

Management Article
Is Your Advertising Working? Calculating Customer Acquisition Cost
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Whenever you are wondering whether you should continue to run an advertisement or whether your last mailer was worth the cost, you need to consider customer acquisition costs.

Customer acquisition cost is not hard to understand, but few businesses do the math required to evaluate their advertising efforts.

I first learned about calculating customer acquisition costs while serving on the board of an Internet games company. At this firm, revenue per employee was fairly low, but the cost of acquiring a customer from certain kinds of promotional efforts was very high.

The calculations go like this. If you mail out 1,000 advertising fliers at a cost of 50 cents apiece, you will spend \$500. If you get 20 responses, it cost you \$25 per response. But you can't spend responses; you can only spend sales/profits. Now, if you were able to convince 100% of the people who responded to become customers, your customer acquisition cost would be \$25. But no one closes all their prospects.

In most businesses, closing 25% would be a reasonable rate. So, from the 20 responses, with a 25% close rate, you can expect to add 5 customers. Now your customer acquisition cost is \$125. WOW. That could still be great if your average sale were \$1,500, with a 50% gross margin. Simply put, it would cost you \$125 to bring in one customer that produces \$750 of gross margin.

Now, if your cost to mail those brochures were \$1.00 each, then your customer acquisition cost just doubled, to \$250. If the value of the sale were only \$30 with no repeat business, the advertising would be costing you money.

Without considering the numbers and the lifetime value of the customer in the case of repeat business, it's impossible to make an intelligent decision about whether your advertising is working.

In my small business consulting, I frequently find businesses that run \$1000 print ads without ever doing the customer acquisition math. Even if the advertisement only resulted in one new customer per time it ran, it still could be a good investment if the new customer contributes enough to profits.

Are you doing customer acquisition cost analysis on all of your advertising? If you are being advised to run ads that don't make money because you need to "build your brand" or "be in the market", you need to adjust your thinking and go where the numbers tell you to go.

Customer acquisition cost is always a part of any consulting or speaking assignment I do, and we always make sure participants in our Peer Benchmarking Group Sessions understand this important calculation as part of their overall small business marketing strategy.

As a promoter of my businesses, I have had to become a web expert. Now I'm helping other small business owners. I'll be glad to share some of the dos and don'ts of **creating an effective business web site** with you and the unique aspects of measuring customer acquisition cost for those customers your website attracts.

Remember only you can make business GREAT!

Ron Sturgeon, founder of [Mr. Mission Possible](#) small business consulting, combines over 35 years of entrepreneurship with an extensive resume in consulting, speaking, and business writing, with 3 books published and 2 more expected in 2010.

A business owner since age 17, Ron sold his chain of salvage yards to Ford Motor Company in 1999, and his innovations in database-driven direct marketing have been profiled in [Inc. Magazine](#). After the repurchase of Greenleaf Auto Recyclers from Ford and sale to Schnitzer Industries, Ron is now owner of the [DFW Elite Auto](#) suite of businesses and a successful real estate investor.

As a [consultant](#) and [peer benchmarking](#) leader, Ron shares his expertise in strategic planning, capitalization, compensation, growing market share, and more in his signature plain-spoken style, providing field-proven, high-profit best practices well ahead of the business news curve.

Ron is a web expert, but he is also an expert in helping all types of small businesses become more successful and more profitable. He has helped owners in industries from restaurants to law firms with a wide variety of business issues, including sales, promotion, production, financial measures, business strategy, and planning for start ups. Whatever your unique challenges, Ron can help you.

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