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Customer Churn Essentials: What It Is, How to Measure It and How to Manage It

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Customer churn directly reflects your client retention rates and determines your revenue levels. Understanding churn and knowing how to manage it can make the difference between a successful business model and lost business. In this guide, we'll cover the essentials of customer churn, including:

- The definition of customer churn
- The important distinction between voluntary and involuntary churn
- The difference between revenue churn and customer churn
- How to calculate customer churn
- How to analyze the causes of customer churn
- How to reduce customer churn

Read on to learn what you need to know to prevent customer churn and maximize client retention.

Customer Churn is the net percentage of customer you lose over the course of a month or another selected time frame.

01

Defining Customer Churn

Customer churn also goes by terms such as customer attrition, customer turnover and customer defection. It refers to the net percentage of customers you lose over the course of a month or another selected time frame.

Churn is expressed and measured mathematically in terms of a ratio known as a churn rate. Your churn rate is the ratio of the net number of customers who churn (after new customers are factored out) to your total number of customers for a given time frame.

Customer churn rate is the opposite of customer retention rate. Customer retention is the net percentage of customers you keep over the course of a given period. The net customers you don't keep are equivalent to your customer churn. Together, the customers who are retained and those who churn add up to your total number of customers. In this way, customer churn rate and customer retention rate go together. The higher your retention rate, the lower your churn rate, and vice versa. Likewise, a higher churn rate means a lower retention rate.

Distinguishing Voluntary vs. Involuntary Churn

A distinction can be drawn between churn which is involuntary and churn which is voluntary. Involuntary churn occurs when a customer would like to buy from you again but is prevented from doing so through reasons beyond their control. This can happen for a number of reasons, including:

- They forgot that it was time to renew their contract with you
- They can't log into their account to renew a subscription or make a purchase because of a lost password
- They are struggling to get a demo of your product
- Their automated renewal failed because their credit card information is outdated
- They can't afford your product any longer
- Covid is impacting their business

None of these reasons reflect dissatisfaction with your product or service. In contrast, voluntary churn indicates that customers chose not to continue doing business with you for reasons such as:

- They didn't get the benefit they were hoping for when they purchased your product or service
- They didn't find your product design user-friendly
- They don't utilize all of their licenses to justify continuing on
- They had a bad experience with your customer success team
- They decided to buy from a competitor instead

These reasons involve a conscious decision by your customer not to buy from you again. Both involuntary and voluntary factors can cause a customer to churn.

Revenue Churn vs. Customer Churn: What's the Difference?

In discussions about customer churn, you may sometimes come across the term revenue churn. These concepts are related but distinct. Whereas customer churn refers to the percentage of customers you lose over a given period, revenue churn refers to the percentage of revenue you lose because of lost customers over a given period. Likewise, whereas customer churn is measured by the ratio of customers lost to total customers for a given period, revenue churn is the ratio of revenue lost through customer churn to total revenue. This can also include customers who have downgraded their subscription.

From these definitions, you can see that revenue churn and customer churn are distinct concepts. At the same time, they are closely related. The higher your customer churn, the more revenue you will lose from departing customers. Conversely, retaining customers maintains and increases revenue.

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Why Customer Churn is Important

The relation between revenue churn and customer churn underscores why customer churn is important. Customer attrition directly cuts into your revenue. The higher your customer churn rate, the faster your revenue is shrinking. If left unchecked, customer churn can result in your business losing money instead of making money.

Customer churn is important for other reasons as well. Analyzing customer churn and identifying its causes can help you pinpoint problems with your product or service so that you can correct them. For example, if you notice that you have a high churn rate coupled with customers failing to complete their onboarding goals, this can alert you that you need to update your onboarding process and reevaluate the goals you're setting with customers. If you notice that you have a high churn rate among customers who have requested support for a particular service issue, this may be a sign you need to fix the underlying issue or improve your support process. Monitoring customer churn can help you respond to these types of problems before they escalate to the point where they're hurting your business.

Analyzing customer churn and identifying its causes can help you **pinpoint problems** with your product or service so that you can correct them.

03

Calculating Customer Churn

You can use a number of common methods to calculate churn rate. These range from the simple to the complex.

A Simple Method of Calculating Churn

The simplest way to calculate churn rate is to divide the number of customers who churn over a given period by the number of customers you had at the beginning of the time frame:

CALCULATING CHURN: SIMPLE METHOD

$$\frac{\text{Churned Customers}}{\text{Total Initial Customers}} \times 100 = \text{Churn Rate}$$

To illustrate how this formula is applied, let's say you started the month with 200 customers. Over the course of the month, you lost 20 customers while gaining 10. Your churn rate would be 20/200, equivalent to 10%.

example

$$\frac{20}{200} \times 100 = 10\% \text{ Churn Rate}$$

Calculating Churn Based on Averages

The above method gives you a simple way to calculate churn. It works in simple situations, but it proves less useful if your number of customers is changing quickly because of rapid growth. For example, if your customer base suddenly went from 100 to 1,000 customers over the course of the month, a 2% churn rate would have a significantly different impact on your revenue at the end of the month than at the beginning.

To address this, you can use an alternate version of the formula which uses your average number of customers over a given time frame instead of your initial number of customers. You can find your average number of customers by taking your initial and final number of customers and dividing by 2:

CALCULATING CHURN BASED ON AVERAGES

$$\frac{\text{Churned Customers}}{[(\text{Total Initial Customers} + \text{Total Final Customers})/2]} = \text{Churn Rate}$$

To illustrate this formula, let's say you started the month with 300 customers and ended with 200. Your churn rate would be 100 / [(300 + 200) / 2] = 100/250 = 0.4, or 40%. In contrast, if you were using the basic churn formula for this scenario, your churn rate would be 100/300, or about 67%, painting a significantly different picture.

example

$$\frac{100}{[(300 + 200)/2] = 250} = .4\ (40\%)$$

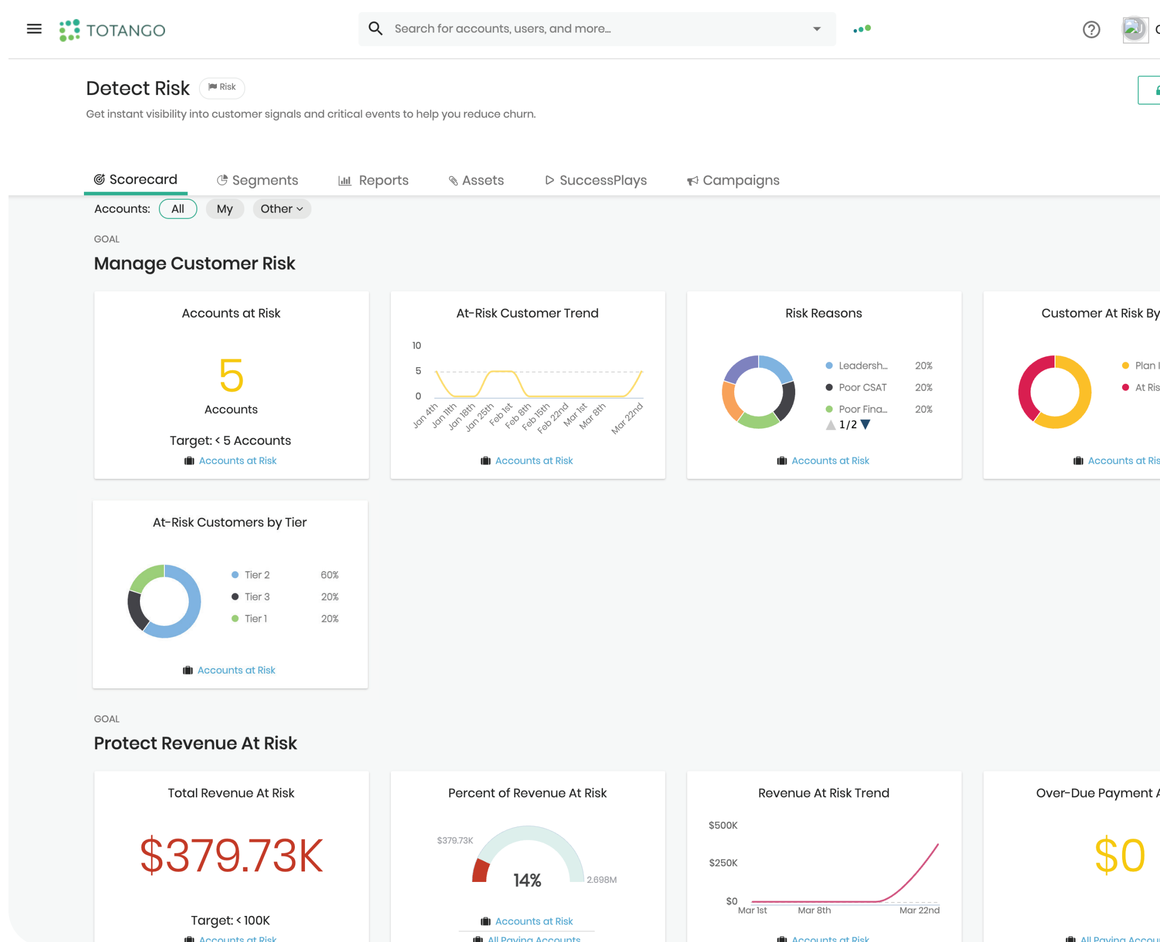
This alternate version of the churn rate formula is often used to average churn over the course of a month. This can give a more accurate picture of churn than only going by the beginning of the month.

Advanced Churn Formulas

Just as churn calculations can be averaged over the course of a month for greater accuracy, they can be averaged over even smaller intervals for still finer approximations.

Advanced formulas are used to predict churn for future time frames based on current trends and customer segments. For instance, you can extrapolate from churn rates over the past month, quarter or year to predict how many customers will churn next month.

Software with churn analytics capability can make it easier to apply advanced churn calculations.



04

Churn Analysis: What Causes Customer Churn?

You can gain more practical value from tracking churn rate if you do a follow-up churn analysis to identify why you're losing customers. Factors that promote customer decisions to leave may emerge at any stage of your customer's journey with your brand, including:

- Sales misrepresenting your product
- Problems experienced during their initial purchase
- Issues during or failure to complete Onboarding
- Difficulties with product adoption, such as trouble learning to use advanced features
- Frustrations experienced with customer success and support issues
- Problems with your renewal process
- Stakeholder or key champion leaving the company
- Company organization restructures
- Customer business model changes

Systematically charting your customer's journey by creating a customer journey map can provide you with a basis for analyzing potential causes of churn. A churn analysis checklist looks for trends in your data to answer questions such as:

- [ ] Are your customers experiencing any problems from the handoff between sales to onboarding?
- [ ] Are they able to complete the onboarding process smoothly and in a timely manner?
- [ ] Is their usage of your product been frequent enough to deliver consistent value?
- [ ] Have they submitted customer support tickets for help with a frequently asked question or a common issue?

You can ask these types of questions with respect to your customers as a whole, segments of your customer base or individual customers. Analyzing trends in your churn data and other customer data with these types of questions in mind can lend you insight into issues that are costing you customers, empowering you to take corrective measures.

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How Can You Reduce Customer Churn?

If you're noticing negative patterns in your churn data, what can you do to improve them? There are a number of customer retention strategies and best practices you can implement to prevent customer churn:

- [ ] Track and review churn data regularly to flag potential problems
- [ ] Use key performance indicators (KPIs) to set churn rate goals and benchmarks representing improvements
- [ ] Prioritize making your product and website user-friendly
- [ ] Verify that your site or product's online shopping experience works properly
- [ ] Set customer success goals representing customer engagement with your product
- [ ] Use customer success playbooks to automate the process of promoting successful outcomes for customers
- [ ] Develop standard procedures for assisting customers through the onboarding process
- [ ] Promote and monitor post-purchase adoption of your product by using tools such as tutorials and analytics tracking of feature adoption
- [ ] Develop escalation management strategies to optimize your response to frequent customer inquiries
- [ ] Take proactive steps to increase customer renewals, such as identifying customer behavior patterns that tend to precede churn and pre-emptively intervening with customers who exhibit these patterns

Choosing the right software can make it easier for you to implement a customer retention strategy successfully. The Totango Spark platform automates customer success by providing a dashboard for monitoring customer success KPIs along with tools for implementing success playbooks that promote customer retention. These tools include modules called SuccessBLOCs which expand the platform's functionality to promote specific customer outcomes. For example, the Detect Risk SuccessBLOC module helps you identify early warning signs of customer churn. In addition, it will help you better manage your customers by being proactive instead of reactive.

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Lower Your Customer Churn to Increase Retention and Revenue

Customer churn is the percentage of customers you lose over a period of time, in contrast to those you retain. It includes both involuntary churn, which can stem from issues such as your key champion leaving the company, and voluntary churn, triggered by factors such as poor service and product adoption. It is distinct from revenue churn, the amount of revenue lost from losing customers, but it stands in close relation to it. Churn has a critical relationship to repeat business and sales revenue, making churn tracking and management essential.

Customer churn can be calculated through several different formulas that compare the number of customers who churn over a given period to total customers at some point during that period. Different formulas can be used to focus on churn during different time frames. The most basic formula uses the beginning of the interval as a reference point, while more advanced formulas use a more complex data set.

Factors that contribute to churn can occur at any point in the customer journey, from the initial purchase to onboarding and adoption to escalation and renewal. You can reduce churn by taking steps to improve and optimize your customer journey at the point causing churn and putting automated systems in place to notify you when a customer is at risk.

The Totango Spark platform's SuccessBLOCs are designed to promote optimized customer journeys by automating best practices that maximize retention and reduce churn. Register to try it free and see for yourself how we can help you retain more clients and reduce customer churn.

Sign up for a free account: totango.com/signup
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