revenue we can expect to receive over the next year(s).

HIGHLIGHTING A PATH TO PROFITABILITY

When you're raising capital, most investors won't expect your startup to be profitable. But they may ask how you will achieve profitability. To keep investors interested in your business, you must have a plan outlining the path to achieving profitability.

METRIC #6 :: CUSTOMER ACQUISITION COST (CAC) RATIO

What is CAC Ratio?

The CAC Ratio compares two factors: the total sales and marketing expenses associated with gaining a new customer, and the gross profit from those new customers in a given period.

Two key metrics help you chart your path to profitability: Customer Acquisition Cost (CAC) Ratio and Customer Lifetime Value (LTV).

First, let's lay a foundation for those complex concepts.

GROSS MARGIN VS. PROFIT MARGINS

Not all SaaS companies accurately calculate gross profits, which leads to overinflating CAC, so let's distinguish them from profit margins.

Annual revenue	$500,000
Cost of goods sold	$100,000
Operating expenses	$300,000

Gross margin is gross profit (revenue minus cost of goods sold) divided by revenue. Gross profit does not take into account operating expenses.

Here's a simplified example for a fictitious software company making apps:

The gross profit for this tech company is $400,000 ($500K-$100K), which makes their gross margin 80% (400K/500K).

Software companies often have a high gross margin because the costs of goods sold are minimal and limited to endemic expenses such as server costs and hosting costs.

However, the app company has a lot of operating expenses:

They have to rent office space, pay salaries to developers and salespeople, and allocate money for marketing and advertising. The operating expenses of tech companies are usually a lot higher than the cost of goods sold, but operating expenses are variable and can be reduced to control burn.

Once operating expenses are also deducted, the net income for the startup is $100,000 ($500K-$100K-$300K), which makes the profit margin 20% (100K/500K).

WHY THE CAC RATIO IS IMPORTANT TO ENTREPRENEURS

Any ratio can be conveyed as a fraction. Which number goes on top (the numerator) and which goes on the bottom (denominator) determines not just the numerical value, but also its meaning for your business.

The CAC Ratio will produce either the percentage of expenses recovered over a given period (gross profit / expenses) or the time it will take to recover the expenses associated with acquiring the new customers (expenses / gross profit).

This ratio tells you how long it takes to recoup your sales and marketing investment. That's why we use gross profit rather than total revenue.

CAC RATIO EXAMPLE CALCULATION

Last month, SaaS Co. spent $1,000 on pay-per-click advertising, $3,000 for print ads, and $6,000 for one sales rep to reach out to the leads generated from the new marketing campaign. SaaS Co. generated 50 new customers, all of which purchased monthly subscriptions for $10/month. SaaS Co.'s product is fully developed and costs only $50/month for unlimited hosting.

Here's a breakdown of their key financials:

Revenue	August
Monthly Subscription	**$500**
Total Revenue	$500
COGS: Hosting	**- $50**
Gross Margin	$450

Sales and Marketing	
Pay Per Click	$1,000
Print Ads	$3,000
Sales Rep Salary	$6,000
Total Sales and Marketing	**$10,000**

SaaS Co. has a gross profit of $450/month, or $5,400 when annualized, and sales and marketing expenses were $10,000 for the month. Based on these numbers, we can calculate:

CAC Ratio	
Gross Margin (Annualized)	$5,400
Total Sales and Marketing	$10,000
CAC Ratio	**54%**

This shows that the new customers acquired last month will recover 54% of the month's sales and marketing efforts in one year. It can also be useful to flip the numerator and denominator to see a different result. Doing so yields the following:

CAC Ratio	
Gross Profit (Annualized)	$5,400
Total Sales and Marketing	$10,000
CAC Ratio	1.85

This inverted CAC Ratio tells us how many years—in this case, 1.85 years—it will take SaaS Co. to recover its initial investment in sales andmarketing for August.

Note: We assumed that all new customers acquired last month were a direct result of sales and marketing efforts in the same month. However, most businesses have a lag time between the sales and marketing efforts and actual sales. Establishing a direct correspondence between sales and marketing efforts can be complicated, though, and the method used above can be a helpful proxy.

At Lighter Capital, we use the inverted ratio most often because it gives us a faster way to gauge the time it will take to recover a company's investment in sales and marketing.

HOW TO CALCULATE YOUR CAC RATIO

Annualized Gross Profit for period Q / Sales and Marketing Expenses for period Q

WHY CAC RATIO MATTERS TO INVESTORS AND LENDERS

	EQUITY INVESTORS	TRADITIONAL LENDERS	LIGHTER
PATH TO PROFITABILITY	How quickly will new customers increase your profitability?		How quickly will new customers increase your profitability?
GROWTH POTENTIAL	How quickly can you grow after an injection of capital considering the cost of acquiring customers?		How quickly can you grow after an injection of capital considering the cost of acquiring customers (CAC)? How quickly will those new customers increase your profitability (CAC Ratio)?
DOWNSIDE PROTECTION		Want to feel comfortable with how much you are spending on acquiring customers (CAC).	Revenue is tied directly to our funding model as our loans are repaid by taking a percentage of revenue every month.

METRIC #7 :: CUSTOMER LIFETIME VALUE (LTV)

What is LTV?

Customer Lifetime Value (LTV) is the total amount of revenue, on average, you expect to earn per customer.

Put another way, LTV is an estimate of the total subscription value of an average customer over his or her lifetime.

WHY IS LTV IMPORTANT TO ENTREPRENEURS?

Knowing how much revenue you can expect to generate for an average customer is important. Viewed in isolation, LTV doesn't give you the whole picture. It's much more valuable to view your LTV relative to the average cost to acquire a new customer—a.k.a. Customer Acquisition Cost (CAC).

LTV EXAMPLE CALCULATION

SaaS Co. offers two different pricing options:
Basic ($10/month) and Premium ($15/month).
SaaS Co. has 1,000 Basic and 1,000 Premium customers.
Average customer lifetime varies by pricing plan.

Average Customer Lifetime

Basic: 12 months

Premium: 24 months

With these data, we can calculate the LTV of the company's average customer:

$$\text{LTV} = \frac{[(\$10 \times 1{,}000 \times 12) + (\$15 \times 1{,}000 \times 24)]}{2{,}000} = \$240$$

This means that, on average, SaaS Co. can expect to generate $240 in revenue per customer.

HOW TO CALCULATE LTV

LTV = Average Revenue Per Account (ARPC) x Average Customer Lifetime

Is there a particular value that SaaS companies should be targeting? There is no "right" answer because it's not the standalone LTV that really matters but the LTV relative to CAC.

At a minimum, you want your LTV to be greater than your CAC. If you spend more to acquire the average customer than you gain from them, your business is destined to fail. Especially during boom cycles, seemingly promising startups can be hyper-focused on expanding their customer base quickly without considering the risks of overspending on customer acquisition.

Aim for an LTV that's at least triple your CAC. This provides a buffer for unexpected variations—such as higher acquisition costs or a shorter customer lifetime—while still generating an attractive margin.

You can get the lifetime value of your customers from your accounting software. As we mentioned above, you may also want to investigate third-party software to track this metric.

WHY LTV MATTERS TO INVESTORS AND LENDERS

	EQUITY INVESTORS	TRADITIONAL LENDERS	LIGHTER
PATH TO PROFITABILITY	Want to know the value of newly acquired customers over the long run.		Want to know the value of newly acquired customers over the long run.
PRICING MECHANISM			CAC ratio and LTV determine how long it will take you to repay the loan. LTV also determines if you can take on additional loans as you add customers and increase your revenues.

METRIC #8 :: LTV/CAC RATIO

What is LTV/CAC Ratio?

The LTV/CAC Ratio is the total average value you expect to receive from a new customer compared against the average cost to acquire a new customer.

LTV :: Customer Lifetime Value

CAC :: Customer Acquisition Cost

WHY LTV/CAC RATIO IS IMPORTANT TO ENTREPRENEURS

The LTV/CAC Ratio summarizes an abundance of information—including anticipated average lifetime revenue per customer, customer churn, and sales and marketing costs—into a single, easily understood number that can be used to evaluate the prospects for your business.

The key question: On average, do we earn more revenue per customer than it costs to acquire new customers? If the answer is “yes,” you could have a successful company. If it’s “no,” you probably won’t be in business for long.

The exception is if your SaaS startup is in its early stages. In that case, your LTV is likely to be low relative to your CAC. This isn’t necessarily an issue, as long as your LTV trends up over time relative to your CAC.

A high LTV/CAC Ratio means you have the potential to grow faster and need less capital to do so. Companies with higher LTV/CAC Ratios typically have higher valuations and an easier time securing funding from investors.

A lower LTV/CAC Ratio means your company is not as efficient at acquiring high-value customers and will probably need more capital to fuel revenue growth. The need for more capital and the slower growth rate means lower valuations from investors.

SO, WHAT'S A HIGH OR LOW LTV/CAC RATIO?

Average LTV/CAC Ratios vary across industries and business models, but you should aim for an LTV/CAC Ratio of at least 3:1, especially when seeking equity investors. This provides the necessary profit to invest in continued growth and provides a cushion should LTV decrease or CAC increase.

That's not to say a business cannot thrive with a LTV/CAC Ratio under 3:1. If you do not desire or need a large exit, and if you're not looking to raise equity, having a high LTV/CAC Ratio is less important. Debt investors, for example, are more interested in seeing a stable or slightly expanding LTV/CAC Ratio than in an LTV/CAC Ratio at or above 3:1.

HOW TO CALCULATE LTV/CAC RATIO

$$\frac{\text{LTV}}{\text{CAC}}$$

LTV = Average Revenue Per Account (ARPC) x Average customer lifetime
CAC = Total sales and marketing expense / Number of new customers

LTV/CAC RATIO EXAMPLE CALCULATION

SaaS Co. offers two different pricing options: Basic ($10/month) and Premium ($15/month). It has 1,000 Basic and 1,000 Premium customers. Average customer lifetime varies by pricing plan.

Average Customer Lifetime

Basic: 12 months
Premium: 24 months

With these data, we can calculate the LTV of the company's average customer:

$$LTV = \frac{[(\$10 \times 1{,}000 \times 12) + (\$15 \times 1{,}000 \times 24)]}{2{,}000} = \$240$$

On average, SaaS Co. can expect to generate $240 in revenue per customer.

WHERE TO GET THE DATA TO CALCULATE LTV/CAC RATIO

You'll need both CRM data and a well-organized accounting system to figure out your LTV/CAC Ratio.

WHY LTV/CAC RATIO MATTERS TO INVESTORS AND LENDERS

	EQUITY INVESTORS	TRADITIONAL LENDERS	LIGHTER
PATH TO PROFITABILITY	Want to know the revenue potential generated by new customers significantly outpaces the cost of acquiring them.		Want to know the revenue potential generated by new customers significantly outpaces the cost of acquiring them.
PRICING MECHANISM		Want to make sure you're not spending more on getting new customers than they're worth to your bottom line.	Want to make sure you're not spending more on getting new customers than they're worth to your bottom line.

SUMMARY

Tracking some or all of the eight metrics in this guide will help you gain insights about your business and help you make better decisions. Having a clear understanding of how your company is performing against key SaaS benchmarks demonstrates that you know your business well, which is essential when you interact with investors.

Two key things to know about sharing your company's data with potential investors or lenders:

Make sure your metrics go beyond a "snapshot." You'll want to show how your key indicators have evolved, and how your company compares against industry peers and competitors, if the data is available.

Make sure your data is clean and easily consumable— a link to an online dashboard is great, but a simple PDF or similar will work to share metrics reports. If you're prepping financial information, make sure your information is clean, clear and concise. Messy or complicated financials are not only hard to evaluate, but they may cast doubt on the information's reliability and your company's credibility. We recommend using an accounting program such as QuickBooks, which integrates with many third-party tools and systems, including Lighter Capital's application process.

> Lighter Capital's model is so innovative—a debt provider that's essentially a VC partner. We get the financial rigor that a VC would give us, as well as strategic guidance, and that's been incredibly helpful."

BANT BREEN
FOUNDER AND CHAIRMAN

ABOUT LIGHTER CAPITAL

Lighter Capital is the leader in founder-friendly financing. Our unmatched combination of up to $4 million in non-dilutive financing, professional networking resources, product discounts, and capital partner connections have helped hundreds of US, Canadian and Australian startups succeed on their terms. Founders find our application process easy and prefer how our financing features no hidden fees, equity, warrants, or covenant requirements. We've already financed numerous startups, yours could be next.

INTERESTED IN APPLYING FOR A LOAN?

If you're ready to expand your tech startup and still want to maintain ownership and control, connect with our investment team by applying for funding today.