

SaaS Metrics that Drive Valuations Series

Top CLTV Pitfalls

Navidar has been the trusted advisor for many SaaS companies that call the middle-corridor of the U.S. home. Collectively, our team has completed more than 50 SaaS transactions, representing \$10 billion in M&A, capital raises, and public offerings.

Customer lifetime value (CLTV) is among the key SaaS M&A metrics that drive valuation. Although CLTV is often ignored, we use it to our clients' advantage by helping them avoid all-too-frequent pitfalls. The following top 5 CLTV missteps were compiled based on Navidar's deep SaaS expertise. We have found that by appropriately analyzing, optimizing, and presenting CLTV, companies are more likely to achieve operational excellence as well as elevated valuations during exit discussions.



1 One-Off Exercise

[Frequent Measurement and Course Correction](#)

Some SaaS companies view CLTV as one-off or annual exercises. But, much like a ship on a voyage, if navigation is off by a fraction of a degree and it is not regularly measured or adjusted, the ship will never reach its intended destination. Navidar encourages the companies we work with to capture and actively manage CLTV on a quarterly basis at a minimum, ideally on a monthly basis. Frequent CLTV analysis not only ensures companies are on-course, but also provides insight into strategic alternatives, such as where sales-and-marketing and product-development dollars should be allocated to achieve desired results.

2 Lack of Segmentation

[Leave No Stone Unturned to Drive Valuation](#)

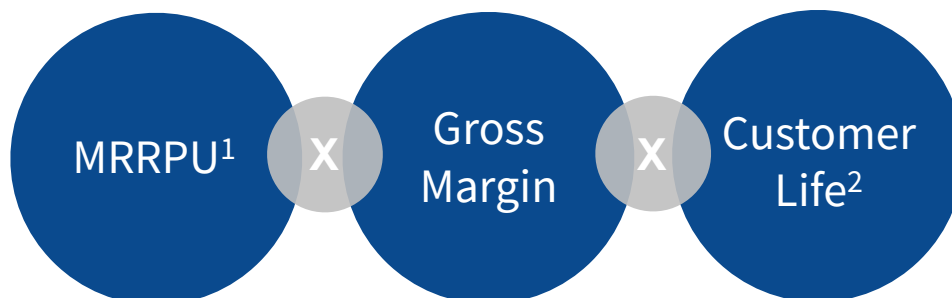
While an overall company CLTV can be helpful for identifying general trends and all-inclusive business health, Navidar helps companies identify value for different types of clients. We do this by breaking out characteristics, such as geography, industry, size, buyer persona, renewal or new client, and marketing channel (e.g., referrals and clients sourced through partners typically carry higher retention rates). We often find that this new insight fuels the appropriate strategic decisions that ultimately drive higher valuations.

Not Considering Upsells

3 Get Paid What You're Worth

An admitted weakness of standard CLTV formulas, including our preferred formula, presented later, is that they do not consider upsells and negative churn. Thus, companies that successfully land and expand while enjoying a 100%-plus dollar retention (including contract overages and upsells) may not get full valuation credit—but they are clearly worth more. To ensure our clients get full valuation credit in these situations, we first confirm that they truly have 100%-plus retention through rigorous analysis. Next, we ensure companies are taking measured steps for improvement. Lastly, we incorporate this attractive attribute into CLTV by highlighting it to potential suitors, applying a multiplier, and/or utilize an advanced CLTV formula. We have found that investors and buyers are more likely to appropriately value this beautiful business-model quality when it is presented optimally.

Our Basic CLTV Formula



¹ MRRPU (monthly recurring revenue per user) is typically calculated as the most recent month's new recurring revenue divided by new customers added

² Customer life is calculated as 1 divided by average churn and presented on a monthly basis

4 Over Burdening Gross Margin Embrace Renewal Margins to Increase CLTV

Some SaaS companies experience high cost of revenue to onboard new customers, which depresses overall gross margin. But, as the percentage of renewing contracts become a higher percentage of total contracts, there is upward movement in gross margin. To account for this factor when calculating CLTV, rather than using overall company gross margin, when appropriate, we apply an adjusted margin that places more weight on renewal contracts. By doing so, gross margin is not overly burdened by excessive cost of sales.

5 Evaluating CLTV in Isolation Broaden Horizons for a Holistic View

CLTV is an insightful SaaS metric that matters to buyers and investors because it shows the lifetime-recurring-revenue gross profit per client. However, since the formula does not address costs related to acquiring a customer (CAC), companies relying solely on CLTV could be flying too close to the sun. Because if CLTV does not handily exceed CAC, barring some early stage of corporate development exceptions, the company will find itself burning cash too quickly. **Stay tuned for future notes in this series that address CAC, retention, and other SaaS Metrics that Drive Valuation.**

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About Navidar

Navidar Holdco LLC, with a presence in Austin, Cleveland, Dallas, Denver, Indianapolis, Minneapolis and San Antonio, is an investment banking firm that provides businesses and investors in dynamic industries with strategic merger and acquisition advice, capital raising solutions, and corporate advisory services. The firm focuses on SaaS software, eCommerce & Internet, IT and engineering services, specialty manufacturing, and health care information technology companies. Navidar principals have completed more than 300 transactions representing transaction volume of nearly \$70 billion in M&A and capital raising, for both private and public companies, over the past 20 years. Navidar Group LLC, a wholly owned subsidiary, is a broker-dealer that is registered with FINRA and SIPC. To learn more about Navidar, please visit www.Navidar.com