Steering the Sales Force Away From the ‘Easy Sale’

Build an effective sales force by redirecting its energy toward value maximization.

By Marwaan Karame

Discussions about increasing sales force effectiveness happen a lot these days. They usually result in ideas to help salespeople generate more revenue. However, not every dollar of revenue is created equal. Misguided efforts to sell unprofitable products and services to customers destroy rather than create value.

So, building a highly effective sales force begins by ensuring the team is strategically and effectively selling the right products and services to the right customers.

To make this point more precise, we calculated the ratio of 2021 year-end total enterprise value to 2021 revenue for the S&P 500. This cumulative “value-to-sales” ratio varied widely. The top-quartile companies had a median value-to-sales of 13.4x, compared with 1.4x for the bottom quartile.

Within one company, there may be businesses, product lines, or even individual products that would be in the top quartile while others in the bottom quartile. Similarly, some customers or customer groups buy in ways that create a lot more value. So, just motivating the sales team to drive sales, without guiding them toward selling the most valuable products to the most desirable customers, is woefully misguided.

Driving Profit

Value is created when resources, including a sales force's time and energy, are invested in activities that generate more profit than an alternative investment of similar risk. This is commonly known as economic profit.

Understanding which products and services, as well as customers, create the greatest economic profit provides a blueprint for deploying the most effective salespeople. It also helps determine which channels drive the most economic profit for each product and customer segment.

For a salesperson, decisions on where to focus time and energy are simple. Predictably, the salesperson often focuses on what is "easy" to sell. As a result, management berates him or her for being ineffective and neglecting to sell the tougher-to-move products or services. Before management draws such conclusions, however, they should take a hard look at what makes the sale "easy" or "hard" in the first place.

The ineffectiveness may not be a sales issue. Instead, it could be a pricing or product offering problem. Processes can also contribute to poor sales performance. Or perhaps the cost to sell directly to specific customer segments is too high.

The easy products to sell or customers to serve may necessitate more inventory or demand longer payment terms. They might monopolize more capital resources than they reasonably should, resulting in less economic profit. Assessing the economic profitability of products sold and the customers served reveals operating and capital efficiency opportunities. Doing so makes each revenue dollar more profitable and makes the sales force more effective at creating value.

Redirecting and incentivizing a sales force's energy toward value maximization requires two critical factors that strongly align with the mandate to maximize value. These two factors in incentive design make what's beneficial for the company and investors also beneficial for salespeople and their families: (1) the methodology for setting sales quotas or targets and (2) the weighting of commission rates by product and customer segment.

Commissions and Sales Targets

Gross profit margin (gross profit divided by revenue) is often used to rank products and customers; yet, in reality, that measure is only a small part of the value equation. Management needs to consider the total cost to serve — not only the cost of goods sold but also operating expenses and the opportunity cost of the capital investment. Developing a matrix of economic profit by both products and customers provides an objective lens and fact-base to establish commission rates weighted toward selling more profitable products. The information also provides the foundation to set the minimum sales targets required to generate the return investors expect.

Roughly speaking, if we know the expected profit margins, capital invested, and the required return (e.g., cost of capital), then we can solve for the minimum revenue growth necessary to create value.

For example, assume a company's current revenue is $2 billion and investors require a 10% return on invested capital (ROIC). If new investment is $100 million, the company would need to generate an incremental profit of $10 million (10% required return multiplied by $100 million of incremental investment). Further, assume the expected profit margin is 20%. The company needs to grow revenue by a minimum of $50 million ($10 million profit divided by 20% profit margin) or 2.5% revenue growth ($50 million of new revenue divided by existing revenue of $2 billion).

Evidence-Based Sales Goals

This method of calculating revenue targets offers an objective starting point for sales goal setting at the corporate level. The goals can then be allocated toward business units or sales territories. Management can also use such an analysis as a check against "bottom-up" sales targets to determine if they are reasonable. Having an objective, evidence-based methodology for setting sales targets goes a long way to motivating the sales organization to grow revenue. Salespeople put their efforts toward selling rather than expending unnecessary energy questioning and negotiating sales quotas.

CFOs are uniquely positioned to broaden the concept of sales force effectiveness. They can move the sales organization away from a narrow and tactical focus on "how to sell effectively" to a profoundly strategic view of where to "effectively allocate sales resources" to create the most value.

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