How to Thrive in the Subscription Economy

By Tien Tzuo , Founder & CEO, Zuora

What you deliver and how you deliver it to customers has to be completely rethought.

A trend began in 2007 that would soon be recognised as a once-in-a-century transformation of the way business is transacted: away from buying products towards subscribing to services. We call this new business environment the “subscription economy”. Companies like salesforce.com, Amazon, Netflix, and Box were the vanguard. Not only did they completely change how companies deliver services to customers, they also reinvented customer relationship management (CRM). Their almost total customer centricity is not just good customer service, it is a massive revenue opportunity that is relevant to nearly every industry.

In the traditional 20th century model of doing business, companies aimed to create hit products and sell them through as many channels as possible. Products were consumed mainly on a one-off basis by a mostly anonymous customer. Getting a sense of the customer was the job of market research firms which conducted surveys on foot to understand who was buying what. Leaders in the subscription economy have changed this model and now view their customers as subscribers. They form an ongoing relationship with consumers: Getting to know who they are, what they view, what the customers buy, where they spend their time, what sort of products they like, and other demographic information.

These companies, therefore, extend value to their customers that is anchored in their brand, opening up an entirely new set of possibilities. And all prominent subscription economy players aren’t selling purely digital products. Industrial companies like General Electric and Caterpillar are getting in on the action. When Caterpillar started enabling its tractors and engines with internet-enabled sensors, it opened up massive revenue opportunities in predictive maintenance and management systems, above and beyond the old model of selling a piece of hardware.

Providers of software, books and music, media and entertainment companies (News Corp, HBO); consumer services (TripAdvisor, Touring Club Suisse); telecom and utilities (Telstra); financial services (AXA); healthcare (Thermo Fisher Scientific); education (lynda.com, Kaplan); and farming (FarmIQ) are pivoting to or starting up as subscription businesses with recurring revenue.

A new type of customer

To thrive in the subscription economy, it’s not enough to slap a low monthly price on a product and call it a service. What you deliver and how you deliver it must be completely rethought – not in the boardroom or a conference room, and not just with product managers and the finance team.

Instead, the whole business model needs to be rethought from the perspective of the relationship to subscribers, because the shift to the subscription economy is driven by subscribers, not vendors. According to a 2014 **report** by *The Economist Intelligence Unit*, 80 percent of customers demand new consumption models including subscribing, sharing and leasing – anything other than actually buying a product outright.

Customers today, especially millennials, see less separation between their business selves and personal selves and therefore expect their business relationships to be more personalised. They also expect a real-time experience with immediate fulfilment. By definition, subscribers can easily switch service providers, so vendors who want to earn the loyalty of their subscribers must present on-going value and memorable services that improve over time. To provide this, they must be able to sell, market and deliver based on a clear understanding of subscriber behaviour, and vendors must nurture each subscriber relationship.

New tools for new relationships

To operate in the subscription economy, companies need new software applications that will facilitate their transformation. Over the past 20 years, companies large and small have invested millions and even billions into CRM and enterprise resource planning (ERP) systems to support sales automation, customer service, inventory management, supply chains and accounting.

CRM and ERP systems, however, were designed for products, not subscriptions. In a world where every customer is now a subscriber, companies must adopt new technology to manage the entire subscriber lifecycle, including new subscriber acquisition, subscription management (i.e. enabling subscribers to upgrade, downgrade, renew or otherwise modify subscriptions), automating recurring billing and payments and measuring recurring revenue and subscription metrics.

Making the change

In addition to deploying new software to manage subscriptions, companies shifting to a subscription model must transform themselves in four key areas:

- **Subscriber identity** – It is now insufficient to maintain customer records that only include contact information such as name, phone and email address. A “subscriber identity record” must include purchases, products, local pricing, promotions, payment history, refund history, renewal value, usage metrics and much more.
- **Subscriber journey** – Companies must now create and manage a complete subscriber journey that personalises and deepens the relationship from initial signup and purchase to include upgrades, add-ons, new services and renewals.
- **Subscriber culture** – Creating a subscriber culture means that every working professional that touches the brand and subscription experience – every marketer, seller, partner, product specialist, customer service representative and finance professional – is focused on the subscriber relationship. They put the subscriber first, generously share knowledge and are always adapting to the evolving needs of subscribers.

- **New metrics** – Subscription-based companies must be able to track a new set of metrics for subscriber health (subscriber growth and change), business velocity (annual contract value and total contract value), subscriber engagement (payments and declined transactions), subscription finance (monthly and annual recurring revenue) and relationship retention (renewals, upsells and **churn**).

Market opportunity

The need for new technology has created a multi-billion dollar software category focused on "relationship business management". While reliable statistics are not yet available to measure this new and rapidly growing market, companies such as GM, News Corp, and Schneider, predict that anywhere from 40 to 100 percent of their revenues will eventually be subscriptions. If just 10 percent of the companies in the world transition 50 percent of their revenues to subscriptions, that is easily a US$10 - $20 billion market.

The shift to the subscription economy is accelerating. Companies that want to become or remain industry leaders and enjoy the financial, market, technology and customer loyalty benefits of deep, long-term subscriber relationships need to begin planning their transformation today.

The article is based on a ***webinar*** *given by Tien Tzuo, organised by the INSEAD Technology, Media and Telecoms (TMT) Alumni Network with the support of INSEAD eLab, with Vikas Pandurkar of the INSEAD TMT Network and Theodoros Evgeniou, INSEAD Professor of Decision Sciences and Technology Management.*

Tien Tzuo *is the founder and CEO of Zuora.*

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About the author(s)

Tien Tzuo Tien Tzuo is the founder & CEO of Zuora.