How Customers Pay Impacts How Long They Stay

A SIMPLE AND COST-EFFECTIVE WAY TO CUT CHURN

Subscribed Institute

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IN THE SUBSCRIPTION ECONOMY:

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- ANNUAL CUSTOMER CHURN FOR SUBSCRIBERS WHO PAY VIA PAYPAL IS 16% - FOUR TIMES THAT OF BANK DEBIT
- 20% TO 40% OF SUBSCRIBER CHURN HAPPENS AS A RESULT OF PAYMENT FAILURE
- BUSINESSES ACCEPTING 5+ PAYMENT METHODS HAVE 5% LESS CHURN THAN THOSE THAT ACCEPT 1-3 PAYMENT METHODS

*Defined in the methodology

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A SIMPLE AND COST-EFFECTIVE WAY TO CUT CHURN

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Introduction

The growth of the subscription economy has put digital transformation firmly on the top of the agenda for many businesses. The pandemic has accelerated this trend, not just by temporarily pushing activities from gym classes to tech conferences online, but also by permanently changing customer preferences. In particular, we've seen even more businesses large and small really understand that the subscription model helps to give customers great experiences.

While customer acquisition is a focus of all businesses, retention and expansion of customer relationships is the key to growth for subscription businesses. Understanding subscriber preferences and using this to predict behavior is something that best-in-class subscription businesses must do. That is why the findings of this report are so important — they highlight how the choice of payment method directly impacts involuntary churn. We hope that this ebook helps you to assess your end-to-end payment processes and discover how some easy-to-execute changes can meaningfully increase your revenue over time.

Methodology

For the purposes of this report, subscriber churn rate is determined as the rate at which subscribers cancel their subscriptions over a given period. This is calculated as Subscriber Churn Count / Start of Period Subscriber Count. If you had, for example, 200 subscribers at the start of the period and 10 subscribers churned during that period, the subscriber churn rate equals 5%.

The dataset was derived from Zuora's Subscription Economy IndexTM (SEI) database, which tracks subscription business volume, as well as the prevalence of various pricing and packaging practices. The SEI consists of anonymized and aggregated, system-generated activity on the Zuora billing service, and metrics derived from it are meant to be indicative of subscription-based business in the broader economy.

The initial data extract included approximately 500 customers across a wide range of industries with at least 2 years of consecutive operations on the Zuora Billing service. Further, we split the subset into cohorts: bank debit, credit cards and PayPal and compared the cohorts across the last six quarters.

In this report, we assess the differential churn rates of three popular subscription payment methods: bank debit, credit cards and PayPal. These were chosen because together they represent the majority of subscription transactions.

BANK DEBIT

Bank debit refers to all automated payment methods that allow businesses to pull payments directly from a subscriber's bank account. The term bank debit is used throughout this ebook. This is referred to as Direct Debit in the UK, Australia, New Zealand, and Europe and ACH Debit in the U.S.

CREDIT CARDS

Credit cards refers to all payments triggered by a credit card, typically stored by the merchant and charged periodically as part of the subscription.

PAYPAL

PayPal refers to all payments triggered by a PayPal digital wallet. The underlying payment mechanism used may be a credit card or bank debit, but the subscriber has signed up using a PayPal account.

Dissecting Churn

THERE ARE MANY REASONS WHY CUSTOMERS STOP SUBSCRIBING TO A PRODUCT OR SERVICE. LET'S TAKE A LOOK AT THE DIFFERENT TYPES OF CHURN.

VOLUNTARY CHURN

Voluntary churn is when a customer voluntarily chooses to no longer use your service. There can be many reasons for this, including your product or service no longer being fit for use or a cheaper competitor has come on the market. These areas are addressable but it can take a lot of work.

INVOLUNTARY CHURN

Involuntary churn is when a customer churns without choosing to. Payment issues related to payment methods are the prime causes of involuntary churn. However, involuntary churn is actually fairly simple to solve by offering the right payment methods.

How Payment Methods Directly Impact Churn

From data compiled by the Subscribed Institute, looking firstly at the revenue churn rate of different payment methods across six quarters, here is what we see:

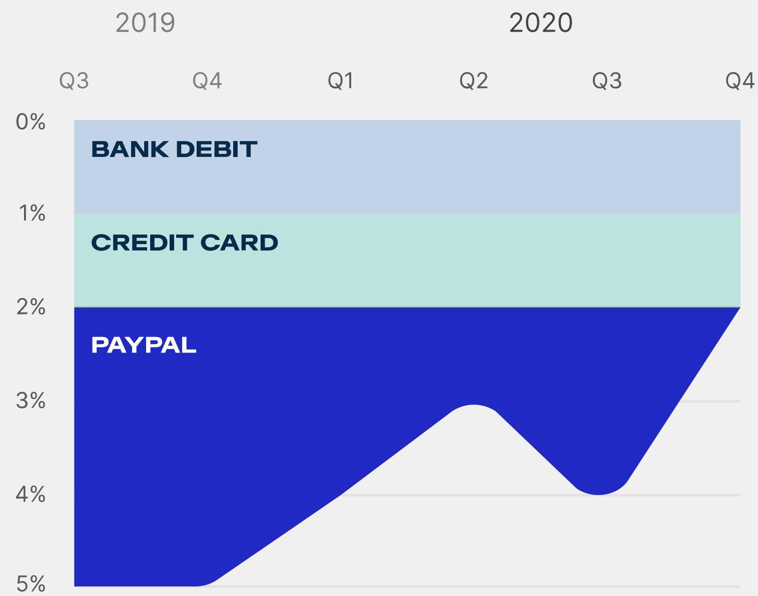
When you look at revenue lost to churn quarterly, the figure to the right shows that bank debit is a fairly stable 1% across all quarters. Credit cards are double that at 2% and PayPal is higher, at between 2% and 5% and more fluctuating than the other payment methods.

When we look at the quarterly customer churn rate, a similar pattern emerges, as the figure bottom right demonstrates. We see bank debit has between 1% and 2% of subscribers lost to churn every quarter. Credit cards have between 3% and 4% of subscribers lost to churn every quarter. And, PayPal between 3% and 6% of subscribers lost to churn every quarter.

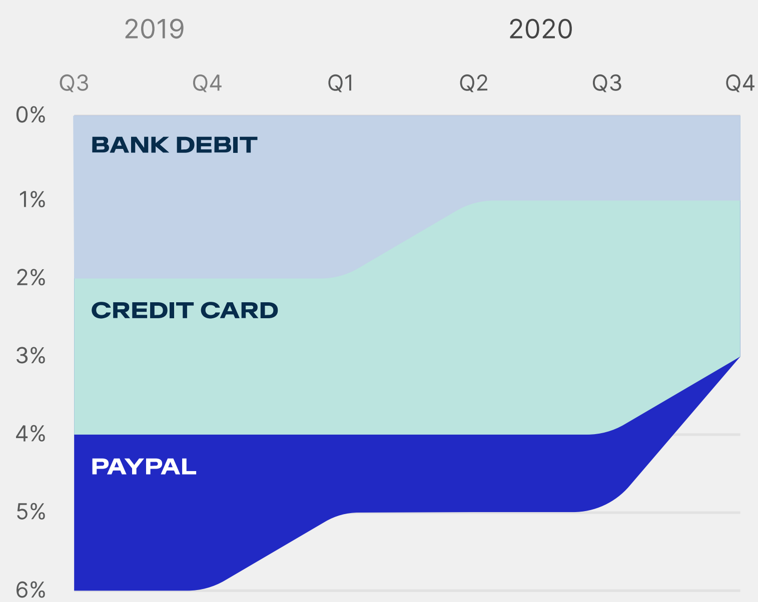
THE COST OF CHURN:

Every quarter, subscription businesses needlessly lose between 1% and 6% of their customers. For a business with 100,000 transactions a month with an average transaction value of $15, that could mean a loss of $36.7 million in cumulative revenue over five years.

REVENUE LOST TO CHURN



CUSTOMERS LOST TO CHURN

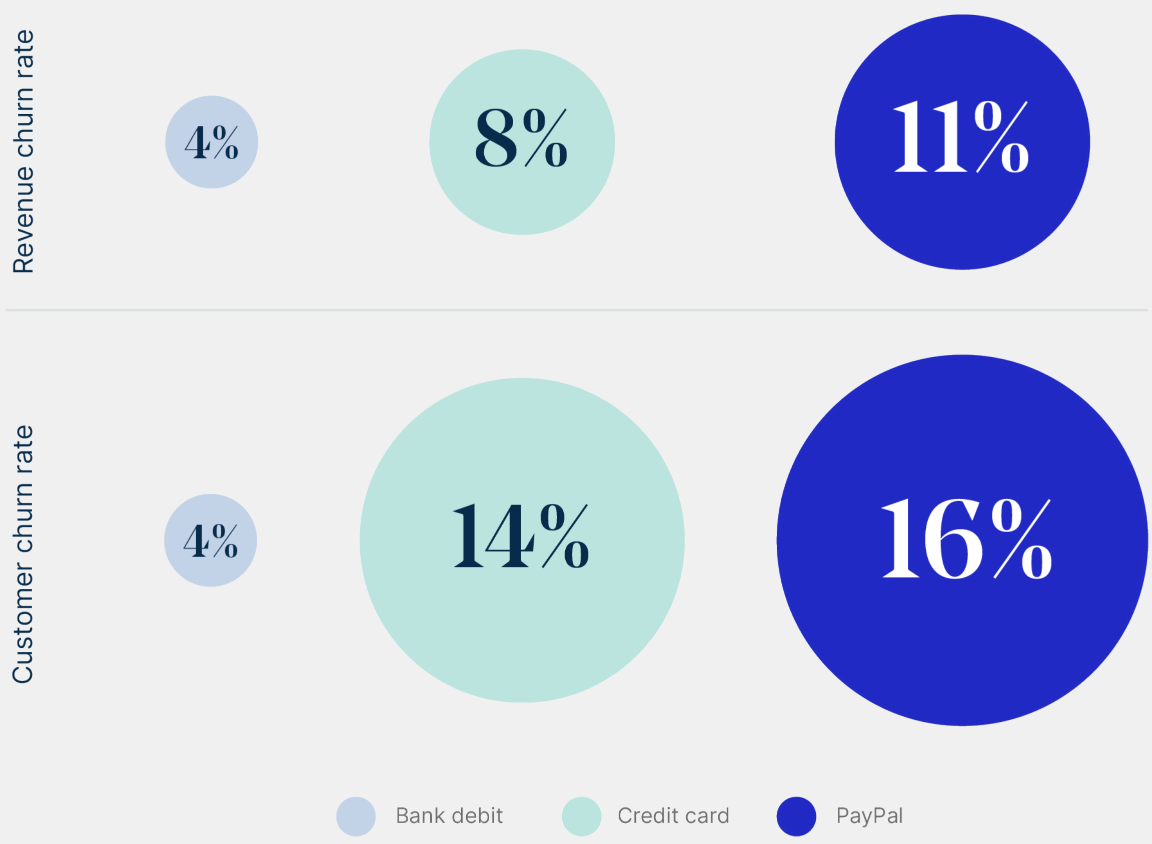


Now let's look at this on an annualized basis, over those six quarters. The below chart shows that the percentage of average annual revenue lost to churn is 4% for bank debit, while this doubles to 8% for credit cards. For PayPal, the average annual revenue lost to churn is highest at 11%. When it comes to the average annual customer churn rate, for bank debit it is 4%. Credit cards more than triple this churn rate at 14% and PayPal's customer churn is four times that of bank debit at 16%.

We can see that there is a clear correlation quarter-on-quarter between payment method and churn rates. Usage of bank debit correlates very strongly with a consistently low customer churn rate, whereas churn rates for customers who use credit cards and PayPal are higher. And, as churn compounds over a five-year-period, these differences become really meaningful.

Failed payments cost you in subscription fees and revenue, although as the chart below shows, customer churn rates and revenues don't always correlate. This is likely because some customers will have signed up for, for example, a three-month free offer.

AVERAGE ANNUAL REVENUE & CUSTOMER CHURN RATE



Comparing Revenue Churn With Customer Churn

Aside from thinking of voluntary or involuntary churn, you can also compare revenue churn and direct customer churn to help assess whether or not you are pricing your solutions right. This will give you an indication of whether you stand to gain something from changing your approach, either to pricing and incentivization or to customer care and support.

As we can see from the Subscribed Institute's data above, there is a consistent difference between revenue and customer churn depending on the payment method. This difference could be an indication that customer growth is offsetting the loss in revenue, which therefore is lower.

DocuSign

TAPPING INTO NEW REVENUE STREAMS BY OFFERING BANK DEBIT

Over a million customers and more than a billion users in over 180 countries use the DocuSign Agreement Cloud to accelerate the process of doing business and simplify people's lives. DocuSign has integrated with both Zuora and GoCardless, to be able to better cater for different payment needs.

Eighteen months after introducing bank debit via GoCardless, 11% of new customers choose this method. This figure continues to rise, with bank debit proving particularly popular in the Netherlands, where 35%, and Germany, where 23%, of customers choose to pay like this.

Retention rates for customers using bank debit after 12 months stands at 70%, compared to 69% with credit cards and 61% with PayPal. This is because there is less churn caused by payment failure among customers paying by bank debit, ultimately resulting in a higher customer lifetime value (LTV) for the GoCardless cohort.

There has also been an unexpected halo effect wherever GoCardless and bank debit is available. The conversion rate across all payments has increased by 10% compared to when only credit cards and PayPal were available. This shows that not only are customers getting a better choice of payment methods, but new customers are choosing DocuSign because their favourite payment method is on offer.

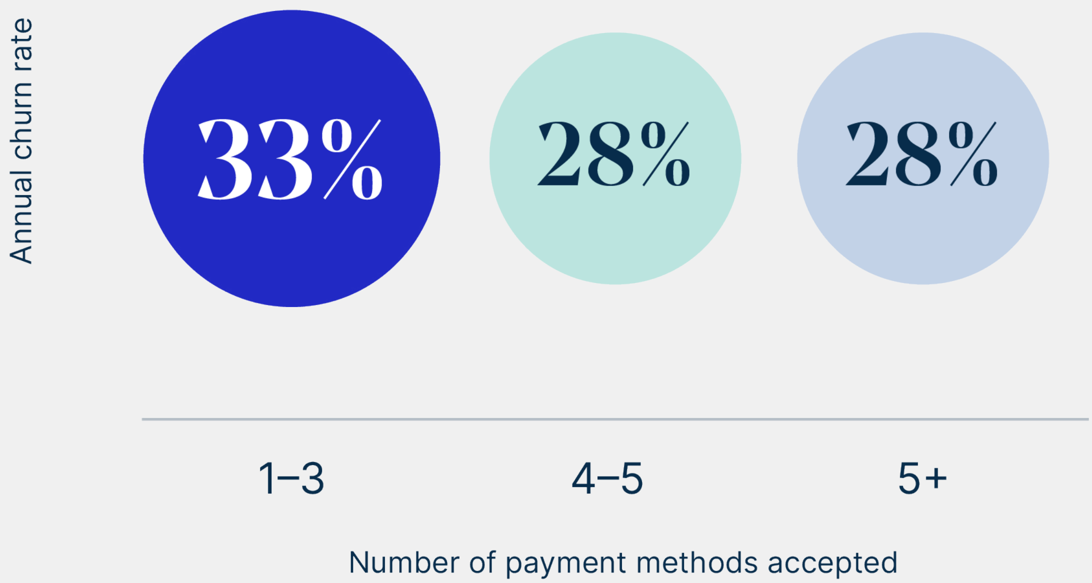
Payment Choices

Whether you're just starting out on your subscription journey or looking to optimize an established subscription business, you want to do everything you can to eradicate involuntary churn quickly and cost-effectively.

There are multiple ways people can pay for subscriptions, and research by Zuora's Subscribed Institute and GoCardless shows that businesses that accept more payment methods grow their revenues faster. Those that accept five+ payment methods saw revenues rise on average 4% faster than those that had up to three payment methods.

We also know that businesses that accept five+ payment methods have 5% less churn than those that accept less than three, as this graph illustrates. Accepting more currencies has a positive effect on your revenue and subscriber base too. Research by Zuora's Subscribed Institute shows that companies that accept payments in five or more currencies saw revenues rise 8% faster than those just accepting one; their subscriber base grew almost 5% faster too. When it comes to involuntary churn, every barrier that you remove equals greater customer retention.

BUSINESS THAT ACCEPT MORE PAYMENT METHODS REDUCE THEIR CHURN



The Link Between Involuntary Churn and Payment Failures

The subscription model utilizes a number of payment methods in various currencies. When subscription companies select a payment method, they typically look at cost, market coverage, target customer preference, ease of sign-up, and success rates. What they also need to look at is how different payment methods impact customer retention.

Research by GoCardless proves that the method by which people pay for goods and services in the subscription economy directly impacts the rate of churn. It found, for example, that 7% to 10% of all payments for subscription businesses collected via credit card fail. In contrast, payments collected via bank debit will typically have a success rate of around 97% on the first try.

It's clear why credit card payments have a much higher payment failure rate than bank debit. Credit cards expire, can be lost or stolen and their issuing banks can block transactions. Credit cards are more likely to fail at the initial sign up too. This might be because the credit card sign-up processes increasingly employ enhanced multi-factor authentication security measures.

What is known as Strong Customer Authentication (SCA) is now a regular and soon-to-be-required feature of European credit card payments. Here, a one-time passcode is sent to your mobile device or email address to qualify the payment. Bank accounts, meanwhile, never expire and their details never need to be updated. And when you make a payment from a bank account, multi-factor authentication is rarely required.

The Forrester Consulting study published by GoCardless, found that, on average, B2C businesses spend between 11% to 15% of the payment value trying to recover failed payments, while B2B businesses spend between 16% and 20% on this. Plus, it can take a few weeks for a failed payment to register, which stalls your cash flow.

Failed credit card payments cost you, and not just in terms of lost revenue. You have to cover the fees to your payment platform for processing those failed transactions. You have to pay to attempt to recover the debt and you have to absorb the costs of the salaries of staff chasing the debt. All of this adds up.

Key Takeaways

It is important to regularly monitor, track, and assess the success of each of your payment methods, which some payment platforms currently offer as part of their offering. Only by continually analyzing your payment data can you understand how much of your churn is voluntary and involuntary, and then take action to minimize any unintentional churn. You may find the data presents payment changes you hadn't considered, such as a shift from annual to monthly payment terms to reduce involuntary churn, for example. Or the data may encourage you to use A/B testing, where you offer one group of customers the option to suspend payments over holiday periods, don't offer the other group, and see whether this has a positive or negative impact on churn.

What is clear, is that there is a strong link between overall churn rate and method of payment. Payers who use bank debit have the lowest churn rates, credit card payers have higher churn rates than bank debit and PayPal payers have the highest churn rates overall. And, as we have seen, an optimal mix of four to five payment methods correlates to higher revenues and lower churn. Plus, the more currencies you accept payments in positively impacts your revenue and subscriber base too.

When choosing which payment methods to offer at your checkout, it's important to consider which might be most efficient in terms of reducing churn for the geographical area you're working in. Automated bank-based payment methods, such as bank debit, correlate with longer-lived customers which in turn will mean more revenue and higher growth.

About Zuora's Subscribed Institute and GoCardless

Zuora's Subscribed Institute is a dedicated think tank focused on the Subscription Economy. The Institute supports its 1500+ business executives across 600+ global companies with critical data, thought leadership, and connections. Research provided by the Institute helps business leaders and their organizations to maximize the opportunities of the Subscription Economy.

To help customers across the world optimize their end-to-end payment processes, Zuora entered into a partnership in 2014 with GoCardless, a global leader in account-to-account payments, making it easy to collect both recurring and one-off payments directly from customers' bank accounts. GoCardless processes $25 billion+ in transactions a year for over 70,000 businesses worldwide, from solopreneurs and small businesses to enterprises such as DocuSign, TripAdvisor, and The Guardian.

Together, Zuora's Subscribed Institute and GoCardless are uniquely placed to provide a comprehensive analysis of data generated by the global subscriptions payments market.