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Profit-Focused Selling

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Jonathan Byrnes relates the story of a General Manager's five-year program to increase sales force productivity and dramatically enhance company profitability.

by Jonathan Byrnes

Part VII

The General Manager of a paper and janitorial supply distributor in the southern U.S. wrote to me recently. "We have sliced our numbers as you described and found the 80-20 rule throughout. We then segmented/stratified our customers to be handled by different sales methods (outside sales, inside sales, and customer service). Our results are significant (i.e., gross profit per order has increased 82 percent in the last four years). Also, our net profit will be up over 50 percent over three years ago. I want to take our business to the next level, and I would be willing to share our experiences with you."

I receive e-mails with success stories of profitability management from many readers, and I'd like to encourage you to send a note to me telling me about your experiences. I called the General Manager, and here's his story.

The General Manager's story

About seven years ago, the GM took charge of a successful seventy-year-old distribution company. The company sells its products to a variety of customers including universities, manu-facturers, healthcare providers, and food processors. The sales force averaged twenty years of experience.

Five years ago, the GM started looking for ways to improve profitability. Over a five-year period, he instituted an insightful process that increased sales force productivity and dramatically enhanced company profitability. The process reflects the three key elements of profitability management, profit map, profit levers, and profit management process, that I described in Part I of this series.

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Profit map

The GM began by working with his IT manager to develop a set of spreadsheets to analyze account profitability. To calculate account profitability, they started with account gross profit, and subtracted (1) sales expense, and (2) operating cost. (They divided total company operating cost by total number of company orders, and allocated the resulting cost per order to accounts according to the number of orders each account generated.) This gave them a rough estimate of operating profit per account and per order.

They then clustered the accounts by sales rep, and ranked the accounts in descending order by operating profit per order. When they showed the results to the reps, the typical reaction was that the data had to be wrong because "my top account is second from the bottom." If a rep contested the data for an account, they jointly looked up the details and reviewed the calculations. In all, only 30 of 2,400 account calculations needed adjusting.

Profit levers

The GM saw that one of the key profitability drivers was the operating profit per order. At the time, each order was taken by a sales rep during a visit to the customer. Because the visit was costly, each order had to generate a minimum amount of gross profit in order to cover the cost of the visit and related costs. (I think of this as the "gross margin to windshield time" ratio.) In light of this, the GM developed several initiatives to increase profitability.

In the first initiative, the GM reduced the account load for each sales rep from 240 to 56 customers. The objective was to force the reps to get deeper penetration in the highest-potential accounts. The GM saw that the reps had to learn to get past the purchasing managers and form better relationships with the key decision makers in the accounts. To accomplish this, he created an account profile template that the reps could use to develop a more systematic understanding of their accounts.

In the account profiling process, the rep identified the decision makers, competitors, and cus-tomer strategy, and devised an account-penetration strategy. Developing the profiles required that the reps interview their customers. The reps were surprised to find that the customers liked talking about themselves and about the competitors, and even volunteered their view of competi-tor weaknesses and ways that the company could generate more business.

Several reps commented to the GM that the customers thought that the company was better than even the reps thought. This went a long way in developing the reps' confidence in the new strategy of focusing on deep penetration of key accounts. The GM also instituted team sales calls, in which several key company operating managers (Distribution Manager, IT Manager, Finance Manager) would walk through the customer facility and suggest ways for the customer to reduce cost. (This parallels the actions of the national trucking company I described in Part II.)

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In his second initiative, the GM developed appropriate sales channels for the smaller, "B" and "C" accounts. Initially, all of the accounts that were below a certain operating profit threshold were designated house accounts, and were serviced through an inside customer service group.

This year, the GM started a middle-market inside sales group, focused on the 600 to 750 midsize accounts. This group combines inside sales with occasional face-to-face meetings.

The GM's third initiative focused on customer education. The reps told the smaller customers that in order for the company to service them, they had to provide a minimum number of orders of a certain size. Many customers elected to change their purchasing process and order patterns in order to continue the relationship with the company.

Profit Management Process

The GM changed the sales compensation system to ensure that the new profit management process was successfully instituted on a day-to-day basis. Under the new system, direct sales reps' compensation had three components: (1) 45 percent of the compensation was salary; (2) 35 percent was based on commissions; and (3) 20 percent was composed of a bonus based on growth in gross profit per order over the previous year. Moreover, the GM instituted a minimum order size to qualify for a commission.

In all, the GM considered the profitability management program a great success. He said, "The key is to show the numbers to the employees, and explain the logic to the customers."

The GM's pervasive focus on raising operating profit per order had stunning results. The number of lines per order increased by 33 percent, the operating profit per order increased by over 80 percent, and the company's net profits soared by over 50 percent!

You are what you sell

Your sales force is like the front-wheel drive of a car: it pulls you through the marketplace. Regardless of your plans and intentions, your company is what it sells.

What then do you sell? To answer this question, just look at your sales compensation system. In most companies, the sales force is rewarded for bringing in revenues, occasionally for units of product, but rarely for profitability. Yet all revenue dollars are not equally profitable. This is the essence of the problem—and the opportunity!

The GM in the General Manager's story increased his company's profitability by over 50 percent, without capital investment, by shifting from revenue-focused selling to profit-focused selling. He did this in three ways.

First, the GM identified the highest-potential accounts, and tightly focused his direct sales resources on these accounts. I remember the President of a successful company saying to me in frustration, "My salesmen are like bumblebees, bouncing from flower to flower." By reducing the account span of the direct sales reps, the

GM forced them to focus all their energy on pene-trating and broadening their relationships with the best customers. This secured the company's key sources of profitability.

Second, the GM created a multi-tiered selling system. In this system, the best accounts re-ceive intensive direct-sales attention, the middle-market accounts receive a blend of inside sales plus occasional visits, and the small accounts are served by inside sales customer service reps. (Distributors have an important role—more on this in a future column.) In doing this, not only did the GM focus his direct sales force on the highest-potential accounts, but also he matched the cost of the selling resource to the margins generated by the accounts.

The GM instituted a powerful profit-focused selling system that drove up penetration in the highest-potential accounts and turned bad accounts into good accounts.

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In essence, if the gross margin of an order, or transaction line, is less than the cost of selling and servicing the order, it will be unprofitable. By developing a multi-tiered selling system, the GM reduced the sales expense relative to gross margin for the "B" and "C" accounts. Not only does this system increase account profitability, but importantly, it can also better meet customer needs: if your company supplies a relatively small proportion of a customer's overall purchases, the customer often will prefer a crisp, effective inside sales relationship to prolonged direct sales visits.

The effect of multi-tiered selling is analogous and complementary to the effect of selecting appropriate customer service intervals and the effect of managing product flow (order patterns) that I wrote about in Part V and Part VI. All three of these profit levers lower either the sales expense or service cost relative to the gross margin of an order. This is why multi-tiered selling, like customer service interval selection and product flow management, is an essential lever to improve the profitability of your existing business. And all three are management measures that can very rapidly improve profitability without the need for capital investment.

Of course, developing customer operating partnerships with your best accounts, as I described in Part IV, is the most powerful form of multi-tiered selling, and the 30 percent to 40 percent sales increases that result testify to its effectiveness.

Third, the GM took several measures to increase the operating profit of orders by inducing the customers to consolidate their orders. He drove the sales force to accomplish this by develop-ing the new sales compensation system and complementing it with an extensive customer educa-tion program.

Through these three measures, the GM instituted a powerful profit-focused selling system that drove up penetration in the highest-potential accounts and turned bad accounts into good accounts.

By the way, if a company is what it sells, what is YOUR COMPANY? The answer should be: as profitable as possible because our profit-focused selling is driving us right through the sweet spot of the market!

See you next month.

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