9 KEYS TO BUILDING A SUCCESSFUL SUBSCRIPTION BUSINESS
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INTRODUCTION: THE SUBSCRIPTION ECONOMY

The rules of success are changing for all businesses, and there's a hunger for new ideas for how to drive growth. One key strategy is clear: a shift to recurring revenue or subscription-based business models. The shift to subscriptions is happening broadly across all industries, as consumers are changing their preferences for how they want to purchase, pay for and use products and services. For businesses, subscriptions represent a better business model built around recurring customer relationships where you’re paid over time as long as you deliver value. Zuora has coined this new world the Subscription Economy.

However, this shift to the Subscription Economy is not easy for businesses to operationalize, because how you price, sell, bill, collect payments and account for your subscription service is significantly more complex than in the traditional product world. Internal stakeholders, whether in Marketing, Operations, Finance, IT or General Management, must be prepared and aligned to support this transformation. This often requires knowledge of new processes and how to implement them.

Until now, there has been no blueprint for how to succeed in the Subscription Economy. In the past, businesses have had to forge their own path, learning through trial and error along the way. Business leaders today are thirsting for this knowledge and eager to connect with others on the same journey to share best practices and lessons learned about what’s worked and what hasn’t.

This paper is the first in a series Zuora created to help companies thrive in the Subscription Economy with practical guidance. Based on key insights gleaned from Zuora customers, partners and the community of subscription businesses at large, the series will continue with subsequent learning tools that dive more deeply into each of the components required for success.

A CLOSER LOOK

A recent global study by the Economist Intelligence Unit (EIU), sponsored by Zuora, provides compelling evidence of the shift to the Subscription Economy. This study surveyed nearly 300 senior business leaders in the United States, United Kingdom and Australia. These leaders offered insight into their preferences and plans for moving their businesses to new models of service delivery, along with their views on key drivers of change and expected benefits and risks in making the shift. The results? Four out of five respondents believe that their customers are changing how they prefer to obtain access to goods and services. 51% of businesses are in the process or already changing how they price and deliver goods and services. 40% of businesses surveyed are already starting to implement the subscription business model.

“As someone who has run operations in both the subscription and traditional models, I know how challenging it is in a subscription business,” said Bill Plummer, Business Enablement Officer at NCR Corporation. “I think a guide to help businesses based on real experience is a beneficial step for the growth of the Subscription Economy.”
This research by the EIU supports the transformation that we are seeing in industries around the world. The shift in software to SaaS began over a decade ago with Salesforce moving to a recurring revenue-based model. The momentum has been building since then as start-up after start-up was launched to disrupt traditional software models by providing cloud-delivered, subscription-software services in virtually every segment of the software industry. ServiceNow, Zendesk, Docusign, Box, Yammer, and Marketo are just a few of the hundreds of examples. And large established traditional software companies like HP, Informatica, Dell, and BMC Software have pivoted to subscriptions as they launched or acquired recurring revenue based SaaS services. And just in the last year, Adobe, one of the bellwethers of the software industry, shocked the world by saying they are embracing subscriptions 100%. According to Gartner, “By 2019, cloud computing and the new digital economy will cause subscription pricing to overtake perpetual licensing and maintenance.”

Perhaps nowhere has this trend been as transformative to an entire industry as in Media. Newspapers, magazines, television and music have all used subscriptions in various forms for a long time. But these media segments have largely relied on advertising as its core revenue source. When free online content proliferated and Google advertising drove traditional media advertising through the floor, the media industry was on the brink of collapse. Fortunately, global media companies like News Corp, The Financial Times, Fairfax Media, and IPC Media have all found reemerged with new growth strategies as they’ve launched next generation “Paywall 2.0” subscription models to monetize their content and services.

Sharing services are gaining popularity as new companies like AirBNB, RelayRides, HomeAway, City Car Club and others join the ranks of Zipcar. These innovative services provide consumers with convenient access to everything from cars to bikes to accommodations as you need them, without having to pay, store, and maintain them when you don't.

There's also growth in demand for membership loyalty programs provided by companies like Amazon and United Airlines, for which consumers subscribe to extra white glove benefits that enhance their service. Amazon Prime delivers unlimited free 2-day shipping, movie and television show streaming, and free Kindle book titles for $79 per year. Today, there are tens of millions of Prime members representing well over $1 Billion in annual membership fees. And Amazon benefits further as its customers spend on average 150% more after they become Prime members.

This list goes on. We are seeing this shift to subscriptions in industry after industry: in online education with Kaplan, in healthcare IT with CareCloud, in financial services with American Express, and even in personal care with GoodMouth and Dollar Shave Club, which are disrupting the multi-billion dollar consumer packaged goods industry.

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2 Source: Amazon, 2013

3 Source: Businessweek, 2010
A BETTER WAY TO RUN YOUR BUSINESS

A subscription model is a win/win for both end-customers and businesses. Customers benefit because subscription-based businesses are focused on customer success, earning trust and continually providing new offerings to meet customers' requirements. Businesses win because as long as they continue to meet their customers' needs, they will continue to earn a more predictable recurring revenue stream. In addition, businesses have direct insight into customers' usage patterns and can tailor new offerings based on real usage metrics. In the traditional product world, direct relationships between businesses and their customers were difficult to build, since businesses typically only interacted with customers at the time of initial sale, or not at all if it was sold through an indirect sales channel.

Many companies have already realized that a business model built on recurring revenues is a better way to run their business and that traditional approaches to running a business do not ensure success. In order to grow, companies must recognize and operate around four critical values:

- Developing deeper customer relationships versus selling one-time transactions
- Establishing dynamic, value-based pricing versus fixed, cost-plus pricing
- Delivering efficient, consumption-based services versus shipping unit after unit
- Measuring and reporting predictable, forward-looking revenue versus backwards-looking financial statements

Read more about the benefits of the subscription model for consumers and businesses in the EIU survey report here.

IS THERE A BLUEPRINT FOR SUCCESS?

As business leaders shift their business model to subscriptions, they are searching for knowledge and practical guidance on how to do it. They are asking questions such as, “How do I price effectively?” “What is the best way to launch a new service?” “How do I reduce the number of failed credit card transactions?” “What are the metrics I need to understand and grow my subscription-based business?” “How do I account for multi-year contracts?” “How do I reduce churn?” and “Do I build or buy a system to reliably support my business growth?” Many have turned to Zuora and its partners seeking answers to these questions and asking for a blueprint to guide their success.

“The shift towards subscription business models is driving companies to build better ways to run their businesses. In this new world, how you price, sell, bill, collect payments and account for your business is entirely different,” said Amy Konary, Research Vice President at IDC. “The community of businesses, analysts, and partners in the Subscription Economy have come together with Zuora to structure this framework of guiding principles to help every business become a successful subscription business.”
Over the past 6 years, Zuora has gathered input based on thousands of conversations with companies of all sizes like HP, DocuSign, Box, Reed Business Information, News Corp, Dell, Branchout, Mindbody, Ooyala, BorderFree, Dice, NCR and more, and distilled it down to analyze common themes. It turns out, when we did the synthesis, a very clear and consistent picture began to emerge.

THE 9 KEYS TO SUBSCRIPTION SUCCESS

Price. Find your sweet spot.
Dynamically adjusting pricing and packaging is the surest way to attract and retain customers, and multiply the value of your relationships.

Collect. Get paid.
Collect payments instantly through automated and manual channels, while maximizing completed transactions and minimizing write-offs.

Measure. No paper, no worries.
Analytics make forecasting, accounting close and audits a breeze. Plus, it gives you the right insight into your subscribers, so you can make smarter decisions.

Acquire. Go get ‘em.
Boost subscription rates with tools like flexible pricing, promotions, integrated quoting and multi-channel commerce.

Nurture. Build beautiful relationships.
Keep your customers engaged and happy. Seamlessly manage rapidly changing upgrades, conversions, renewals and other orders.

Iterate. Try something new every day.
Subscriptions can involve complex customer relationships. Zuora lets you iterate and test what’s working with just a couple of clicks.

Bill. Easy.
Subscriptions mean more invoices and more payments. Automatically generate fast, accurate bills and deliver them online.

Zuora plugs straight into your accounting software and General Ledger. Register subscription transactions and process deferred revenue with ease.

Scale. Get growing.
Zuora is built on a secure, scalable technology infrastructure. So wherever you start out, we’ll keep the system running as you grow.
Zuora has built a composite view of what it takes to build and run a successful subscription business. This was not an easy task. Distilling down the thousands of conversations with businesses clearly showed that there are nine core things that all subscription businesses are trying to do to drive success.

These key principles serve as a foundational blueprint for building and scaling a subscription-based business:

We then tested this “9 Key” framework over many months — first when we initially engaged with companies to talk about their business. We tested it during our implementations and by looking at support cases from live customers. We tested it by looking at what features are requested for us to build or enhance.

In mid-2013 we conducted a survey with 200 companies about the 9 Keys and affirmed that they are all important to the success of any subscription business — while individual keys may be prioritized at different times, a business must focus on the collective set as a whole. The survey also showed that businesses consistently recognize opportunity for improvement in their ability to perform each of the keys. Further, these companies also indicated that they are currently investing or planning to invest in these key capabilities in the next 12 months.

Figure 1: Respondents’ assessment of the 9 Keys by level of importance for their business, current level of capability in their business, and calculated gap between the two.

Source: Zuora market survey, June 2013, n = 200.
UNDERSTANDING THE 9 KEYS

1. PRICE in Support of Your Business Goals

In the Subscription Economy pricing and packaging is the most valuable strategic weapon because it’s directly tied to revenue growth and the strategic levers of acquiring new customers, increasing the value of existing customers, and/or reducing customer churn. But it turns out that subscription pricing and packaging is complex. You can price by number of users or capacity, by different time periods — monthly, quarterly, annually. You can utilize promotional models like freemium to hook in customers at no cost. You can discount for multi-year purchase to incent long-term use.

Zuora has identified hundreds of pricing and packaging strategies in the Subscription Economy. The key is to start simply with basic models and iterate rapidly over time as you learn from your customers. But you must have the operational systems to support you.

“Having the ability to manage complex pricing structures in a very transparent, organized manner, is really important for us to get a competitive advantage in the market.”
— Chris Purpura, VP & GM Cloud Platform, MuleSoft

2. ACQUIRE Customers Across Any Channel

Signing up customers for subscriptions needs to be a seamless user experience that can be done across multiple channels such as the web, mobile or through assisted sales. B2B companies with assisted sales models often want to create a quote for the customer before they buy. But this process can be difficult compared to one-time product sales. Your systems were not designed to support the elements of the subscription, such as term length and all the attributes of subscription pricing mentioned above.

These complexities in the customer acquisition process often lead to slow time-to-market and to single-channel commerce. Subscription businesses need to establish fast, simple, streamlined and automated customer acquisition workflow across multiple channels.

“Subscriptions get very complex very quickly.”
— Drew Martin, CEO, DriveCam
In a traditional business, products and services are purchased one-time and then invoiced for. In a subscription business, billing is more complex — businesses have to bill new customers at sale, prorate customers that sign up mid-month, bill existing customers at different times of the month, bill for usage and more. Without the right billing engine, it can take weeks to generate bills, errors may lead to frustrated customers, and it can be a challenge to scale.

The new complexities in billing posed by the Subscription Economy require extra focus for businesses to ensure accurate bills for their customers. The billing system needs to be a programmable engine that can take all the inputs you have to calculate bills accurately. Bills then need to be presented clearly in a way that supports a company’s brand and image.

“Our homegrown billing system had limited our ability to flex to the market needs.”
— Tom Gonser, Founder, DocuSign

In the product world, payments are relatively simple: You either paid for it up front, cash or credit, before being given the product, or companies would check credit history and open a line of credit, allowing the customer to pay on net-30 terms. That does not work with a recurring model.

Businesses deal with many more collections in the Subscription Economy, and the collections process is much more complex. Automation is the key to optimizing cash collections. Subscription businesses need to collect cash fast while maximizing collections and minimizing write-offs.

“Zuora has helped us completely streamline our back end processes”
— Gray Chynoweth, COO, DYN

Developing deeper customer relationships is at the core of the subscription business model, as it enables sustainable recurring revenue growth. As a company’s customer base gets bigger, this becomes one of the most important keys in the entire framework.

Acquiring new subscribers is critical, but in the Subscription Economy the vast majority of customer transactions consist of changes to existing subscriptions: renewals, suspensions, add-ons, upgrades, terminations, and more. As a result, businesses need to provide customers with intuitive and comprehensive tools to manage their accounts over the entire subscription lifecycle. Subscription businesses must give customers the control they
want or risk customer dissatisfaction, which leads to churn and revenue loss. In addition, businesses must closely monitor customer usage and adoption to mitigate churn risk.

“The Subscription Economy means we’re constantly engaging our customers.”
— Jackie Choy, Controller, PowerReviews

6. ACCOUNT for Revenue and Close Books Faster

A subscription typically has a large number of order transactions and changes over its lifecycle. This causes a complex ripple effect on bookings, billings, cash and revenue. Traditional GLs alone cannot handle the complex processes brought on by the subscription model such as revenue recognition rules, but businesses still need a GL to generate financial statements.

This challenge may not get addressed as a company initially launches its subscription offering. As a result, subscription finance processes end up manual in spreadsheets. Businesses need a way to streamline their accounting-close process and maintain compliance.

“It’s just not natural for a traditional accounting system to be able to manage subscriptions.”
— Lisa Bailey, VP of Business Operations, InsideView

7. MEASURE to Get Visibility Into the Right Customer, Subscription & Financial Metrics

Subscription businesses need to drive accurate and timely decisions, leveraging key metrics from bookings through revenue recognition that provide unparalleled insight into customer value and the financial health of the business. Traditional GAAP reporting will not go away soon, yet subscription businesses must also focus on metrics like ARR, retention rate, recurring profit margin, and growth efficiency index to be successful. Unfortunately, many businesses are flying blind since traditional financial systems can’t tell you these.

Learn more about the 3 Metrics That Matter here.

“With real data to inform the discussion, we’ve been able to make better business decisions faster”
— Jim Franklin, CEO, Sendgrid
8. ITERATE and Rapidly Deploy New Pricing

The Subscription Economy has infinite pricing options and many companies typically start with a simple recurring pricing model when launching their subscription offering. But markets can evolve quickly and customers’ needs will likely change over time. Competitors may enter with a differentiated offering.

It’s critical that pricing and packaging — a strategic weapon for driving growth — is flexible and dynamic. Subscription businesses need to rapidly iterate on pricing models to maximize subscriber acquisition and market share.

“We took customer feedback and entirely shifted our pricing model.”
— Donna Wells, CEO, Mindflash

9. SCALE With Mission Critical, Reliable and Secure Infrastructure

Subscription businesses need a reliable enterprise-grade system with services that are built on a secure, mission-critical and scalable infrastructure with reliable 7x24x365 operations and assured business continuity. B2C companies especially need the infrastructure support to scale rapidly. All companies need seamless integrations with commerce systems, payment gateways and other technology systems.

“Zuora is able to match our high growth and will deliver as we scale.”
— Joerg Rathenberg, VP Marketing, Cloud Passage

NEXT STEPS

This paper is the first in a series of papers and learning tools that will dive deeper into each one of these keys. Visit www.zuora.com/9keys for up-to-date information on the 9 Keys.
Zuora is the global leader in subscription commerce and billing, helping companies in every industry transition to the Subscription Economy. Enterprise leaders and high-growth companies alike use Zuora’s multi-tenant cloud platform to launch, scale, and monetize their subscription services. Zuora’s applications work where traditional ERP applications fail: Subscription pricing, quoting, orders, billing, payments, and renewals. Built from the ground up by SaaS industry veterans from salesforce.com, PayPal, and Netsuite, Zuora services innovative customers like Informatica, Tata Communications, Box, Xplornet, Ustream and Reed Business Information.

Learn more at: www.zuora.com.