High Performance Marketing
DEMAND METRIC

REFERRAL MARKETING

Acquiring and Retaining Ideal Customer Advocates through Best Practices

A Demand Metric Benchmark Report
June 2016

IN PARTNERSHIP WITH rewardstream

Table of Contents

INTRODUCTION

When a customer refers a friend, peer or acquaintance to a vendor, it's an indication of trust and satisfaction. A customer who refers is essentially putting their reputation at stake, so rarely are referrals made lightly. From the vendor perspective, **referrals are the most coveted type of lead, because they come assuming that a vendor is trustworthy and competent**. Referred customers are a faster path to revenue, and a previous study completed by Demand Metric showed that referral marketing has one of the lowest costs per acquisition.

Surprisingly, many vendor firms allow referrals to occur organically, hoping that they generate enough satisfied customers who will then take the initiative to refer others to the vendors with whom they are pleased. This type of organic referral does occur, but rarely with the frequency to have a noticeable revenue impact. There is benefit for marketers to be more intentional about referral marketing, to blaze a trail that makes referrals more likely and easier to make.

Demand Metric and RewardStream conducted a study to learn about the current state of referral marketing. This follows up on a study completed in the fall of 2014, so this report can now share trend data about the interest in, evolution of and success with referral marketing. This report shares the findings and recommends some best practices based on the data.

EXECUTIVE SUMMARY

This study's participants were primarily marketers in both B2B and B2C organizations. Participants represented a wide range of industry affiliations and are with companies whose total employment ranges from less than 25 to more than 15,000 employees. Responses were collected from those who reported having a referral marketing program and those that did not. For those that did report having a program, the study investigated its parameters and effectiveness. For those that reported not having a referral marketing program, the reasons why were investigated, along with future plans for implementing one.

The analysis of this study's data provides these key findings about the current state of referral marketing:

- ✓ Almost 60% of study participants report having a referral marketing program of some type.

- ✓ Of those that do, only five % have a system in place to support their program.

- ✓ Those with referral marketing programs agree (85%) that they are effective for new customer acquisition.

- ✓ B2B and B2C organizations in this study have similar adoption rate of referral marketing, but B2B organizations enjoy the greatest success with it.

- ✓ For all sizes of companies, almost two-thirds of them report success acquiring, retaining and rewarding customers with their referral programs.

- ✓ Over one-fourth of study participants generate over 30% of their new customers through their referral marketing programs.

- ✓ Over half of study participants are using five or more types of incentives in their programs.

EXECUTIVE SUMMARY

✓ Almost three-fourths of study participants agreed or strongly agreed that referral programs produce profitable customers.

✓ Over 60% of study participants report that referral programs produce the lowest, or one of the lowest cost per customer acquisition compared to other programs.

This report details the results and insights from the analysis of the study data. For more detail on the survey participants, please refer to the Appendix.

THE STATE OF REFERRAL MARKETING

To get an overall perspective on referral marketing effectiveness as a means of acquiring new customers, the study survey asked all participants – whether or not they currently have a program – to indicate their level of agreement with this statement: "*I believe that referral marketing is an excellent method of acquiring new customers*." Figure 1 shows the results from the 2014 and current survey.

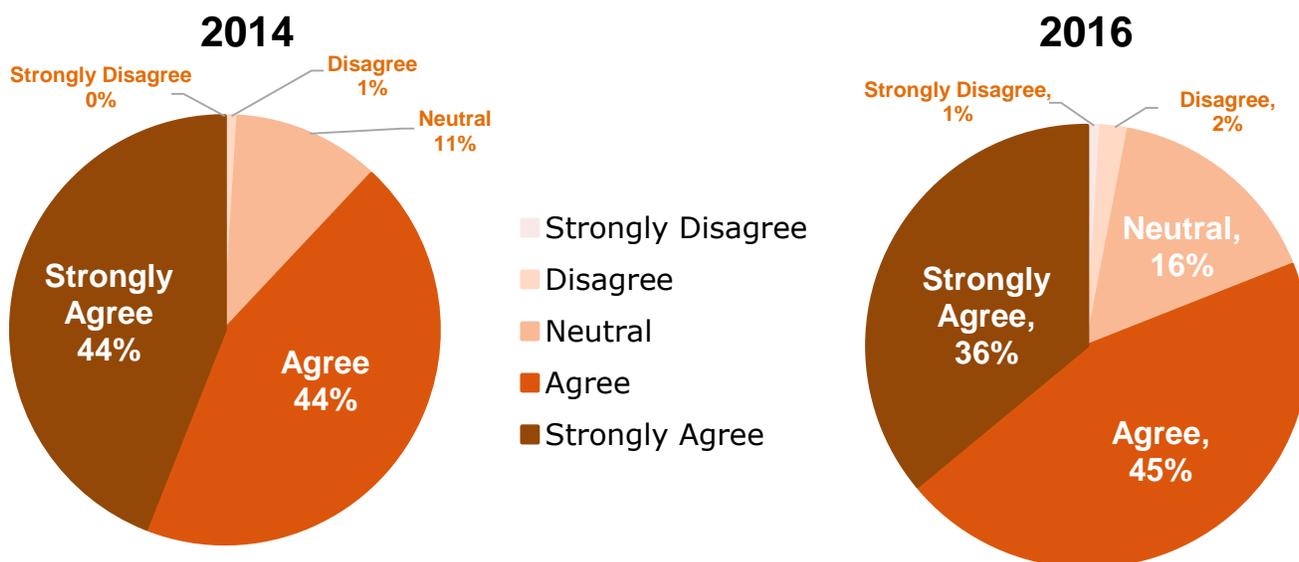## Perception of Referral Marketing Effectiveness for New Customer Acquisition

Figure 1: Agreement about the effectiveness of referral marketing is strong.

Down slightly from 2014, agreement is still strong that referral marketing is effective for new customer acquisition. Those who currently have a referral marketing program are more likely to agree on its effectiveness: 85% agree while 15% are neutral or disagree with the statement above.

THE STATE OF REFERRAL MARKETING

Table 1 shows the existence of referral marketing programs in the companies studied:

	2014	2016
We have no referral marketing program	43%	41%
Referral marketing program exists at some level	57%	59%

Table 1: The presence of some type of referral program is the norm.

Of the study participants with a referral marketing program, half report that their programs were designed and are managed using internal resources, while four percent are using an external marketing or creative agency for program design and management. Almost five percent indicate that they are using a referral marketing solution provider for their programs.

THE STATE OF REFERRAL MARKETING

B2B and B2C organizations in this study were equally likely to have a referral marketing program: 51% and 50%, respectively. Mixed B2B/B2C firms in the study are the most likely to have a program: 62%. However, only five percent of study participants are using a referral marketing solution, as Figure 2 shows.

Status of Referral Marketing Programs

Referral marketing
solution provider in
use, 5%

Other, 4%

Program
designed/managed with
external resources, 4%

No referral
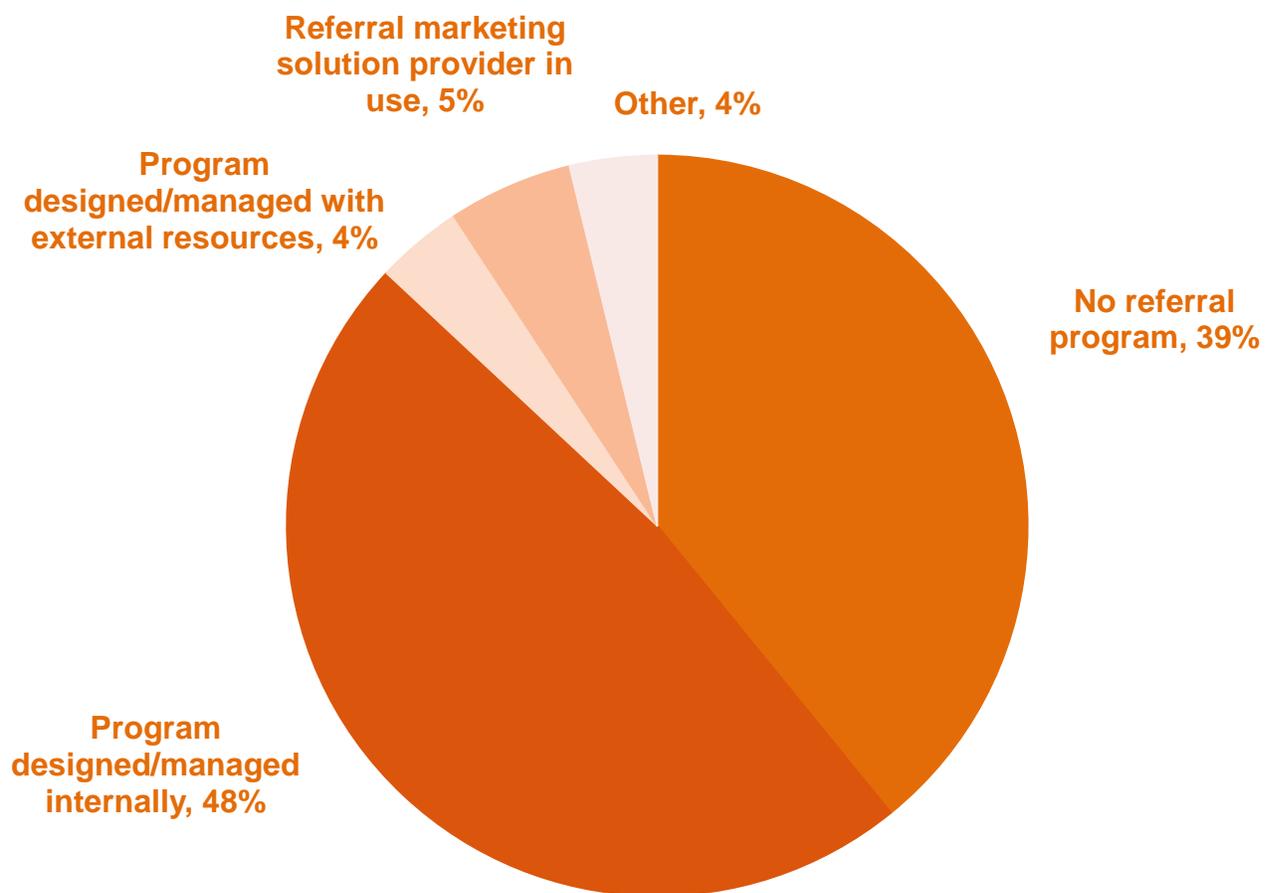program, 39%

Program
designed/managed
internally, 48%

Figure 2: Referral marketing programs are commonly used,
but rarely with a referral marketing system.

REFERRAL MARKETING BENEFITS

Referral marketing programs deliver multiple benefits, and this study asked participants who have a program to rank the benefits they receive in terms of importance. This ranking is shown in Figure 3.

Referral Marketing Benefits Ranked by Importance

Benefit	Percentage
Acquire new customers	88%
Retaining customers	75%
Enhance brand awareness	72%
Reward existing, loyal customers	70%
Gain customer insights	69%
Promote new products via referral	65%
Acquire marketing knowledge	60%

*Figure 3: Acquiring new customers is the most important benefit
of a referral marketing program.*

Referral marketing programs are unusual in their ability to deliver benefits across a number of key areas, as Figure 3 shows. Acquiring new customers is probably most often associated with the purpose and benefit of a program, but retaining and rewarding customers while also enhancing awareness of the brand are also benefits clearly within the utility of referral marketing.

REFERRAL MARKETING BENEFITS

The study further examined these benefit areas, measuring how successful programs are at delivering the benefits that are ranked in Figure 3. The study participants who reported having a referral marketing initiative were asked to rate the success of their programs at acquiring new customers, and Figure 4 shares the performance of this most important benefit.
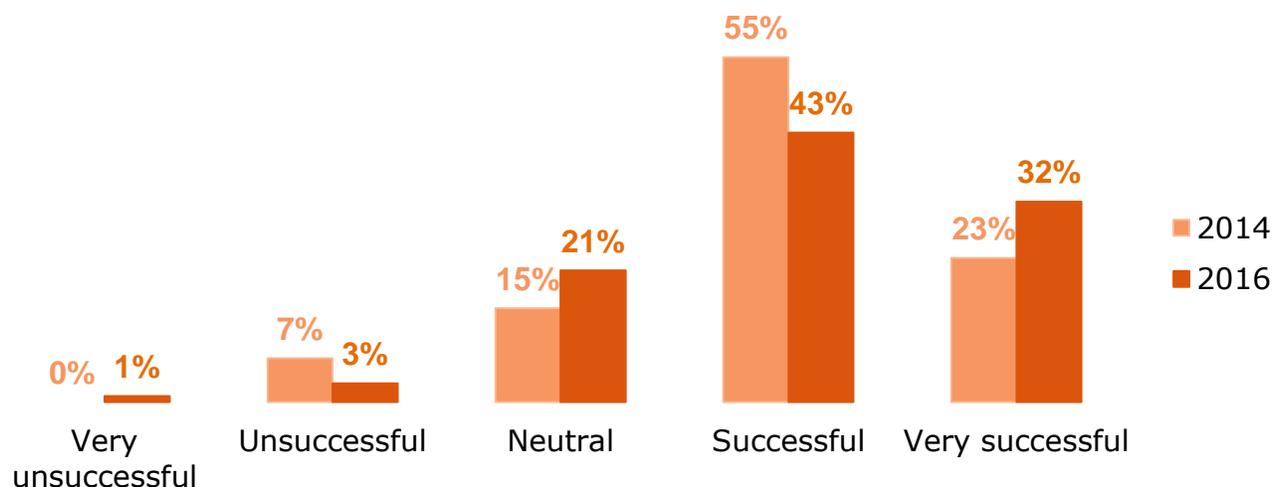
Success Acquiring New Customers

Figure 4: Referral programs have a high rate of success in acquiring new customers.

While the sum of "Successful" and "Very successful" responses differs little in Figure 4 between surveys, there has been movement from the previous study with an almost 10% increase of 2016 study participants reporting their programs were "Very successful."

There are differences in the rate at which different types of companies experience success with the benefits and aspects of referral marketing. Figure 5 summarizes these differences.

High Performance Marketing
DEMAND METRIC

REFERRAL MARKETING BENEFITS
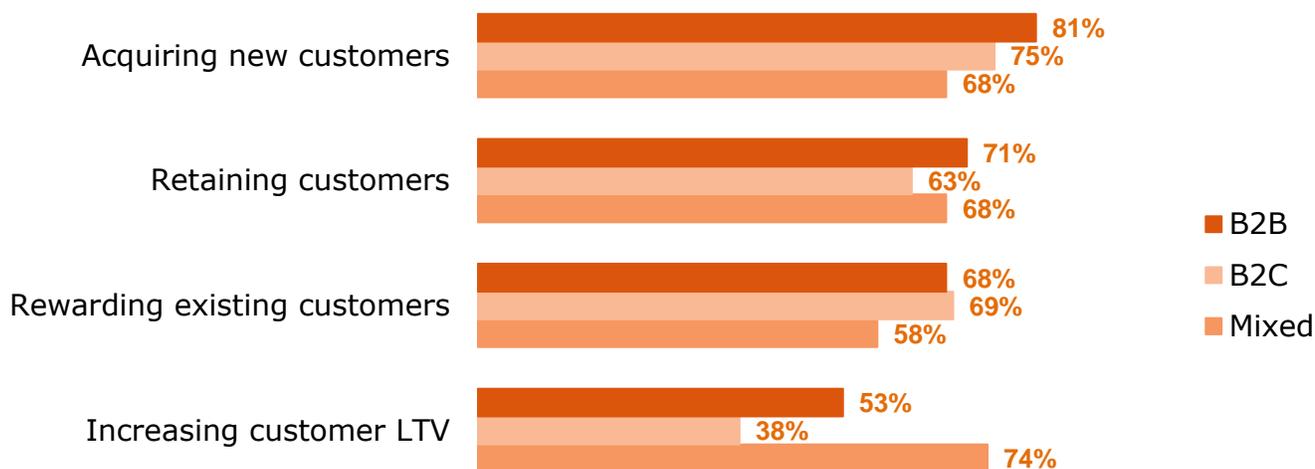
% Success of Referral Programs at:

Figure 5: B2B companies experience the greatest success with all but one of the outcomes listed.

Ironically, B2B organizations that have the lowest adoption rate of referral marketing programs consistently report the greatest success achieving most of the outcomes shown in Figure 5. The margins are most significant for acquiring new customers, where B2B organizations typically have the advantage of a personal relationship with their clients, something many B2C organizations don't enjoy.

Most curious in Figure 5 is the success of the mixed B2B/B2C segment at increasing customer Lifetime Value (LTV) at 74%, far in excess of either the B2B or the B2C segments. This difference begs more research that is outside the scope of this study, but a possible explanation emerges from the data: analyzing program results. There is a correlation between the outcomes shown in Figure 5 and retention. The mixed B2B/B2C segment reports the highest level of agreement with the statement "our referral program helps us retain customers," and the relationship between retention and LTV is well known. Furthermore, 37% of the mixed segment report that they never or rarely have a challenge in analyzing their program results. For B2B and B2C segments, just 19 and six percent respectively report never or rarely having this challenge. The mixed segment, by virtue of better program analysis, is seeing greater program performance in the area of customer LTV.

REFERRAL MARKETING BENEFITS

The success of referral marketing based on company size was studied, and headcount was used to segment company size. Table 2 summarizes the comparisons key referral program outcomes by company size.

Reported Success Rate At:	Small (100 of fewer employees)	Medium (101 to 1,000 employees)	Large (1,000+ employees)
Acquiring new customers	77%	**81%**	67%
Retaining customers	66%	65%	**83**%
Rewarding existing customers	60%	65%	**83%**
Increasing customer LTV	49%	**65%**	50%

Table 2: The bold numbers represent the highest reported success rate.

While medium and large companies report the greatest levels of success with different aspects of their referral marketing programs, **for all company sizes, almost two-thirds or more are successfully acquiring, retaining and rewarding customers with their programs**. Where referral programs exist, the study survey measured the percentage of new customers attributable to these programs, and Figure 6 displays this results.

REFERRAL MARKETING BENEFITS

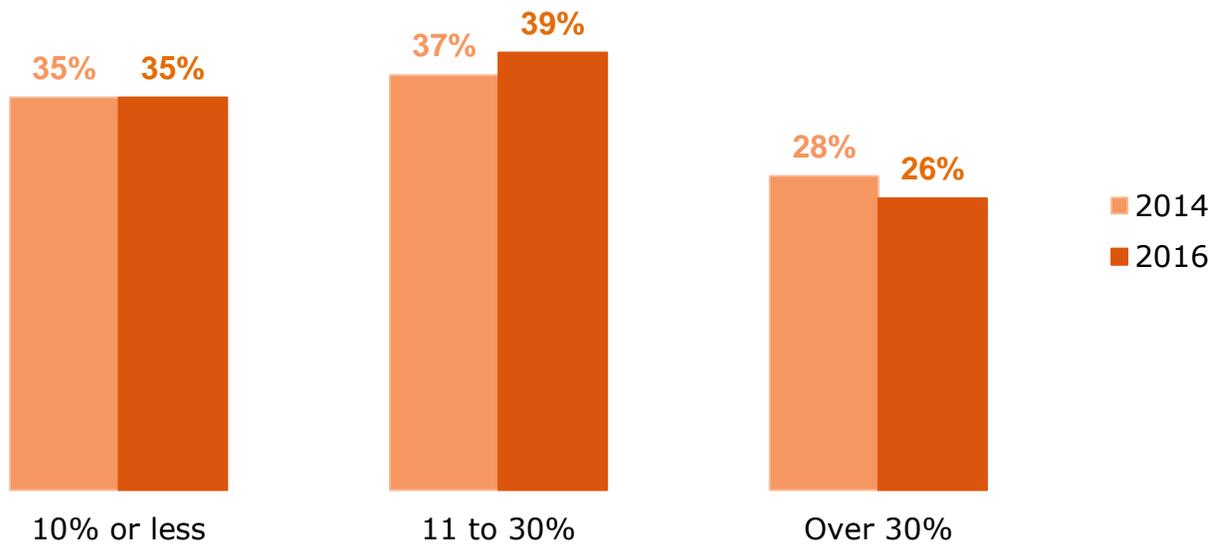## Percentage of New Customers Coming via Referral Programs

Figure 6: The performance of referral programs in generating new customers remains steady between survey periods.

Over one-fourth of study participants have referral programs that generate over 30% of their new customers. **Marketers that view referrals as simply incremental or "bonus" revenue must revise their view based on the data**. Referral marketing is clearly capable of generating significant volumes of new customers.

METHODS OF ACQUIRING NEW CUSTOMERS

Referral Marketing is one of many methods that companies use to acquire new customers. What other methods are in use, and how do they compare in terms of effectiveness? The study survey asked all participants – regardless of whether they had a Referral Marketing program – to indicate which methods are in use and to rate their effectiveness. Table 3 compares the top five methods in terms of usage and effectiveness.

Method	Usage		Effectiveness	
	Rank	% in Use	Rank	% in Use
Email	1st	98%	2nd	67%
Social Media	2nd	93%	5th	56%
Events	3rd	92%	1st	68%
Digital Advertising	4th	90%	4th	63%
Referral Programs	**5th**	86%	**3rd**	66%

Table 3: Usage and effectiveness rankings are not parallel.

Compared to the previous study, all methods shown in Table 1 are at higher levels in the current study, except for social media, which ranks last in this list of effective ways to acquire new customers. From last year, email has also taken over the top usage spot from social media.

As was the case in the previous study, referral programs rank 5th in usage. **However, the three most effective methods are virtually tied – events, email and referral programs –in these rankings**. Effectiveness should ideally drive methods usage, but many organizations don't track the effectiveness metrics that allow them to know how their initiatives truly perform.

REWARDING EXISTING CUSTOMERS

This study has shown that a high percentage of those organizations with a referral marketing program consider it a success at acquiring new customers (Figure 4). With referral marketing, the opportunity also exists to reward existing customers who become advocates, and Figure 7 shows that the participant organizations with programs report even greater success with this outcome since the last survey, and some brands are leveraging this strategy for retention and loyalty.
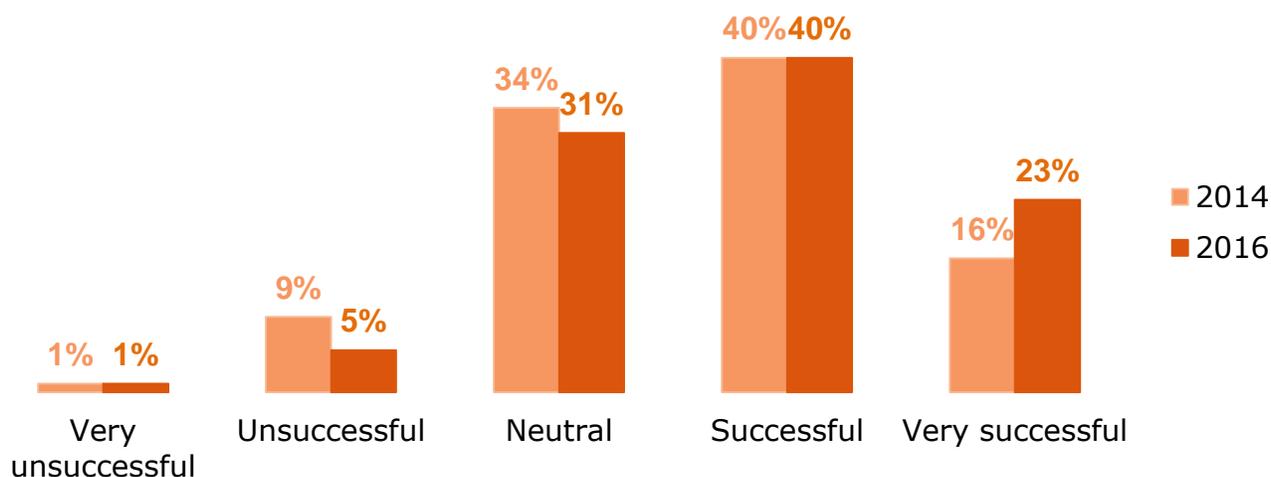
Success Rewarding Existing Customers

Figure 7: 63% of study participants rate rewarding existing customers a success.

Success in rewarding existing customers is 12% lower than success acquiring new customers (Figure 4). While still out of balance, there is greater parity in the measurements in the current survey. **Marketers that use referral programs must keep in mind the relationship between acquiring new and rewarding existing customers: the former depends on the latter. Investments in rewarding existing customers for their advocacy will provide a return in the form of new customer acquisition**. Figure 8 summarizes who is rewarded through referral marketing programs.

High Performance Marketing
DEMAND METRIC

REWARDING EXISTING CUSTOMERS
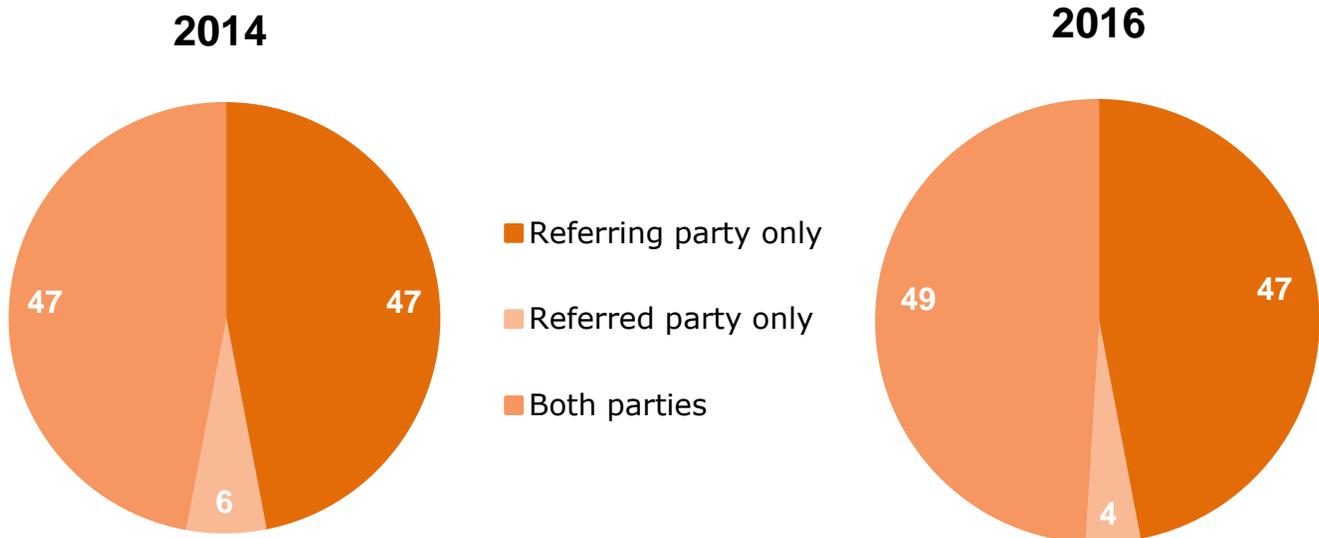
Who is Rewarded?

2014

2016

Figure 8: Referral reward strategies are virtually unchanged.

The current study took a more nuanced view of the strategy to reward both parties, which is in use by 49% of study participants. Data was collected to determine how the reward is allocated, and over two-thirds shared that they reward both parties equally.

As expected the "both parties" reward strategy produced much greater success at rewarding existing customers, compared to rewarding only the referring party. While the study didn't provide the reasons for the difference, logic can. Existing customers are rewarded in both strategies, but since they are referring those with whom they have some relationship, it's natural to expect referrers to feel some satisfaction for referral activity. They receive acknowledgement from the vendor through the program, and they also receive the gratitude of the referred party for helping them address a need. For this reason, an important part of the referral process is closing the communication loop with the referring party to ensure they know of their involvement in helping the vendor acquire a new and satisfied customer.

REWARDING EXISTING CUSTOMERS

What incentives are organizations with referral marketing programs using? Figure 9 summarizes the study's inquiry on this matter.

Referral Marketing Program Incentives

* New incentive category added in the current survey.

***Figure 9: Account credit and free merchandise are the top
referral marketing program incentives.***

The 2016 study survey expanded the list of incentive compared to the previous study, and that probably accounts for the lower response percentages for each incentive listed in Figure 6. More than half of the referral marketing programs in this study offer account credit, free gifts/merchandise, eGiftcards or entry into a prize drawing for a high-value item. eGiftcards provide an digital reward that is instantly fulfilled and available for immediate use. This characteristic has the psychological advantage of closely tying the advocacy action to the reward itself.

REWARDING EXISTING CUSTOMERS

Some comments provided by survey participants describing the "Other incentives" in use:

- ✓ Cash
- ✓ Co-marketing funds
- ✓ Software updates
- ✓ Travel
- ✓ Additional months of service

It is the norm to use multiple types of incentives with referral programs. Slightly less than one-fourth of study participants use just a single type of incentive. Over half are using five or more of the incentive types shown in Figure 9.

As important as knowing which incentives are in use is knowing which are most effective. Figure 10 ranks the top five incentive types based on the effectiveness ratings study participants gave them.

Incentive Ranking (% Effective)

1. Account Credit	39%
2. eGift Card	34%
3. Prepaid Visa/Mastercard gift card	29%
4. Free gifts/Merchandise	27%
5. Discount E-coupons	25%

Figure 10: The incentives that participants rate as most effective.

It is of note that the effectiveness rankings in Figure 9 do not match-up entirely with the usage data shown in Figure 9. For example, prepaid Visa/MasterCard gift cards rank sixth in usage but third in effectiveness.

High Performance Marketing
DEMAND METRIC

REFERRAL PROGRAM PERFORMANCE

The results of this study have already proven the effectiveness of referral marketing programs in acquiring new customers and rewarding existing ones. What are the characteristics of the new customers produced by referral marketing? The study asked participants to provide input across four important dimensions of customer relationships: profitability, loyalty, satisfaction and advocacy. Figure 11 shows the results of this analysis.

Customer Types Produced by Referral Marketing Programs
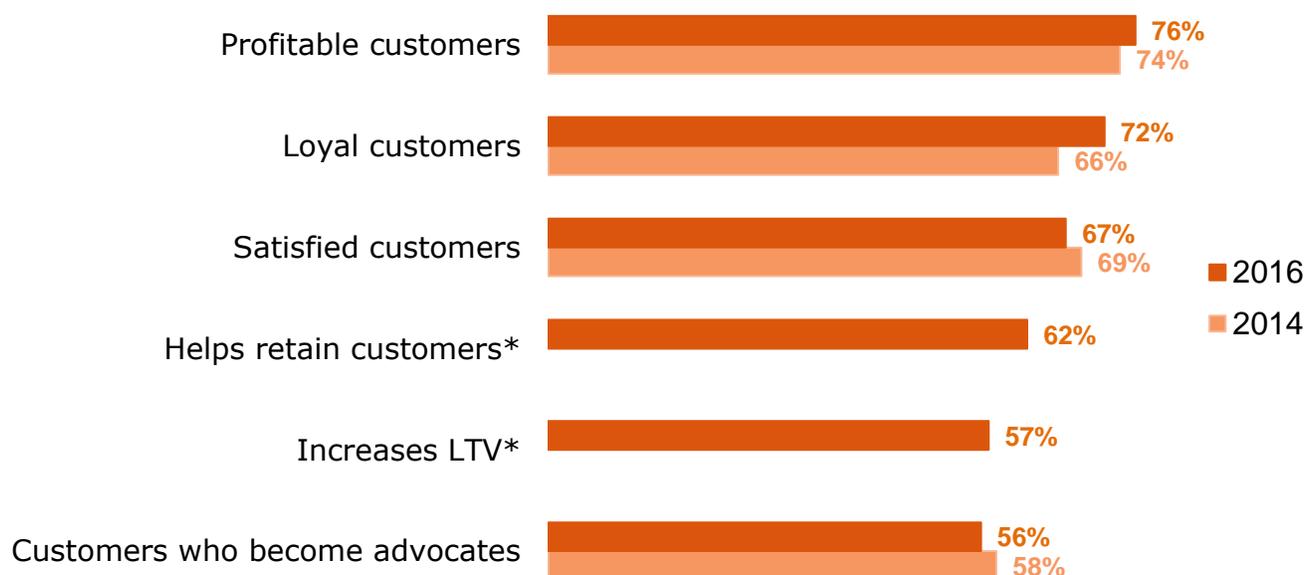

Figure 11: Referral marketing programs are producing customers with highly desirable attributes, leading with profitability.

Almost three-fourths of this study's participants agreed or strongly agreed that referral marketing programs produce profitable customers. While each of the attributes listed in Figure 11 are highly desirable, profitability heads the list for most organizations. What this data infers is that **customers acquired through referral have the potential to become more valuable – loyal, profitable and satisfied – than customers acquired through other means**.

REFERRAL PROGRAM PERFORMANCE

In this study, B2B organizations enjoy the impacts on customers shown in Figure 11 at a higher rate than their B2B counterparts, or those organizations representing a blend of B2B and B2C. Table 4 shows the percentage of respondents who agree that their referral programs produce the customer outcomes shown in Figure 11.

Agreement that our referral program:	B2B	B2C	Mixed
Produces profitable customers	87%	63%	68%
Produces loyal customers	84%	63%	68%
Produces satisfied customers	86%	56%	63%
Helps retain customers	72%	50%	74%
Increases customer LTV	69%	50%	63%
Produces customer advocates	82%	50%	68%

Table 4: Referral program outcomes by business type.

At least half of all business types agree that they get outcomes from a referral program that are shown in Table 4, but B2B organizations are positioned most advantageously to experience them.

The cost to acquire a new customer is a key marketing metric, and marketers are increasingly using Cost Per Acquisition (CPA) to measure their acquisition efforts. CPA isn't the only metric a marketer should track, but it is important for understanding if customer acquisition is occurring affordably. It is conceivable that the strategy that produces the most profitable customers is also the least affordable one. Figure 12 shows how study participants rate the CPA of referral marketing programs compared to other things they are doing.

REFERRAL PROGRAM PERFORMANCE

Relative Cost Per Acquisition of Referral Marketing Programs

2014

2016

- Highest CPA compared to other programs
- Slightly higher CPA than other programs
- CPA is equal to other programs
- Among the lowest CPA of all programs
- Lowest CPA of all programs

2014 pie chart: 2%, 8%, 19%, 32%, 39%

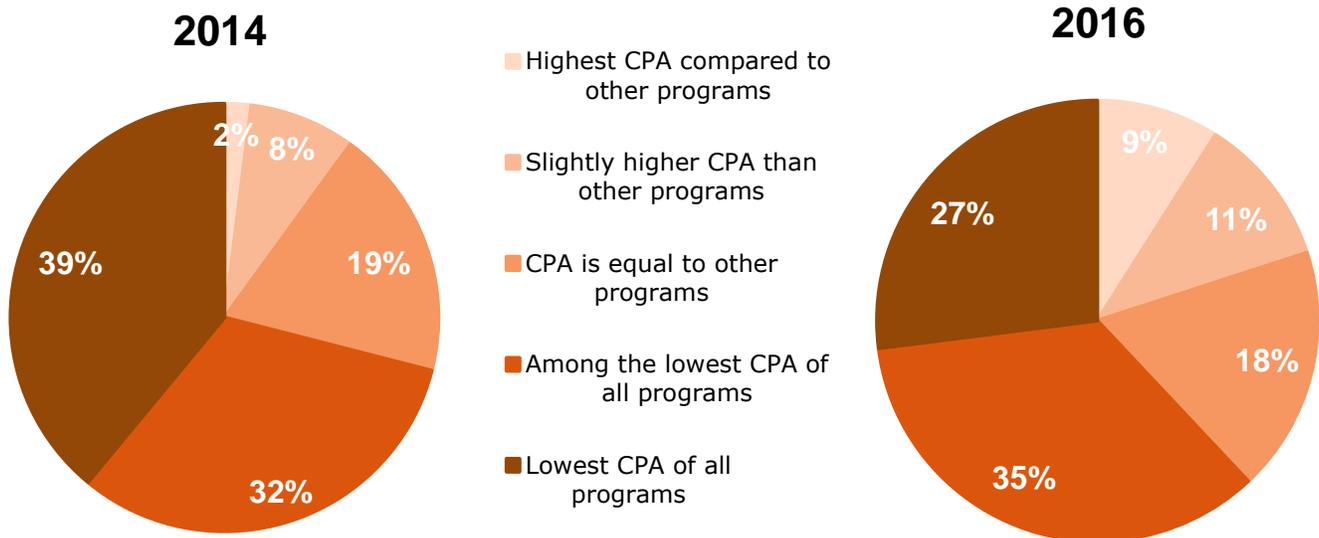*2016 pie chart:* 9%, 11%, 18%, 35%, 27%

Figure 12: Over 60% of study participants report that referral marketing programs are the lowest or among the lowest in Cost Per Acquisition compared to other programs.

Figure 11 reveals that referral marketing programs produce profitable, loyal customers. Now Figure 12 adds that the associated CPA is among the lowest compared to other types of programs. **This combination of profitability and low CPA that referral programs deliver is ideal for marketers and the organizations they serve.**

REFERRAL MARKETING CHALLENGES

Any marketing initiative will have challenges associated with achieving the desired results, and referral marketing is no exception. The study inventoried these challenges and presents a year-to-year comparison of them in Figure 13.
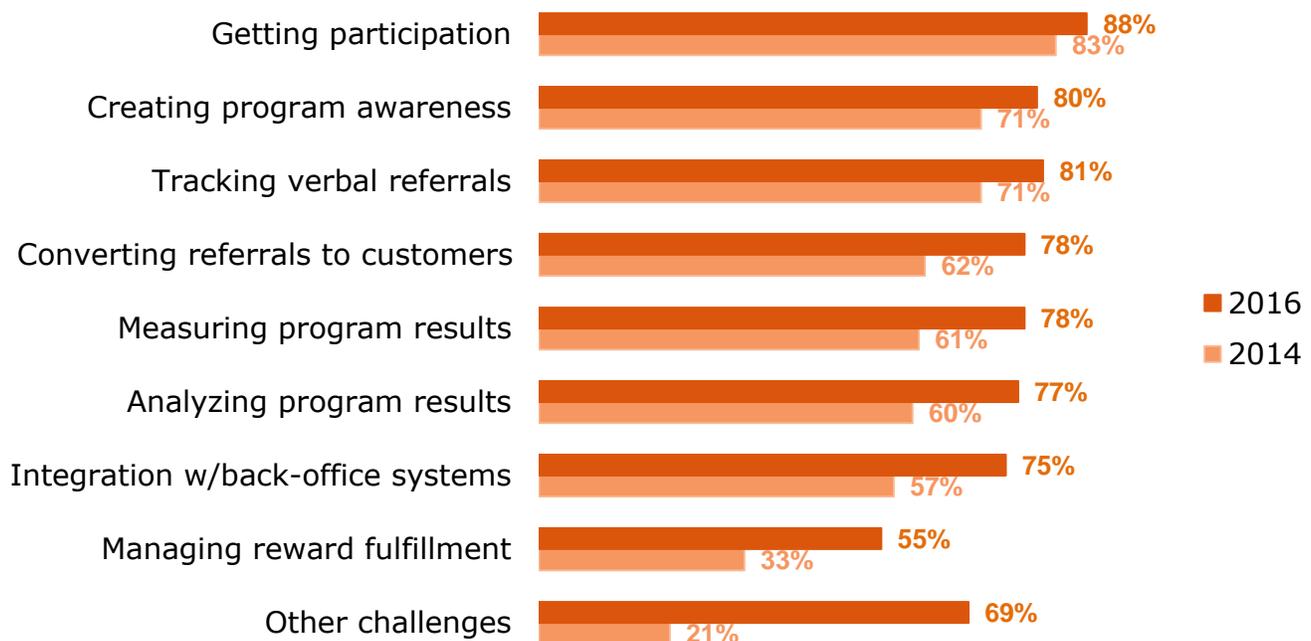
Referral Marketing Program Challenges

Figure 13: Getting participation in referral programs remains the greatest challenge.

The challenges associated with referral marketing have increased across the board in this most recent study.   The year-to-year increases in those reporting these challenges are in double-digits for each challenge except "getting participation" and "creating program awareness."   It's clear that most organizations have some challenges with their referral marketing programs, however, most of the referral programs in this study were designed and managed with internal resources.   It is therefore very likely that three of these challenges – measuring program results, analyzing program results and integration with back-office systems for tracking reward redemptions – are a greater challenge than for organizations using automated commercial solutions.

REFERRAL MARKETING CHALLENGES

The study shows that a majority of programs are managed manually in house, and manual programs are harder to manage than automated systems. **The value of automation is program simplification through elimination of manual and time-consuming processes.**

Survey participants offered a few write-in comments regarding the challenges they experience with their referral marketing efforts:

- ✓ "Making it easy to become involved."

- ✓ "Verifying how customers are made aware of our brand."

- ✓ "Coming up with a training program and incentive program so this becomes part of the sales routine."

These comments suggest that **many of the challenges of referral marketing are mitigated through simplicity: a program that is simple to understand, participate in, manage and administer**.

BARRIERS TO PROGRAM IMPLEMENTATION

Just over 40% of study participants do not have a referral marketing program (see Table 1), and those participants were asked to share their barriers to implementing a program. Figure 14 summarizes the reasons given in the current and past study.

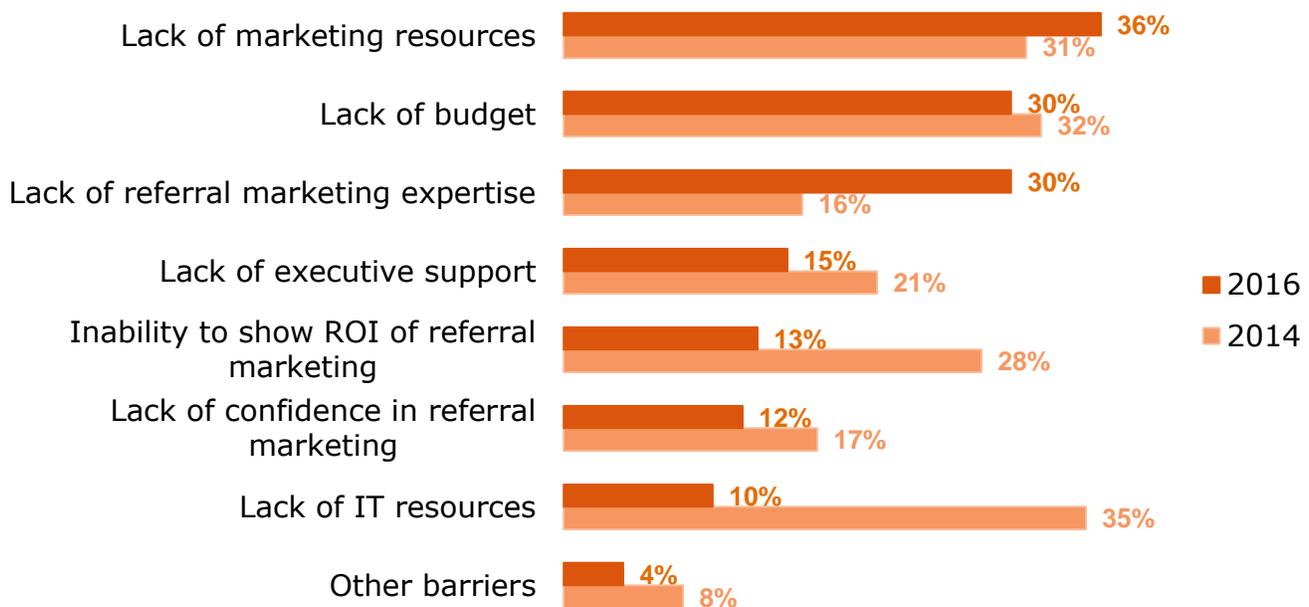## Greatest Barriers to Launching a Referral Program

Figure 14: There are big changes in the two surveys for barriers to launching a referral program.

The biggest barrier in the previous survey – a lack of IT resources – has dropped dramatically as a barrier. The previous study report speculated that the IT barrier was a perception and not a real issue. This current study data seems to validate that assumption, as study participants have concluded that technology barriers to referral marketing are minimal.

In the previous study, three of the barriers shown in Figure 13 were experienced by more than 30% of the study participants, but now there is only one: a lack of marketing resources.

BARRIERS TO PROGRAM IMPLEMENTATION

It seems clear that the barriers to implementing a program are falling, and for those that don't yet have a program, their biggest barrier is that is simply isn't a priority. Marketers are very smart about doing things that work or produce the best result. Given the data in Figures 11 and 12 about the profitability of referred customers, and their low CPA, ignorance of these advantages surfaces as the most likely reason marketers aren't being more intentional about referral marketing.

Of these study participants that do not currently have a referral program, half intend to launch one in the future, and of this group, 19% say they plan to by the end of 2016, as Figure 15 shows.
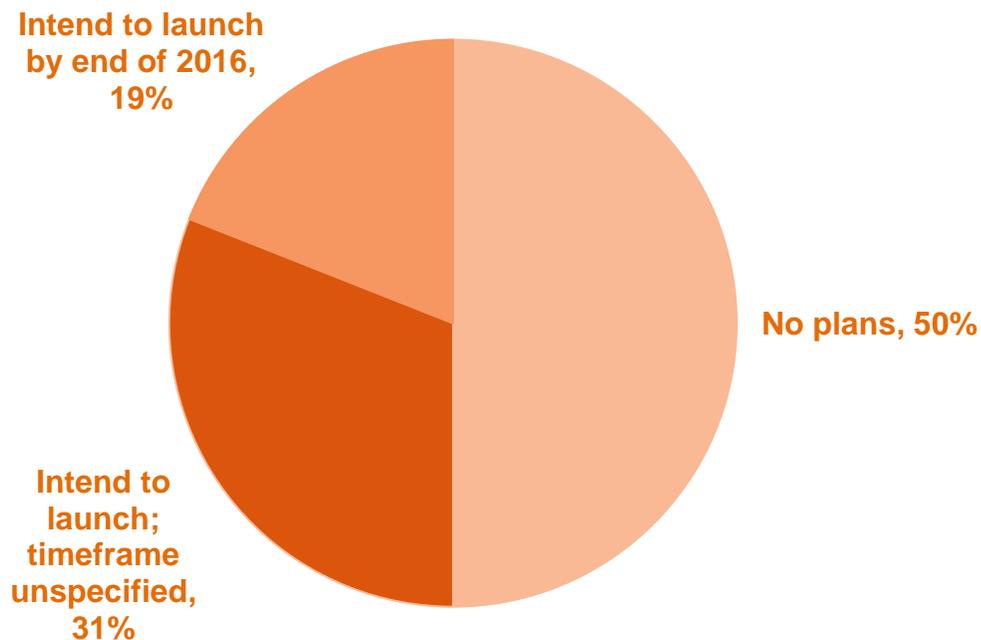
Plans to Launch a Referral Program

Figure 15: Half of survey participants that do not currently have a referral program plan to launch one.

ANALYST BOTTOM LINE

There are few marketing initiatives that deliver so such a broad set of customer outcomes that are critical to business success: profitable customers who are loyal, satisfied and easily retained. Referral programs are one such initiative. When a company is able to create these kinds of customer outcomes – through any campaigns or programs – it will experience an increase in customer lifetime value. The ability to improve LTV is a sure path to greater, sometimes much greater, profitability.

The previous and current referral marketing studies both show that referral marketing programs have two highly coveted performance characteristics. First, they acquire ideal customers at a low CPA, and then, they help the organization retain those customers.   The financial benefits of improving customer retention are well documented, but often overlooked.   Arthur Middleton Hughes of the Database Marketing Institute estimates[1]that the profit impact of greater retention falls within a range between 17% and 23%.

The benefits of referral marketing are so compelling that it is difficult to imagine why an organization wouldn't have one. The reality of a marketer's existence, however, is that there are more things to do than there is time or resources to do them. Still, these study results show that referral marketing deserves a place at the top of the priority list. Companies that plan to implement or enhance referral marketing should keep these things in mind:

✓ **Measure and analyze the results**. No marketing or sales professional will argue with the merits of having a referral marketing program. That doesn't mean, however, that they run on autopilot and need no performance metrics. This study shows that marketer who analyze their referral program performance data are getting greater results in the area of increasing customer LTV.

---

[1] http://www.dbmarketing.com/articles/Art154.htm

ANALYST BOTTOM LINE

- ✓ **Think "big."** Marketers that view referral activity and the business that results from it as incremental or "bonus" revenue have the wrong view. The study data shows that referral marketing programs are capable of generating significant numbers of new customers (Figure 6), and marketers should build their programs around that expectation.

- ✓ **Use what works, not what's familiar**. Table 3 shows how study participants rated and ranked various means of acquiring new customers. Referral programs rank third in effectiveness, but fifth in usage. Marketers must trust the data and use approaches based on what works, not what they know best.

- ✓ **Incent well**. The incentives used with referral programs must have appeal to the party earning the reward. Companies who practice referral marketing must study the beneficiaries of their programs to ensure the incentives are effective (Figure 10), not simply what is easy for the company to provide.

- ✓ **Market your program**. The benefits of referral programs are so obvious to the marketers that administer them, it seems as if they should market themselves. But this is not the case. Getting participation in referral programs remains the top challenge (Figure 13), so marketers must invest some of their marketing savvy and resources to promoting their own referral programs.

The existence of customer advocates is the best form of validation a company can have. A good referral program may take time to mature, but as it does, the momentum it develops grows and becomes a powerful force of attraction. Referrals can happen naturally, without any intervention. But companies that intentionally manage the referral process by providing a clear, smooth and simple path for them to occur will accelerate the realization of benefits. For most organizations, this simply requires commitment, or as one study participant share, "Make referral marketing more of a priority."

ACKNOWLEDGEMENTS

Demand Metric is grateful to RewardStream for sponsoring this benchmarking study and for those participants that took the time to provide their input to it.

About RewardStream

RewardStream is the foremost authority on referral marketing, combining an innovative blend of marketing insight and proprietary technology to design and manage referral programs for some of the world's most prestigious brands. The company was founded in 1999, operates in 39 counties globally and processes more than 20 million referrals. For more information, please visit www.rewardstream.com.

About Demand Metric

Demand Metric is a marketing research and advisory firm serving a membership community of over 80,000 marketing professionals and consultants in 75 countries.

Offering consulting methodologies, advisory services, and 500+ premium marketing tools and templates, Demand Metric resources and expertise help the marketing community plan more efficiently and effectively, answer the difficult questions about their work with authority and conviction and complete marketing projects more quickly and with greater confidence, boosting the respect of the marketing team and making it easier to justify resources the team needs to succeed.

To learn more about Demand Metric, please visit: www.demandmetric.com.

APPENDIX: SURVEY BACKGROUND

This Demand Metric Referral Marketing Benchmark Study survey was administered online during the period of January 19, 2016 through March 24, 2016. During this period, 214 responses were collected, 192 of which were complete enough for inclusion in the analysis. The representativeness of these results depends on the similarity of the sample to environments in which this survey data is used for comparison or guidance.

Summarized below is the basic categorization data collected about respondents to enable filtering and analysis of the data:

Type of organization:

- Primarily B2B   55 percent
- Primarily B2C   23 percent
- Mixed B2B/B2C   22 percent

Primary role of respondent

- President, CEO or owner   20 percent
- Marketing   62 percent
- Sales   7 percent
- Other   11 percent

Number of employees:

- 25 or fewer   34 percent
- 26 to 100   23 percent
- 101 to 500   21 percent
- 501 to 1,000   8 percent
- Over 1,000   14 percent

APPENDIX: SURVEY BACKGROUND

Number of customers, members or subscribers served:

- 1,000 or fewer   41 percent
- 1,001 to 5,000   23 percent
- 5,001 to 50,000   17 percent
- More than 50,000   19 percent