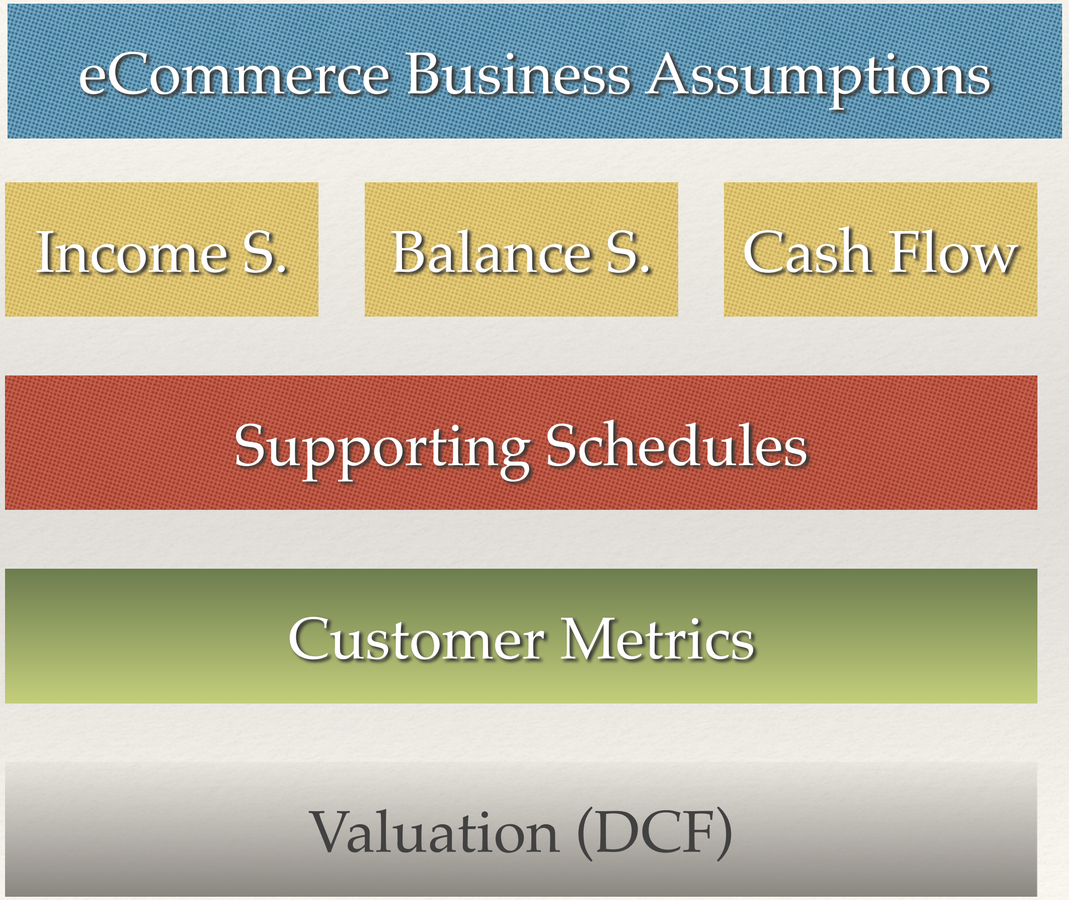
eCommerce Valuation

eCommerce Valuation

- The challenge with an eCommerce business is not in creating the financial model but in adapting the business drivers to address a very different type of business, when compared to a bricks and mortar firm

eCommerce Valuation

- The structure of the model is shown here
- We need to focus on the eCommerce Business Assumptions and the Customer Metrics to show how these differ from more traditional business models



eCommerce Valuation

- This approach can be used to value:
  - an eCommerce company
  - an Internet business
  - a Software as a Service (SaaS) business
  - a Website

eCommerce Valuation

- We are going to walk through the key eCommerce valuation metrics one by one…

eCommerce Valuation

- Monthly Unique Visitors
  - Traffic is the lifeblood of internet businesses
  - We want to know how many unique visitors come to the site each month
  - This is the top of the sales funnel
  - Based on SEO (earned traffic) and Advertising (paid traffic)

eCommerce Valuation

- Customer Conversion Rate
  - This is the rate at which visitors are converted into customers
  - This conversion may be measuring an opt-in to an email list in return for a lead magnet or even a small sale
  - Different companies measure "conversion" in different ways
  - You have to get your visitors taking action in some way

- Customer Conversion Rate = Signups per month / monthly unique visitors per month

eCommerce Valuation

- Bounce Rate
  - This is the measurement of people who arrive at your site and leave almost immediately
  - They take no action and are lost to you as customers (although you might cookie them or tag them with a Facebook Pixel to reach them later with advertising)
  - Single Interaction Visits
  - Divided by total number of site visitors
  - This can range from 20% which is low to 80% which is very high

- Bounce Rate = Number of visitors who leave without taking action/number of site visitors

eCommerce Valuation

- Average Order Value
  - The average order level is critical to revenues and profitability
  - The cost of getting a visitor to the site is a given
  - The more money you extract from them dictates the level of revenues and ultimately profits

- Average Order Value = Total Revenue from orders / Number of orders placed in a period

eCommerce Valuation

- Monthly Active Users
  - The important factor here is active users rather than having a long subscriber list who never engage
- Monthly Active Users = Sum of all users who have logged in to the website in a month

eCommerce Valuation

- Average Revenue Per User
  - ARPU
  - This takes into account non paying subscribers
  - A very useful metric for internet and eCommerce companies
  - ARPU = Revenue/Number of active users in a month

eCommerce Valuation

- Monthly Recurring Revenue
  - Recurring revenue is the highest value revenue to an internet business
  - This revenue repeats every month unless the subscriber cancels their subscription
  - Has a significant impact on business valuation
  - MRR = total of all revenue that renews on a monthly basis

eCommerce Valuation

- Revenue Run Rate
  - A very useful metric for early stage companies
  - Multiplies the current month by 12 to annualise it
  - More meaningful than summing up the historical 12 months in a fast growing business

- Revenue Run Rate = Monthly Revenue x 12

eCommerce Valuation

- Contribution Margin Per Order or Customer
  - By deducting cost of goods sold, shipping and fulfilment expenses we arrive at the gross contribution on average for each sale
  - This is a critical piece of information for eCommerce businesses and should be tracked weekly if not daily.

- Contribution Margin per Order = (Revenue - Direct Variable Costs)/No of Orders

eCommerce Valuation

- Contribution Margin after Marketing
  - CMAM
  - This includes marketing expenses into the calculation when calculating the margin per customer
  - It is important when discussing contribution margin to understand whether marketing costs are included or not

- Contribution Margin after Marketing = (Revenue - Direct Variable Costs - Marketing Expenses)/ Number of orders

eCommerce Valuation

- Customer Acquisition Costs
  - CAC
  - Another critical metric
  - Should focus only on new customers
  - Marketing spend may vary and the different marketing campaign types have differing metrics, which are shown here

- Customer Acquisition Costs = Marketing expenses / number of new customers
- CPM = Cost per 1,000 impressions
- CPC = Cost per Click
- CPA = Cost per Acquisition

eCommerce Valuation

- Churn Rate
  - This measures the rate at which customers cancel subscriptions
  - In order to grow, new customer growth must exceed customers who cancel
  - This is another critical metric and its trend is also important to a growing internet business

- Churn Rate = Number of Customers Lost / Total Customers

eCommerce Valuation

- Burn Rate and Runway
  - Venture Capital firms watch the Burn Rate very quickly
  - Loss making business “burn” cash
  - The total cash holding when divided by the burn rate tells you how many months of cash the company has i.e. its runway

- Burn Rate = Average cash consumed by the business per month

eCommerce Valuation

- Life Time Value
  - LTV
  - This calculates the life time value of a customer to the business
  - How much do they pay for the time they are subscribed?
  - Contribution margin per customer per year
  - Do not use revenues for this calculation

- Life Time Value = Contribution Margin after Marketing / Churn Rate

eCommerce Valuation

- Life Time Value/CAC Ratio
  - This makes comparisons between companies possible
  - If the CAC is $25 and the LTV is $125, then the LTV/CAC ratio is 5x, the higher the better
  - LTV/CAC = Life Time Value / Customer Acquisition Cost

eCommerce Valuation

- Payback
  - CAC/CMAM
  - How many orders does a customer have to place in order to pay back their cost of acquisition?
  - This assumes that repeat customers cost nothing although they may still click on ads and paid links when return to the site

- Payback = Customer Acquisition Cost/ Contribution Margin after Marketing

eCommerce Valuation

- Viral Coefficient
  - The viral coefficient is the number of new users the average customer generates.
  - The viral coefficient is not simply the number of referrals a customer makes, it's the number of those referrals that convert into customers.
- Viral Coefficient = (number of existing customers x number of invitation sent per user)/number of existing customers

eCommerce Valuation

- eCommerce Valuation Model
- Created an Excel model, available to download

eCommerce Valuation

- Input monthly data into the green cells for:
  - Website
  - Conversions
  - Customers
  - Revenue
  - Expenses
  - Cash Flow

Inputs (monthly)		Code Letter	Input
Website Inputs			
Monthly Unique Visitors		A	
No of Visitors who hit back button or closed browser (single interaction visits)		C	
Total Visits to Site		D	
Sum of all users active on website in a month		G	
Conversion Inputs			
Number of invitations sent per User		P	
Invitation Conversion Rate		Q	
Number of Signups per Month		B	
Customer Inputs			
Number of New Customers		K	
Number of Lost Customers		L	
Total Customers		M	
Income Statement Inputs			
Total Revenue from Orders in a month		E	
Number of Orders Placed in a month		F	
Monthly Recurring Revenue		H	
Expense Inputs			
Direct Variable Costs		I	
Marketing Expenses		J	
Cash Flow Inputs			
Cash losses per month		N	
Total Cash Month End Balance		O	

eCommerce Valuation

- The outputs from the model will calculate the metrics discussed in this lecture for you
- The formulas are shown in the output section too so that you can track and understand the calculations

Valuation Metrics	Acronym	Formula	Output
Monthly Unique Visitors		A	0
Customer Conversion Rate		A/B	⚠
Bounce Rate		C/D	⚠
Average Order Value	AOV	E/F	⚠
Monthly Active Users	MAU	G	0
Average Revenue per User	ARPU	E/G	⚠
Monthly Recurring Revenue	MRR	H	US$0.00
Revenue Run Rate		E x 12	0
Contribution Margin per Order	CM	(E - I) / F	⚠
Customer Acquisition Costs	CAC	J/K	⚠
Contribution Margin after Marketing	CMAM	(E - I - J) / F	⚠
Churn Rate		L/M	⚠
Burn Rate		N	US$0.00
Cash Runway (months)		N/O	⚠
Life Time Value of a Customer	LTV	(E - I - J) / F) / L/M	⚠
Long Term Customer Value to Customer Acquisition Cost Ratio	LTV/CAC	(E - I - J) / F) / L/M) / J/K	⚠
Payback	CAC/CMAM	(J/K) / (E - I - J) / F	⚠
Viral Coefficient		(M x P x Q) /M	⚠

eCommerce Valuation

- The metrics discussed in this lecture will help you to monitor your eCommerce business and contribute to your valuation model

eCommerce Valuation