RESEARCH

Recurring Revenue Growth Trends in Europe

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Summary Points

Winning by Design recently conducted a study to understand how conditions of the past 15 months changed software-as-a-service (SaaS) and other recurring revenue businesses in Europe. We looked at various go-to-market factors, including sales cycle time, deal size, conversion, and growth rates. We found that an increasing share of European SaaS companies are achieving hyper-growth status by focusing less on new business acquisition and more on customer expansion and higher deal values.

Unfortunately, as the business climate improves, companies told us they intend to return to pre-COVID growth tactics, reverting to emphasis on new business volume. We believe this is a step backward that will slow revenue growth, not sustain it.

To avoid this, we have four recommendations for European companies who want to sustain hyper growth:

a. Install a standardized data model that includes the compound growth engine to monitor all critical conversion rates through the pre- and post-sale customer journey
b. Understand and deliver impact across the customer journey
c. Focus on expansion of existing clients
d. Measure and manage compound impact

Introduction

The findings in this report cover research conducted by Winning by Design (WbD) over the period from March 2020 to July 2021. Respondents observed that during this period, it was harder to generate new leads and win new deals. As a result, companies shifted focus to existing customer expansion and higher deal values for new business.

The impact of this shift is that a growing number of European SaaS companies are poised to achieve hyper-growth status (40 percent or higher annual revenue growth). By reallocating attention and budget to customer retention and expansion, they created a better recurring revenue stream, which creates a stronger foundation for growth.

Companies anticipate this growth to continue throughout 2022, but as market conditions improve, they expect this growth to come from three sources:

1. Larger deal sizes
2. Higher lead volume driven by better market awareness
3. Higher conversion rates based on improved sales skills and execution

We caution companies not to lose the recurring revenue gains they made by being too quick to return to a focus on lead volume and new business acquisition.

Instead, as companies plan for 2022, WbD recommends building on progress made from the shift to focus on customer retention and expansion. Rather than adding back tactics to deliver lead volume, maintain focus on delivering customer impact.

This will allow companies to support a foundation of recurring revenue that compounds growth and creates positive customer relationships that make retention and expansion easier and reduce cost of sales.

Strong customer relationships deliver positive brand perception and customer advocacy, which have a significant impact on demand volume and new business win rates.

By comparison, reverting to a focus on customer acquisition will likely lead to lower customer retention and expansion, which shrinks the recurring revenue foundation.

Growth rates are lower because more new business is required to fill revenue gaps created by higher churn, and cost of sales go up when fewer deals come from existing customers.

How We Conducted The Study

We are thankful to the dozens of respondents willing to share their stories and data via individual video interviews with WbD. These allowed us to capture both data and the details and context behind the numbers.

Respondents were primarily sales leaders (Vice President of Sales) and company Founders from companies based in Europe with annual revenue between €10 million and €25 million. Countries represented included The Netherlands, Belgium, DACH, and the UK.

The WbD Data Model (also known as "The Bowtie") was used as a foundational construct for respondent interviews and data gathering. We then applied the model to perform analysis and comparisons of current customer results with past customer data.

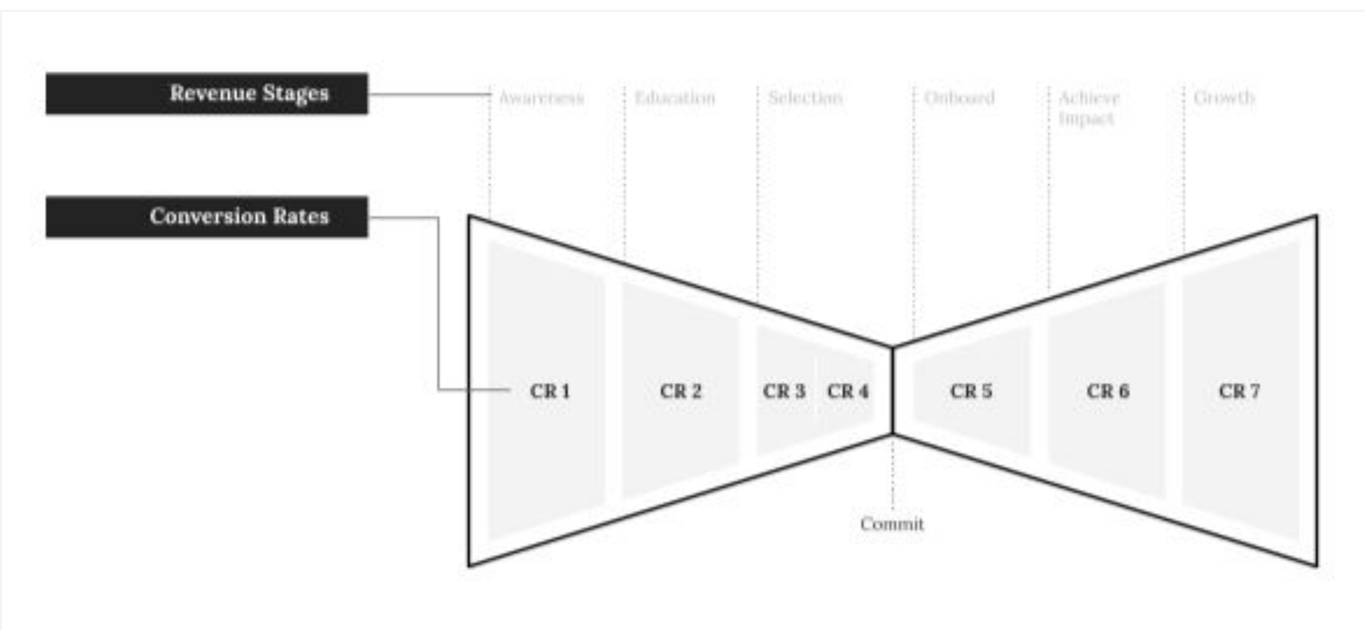


Figure 1: Data Model – Bowtie

Research Findings: Improvements and Challenges

Respondents experienced higher revenue growth, larger deal sizes and shorter deal cycles, but were challenged by market awareness and onboarding existing customers.

Observation: In volatile conditions or downturns, it is common for SaaS companies to outperform the overall market in terms of revenue growth and hiring demand, as we saw in 2008.

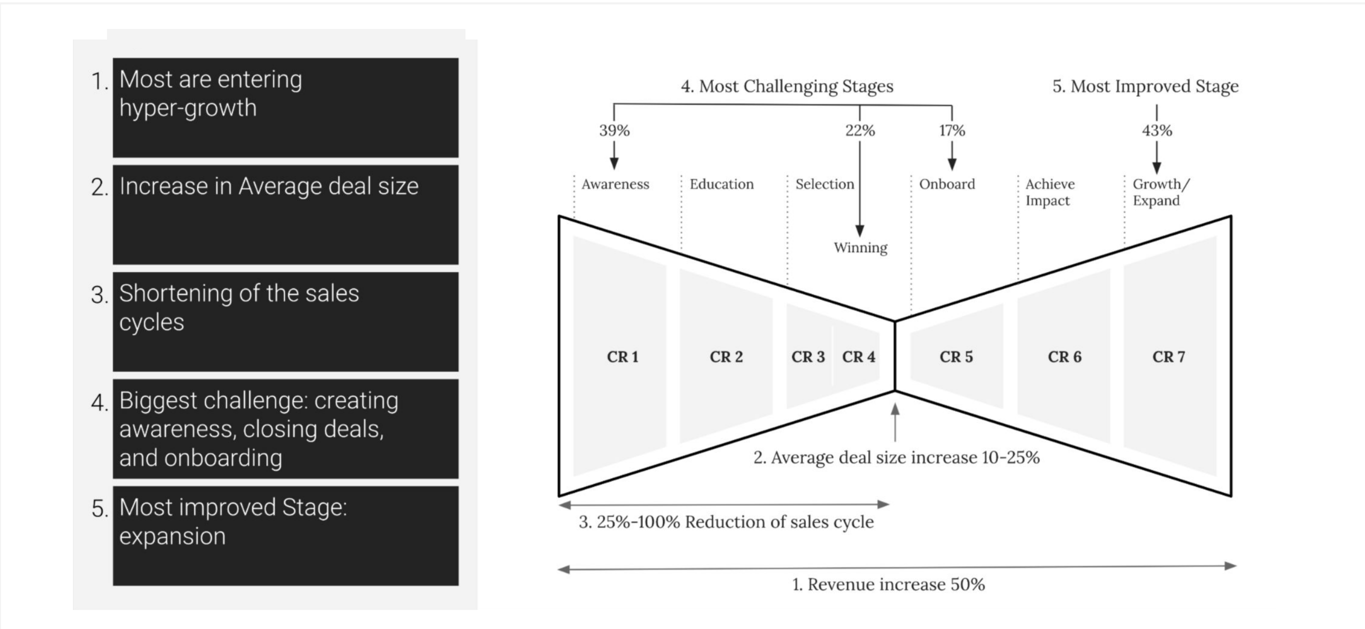


***Figure 2:** Recurring Revenue Recommendations*

Most are in Hyper-Growth Mode

- **Revenue growth:** Majority of respondents are in hyper-growth mode, with revenue increases of more than 50 percent in the last 15 months.
- **Hiring growth:** 44 percent of respondents expect to expand their sales teams by more than 50 percent in the next 12 months.

Increase In Average Deal Size

- **Deal size:** Companies typically increased average deal size by 10 to 25 percent. More than half of respondents have a deal size between €10.000 and €100.000.
- **Improvement opportunity:** 75 percent of respondents said a better product would have the most significant impact on increasing deal size, while 25 percent said a better market would help most.

Observation: During an economic downturn, companies focus more on existing customers out of necessity. Because existing customers want help to achieve impact from your product, a common result is an improved product. When companies deliver more impact with a better product, both new and existing customers are willing to pay a higher price.

Shortening of Sales Cycles

- Faster decisions: Companies in the study saw their sales cycles shorten or stay the same; very few companies saw cycle times get longer. Sales cycles for respondents were typically 90 days or longer.
- Significant time reductions: 70 percent of respondents encountered a reduction of the sales cycles beyond 26%.
- Further reduction potential: Respondents expect that optimizing sales team skills and defining a better target account approach will be vital to shortening sales cycles even more.

Observation: The key driver behind a commitment (and therefore a shorter sales cycle) is to identify a critical event that requires a customer to make a decision. A critical event is the need to achieve a desired impact by a specific time or risk consequences. In 2020, the sense of urgency was heightened by market challenges, creating a need for immediate impact and faster decisions.

Top Three Challenges: Awareness, Closing Deals, and Onboarding

- **Go-to-market challenges:** 91 percent of respondents said they measure conversion rates. Respondents said in the last 15 months, their biggest challenges were creating awareness (39 percent), winning deals (22 percent), and onboard clients (17 percent).
- **Sales stage improvement:** Respondents said the expansion sales stage improved the most by far (43 percent). *(see Figure 1 for definition of expansion stage)*
- **Sales stage challenges:** Respondents said that over the next 12 months, they will apply the most effort and resources to the awareness and education stages.

Observation: With the shift to focus on delivering customer impact, respondents saw their funnels naturally reset to a more productive level. Companies who experience this are achieving a natural growth state. For SaaS companies, this creates hyper growth because happy customers who achieve desired impact naturally want to buy more.

Research Findings: Continued Growth Expected in 2022

Respondents anticipate growth to continue in 2022. They are investing in tactics expected to deliver growth from finding more leads, closing more deals, and increasing deal size.

2022 Investment Plans

Find more leads: Respondents share that in the next 12 months, the most efforts and resources should be invested in Awareness and Education.

Convert more leads into deals: Respondents expect optimizing the skillset of the sales team and optimized targeting account approach to be vital in shortening the sales cycles.

Deal size: Respondents expect a better product (75%) will have the most significant impact on increasing the Deal Size followed by Market (25%).

Research Findings: Perspective on Strategy Risks

A *disproportionate improvement in revenue can only come from the compound growth of existing customers. Reverting to pre-COVID tactics and shifting focus and resources away from helping customers achieve impact will slow down growth*

Risks of Traditional Volume-Focused Growth Tactics

Study findings show that companies are planning a return to pre-COVID growth tactics with increased focus on deal volume. Although deal volume does impact growth and should be part of go-to-market strategies, it is winning the right accounts that delivers hyper growth. Often, deal volume means winning any account, not just the right ones.

The consequence of winning the wrong deals is increased churn, which consumes valuable resources and slows down growth. (*Note: Root causes of this are explained in a storyboard found in the Annex*)

WbD recommends companies proceed with caution when considering the return to a more traditional growth strategy with tactics focused primarily on lead volume and new customer acquisition.

Advantages of Maintaining Shift to Focus on Customer Impact

Study respondents said circumstances in 2020 caused a shift to focus on existing customers. The positive result they delivered was a stronger foundation for recurring revenue based on two factors:

1. Focus on helping existing customers achieve a positive impact
2. Ability to realize higher prices based on positive customer impact

Our research found evidence of this based on revenue growth attainment and improvement of conversion metrics across pre-and post-sale stages from March 2020 to June 2021.

Pay Attention to Performance Metrics in 2022

As companies plan for 2022, WbD recommends building on the progress of 2021. To revert to the old focus on customer acquisition will lead to a less efficient cycle of the higher customer acquisition cost, and lower customer retention and expansion. This less efficient model means companies will miss out on continued hyper growth.

We see evidence of the benefit of this focus in the top 40 most successful SaaS companies. These businesses have two metrics in common: It takes them on average 21 months to recoup CAC, and their LTV to CAC ratio is 3:1, meaning the long-term value of a customer is three times the cost of winning them.

That means to run a successful and sustainable SaaS operation, companies must hold on to a customer's business for an average 63 months or 5¼ years. Most companies can't expect customer relationships to last this long, so they need to look for ways to reduce CAC and increase LTV faster. Paying attention to performance metric improvement is the best way to optimize the recurring revenue engine for hyper growth.

Recommendations

Four actions will help companies deliver customer impact and maintain hyper growth status in 2022 and beyond.

Recommendation One: Install a Standardized Data Model

Companies cannot improve what they do not measure.

Most revenue teams have plenty of data at their fingertips but get lost when interpreting it. The result is not identifying critical problems, and therefore not taking the right actions to remediate issues. Companies define their own set of data and metrics, which makes benchmarking against peers challenging.

This challenge can be solved by applying the Recurring Revenue Operating Model that defines a standard set of metrics across all stages of the customer journey and makes it easier to measure, interpret and monitor improvement.

Recommendation Two: Understand and Deliver Impact Across the Customer Journey

Recurring revenue is the result of recurring impact.

Winning by Design's work with more than 600 SaaS companies shows hyper growth originates not just from finding more leads and winning more deals but from a shift to winning the right deals and helping customers achieve impact.

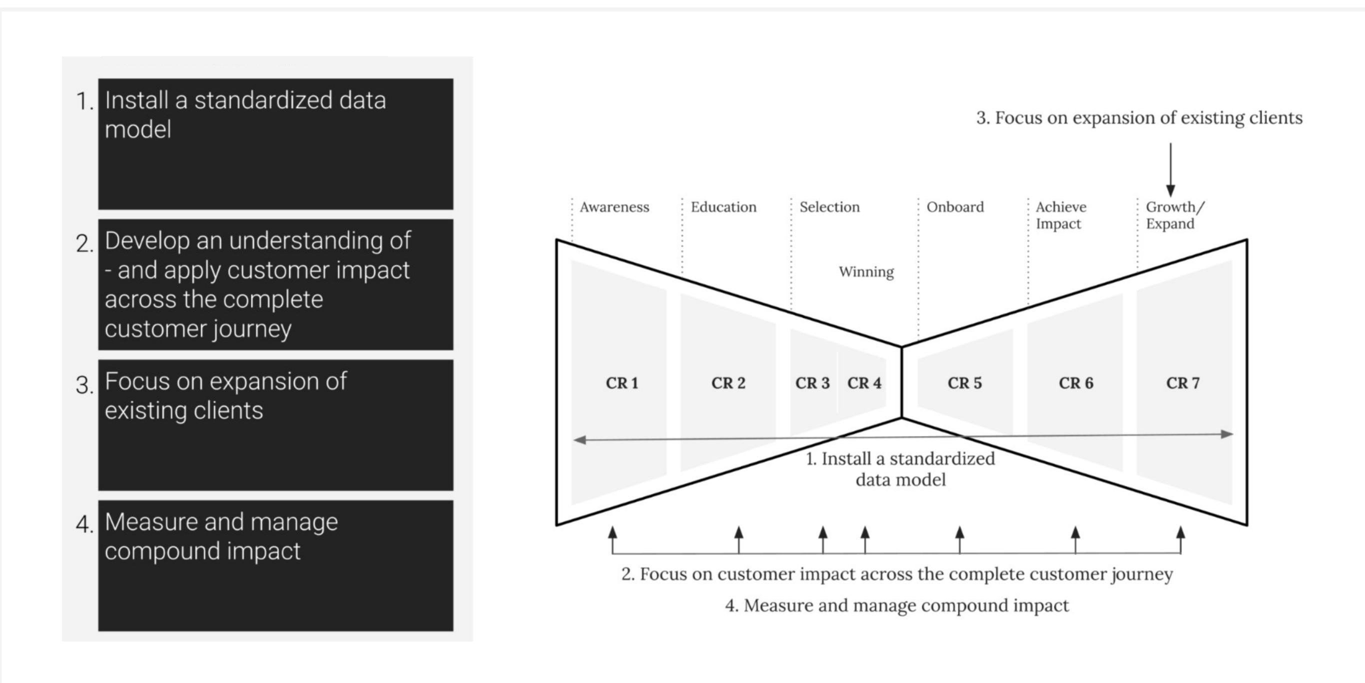


Figure 3: *Recurring Revenue Recommendations*

The result is an increase in higher net retention and organic customer advocacy that fuels recurring revenue growth.

Companies should identify what rational and emotional impact customers expect when they buy, then address gaps in ability to deliver impact or customers' ability to realize and measure it.

Recommendation Three: Focus on Expansion of Existing Clients

Balance resources and time across both sides of the Bowtie.

Companies typically place outsized emphasis on the first half of the Bowtie, the buying cycle. This leads to a heavy focus on awareness, education, and winning more new deals, all of which require significant budget investment and increase CAC.

Instead of maintaining this old approach, most companies have excellent opportunities for growth from existing customers. By measuring and analyzing metrics from the right side of the Bowtie, companies can determine where they have retention and expansion potential. By balancing investment across pre- and post-sale stages, companies will maintain the gains of the last 15 months.

Recommendation Four: Measure and Manage Compound Impact

Happy customers are the best way to maximize sales, marketing and CS results.

Recurring revenue can be optimized through incremental improvements to critical conversion points across the customer journey. Exponential growth can come from the compound impact of retaining and expanding customers.

A big reason for this is that happy customers become an extension of your marketing and sales teams. Companies lower CAC and increase LTV when customers stay longer, expand revenue with you and support greater brand awareness and positive perception. By knowing which Bowtie stages have experience gaps, you improve your ability to create these gains.

Definition of the Recurring Revenue Operating Model

Recurring revenue is built outside of the stages covered by the traditional marketing and sales funnel. That means companies must use a new model to measure, understand, and design recurring revenue growth.

We refer to this model as the *Recurring Revenue Operating Model* (ROM). It is an open standard that can be used by anyone under a Creative Commons license and can be found at www.thescienceofrevenue.com.

We used the metrics in this model to understand performance changes in the companies profiled for this research.

The ROM focuses on three kinds of metrics:

1. **Volume metrics**: This includes measures such as number of leads, deals closed, monthly recurring revenue (MRR), active clients, etc. Historically, companies in growth mode are very focused on volume metrics.
2. **Conversion metrics**: These include tracking conversion percentages through customer journey stages, such as lead to opportunity, win rate, churn (percentage of customers who do not renew), and expansion of business with current customers (cross- or upsell).

Most SaaS companies track these today for pre-sales stages, and more or tracking them for post-sale. We use the Data Model, or Bowtie, to track these measures across all stages.

3. **Performance metrics**: Performance metrics look at indicators such as client acquisition cost (CAC), customer lifetime value (LTV), and cost to serve. These are less common today but moving forward, we expect more companies to add these metrics to their reporting and goal setting.

All three are needed for complete understanding of recurring revenue performance and efficiency. Use them to track progress and to identify opportunities for improvement by stage.

Definition of Growth Categories

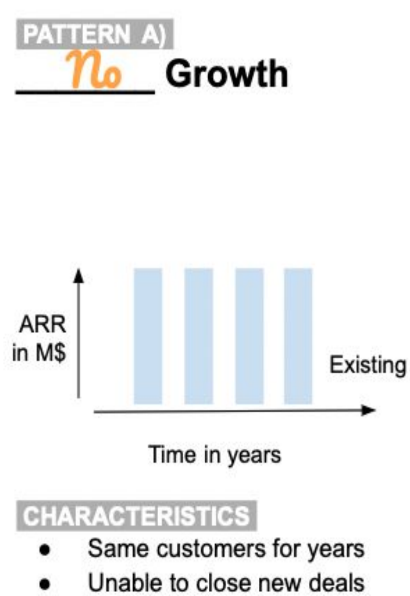
We used growth categories to segment companies in this research. Winning by Design defines three growth categories:

Hyper Growth: 40 percent or higher annual revenue growth rate for more than two years. Commonly seen in start-ups in their first years

Rapid Growth: 10 percent to 39 percent annual revenue growth. Typically seen in companies in scale mode, who have reached $20M in annual recurring revenue (ARR) or higher.

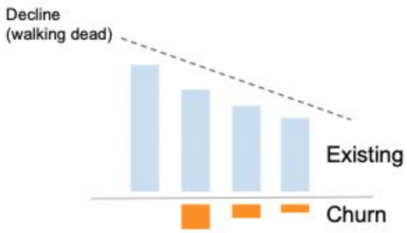
Modest Growth: Annual revenue growth between one and nine percent. Typical for larger public or other enterprise-level companies.

Annex Storyboard on the Origins of Hyper-Growth



PATTERN A)

No Growth = Decline

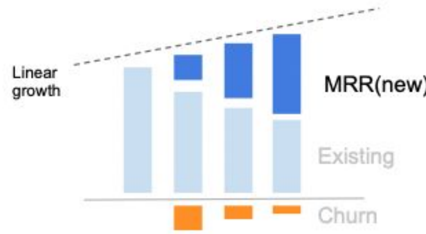


CHARACTERISTICS

- Customers churn

PATTERN B)

Linear Growth

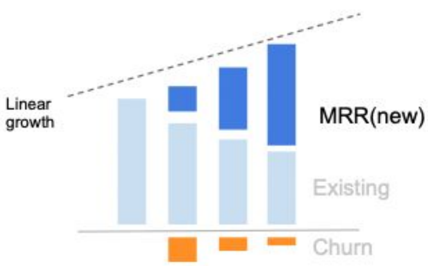


CHARACTERISTICS

- Focus on closing deals

PATTERN B)

Linear Growth



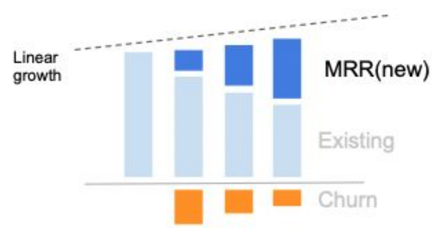
CHARACTERISTICS

- Hire more sales people
- Demand for more leads

PATTERN B)

Linear Growth

Feels like you are swimming upstream



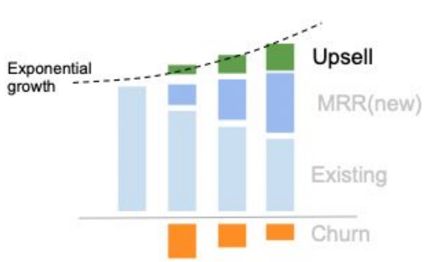
CHARACTERISTICS

- Lead quality drops
- Churn increases
- Growth slows down

} CAC ⬆

PATTERN C)

Rapid Growth

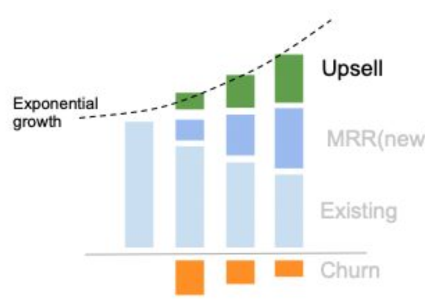


CHARACTERISTICS

- Help customers achieve impact

PATTERN C)

Rapid Growth

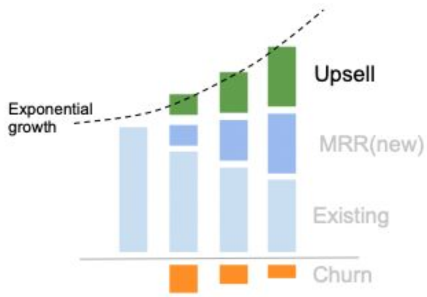


CHARACTERISTICS

- Focus on the customers who can achieve impact

PATTERN C)

Rapid Growth

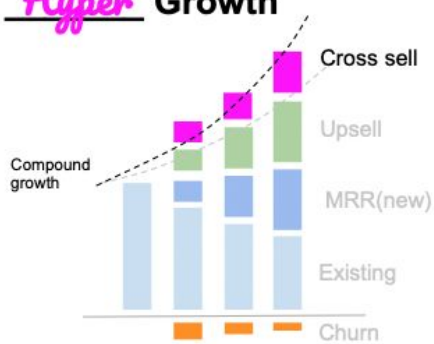


CHARACTERISTICS

- Customers buy more
- Churn reduces

PATTERN D)

Hyper Growth

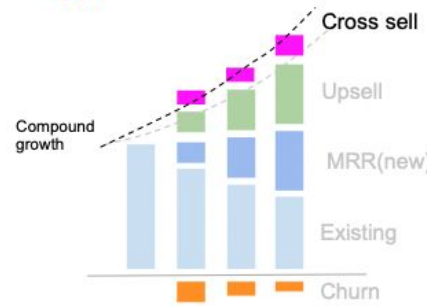


CHARACTERISTICS

- Customers *discover new* impact

PATTERN D)

Hyper Growth

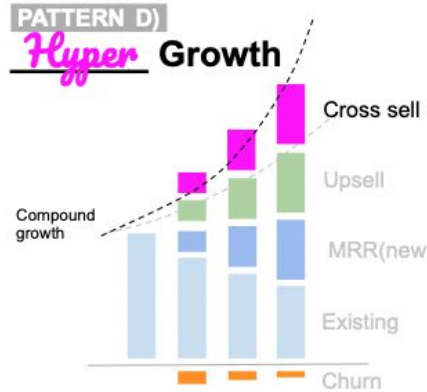


CHARACTERISTICS

- Customers achieve impact
- Successful customers grow

PATTERN D)

Hyper Growth



CHARACTERISTICS

- Customers generate qualified leads
- Growth *compounds*

Feels like you are running downhill

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