Average Revenue Per User: Your Questions Answered

An important metric in nearly all businesses, ARPU (average revenue per unit) is a great way to measure the effectiveness of subscription-based services. This metric is useful if you run an eCommerce business that relies on subscription revenue, such as a SaaS platform or a suite of mobile apps.

In this post, we'll be talking about what ARPU is, how you can calculate it, and interpret it. We'll also include examples of good and bad ARPU, and the common ARPU meaning, and industry definition.

What is Average Revenue Per Unit (ARPU)?

What does ARPU stand for? The ARPU definition is as follows: ARPU stands for *Average Revenue Per Unit* or *Average Revenue Per User*. The term is commonly used in the software and telecom industries.

Average revenue per unit is calculated by dividing average revenue over a time period by the number of actively subscribed users. The ARPU calculation formula looks like this:

ARPU = (Monthly Revenue) / (active subscribers)

Most businesses use a time period of a month. So, for example, if your SaaS accounting platform has monthly revenue of $600,000 and 30,000 active subscribers, you'd be looking at ARPUs of $200 per user, per month. This is the most common way to define ARPU.

ARPU is commonly used for online businesses, in telecom, and with any business that uses subscription services.

Understanding and Calculating Average Revenue Per Unit (ARPU)

While knowing how to calculate ARPU is simple, it's important to understand that this is a revenue figure, not a profit one. An important step that you will need to take will be to also compute your customer acquisition cost and subtract it from your Lifetime Customer Value, so you can determine your margin figure and thus potential profit. Your CAC (customer acquisition cost) is a number that goes along with the ARPU, and is just as important. We'll be explaining LTV below, which is derived from ARPU.

How to Interpret Average Revenue Per Unit (ARPU)

There are a few ways to interpret whether you have a good ARPU number. Here are a few examples:

Comparison to Competitors

If you can find out your competitors ARPU, LTV, and CAC, you can adjust your product and pricing to provide a better value to your customers.

Segmenting Your Customers to Determine Profitability

Some customers will be "whales" and provide you with the majority of your profits. By focusing on your most profitable customers, you can determine how to strategically use your resources for the best performance.

Different customer channels and segments may have different customer acquisition costs, based on the product being sold, incidental costs to onboard a client, and so on. This will mean that each subscription product will have a different CAC number and thus a different

profit margin. CAC and ARPU should be carefully modeled and discussed when setting subscription prices for products.

Forecasting

Using past performance and market information should in turn be used to set CAC and ARPU numbers. If, for example, set up costs and thus CAC for a particular product goes up by 30%, can the market bear a 30% subscription increase to match? Can ways be found to lower the CAC in response? Can a reduction in materials or labor costs help bring prices under control for a particular product? Can product development and improvement in features and value enable an increase in subscription prices and ARPU? Forecasting these changes will help.

The Importance of ARPU in LTV

ARPU is important because it helps you calculate Lifetime Customer Value. Lifetime customer value is the revenue that a customer is expected to generate over the lifetime of their account, subtracted from the customer's CAC. So, say you have a customer who has a monthly ARPU of $30 per month, and they remain your customer for five years. This then means that the customer's LTV is their ARPU multiplied by 60 months, and then subtracted from their CAC. Say this customer cost $500 to acquire. Thus:

(Monthly ARPU) X (Subscription Lifetime in Months)-(CAC)=LTV
[($30 per month)X(60 months)=$1800] – [500] = $1300

The obvious way to increase profits in a subscription model is to maintain engagement and provide value in the product over the course of the subscription while keeping CAC as low as possible.

Examples of Good and Bad ARPU

Standard definitions of what constitutes a good ARPU are hard to come by, as most firms keep their detailed financials private. Generally, in the mobile game space, an ARPU of $1-$2 USD monthly is considered a benchmark. An average figure of $.04 US is given for most mobile apps.

An example of good ARPU is a subscription product that enables CAC costs to be quickly recuperated. This can be seen in the field of mobile games, where most costs are upfront development ones and where only minimal costs are paid for content updates.

An example of a bad ARPU is a subscription repair service that where constant calls for service on a product drive up the CAC and call for a longer subscription cycle to recoup costs.

The idea here is that by providing greater value, a business can keep a customer subscribed longer, and can demand a higher subscription cost, thus increasing ARPU and profit margins.

Let FastSpring Answer Your Questions About ARPU

Do you have more questions about ARPU? FastSpring has been working with e-commerce and subscription model services for years. Contact us so that we can help you with your questions about ARPU, lifetime customer value, customer acquisition cost, and subscription billing software.