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Sales forecasting - Pipeline

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Abstract

This article is a logical continuation of the first article published in "IES-2008 - Internet Education Science", page 282. In this article we provide a "recipe of earning money". The underlying parts of the selling process can be analyzed, divided into a selling cycle and weighted in order to get a pipeline which follows logical sales process from start till end. After applying the appropriate sales methodologies, a company can predict future sales and thus increase earnings.

Introduction

Last week a large shipping company came with the correction to their expected earnings for 2012 for approximately milliard Danish kroner. A considerable amount in itself, however compared to the expected earnings of 18 milliard a relatively small adjustment of 2,7%. Two hours later the company has lost more than 35 milliard of their total market value on the Exchange. This shipping company is not the only one, almost every day we can see large reputable public companies coming with "profit warnings", after which they are promptly punished. It's quite remarkable when you see how much money and resources there are often invested in prognosis tools. The question is: why cannot they get it right? The general answer is that it is difficult to predict the future. There are many parameters which play in and their influence differs from a company to a company. In return the companies which manage it, save lots of money. And often it's the basic things which go wrong in the company hierarchy. In this article we will describe some of the basic methodic which help predict a sale. The problem formulation in this article is limited to B2B market.

Processes "Recipe of Earning Money"

Majority of the companies earn money. Often they achieve it by doing the same day after day. Thus, there are some underlying processes which form basis for their profit. The latter can range from being very simple to being very complex. If they are not described, a company will often have difficulty copying relatively simple processes to for example another market. Certain and often very successful companies know exactly how their processes are set up. McDonalds, Starbucks, Coca Cola etc. to name a few, but there are rare. The recipe for making money is unfortunately often hidden in the heads of a few key persons who maybe don't even know that they are the ones with the "recipe". If one or two of such persons are removed, the consequences can be disastrous. There are many such examples in the history. An example at hand could be Apple where it is interesting to follow whether they can continue development now that Steve Jobs is gone. They have tried it once before, and last time Steve Jobs was forced to leave Apple the company almost went bankrupt, so if any they should be prepared.

Sales Processes And Sales Methodology

An important part of a "recipe for making money" is the sales process. Sales process is the process which describes how to sell a product, i.e. from market influence to lead generation to the first order. There is no need to reinvent the wheel when it comes to the sales processes. The majority of the ways to sell a product are already described in such books as "Solution selling"[1], "Strategic selling"[2], "Spin Selling"[3] etc. The art here is to choose the methodology which is the closest to your own reality. "Strategic selling" is thus appropriate when a customer is responsible for a great part of your turnover - 20% . "Solution selling" is good for less complex IT projects and thus all these methodologies have a starting point which you have to understand before you choose the one you want to use in your own company. There are many advantages in using an already developed sales methodology. You receive a common reference frame in your company which means that you all speak the same language and thus understand and consider things in the same way both in the management and in the operational level. If you don't have such common understanding, it is basically impossible to prognosticate sales. Unfortunately there are very many companies which do not have such common understanding.

Sales Processes And Statistics

Statistics is used to estimate future sales. There are various accelerators you have to identify and pay attention to. These can again differ from a company to a company, and below we have a few examples.

Sales Meetings

Many orders require a physical visit by a salesman before a customer actually submits an order. Purchase of a new economy system normally falls into such a category. There are probably very few companies which will buy a new economy system over the phone without prior meeting with the supplier representative. An accelerator here would thus be number of sales meetings, in other words this or these parameters which you can influence yourself and which influence the sales development.

There would be a relationship between the number of sales and orders. Let's imagine that you receive 10 orders out of 100 sales meetings. The relationship would thus be 1:10. This number would typically be rather stable when the number of sales is scaled. There can be salesmen who qualitatively deviate because of some reason, but generally speaking the relationship would be the same and will only change slightly over time. This way on the list of 100 held sales meetings you cannot see who the coming ten customers would be before all the sales cycles are concluded, but you know that with the great probability it will end up with 10 out of 100 on the list. This relationship can be used in the sales estimation.

This relationship can be shown in the Pipeline graph, see fig. 1.

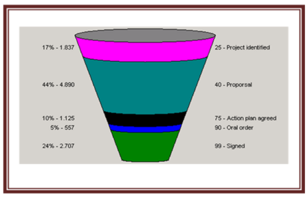

Fig 1 - Pipeline

Another factor that would normally distribute is the sales cycle's length. Some customers make a decision relatively quickly, and some use significantly more time but again – you can fairly quickly get an average sales cycle length which can be used as a standard to estimate when an order can be expected. On the aggregated level it will function well.

Early Warnings

If a sales cycle is say 180 days, there are many sales managers who do not want to wait +180 days to ascertain that the sale didn't go as planned. Therefore it is a good idea to use "Early Warnings" which can be used to weight the pipeline (a pipeline here is the aggregated number of sales cases in progress). This can be done by defining some exact sales milestones. You can then measure relationship of how many sales cases have passed the milestone seen in relation to the number of orders which were generated at the end. Thus if out of 100 cases 25 become an order, you can use the weight 25% on the aggregated level to measure your pipeline as in fig.1 where there are many levels and each level illustrates a sales milestone, in other words a precisely defined place where the sales cases are placed.

Normally a pipeline is built to follow a logical sales process from start till end. Here again the sales methodologies give a great value as they can describe the logical order in which things should be done. A simple sales process can look like this:

- Sales meeting 1 – a meeting to discover the requirements which weighs 10- Sales presentation which demonstrates how the problems can be solved – it weighs for example 25- Offer – 50- Order – 100

When you know the weightings in question and standard time between the corresponding milestones, you can compare pipeline as a graph compared to the budget. See fig 2.

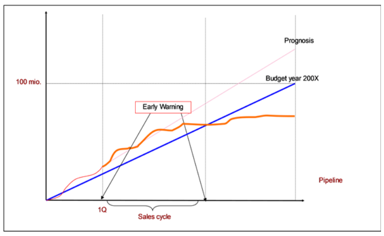

Fig 2 Pipeline vs. Budgete

Figure 2 shows "Pipeline" as a graph with the starting point in the invoiced sale for 1Q estimating how the sales will proceed based on the known sales cases. At some point the "Pipeline" will always cut the "Budget" graph. Here it is the sales manager role to make sure that there is minimum one sales cycle between today and the point where "Pipeline" cuts "Budget" graph. If a company is heading towards the relationship where there is only one sales cycle between today and the point where the pipeline cuts the budget graph, an "Early Warning" should be released.

When it happens, the sales manager can influence the "Pipeline" by influencing the accelerators in the sales process, in our case number of sales meetings; in other words the more sales meetings will be held, the more the "Pipeline graph" will rise and it will cut the "Budget" graph later.

Safety In The Forecasts

When you establish your model you can start working with the safety in the forecasts. There are many ways to increase safety, the most important of them is that everybody has the same reference frame; but there are also others.

In solution selling for example the work is designed so that it is the customers who decide where they are in the sales process. It is done by asking the customers per e-mail to accept that the sales consultant understood the problem correctly. The customer should also acknowledge that the meeting summary is correct. This way there is a customer/potential customer acceptance for each step of the sales process.

Importance

Finally, we would like to mention the importance. We have previously described this relationship in another article, see "IES-2008 - Internet Education Science" page 282. Almost all B2B companies operate under different 20/80 rules, for example when a relatively small number of customers generate 80% of the revenue/earnings; another typical example would be that 20% of products generate 80% of the revenue/earnings, etc. When you have managed these important correlations, you can then focus on what is important and again prioritize your resources and thus create a better basis for your forecasts.

References:

1. Solution Selling: Creating Buyers in Difficult Selling Markets, Michael Bosworth
2. New Strategic Selling (Miller Heiman Series)
3. SPIN Selling, Neil Rackham