

Revenue Models & Forecasting

Dave Parker

@DaveParkerSEA

www.GetTrajectory.com

@DaveParkerSEA



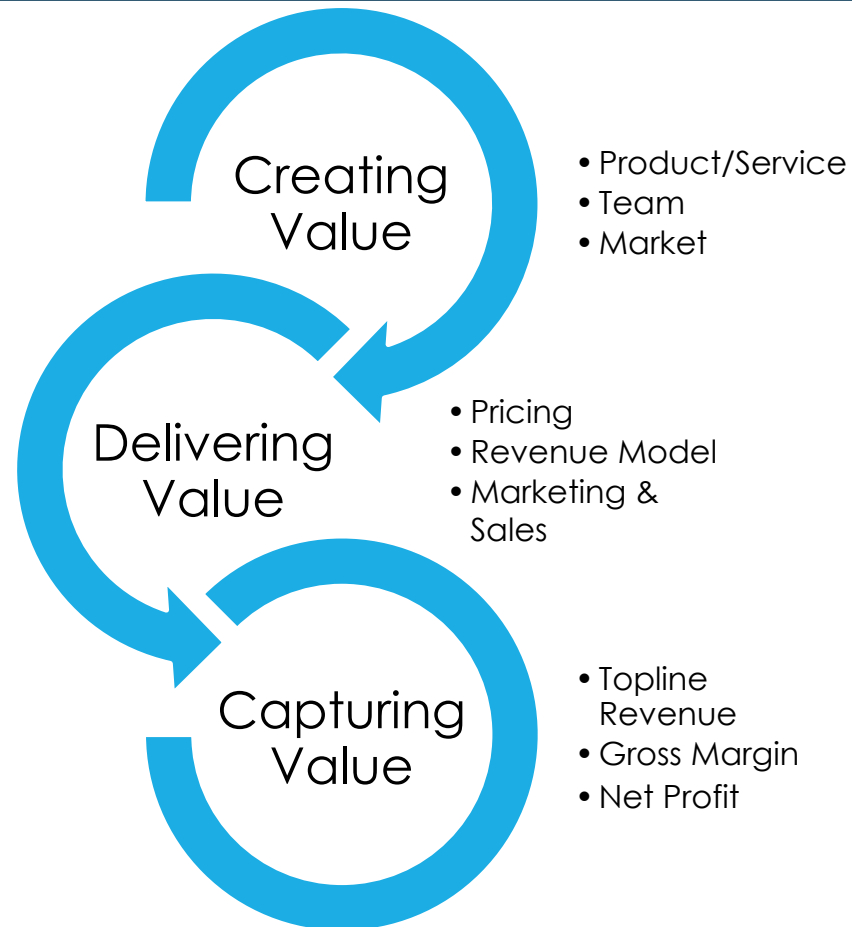
Agenda

- Outcomes for the day:
 - Business model breakdown
 - Identify Key Inputs (Quarterly planner)
 - Identify Unit Economics
 - Choose primary/secondary revenue models
 - Choose financial template
 - Common mistakes
 - Rolling up your sleeves

About Dave

- 5X founder, raised \$12M, exited \$85M
- Former SVP Programs at UP Global (Startup Weekend)
 - Startup Next creator, Startup Week
- Author – "[Trajectory: Startup – Ideation to Product Market Fit](#)" shipping 3/2021
- 2X VC and random Angel
- 10 transactions – 8 sell side, 2 buy side now with [NextPath Advisors](#)

Business Model Breakdown



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Revenue Models– Pick One or Two

1. Services/Fee for Service
2. Commerce
3. Subscription
4. Metered Service
5. Transaction Fee/Rental
6. Productize a Service
7. Combinations
8. Marketplace
9. Lead Generation
10. Gaming
11. Advertising/Search
12. New Media
13. Big Data
14. Licensing

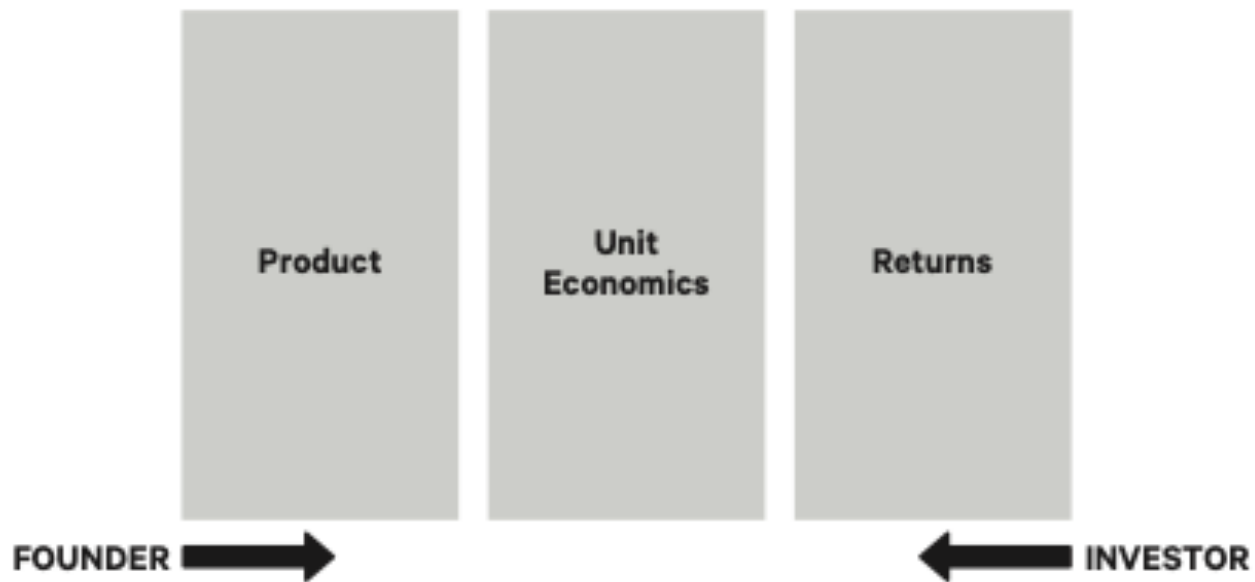
Revenue Models

- ▣ Full post [here](#)
- ▣ What you need to know
 - ▣ Mark up
 - ▣ Commerce, services,
 - ▣ Subscriptions
 - ▣ MRR, ARR
 - ▣ Transaction Fees
 - ▣ Rental, marketplace

Telling a Financial Story

- Finance is the language of business
- The story comes down to numbers, in cells on a spreadsheet, the model validates the story.
- Investors want to stress test the models and assumptions
- Models serve multiple purposes
 - Fundraising – pitch deck
 - Budgeting and forecasting – scalable revenue
 - Cashflow forecasting – runway

Two Views of Your Startup



The Model Supports the Deck

- ▣ The pitch deck provides a 3-5 year summary
 - ▣ You need to know the numbers
- ▣ The summary at a high level
 - ▣ Revenue, cost of revenue and gross margin (\$/%)
 - ▣ Operating expenses
 - ▣ Profitability and cashflow breakdown
 - ▣ Headcount
 - ▣ Key drivers (unit economics/customers)

Financial Model Best Practices

- The success drivers (metrics, KPI's) are simple and easy to understand. Avoid complicated formulas
- The revenue categories map to one or more of the 14 models
- The five-year ramp is realistic (not \$100M)
- Cost of revenue is complete, so gross margin is correct:
 - Hosting, fulfillment, shipping
 - Labor (customer service)
 - Production costs

Financial Model Best Practices

- Operating expenses are complete:
 - Expenses grouped by department (fixed vs. variable, cost of sales, etc)
 - Headcount – roles, compensation, benefits
 - Contractors – HR, Accounting, Engineering
 - Travel expense
 - Marketing – reflects go-to-market strategy
 - G&A – facilities, insurance, other operating expenses
- Investments are reasonable to estimate:
 - Intellectual property, equipment

Financial Model Best Practices

- GAAP/Accrual based accounting
- Revenue recognition
- A great model answer the burning questions:
 - When does the company become profitable?
 - When does cash flow breakeven occur?
 - How much investor capital is needed?
 - Will more than one round of funding be necessary?

Forecast vs Actual

- ▣ Four dimensions of financial reporting:
 - ▣ Actuals – QuickBooks (accrual)
 - ▣ Operating Plan – Budget (roadmap for the quarter & year)
 - ▣ Forecasting
 - ▣ Variance analysis
 - ▣ Actual to plan
 - ▣ Actual to forecast

Use Cases

- ▣ Why do a financial model
 - ▣ Scoping the business – for you and investors
 - ▣ Fundraising requirements
 - ▣ Pre/Post Product/Market fit impact
 - ▣ Risk capital
 - ▣ Growth capital

Key Metrics

- ▣ Assumptions
 - ▣ Staffing
 - ▣ Timing
 - ▣ Product & Pricing
 - ▣ Launch timing
 - ▣ Prices
 - ▣ Sales Models
 - ▣ Scaling past the founder
 - ▣ Time to close
 - ▣ Marketing Methods

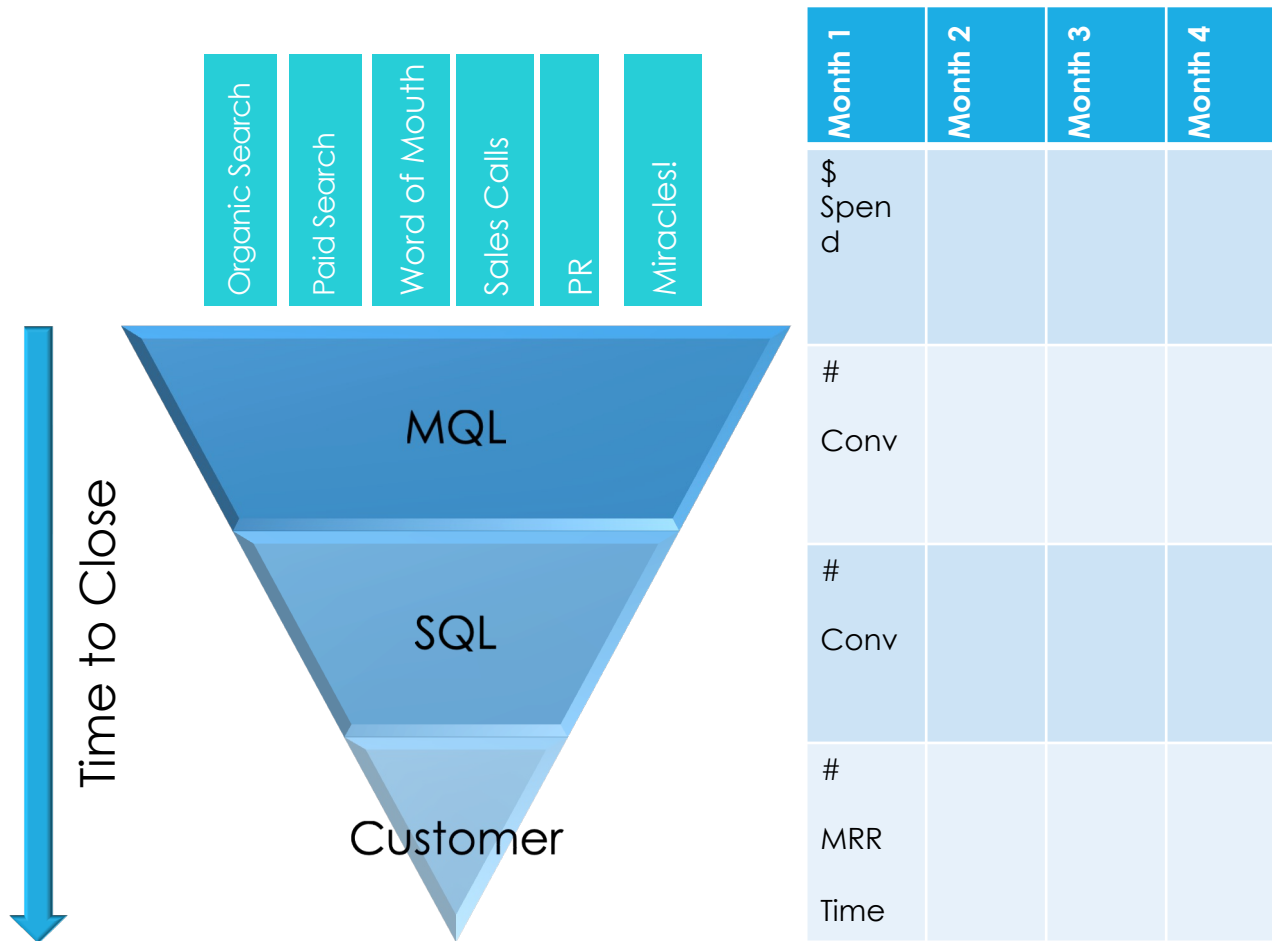
Marketing – Finding the right customers

Marketing – Finding Customers

- Messaging/Value Proposition
 - Does it resonate with the target customer segment
 - They are the hero of the story
 - Is it repeatable?
- Strategy
 - Outbound first
 - Inbound second

Unit Economic Terms

- ▣ State your hypothesis
 - ▣ CAC – customer acquisition cost
 - ▣ LTV – lifetime value
 - ▣ ARPU – average revenue per user
 - ▣ ACV – annual contract value
 - ▣ Churn – customers that leave monthly
 - ▣ Net Negative Churn – increase in annual contract value
 - ▣ Time to Close – in days
 - ▣ Customer engagement – time on site, in app



Sales – capturing value creation

Sales Model Hypothesis

	Known Market	Unknown Market	Low Price Point	High Price Point	Known Search Words	Unknown Search words
Web Direct	✓		✓		✓	
Direct	✓	✓		✓	✓	✓
Indirect	✓		✓		✓	
Retail						

Sales Staffing

- ▣ Sales Development Reps (SDR)
- ▣ Account Managers
- ▣ OTE – On Target Earnings
 - ▣ Base
 - ▣ Commissions
- ▣ Timing of hires

Pricing

Ultimately pricing needs to cover

- ▣ Cost of Customer Acquisition
- ▣ Cost of Delivering
- ▣ Margin (Profits and Returns)
- ▣ Lifetime Value (LTV) is calculated at 12 or actual
- ▣ Pricing is not an afterthought
- ▣ 10, 100, 1000 customers

Pricing Mechanics

Pricing Tiers

- ▣ Pricing should be appropriate for the stage/type of customer
- ▣ Usage based
- ▣ User based
- ▣ Balance friction, easy to start
- ▣ With cost of sales, minimum user size

Hubspot Example

Grow better with the right plan.
Pay for what you need (when you need it).

Products & Plans Bundles

Free Tools Marketing CRM & Sales Customer Service CMS **NEW**

Marketing Hub™

Everything you need to capture leads and turn them into customers. [Calculate your price](#) ↓

NEW: Only pay for marketing contacts.
Enjoy transparent pricing by choosing the contacts you pay to market to (and store up to 1 million non-marketing contacts for free). [Learn more](#) ↗

Your 90% discount is waiting. Use it today! You're still eligible for the HubSpot for Startups program discount. [Use my discount](#)

Plan	Starts at	Price	Contacts	Buttons
Starter	\$50	\$45/mo billed at \$400 \$540/yr	1,000 marketing contacts	Buy now, Pay Monthly, Pay Upfront SAVE 10%
Professional	\$89	\$89/mo billed monthly	2,000 marketing contacts	Talk to Sales, Start a free 14-day trial
Enterprise	\$3,200	\$320/mo billed monthly	10,000 marketing contacts	Talk to Sales, Start a free 14-day trial

Free tools plus: Starter plus: Professional plus:

Competitive Analysis

- Use the [Wayback](#) Machine – Internet Archive



Explore more than 362 billion [web pages](#) saved over time

BROWSE HISTORY

- Know the Market
- Price changes over time
- Service/Product Offerings
- Terms – duration, contract length

Hubspot Example

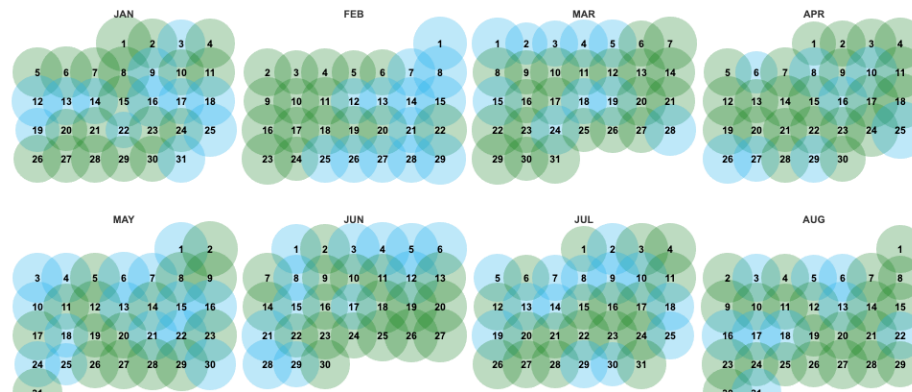
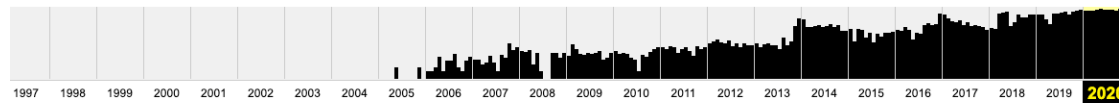
INTERNET ARCHIVE Explore more than 510 billion web pages saved over time

[DONATE](#) **WaybackMachine**

Results: 50 100 500

[Calendar](#) · [Collections](#) ^{beta} · [Changes](#) ^{beta} · [Summary](#) · [Site Map](#)

Saved **39,589** times between [May 10, 2005](#) and [December 16, 2020](#).



Hubspot example



[Software](#) [Pricing](#) [Case Studies](#) [Partners](#) [About Us](#) [Blog](#)

The only marketing software you'll ever need. Pricing that scales with your business.

1 Choose your base package

Basic

\$200/mo

A complete marketing system for hosted small businesses.

Professional

\$600/mo

A fully integrated software system for professional marketers.

Enterprise

\$1,000/mo

Our most advanced system for pro marketing teams.

Don't know which package is the best for you?

Compare Packages

Feature	Basic	Professional	Enterprise
Website Hosting with HubSpot's CMS			
Blogging tools			
Landing pages			

Promotions

- ▣ Freemium
- ▣ Time based
- ▣ Early Adopter based
- ▣ Percentage Discount
- ▣ Grandfather early users

How to Monetize Your Startup: Revenue Models

3. Subscription

- ▣ Example: [Salesforce](#), [Box](#), [Spotify](#)
- ▣ Use: B2C & B2B
- ▣ Key Metrics
 - ▣ Average Revenue Per User (ARPU)
 - ▣ Conversion ratio – e.g. trial to purchase
 - ▣ Churn
- ▣ Challenges: MVP won't be enough to be Kick Ass Product
- ▣ Notes: Highest multiple, forecastable revenue

5. Transaction Fees/Rental

- ▣ Example: [99Designs](#), [KickStarter](#), [Elance](#), [Chugg](#)
- ▣ Use: B2C & B2B
- ▣ Key Metrics
 - ▣ Average transaction revenue
 - ▣ Fee % per transaction
 - ▣ Number of transactions
- ▣ Challenges: Margins are small (15%), need efficiency
- ▣ Notes: Don't start too low

6. Productize a Service

- Your offerings is generally complex and requires services to deploy
 - Gross margin on Services >35%
 - Product development comes with services
- Use: B2C & B2B
- Examples: Moz, service company convert to tools.
- Challenges – difficult to make the transition away from services

8. Marketplaces

- Example: [eBay](#), [Alibaba](#)
- Use: B2C & B2B
- Key Metrics
 - ▣ Average Transaction Amount
 - ▣ Number of Monthly Transactions
 - ▣ Commission %
- Challenges: two sided market places require you start with one side, value to seller & Product market fit (x2)
- Notes: critical mass or marketplace required

Revenue Models– Primary/Secondary

1. Fee for Service
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Top Templates

- ▣ [Templates folder](#)
- ▣ Subscription
 - ▣ Recurring revenue, churn, ARR/MRR, LTV:CAC Ratio
- ▣ Transaction Fee/Rental (not booking topline revenue)
 - ▣ Avg transaction amount, % commission, # transactions/mo, LTV:CAC
- ▣ Productize a Service – people are required for some portion – most robust model, includes subscription
 - ▣ Split of revenue between product/services
- ▣ Marketplace –
 - ▣ Two funnels, buy/sell side, % fee, 2X LTV:CAC

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Staffing & Major Milestones

Mapping Expenses

- ▣ Product Team
- ▣ Marketing
- ▣ Sales
- ▣ General and Administrative Expense
- ▣ Other milestones
 - ▣ Legal, Trademark

Quarterly Planner Example

A1:A2 fx Quarterly Milestones

	A	B	C	D	E	F	G	H	I	J
1	Quarterly Milestones	Q4 2020	Priority (ABC)	Impact (HML)	Q4 2021	Priority (ABC)	Impact (HML)	Q2 2021	Priority (ABC)	Impact (HML)
2										
3	Marketing Customer Acquisition (Owner)									
4										
5	Marketing Budget				\$1,500					
6	Marketing Channels				Social					
7	New Marketing Qualified Leads				22			30		
8	Leads passed to sales									
9	Return on Adversiting Spend (ROAS)									
10	LTV:CAC Ratio				4.7			5.1		
11										
12										
13	Sales (Owner)									
14	Reps headcount									
15	SDR/Customer Success headcount									
16	New Sales Qualified Leads				8			10		
17	New Closed Customer				2			3		
18	Time to Close									
19	Average Contract Value (ACV)									
20	Repeat Customers				4			6		
21										
22	Revenue (Owner)									
23	Billings				Revenue Splits					
24	Major Accounts									
25	Collections				Day Sales Outstanding (DSO) how long from billing to collections					
26	Churn (lost accounts)									
27										
28					MRR					
29	Growth from prior quarter				ACV trends					
30	Total (quarter ending run rate)	\$	-		\$	212,000.0		\$	-	\$
31	Product/Services (Owner)									

Inc. 500

Inc 500 Data – Quiz: How much revenue to you need in three year to end up on the Inc 500 List?

<https://www.inc.com/inc5000/list/2017>

	2019	2018	2017	2016	2015	2014	2013	2012	2011	2010	Average
1	\$36.90	\$99.00	\$54.20	\$116.20	\$118.20	\$195.60	\$117.90	\$59.50	\$195.60	\$325.00	\$131.81
2	\$33.60	\$168.80	\$37.40	\$55.00	\$34.40	\$82.60	\$49.60	\$26.90	\$38.00	\$15.60	\$54.19
3	\$24.90	\$255.00	\$48.80	\$33.50	\$33.60	\$85.10	\$25.50	\$21.80	\$20.90	\$37.50	\$58.66
4	\$32.40	\$49.20	\$26.80	\$30.70	\$83.70	\$35.30	\$1.9b	\$14.70	\$17.10	\$14.40	\$33.81
5	\$22.50	\$219.60	\$49.10	\$33.40	\$44.60	\$77.70	\$87.00	\$55.00	\$16.40	\$17.90	\$62.32
6	\$271.80	\$21.90	\$19.70	\$17.70	\$32.90	\$138.00	\$45.70	\$55.60	\$14.20	\$249.80	\$86.73
7	\$20.50	\$43.10	\$23.20	\$15.70	\$37.20	\$27.30	\$25.50	\$12.40	\$15.10	\$26.20	\$24.62
8	\$23.30	\$16.90	\$59.60	\$15.60	\$30.50	\$159.90	\$23.90	\$21.80	\$15.20	\$131.40	\$49.81
9	\$225.90	\$224.70	\$41.70	\$42.40	\$32.10	\$26.30	\$33.10	\$31.70	\$14.90	\$19.10	\$69.19
10	\$21.40	\$50.30	\$17.20	\$25.90	\$31.10	\$32.90	\$18.60	\$14.20	\$12.40	\$11.20	\$23.52
	\$71.32	\$114.85	\$37.77	\$38.61	\$47.83	\$86.07	\$42.68	\$31.36	\$35.98	\$84.81	

Inc 500 List

- Data from Top 10 over 10 years
 - Avg \$59.47M
 - High Average \$131.81M
 - Low Average \$23.52
 - All from a baseline revenue of \$1M in first of three years

Common Mistakes

- ❑ Complex and confusing assumptions - not on one tab
- ❑ Confusing model design
- ❑ Metrics and success factors not defined
- ❑ Overly aggressive revenue ramp
- ❑ Understanding expenses and cash needs (optimism)
- ❑ Key milestones not clearly outlined

Templates

1. Choose one
2. Familiarize yourself
3. Startup with Assumptions
4. Move to Compensation and people
5. Revenue next
6. Forecast

Supporting Slides

Corp Hygiene Note

- Museum Quality
 - Fully executed contracts
 - In OneHub, Drive, etc.
 - Offer letters, W-4, I-9, options, PIIA
 - Termination procedures
 - Contractor files – NDA, Inventions Agreements
 - Closed monthly books
 - Payroll and tax payments