

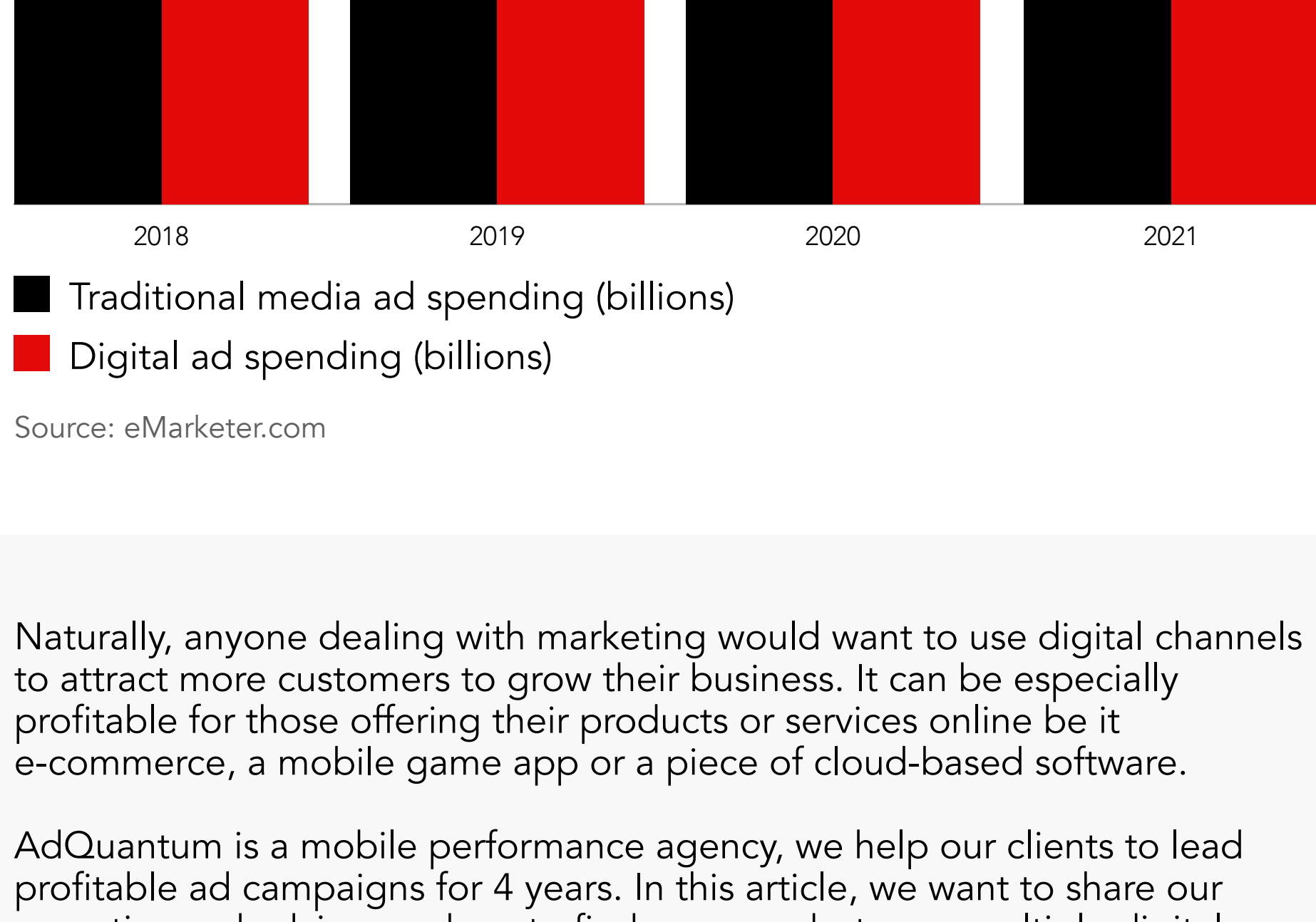
How to Get More Profit via Digital Channels

LTV > CAC

This year Digital ad spending became bigger than Traditional ad spending in the US for the first time. From now on the gap between Digital and Traditional advertising will only grow.

Digital vs. Traditional Ad Spending

United States, 2018-2021



Naturally, anyone dealing with marketing would want to use digital channels to attract more customers to grow their business. It can be especially profitable for those offering their products or services online be it e-commerce, a mobile game app or a piece of cloud-based software.

AdQuantum is a mobile performance agency, we help our clients to lead profitable ad campaigns for 4 years. In this article, we want to share our expertise and advise you how to find your way between multiple digital channels and make the right decisions to increase your profit.

Vocabulary

We use a lot of funny words here in digital marketing so let's agree on their meaning first.

- **User** - is your (potential) customer. A person who is genuinely interested in your product or service. If a user buys something from you they become a **Customer**.
- **Offer** - is your product or service that you want to advertise. If you are using some agency to help you with advertising then every single product, app or service you are running with them will be referred to as **Offer**.
- **Traffic** - is the flow of Internet users exposed to your offer one way or another. We may speak here about people who saw your ads or who visited your Facebook page or who browsed through your e-store. Traffic has parameters such as Impressions, Clicks, Conversion Rates, Costs, etc. which help marketers understand its amount and quality.
- **Tracking** - usually a third-party solution that allows you to gather and keep a record of your Traffic data. Tracking possibilities in digital are quite elaborate and it would be foolish not to use them for detailed analytics and optimization.
- **CPx** - Cost Per [enter your parameter here]. Most often we use **CPM** (Cost Per Mille / 1k views), **CPC** (Cost Per Click), **CPS** (Cost Per Sale), **CPA** (Cost Per Action) and a few others.
- **CTR** - not to confuse with the previous entry. CTR stands for Click Through Rate and is basically an indicator of your ad's success with the audience. The higher the better.
- **CAC** - Customer Acquisition Cost, rather self-explanatory.
- **LTV** - Life-Time Value of your customer, meaning how much money will you (probably) get from one customer.

As you can guess the path to success is to maximize your LTV while keeping your CAC low.

The logic is the same as when you buy something at a lower price to sell it at a higher price. In this case, you are buying your customers and they pay you back later.

Rule of thumb:

$$LTV > CAC \text{ or } \frac{LTV}{CAC} > 1$$

Let's look into a few examples.

NB: We've made up those numbers, none of them are real and serve for educational purposes only. Your real data may be very different, it is fine.

CAC (Customer Acquisition Cost)

Let's say you have 3 digital acquisition channels: Facebook, Google Ads, and Snapchat.

There are a few ad campaigns in each channel. Every channel has a different allocated budget and every ad campaign has a different conversion rate. Each channel generates some number of customers.

Channel/Campaign	Costs	Customers	CAC
Facebook	\$3 000	53	\$57
FB1	\$1 400	37	\$38
FB2	\$1 600	16	\$100
Google Ads	\$4 000	68	\$59
GA1	\$1 000	28	\$36
GA2	\$1 300	22	\$59
GA3	\$1 700	18	\$94
Snapchat	\$2 000	44	\$45
S1	\$1 100	23	\$48
S2	\$900	21	\$43
Total	\$9 000	165	\$55

CAC is a common metric to evaluate traffic quality. Remember, you want to keep it low.

$$CAC = \text{Costs} / \text{Customers}$$

Based on the above table, which Channel/Campaign is performing better?

- We can see that Snapchat has the lowest CAC = \$45 and Google Ads has the highest CAC = \$59. Does it mean we should stop Google Ads? Not yet.
- If we have a closer look at separate ad campaigns we'll see that there are two campaigns with very high CAC marked in red. In fact their CAC about the double than the average of \$55.
- So, we'd rather stop FB2 and GA3 campaigns and reallocate their budgets to the best performing green FB1 and GA1 campaigns.

**We presume that the conversion rate will stay the same regardless of the budget.*

Let's see our table after this optimization.

Channel/Campaign	Costs	Customers	CAC
Facebook	\$3 000	79	\$38
FB1	\$3 000	79	\$38
FB2	\$0	0	
Google Ads	\$4 000	98	\$41
GA1	\$2 700	76	\$36
GA2	\$1 300	22	\$59
GA3	\$0	0	
Snapchat	\$2 000	44	\$45
S1	\$1 100	23	\$48
S2	\$900	21	\$43
Total	\$9 000	221	\$41

It looks a lot better, doesn't it? For the same spend, we've got 56 more paying customers or +34%. The average CAC went down from \$55 to \$41.

We could stop our optimization at this point and it would be all right, but let's take a dive further.

LTV (Life Time Value)

There is something else to consider besides how much you pay to bring a customer on board. It is how much the customer pays you.

Different ad channels have different traffic quality. Users who come from those channels will have different payment habits and spend different amounts of money in your store or app. That's why we want to add some more columns to our table.

This is our campaigns data before the optimization.

Channel/Campaign	Costs	Customers	CAC	Gross margin	LTV	LTV/CAC	acc Profit
Facebook	\$3 000	53	\$57	\$10 900	\$550	\$9,7	\$7 900
FB1	\$1 400	37	\$38	\$3 700	\$100	\$2,6	\$2 300
FB2	\$1 600	16	\$100	\$7 200	\$450	\$4,5	\$5 600
Google Ads	\$4 000	68	\$59	\$9 640	\$420	\$7,1	\$5 640
GA1	\$1 000	28	\$36	\$2 800	\$100	\$2,8	\$1 800
GA2	\$1 300	22	\$59	\$5 940	\$270	\$4,6	\$4 640
GA3	\$1 700	18	\$94	\$900	\$50	\$0,5	-\$800
Snapchat	\$2 000	44	\$45	\$5 115	\$225	\$5,0	\$3 115
S1	\$1 100	23	\$48	\$4 485	\$195	\$4,1	\$3 385
S2	\$900	21	\$43	\$630	\$30	\$0,7	-\$270
Total	\$9 000	165	\$55	\$25 655	\$1 195	\$21,9	\$16 655

- Firstly, we see that GA3 is non-profitable as LTV/CAC < 1. We were not wrong for wanting to stop it. We remind you that your spend (CAC) should not be higher than your revenue (LTV). Don't run campaigns where CAC > LTV unless you have a very good reason to do it (for example brand campaigns).
- On the other hand, FB2 campaign has a very high LTV = \$450. Sure, the customers here cost a lot, but they will repay you.
- Have a look at S2 campaign. While its CAC was all right, the LTV/CAC < 1 and we can see that we are operating at a loss here.
- The total Profit of non-optimized campaign was \$16,655.

Now, let's see what happened to the profit after our first CAC optimization.

Channel/Campaign	Costs	Customers	CAC	Gross margin	LTV	LTV/CAC	acc Profit
Facebook	\$3 000	79	\$38	\$7 929	\$100	\$2,6	\$4 929
FB1	\$3 000	79	\$38	\$7 929	\$100	\$2,6	\$4 929
FB2	\$0	0					
Google Ads	\$4 000	98	\$41	\$13 500	\$370	\$9,0	\$9 500
GA1	\$2 700	76	\$36	\$7 560	\$100	\$2,8	\$4 860
GA2	\$1 300	22	\$59	\$5 940	\$270	\$4,6	\$4 640
GA3	\$0	0					\$0
Snapchat	\$2 000	44	\$45	\$5 115	\$225	\$5,0	\$3 115
S1	\$1 100	23	\$48	\$4 485	\$195	\$4,1	\$3 385
S2	\$900	21	\$43	\$630	\$30	\$0,7	-\$270
Total	\$9 000	221	\$41	\$25 544	\$695	\$17,1	\$17 544

- When we stopped the GA3 campaign we saved you -\$800 loss. The reallocated budget is allowed to bring in more customers and more money. Now Google Ads profit is \$9,500 as compared to \$5,640.
- The Facebook campaign looks different. While we were able to attract 79 customers instead of 53, our profit dropped from \$7,900 to \$4,929.
- The total profit is 5% higher and is now \$17,544. This is good enough, but we can do better!

Now, we will optimize by LTV (and forget the CAC).

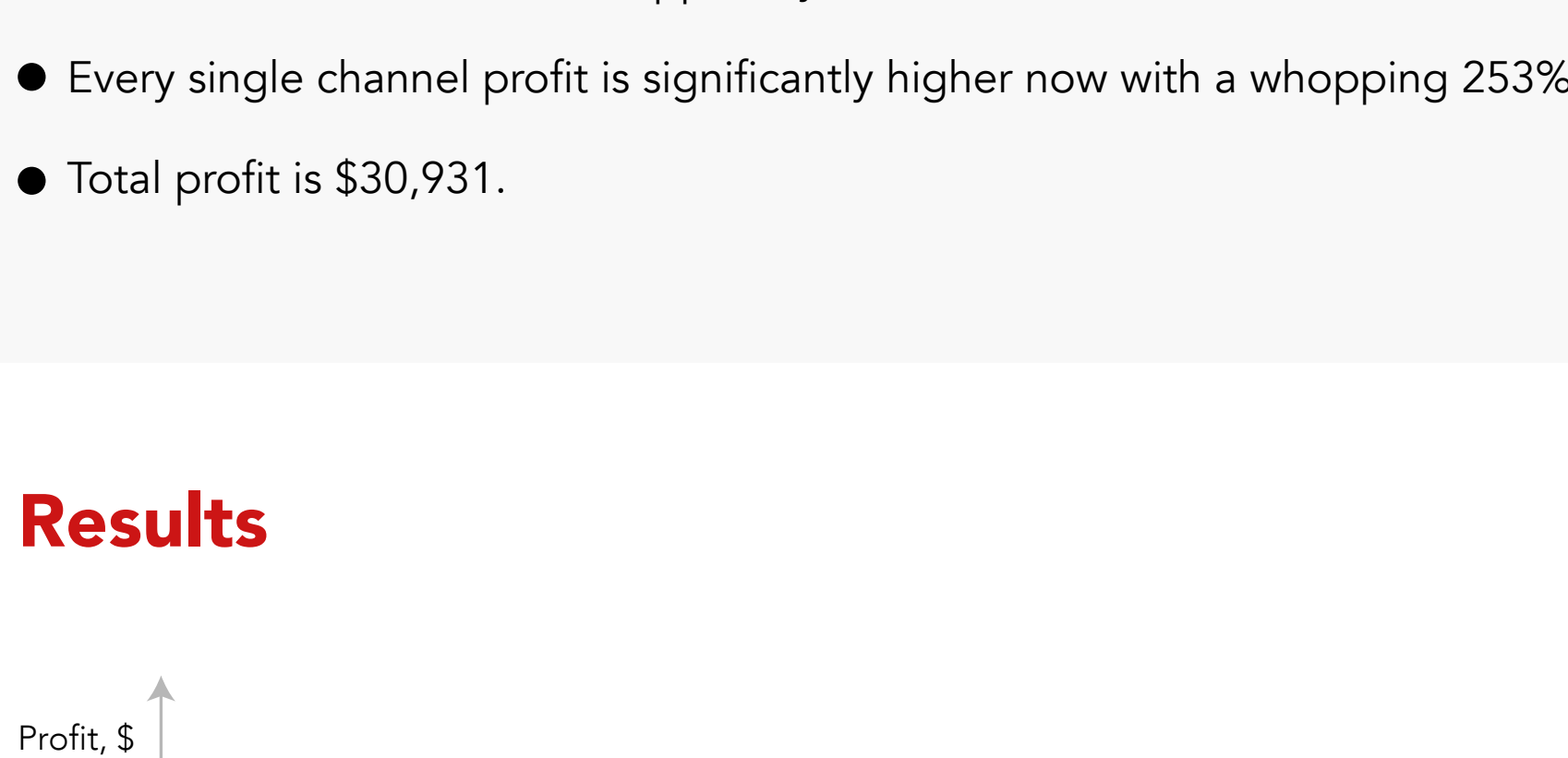
- We will reallocate Facebook budget to FB2 campaign with high-paying customers.
- We will reallocate Google Ads budget to GA2 campaign with the highest LTV/CAC.
- We will stop the losing S2 campaign.

Channel/Campaign	Costs	Customers	CAC	Gross margin	LTV	LTV/CAC	acc Profit
Facebook	\$3 000	30	\$100	\$13 500	\$450	\$4,5	\$10 500
FB1	\$0	0					\$0
FB2	\$3 000	30	\$100	\$13 500	\$450	\$4,5	\$10 500
Google Ads	\$4 000	68	\$59	\$18 277	\$270	\$4,6	\$14 277
GA1	\$0	0					\$0
GA2	\$4 000	68	\$59	\$18 277	\$270	\$4,6	\$14 277
GA3	\$0	0					\$0
Snapchat	\$2 000	42	\$48	\$8 155	\$195	\$4,1	\$6 155
S1	\$2 000	42	\$48	\$8 155	\$195	\$4,1	\$6 155
S2	\$0	0					\$0
Total	\$9 000	140	\$65	\$39 931	\$915	\$14,2	\$30 931

What can you spot?

- CAC went up with an average of \$65. Now we are paying more to attract higher-quality customers.
- The number of customers dropped by 15%.
- Every single channel profit is significantly higher now with a whopping 253% raise
- Total profit is \$30,931.

Results



As you can see the LTV optimization is a very profitable approach to run ad campaigns with a good profit.

And, if you want some help increasing your app revenue AdQuantum will be happy to partner with you for traffic. Take advantage of our know-how and talk to one of our specialists today!