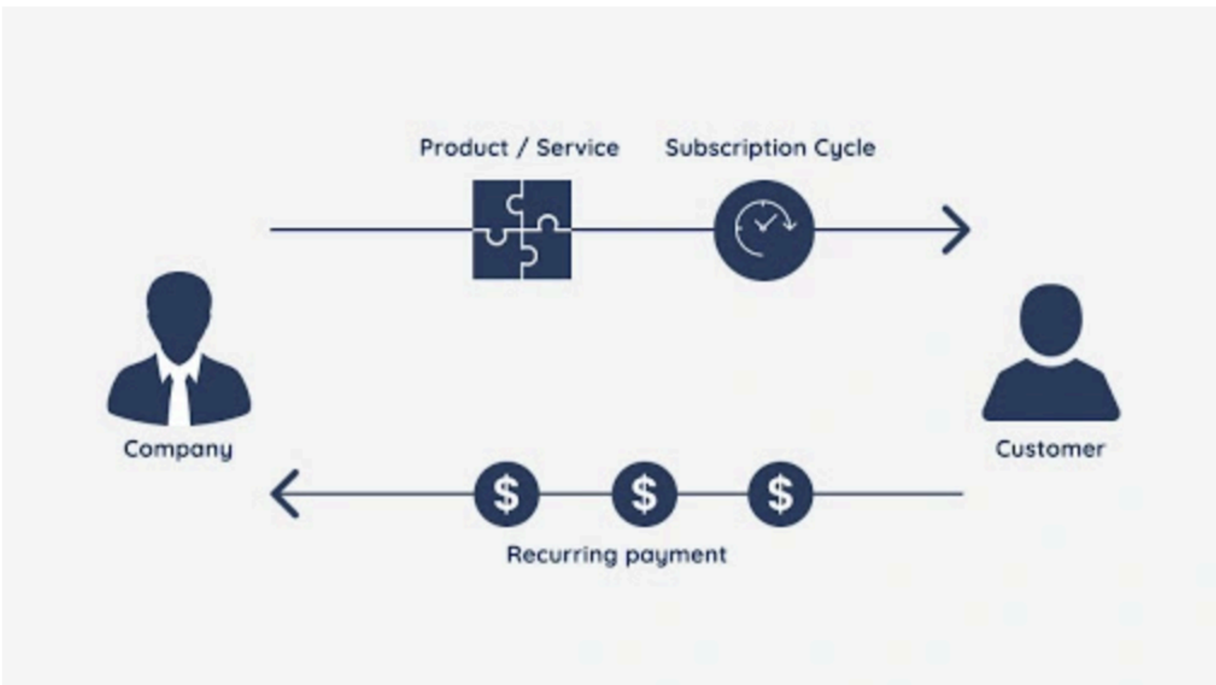
Subscription Business Model

(Subjective Research Case Study)

What is a subscription business model?

Think of a subscription as a contract between business and the customer. The customer agrees to pay for a product or service for a period of time and the business fulfills that offer so long as the customer completes their recurring payments. When the contract is up, the customer has the option to renew or cancel their subscription.

The diagram below illustrates what this looks like



This case study explores how Netflix and Amazon Prime have successfully managed customer churn and increased customer lifetime value (CLV), emphasizing the interplay between strategies, challenges, and outcomes.

Understanding CLV and Churn in Subscription-Based Models

- **Customer Lifetime Value (CLV)**: The total revenue a company can expect from a single customer throughout their relationship. High CLV indicates strong customer loyalty and profitable long-term relationships.

  Customer Lifetime Value = (Customer Value * Average Customer Lifespan)

- **Churn Rate**: The percentage of customers who cancel their subscriptions within a given time frame. Reducing churn is critical to maintaining a healthy subscription base and maximizing CLV.

  Churn Rate = Lost Customers ÷ Total Customers at the Start of Time Period) x 100

Some other metrics to track

- **Net Promoter Score (NPS):** a higher NPS can indicate customer satisfaction, referrals and loyalty, leading to higher CLV over time.
- **Customer Acquisition Cost (CAC):** Track how much it costs to acquire a new customer. For CLV to be meaningful, it should significantly exceed the CAC. Subscriptions decrease customer acquisition costs.
- **Average Subscription Length**:Track the average duration customers remain subscribed. A longer average subscription length suggests better retention and lower churn.
- **Engagement Metrics**: Monitor metrics such as login frequency, usage of services, or interaction with emails. Higher engagement often correlates with lower churn.
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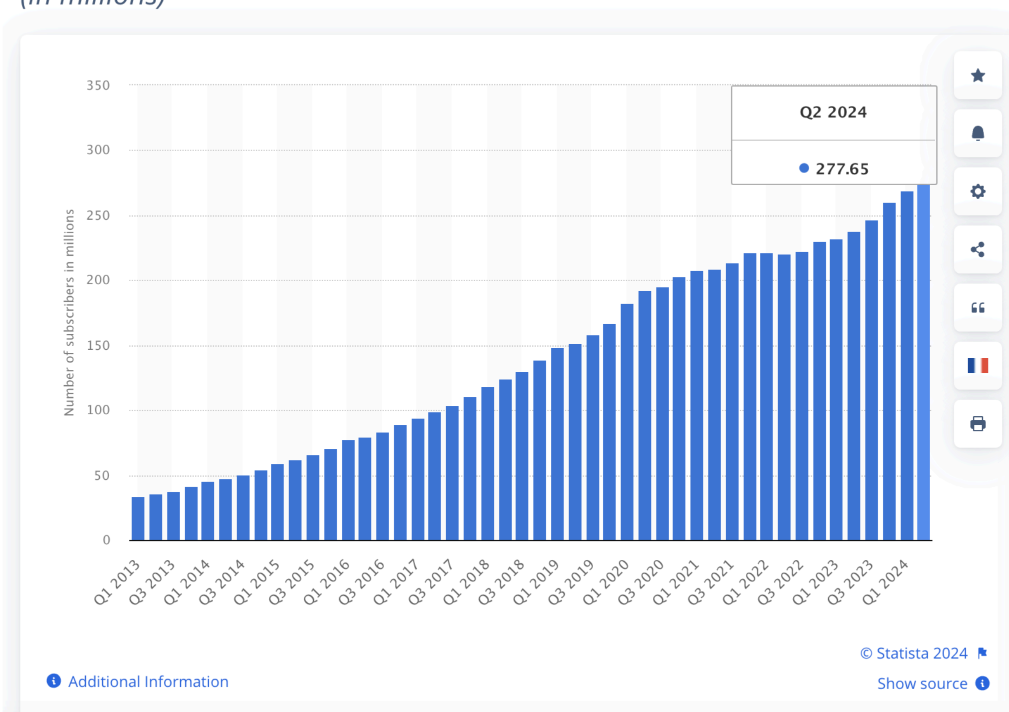
Case Study Netflix(Streaming service)

Netflix is a subscription-based streaming service that allows its members to watch TV shows and movies on an internet-connected device. Depending on their plan, users can also download TV shows and movies to your Android phone or tablet, iPhone, iPad, or Google Chromebook device and watch without an internet connection.

- **Strategies**:
  - **Content Personalization through Innovation**: Netflix follows a **data-driven and customer-centric strategy** to deliver a seamless experience. It uses data-driven algorithms to personalize content recommendations, keeping users engaged and reducing the likelihood of cancellation. For example, if a Netflix user likes Rocky, it will also offer them sports documentaries.
  - **Global Expansion**: Expanding its content library globally to cater to diverse audiences. As per livemint Netflix has over 277.7 million paid members from over 190 countries.
  - **Integrated viewing experience:** Multi-device and up-to-date no matter where you view it from, makes the experience combined.
  - **Emotional Connection through new experiences:** Netflix introduced interactive features such as watch parties and game-like viewing experiences, for example Black Mirror Bandersnatch which gave different people different endings depending on the choices they made during the film, it has added another layer to the experience provided by Netflix.
- **Challenges**:

- **Content Licensing**: Securing rights to content in different companies and regions. Like, they have a deal with Disney to license movies released between January 2016 and December 2018, but they can't stream these until 2026. This gives competitors ample time to eat into Netflix's customer base.
- **Competition**: Increasing competition from other streaming streaming companies such as Disney + and Amazon Prime. Disney+ offers arguably better content at a lower price, making it a more attractive option for viewers.
- **The Binge-Watching Dilemma:** Netflix's model of releasing entire seasons at once has led to binge-watching but also makes it easy for customers to subscribe for just a month and then cancel. This is detrimental to customer retention and long-term profits.
- **The social media threat:** The rise of short-form content and decreasing attention spans pose a significant threat to Netflix's long-form content model.

(in millions)



Number of Netflix paid subscribers worldwide from 1st quarter 2013 to 2nd quarter 2024

Case Study Amazon Prime(Streaming + Perks subscription business model)

Amazon Prime is a membership program where subscribers pay a monthly or annual fee (currently 799 in India per year) to get perks like free shipping, same-day grocery delivery and unlimited digital content. For subscribers who place orders often, this represents significant savings. Amazon Prime Video stands out as one of the top perks available to Amazon Prime members, others perks are amazon prime gaming, prime music, prime reading.

- **Strategies**:

- **Bundling Services**: Offering a variety of services like free shipping, streaming, and exclusive deals under one subscription.
- **Convenience and Affordable Services**: Emphasizing the convenience and value proposition of Prime membership. Reduced churn as customers found value in multiple services, making cancellation less likely.
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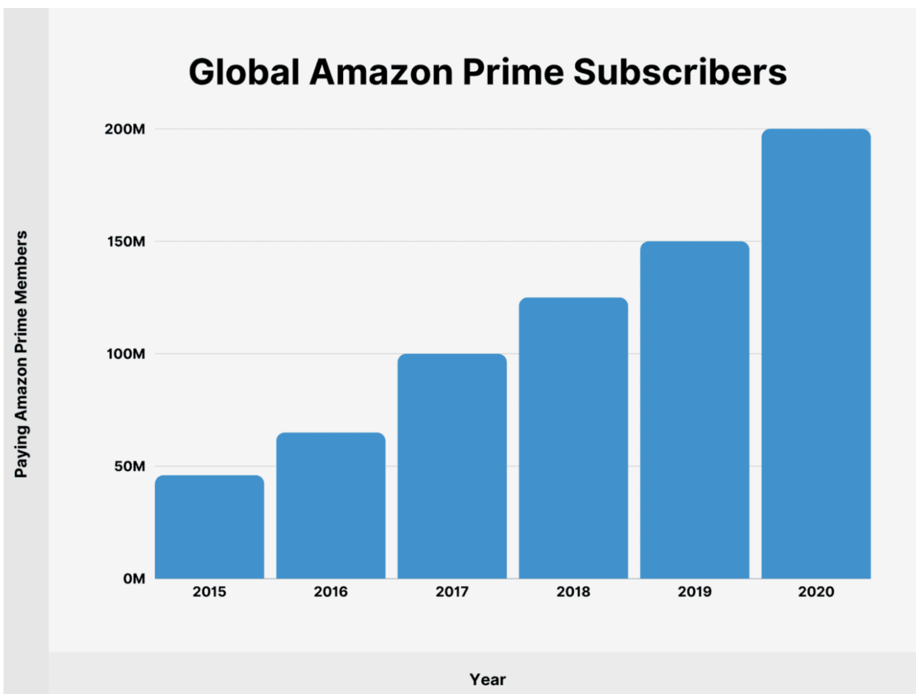
- **Challenges**:
  - **Cost Management**: Balancing the costs of offering multiple services with maintaining a profitable subscription model.
  - **Customer Expectations**: Continuously meeting high customer expectations across diverse services.
  - **Limited Original Content**: Unlike its competitors like Netflix, Amazon Prime Video lacks a robust library of original content.



Factors Influencing the decision to subscribed and remain subscribed, increasing the CLV:

1. **Ongoing Perceived Value**: Customers will continue their subscription if they consistently perceive the service as valuable, providing a good return on investment.

2. **Personalization**:Tailored offerings that meet the specific needs or preferences of the customer can increase the likelihood of a subscription. Personalization in marketing messages, product recommendations, and pricing can be persuasive.
3. **Customer Experience**: Positive interactions with customer service, ease of access to the product or service, and a hassle-free experience all contribute to customer retention.
4. **Content or Product Freshness**: Regular updates, new content, or product variations can keep customers engaged and prevent boredom, reducing the likelihood of cancellation.
5. **Rewards and Loyalty Programs**:Offering rewards for continued subscription, such as discounts, exclusive content, or early access, can incentivize customers to remain subscribed.
6. **Customization and Flexibility**:Allowing customers to customize their subscription plans or pause/resume their service without penalty can increase satisfaction and retention.
7. **Emotional Connection**:Building a strong emotional connection with customers through brand storytelling, community engagement, and shared values can foster loyalty.

Factors Influencing the Decision to Cancel, causing customer churn:

1. **Perceived Decline in Value**: If customers feel that the service no longer justifies the cost, they are likely to cancel their subscription. This could be due to price increases, declining quality, or a mismatch between expectations and reality.
2. **Financial Constraints**: Economic factors such as personal financial difficulties, job loss, or broader economic downturns can lead to subscription cancellations.
3. **Poor Customer Service**: Negative experiences with customer support, unresolved issues, or difficulty in managing the subscription can push customers to cancel.
4. **Competitive Alternatives**: The availability of better or cheaper alternatives can entice customers to switch services, leading to cancellations.
5. **Lack of Engagement**: If customers are not regularly using the service, they may question the need to continue paying for it and eventually cancel.
6. **Complex or Rigid Cancellation Process**: A cumbersome or frustrating cancellation process can drive customers away, especially if they feel trapped in a subscription they no longer want.

Conclusion and Actionable Insights

The success of subscription-based e-commerce companies in reducing churn and increasing CLV hinges on understanding and addressing customer needs and expectations. Studies have shown that companies that invest in customer-centric strategies see a marked improvement in both CLV and churn rates. Companies must continue to innovate and adapt their offerings, emphasizing personalization, value, and customer experience. By focusing on the right metrics, companies can ensure they are on the right track to achieving sustainable growth and profitability.