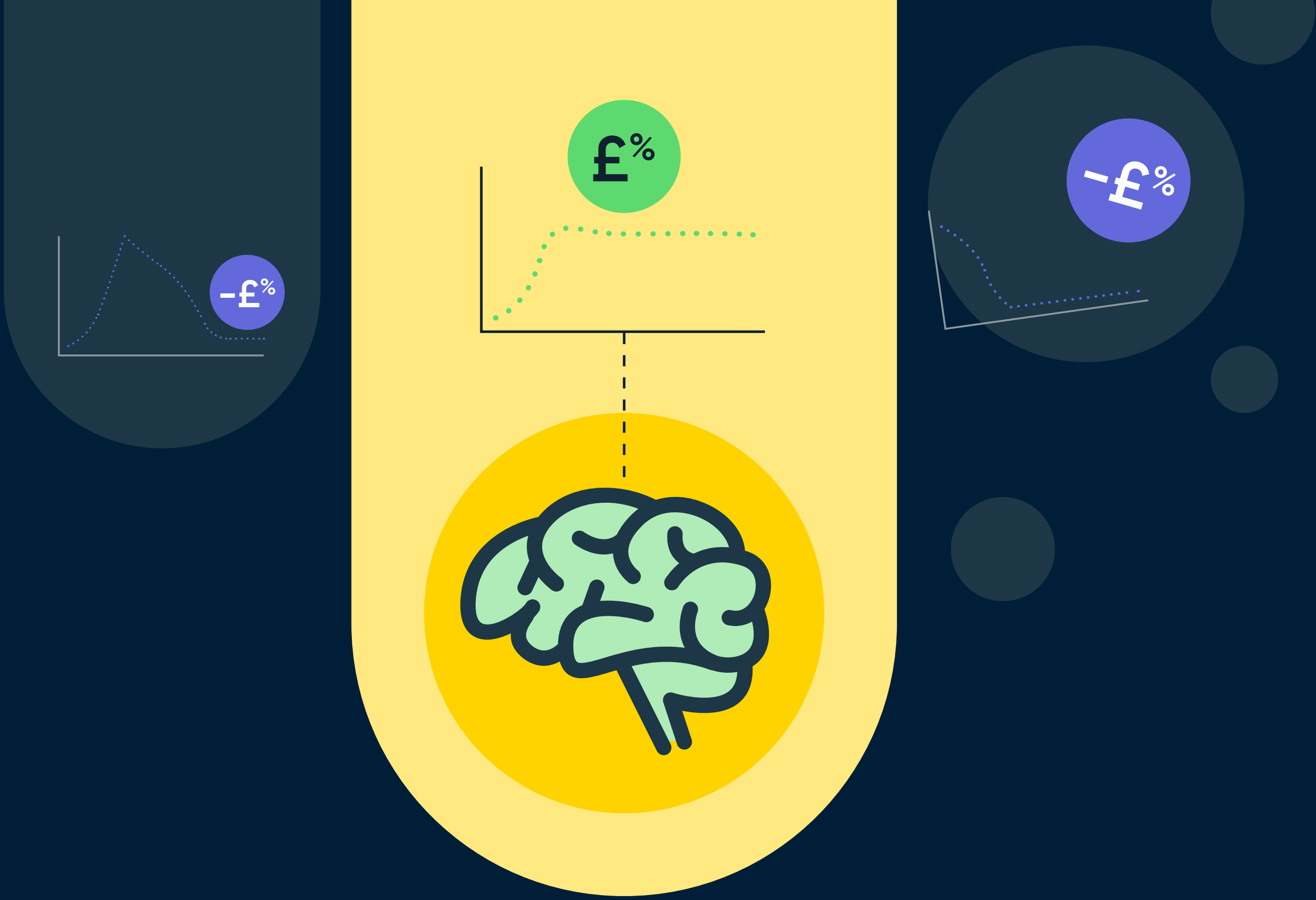
The Complete Guide to Customer Acquisition Cost (CAC)

CATALYST
Marketing Agency



The way SMEs are choosing to grow is changing. Gone are the days of 'growth at all costs'; a revolution of scalability, cost-effective processes and intelligent investment in marketing has arrived, and we're all for it!

For a long time, 'growth' has been synonymous with 'profit'. However, rampant growth without proper preparation is not, and has never been sustainable.

That's where customer acquisition cost analysis is so important for any business, from startups and SMEs all the way up to multinational conglomerates. It's the process of understanding how much it costs your business to acquire high-value customers, and knowing what needs to be done in order to reduce that cost.

Every business can calculate their customer acquisition cost (CAC), and every business should be comparing it to their LTV (customer lifetime value). By working out your LTV:CAC ratio, you can effectively optimise your processes to promote longevity, profitability and sustainable growth.

In this guide, we'll teach you how you can do exactly that, as well as running through everything you need to know about your CAC.

What is Customer Acquisition Cost?

How much does it cost your business to win a new customer?

This is the question at the core of CAC – it's a measure of everything you spend on sales and marketing when attracting, nurturing and closing new customers.

Many businesses use it to identify where the majority of their profit is coming from. If you don't know how much you're spending to attract customers, how will you ever understand your return on investment?

CAC is used to:

- Calculate your ROI
- Identify which marketing channels are best
- Project budgets
- Assess how viable your business is

When compared to your customer lifetime value (LTV) your CAC yields incredibly valuable information that every business should be relying on.

How to calculate your CAC

It's time for a little maths – calculators, at the ready!

To calculate your CAC, you need to add your sales and marketing expenditure together. You then divide the sum by the total number of customers acquired through that expenditure.

Do this on a timeframe, so X expenditure in a quarter or year yields Y customers.

Costs you need to consider are:

- **Salaries**
- **Production costs** (costs of producing content, campaigns, events, etc.)
- **Software** costs (sales and marketing tools such as automation software and analytics tools)
- **Paid media**, ads and publications (Google Ads, sponsored content, social ads, etc.)

Example

Say your sales and marketing spend in a quarter came to a total cost of £30,000 .

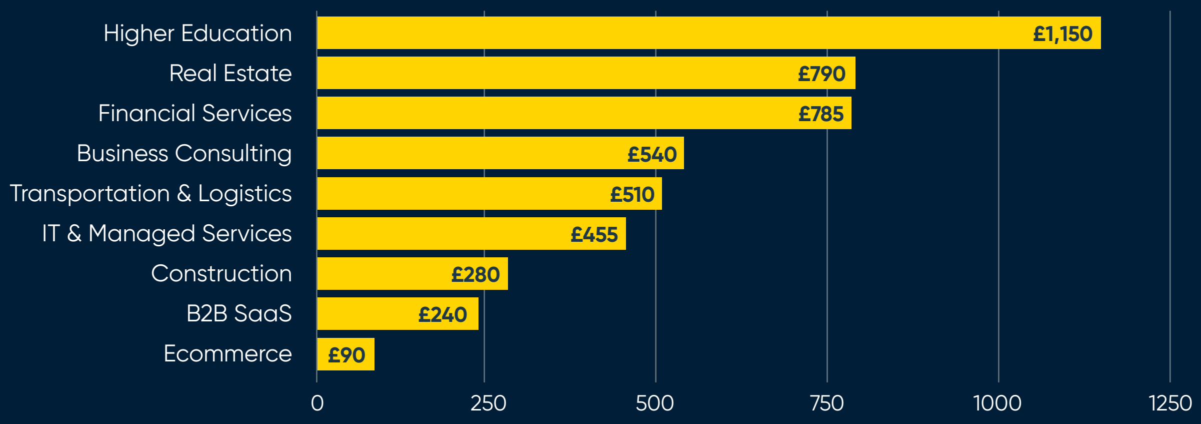
In that time, you managed to acquire 500 customers. By dividing £30,000 by 500 , you get a customer acquisition cost of £60 per customer.

Of course, this value will vary dramatically depending on your LTV, as mentioned earlier. Low value, high volume businesses will likely have a lower CAC, whereas high value, low volume businesses will have the opposite – it's all about balance, which leads us to our next section...

What does a good CAC look like?

To know whether your CAC is up to standard, it's good to benchmark your business against the industry average.

Here's some averages:



These averages give you a good idea of what you should be looking at, however, if you're a startup or a young SME, then your CAC will likely be higher as you'll have other expenses too, such as establishing your brand, building a website or setting up processes.

As you grow, you'll start to see the impact of your long-term strategies such as SEO, gated content and your social channels. All of this will help to lower your acquisition cost, so don't be demoralised if your CAC is high at the moment!

Remember – even if you're spending upwards of a grand to attract each customer, and that seems like a lot, you need to consider how much that individual will spend with you over their lifetime.

Consider the price of your products/services, your sales cycle and business model.

For example, if your CAC is £1,000, but you've just landed a client who is going to pay £1,000s over the next few years, your margins will be significant. If you're spending the same money to attract high-churn, low-paying customers, then your CAC isn't sustainable.

That's why it's so essential to calculate your LTV:CAC ratio.

What is the LTV:CAC ratio, and how to calculate it

This is one of the most important metrics that every business owner should understand.

It compares how much you're spending to win new customers to how much they're going to spend with your business in their lifetime.

Generally speaking, you want your LTV to be roughly 3x your CAC, so every new customer comes with a 300% profit.

It's time for a little more maths – your LTV is the product of three factors, multiplied together:

Your LTV =

The average value of a purchase X The average number of purchases per year X The average customer lifespan in years

We'll keep the numbers small to help keep the maths simple.

Imagine your customers spend £20 on average. They make a purchase twice a year, and usually buy from you over the course of 5 years.

That's 20 x 2 x 5, or a LTV of £200. **To calculate your LTV:CAC ratio, you then need to divide this by your CAC.**

Take our hypothetical CAC from earlier, £60. £200/60 = £3.33.

In this instance, for every £1 you invest in obtaining a customer, they will spend £3.33 with you. This is, of course, more than 3x your initial investment, which is fantastic news - a 300% return on investment!

What do different LTV:CAC ratios tell you?

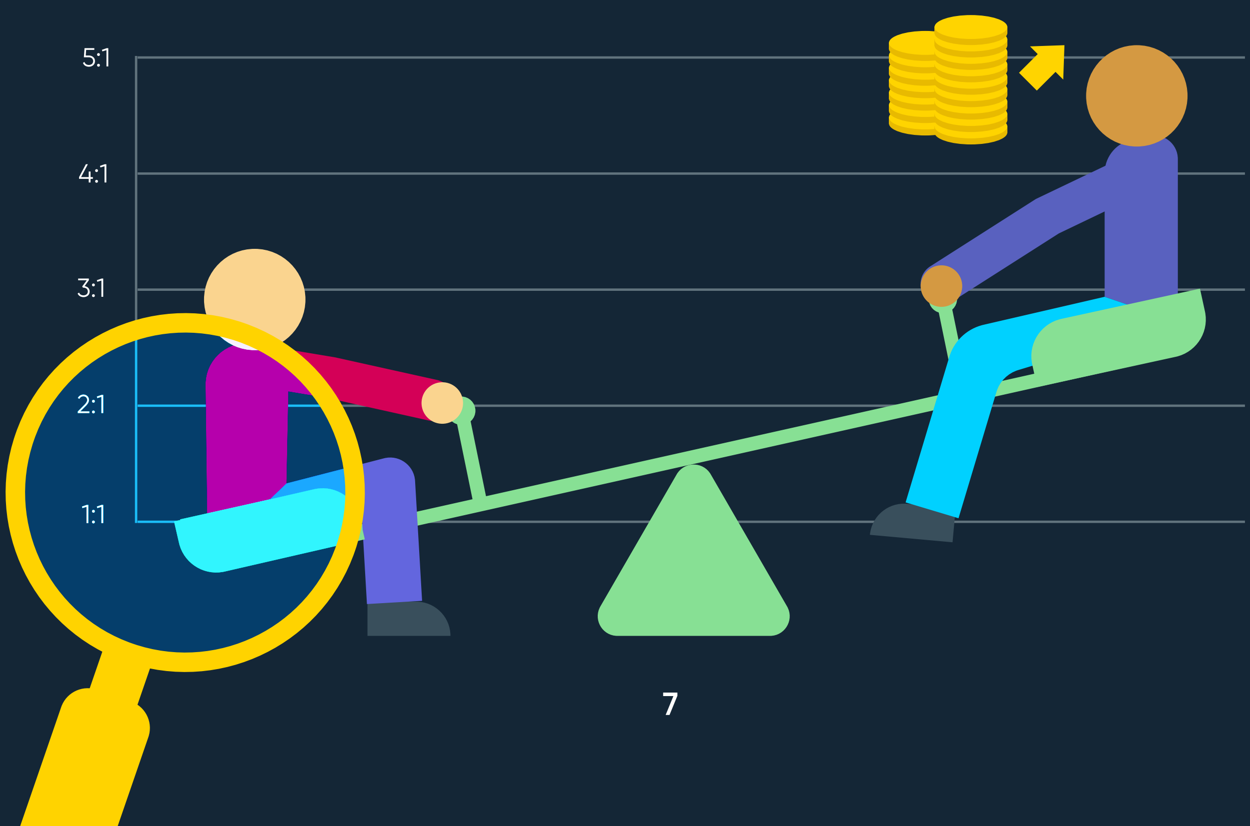
If your ratio is less than 3:1, that means you're spending too much to acquire customers who aren't high enough value – they're not spending enough. Your ROI is low, so you need to identify why this is.

Generally, we see the following leading to a low LTV:CAC ratio:

- Overreliance on expensive acquisition channels
- Poor messaging/brand positioning
- Incorrect pricing strategy (you might be charging too little!)
- High overheads
- Failure to identify the right target audience

On the other hand, if your ratio is too high (anything more than 5:1), then you have the capacity to invest in your sales and marketing to accelerate growth. Ratios like this suggest that you're missing out on opportunities.

More money spent = more profit here.

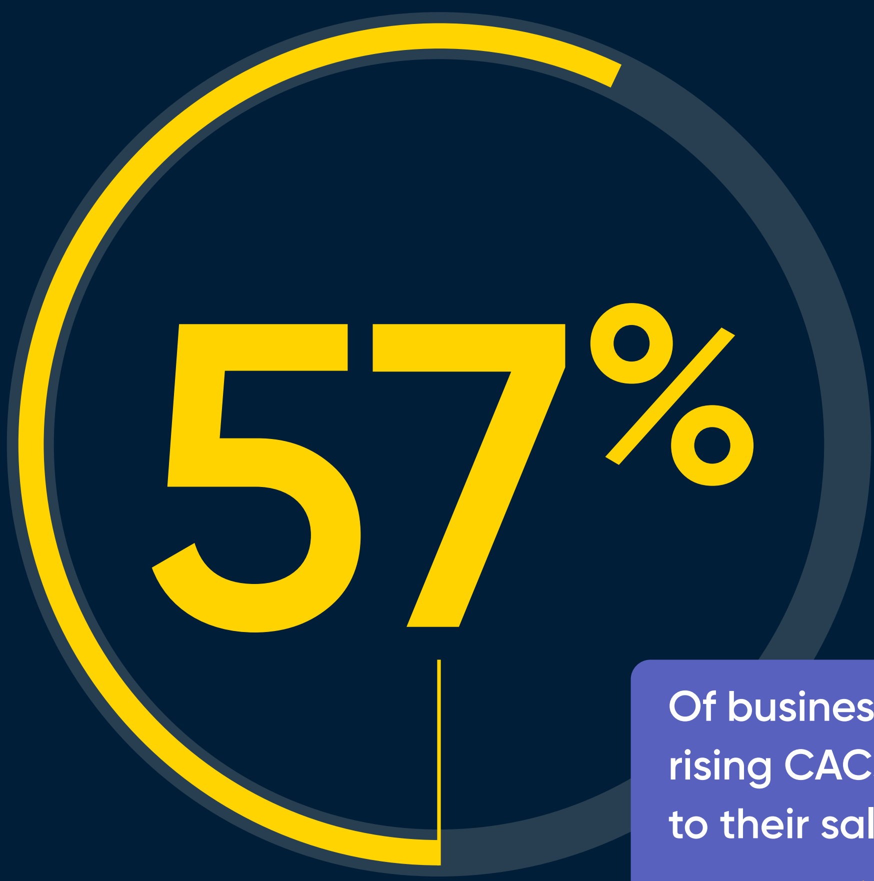


How to reduce your CAC and improve your LTV:CAC ratio

It's getting more and more expensive to acquire customers.

In fact, CommerceNext surveyed a broad range of businesses and found that 57% of them identified rising CACs as a threat to their sales goals.

It's more important than ever to focus on improving your LTV:CAC ratio – on the following pages are some strategies that can help.



Of businesses identified rising CACs as a threat to their sales goals

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Identify and use lower-cost channels

Choosing the best channels for your business can be incredibly hard.

You need to consider:

- What channels your customers use (this is the most important)
- How much the channels cost to use
- How well you can target on those channels
- How long does it take for you to see a return from the channel

The following matrix should help you when choosing your ongoing marketing channels:

Startup Inc Channel Matrix

	Cost	Targeting	Central	Input Times	Output Times	Scale
Perfect World	Low	High	High	Low	Low	High
Email	Medium	Medium	High	Low	Low	Medium
SEO	Low	Medium	Low	Medium	High	High
PPC	High	Medium	Medium	Medium	Medium	High
Paid Social	High	Medium	Medium	Medium	Medium	High
Organic Social	Low	Low	Low	Low	Medium	High
ABM	High	High	High	Medium	Low	Low

Channel value depends on business. For example, SEO input time could be high for one busines and low for another depending on how competitive the terms are.

It's worth noting – investing heavily into the cheapest channels won't necessarily work. Sometimes you have to spend money to make money.

For example, if your business operates in a niche industry with a high learning curve, it's unlikely that any of your content will go viral. You'll do better investing in SEO, email, podcasts, webinars and a new website, instead.

Struggling to decide which marketing channels are best for you? Don't worry, it's an incredibly difficult decision to make alone. Our digital marketing experts are on hand should you need bespoke advice about how you should proceed. You can give us a shout by clicking the link below.

Identify your key marketing channels

Balance paid vs organic

You'll want a good mix of both paid and organic marketing channels.

Organic channels are things like search engine optimisation (SEO), content marketing, email newsletters, etc.

Paid channels are ones that cost money, such as social ads, pay-per-click (PPC) advertising, etc.

This doesn't mean organic is free, you still need to invest in creating the content that will organically bring people to your website, but there are no ongoing costs. Any successful marketing strategy will utilise both types of channel; it's the best way to balance your CAC.

Broad vs deep

Are you casting a wide net and hoping to catch lots of fish, or are you throwing a harpoon into the sea looking for that big money catch?

You have two choices on how you spend – **broad** or **deep**.

Going broad allows you to reach more prospects across many channels, but it also spreads your attention and resources, meaning you can't invest as much into a single channel. This can help drive general awareness and volume, but won't necessarily drive the best leads.

Going deep is where you focus on one or two channels, investing heavily and leaving a lasting impression. Chances are you'll reach fewer prospects, but the ones you do reach will be better nurtured and more ready to purchase from you.

We recommend a varied approach. Some basic **broad marketing** can be great to help you capture low-hanging fruit and quick wins, while **deep marketing** can help you grab cream-of-the-crop leads.

Better optimise your funnel for conversion

Conversion rate optimisation is key for every business on the planet.

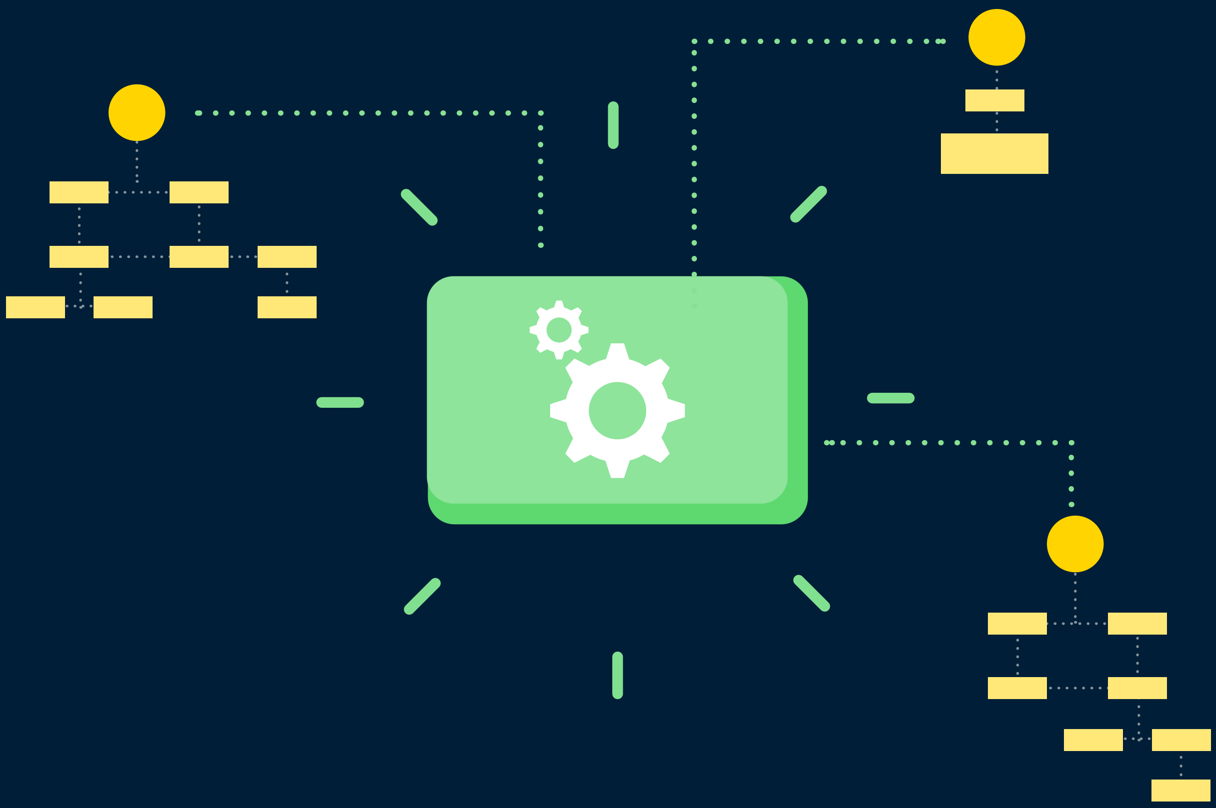
It's the process of improving the rate that visitors to your marketing channels take your desired action. By identifying which parts of your marketing funnel are good at converting leads, and which parts are underperforming, you can take what works and apply the same principles to what's not.

The best place to start is by mapping out the process prospects follow on their journey to become customers.

Chat with existing customers to learn how they found you and use Google Analytics data to help inform this. You may also choose to try out the prospect experience for yourself by browsing your site and pretending to be a customer!

Next up, you'll want to gather data. Heatmaps, surveys, analytics, A/B testing. All of these techniques can be used to quantify what's working.

Want to learn a little more about how you can better use website analytics? Click here.



Use automation to make your life easier!

One of the best ways to reduce your CAC is by removing monotonous, repetitive jobs from your employees' workload, allowing them to focus on creative and profitable projects.

This is where automation comes in. Automation can:

- Send out and manage workflows
- Automate your pipeline to ensure nothing is missed
- Answer frequently asked questions
- Operate a chatbot on your website
- Creating lead scores
- Determining marketing attribution

And much, much more. It's the best way to help your business scale, as automation grows alongside your needs.

More leads, less effort – what's not to love?

How Catalyst can help you improve your LTV:CAC ratio

Our specialist team at Catalyst consists of digital marketing specialists, design masters, copywriting whizzes and search experts, all of whom are ready to help you improve your LTV:CAC ratio.

How? By:

- Optimising your digital marketing process
- Improving your existing website, or building you a new one
- Creating and executing a killer content marketing plan
- Building up your SEO, PPC and email marketing

Everything we do is informed by data and in-depth research.
We'll never make a decision based on guesswork.

It's time that you took your business to the next level. Let's reduce your marketing spend and increase the number of leads generated together.

Talk to our marketing specialists

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