PRIVATE EQUITY PERFORMANCE IMPROVEMENT

SHOW ME THE MONEY, BUT THE RIGHT MONEY PLEASE!

PART 2: WHAT IS MY SALES FORCE DOING?

ALVAREZ & MARSAL

LEADERSHIP. ACTION. RESULTS.℠

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In Part I of our series, we discussed how understanding cost-to-serve as well as creating transparency around margins and the market are foundational. This informs new product development, pricing, selling process (the "company way"), and sales organization structure to create an effective commercial strategy that drives profitable growth.

In Part II of our series, we examine how the sales force is sized, structured, and deployed to uncover and capture profitable growth opportunities. When looking at the overall performance of the sales organization, the most obvious metrics measure how much the organization costs relative to the revenue, revenue growth, and margin that it brings in. The most telling metric is margin when using a cost-to-serve-driven net margin as discussed in Part I of this series. Whether the overall selling cost is too high relative to returns or could simply be better allocated to a more efficient sales model, understanding true returns on sales effort by channel enables decisions that improve the ability of the sales organization to deliver more profitable growth.

A&M COMMERCIAL EXCELLENCE APPROACH

A&M's strength in execution drives a differentiated commercial excellence approach, divided into six key areas

We identify and drive end-to-end cross-functional change for sustainable EBITDA growth

Market Intelligence/ Commercial Due Diligence
Understand market trends, competitive dynamics, growth opportunities, and customer and end-user behavior and purchasing decisions

External Lens

Product Portfolio Optimization
Ensure the product portfolio and new product pipeline maximize profit opportunity

Price Optimization
Ensure that costs to serve are recovered and pricing captures maximum value

Sales Force and Market Coverage
Understand the market drivers, how to differentiate by segment/channel to optimize the sales organization design

Segmentation and Channel Optimization
Optimize the size and structure of the sales force and ensure it is properly incented to grow profitable business

Sales Operations & Customer Success
Ensure leads are efficiently generated and converted into profitable sales, and sales is held accountable to KPIs and metrics

Margin Transparency and Recovery
Determine where money is actually being made at the customer, market, Channel, category, and SKU level by unpeeling margins and cost-to-serve

Digital Enablement
Customer experience value acceleration, digital growth marketing, optimization, and loyalty, intelligent commerce, product innovation

IMPACT OF COMMERCIAL EXCELLENCE:

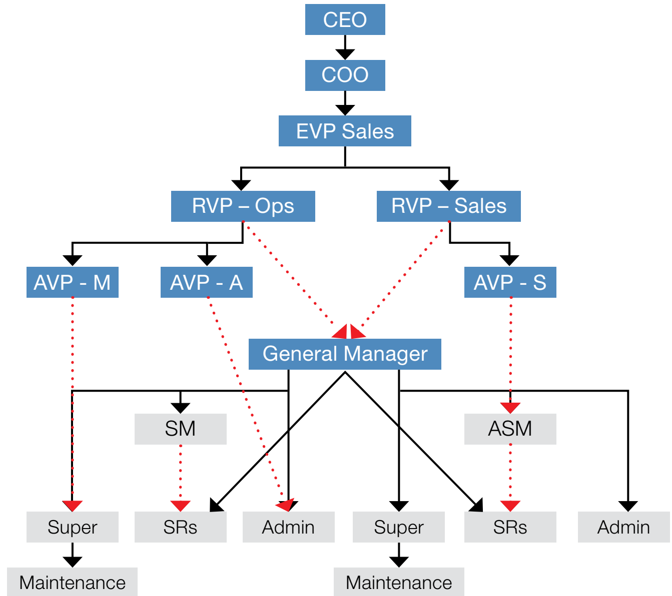
- **Performance Improvement Plan:** Identified, quantified, and prioritized opportunities to improve performance and cost structure
- **Execution Roadmap:** Action plan to execute on the restructuring, e.g., finalization of detailed structure, selection, seperation, etc.
- **Cost to Serve Model:** Repeatable tool for clients giving visibility into customer, SKU, and product category profitability

SELLING COSTS – HOW DOES YOUR ORGANIZATION COMPARE TO OTHER SALES DEPARTMENTS?

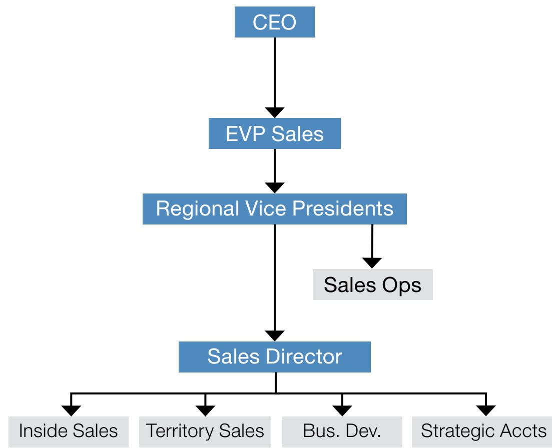
In many cases, a clean sheet approach to organizational restructuring is necessary to properly size the sales force dedicated to declining revenue/profitability streams. Take this opportunity to compare your sales organization to others in adjacent industries. Pay close attention to the span-of-control (number of direct reports per manager) and the number of management layers. Many legacy organizations are very complex, coming from years of mergers, acquisitions, and organization changes that have added resources without a clear return on investment. Departmental layers add complexity and costs and make it difficult to run a tight ship.

It is best to create an unbiased picture of your talent by cross-functionally soliciting feedback on key personnel to get a true depiction of a salesperson's value to the organization. Document your results by using a tool, such as a 9-Box Talent Assessment, to support your decisions and ensure your choices are accurate and equitable. A word of warning, there are sales reps in every organization that may seem valuable on paper (i.e. outperforming their plan) but are not pulling their weight and contribute negatively to company culture. Historically, you will find that at least one veteran sales rep exceeding his/her plan will fall into this category in every sales organization, so spend time analyzing the performers just as rigorously as the underperformers.

As you reset the organization, this is a perfect time to analyze the “hunters” and “farmers” in your organization. With many legacy sales organizations, farming existing customer account becomes the norm and hunting for new business is less of a focus. The risk is that a customer-oriented organization begins to see a loss of share, especially when executing a price increase strategy. When segmenting the sales team, remember that there is a vast difference in skill sets between a customer account manager (farmer) versus a new customer acquisition salesperson (hunter). They are simply wired differently, and it is a mistake to try to turn a farmer into a hunter or vice versa.



Existing Org Structure
Unclear, dotted line reporting structure with excessive organizational layers and duplicative roles.



Revised Operating Model
Delayered organization with clear, linear reporting structure and well-defined roles/titles.

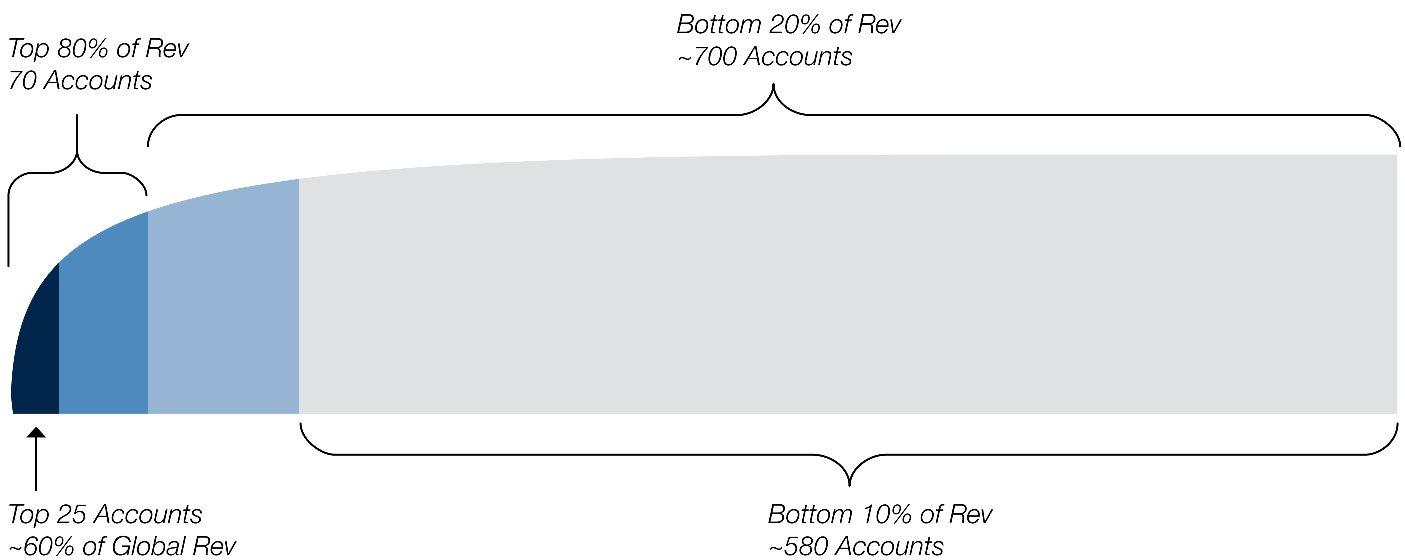
Consider the psychological impact of a reorganization on your commercial team. It sends a clear message that the company will not accept mediocrity, and everyone is accountable for moving the needle on profitability. In most cases, the retained employees are reenergized and will take on a leadership role to help with the performance improvement agenda. Changing how the team operates day-to-day is just as important as the reorganization itself.

Tip: Span-of-control and management layers should be reviewed prior to any headcount reduction. In many cases, sales departments become “management heavy” with too many layers, which impede effective decision making. A good rule of thumb for span-of-control ratio is an average of 1-7 for a B2B sales organization. In a recent project, a client’s span-of-control was an average of 1-2 and the sales org was restructured reducing run rate sales cost by $17.5 million (29 percent reduction) and improving span-of-control to 1-7 while reducing two management layers from a total of 7 to 5.

THE 80/20 CUSTOMER RULE: DO YOU ALIGN YOUR CHANNELS TO MAXIMIZE PROFITABILITY?

As we have discussed, maintaining an outside sales team is often an expensive proposition. Building a cost-to-serve model will often highlight the 80/20 rule (80 percent of your revenue comes from 20 percent of your customers). We then suggest refocusing the outside team on the customers generating 80 percent of revenue and standing up an inside sales team or indirect team to handle the likely less profitable “tail” customers that comprise the remaining 20 percent of revenue. Then, ask the question: “Does your customer find value in face-to-face meetings?” This is not a suggestion to replace all outside sales reps with an inside sales team but to match the right resource to the right customer segments, which will not only reduce cost but improve customer satisfaction in the process.

A high-cost, face-to-face model may be misaligned with the support a customer requires. Consider the risk of paying a premium for outside sales reps (high salary, bonus, commission) for simply managing an account that is not part of your strategy. Outside sales reps typically concentrate on a small percentage of large customers while leaving the smaller accounts for a rainy day. In this scenario, most of your customer base goes untouched and becomes disenchanted with the declining level of service. An inside rep or indirect channel will improve consistency in contacting this customer segment and you may see a rise in profitable revenue with a clear reduction in cost-to-serve.



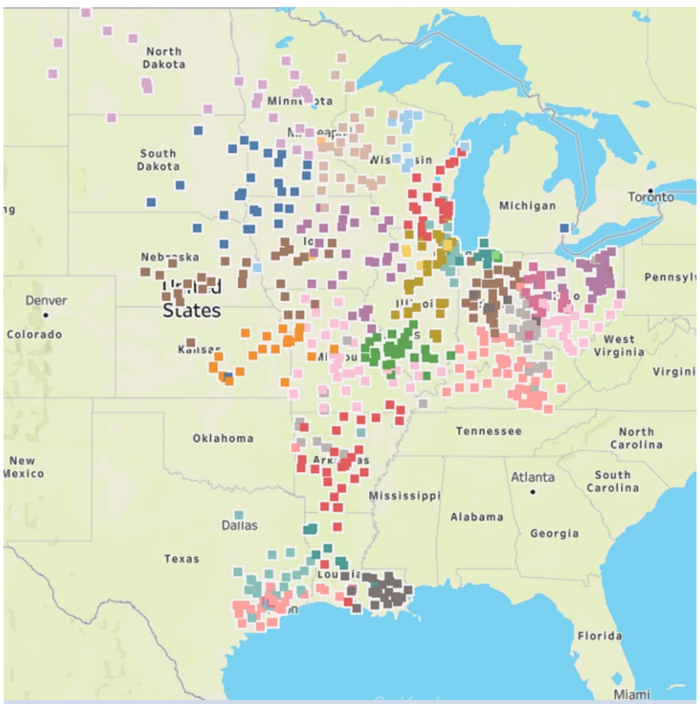
Case in point: On several recent projects, we interviewed 32 divisional vice presidents of sales with 74 percent of study participants reporting a shift from a field sales model to an inside sales model due to changing customer buying habits. But be cautious and take the necessary time to analyze your go-to-market strategy and document the type of support your customer needs before changing your ratio of sales personnel as to not interrupt your top-line revenue.

Tip: Challenge the traditional 80/20 paradigm by engaging the bottom percentage of your customers with an inside digital strategy, transforming them from declining revenue sources to new drivers of growth. To verify the 80/20 rule, utilize the data in your customer relationship management (CRM) system or consider sending a survey to your customer base asking how many visits they received last calendar year from their sales rep, and whether a monthly call from an inside rep would add value. Then reassign those underserved customers to an inside resource.

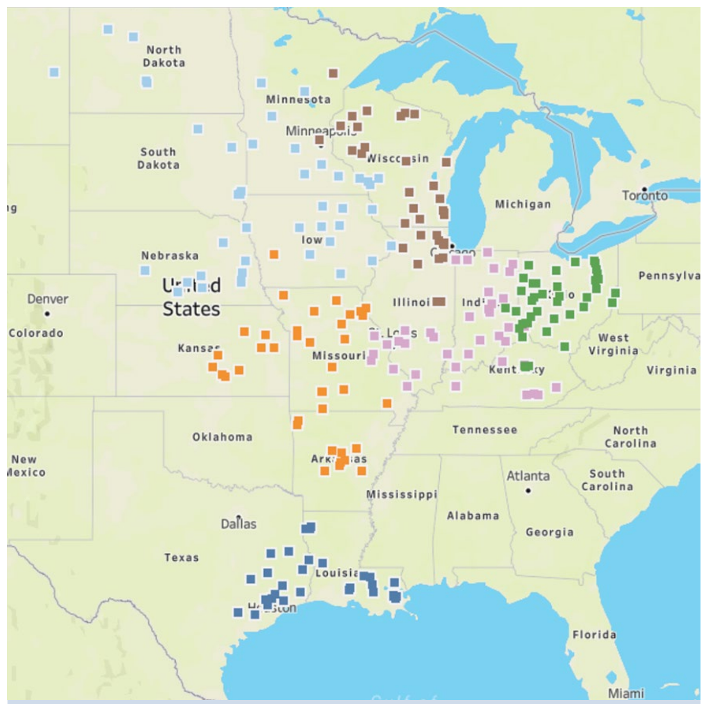
MARKET COVERAGE AND TERRITORY PLANNING: WHEN WAS THE LAST TIME YOU REVIEWED YOUR SALES TERRITORY LOADING?

Analyzing your coverage model and your sales territories will provide insight on where you can reduce cost and better align resources to drive profitable growth. In many sales organizations, customer territories are believed to be hallowed and can remain constant for years with reps believing that they own the rights to certain customers. This passive approach leads to unnatural territory lines created to preserve relationships, adding additional travel costs with little return.

For example, you may find legacy territories that were formed years prior due to special circumstances (e.g. key relationships, rep turnover, tenure) and never unwound or revisited. In one client instance, a territory rep who lived in Boston managed a territory in Florida due to its assignment after a sales rep's termination. He was instructed by his manager to work the state for a few months until he could hire a replacement. Unfortunately, a few months turned into three years. This special arrangement resulted in a significant drop in revenue and profitability for the Florida territory due to a manager's unwillingness to make the right decision and hire local talent or reload the coverage model.



Existing Territories
High overlap between territories, resulting in high T&E costs and limited customer interaction.



Realigned Territories
Optimal territory loading with clear geographic boundaries. Tail customers in high cost-to-serve areas moved from outside to inside sales coverage.

Tip: Stress test territory account assignments annually to confirm that they are aligned with rep/managers location to increase productivity and to improve the customer experience. This practice, if done correctly, will unlock new sales as well as reduce travel expenses.

CHANGE MANAGEMENT AND WHY SALES FORCE EFFECTIVENESS MATTERS

As with any significant transformation, the change management aspect of reshaping the commercial organization needs to be carefully orchestrated and requires a combination of strong leadership, analytics, and a rigorous business cadence. Successful commercial leaders can manage all revenue generating functions including sales, but also marketing, product, pricing, customer service, compensation and recruiting.

Portfolio companies are moving away from individuals with narrow sales experience, and towards experienced commercial leaders (who have experience running all aspects of a business and who can develop a scalable organization that achieves sustainable, profitable growth). This new breed usually has years of sales management experience in companies selling large portfolios across multiple industries and geographies, but also have managed P&Ls requiring deep operational experience. They have worked closely with the CIO/CTO to ensure that key information is shared and utilized, with the CFO to monitor profitability, and with the CEO to implement growth targets and a rigorous business rhythm.

An example: Kraft Heinz recently announced the position of a Chief Growth Officer to focus efforts on profitable growth with a clear mandate to sort out the “winners” and “losers” in their portfolio of existing and new products.

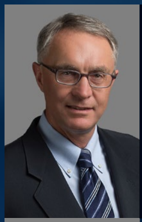
A word of caution, in any change management process there are likely going to be passive resistors. Staff that believe they know all the answers are quick to say, “we’ve tried this before,” and can kill any chance for improved performance by acting as “company historians” leveraging their relationships with customers to hold back change.

In a recent project, a sales leader refused to deliver a price increase to a legacy customer, where he had a long-term relationship, even though the profit margins showed negative profitability to the organization. The sales leader was removed, the price increase was implemented, and a year later the customer became profitable and has grown in revenue. Shying away from addressing these issues early in the change management process will derail any chance for sustainable change that produces results.

The optimal path will depend on the current state culture that is present in the organization and the available levers such as incentives, systems and tools, and organization structure.

In Part III of our series, we look at the sales management function within the organization and the importance of aligning incentives, systems, tools, and sales leadership to drive accountability and profitable growth.

KEY CONTACTS



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