Essential Sales Metrics for Startups

Sales is booming, but we can always make it better

Sales and marketing play an important role in growing the firm, but this oftentimes occur in an inefficient manner, where the cost of these functions overshadow the progress made by revenue growth. With a thorough understanding of a few sales metrics, you can further optimize your sales and marketing functions, lowering the cost needed to acquire customers and making the business more sustainable

Value Metrics

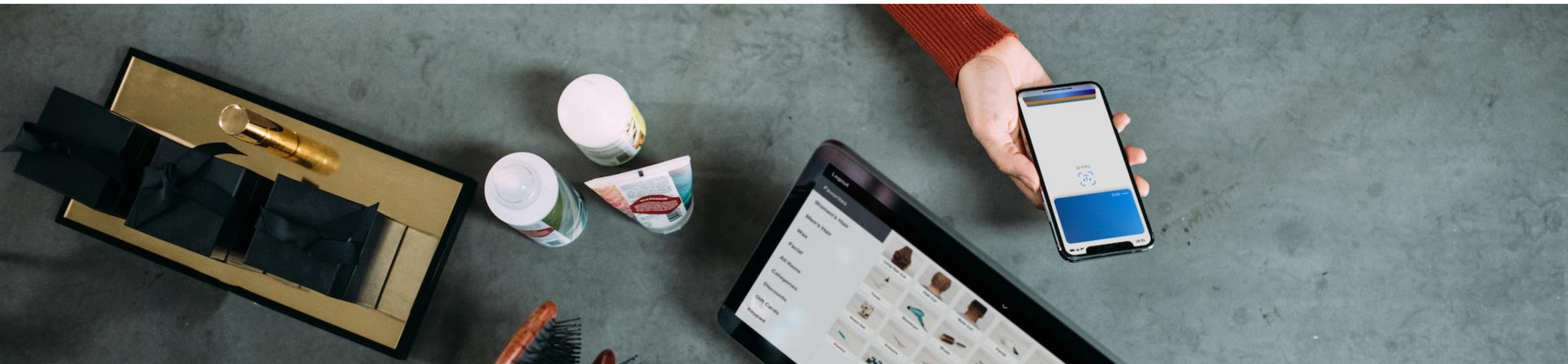
- These metrics are helpful understanding the value of customer relationships in a tangible manner. They are the key building blocks in calculating the Efficiency Metrics

- **Includes:**
  - Customer Lifetime Value
  - Customer Acquisition Cost

Efficiency Metrics

- These metrics are useful in understanding the cost-effectiveness of the sales and marketing strategies employed by the firm in acquiring new customers

- **Includes:**
  - LTV/CAC Ratio
  - CAC Payback Period



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Value Metrics: Customer Lifetime Value

Definition

- The Customer Lifetime Value (LTV) is the average amount of money the firm can expect to receive from a customer over the life of their relationship with the company

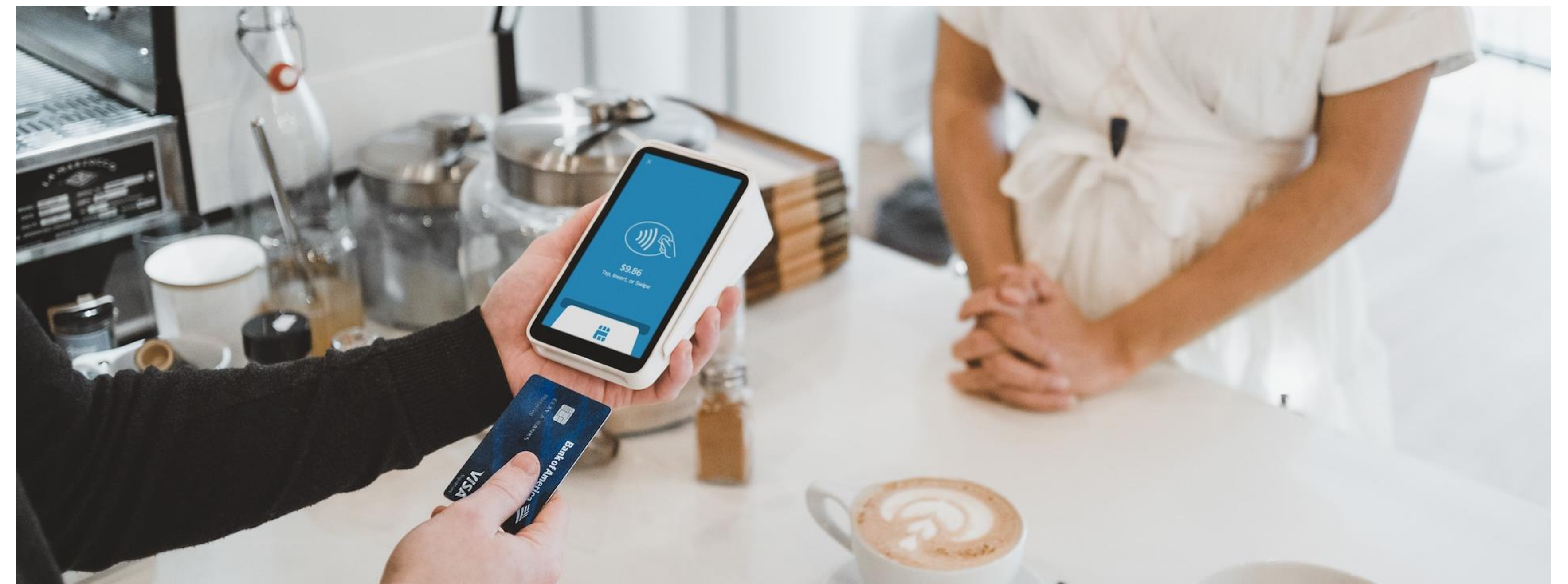
$$\text{Customer Lifetime Value} = \frac{\text{Average Revenue Per Client (per month)} \times \text{Gross Margin}}{\text{Churn Rate}}$$

$$\text{Gross Margin} = \frac{\text{Total Revenue} - \text{Cost of Revenue}^{1}}{\text{Total Revenue}}$$

Churn Rate = The percentage of customers who stopped using the firm's product or service in the given period (usually monthly)

Importance of LTV

- LTV helps tremendously in understanding the value of customer relationships
  - You can justify the implementation of loyalty programs by comparing the costs incurred with the increases in LTV
- Segmenting LTV into different demographics can be helpful in identifying valuable accounts and zoning in on them for cross selling and further marketing
- LTV is also an important factor in projecting future revenue growth, allowing for more accurate and grounded forecasts



[1] For more information: Refer to "Essential Growth Metrics for Startups" by Castellum Capital at https://tinyurl.com/castellumcapitalgrowthmetrics

Value Metrics: Customer Acquisition Cost

Definition

- The Customer Acquisition Cost (CAC) is the average amount of money a firm spends to acquire a new customer
- When calculating CAC, ensure to include all relevant expenses to get the complete picture of acquisition costs. This includes wages, paid advertisements, etc

$$\text{Customer Acquisition Cost} = \frac{\text{Cost of Sales} + \text{Cost of Marketing}}{\text{Number of new customers acquired}}$$

How to lower CAC?

- **Focus on customer retention**
  - With poor customer retention, you would have to rely on acquiring new customers to meet growth targets
  - Improving retention reduces the need to invest additional capital in customer acquisition to meet the same growth targets, hence making sales and marketing more efficient

- **Increasing the efficiency of sales and marketing functions**
  - Speed is key when experimenting with new sales channels
  - Pivoting quickly from unpromising platforms to another will help tremendously in cutting inefficient and costly operations

Efficiency Metrics: LTV/CAC Ratio

Definition

- The LTV/CAC ratio is a measure of the relationship between the company's customer lifetime value (LTV) and customer acquisition cost (CAC)

$$\text{LTV/CAC Ratio} = \frac{\text{Customer Lifetime Value}}{\text{Customer Acquisition Cost}}$$

Why is LTV/CAC Ratio so important?

- **The standard benchmark for LTV/CAC ratio is 3:1**
    - This indicates that a customer will bring in three times the cost needed to acquire them
    - This also indicates that sales efficiency is good, and that the firm's customer acquisition strategies are working, which will lead to revenue growth
- **However, a high LTV/CAC may not be a good sign**
    - This could be an indication that the firm is missing out on significant growth opportunities
    - By increasing investments into your sales and marketing functions, you would be able to optimize the number customers acquired at the right spending rate

Efficiency Metrics: CAC Payback Period

Definition

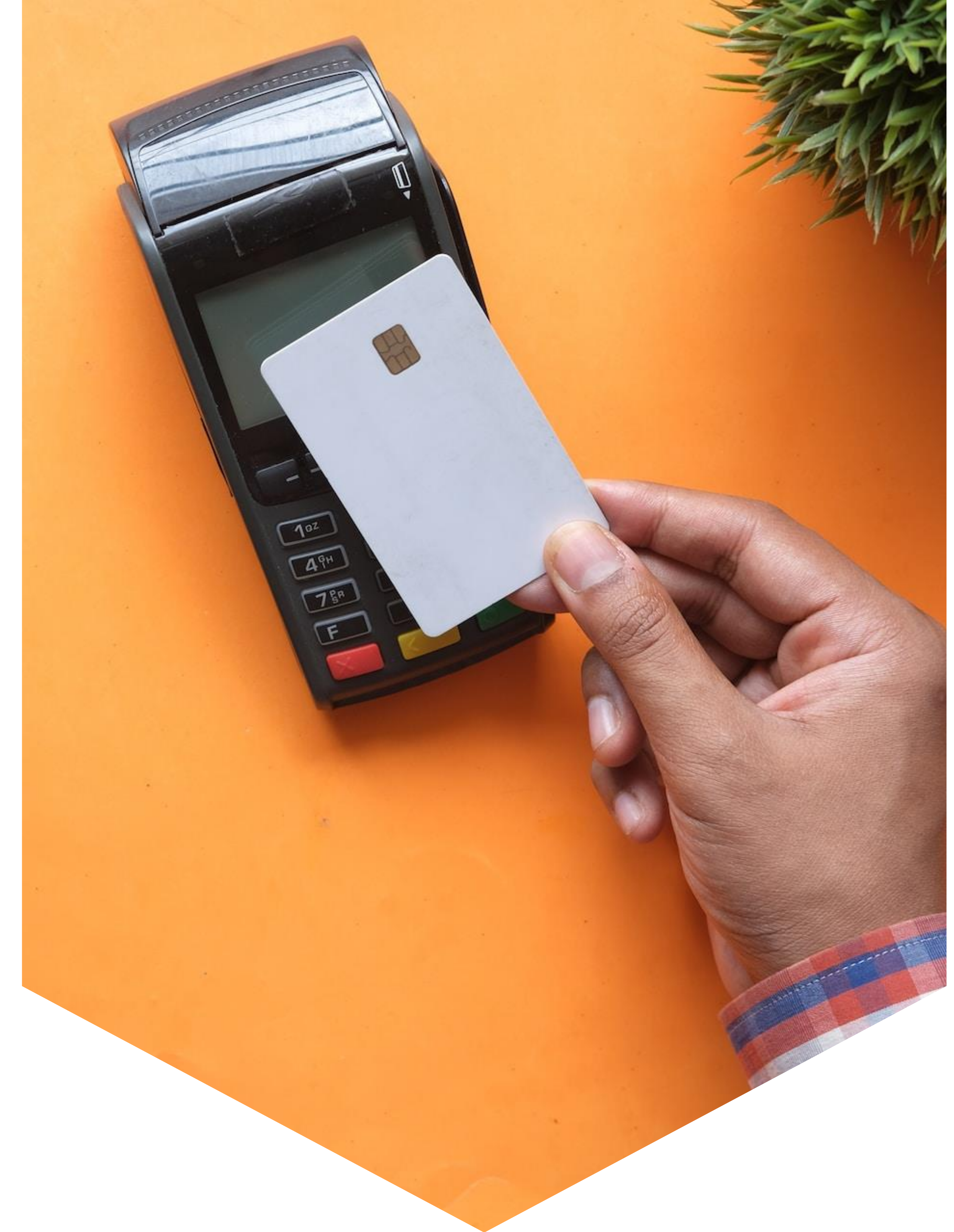
- The CAC payback period is an indicator of the duration it takes to recover the costs incurred to acquire a single customer

$$\text{CAC Payback Period} = \frac{\text{Customer Acquisition Cost}}{\text{Revenue from Product/Service} - \text{Cost of Product/Service}}$$

Why is the CAC Payback Period so important?

- **For investors:**
  - The CAC Payback Period is an indicator of the firm's ability to consistently drive returns on invested capital

- **For management and internal finance teams:**
  - The CAC Payback Period is an indicator of the firm's ability to deploy capital effectively
  - A high CAC Payback Period could indicate inefficient spending and that resources committed to customer acquisition could be better invested into product development and employee training



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