Subscription Business Economics

The Total Cost of Failed Payments and the True Value of Recovered Customers

FlexPay

MEASURING THE EROSION IN CUSTOMER LIFETIME VALUE FROM FAILED PAYMENTS

Businesses with subscription or recurring billing models focus all their energy on acquiring and retaining customers. Customer retention is a primary measure of company revenue growth and profitability because subscription companies need to keep customers active long enough to fund both the Cost of Goods Sold (COGS) of the product or service delivery and the significant customer acquisition costs.

Simply put, increasing customer tenure directly drives revenue growth and higher profitability for subscription companies. The importance of this relationship means subscription businesses must understand and manage all drivers of customer churn because reducing churn significantly improves the KPIs of subscription-based businesses.

INCREASING RETENTION DRIVES REVENUE GROWTH AND HIGHER PROFITABILITY

ROOT CAUSES OF SUBSCRIPTION CUSTOMER CHURN

Customer churn is the enemy of subscription businesses because each lost customer eliminates revenue from all future billing cycles.

Most causes of customer churn are well understood and well-managed. In fact, most well-run subscription businesses invest significant resources to minimize the churn created by these factors:

1. Customer fatigue

The customer no longer sees value in the product or service and decides it is time to end the subscription

2. Competitive loss

The customer finds another provider they believe is better or finds a lower price point than their current vendor and decides to switch

3. Customer service issue

The customer has a negative experience with the product or brand and decides to cancel or not renew their subscription

Unfortunately, even well-run subscription businesses may not know that up to 48% of subscription customer churn is not caused by the customer cancelling their membership, but by failed credit card payments.

What is even more painful is the fact that most failed credit card payments are not declined for NSF or by authorization systems identifying fraudulent transactions, but by decline decisions made on legitimate transactions where the customer intends to buy the product or service and has credit to complete the purchase. In these cases, the customer is ready and willing to buy but the card authorization system won't let them complete the purchase.

To learn more about the frictions and limitations in the payments system that lead to false declines, also known as credit card authorization declines on legitimate transactions, read the Payments Authorization Management eBook.

MEASURING THE TOTAL ECONOMIC COST OF FAILED PAYMENTS

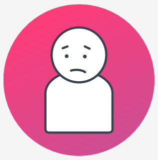
The direct link between failed payments and customer churn is often not well understood. However, understanding the total economic cost of failed subscriptions payments is rarer still.

As you'll see, there is an obvious direct link between customer churn and failed payments, plus a not-so-obvious indirect cause that is also a significant driver of churn.

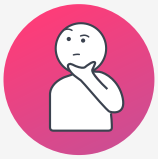
The obvious: Every failed payment from a subscription customer that is not recovered results in a churned customer.

The not-so-obvious: Subscription customer churn is also created when customers are made aware when their recurring payment is declined. Customer visibility into failed payments occurs when service delivery is interrupted or when the recovery methods a business uses force the customer to help solve the payment issue through customer service outreach or a dunning recovery method.

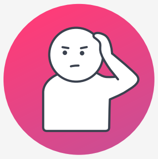
Asking customers to help fix a failed payment might not seem like an obvious contributor to churn, so let's review the typical ways a customer reacts when asked to help solve a failed payment:



The customer has an emotional reaction to the news their credit card failed. This reaction ranges from annoyance to a defensive response as customers interpret the failed payment as a judgment on their ability to pay.



A bad brand experience is created when the merchant forces the customer to solve a problem they didn't create.



The brand becomes associated with a credit card issue in the customer's mind, which they probably haven't experienced with other brands.

The customer is forced to decide if they want to continue with the subscription or just let it end by not acting.

CALCULATING THE ECONOMIC COST OF FAILED PAYMENTS

Once the relationship between failed payments and customer churn is understood, it becomes apparent that the total cost of unrecovered failed payments must be calculated by measuring the revenue lost from all future payments the customer would have made if their subscription hadn't ended prematurely. **That is the actual cost of a lost customer, which is a far higher cost than a single declined payment.**

The equation used to calculate the Lifetime Value (LTV) of a customer can also be used to calculate the cost of a customer prematurely lost to a failed payment.

Monthly Billing $ Amount x **Blocked Quantity of Billing Cycles** = **Total Failed Payment Cost**

Let's use an example of a subscription company with a customer who is billed $49.99 per month and experiences a failed payment in their third month of billing. The average lifespan of customers for this company is 10 months.

Monthly Billing $ Amount		Blocked Quantity of Billing Cycles		Total Failed Payment Cost
$49.99	**x**	**8** missed months of billing	**=**	**$399.92**

This equation makes it clear that solutions which recover failed payments must optimize for customer recovery and customer LTV.

THE ECONOMIC VALUE OF CUSTOMERS RECOVERED AFTER A FAILED PAYMENT

The same calculation can now be applied to the value of a customer recovered following a failed payment. Let's use the same example above but calculate the benefit to the company if the customer is recovered by a failed payment recovery solution:

Monthly Billing $ Amount x All Recovered Billing Payments		Cost of Recovery		Total Value of Recovered Customer
$49.99 x 8 Months = $399.92	–	$15	=	$384.92

When the calculation of the full value of a recovered customer includes both the failed payment recovery and the ongoing successful billing cycles following the recovery, two conclusions are clear:

1. Failed payment recovery solutions must be optimized to deliver both recovered customers and overall recovery dollars

2. Businesses must prioritize with the highest urgency the deployment of the failed payment recovery solution that delivers the longest post-recovery lifespan in order to maximize LTV

Conclusion: Subscription-based businesses must deploy a solution that delivers the highest recovery of customers lost to failed payments AND delivers the longest customer retention following recovery.

Introducing

INVISIBLE RECOVERY™

The FlexPay Invisible Recovery™ platform is an AI-powered solution that optimizes customer recovery from failed payments and delivers proven long-term customer retention following recovery.

Invisible Recovery™ delivers the highest rate of customer recovery by creating an individual strategy for each failed payment, resulting in optimal total customer and revenue recovery.

Plus, Invisible Recovery™ works quickly while completely avoiding customer visibility to the failed payment, thereby avoiding the customer churn created when subscription customers are made aware of the payment issue.

FLEXPAY RESEARCH SHOWS INVISIBLE RECOVERY™ DELIVERS THE HIGHEST RECOVERY, AND SUSTAINED RETENTION:

- Up to **70%** improvement in failed payment recovery rates compared to other recovery solutions
- Up to **54%** longer customer retention following recovery compared to other failed payment recovery solutions

You can use FlexPay's calculator tool to estimate the additional revenue and the number of active customers Invisible Recovery™ can deliver for your subscription business. Measure the results for your company now and contact us to schedule a consultation with one of our declined payment experts.

Revenue Recovery Calculator

Schedule a Consultation

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