

Subscribed: Why the Subscription Model Will Be Your Company's Future and What to Do About It

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Summary

1. Discussion of the rise of the subscription economy and how to position your company for success.

Key Takeaways

1. Fundamental goal of a business used to be to create a hit product, sell as many units as possible to achieve economies of scale and compete on margins; the new model today is to start with the customer and create a service that delivers ongoing value to customers and develop recurring revenue.
 - a. In old world, you could grow by selling more units, increasing the price, or decreasing cost required to make units.
 - b. New world: Acquire more customers, increase value of customers and hold onto them longer.
2. Large Trend: consumers are no longer interested in owning stuff as much as being able to access services that meet their needs. The world is moving from products to services and consumer favor access over ownership.
 - a. This is a prevalent trend you see happening in media: first with music, migrating from ownership of CD's to downloads to movies / TV. You want access to a Netflix membership; you don't want to own a bunch of DVDs.
 - b. People now view ownership as unnecessary baggage.
 - c. Look to sell convenience!
3. Keep in mind: to an entrepreneur, any business process that is universally hated, hopelessly complex, and massively expensive creates a huge opportunity.
4. A subscription model gives you a lot of visibility into your revenue year to year.
 - a. The calculus changes from (price * quantity) to (new customers * price) + (old customers * (1 - churn) * price)
 - b. Subscription model for investment banking and / or advisory work?
5. Customers are different today: prefer outcomes over ownership; customization not standardization; constant improvement, not planned obsolescence; want services not products.
6. Mentions stories of Amazon Prime and Apple as a service as discussed by both Thomson and Ball.
 - a. **Using your products as a means of enabling customer-based services (spend some time dwelling on this point).**
7. Guitar Center Example: instead of thinking about reseller margins and unit sales, the company is thinking about subscriber bases (installed base) and engagement rates.
 - a. It isn't about owning guitars but rather being a guitar player and music lover for life.
8. There is no retail apocalypse: the difference is between data-driven, app-centric and flexible omnichannel retailing and old stale retailing on the other.
 - a. Bonobos: guideshops don't store inventory but help kickstart customer relationship.
 - b. Tesla: dealerships aren't to sell cars, but to inform and answer questions.
9. b8ta
 - a. a retail store that doesn't make money on product sales but rather based on subscriptions from the vendors so it keeps them focused on vendors.

10. New business model imperative is to grow and develop a dedicated subscriber base; in retail, this means establishing a digital identity with customers that encourages discovery and engagement and use physical stores as an extension of online experiences.
11. Motor Trend started its own streaming video service for \$5.99 a month for enthusiasts complemented by its magazine.
12. Way to monitor for churn: recency (when did they last visit?), frequency (how often do they visit?), and volume (how many articles have they read?)
13. As technology shifts to the cloud, there is a shift of technology spend going from capex to opex.
 - a. Amazon Web Services and WeWork are examples of this.
 - b. Other benefits include freeing up cash to drive growth and being more nimble.
14. Model to figure out service behind product: tease out the service level agreement that sits behind the product. Service level agreements are replacing bills of sale. For example,
 - a. Refrigerator: it is the guarantee of cold, fresh food.
 - b. Roof: guaranteed source of solar energy.
 - c. Excavators: its quick removal of certain amount of dirt.
15. IoT is digitization of the physical world through sensors and connectivity and analytic services based on data will result in system efficiencies and business ideas.
 - a. What value can I generate from the information generated from my connected device?
16. Manifesto for Agile Software Development.
 - a. Individuals and interactions over process and tools.
 - b. Working software over comprehensive documentation.
 - c. Customer collaborations over contract negotiation.
 - d. Responding to change over following a plan.
17. Companies with the lowest churn rate usually offer several services that are bundled or cross-sold so if you can solve a broad range of customer problems with solutions it increases retention.
18. In working with hundreds of companies, we've learned that the solution to sustaining a high growth rate is to diversify your approach to growth and embrace multiple growth strategies:
 - a. Acquire your initial set of customers
 - b. Reduce your churn rate
 - c. Expand your sales team
 - d. Increase value through upsells and cross-sells
 - e. Launch into a new segment
 - f. Go International
 - g. Maximize the growth opportunities of your acquisitions
 - h. Optimize your pricing and packaging
19. Subscription Economy Income Statement
 - a. Annual Recurring Revenue (\$100) – Churn (\$10) = \$90
 - b. Recurring COGS (\$20)
 - c. G&A (\$10)
 - d. R&D (\$20)
 - e. Recurring Profit (\$40)
 - f. Sales and Marketing (\$30)
 - g. Net Operating Income (\$10)
 - h. New Annual Recurring Revenue (\$30) = \$120
20. Sales and marketing cost: in a subscription business, these costs are matched to future revenue and function more like capex.
 - a. Assumes 100% of this spend is towards new customers.

21. Remember, as long as you are growing your ARR faster than your recurring expenses, you can step on the gas.
 - a. As Ben Thompson of Stratechery notes, “You’re not so much selling a product as you are creating annuities with a lifetime value that far exceeds whatever you paid to acquire them.”
 - b. John Malone also used to say if your growth > cost of debt your value is infinite.

What I got out of it

1. Helpful introduction to understand how a subscription business model works and how to think about the model.

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