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ACCOUNTING SERVICES

Important metrics to measure your FINANCIAL HEALTH

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Financial metrics:

Financial metrics are simply financial measures that are used to track, assess, and evaluate the financial performance of a company. Financial metrics are key indicators of a company's financial health.

By tracking these metrics, managers can make informed decisions about where to allocate resources and where to cut costs. They can ensure that their company is on solid financial footing.

However, the main problem is that many entrepreneurs worry too much about their company's finances and don't know enough on how to collect data. They end up being anxious when pitching investors for funding later down the line.

Therefore, accurately tracking financial numbers from start can help you identify problems early and save time and hassle!

Every business, no matter how big or small, needs to keep track of its finances. This is especially true for startups, which often have limited resources and need to be very mindful of where their money is going.

While there are many different financial metrics that businesses can track, in this guide we have put together 10 metrics that are particularly important for startup

Index

01 Runway 04

02 Burn Rate 05

03 Revenue 06

04 Monthly Recurring Revenue (MRR) 07

05 MRR Churn 08

06 Average Revenue Per Account (ARPA) 09

07 Customer Lifetime Value 10

08 Customer Acquisition Cost (CAC) 11

09 CAC Payback 12

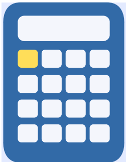
10 Gross Margin 13

Runway:

A cash runway is a projection of how long a company can continue to operate with its current level of cash on hand.

This is important to know for startups as they often have little to no revenue in the early stages and need to know how long they can last before they need to raise more money.

To calculate the cash runway, you need to consider two things – the current cash balance and the burn rate.



The formula is:

Cash Runway = Current Cash Balance / Monthly Burn Rate.

For example,
if a startup has $60,000 in the bank and is burning $10,000 per month, their cash runway would be 6 months.

The size of a company's cash runway is important because it affects how much time the company has to achieve profitability. A longer cash runway gives a company more time to achieve profitability or raise additional funding.

A company's cash runway can be affected by a number of factors, including its burn rate, revenue growth, and expenses. Let's say, if a company increases its sales efforts and begins to generate more revenue, then, its cash runway will lengthen.

In general, investors prefer companies with longer cash runways because they are seen as being more financially stable.

Burn Rate:

The burn rate is a measure of how much cash you're spending every month. It is used to measure how quickly a business is using up its cash reserves.

It doesn't include outstanding obligations, money that was transferred into another account or on its way, but it does show the amount currently being spent for regular operating expenses.

A high burn rate can be a warning sign that a company is in trouble, as it may not have enough cash to sustain its operations. Conversely, a low burn rate may indicate that a company is too conservative and is not investing enough to grow.

The burn rate can also be used as a tool to manage cash flow. By understanding the burn rate, a company can make sure that it has enough cash on hand to cover its expenses.

Controlling burn rate is essential for keeping a company afloat in the long run.

The formula to calculate burn rate is:

Burn rate = Cash balance in prior month – Cash balance in current month

For example,
the cash balance for the month of March is $50,000 and that for the month of April is $35,000, then the burn rate will be $50,000 - $35,000 = $15,000.

As long as the company is generating enough cash to cover its expenses, investors may not be concerned about the burn rate.

Some other formulas to calculate burn rate could be:

- To divide a company's monthly operating expenses by its monthly revenue or,
- To divide the total cash expended by the number of days in the period or,
- To subtract monthly expenses from the monthly revenue.

Revenue:

Revenue is a financial metric that measures the total income generated by a company through its core business activities. This figure includes all forms of revenue, such as sales of goods and services, interest and investment income, and royalties.

Revenue is often broken down into separate categories in order to provide more insight into the specific sources of income. For example, a company's sales revenue may be divided into product sales, service sales, and other sales.

Revenue is an important metric for assessing a company's financial performance, as it is a direct measure of the amount of money generated by the business.

A company with strong revenue growth is typically doing well, while a company with declining revenue may be struggling. Revenue is also an important metric for investors, because it can give them an idea of how much money a company is bringing in and how quickly it is growing.

There are a number of different ways to measure revenue:

- Gross Revenue: It is the total amount of money that a company takes in from its sales, before any expenses are deducted.
- Net Revenue: It is the gross revenue minus any refunds, returns, or discounts.
- Operating Revenue: It is the net revenue plus any other income, such as interest or investment income.

A company's revenue can fluctuate from month to month or year to year, depending on a number of factors, such as the economy or seasonal trends.

However, over time, it is hoped that a company's revenue will continue to grow, indicating that the business is healthy and successfully meeting customer needs.

Monthly Recurring Revenue (MRR):

Any business owner knows that one of the most important metrics to track is monthly recurring revenue or MRR. This is a measure of the amount of revenue that a business can count on every month, and it provides a valuable way to track growth.

There are a number of benefits to tracking MRR.

- It provides a clear picture of growth over time. This can be helpful in setting goals and benchmarking progress.
- It can help identify trends and areas for improvement.

For example,
if MRR is stagnating or declining, this could be an indication that something is wrong with the business model or that customer churn is becoming an issue.

- It can help businesses make more informed decisions about pricing and marketing strategies. By understanding how much each customer contributes to monthly revenue, businesses can tailor their strategies to target high-value customers and maximize growth.

MRR is calculated by multiplying the number of paying customers by the average monthly price per customer.

The formula is:

MRR = Average monthly price per customer * No. of paying customers

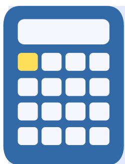
For example,
if a business has 100 paying customers at an average price of $50 per month, its MRR would be $5,000.

MRR Churn:

Month-to-month recurring revenue (MRR) churn is a critical metric for subscription businesses. It measures the percentage of recurring revenue that is lost each month, due to customer cancellation or downgrades.

It can provide valuable insights into a business's sales and retention practices

To calculate MRR churn, simply take the total amount of revenue lost in a given month and divide it by the total MRR at the beginning of the month.



The formula is:

MRR Churn = Total monthly revenue lost / Total MRR at the beginning of the month

For example,
if a company starts the month with $10,000 in MRR and loses $500 in MRR due to cancellations, their MRR churn rate would be 5%.

While some level of churn is inevitable, high churn rates can be detrimental to a company's growth.

For example,
if a company has an MRR churn rate of 5%, that means that it is losing 5% of its monthly recurring revenue each month. In order to offset this loss, the company would need to generate 5% more in new MRR each month just to break even.

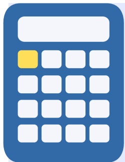
As such, reducing MRR churn should be a top priority for any subscription business. There are a number of strategies that companies can use to reduce churn, such as:

- offering discounts or incentives for customers who stay longer,
- providing better customer support, or
- increasing the value of the service.
- increasing transparency around pricing and billing

By taking steps to reduce MRR churn, companies can fuel their growth and financial stability.

Average Revenue per Account (ARPA):

Average Revenue per account (ARPA) is a metric used to measure the average revenue generated by a customer or account over a specified period of time. It is calculated by dividing the total revenue by the number of accounts.



The formula is:

ARPA = Total revenue / Number of customer accounts

This metric is a useful tool for evaluating the health of a business and its growth potential.

For example,
if total revenue is growing but the number of accounts is staying the same, then ARPA is likely to increase. Conversely, if total revenue is stagnant or declining, then ARPA will decrease.

By tracking ARPA over time, businesses can get a better understanding of their growth trajectory and identify opportunities for improvement.

The ARPA can also be used to compare the performance of different businesses.

Let's say, if two businesses have the same ARPA, but one has twice as many accounts, then the latter business is growing at a faster rate.

Additionally, the ARPA can be used to assess the profitability of a business.

A high ARPA indicates that customers are spending more with the company and are likely satisfied with the products or services they are receiving.
A low ARPA, on the other hand, may be indicative of problems such as poor customer service or a lack of product value.

Customer Lifetime value:

Customer lifetime value (LTV) is the total amount of revenue that a business can reasonably expect to earn from a single customer over the course of their relationship. LTV takes into account both the revenue generated by a customer over the course of their relationship, as well as the costs associated with keeping them as a customer.

Calculating LTV is a helpful way for businesses to assess the potential value of new and existing customers, and to allocate marketing resources more effectively.

For example,
if a company has an LTV of $1,000, it can afford to spend more on a customer than any other company with an LTV of $600.

To calculate LTV, businesses first need to identify their average customer lifespan and average customer value. These can be estimated using data from past customers.

Once these numbers are known, LTV can be calculated by multiplying the average customer lifespan by the average customer value.

The formula is:

LTV = Average Customer Lifespan * Average Customer Value

For example,
if the average customer lifespan is 5 years and the average customer value is $100, then the LTV of a customer would be $500.

While LTV is often used to assess the profitability of a customer, it can also help businesses take steps to improve customer satisfaction and loyalty and, marketing and sales strategy.

For example,
if the LTV of a customer segment is low, it may be necessary to spend more on acquisition to generate enough revenue to offset the costs of acquisition and retention. Conversely, if the LTV of a customer segment is high, acquisition costs can be allocated elsewhere to maximize profits.

Customer Acquisition cost (CAC):

The customer acquisition cost (CAC) is the amount of money that a company needs to spend to acquire a new customer. In other words, it is the cost of persuading a new customer to purchase your product or service. CAC can vary depending on the industry.

For example,
the average CAC for tech startups is around $3,000. This means that for every new customer that a tech startup acquires, it needs to spend an average of $3,000.

Of course, acquisition costs can vary depending on how much a company is willing to invest in marketing and sales efforts.

For example,
a company with a limited budget may only be able to afford to spend $500 on acquiring each new customer. On the other hand, a company with a large budget may be willing to spend $10,000 or more on acquiring each new customer.

Ultimately, the goal is to acquire customers at a lower cost than the revenue that they generate.

For example,
if a company spends $3,000 on acquiring each new customer and each customer generates $5,000 in revenue over their lifetime, then the company will be profitable. However, if the company spends $3,000 on acquiring each new customer but each customer only generates $2,000 in revenue, then the company will be in loss.

The cost of acquiring new customers can be a major expense for businesses, especially in highly competitive industries. There are many ways to reduce customer acquisition costs, but it is important to first understand the different factors that contribute to this cost, some of which are:

- the cost of advertising and marketing to reach potential customers
- the cost of sales staff salaries and commissions
- the cost of providing incentives to customers to make a purchase (such as discounts or coupons)

By understanding the above costs, businesses can develop strategies to reduce these costs and acquire new customers more efficiently.

Customer Acquisition Cost Payback (CAC Payback):

The customer acquisition cost payback period is the amount of time it takes for a company to recover the costs associated with acquiring a new customer. This metric is important because it provides insight into how quickly a company can generate revenue from its marketing and sales efforts.

A short payback period indicates that a company is efficient at acquiring new customers, while a long payback period suggests that improvements are needed.

The customer acquisition cost payback period can be calculated by dividing the total cost of customer acquisition by the average revenue generated per customer

The formula is:

CAC Payback = Total CAC / Average revenue generated per customer

For example,
if a company spends $100 on marketing and sales for each new customer, and each customer generates an average of $200 in revenue, the payback period would be 0.5 years (6 months).

Companies typically aim for a payback period of 12 months or less. To achieve this, they must focus on generating high-quality leads and converting them into customers efficiently.

By doing so, they can ensure that their marketing and sales efforts are generating a positive return on investment.

Gross Margin:

Gross margin is a financial metric used to assess a company's profitability. It is calculated by subtracting the cost of goods sold from the total revenue, and then dividing by the total revenue. The resulting number is expressed as a percentage.

The formula is:

$$\text{Gross Margin} = \frac{\text{Total Revenue} * \text{COGS}}{\text{Total Revenue}} * 100$$

For example,
if a company's total revenue is $100,000 and the cost of goods sold is $40,000, the gross margin would be 60%.

A company's gross margin can be affected by many factors, including the price of its products, the cost of manufacturing and shipping, and the amount of competition in the marketplace.

Gross margin is a key indicator of a company's financial health, and it can be used to compare businesses within the same industry.

A high gross margin indicates that a company is efficient in its production and pricing and therefore, is able to generate significant profits, while a low gross margin indicates that a company is struggling to generate profits.

Companies with high gross margins are typically more profitable than those with low gross margins.

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Thanks for reaching out!

With these metrics, we hope you can track the financial health of your business.

Keep an eye on these financial metrics to make sure you're not losing money. From revenue, expenses and more - this list will give a good foundation for your business insights!

We hope that by providing this list of metrics, you will be able to track your business's progress and see how it is improving over time.

It's time to put your mind at ease and let us take care of all the business transactions for you. With our easy-to use system, there is no need worry about anything other than what matters most - growing yourself as a company! ***Book an appointment*** with ***Accruratee*** now

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