SaaS Checklist/Evaluation

* Why is SaaS different?
  + Like any busines, success will be determined by the company’s ability to generate free cash flow. Economics of business and the way financial statements work creates slightly different dynamics than other firms
  + Revenue for the product/service comes over an extended period of time while investments to acquire that revenue are made up front and typically flow entirely through the income statement vs cash flow/capex
  + There are three keys to success in a SaaS business:
    - Acquiring customers
    - Retaining customers
    - Monetizing customers
* **Acquiring customers**
  + Who is the customer?
    - Consumer/SMB- higher churn, lower LTV but also lower CAC
    - Enterprise- lower churn, higher LTV, higher CAC
  + TAM?
  + Sales cycle- self-service, inside sales, outside sales- will have implications on margins, sales cycle length, retention
    - All can work- Atlassian/TWLO, Appfolio, Workiva
  + How much is the company paying to acquire a subscriber?
    - CAC = S&M / new subs. Ideally know how much of S&M goes to new subs versus customer success.
    - How is this trending over time?
  + APRU – how is this trending over time?
  + Subscriber growth versus revenue/ARR growth
  + Sales efficiency
    - How long until company recoups CAC-CAC payback. S&M divided by incremental gross profit/ Less than 24 months is good.
      * Can also do CAC / (ARPU x GM)
    - Magic number- incremental recurring revenue/S&M spend during the period
      * How much new rev is coming from $1 spend in S&M. Above 1 is really good and above .75 is pretty good
      * Efficient GTM helps- self serve, virality, ability to sell into base
  + Cohort curves
    - How does ARR from cohort of customers trend over time?
    - How does churn compare across cohorts and trend over time?
  + Employee count
* **Product/customer- retaining**
  + What problem does the product solve?
  + Is the product replace an incumbent software provider? An inhouse solution? Or greenfield opportunity?
  + To what degree is the product engrained in the customer’s workflow? Switching costs.
    - Is it a system of record- serve as backbone for certain business process
    - Vertical software usually pretty good at this.
    - Does software run mission critical business process?
    - Does software store proprietary business data?
    - Do large portions of the customer employee base interact frequently with the software?
  + Evaluating- churn/ logo retention
  + Integrations with other applications?
* Monetizing- What problem does the software solve?
  + Look at net dollar retention
  + Is it priced on a usage basis? Seat basis?
  + ‘Delivering a service that can be metered and grows in tandem with the growth of your underlying customers is the gold standard of pricing strategies. And thanks to cloud service providers, companies now expect to only have to pay for what they compute, down to the nanosecond’
  + Opportunities for dollar expansion with the existing customer base?
    - Ex APPF- charges on a per unit basis then also layers on additional services on *a la cart* basis, can grow within its customer base.
  + Opportunities for scalable/multi axis pricing
    - Number of features
    - Number of users
    - Depth of usage- ie mailing list size, database size (best if it can grow automatically)—However, we need to pay attention to the incremental value of the database can bring.
    - Quality of support
    - Find features/ other things to move customers along spectrum from free to highest value
  + Value-based pricing- try to find a way to estimate value
  + Opportunity to increase price
  + Cross-sell
  + Differences across customer base? Ie large customer growth vs small customer growth
* Metrics to watch- make sure that narrative is aligning with numbers
  + Revenue/ARR growth
    - Both % and $
  + Billings
  + Customer growth- segmented by ACV
  + Logo churn
  + Dollar retention
  + LTV/CAC
  + Gross margin
  + Opex/OPM/Incremental OPM
  + Free cash flow- working capital benefit?
  + Rule of 40%- revenue growth + Free cash flow margin
* Laws of the cloud
  + Scale usually wins. Expanding to new TAMs and building adjacent products is important
  + Growth at optimal cost
    - Large markets can have high burn initially but longer term the model must be self sustaining
  + In S&M, invest behind what works. Make sure reps are hitting quotas and invest in what is delivering the best marginal productivity
  + Product as a competitive advantage- product matters more than ever- product first evaluations and bottoms up distribution models can build very large businesses. Even for B2B, need customer-like UX. Adopt an API-first dev mentality to avoid wasting time on things that already exist
  + 5C’s of finance
    - Committed annual recurring rev
    - Cash flow- usually best to get it upfront- customer is funding investments
    - CAC payback period- SMB should be 6-18, enterprise can be 24-36
    - Customer lifetime value- contract value adj by churn or upsell rate, x gross margin, subtracted CAC. Track based on multiple segments to identify most efficient channels
    - Churn- avoid the leaky bucket- investments in customer success can be high return
  + Discover secret KPIs
    - Product or company specific metrics that provide more granularity into usage and customer behavior
    - Ie TWLO- messages sent
    - Can be leading indicator
  + Customer success is company success
    - New logos are important early on but renewals and upsells become biggest inputs into enterprise value
    - Renewal dollar is ARR is cheaper to acquire than new logo dollar of ARR
    - Great sales orgs still struggle with leaky buckets
    - Scaling becomes harder if you have high churn- need to replace larger and larger amount of revenue
  + Impact through engagement or insight
  + Culture matters
  + Map fuel stops