The State Of

Subscription Business:

Best Practices And Business Performance Drivers

January 2023

PYMNTS | FlexPay

The State Of Subscription Business: Best Practices And Business Performance Drivers, a PYMNTS and FlexPay collaboration, examines the relationship between payments friction and customer churn in the subscription industry and takes a deep dive into the best practices of the firms that effectively manage these challenges. We surveyed 200 executive decision-makers at companies that offer subscription-based services and products in retail, health and fitness, media and publishing, home security and online gaming. These businesses generated 40% or more of their revenue from subscription relationships and reported annual revenues of at least $100 million. The survey was conducted from Sept. 12, 2022, to Sept. 28, 2022.

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ACKNOWLEDGMENT

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Introduction

"You cannot manage what you do not measure." It is an axiom that holds particular importance to subscription providers, which are losing hundreds of millions each year due to a failure to track one key metric.

The majority of subscription-focused companies anticipate an economic downturn in 2023, and 48% expect the cost of acquiring new customers to be a challenge. Additionally, 37% believe that retaining their current customers will be difficult. This coincides with a lack of consensus regarding the key factors that drive business performance as well as a lack of data-driven knowledge about the best practices of the most successful subscription companies.

PYMNTS' latest research finds that 58% of subscription businesses track metrics that measure the outcome of the customer's relationship with the business — customer churn or retention — but only 8.5% measure customer lifetime value (LTV).

Subscription providers that track and optimize customer LTV are five times more likely to be top performers — defined as those that minimize revenue loss due to failed payments. Moreover, our research finds that only two in five subscription firms even recognize the connection between failed payments and LTV.

Top performers leverage LTV to guide their strategies and take action to retain customers before they become missed opportunities. This has a direct impact on business performance: In the sectors studied, subscription companies lost an average of 9% of sales to failed payments, totaling an estimated $278 billion in the last 12 months. Top performers, however, recover 60% of failed payments that would have otherwise been lost.

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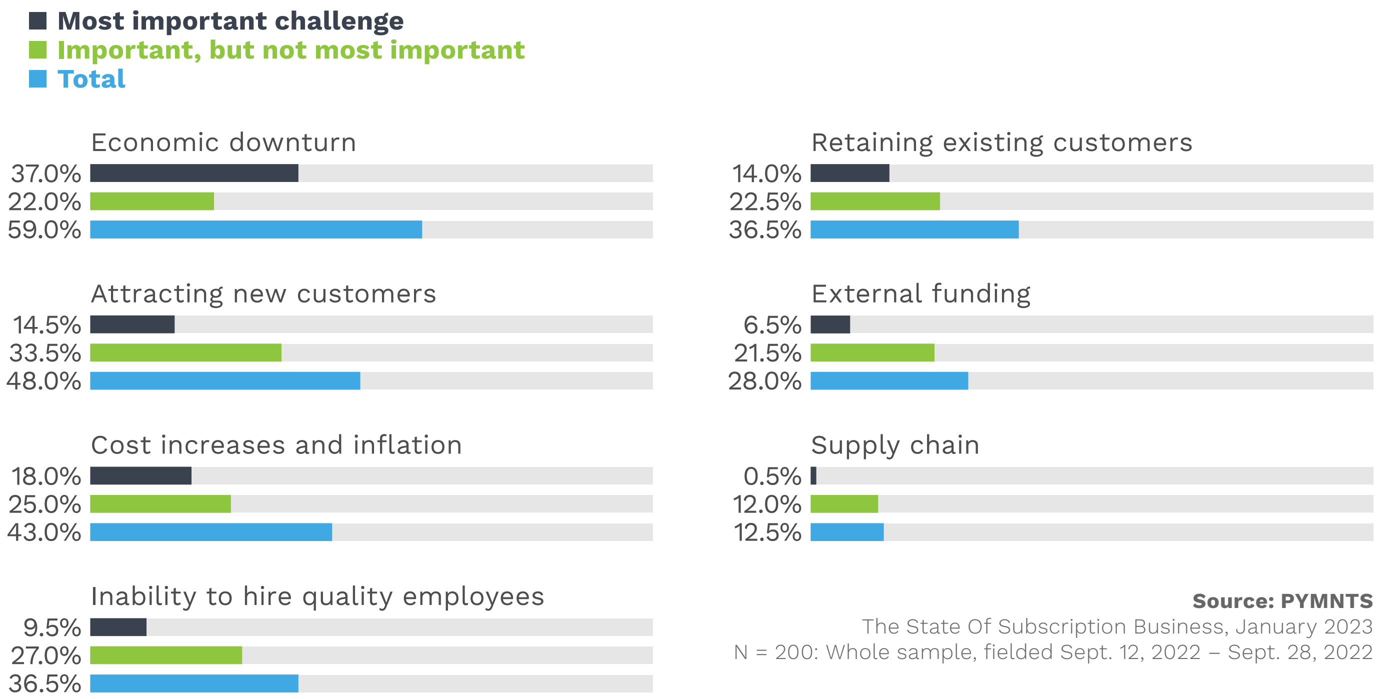
This is what we learned.

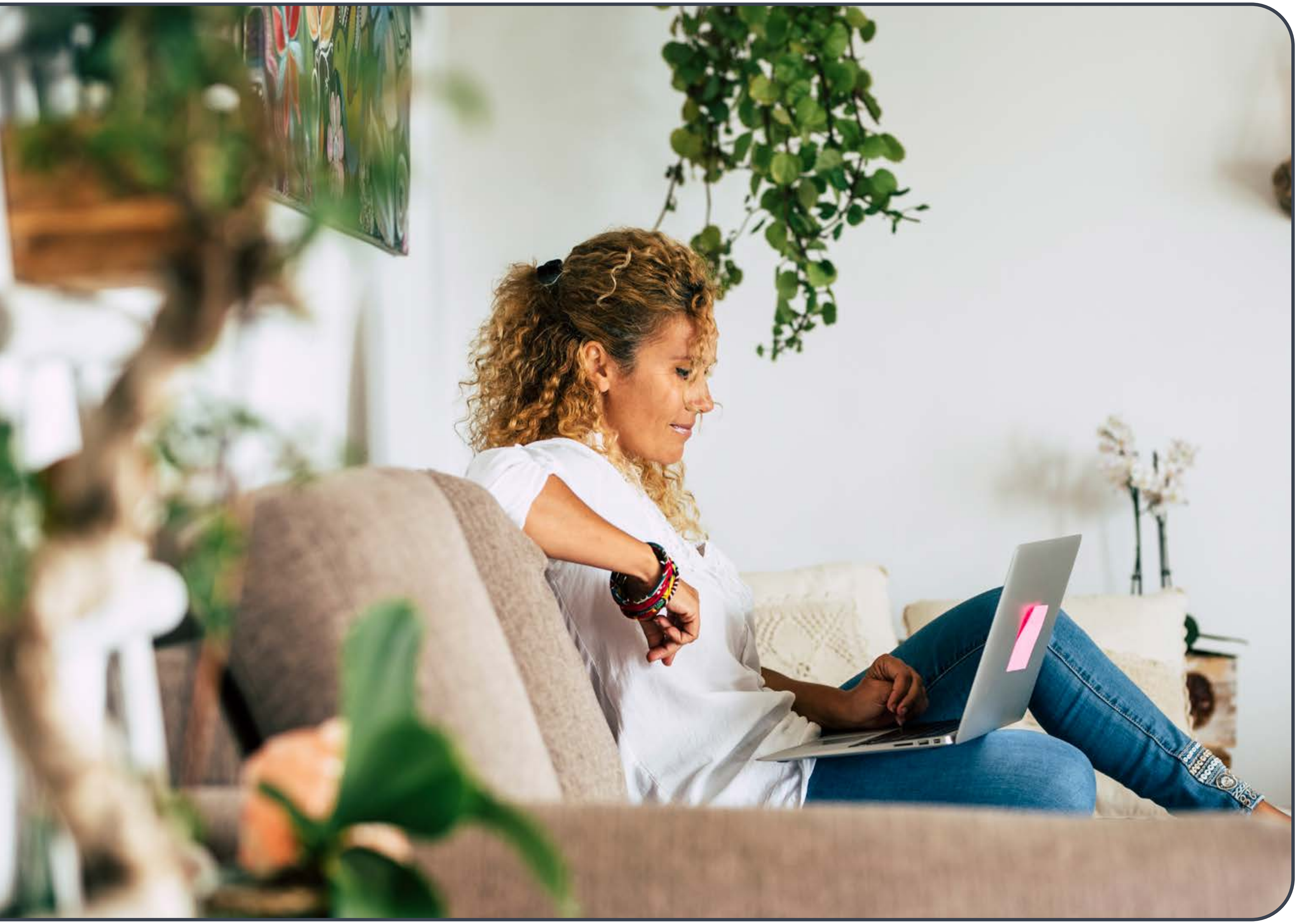
FIGURE 1:

Challenges businesses expect to face in the next 12 months

Share of companies citing select challenges expected in the next 12 months, by level of importance



Source: PYMNTS
The State Of Subscription Business, January 2023
N = 200: Whole sample, fielded Sept. 12, 2022 – Sept. 28, 2022



Metrics and measurement

Ninety-one percent of subscription merchants do not measure customer LTV. There is no industry standard for how to define and track it.

Customer LTV matters for all companies, but it plays an especially critical role in the profitability and growth of firms offering subscription-based products and services. Yet PYMNTS' latest research shows that just 8.5% of subscription-focused firms actively monitor and analyze customer LTV. This is partly explained by the industry's lack of clarity and consensus on the definition and metrics for measuring it.

One consequence is that the industry tends to focus on measuring outcome-based metrics rather than the underlying drivers of business performance. To better understand this dynamic, we asked firms in the subscription space to identify the subscription-based metrics they track. Our research finds that 58% of subscription-focused companies track either customer churn (36%), customer retention (28%) or both.

In contrast, top-performing firms in the subscription space — those that effectively reduce revenue loss due to involuntary churn caused by failed payments — track and analyze an average of three metrics linked to customer LTV, compared to the two metrics measured by their bottom-performing counterparts. The most measured metric among these top performers is failed payments (67%), followed by customer churn rates (40%) and customer LTV (33%).

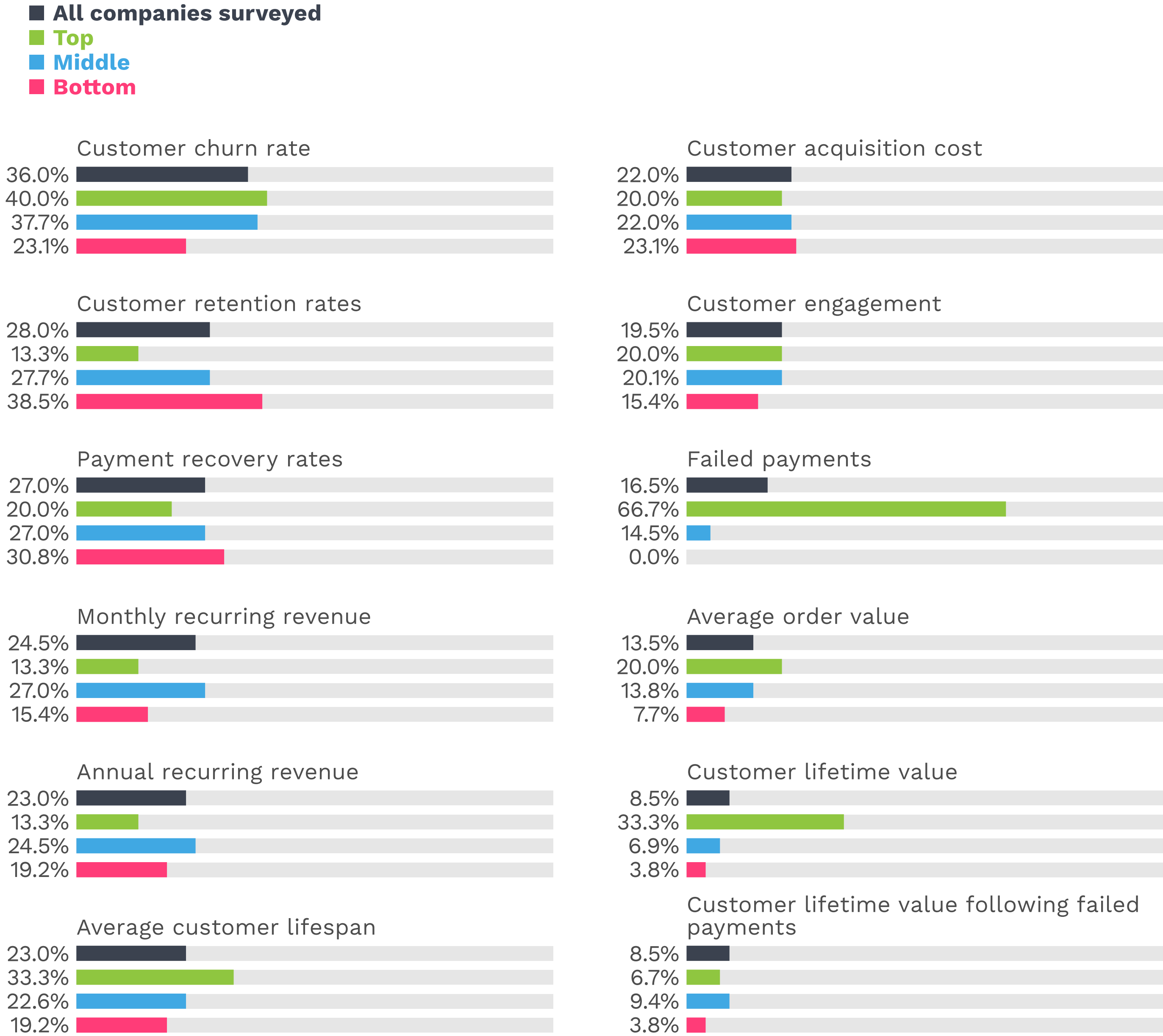
67%

Share of top-performing firms that **measure failed payments**

FIGURE 2:

Top operating metrics subscription companies track

Share of companies that track select subscription-based metrics, by failed-payments recovery performance



Source: PYMNTS
The State Of Subscription Business, January 2023
N = 200: Whole sample, fielded Sept. 12, 2022 – Sept. 28, 2022

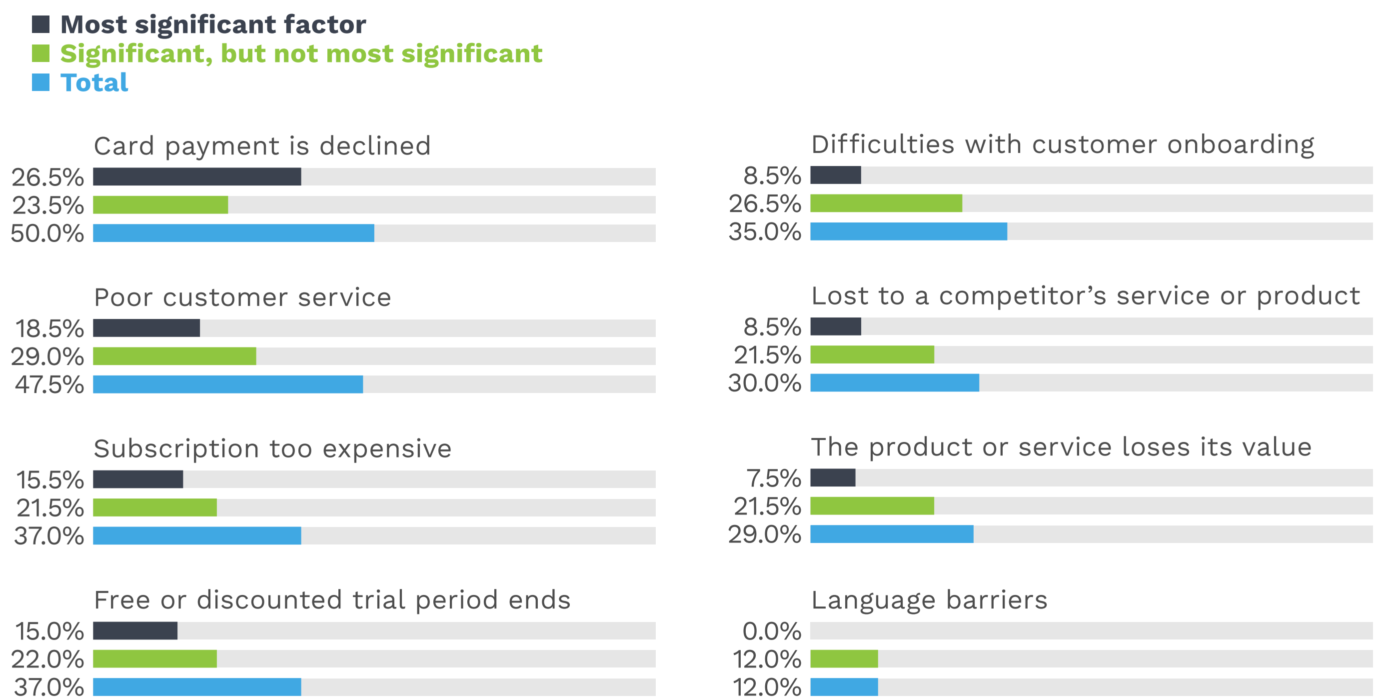
Only two in five merchants recognize failed payments as a strategic driver of customer value and business performance.

Subscription businesses do not fully grasp the extent to which failed payments contribute to customer churn and the resulting impact on business performance. Our data shows that over two-thirds of subscription-focused firms recognize the negative impact of failed payments on customer retention, yet only 27% consider it the most significant contributor to churn.

FIGURE 3:

Top reported causes of customer churn

Share of companies citing select factors that contribute to customer churn, by level of importance



Source: PYMNTS
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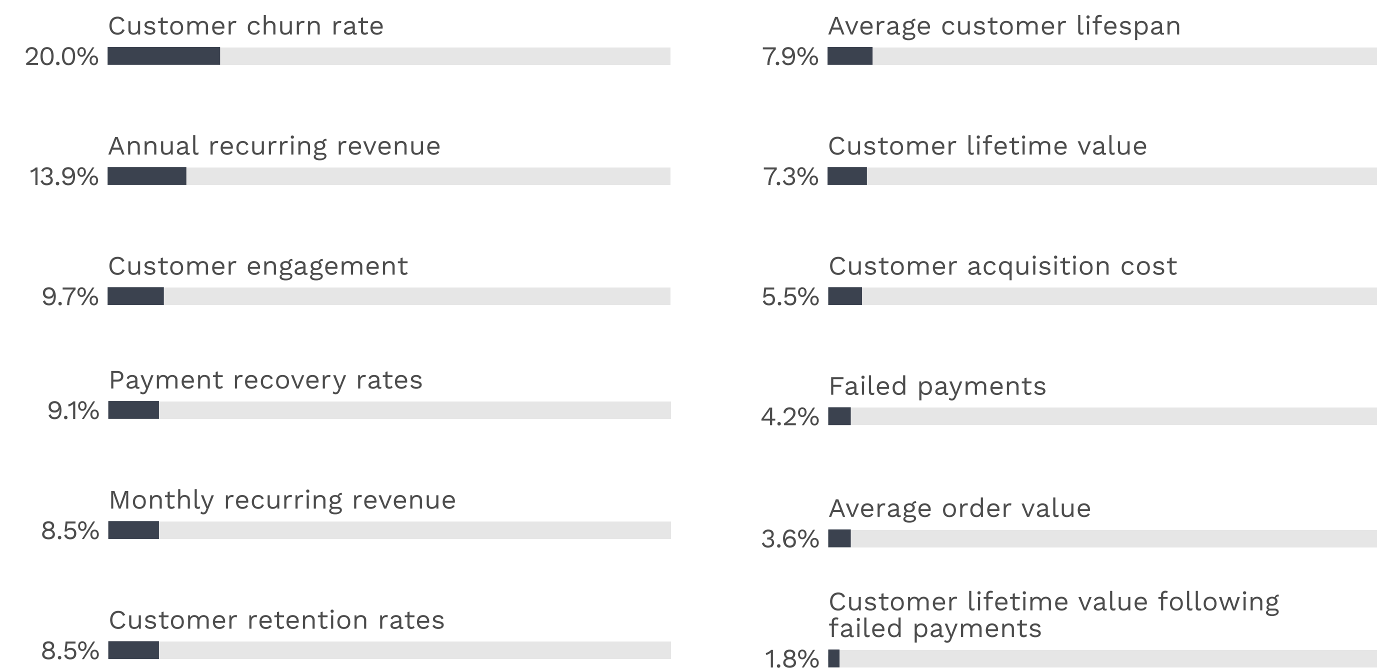
N = 200: Whole sample, fielded Sept. 12, 2022 – Sept. 28, 2022

In fact, involuntary churn caused by failed payments accounts for approximately 50% of total customer churn — yet our research finds that only 53% of subscription companies track involuntary churn in the first place. Even among those businesses that track total customer churn, only 20% identified it as the most important metric for improving business success. In other words, most firms are either underestimating the severe impact of failed payments on customer LTV or overlooking this dynamic completely.

FIGURE 4:

The metrics subscription providers view as most important

Share of companies that cite select subscription-based metrics as most important



Source: PYMNTS
The State Of Subscription Business, January 2023
N = 200: Whole sample, fielded Sept. 12, 2022 – Sept. 28, 2022

27%

Share of consumers who are likely to **cancel their subscriptions** if they experience service interruptions due to failed payments

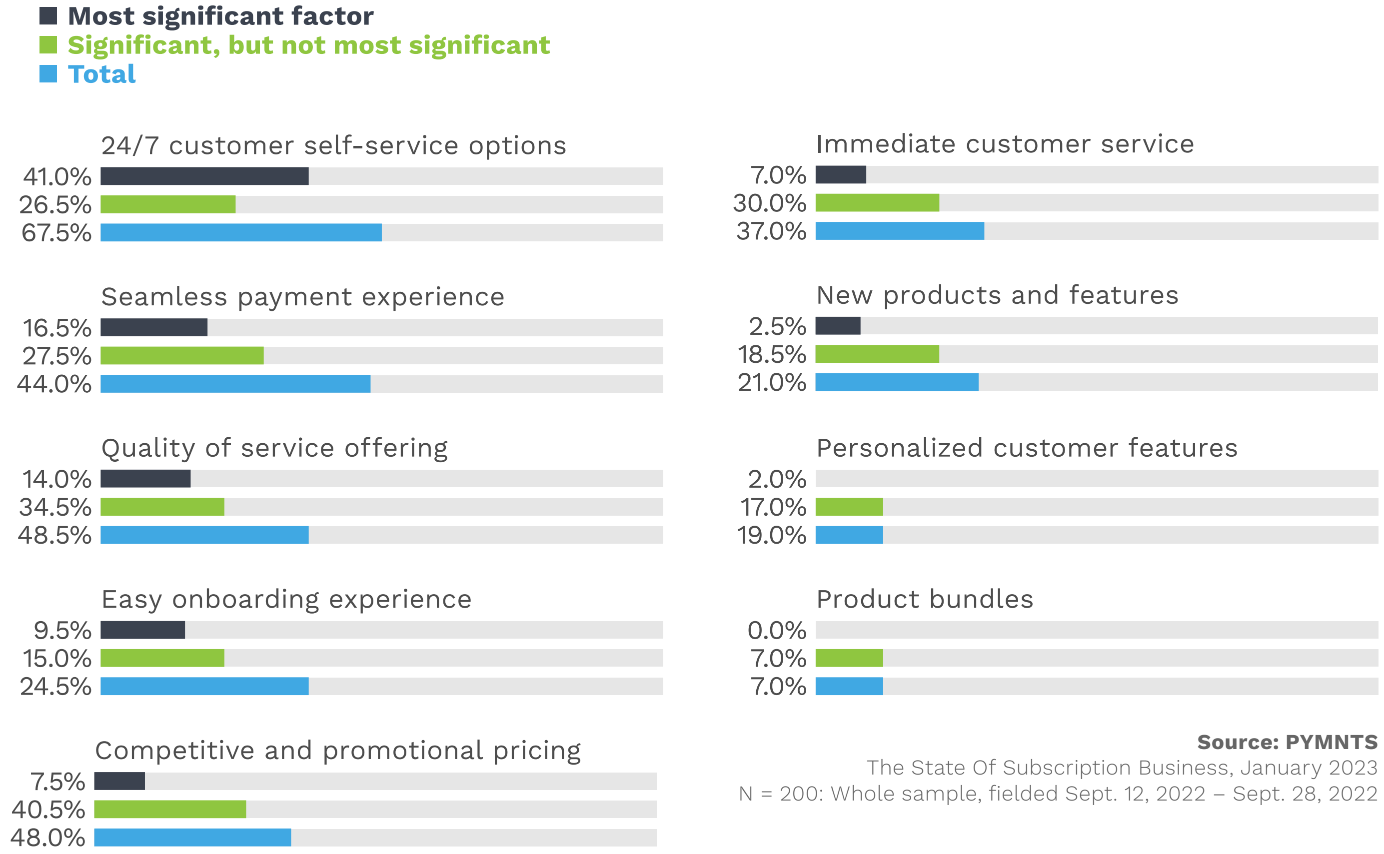
Despite data that shows 27% of consumers are likely to cancel their subscriptions if they experience service interruptions due to failed payments, our latest research found that just 44% of subscription providers believe that consumers place a high value on the payments experience.[1] This further underscores that many firms do not grasp the impact of payments friction on their bottom lines. Indeed, only 15% of the subscription providers we surveyed say they track failed payments primarily to improve customer LTV — meaning that 85% view failed payments as “the cost of doing business” and out of their ability to control or improve.

1 Optimizing Subscription Payments: How Providers Can Take The Sting Out Of Payment Declines. PYMNTS. 2021. https://www.pymnts.com/study/optimizing-subscription-payments-declined-payments-customer-churn/. Accessed January 2023.

FIGURE 5:

What subscription providers think customers value

Share of merchants citing select factors that they think consumers value as part of their subscription experience, by level of importance



Source: PYMNTS
The State Of Subscription Business, January 2023
N = 200: Whole sample, fielded Sept. 12, 2022 – Sept. 28, 2022

The art of minimizing churn:

Best practices

How top performers minimize the impact of failed payments on revenue

1. Track customer LTV

Top performers do this 8.2 times more frequently than bottom performers.

2. Track failed payments

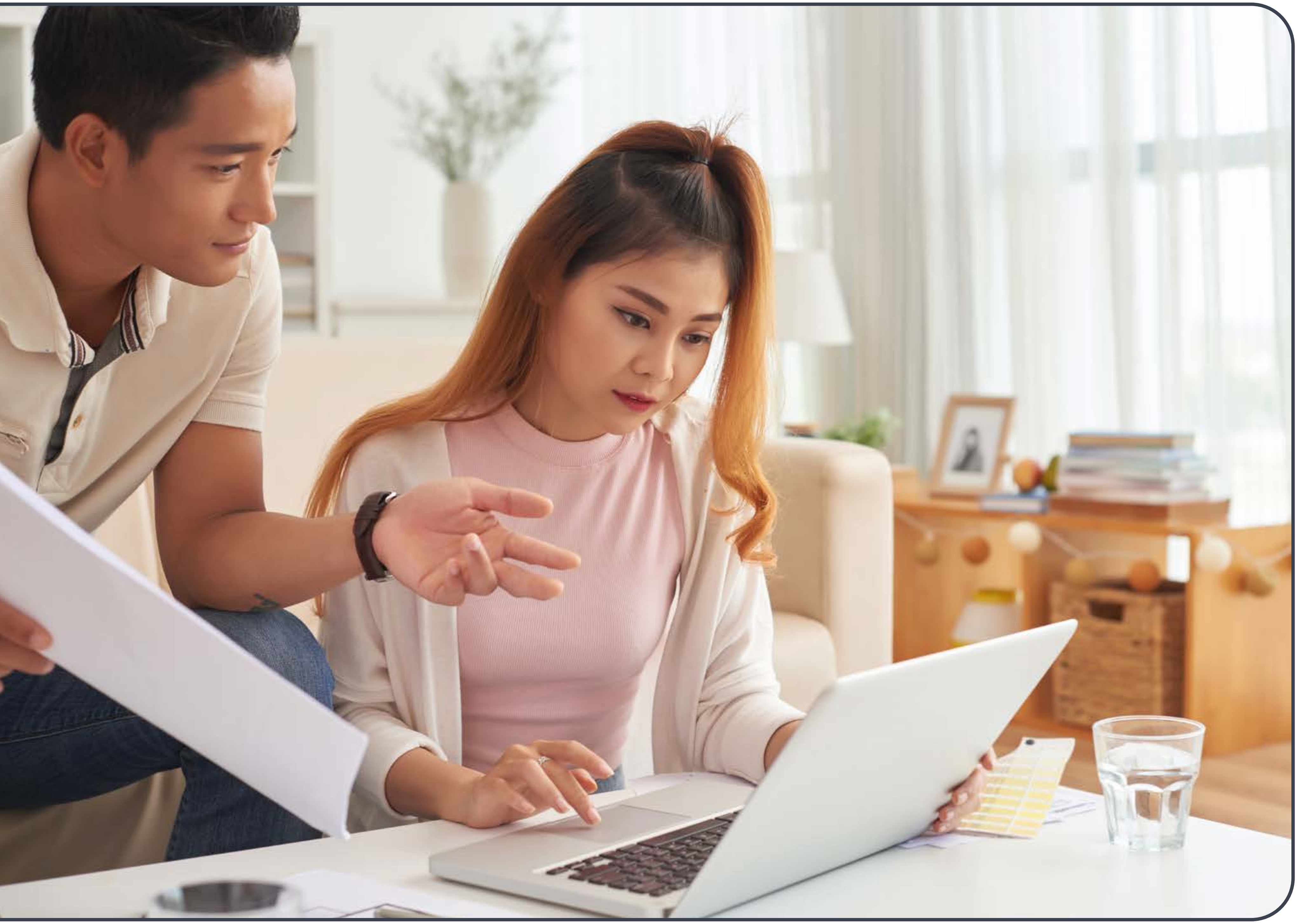
Top performers do this six times more frequently than bottom performers.

3. Use third-party payment recovery software

Top performers do this 12 times more frequently than bottom performers.

4. Use multiple tools to track and recover failed payments

Top performers use 1.7 times more tools than bottom performers, on average.



Best practices

Top-performing merchants are eight times more likely than bottom performers to track LTV and six times more likely to track failed payments.

LTV measurement and accountability are directly linked to company performance. Top-performing subscription-based companies — those that minimize revenue lost to failed payments — are more likely to track the drivers of LTV and customer churn more comprehensively. Over two-thirds of them specifically track payments — a leading contributor to involuntary customer churn.

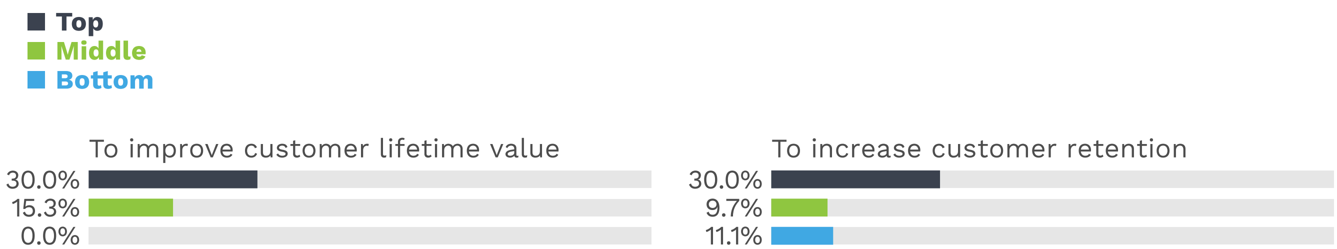
Indeed, our research discovered significant discrepancies in the share of subscription businesses tracking LTV-related metrics, particularly failed payments. Most notably, top performers are six times more likely to measure and analyze failed payments and 8.2 times more likely to measure customer LTV than their bottom-performing counterparts.

Top-performing subscription-based companies are also more likely to recognize the connection between failed payments and customer LTV. On average, 30% of these firms track and analyze failed payments to improve customer LTV, while none of their bottom-performing counterparts did so. Additionally, top performers are much more likely to measure failed payments to improve customer retention, with 30% of these firms doing so on average, compared to just 11% of bottom-performing companies.

FIGURE 6:

Top reasons for tracking failed payments

Share of firms citing select reasons as most important in their decision to track failed payments, by failed-payments recovery performance



Source: PYMNTS
The State Of Subscription Business, January 2023
N = 91: Companies that measure failed payment metrics, including failed payments, payment recovery rates and LTV following failed payments, fielded Sept. 12, 2022 – Sept. 28, 2022

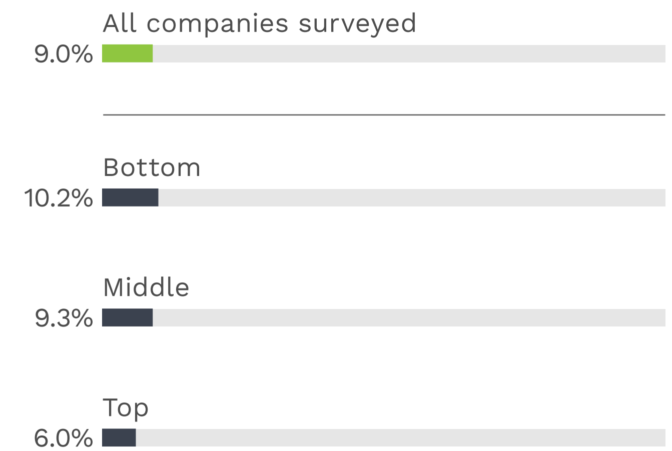
Top performers recover 60% of failed payments.

Recognizing that failed payments are a leading cause of involuntary customer churn and adopting methods to measure and analyze this metric can reduce a company's churn rate and, by extension, improve LTV and revenues. PYMNTS' research found that companies in the subscription industry lose, on average, 9% of revenues due to failed payments, totaling an estimated $278 billion over the past 12 months across the five industry sectors included in the study.

FIGURE 7:

The cost of failed payments

Average share of revenue lost to failed payments, by failed-payments recovery performance



Source: PYMNTS
The State Of Subscription Business, January 2023
N = 200: Whole sample, fielded Sept. 12, 2022 – Sept. 28, 2022

30%

Share of top-performing subscription companies that **track and analyze failed payments** to improve customer LTV

Subscription companies that track involuntary customer churn caused by failed payments are twice as likely to be top performers in minimizing revenue lost to failed payments. Our research also found that top performers, on average, lose 70% less revenue due to involuntary churn caused by failed payments than bottom-performing companies. Notably, when compared to bottom-performing companies, they are more effective at recovering a higher share of failed payments, resulting in a failed payment recovery rate that is 13% higher than that of bottom performers.

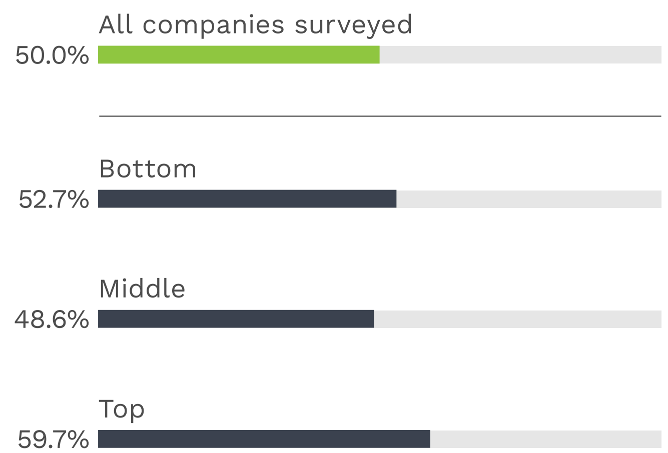
61%

Share of **failed payments recovered** by firms that track LTV following failed payments

FIGURE 8:

Recovered revenue from failed payments

Share of failed payments that firms recover, by failed-payments recovery performance



Source: PYMNTS
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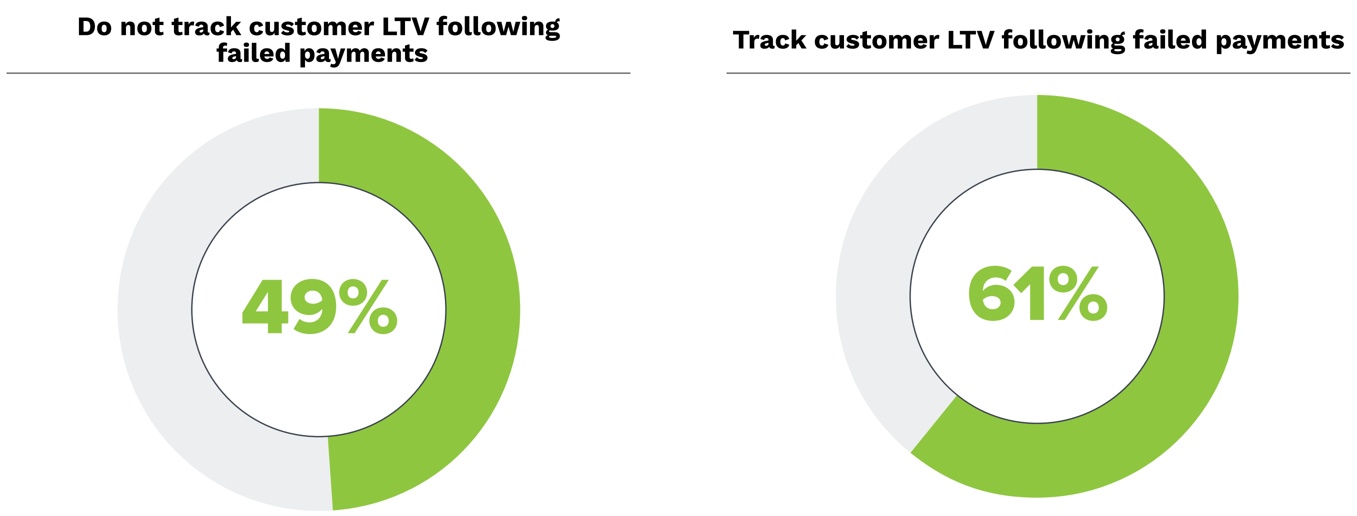
Although only 8.5% of subscription-based companies measure the LTV of customers retained due to successful failed payments recovery, these businesses tend to be leaders in this area.

Firms that track LTV following failed payments recover, on average, 61% of those payments, while those that do not track this metric recover only 49% of failed payments, on average. Moreover, top-performing companies are 1.5 times more likely to track LTV following failed payments than bottom-performing ones, highlighting the importance of aligning LTV with tracking metrics and taking action to improve failed payment recovery rates.

FIGURE 9:

Failed-payment recovery rate

Average failed-payment recovery rates, by whether companies track LTV following failed payments



Source: PYMNTS
The State Of Subscription Business, January 2023
N = 200: Whole sample,
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Top performers use multiple tools to track and recover failed payments. They are 12 times more likely than bottom performers to use third-party payment recovery software.

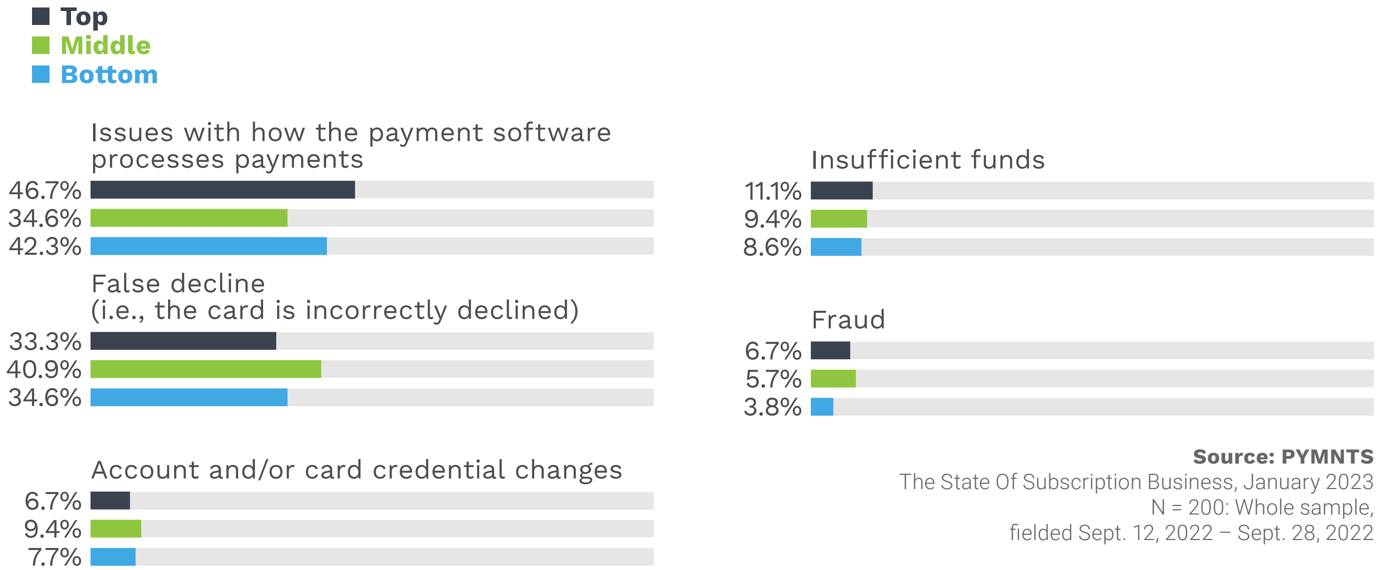
Failed payment transactions can significantly impact the revenue of subscription-based businesses — but actionable solutions can address this issue. Our research shows that top-performing subscription providers minimize revenue loss from failed payments by adopting a multifaceted approach that includes tracking multiple metrics, implementing specialized payment recovery solutions and having a thorough understanding of the factors that lead to customer churn.

Our data also reveals that 47% of top-performing subscription businesses recognize that most failed payments are attributed to problems with payment processing software — and they take action to address this issue. On average, these firms employ 3.1 different payment recovery methods to minimize revenue loss, compared to the 1.8 payment recovery methods their bottom-performing counterparts use.

FIGURE 10:

Top causes of failed payments

Share of firms citing select reasons for experiencing failed payments, by failed-payment recovery performance



Source: PYMNTS
The State Of Subscription Business, January 2023
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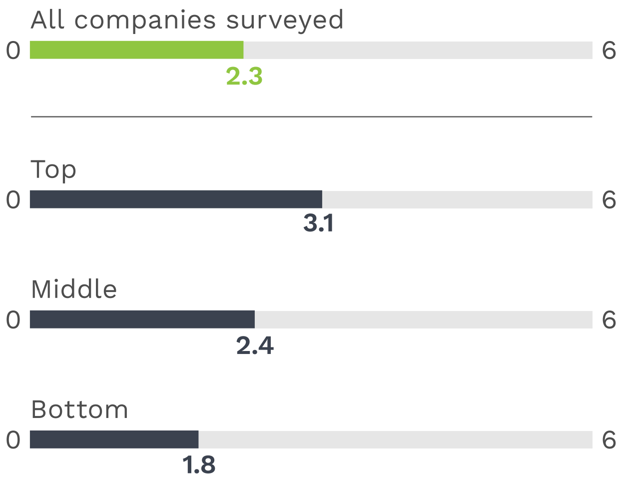
Top-performing companies in the subscription space are also 12 times more likely to use third-party payment recovery software solutions than bottom-performing companies, at 47% versus 3.8% — and they recover 13% more failed payments. This underscores the significant financial benefits of adopting a comprehensive approach to addressing failed payments.

FIGURE 11A:

Top firms employ more failed payment recovery methods

Average number of payment recovery methods firms use, by failed-payment recovery performance



Source: PYMNTS
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N = 200: Whole sample,
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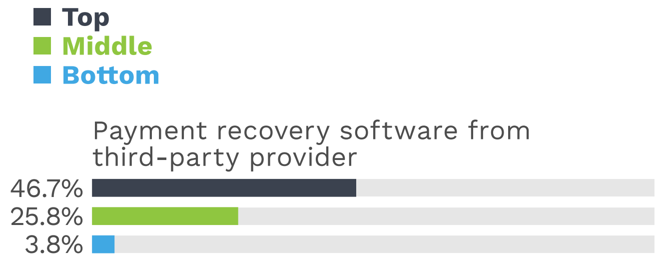
FIGURE 11B:

Top firms employ more failed payment recovery methods

Share of companies that use third-party payment recovery software, by failed-payment recovery performance



Source: PYMNTS
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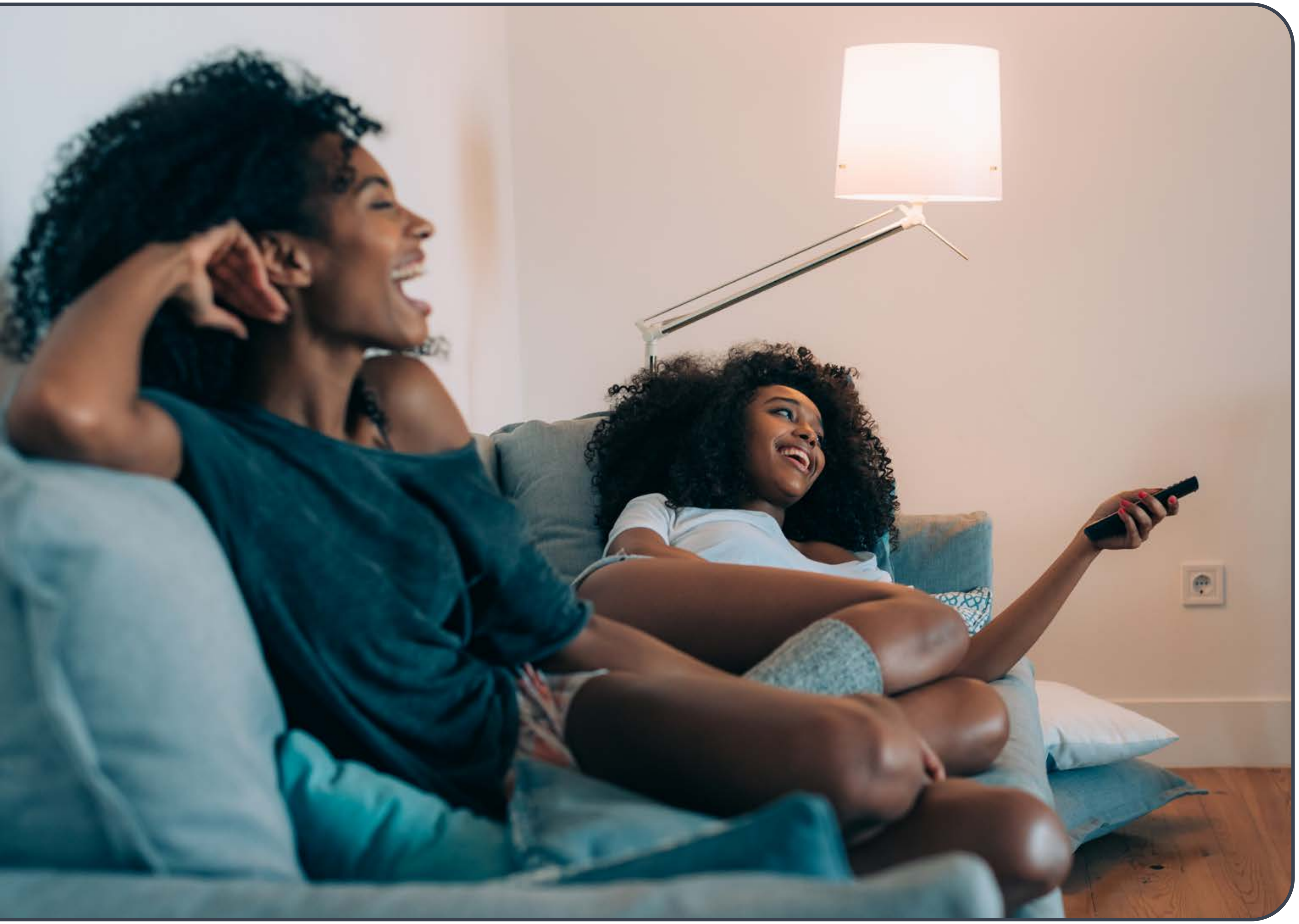
47%

Share of top-performing subscription businesses that recognize that most failed payments are **attributed to problems with payment processing software**



Organizational alignment

Two-thirds of subscription businesses do not report customer churn rates to senior management.

Our research has uncovered significant gaps in subscription-based companies' organizational stances regarding the role of LTV and customer churn in driving business performance.

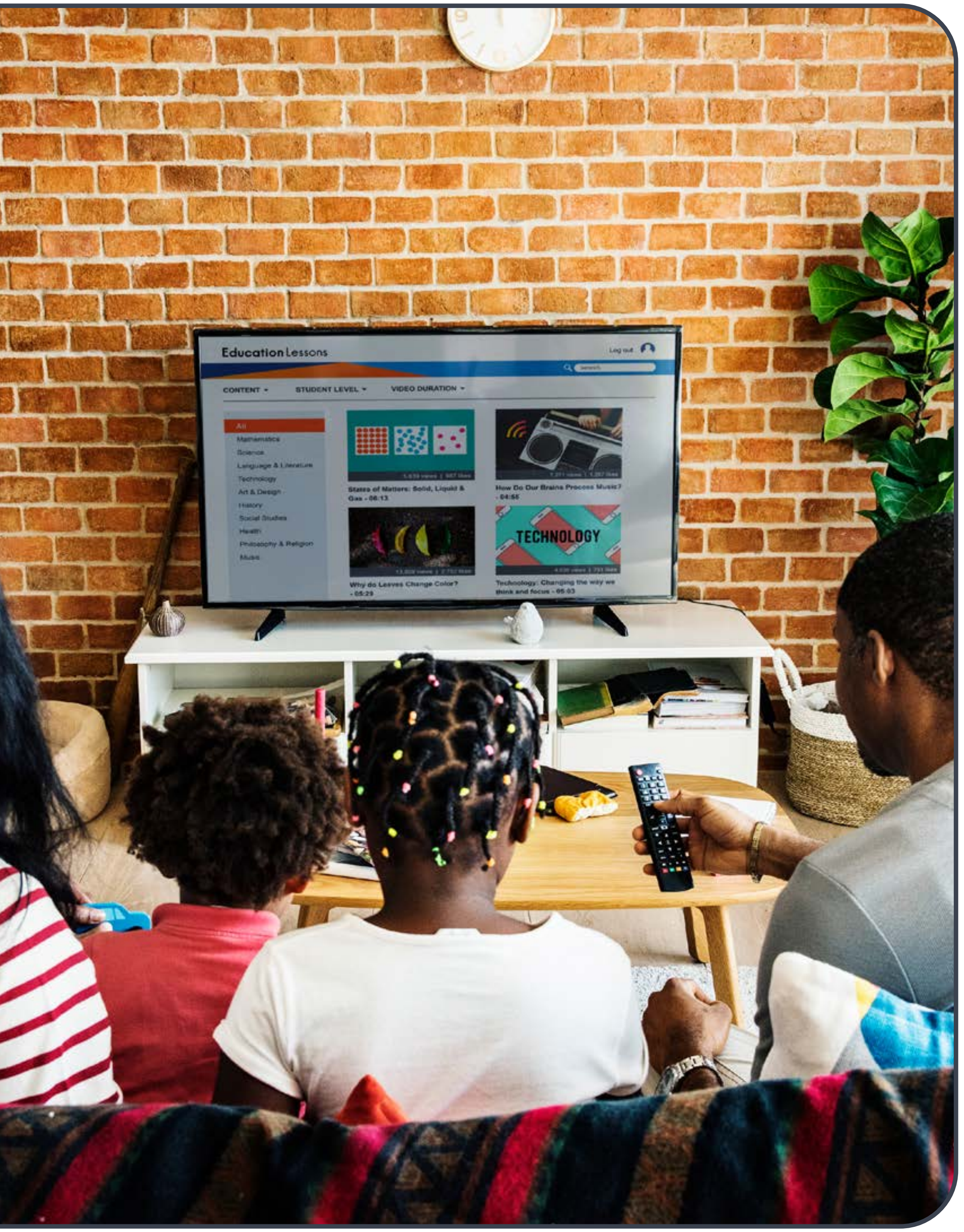
We found a disconnect between the data being collected by sales or analytics teams and the metrics being reported to senior management. While all subscription-focused businesses included in our study tracked customer churn in some way, only 36% explicitly reported churn rates to management. This lack of alignment can hinder the ability of senior management to make informed decisions based on key performance indicators.

Similarly, while two-thirds of companies recognize the negative impact of failed payments on customer LTV, only 15% track this metric, further emphasizing the importance of prioritizing data tracking and reporting to drive business success.

Chief subscription officers are emerging as the organizational stewards of LTV, focused on aligning business performance to the customer experience.

The role of chief subscription officer is gaining prominence as a key player in driving business success through the alignment of LTV and customer experiences. Our survey found that while less than 5% of subscription-based companies currently have a chief subscription officer in their C-suite, 40% of the firms that do are top performers.

These executives prioritize failed payments recovery strategies and tracking metrics that are closely linked to the customer experience, payment practices and LTV. Overall, the presence of a chief subscription officer is associated with improved business performance in the subscription industry.



Conclusion

To maximize profits and stay ahead of the competition, subscription businesses must understand the links between failed payments, involuntary churn and customer LTV. Failed payments are the top cause of involuntary churn, which wipes out hundreds of millions of dollars in revenue annually by reducing LTV. While most subscription providers do track churn or retention, only a small fraction measure customer LTV — and fewer still focus on the underlying causal relationship between failed payments and involuntary churn.

Our research has identified a set of best practices widely used among firms that succeed most at minimizing revenue lost due to failed payments. First, these top performers track and analyze customer LTV and failed payments. Second, they use multiple tools to track and recover failed payments, particularly third-party payment recovery software. A few top performers also have a chief subscription officer in their C-suite — something we expect to become more common.

By focusing on customer LTV and its drivers, and following the best practices identified in this report, subscription businesses can improve customer retention and boost commercial and financial performance.

About

PYMNTS

PYMNTS is where the best minds and the best content meet on the web to learn about "What's Next" in payments and commerce. Our interactive platform is reinventing the way companies in payments share relevant information about the initiatives that make news and shape the future of this dynamic sector. Our data and analytics team includes economists, data scientists and industry analysts who work with companies to measure and quantify the innovations at the cutting edge of this new world.

FlexPay

FlexPay was founded by online merchants and payments industry veterans who recognized the friction in the payments ecosystem caused by the lack of data transparency, and misaligned priorities between payment authorization systems, merchants and customers.

We have a deep and long history with both acquiring and card-issuing banks. This is how we understand the systems that control the transaction approval processes within issuers for card-not-present transactions, known as a "risk decline system."

The FlexPay platform delivers the highest failed payment recovery rates while also optimizing critical subscription business priorities. FlexPay understands that subscription businesses must recover the customers and revenue lost to failed payments, without sacrificing customer retention and merchant account health. To learn more, visit flexpay.io.

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