Smith Insights
Whitepaper

Control your costs. Maximize your profits.

Optimize your organization's customer acquisition strategies.

Smith

How do you know if you're spending too much, or not enough, on acquiring new customers? Finding the right balance between what you spend on marketing (including salaries, ad spend and commissions) and on new customer support and what you bring in from those new customers, not to mention how you retain those customers, will mean all the difference to your growth and profitability. A basic metric that every business should know is its customer acquisition costs.

Simply put, CAC is how much it costs to win the business of a new customer. It's an essential number that you need to know, no matter what sort of business you're in. It's a calculation that considers every cost that goes into acquiring new business.

You can perform a simple calculation and get a basic CAC, or you can include more detailed data for a more complex, but also more precise, CAC.

The Basic Method

$$CAC = \frac{MCC}{CA}$$

CAC: Customer acquisition costs

MCC: Marketing costs for new customers

CA: Customers acquired

The Complex Method

$$CAC = \frac{MCC + W + S + PS + O}{CA}$$

CAC: Customer acquisition costs

MCC: Marketing costs for new customers

W: Wages for sales and marketing staff

S: Software and resource costs for marketing and sales

PS: Outside professional marketing services used

O: Overhead

CA: Customers acquired

If your marketing program is relatively simple and self-contained, or if you are happy with a simpler calculation, go with the basic method. If your organization uses a complex, multi-pronged marketing and sales approach, you may be better served by the greater clarity provided by the complex calculation. It's up to you to make the choice for you and your company.

Now that we've established what CAC is and how you can calculate yours, let's talk about goals.

It's all well and good to want to improve your customer acquisition strategies, but if you don't know precisely how you want it to improve, your attempts will be made blindly. The first thing you should do is decide what you're trying to achieve with your strategy and how you will measure that performance.

Maybe your goal is simply to acquire a certain number of new customers out of a new marketing campaign, or over a set amount of time. Great—that's a clear goal that's easy to measure.

Maybe your goals are more nuanced: you are looking to drive up web traffic by 20%, email open rates by 25%, click-through rates by 15%, and so on, on top of acquiring 100 new customers. Fantastic—those are all important outcomes, and a smart and strategic plan with measurable and defined KPIs should be able to help you reach them. At the end of the day, though, the biggest metric every business is looking to improve is profitability.

Profitability is the truest measure of the growth potential for any business. You need to know how much money you're bringing versus what you're spending in order to plan for growth and the long-term sustainability of your company.

In a previous article, we made our case for why we believe Customer Lifetime Value (CLV) to be the best metric to use to track the effectiveness of your strategies. When you measure your customer base, you need to track not only sales and monetary value, but also which segments of your customers represent the longest-lasting and most profitable relationships. CLV does this best with the broadest view across your entire customer base.

The real marketing wizardry comes in learning how to read both figures—CLV and CAC—in relation to each other, and to use them together to judge the true effectiveness of your customer acquisition strategy. CAC is the ultimate way to understand the ROI you are getting from your marketing efforts. You can learn to see exactly how much you are spending to acquire new customers, how valuable those customers are, and how you can adapt your marketing to be even better at drawing in your target demographics. For instance, if you find one particular tactic or channel that brings in a high-CLV customer segment, you could tailor your marketing to appeal more directly to those segments, trim away excess or underperforming campaigns, and improve your overall CAC.

As with any proper analysis, however, it's very important to measure CAC on a customer segment level. Just like we recommended with CLV, tracking CAC by segment means you get a much clearer picture of where you are getting the greatest value for your marketing dollars and where you need to improve. You can easily get a picture of where your campaign spending is getting the best returns and adjust your strategy accordingly.

Finding your best strategy

Now that we have a sense of what CAC is, we can begin to think about how to lower costs and improve results.

There are lots of different ways to go about optimizing customer acquisition. There is no one-size-fits-all plan. Depending on your type of business, or how you specifically measure customer value, any number of techniques—or a combination therein—could be the key to profitable customer acquisition.

Each of these methods involve a different set of tactics and strategies to achieve the greatest results. Let's explore them in greater detail so you can determine which is the best path forward for your business.

At a high level, there are seven main ways to improve your CAC:

- Customer research
- Personalization
- Retargeting
- Content marketing
- User-generated content
- Search engine marketing/search engine optimization (SEM/SEO)
- Price optimization

Interested in learning more about CAC?

Visit smithcommerce.com/customer-acquisition-costs to download the full whitepaper.

The first thing you should do is get to know your customers. It sounds simple—maybe even misleadingly so—but many companies don't know their customers as well as they think they do.

When you don't know—or understand—who your customers are, what they want and what they value, what you're really doing is using a 'Spray and Pray' approach to marketing: you blast out as many ads, campaigns [illegible] (and praying) something works.

This is, to put it kindly, not the best approach. You could literally be throwing money away on marketing campaigns that achieve zero results. Even if they do somehow succeed, you end up with a campaign whose results you will have big trouble replicating, since you can't always know how or why your approach worked.

Without knowing who your customers are, you fall victim to one of the oldest sales clichés in the world: you can't sell to everyone. You need to know who is most likely to buy your product and then aim your marketing efforts at places those people are likely to see. This way, your marketing campaign is focused to a much greater degree before you've even begun.

Before you spend a single cent on marketing, you should know a lot about the customers you're trying to appeal to.

There's a lot to consider. Do you know all this information about your current customers? If not, it's time to get learning.

Who your customers are:

- Age, demographics, locations, socioeconomic status, and for B2B businesses, their position, industry, use cases, buying power, etc.
- What problems your customers are trying to solve, and how they are currently dealing with their problem—either through a competing product, internal process, or not at all
- Exactly what products and services they require
- [illegible]—when they buy, how often and under what circumstances, such as urgent need, annual or biannual refreshes, or on a whim

- Who the decisionmakers are
- What entices them to buy
- What information they need to either make their decision or influence others at their company who can affect the final decision
- Your value proposition and how you differ from your competitors (and how your competitors position themselves to this same audience)