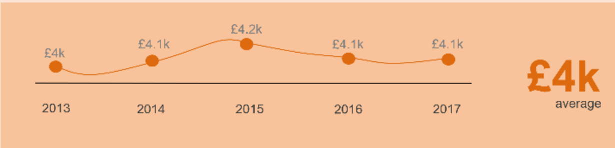
Customer Acquisition Cost & Lifetime Value

This case study >> Show how knowing LTV and CAC helps the automotive industry think about how to optimize their acquisition spending for maximum value to the right audience (value target) rather than focussing on minimum cost.

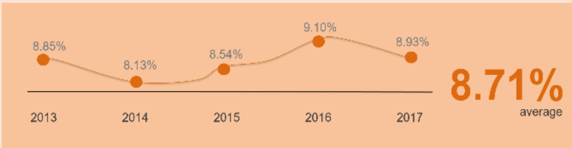
Step 1: The 6 key variables averaged

Average revenue and gross margin are well known to the dealership, but churn needs to be extracted over a 2 year period and elements that skew the data (e.g. fleet sales) are removed.

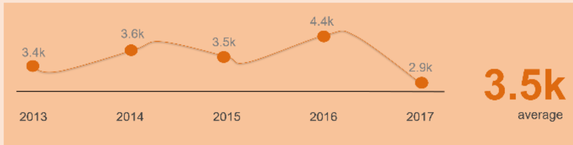
Average revenue per customer



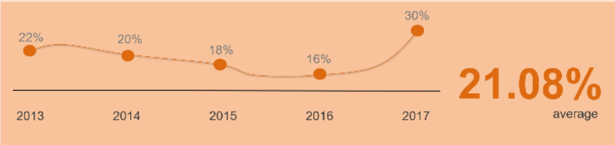
Gross Margin %



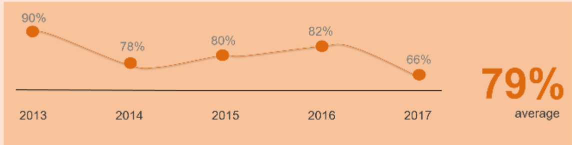
Number of new customers acquired



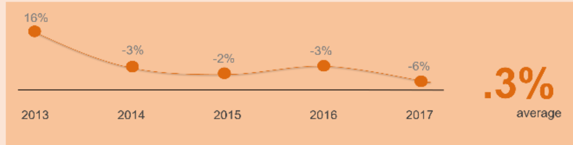
Churn %



Revenue Retention Rate %



Growth Rate %



Step 2: Calculate Customer Acquisition Cost (CAC)

$$\left(\frac{marketing + sales\ expenses}{number\ of\ new\ customers}\right)$$

2016 CAC =
£287

Step 3: Calculate Lifetime Value (LTV)

$$LTV = Averager\ Revenue\ Per\ Customer\ x\ Gross\ Margin\%\ x\ \left(\frac{1}{(1-K)} + \frac{G\ x\ K}{(1-K)^2}\right)$$

$$K = (1 - Churn)\ x\ (1 - Discount\ Rate)$$

Where:

Churn = $\left(\frac{\#\ customers\ @\ year\ end - \#\ new\ customers\ acquired\ during\ year}{\#customers\ @\ beginning\ of\ year}\right) x\ 100$

Growth = $\left(\left(\frac{revenue\ retention\ rate}{retention\ rate}\right) - 1\right) x\ 100$

Discount Rate = Is the interest rate used in discounted cash flow analysis to determine the present value of future cash flows. Usually the number is between 8% and 15%. We use 10%.

2016 LTV =
£1.2k

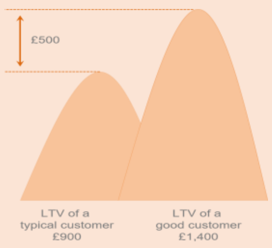
CAC:LTV ratio is: 1:4 Industry average is 1:3, so this is ✓ But could it be better?

Step 4: Breaking down LTV and CAC further

LTV & CAC will be different for different types of customers. The above calculations for LTV and CAC were done on company level. In this section we segmented the data: broke it down in order to perform different calculations for different types of customers:

Investing in "good" customers (LTV):
segmented by GM%

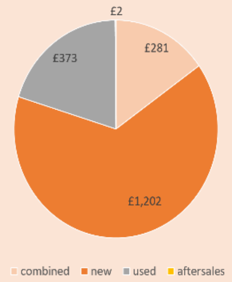
LTV can rigorously define the distinctions between *typical* and *good* which leads to greater creativity in increasing customer value.



A "good" customer may also be expensive to acquire (CAC) –
segmented by new/ used/ aftersales

X3

The CAC to acquire a new customer on a new car sale is ~3 times more expensive than a used car sale



Step 5: Individual level customer insight

Optimizing your acquisition spend for maximum LTV value to the right audience

Good customers

a My "good" customers have a greater LTV when:

A service plan is offered
A warranty is extended
A specific make or model is bought
A loyalty plan is offered
A certain amount is spent

\+

b My "good" customers have a lower CAC when:

They come direct to the website
They can complete a service online (new customers)
They are able to book a test drive online (new customers)

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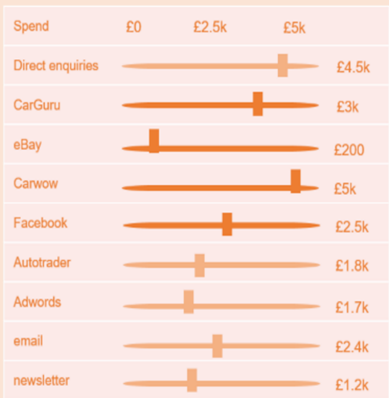
Good practice

c Ability to model CAC channels using "what if" analysis, for best CAC:LTV ratio:



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The result?

New CAC:LTV ratio 1:6

= super cool! ✓✓