The Handbook of Channel Marketing

How to select, motivate, and manage the people and organizations who sell your goods and services: Direct, Distributor, OEM, VAR, Systems Integrator, Rep, Retail

by

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— Innovators and early-adopters edition —

To

Arnold Jorgensen

An engineering craftsman, a recreational adventurer, my mentor, and my friend.

Thanks

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Author’s Foreword

Thirty years of personal experience led to this book. So did the help and support of many people, including sales and marketing professionals from all over the country. This is the book we needed when a group of us, technologists all, started our first company.

I am an engineer and an entrepreneur who learned how to market and sell as the need arose. I founded two successful high-tech companies and two other learning experiences. The successful companies are Pro-Log Corporation, which makes industrial computers, and MSI Data Corporation, which made order entry systems. The other learning experiences were Drag Mag, a toy company, and Digital Devices, maker of test equipment for capacitors.

Digital Devices was my first entrepreneurial endeavor. In the early 1960s, we four engineers worked nights and weekends out of a garage, while employed full-time at a computer company. I had designed a piece of test equipment that no one else had been able to make, and we learned the hard way that the world market for our $5000 instrument was 30 units. After two years of hard work at no pay, we sold three units, broke even, cleaned out the garage, and resumed a more normal existence.

Several years later, two of us from Digital Devices teamed up with a third person and started MSI Data Corporation. This time we identified a sizable market first: the supermarket industry. Then we found a product it needed in large quantities: order entry systems which supermarkets used to order groceries from their wholesalers via the telephone. Then we designed and sold the product. I was the VP of Engineering. I led product development, helped close the initial sales, found the SBIC (Small Business Investment Corporation) that financed us, and established our nationwide field service organization.

MSI was very successful for a few years, went public, and was eventually acquired by a competitor. However, the three of us who founded it disagreed strongly among ourselves about how to run a company, so I left after three years and a second founder left a year later. Mine wasn’t a happy departure, but in retrospect it was a blessing. I had neglected my family, and a period of rest reestablished my perspective about what was most valuable to me.

A year after leaving MSI, I founded, and was President, of an ill-fated toy company: Drag Mag. During its brief existence, we made a toy product, test-marketed it in Bakersfield, advertised it on TV in the Los Angeles market, and sold it through retail channels, including Toys-R-Us.

Then, in late 1972, Matt Biewer and I founded Pro-Log. I was its CEO for the next sixteen years. We started Pro-Log with $150,000 of our own money and a commitment to grow the business entirely from profits. We also vowed to make it an enjoyable place to work, a place that supported family life. Matt had six children; I had five. In August of 1973 we moved Pro-Log from Southern California to the Monterey Peninsula, and proceeded to grow, prosper, and enjoy our families for the next ten years.

During Pro-Log’s first five years I personally developed and managed its sales organization. We sold PROM Programmers and board level microcomputers through two domestic channels: Direct Sales and Manufacturers Representatives. Internationally, we sold through Distributors. In later years we added Distributors and a few VARs to the domestic organization. In Pro-Log’s sixth year I hired the first in a series of sales executives to run the sales organization. I stopped traveling and holed up in the plant to manage our fast growing and profitable company.

By the tenth year Pro-Log was a $20 million/year business with over $4 million net worth (all from retained earnings) and $1 million cash in the bank. Everything looked rosy. However, we'd caught a disease of success: an edifice complex. We plunged the company into debt by purchasing 20 acres of land for our future corporate home. We had big plans. We were confident. We knew the formula for enduring success. In reality, we had already lost touch with our customers.

As our building plans took shape, our business soured. Sales plummeted after I discontinued the PROM Programmers, a product line that had no future but had accounted for over 60% of our revenue in the previous decade. The decision was strategically correct, but my exit strategy was poor. Then we lost $1.7 million unloading our 20 acres. I managed the company for another few years through painful losses, skimpy profits, reductions in force, lost sleep, and alienated family and friends; finally I retired from Pro-Log to regain my bearings.

When I looked back on my performance as CEO, it became clear that I could have done a better job of managing and supporting the Marketing and Sales organization. My results had been mixed: some disappointing, some I'm still proud of.

How could I have been more effective? I studied books on Management, Marketing, and Sales. They helped, but key questions remained unanswered. I traveled the country and interviewed the Manufacturers Representatives, Distributors, and VARs with whom I had worked. I became an associate member of the Association of High Technology Distributors and interacted with its members. All these people were incredibly open and helpful. They encouraged me to communicate what I was learning. Most of them were particularly frustrated with the ignorance and arrogance of many CEOs and regional sales managers. They wanted to be better understood, to be respected for what they did, and to be treated as professionals. They wanted to work with suppliers, not play endless games of cat and mouse with them.

Simplifying concepts emerged as I organized and reorganized the mass of information from the interviews, research, study, and personal experience. I crafted these concepts into practical and useful management tools. In 1991 and 1992 I conducted a nationwide series of one-day workshops for CEOs and Sales Professionals. This book expands and refines the workshop's material.

I'm still learning, so I'd appreciate receiving your comments about this book or about other things that have helped you sell or manage your selling system.

Ed Lee
June 28, 1996

Introduction

Frank was the new CEO of a struggling, high-tech company stuck at $15 million in annual sales and break-even profits. Frank was a technologist with an advanced degree in engineering. He had been hired away from another high-tech company, one that he had successfully transformed into a profitable, growing organization. He was expected to repeat his earlier success.

Frank analyzed the company's situation. Most of its products were becoming outdated. The company sold its products through two channels: company employees (Direct Sales) sold to the largest accounts and commissioned Manufacturers Representatives sold to the rest of the market. The company had stopped most of its advertising eighteen months earlier to cut costs and focus on major accounts and repeat business.

Frank chose three initiatives to return his company to growth and profits: 1) update the product line, 2) add a new sales channel to the selling system, and 3) generate leads. To update the product line he launched an aggressive product-development program. Over the next two years his company introduced some 40 new products that clearly matched or bettered its competition in performance, quality, and price. To add a new sales channel he first hired a junior sales professional from the staff of his old company and made him National Sales Manager. Within a four-month period, the National Sales Manager signed up twenty-five System Integrators, most of whom also worked with his old company. To generate leads, Frank launched a costly advertising campaign. Within six months it dramatically increased the number of inquiries from fewer than fifty a week to more than a thousand a week.

Frank confidently told his board of directors that the existing sales channels would persevere for a year while the company developed its new products. He forecast that his new sales channel, a nationwide network of Systems Integrators, would increase domestic sales at least 10% in the first year and would be the primary source of growth after that. They had done that for his last company. He also said: "*Manufacturers Representatives are just part time contract laborers. They aren't good organizations for selling our products*."

Frank's actions looked good in theory, but his results were appalling. In his first fiscal year, domestic sales were well below the prior year and 30% below Frank's forecast. His company suffered the largest operating loss in its history. There were destructive conflicts between Systems Integrators and the Manufacturers Representatives. Frank fired Manufacturers Representative organizations right and left, while the Systems Integrators did less than half the business projected for them. In the second year sales declined further and the company lost more money. By the third year the company was nearly bankrupt, in spite of its exciting new products, new sales channel, and numerous leads.

As you study this book, you'll learn how to avoid Frank's lamentable results and get the sales and profits you plan for. Frank was a competent engineer, but as a CEO he was handicapped by engineering biases and by limited experience with selling. He made basic mistakes, including these:

- **Hiring channel organizations doesn't mean they'll sell for you.** He didn't have the resources to evaluate, train, motivate, and provide ongoing technical support for twenty-five Systems Integrators.
- **Leads don't mean that people will buy from you.** Advertising often produces numerous inquiries, but few of them are worthwhile. Leads must be answered and evaluated to determine which ones might produce profitable business. Systems Integrators are particularly poor at evaluating and pursuing leads.

- **People will live up to your negative expectations**. Frank's beliefs about Manufacturers Representatives caused him to treat them as problems. His attitude toward them helped to undermine their commitment and performance, and lost some of their major accounts just when his company desperately needed business.
- **Adding a sales channel creates inter-channel conflicts over resources and customers**. Conflicts are intrinsic to multi-channel selling. They can be controlled by careful planning and skilled management, but they can't be ignored or eliminated. The Systems Integrator channel created conflicts which accelerated the collapse of his Manufacturers Representative channel.
- **What works for one business may not work for the next one.** Frank reenacted what had succeed in his previous company. Because his strategy worked before, he continued to pursue it long after his results cried out for a new plan.

Frank's sad-but-true story, illustrates a common challenge facing most CEOs of high-tech companies: they are technologists and not sales professionals. They know how to develop successful products. However, they don't know how to build successful marketing organizations. They deal with technical challenges realistically and systematically, but they approach selling with convictions based on limited experience and cultural bias.

Technologists and Sales Professionals work in two different cultures, and evaluate each other from perspective of their own cultures. When technologists select and manage sales professionals, they do so with a technical bias that overvalues product knowledge and systematic thinking and undervalues motivational skills. When sales professionals work with technologists, they do so with a sales bias that overvalues motivational skills and undervalues product knowledge and systematic thinking. These cultural biases sabotage teamwork, increase stress, lose business, and reduce profits.

Part of the cure for cultural bias is respect for and knowledge of the other culture. Another part is a healthy sense of humor. This book sets out to increase your respect both for sales professionals and for technologists. It will also equip you with a systematic, comprehensive understanding of how best to market and sell your products to your most profitable customers. It will explain what undermined Frank's plans, and how you can confidently develop sales plans that succeed. I hope it will also tickle your funny bone from time to time.

Who can use this book?

If you're a **CEO,** you can use this book. It develops a systematic and useful perspective on the selling process and selling systems; one that you can use to select and manage sales executives. It analyzes the costs, risks, and benefits of selling through each channel. It provides checklists of the goods and services that each channel organization provides. It contains *how-to* information such as: how to find the optimum mix of channels, how to develop a successful channel, how to interview a sales executive, and how to select and manage a channel organization. You can reduce your job stress and make your work with sales professionals more satisfying and enjoyable.

If you're an **entrepreneur,** you can use this book. It can help you avoid selling mistakes that most of us have made. Don't worry! You'll still have plenty of your own mistakes to keep things interesting.

If you're a **sales executive, sales manager, or sales professional,** you can use this book. It describes how to manage sales professionals in channel organizations and technologists in your own organization. There are even tips on how to manage your CEO! It also contains screening criteria for customers and channel organizations that will help you quickly identify the profitable ones.

If you're the **owner/manager of a channel organization,** you can use this book. It describes specific techniques that your peers have used to improve their sales and profits. It suggests workable solutions to the usual conflicts between suppliers and channel organizations. It gives you new insights into your suppliers, customers, and your own employees that can make your job easier and more satisfying. You can use copies of this book as gifts for the CEOs and regional managers you work with.

If you're **a technologist who designs products, works with the sales organization, or works with customers,** you can use this book. It can improve how you design products because it identifies product characteristics that improve sales and profits. It explains sales professionals in a way that will make it easier for you to work with them. It can improve your effectiveness in selling situations.

If you're a **financial executive involved in planning and budgeting**, you can use this book. It systematically presents the selling system in a way that will enable you to support and audit the economic impact of sales decisions more effectively. It also discusses how Generally Accepted Accounting Standards encourage sub-optimal decisions by corporate management.

If you're **studying for an MBA,** you can use this book. It provides practical, street-smart management information to complement academic theory. It updates the management theory of *Management by Objectives,* with a comprehensive and more effective alternative: *Management by (Strange) Personal Attractors*.

Overview

This book systematically explains how to how to develop a selling system that produces long-term, mutually-profitable working relationships with customers and sales professionals. It describes practical ways to stimulate sales and increase profits, but always in the context of sustainable success. It eschews selling gimmicks that temporarily increase sales or profits at the expense of customers, people in the selling system, and future business.

The book has three distinct sections: Methods and Tools, Sales Channels and Channel Organizations, and Where the Rubber Meets the Road.

> Section I: **Methods and Tools** (Chapters 1 through 7) describes the fundamentals of planning, managing, buying, and selling and develops valuable management tools. There are new and useful management concepts introduced in this section including *Management by Personal Attractors* and the *Basic Attitudes of Decision Makers*.
>
> Section II: **Sales Channels and Channel Organizations** (Chapters 8 through 13) develops the data-base for designing and managing a selling system. It describes sales channels, channel organizations, and key jobs within channel organizations.
>
> Section III: **Where the Rubber Meets the Road** (Chapters 14 through 22) explains how to develop, manage, and continue to improve a successful selling system. It contains specific recommendations on almost every aspect of the design and management of a selling system.

You can use the ideas and recommendations of Section III without reading the first two sections. However, they will be far more useful to you after you've studied the tools of Section I and the information of Section

II. Without these tools and information you might implement a suggestion or recommendation "too simply." The significance of this remark is explained in Chapter 1 under the heading: *Solutions that are as Simple as Possible...but not simpler.*

Section I

Methods and Tools

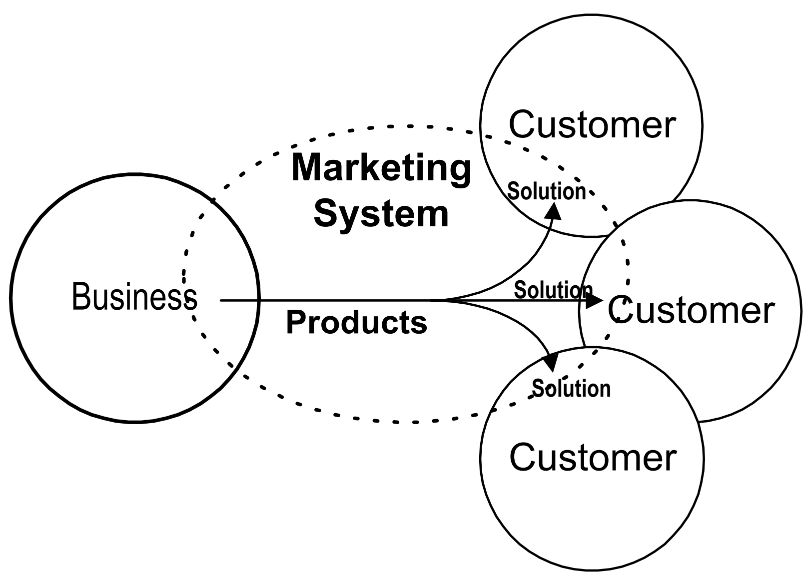
1. Defining the Objective

"*The operation was a success, but the patient died.*" Anonymous

You or I could manage a marketing and sales organization without knowing its objectives, without planning its progress, without understanding or respecting people, and without working hard. However, to manage a *successful* one we need accurate information, realistic plans, interpersonal skills, and hard work. Our objective is to deliberately, knowingly, and confidently produce a *successful marketing system* for your business. Our first step is to present a clear, quantitative picture of that objective in a way that enables us to plan for it. The next chapter will discuss the fundamentals of a successful planning process.

What is a Marketing system?

A *marketing system* is the organization and process a business uses sell its products. The marketing system identifies potential customers, establishes working relationships with them, and transforms products into solutions that meet their needs. (See Fig. 1.1). It includes the Marketing and Sales organizations of the business and elements of customer organizations. It usually includes third-party organizations, ones that are not part of the business itself or part of customer organizations.



A marketing system operates through one or more *sales channels*. A sales channel is a specific kind of connecting path between a business and its customers. The most common sales channels go by the names: Direct, Distribution, Manufacturers Reps, Value Added Reseller (VAR), System Integrator, Original Equipment Manufacturer (OEM), and Retail. A sales channel includes one or more *channel organizations* that share similar characteristics and do comparable tasks. For example, a Direct channel is staffed by employees of the manufacturer who work directly with customers. A Distribution channel is composed of third-party organizations called Distributors. These organizations buy the business's products at a discount and resell them to their customers.

Those familiar with the usual business terminology may wonder why I've chosen to use the term "marketing system" instead of "marketing organization" or "sales and marketing organization." I've done so for three important reasons.

First, a system is dynamic and holistic. It operates within an environment or application to produce an output for a significant period of time. An organization is merely the structure, usually studied out of context. Metaphorically, a marketing system is a frog living in its pond; a marketing organization is a dead, dissected frog in a biology lab. This book is about how to operate a marketing system successfully in its pond (environments, contexts). Its pond includes the business it supports, the customers it serves and the competition it faces. We will study the dynamics of the pond and the significant interactions between the frog and the pond. Now and then, we will dissect dead frogs to better understand the living ones.

Second, the term "system" is a technical term that appropriately suggests to technologists that we're dealing with something that is complex, but has a rational structure which serves a useful purpose. A marketing system is something that technologists can work with, using skills they already have.

Third, my "marketing system" contains essential people, methods, and materials that are outside the boundaries of classic sales and marketing organizations. By adopting a new name, I am able to include these elements without having to argue about standard definitions.

When is it Successful?

We'll carefully develop a working definition of a *successful marketing system* because you are going to use it to specify your objectives and to measure your progress. We'll start by evaluating two definitions of *successful projects*, because a successful marketing system is a successful project. The first definition is the classic, universally accepted one; it describes a dead frog. The second one is recently developed, more accurate and far more useful; it describes a frog thriving in its pond. We'll adapt the second definition to define a successful marketing system.

In 1989, I taught a course on Project Management to business and government executives in Shanghai. While preparing the course, I purchased two massive tomes on Project Management which contained two, significantly different, definitions of a *successful project*. The book by Harold Kerzner,[1] rattled off the classic definition:

"*A successful project is one that is a) on time, b) within budget, c) meets its technical requirements, and d) is accepted by the customer/user.*"

This definition looks good on paper because it is quantifiable and measurable. Unfortunately, it is also inadequate. If you use it to plan for success, you will usually fail. It has two major defects. First, it describes a win-lose project. The persons or organizations who set the schedule, budgets, and technical parameters win, and everyone else involved loses. Second, it only defines success just as the project ends: when the customer/user accepts the results. True success is sustained over extended periods.

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[1] Harold Kerzner, PH.D., *Project Management* (Third Edition), Van Nostrand Reinhold, 1989

A failed project, from the point of view of a rational observer, could satisfy all of Kerzner's requirements for success. A humorous example is illustrated by the phrase: "*The operation was a success, but the patient died,*" first uttered by a surgeon who operated by the book and got paid by the insurance company in spite of the patient's subsequent, uncooperative demise. That surgery was on time, within budget, met its technical requirements, and was "accepted" by the insurance company (customer) and the unconscious patient (user). It met the surgeon's criteria for success. Common sense tells us it wasn't successful.

A successful project might not meet any of Kerzner's criteria. For example, Desert Storm (the project to drive the Iraqis out of Kuwait) was generally considered *successful* shortly after it was concluded. But what significance did on-time have? What financial budget did it have to meet? (At the time, a critical budget for the American public was number of GIs killed.) What constituted acceptance by a customer/user? Who were the customers? Kuwaitis, Saudis, and the American public were just a few of them. They all had different definitions of an acceptable result, and these definitions have changed with the passage of time. In the years following Desert Storm, the American public and the GIs who risked their lives to fight are less inclined to view it as a success. Saddam Hussein is still a threat. Kurds have been slaughtered by Iraqis. The Kuwaiti and Saudi governments remain despotic, and may yet collapse. Many of our veterans suffer from mysterious maladies.

The authors of the second book on Project Management[2] developed an accurate and useful definition of success by interviewing hundreds of successful project managers and carefully distilling their definitions.

"A successful project is one that all its key stakeholders believe is successful!"

The key stakeholders in a project include its:

- Sponsor
- Leadership team
- Major suppliers
- Customers.

This definition seems to have serious problems. A critique of it might go something like this: "*That's no definition at all; it's self referencing. Where are the objective, quantitative measures of success? The old definition let me define a schedule, a budget, and technical requirements, tell everyone what they were and then measure the results. This definition is subjective, fuzzy, and hard to manage.*"

On the contrary! This definition describes a "win-win" project that appropriately benefits all key stakeholders. To be deliberately *successful* according to this definition, each key stakeholder must specify and communicate his or her conditions for success before and during the project. Their conditions will include traditional things like budgets, schedules, and technical requirements. However, the conditions of one stakeholder will differ from those of another stakeholder. For example, the Sponsor's budget requirements will be quite different from those of the Customers, Suppliers, or members of the leadership team. Conflicts in conditions among various stakeholders have to be exposed and resolved to assure success. Where there are unresolvable conflicts, the project can't succeed.

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[2] Cleland and King, *Project Management Handbook* (2nd Edition), Van Nostrand Reinhold, New York, 1988

This definition of success also brings the element of time into the evaluation. A project may be successful to some of its key stakeholders on the day it's completed, and later be deemed a failure. A question that must be resolved is: When, and for how long should key stakeholders consider the project as successful? How long after the "successful surgery" should the patient live, or the doctor get paid, or the lawyers hover around for a piece of lawsuit? The answer to that question determines how the project is managed.

A marketing system is an ongoing project. When we adapt the Cleland and King definition to it, we have:

DEFINITION OF A SUCCESSFUL MARKETING SYSTEM

"***A marketing system is successful only when, and for as long as, all its key stakeholders believe it is successful.***"

The key stakeholders in a marketing system include:

- CEO of the business (Sponsor and Major Supplier)
- Managers and sales professionals in the marketing system (Leadership Team)
- Owners of channel organizations (Suppliers)
- Key customers

Each stakeholder measures success in terms of results in four areas:

- *objectives achieved:* sales objectives, profit objectives, market objectives
- *resources used:* man-hours, money, materials
- *methods employed:* policies, procedures, and personal relationships
- *personal needs satisfied:* financial, security, belonging, recognition, achievement, and fun

However, specifics and priorities will differ among stakeholders. For example:

- The CEO of the business measures success on how well his marketing system meets or exceeds revenue quotas and stays within budget. To that extent his expectations are quantifiable and in line with the academic definition of success.
- The managers and sales professionals in channel organizations, measure success on their personal results, the quotas and budgets of their organizations, the support they receive from the business, and on their customers' reactions.
- Customers measure success on how well the marketing system meets their individual price, delivery, technical support, and personal needs. They don't concern themselves with its revenue quotas or overall budget.

The key to sustainable success is to manage the system so that all parties deem it successful as measured by their requirements. This observation leads to two Corollaries to our definition of success.

Corollary 1:
The fewer the stakeholders with conflicting expectations, the more likely that the system will be successful.
Each additional stakeholder brings personal and professional conditions for success which may conflict with the conditions of the other stakeholders.

Corollary 2:
If at least one key stakeholder has unrealistic expectations, then the system cannot be successful. The most important ingredient for success is to select key stakeholders whose

expectations are aligned with reality and with one another. This book, particularly in Chapters 3 and 4, will provide you with information and tools with which to select stakeholders who can contribute to a successful marketing system and to weed out those who will undermine it.

Our definition of success makes it clear that success requires the careful selection of stakeholders.

The Six Cornerstones of successful business partnerships

A successful marketing system is a win-win-win partnership. Manufacturers win, sales channel organizations win, and customers win. "*Strategic Selling,*"[3] an invaluable book by Miller and Heinman, proves that there are only two stable relationships between customers and sellers: win-win or lose-lose. Relationships that start with the seller winning and the customer losing, or vice versa, always degenerate to lose-lose relationships.

Win-win business relationships are built on six cornerstones:

- Mutual Benefit
- Mutual Competence
- Mutual Respect
- Mutual Integrity
- Mutual Enthusiasm
- Competitive Alternatives

Mutual Benefit

Rational individuals and consistently profitable organizations initiate business relationships to gain benefits that are worth more to them than the relationships cost. These benefits come from the relationships themselves and from the objectives achieved. In a win-win relationship, all participants are aware of the region of mutual benefit and take joint responsibility to see that they operate in that region. This eliminates non-productive conflicts and reduces overhead costs. In fact, mutually beneficial relationships are largely self-organizing, which is why they cost relatively little to manage.

Mutual Competence

Every person and organization has to be able to do what's necessary and what's expected of them. A manufacturer must deliver a product that meets its specifications. A sales professional must know how to select and sell to appropriate customers. A customer must pay for the product and use it successfully. When one or more parties lacks adequate competence to fulfill his or her responsibilities, one of two things happens: the results fail and everyone loses, or one party puts more into the relationship to compensate for another party's failings and it ceases to be mutually beneficial.

Each party must be clear and specific about what it will do and what it expects of the other parties. It must assess competencies before and during the relationship, and act accordingly. Naive manufacturers sign up sales professionals or channel organizations whose competencies aren't appropriate or adequate. Inadequate sales professionals sell to customers who don't pay their bills, misuse the product, suck up support, or give the product a bad reputation. Careless customers buy from manufacturers who don't deliver on time, who don't support the customer after the sale, or whose products don't meet their needs.

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[3] Robert B. Miller and Stephen E. Heinman, *Strategic Selling*, Warner Books, 1985

Naive manufacturers, inadequate sales professionals, and careless customers create win-lose and lose-lose relationships. This book includes check lists and analytical tools to evaluate and quantify the competencies of each stakeholder in a marketing system.

Mutual Respect

Respect is called "credibility" in sales and "trust and confidence" in management. It's a belief in another person or organization that enables us to say **yes** to becoming interdependent without having to undertake endless negotiations to protect ourselves. Jo-Ellen and I have been married over thirty years. We wholeheartedly agree on this: mutual respect enabled us to say "I do" without really knowing what we were getting into, and mutual respect has gotten us through tough times.

Beneficial business relationships are like successful marriages. Win-lose and lose-lose relationships are like affairs or one-night stands. Perhaps the sales culture suffers a lack of respect because it's too often associated with one-night stands!

Mutual respect requires a history of competence and integrity by both parties, particularly in how they deal with each other. While most people in business are worthy of respect, I've gotten into business situations with a few people who weren't. These individuals lacked either integrity or competence, or both. Many of them were pathologically unable to respect anyone else. Unfortunately, some of them reached top management.

Mutual Integrity

Integrity is a bit like success or quality: we all know what it is, but it's hard to define. What people used to say about a businessperson with integrity was "his word is his bond." Integrity is essential for sustaining respect. Integrity is profitable. With mutual integrity, both parties can move ahead to achieve something together and work out the details as issues arise. One-page agreements are possible. Without mutual integrity, people squander substantial amounts of time and money trying to protect themselves from each other, and they can't succeed.

I've been burnt more than once by people with underdeveloped integrity. I've learned to follow this procedure: a) Make certain that I act with integrity, b) Evaluate the integrity of the other party before doing business; if its missing or doubtful, don't do business, c) If I'm in a business deal and discover that the other person lacks integrity, I end the business relationship, take my losses, and get on with something else.

I started Drag Mag, my unsuccessful toy company, with four other "equal partners." When it failed, three of the partners bailed out and left two of us holding the bag. We had written agreements and we could have sued them. We simply paid the bills, walked away, and counted ourselves lucky that the company hadn't succeeded and bound us more tightly to those three yo-yos. We should have known better going in, and the object lesson was worth the money.

Mutual Enthusiasm

Enthusiasm is a word that describes intensity and playfulness in a healthy, natural union. People are enthusiastic when they enjoy being good at what they do, when they have fun. ***Fun!*** There, I said the "F" word of business. A healthy, successful business relationship is fun. It is intrinsically playful.

Winning football, basketball, or baseball teams; practice hard and play intensely. Beyond all that, the team members enjoy playing well. They are enthusiastic. They celebrate what they do while they do it, and they celebrate with each other.

Selling is fun! Buying is fun! A healthy marketing system is fun! A successful business is fun! ...except to business fanatics and humorless bureaucrats. When the fun goes out of a personal relationship, it's dying. The most effective and happiest people say they're having fun working, and as a bonus they get paid to do it! When someone says "this job isn't fun anymore," that person is ready to change jobs.
Many times I have wanted to wear a sweatshirt that read:

"*Let's get serious about fun and make some real money*."

Have you ever wondered why top athletes and mediocre entertainers are paid more than business executives, politicians, or lawyers?

Competitive Alternatives
Countless studies show that we are much more satisfied with products, jobs, relationships, politicians, etc. when we choose them than when they are imposed on us. To have a choice we must have at least one competitive alternative. A customer who chooses a product from among several competitive alternatives is happier with it than one who has no alternatives. An employee who chooses a specific company to work for is far more positive and productive than one who believes she couldn't get another job. A sales professional who freely chooses to sell a product when she could sell any number of other products will be more effective and enthusiastic. Competitive alternatives give us a sense of personal responsibility, commitment, freedom, and enjoyment.

It's frustrating to listen to managers who wish to eliminate their competition and dominate their markets. They seek to control customers, employees, and selling partners by eliminating their competitive alternatives. It's a win-lose approach and it's costly to sustain. Market dominance produces customer hostility and it corrupts the business and the people in its marketing system. Market dominance by Microsoft has produced customer resentment and hostility. It has also produced management arrogance towards customers and competition. The same thing was true about IBM when it dominated the computer industry.

Competitive alternatives are vital resources to all parties in a business relationship. In a buyer/seller relationship, the buyer's competitive alternatives are resources to both parties. Likewise, the seller's competitive alternatives to doing business with a specific buyer are resources to both parties.

I'm convinced that the most successful, the most enduring, the most satisfactory relationships are between "*consenting adults.*" To be a *consenting adult* one has to: a) be informed, b) choose from among desirable competitive alternatives, c) enjoy the relationship.

Exercises

1. Who are the key stakeholders (including yourself) who determine whether or not your job is successful? Make an educated guess about what each stakeholder's top five criteria for your success are (At least one criterion is in each of these contexts: objectives, methods, and personal relationships). Check out your assumptions with them... the discussions should prove interesting and educational.

2. Identify the key stakeholders in your marketing system or in the part of the system you work within. Be specific by organization and by name. What are their criteria for success of your marketing system (first make an educated guess, then check it out)? What are your personal criteria for success over and above your company's business criteria?

2. How to Produce the Objective

"Make all things as simple as possible, but not simpler," Albert Einstein
"*The better you understand something the more simply you can explain it."* Fulton Sheen
"*$E= mc^2$*" Albert Einstein

Marketing systems are often designed to meet unrealistic objectives, such as "*dominate the market and its channels of distribution*." Sometimes they are designed to support half-truths such as "*with more feet on the street, we'll sell more product,*" or "*more inquiries mean more business*." Many of them evolve without much planning. Consequently, most marketing systems are too complicated and too costly: ***too many sales professionals, too many sales channels, too many customers, all producing too many expectations by too many key stakeholders.***

When a marketing system is too complicated, the average sales person isn't competent and committed. Sales managers spend too much time coaching non-performing sales professionals and dealing with unprofitable customers. Executives constantly fight fires to keep the lid on channel conflicts. As you'll recall from the Introduction, Frank beefed up advertising and added a sales channel, but sales plunged and losses soared.

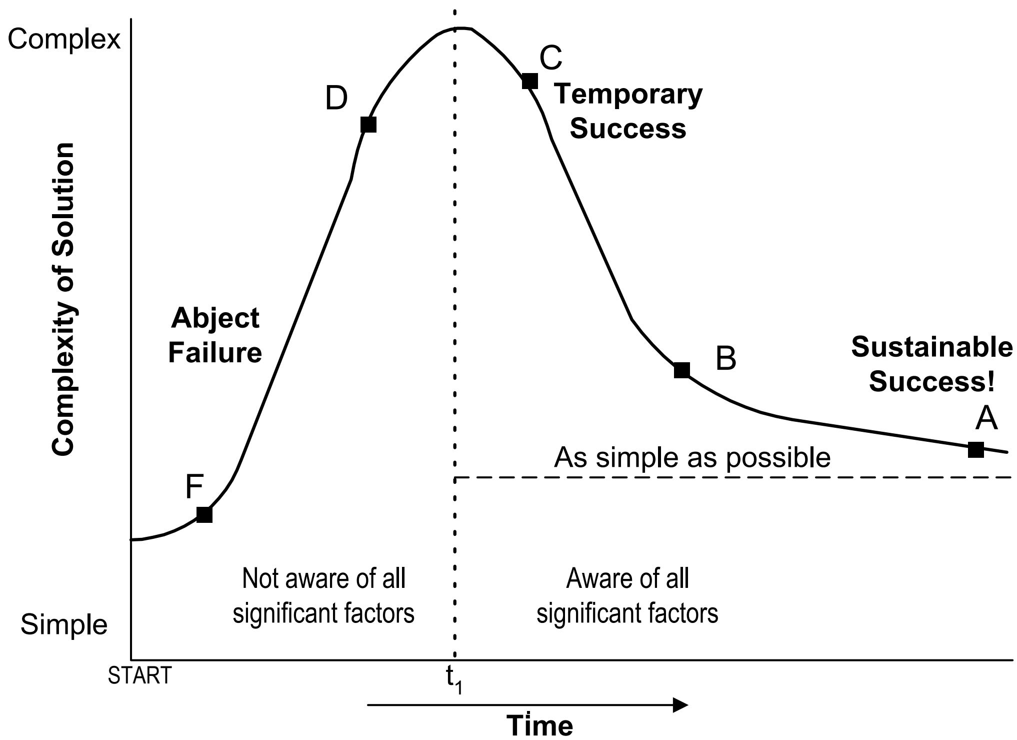
This chapter reveals some good news: a successful solution is always relatively simple, as simple as possible, but not simpler. It also introduces the Scientific Method: a method you already use to plan and manage, whether you realize it or not. Then it shows you how to employ the Scientific Method to produce a relatively simple marketing system that succeeds year after year.

The learning process, through complexity to success

When we first examine any problem, we don't know much about it. Therefore, our initial ideas of how to solve it turn out to be too simple, and fail. As we study a problem, we learn more and our ideas about how to solve it become more complicated. We often reach a point where the problem looks too complicated to deal with. For example, you've already learned that a successful marketing system doesn't involve just your own objectives, it also involves the objectives of your suppliers, customers, managers, and sales professionals. This is just the beginning! You'll find a myriad of issues as you continue to learn about marketing systems in later chapters. You might reach a point where you ask yourself: Is there a simple, manageable way to design and manage a successful marketing system? Fortunately, the answer is yes!

Each of us has an innate ability to simplify complex information. To appreciate your own ability to do this, just examine one of the currently popular "Magic Eye" pictures. At first the picture is a meaningless and confusing array of colored dots and swirls. Stare at it, with eyes focused slightly in front of the page. Eventually, a three-dimensional picture snaps into view. Your brain finds the coherent picture coded in the dots and swirls. It self-organizes a simplifying pattern that was inherent in the complex collage, and you see a meaningful picture.

Simplifying ideas produce equations in science, patents in technology, and competitive advantages in business. This book will present you with several powerful ideas that will simplify your marketing system and how you manage it. Those ideas will give you terrific, sustainable competitive advantages. However, to appreciate them fully and to use them most effectively, I strongly advocate that you study the book's detailed information.



A closer study of the route to success

The curve in Figure 2.1 is an approximate, generalized map of the route to success. It applies to all learning and problem solving including: developing corporate objectives, designing a product, or developing a marketing system. I've marked five points on the curve (F, D, C, B, and A) which also correspond to letter grades for the quality of a solution implemented at each of those times. We start most learning or problem solving processes near point F. When we persevere to the region of point A, we produce strategically successful solutions.

When begin solving a problem, we still know relatively little about it. We are in the region of Point F. Our concept of a solution is "simpler than possible." It will fail. In this book we are at Point F in learning what we need to know about producing a successful marketing system.

When we reach Point D, we understand our problem more completely, but some key pieces are still missing. Our idea of a solution is complicated, composed of pieces and compromises strung together in a patchwork. If implemented, it too will fail. Sometimes this solution can be kept afloat with substantial modifications and improvements. An example of a D solution is a product that is *user unfriendly* and/or has significant defects. As we dig into the information of the next dozen chapters of this book, we will travel from point F to point D on the subject of channel marketing.

When we reach point C, we've learned all the significant facts related to our problem. We will have a brute force solution that is viable, but still fairly complicated. Our solution will work for a while, but it won't be cost effective or robust. By the end of chapter 13, we will have covered enough information about channel marketing to produce a C solution and temporary success.

As we continue to study and develop a deeper understanding of our problem, we will discover simplifying concepts that produce a B solution; one that is somewhat robust and competitively viable for a reasonable period of time. Chapter 14 introduces two critical, simplifying concepts for organizing and managing your marketing system.

After we apply the first simplifying concepts and continue to learn, we discover more simplifications. Eventually we reach an A solution; a simple, robust solution that succeeds year after year. At point A we have a deep understanding of our problem and our solution. Chapters 15-22 of this book should help you produce a marketing system that is an A solution; with sustainable competitive advantages.

The process illustrated in Fig. 2.1 applies to all learning experiences including: learning a language, learning to walk, learning to play the piano, learning to ride a bike, becoming a star athlete, designing successful products, managing effective organizations, developing teamwork, and writing books. The most successful people in each of these areas have systematically worked their way to point A. What they do successfully seems natural and effortless because they've learned and simplified through hard work and self discipline. But they all went through learning processes in which their results were complicated and marginal before they

EXAMPLE

became simple and robust.

The route to success clarifies a classic Marketing/Engineering conflict

Marketing and Engineering frequently engage in protracted struggles about when to release new products. Marketing wants to get to market as quickly as possible to establish market position and market share. Engineering wants to do its job well, before letting go of a design. Unfortunately, Engineering usually takes more time to develop a product than it planned to. Fig. 2.1 helps to explain why.

To begin with, the project engineers are at Point F when they schedule a product development project. Their ideas about the product are too simple because they have yet to go through the design process to discover all the technical issues. Most engineers pad their budgets and schedules to allow for unknowns. However, they either underestimate the padding needed or it is eliminated by shrewd managers. As engineers go through their design process, they find out why they needed more time and more money. By the time Engineering has a D solution, it is behind schedule, over budget, and "90%" complete.

By this time, Marketing is foaming at the mouth. Buzz words like "engineering driven" or "market driven" are tossed around and the battle is joined. To add to the conflict, Marketing is usually hampered by an "F" understanding of the design problem. It believes it could get something to market right away if it weren't for those plodding, over conservative engineers. But, if Marketing wins, a D solution is shipped; the product is unreliable or fails to meet the needs of its market. If engineering wins, an A solution reaches its market far too late to succeed.

The most successful strategy is a compromise: release a B solution, then start an upgrade design cycle to produce an A solution. The time required to develop the B solution is "as soon as possible."

The Scientific Method: our problem solving tool

Western Civilization has developed a systematic way to travel the route to success; the Scientific Method. Technologists use The Scientific Method to solve technical problems, but they assume it isn't part of a sales professional's culture. Most sales professionals thank their lucky stars they aren't burdened with it. They regard it as a clinical, cold, and inhuman process. Actually, all of us use the Scientific Method. It is thoroughly ingrained in Western culture and in our thinking processes. It is a systematic way to do "trial and error" problem solving that supports teamwork. It uses habit, intuition, emotions, ignorance, and reason. It is very human and it is fun!

The Scientific Method applies beautifully to the challenge of designing and managing a successful marketing system. It's a tool we use in this book, and one you'll use to manage your marketing system. Let's study it so that we can eventually implement it as "*simply as possible, but not simpler*." (An "A" implementation.)

A six-step process

The Scientific Method is a systematic, rational process for visualizing a problem (need, objective, opportunity), conceiving a solution, and fitting the solution back into real life. It has six basic steps:

1. Specify a *problem* or *objective* in a way that enables it to be treated like a finite object imbedded in a limited set of contexts.
2. Specify an hypothesis: the characteristics of a probable solution.

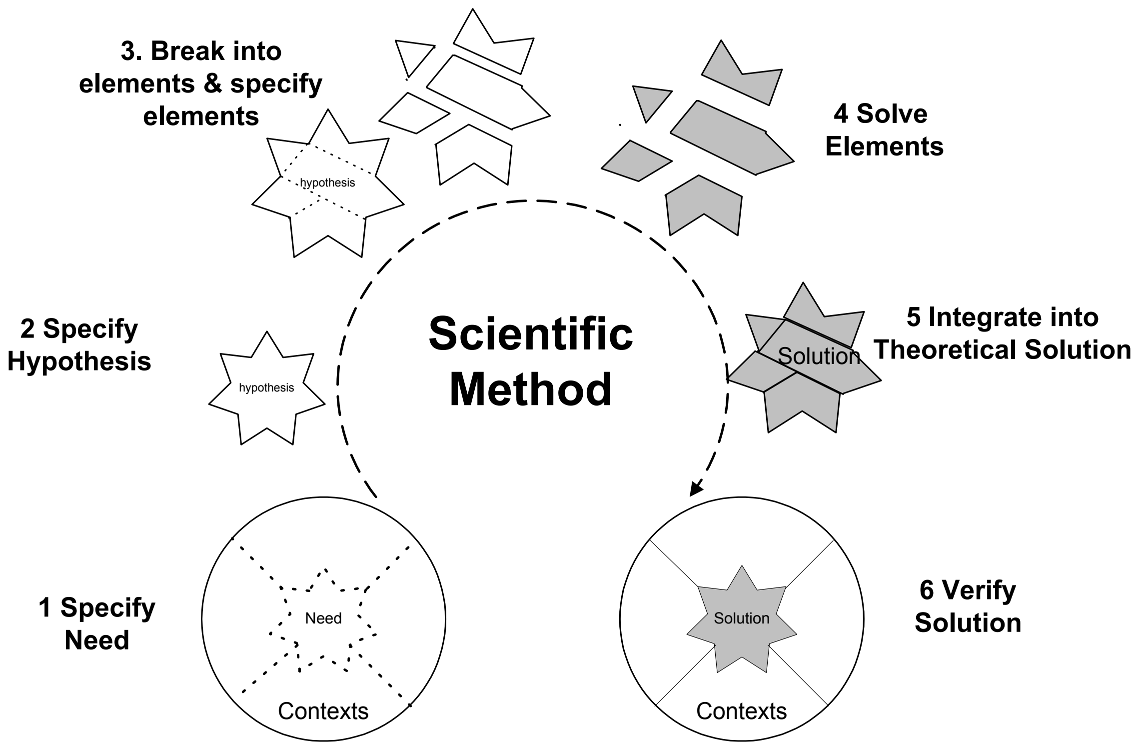
3. Divide the hypothesis into bite-sized elements and specify each element.
4. Solve each element.
5. Integrate elements into a theoretical solution.
6. Verify the theoretical solution in the real world.

Steps 1, 2, and 3 are the *top-down* or *context-to-object* planning sequence. Steps 4, 5, and 6 are the *bottom-up* or *object-to-context* solution development. The steps may look simple, but they are disciplined and profound. Fig. 2.2 graphically represents these steps.

Step 1. Specify a need. Any need, problem, or opportunity is intimately entwined with reality through an infinite number of interdependent relationships. The need may be finite, but its contexts are infinite. Yet, if we must consider an unlimited number of relationships, it will take us forever to develop a solution. We must somehow eliminate the infinite number of "trivial" relationships and correctly identify and quantify the significant ones. We do this with a *Need Specification.* We develop this specification with educated guesses based on what we know at the time we do it. However, there is room for error, no matter how much skill we have or how much time we spend.

Step 2. Specify an hypothesis. An hypothesis is an idea for a probable solution to the specified need. It's also an educated guess based on what we know at the time. An hypothesis has properties and involves resources that are unique to it and not otherwise part of the need. We identify and quantify these characteristics and resources in an *hypothesis specification.*

Step 3. Divide the hypothesis into bite sized elements. When a hypothetical solution is too complicated to be actualized in one piece, we systematically divide it into elements until each element is simple enough to solve. We repeat Steps 1 and 2 for each element to create *elemental hypothesis specifications*.



Step 4. Solve elements of the hypothesis. To *solve* an element means to actualize something which fulfills the requirements of its *elemental hypothesis specification*. We conceptualize a solution for the element, implement it, and test it to its specification.

Step 5. Integrate elements into a theoretical solution. We interconnect the elements and test them as a system to the parameters of the *hypothesis specification*. Success at this step validates the *elemental hypothesis specifications*.

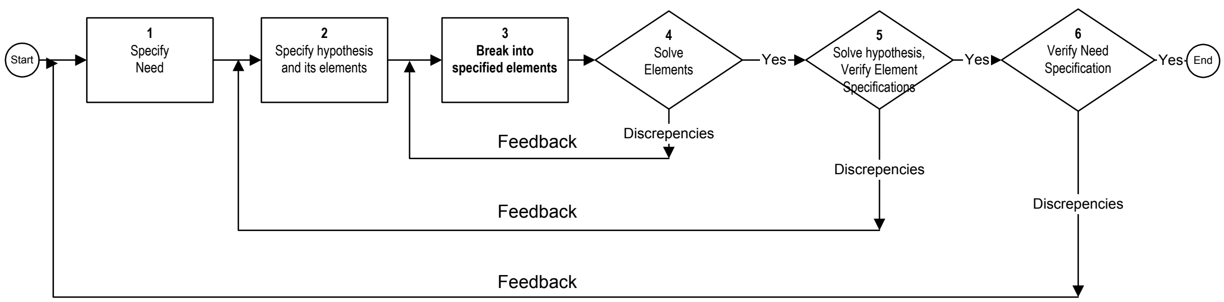
Step 6. Verify the solution in the real world. We test the theoretical solution in real applications. Success at this step validates the *need specification*; it increases our confidence that we accounted for all the significant relationships between the need and its context.

Commentary on the process
The Scientific Method is:

- Based on human judgments
- Iterative
- Specification centered
- Structured and modular
- Facilitates teamwork

Judgment based: Human judgment is critical to every step of the Scientific Method. We make educated guesses to select our needs or objectives from an unlimited number of possibilities. We use judgment to select a limited number of significant contexts from among an infinite number of actual ones. It's mathematically impossible to be certain that we make the best choices. Those executives, managers, lawyers, and other bureaucrats who actually expect perfection, zero defects, or risk free judgments are unscientific.

We form our judgments with the tools of reason, metaphor, habit, intuition, emotion, and ignorance. Reason and metaphor are conscious tools. Habit, intuition and emotion are subconscious tools. Ignorance is an unconscious tool. We use conscious and subconscious tools to make a limited number of choices, and we use ignorance to make an infinite number of choices. In a very real sense ignorance is a powerful focusing mechanism, one that is essential for us to be able to choose at all!



Iterative with feedback: The Scientific Method does not progress in a straight line from one step to the next. Within each step we go through cycles of *trial-error-corrective action*. We often recycle through earlier steps after we perform later steps. Recycling through some or all the steps validates and improves judgments and develops simplifying ideas (see Fig. 2.3). Each step in the process is ultimately a context for all the other steps. They affect one another; they are interconnected.

It is not necessary, useful, or realistic to make a single pass through the process from idea to solution. A single pass through the six steps of the Scientific Method produces at best a C solution, complex, and uncreative. However, it is productive to be systematic about iterations. Feedback is essential to all decision making processes. Feedback uses the interim results from an action to modify the action itself until the final result is successful.

For example, we use feedback to drive an automobile. To control the car's speed we push on the accelerator or the brake. To control its direction we turn the steering wheel. However to drive at an intended speed, we use our eyes to observe the car's speed, compare that to our desired speed,, and then appropriately modify our foot's pressure on the accelerator or brake. To steer the car we observe our direction, compare it to our intended direction, and appropriately turn the wheel to bring the two into sync. In effect we drive through a continuous feedback process of *observe-judge-act-observe-judge-act.......*

It would be asinine to drive without feedback and instead to specify at the beginning of the trip exactly how hard to push the accelerator or how far to turn the steering wheel at each moment of the trip. Traffic conditions, weather, road conditions, a flat tire, or a host of other (context) variables require us to modify our speeds and direction of travel for each trip.

Amplifiers in radios, and TV sets employ feedback to produce stable, desired audio and visual outputs in spite of drifting input signals, noise, and continual changes in the characteristics of their own components. In fact, the diagram of Fig. 2.2 is quite similar to a diagram for a three stage amplifier. If I added the feedback loops that are actually within each step of the processes, it would be even more similar.

It's absurd not to use feedback to develop a business plan, to design a product, or to create and manage a marketing system. A competitor's actions, a new technology, a change in customer requirements, a change in our own staffing or organization, or a host of other things might require us to modify our objectives, products, or marketing systems as we develop them and as we manage them.

Feedback is at the heart of the Scientific Method, improving human judgment. In fact what people are doing is cycling through the sequence: Observe, Judge, Act, and Repent.[4] Repenting is merely re-observing and modifying judgments. So, the truth of the matter is that the Scientific Method is really nothing more than systematized and legitimized "**trial and error,** and correction."

Specification centered: Specifications are critically important tools of the scientific method. They systematically document needs and contexts in a way that enables us to separate them for analysis and then successfully reintegrate them. Specifications are like scalpels and sutures that enable skilled practitioners to cut apart and join together. However, specifications are not effective when they are too detailed, because excessive details obfuscate important factors and their priorities. Specifications must clearly spell out the critical factors, convey a general sense of the secondary ones, and skillfully ignore an infinite number of trivial issues. Excessive detail comes from bureaucratic efforts to identify every factor, important or trivial.

Examples of Specifications in Business:
- Marketing specifications
- Product specifications
- Job Descriptions
- Mission Statements
- Business Plans
- Data Sheets

Specifications are not effective when they remain static. They must be modifiable by feedback. They are only as good as the judgments (educated guesses) of those who produced them at the time they were produced. New information, innovation, and simplifying assumptions will improve the specifications and through them the results.

Specifications also enable us to use ready-made solutions or ready-made elements. When engineers design a product they use the data sheets of components from other companies to design these components into their own product.

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[4]For further discussion on this process see the essay in Appendix A: Effective and Meaningful Jobs

Well defined specifications have three elements: Benefits, Features, and Functions. Conceptually, the Benefits define the object in terms of its contexts. The Functions define the object in terms of its elements and detailed characteristics. The Features link the Functions to the Benefits. In Product Specifications, the Benefits define the values of the product to the customers, the Functions describe in detail how the product works, and the Features describe how the product applies the Functions to produce the Benefits. For example, a Benefit of a car might be that it's safe. Related functions might include anti-lock brakes, built in roll bars, safety belts, and air bags. Features that tie the two together might include a claim that the car won't skid on wet pavement when you slam on the brakes and statistics on driver and passenger safety for head-on collisions at 25 mph.

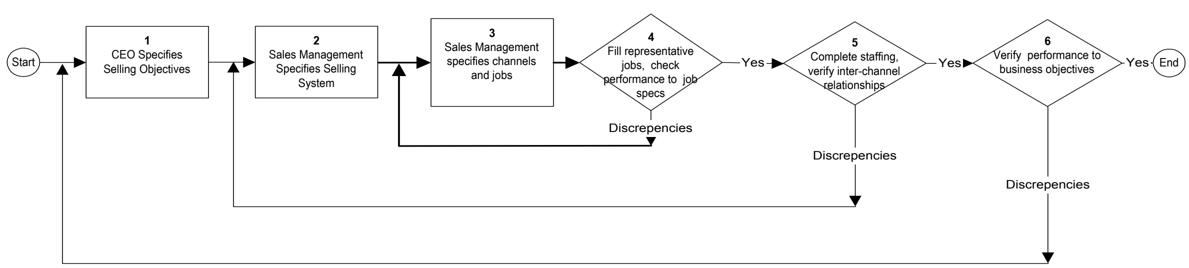
As we will see throughout this book, specifications enable manufacturers to sell, customers to buy, managers to manage, and subordinates to succeed.

Structured and modular: Each step in the Scientific Method has a specific, limited purpose so that it can be successfully managed. A step in the process is itself an object linked to the rest of the process (its context) in a specified way. People get into trouble and their judgments are overwhelmed when they skip steps or intermingle them. For example, when people omit specifications, they usually wind up with faulty solutions. When they attempt to debug element solutions (step 4) during a system test (step 5) they become tangled in an astronomical number of combinations and permutations. Then, bugs slip through the process. (The math bug in Intel's Pentium processor is probably a result of debugging the math module after it was imbedded in the rest of the chip.)

Facilitates teamwork: When a complex hypothesis is divided into well-specified modules, different people, teams, or companies can work on different modules simultaneously and confidently expect their results to fit into a coherent solution.

Using it to Design and Manage a Marketing system

The following is an overview of how to use the Scientific Method to help develop an effective marketing system. In Section 3 of this book we'll add depth and detail to this picture.



Step 1: *Executive management specifies sales objectives* in the context of: business plans, executive expectations, products, target customers, and the marketing system specification.

Step 2: *Sales management specifies a marketing system* in a context that includes: markets, products, channels, competitive alternatives, and the specified sales objectives.

Step 3: *Sales management partitions the marketing system into an organized structure* that includes sales channels, business entities, and jobs. Each of these elements is specified: its key objectives, its job descriptions, and its principal relationships to the rest of the organization.

Step 4: *Sales Management selects and manages (prototype) people and channel organizations* to fit the specified functions and to achieve the specified results.

Step 5**:** *Sales management systematically completes staffing* as it validates effective interaction among jobs, organizations, and channels.

Step 6: *The overall effectiveness of the marketing system is validated by its results in the real world.* Discrepancies between results and plans are used to update the plans and/ or to modify their implementation.

To Modify an existing marketing system

Any ongoing business already has a marketing system that generates revenues essential to its survival. How can it be overhauled without undermining day-to-day operations? It isn't easy! A friend of mine described the problem as "repairing a bike while riding it... downhill." However, skillful use of the Scientific Method makes the process as easy as possible, but not easier.

The first step is still to specify the marketing system's objectives. In the second and third steps, the effective people and organizations in the current system are treated as resources for the new solution. At step 4, any changes in the marketing system are carefully prototyped and thoroughly tested in field trials before being adopted system-wide. Later chapters describe how to carry out these changes effectively using specific types of decision-making people.

Solving sales management problems

The Scientific Method suggests more productive ways to solve sales management problems. For example, suppose that 30% of the field sales people chronically fail to make their sales quotas. The traditional solution is first to threaten the individuals and organizations, then to fire them and hire new ones in a perpetual search for the "right" people. However, in terms of the Scientific Method (See Figs. 2.2 and 2.6) a chronic failure to meet sales quotas is at step 6, and the solution process begins with a return to step 1. We re-examine quotas (even the idea of quotas), market objectives, job descriptions, hiring policies, and agreements as the first step in solving the problem. This process takes more planning and requires executives and sales managers to take more than their customary responsibility for undesirable results. But, in the long term, it produces real and lasting solutions, and it reduces firefighting, job stress, and overall workload.

Short Cuts

We're all faced with a huge number of business decisions. It's not practical to proceed formally through the Scientific Method for most of them. We take shortcuts whenever we can. Most of the time we simply make an educated guess about the answer or simply do what we did last time, implement our guess, and live with the consequences. Usually the results are good enough. Other times we try out two or three conveniently available or readily apparent alternatives and pick the one that seems to work the best. We correct our "mistakes" when we have time and if they hurt enough. Without taking shortcuts, we'd squander our limited time and talents formally evaluating a host of relatively trivial issues.

We usually apply the Scientific Method more thoroughly when the issue is both critical to us and inherently complex. A successful marketing system is a critical business issue. It is inherently a complex system of people, methods, and materials. Its design and management are worth relatively formal applications of the Scientific Method.

Exercises

1. Based on what you already know and with a liberal use of your gut instincts, where do you place your company's marketing system on the curve of Figure 1.2? Identify and list the five to eight most significant reasons which support your judgment. (Suggestion: make the estimate first, then develop the list of reasons.) As you gain more insights from studying this book, periodically review your estimate and your list of reasons. I think you'll be pleasantly surprised about the accuracy of your initial estimate, but you'll probably change some of the reasons.

2. With your company's "marketing system" as the object, develop a list of its top 10 contexts. Make notes of assumptions or educated guesses you made to get this list.

3. For what job related problem do you come closest to using all the steps of the Scientific Method?

4. Under what conditions do you take the most shortcuts in job related problem solving, objective setting, choice of working methods, and choice of personal relationships?

3. How to Motivate and Manage Decisions

"If you give a prospect a reason for buying, he might buy. If you give him an excuse to buy, he might buy. But if you give him a reason and an excuse for buying, then make it easy for him to buy, your chances for a sale are dramatically increased." Zig Ziglar

How do we motivate people to buy our products? How do we motivate sales professionals in channel organizations to sell our products? How do we get ourselves and others to work for our objectives and to act in our best interests? In this chapter and in Chapter 4 we develop generic answers to these questions and develop fundamental principles and tools for managing decisions. In Section III, Where the Rubber Meets the Road, we apply these principles and tools to specific incentive and management programs.

Business decisions are made to fulfill needs: rational business needs and individual personal needs. Many technologists and academics assume that all decisions are (or ought to be) made strictly to meet rational business needs. Many sales professionals and sales executives assume that all decisions are made to meet personal needs

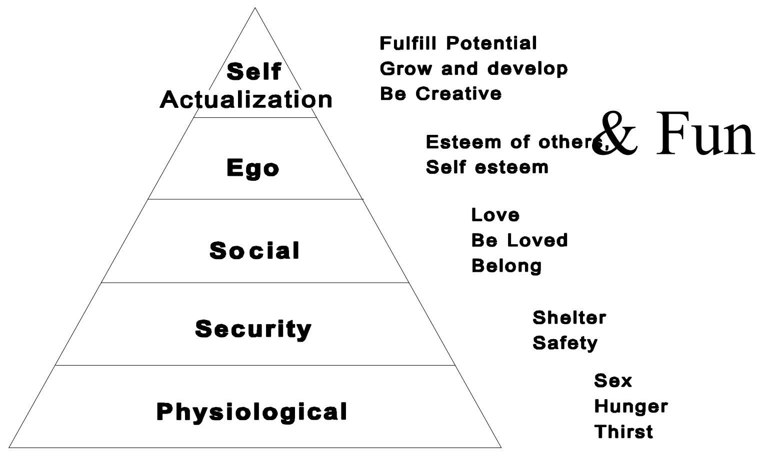
The rationalists subscribe to Management by Objectives (MBO) and the *better mousetrap* theory of sales. Management by Objectives asserts that if you clearly define your objectives, people will work to achieve them. The better mousetrap theory says that if the product meets the customer's technical requirements better than alternative products, it will sell itself. Both theories say the same thing; both are partially true and largely inadequate. However, executives who believe in them conclude that good products sell themselves and the sales force is overpaid to distribute product literature and collect orders.

The personalists subscribe to the *wine and dine* (or shmooze and booze) theory of management and selling: establish trust and confidence with employees and prospects, and you can get them to do anything or sell them anything. They expect the sales force to achieve its quotas through personal relationships, with or without competitive products or technical support from the factory. There is some truth to this view, but it too is grossly inadequate.

In this chapter we'll study our own personal needs and their impact on our business decisions; to buy products, achieve objectives, use specific methods, and associate with specific people. I'll describe Maslow's hierarchy of human needs and add the vital need that Maslow left out, the need for fun. Then I'll use these needs to explain a new management tool: *Management by Personal Attractors*. Finally I'll introduce the *Principle of Three to Five*, a simplifying concept that applies to Personal Attractors, product characteristics, process characteristics, business objectives, and human relationships.

Maslow's Hierarchy of Personal Needs

In the 1950s, Abraham Maslow grouped personal needs into the five-level hierarchy shown in Fig. 3.1. He said that we act to fulfill our needs in a definite sequence of priorities. He concluded that we must satisfy our Physiological needs of hunger, thirst, and sex before we address the other needs. When we satisfy our Physiological needs, we add the Security issues of shelter and safety. Then we address our Social needs including the needs to belong, to be loved, and to love. After we meet our Social needs, we turn to our Ego needs of self esteem and the esteem of others. Finally, after fulfilling all the lower level needs, we use our remaining energies to Self Actualize: to be creative, to grow and develop, and to fulfill our potential. According to Maslow, some people seldom or never operate in the higher levels of the hierarchy, because their energies are consumed satisfying more basic needs.



Needs may be natural or neurotic. We can reasonably satisfy natural needs. Neurotic needs are insatiable. A natural hunger is satisfied by eating. A neurotic hunger endures after a full meal. A neurotic need for security can produce endless efforts at self protection, perhaps to the exclusion of all else.

We usually make specific personal or business choices to satisfy more than one need. For example: I eat lunch to satisfy hunger. However, I choose to eat a specific lunch at a Greek restaurant near work to satisfy hunger, to satisfy my need to be creative by trying Greek food, and to satisfy my need to belong by eating with colleagues at work. At another time, I might eat lunch at home in order to eat familiar food and to be with my family.

The need for fun

Funny thing happened to Maslow on his way to the hierarchy: he forgot his need for fun. Fun is one of the most significant needs of mature, healthy people. I suspect his omission came from a cultural bias of academia that work and fun are separate things. However, when we are most effective as individuals or as members of successful teams, we have fun working and we relish achieving our objectives. Fun and playfulness enhance our teamwork and contribute to our successes. We enjoy a good meal, working with friends, a successful business, a good marriage, and healthy sex. We usually enjoy the process of buying and would prefer to enjoy the process of selling.

We playfully live healthy personal lives, deeply satisfying relationships, and successful teamwork. Our playfulness enables us to relish diversity and competitive alternatives for ourselves and others. I'm convinced that playfulness, not education, is the primary source of tolerance. We can playfully empathize with others without having to decide who is right and who is wrong. Fun and playfulness cross all levels of Maslow's hierarchy for mature, healthy people, and are integral to fulfilling needs.

People who separate work and fun aren't healthy. Fanatics are people who are intense but not playful about their causes. They are attracted by fear and hatred instead of by fun and enthusiasm. Eric Hoffer wrote *The True Believer* a profound study of fanaticism. In it he said: "*Mass movements (of fanatics) can rise and move without belief in a God, but never without belief in a devil.*"[5] Because fanatics are deadly serious about their

[5] Eric Hoffer, *The True Believer*, p 91, Harper and Rowe, 1951

causes, they create devils and use them to motivate themselves and their followers. Their causes are the ultimate, simplistic, contexts by which they judge everyone and everything else. Other people are either loyal followers who sacrifice everything for their causes, or devils who must be destroyed.

In this respect, business fanatics are the same as political fanatics or religious fanatics. They are not playful about work or business success. Winning at business becomes the measure of their lives. They demand that employees become their loyal followers. They treat competitors like devils.

Management by Personal Attractors

I'm going to use Maslow's ideas about human needs and the human need for fun to help explain a new, useful idea: Management by Personal Attractors. I developed the idea in part because Management by Objectives (MBO) is inadequate; it only works some of the time. To paraphrase Zig Zigler, MBO is the reason to perform without the excuse to perform. Management by Personal Attractors involves both. In later chapters, its principles will be used to identify simpler and more effective ways to develop and maintain commitment in the marketing system, to implement changes, and to stimulate sales.

I'm going to start with a working definition of personal attractors, one that describes them by their effect on people. If this kind of definition seems inadequate, please bear with me. The definitions of electricity and gravity are also descriptions of effects, not of substance, but they are nonetheless valuable scientific concepts:

Working Definition of Personal Attractors

> *Personal Attractors motivate each of us to actualize specific futures: to buy specific products, work for specific objectives, use specific methods, and associate with specific people.*

Personal attractors are generated by our personal beliefs about which choices will satisfy our unmet needs. For example, when we are hungry (unmet physiological need) then food in front of us creates a personal attractor because we're convinced that eating that food will satisfy our hunger. When we aren't hungry, the same food no longer has that personal attractor because we no longer have that unmet need.

Characteristics of personal attractors:

Totally subjective: Based on our individual needs and beliefs. What actually "is" doesn't matter. What we believe or are aware of does matter.

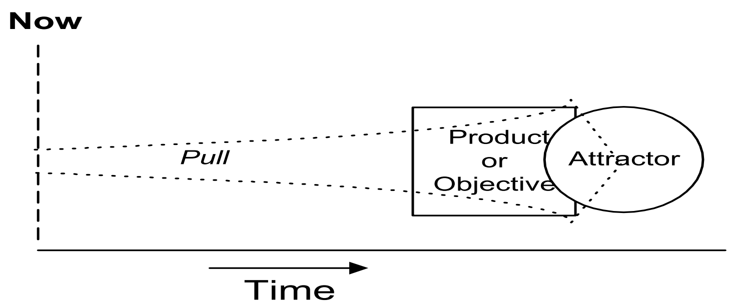
Change with time and circumstance: When a need is urgent, its personal attractor is strong. When it's satisfied, the personal attractor is weak or non-existent.

Associated with choices and commitments including:

a) **Products:** what we buy and use
b) **Objectives:** what we work to achieve
c) **Processes:** the methods we use
d) **People:** those with whom we associate

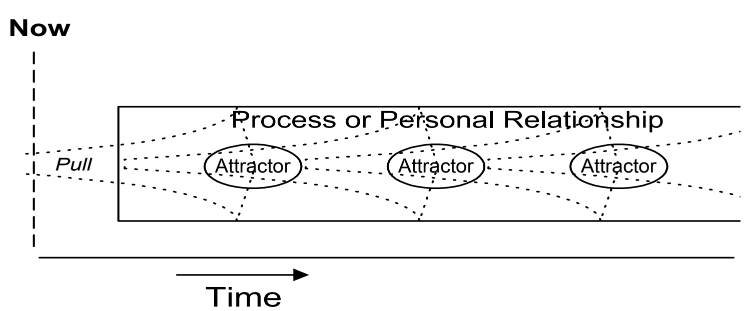
A Personal Attractor's pull

A personal attractor works like gravity or a magnet; it exerts a pull that draws our thoughts and actions in a specific direction towards a specific future. It operates as though it were a something located in our personal future, drawing us to make that specific future happen. (See Fig. 3.2.) The nearer in time it appears to be, the greater is its pull. Personal attractors related to a product or objective pull us to buy that product or achieve that objective.



Personal attractors related to a process, such as working in a specific job, or to relationships with specific people, are connected to needs that are repeatedly met by them. (See Fig. 3.3.) The process or relationship creates a series of pulls lined up within a course of action.

The strength of a personal attractor's pull to actualize a specific choice is proportional to each of the following factors:



1. The priority of the unmet need: According to Maslow, the priority of an unmet need depends upon our character and maturity. However, the priority may also depend upon the facet of life we're focused on such as work, home, vacation, or sports; and upon whether we're dealing with products, objectives, processes, or people. We usually emphasize Self Actualizing needs in one set of contexts, Social needs in another, etc. We do this in part to create a manageable number of variables in various compartments of our life (subconsciously applying step 2 of the Scientific Method). However, when we have a neurotic need, it may have a high priority at all times and in all facets of our lives.

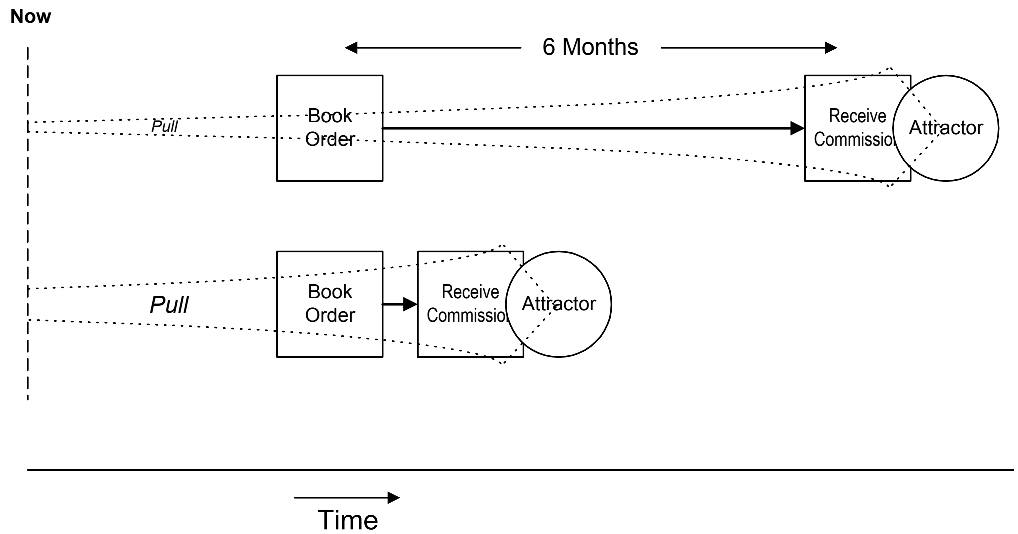
2. The magnitude of the unmet need: The magnitude of an unmet need depends upon how well we usually satisfy it. The magnitude of hunger or thirst varies hourly, swinging back and forth from complete satisfaction to substantial need. However, if we recently ate and we usually know where our next meal is coming from, the overall magnitude of hunger is much less than if we are starving. The magnitudes of other needs, such as ego needs or belonging, vary at much slower rates. A neurotic need is usually substantial and consistent.

3. The degree to which the choice appears to satisfy the need: If the choice looks as though it provides full satisfaction, the pull is stronger than for partial satisfaction. If we're very hungry and our options are a slice of bread or a full meal, the hunger personal attractor related to the full meal is stronger.

4. The clarity and certainty with which we see the personal attractor and its relationship to the choice: In some situations, like eating food in front of us, it's clear that we'll satisfy our hunger and the personal attractor's pull is strong. But the pull is weaker when we're unclear about our objective, or if we doubt that achieving the objective will satisfy the personal attractors. For example, suppose we're hungry and a person promises to give us dinner if we chop a cord of wood. The pull of the hunger personal attractor to get us to chop the cord of wood is also proportional to that person's credibility with us.

5. The nearness of the personal attractor in our future, as we see it: It is the immediacy of the personal attractor that's important, not the immediacy of the objective, product, process, or personal relationship. In general, a personal attractor has the most pull to implement a specific choice when it's concurrent with buying the product, achieving the objective, or participating in the process. The hunger personal attractor for food on a plate in front of us exerts a stronger pull than the one for food that we buy to eat tomorrow. The hunger personal attractor is actually connected to when we expect to eat the food, not when we buy it.

Managers commonly use sales commissions to motivate their sales people to book orders. Fig. 3.4 illustrates the differences in motivation, the pull of a personal attractor associated with the commission, as a function of when that commission is paid. When it is paid immediately after the order is booked, the motivation to close the order is stronger than when it is paid six months later. In fact, the attractor for the commission paid later continues to operate after the order is booked. It motivates the individual to spend time and energy to make sure he gets paid. It may even compete against the individual's motivation to book other orders!



While we pursue long-term objectives, we can experience strong personal attractors from less important but much shorter term alternatives. These personal attractors can be strong enough to sidetrack our commitments to longer term objectives.

Money and Personal Attractors

Money is worth taking a close look at. It is the medium of selling and a tool of business management. It is used by management in the form of paychecks and commissions to motivate workers. However, ***money is not a personal attractor***. It is a unique product that each of us automatically connects to various and sundry of our personal attractors. We know without thinking that when we get money we can immediately buy food and satisfy hunger, or drink and satisfy thirst, buy or rent shelter and satisfy the need for safety, etc. Saving money also has personal attractors for most of us because it increases our sense of security or preserves our freedom to spend it later to satisfy other needs.

The commission money paid in Fig. 3.4 has one or more personal attractors for almost everyone. However, the specifics of what they are and the intensity of their pull varies from one individual to the next. They may also vary over time as an individual receives money from other sources and as other products, objectives, or processes meet his needs.

The collective strength of money's personal attractors produces an individual's overall sense of value for any specific amount of money. The more money a (non-neurotic) person has, the less any specific amount satisfies needs and the weaker the personal attractors related to it. The pull of personal attractors related to $100 is stronger for a person who is destitute than for a person with $1 million. The destitute person is unlikely to spend the $100 on anything but essentials that satisfy Physiological and Security needs.

One of my college psychology courses included an evaluation of money's use as a motivator. In one case-study the military employed Eskimos to help construct an airbase in the far north. However, few Eskimos were willing to work, and those who did only worked for a few days or weeks. Somebody decided to solve the problem by paying the Eskimos more money. It made matters worse because they quit sooner. It turned out that they had very few needs that money could satisfy. They worked until they got just enough money to satisfy specific needs; then they quit. Additional money had no personal attractors for them.

The processes through which we get money can also have personal attractors. For example, when we receive salaries as members of business teams, the money reaffirms that we belong. When we believe that our salaries reflect management's respect for our contribution, it satisfies our need for the esteem of others and increases our self esteem. However, when we, or people we work with, get paid for doing nothing, being paid doesn't satisfy our social or ego needs. We'll address this point later in the book when we discuss sales compensation programs.

Welfare's chronic defects are related to how welfare recipients are paid. Welfare can satisfy security and physiological needs with money, but its method of distribution destroys essential opportunities to satisfy social and ego needs. Welfare requires its recipients to wallow in perpetual failure in order to receive money. The crooks who misuse welfare to rip off the system have actually been creative enough to get the money in a way which satisfies their ego and fun needs!

As I write this, the 1994 baseball season has gone down the tubes and the 1995 season is at risk. Multi-millionaire players and owners are ostensibly fighting over money! They are actually fighting over the basis on which it is distributed; whether it reflects the free market value of the player (ego need) or is "socialized" with a salary cap. They are also fighting over the relative statuses (ego needs) of owners and players.

Competitive Alternatives

> ***A competitive alternative to a decision is any other combination of products, objectives, processes, or personal relationships which has sufficiently strong personal attractors to draw the individual to actualize it instead.***

When we try to get a prospective customer to buy our product, the prospect's competitive alternatives are any other combination of products, objectives, processes, or personal relationships which he views as attractive substitutes. When we try to get a sales professional to book orders for our products, his competitive alternatives are any other combinations of orders, objectives, processes, or personal relationships which he views as attractive substitutes for his time and talents.

Competitive alternatives are essential to all of us. Without them we can't choose, and *freedom to choose* satisfies Social, Ego, or Self Actualizing needs. Freedom to choose is so essential in buying that sales agents learn closing techniques which create artificial alternatives for the prospect. "Do you want your car in black or in red? Do you want it with or without a stereo system? Do you want to drive it off the lot, or have it delivered?"

Competitive alternatives can be overdone. Too many of them confuse us and slow down decision making. I suspect that the optimum number of competitive alternatives from the individual's point of view is between three and five! Fewer than three and the choices are too limited, more than five and they are too confusing. As we shall see later in this book, we create competitive alternatives for customers when we sell our products through more than one sales channel. This may be helpful in moderation, but can be destructive in excess.

A point that cannot be overemphasized:

A manufacturer's competitors and a customer's competitive alternatives are not the same things.

Managers, including CEO's who focus exclusively on the companies they compete with in the marketplace make serious mistakes. Prospects buy a specific product based on their competitive alternatives (which might include not to buy at all and to make rather than to buy). Furthermore, sales professionals actively sell or don't sell specific products based on their personal competitive alternatives. Most of these alternatives have nothing to do with the manufacturer's business competitors!

The Principle of *Three to Five*

The Principle of *Three to Five*

A person will usually choose a product, objective, process, or person which satisfies three, four, or five strong personal attractors.

This principle is particularly true for significant choices for which there is time to consider competitive alternatives. When a specific choice has only one or two personal attractors for an individual, the decision maker usually has numerous competitive alternatives for which those attractors are equally strong. The probability that she will make a specific choice because of that attractor is very low. For example, if I only wanted to satisfy my hunger at lunchtime, I could eat at any number of restaurants, go to MacDonald's or Burger King, make my own lunch, or skip lunch and wait for dinner. The chances that I'll choose to eat at a particular restaurant solely because I'm hungry are slim to none.

However, when an option holds three to five strong personal attractors, it has few competitive alternatives and I'm likely to chose it. For example, if I'm aware that there's a decent Greek restaurant near work, then when I'm hungry, want to enjoy the company of friends for lunch, and we all thoroughly enjoy Greek food, we'll probably eat lunch at that restaurant.

If an option tries to satisfy more than five personal attractors, it will only partly satisfy each of them, and the pull of each attractor will be weaker. What I usually choose instead (as a competitive alternative) are two or more options, each of which satisfies three to five personal attractors well.

Let's illustrate this point with a product example: a vehicle. The characteristics of a vehicle that might hold strong personal attractors are:

- Built like a tank (safety)
- Highest gas mileage (security)
- Fastest acceleration (adventure, ego, fun)
- Styling (social, fun)
- Comfort (physiological)
- Seats six adults (social)
- Rugged, four-wheel drive (self actualization, fun)
- Inexpensive (Security, personal attractors related to competitive alternatives for the money)

No single vehicle can be best at all these characteristics. A vehicle can be designed that is the cheapest or gets the best gas mileage when all other characteristics are ignored. That vehicle would get an A (letter grade) for satisfying the one characteristic and would have the strongest personal attractor for the related need. However, when a design combines two or three characteristics, each one must be compromised to accommodate the others. The average grade among three to five characteristics in one product is at best a B. By the time six characteristics are incorporated in a single vehicle, few (if any) of them come close to their optimums. Their average grade is at best a C, and related personal attractors are weak because the needs are only slightly satisfied. For example: To get highest gas mileage, you can't build the car like a tank, or give it decent acceleration, styling, comfort, seat six adults, etc.

As a result, the automotive industry builds a variety of specialty vehicles: sports cars, minivans, pickup trucks, full sized sedans, and luxury cars. Each of them best fulfills different combinations of three to five specific needs. Many people buy two or more kinds of vehicles to satisfy their needs.

Industry standards usually satisfy three to five critical needs at a B level. They seldom are the best solution for any specific need. The DC-3 airplane was an example of this. The DC-3 wasn't the fastest plane of its time. It didn't carry the heaviest loads. It didn't have the longest range. But it had the best combination of speed, load carrying capacity, and range, and thus became a successful commercial standard for over 20 years. The IBM PC and its clones form another industry standard that isn't the best in any technical or physical characteristic, but has held a 90% market share for more than a decade.

An example in which "management" successfully used three to five personal attractors to achieve an objective comes from Desert Storm. The objective of Desert Storm was to drive Saddam Hussein's troops out of Kuwait. Now consider this question: What motivated the American GIs in the trenches to train for months in the desert and then one morning to conduct an assault across enemy minefields, endure enemy fire, and risk life and limb to achieve that objective? It certainly wasn't the stated objective of driving out the Iraqis (as MBO would suggest). Only a handful of fanatics might risk life and limb to drive strangers out of a strange land, no matter how clearly the objective was articulated.

For most of the soldiers, there were three personal attractors that were so strong that fighting was the only option! The first personal attractor was on the lips of every GI interviewed just before the battle: "*The sooner we drive the Iraqis out, the sooner we can go home.*" By the time they launched the attack, the soldiers had been away from home for months and their longings for home were intense. George Bush had promised them a swift return home, just as soon as their mission was accomplished. But, had that been the only personal attractor there would have been other (competitive) options to waging an attack. The most obvious one: desert and avoid any threat to physical safety.

However, the military had also created social personal attractors for each GI through the buddy system. The military units had trained together, went to Saudi Arabia together, and would return home together. The GI's were buddies (social, belonging, ego). So each man's concept "we can go home" really meant everyone in his unit, in one piece. This reduced his competitive alternatives to: a) train and fight as a unit and achieve the objective with as few casualties as possible or b) have the entire unit desert or refuse to go into battle. But fighting was the only alternative that satisfied other powerful personal attractors: being socially accepted back home, respect of friends and family, feeling self worth, etc. The GI was left with only one viable choice: to fight and to risk his life.

In this situation the soldiers' personal attractors were so strong that they overwhelmed horrifying obstacles and they achieved their objectives. That is the essence of management by personal attractors.
The *Principle of Three to Five* highlights a key problem with centralized planning or market dominance: each centrally planned objective or market dominant product must incorporate far more than five personal attractors in order to get the support of enough constituents, unless those constituents are conditioned to have identical personal attractors (as in the case of the military). When an objective or product is compromised to

gain adequate support, it ends up doing nothing well. This is a problem that plagues large companies, academia, trade associations, and governments.

Reasons to manage by Personal Attractors

The concept of Personal Attractors helps explain our own choices and commitments, and those of other people. We are continually tugged at by various and sundry personal attractors. We don't go through life satisfying one need at a time and being influenced by one personal attractor at a time. We are influenced, motivated, attracted to a plethora of choices in business, family, and social settings. We're drawn to most choices by several personal attractors. Even when we focus on business, we are still drawn by personal attractors in other parts of our lives, and they subtly affect business decisions. When a particular need is fully satisfied in family life, business objectives hold no significant personal attractors for that need. When we become aware of personal attractors and account for them, we can better understand how to manage ourselves and others.

Personal attractors have the same function in human behavior as "*strange attractors*" have in the behavior of physical and biological systems in *chaos theory*.[6] Strange attractors motivate all self-organizing systems. All physical and healthy biological systems are influenced by two or more strange attractors which produce conditions in which their behavior is somewhat chaotic, that is, slightly or completely unpredictable in terms of conventional analysis. However, within the regions of chaos there emerge robust, complex, self-organizing systems. Silicon Valley is a self-organized system; so is the human brain, Internet, and a rain forest. Markets, selling systems, and companies are largely self-organized around common personal attractors.

Management by Objectives ignores this reality and attempts to define and control everything in terms of logic and reason. MBO creates plantations, like IBM and DEC, which lose natural robustness from over-organizing. Plantations disintegrate when the plantation masters fail to keep employees, investors, or customers in line. Management by Personal Attractors combines rational methods with chaos theory's newfound understanding of self-organization to make management easier, more successful, and more satisfying for all concerned. I'm reasonably certain that personal decisions and the underlying patterns of human commitments are describable with the mathematics of chaos theory. However, in this book we'll stick to basics and eschew the mathematics.

The bottom line

You have three competitive alternatives in how to manage yourself or others:

> **1. Select the persons for whom your objectives (products, processes, or personal behavior) hold powerful personal attractors:** Ask questions and learn what the person's three to five most significant personal attractors are and how strong they are for your desired outcome. Then, select only those people for whom your objectives (products, processes, or personal behavior) have the strongest personal attractors. (Market segmentation, niche marketing, and *Selection by Personal Attractors*)

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[6]For an excellent, fun, and easily readable book about chaos theory read *A Turbulent Mirror*, by John Briggs and F. David Peat, Harper and Row, 1989.

2. Modify your objectives (products, processes, or personal behavior) to adequately satisfy three to five of their personal attractors: Ask questions to learn what the person's three to five most significant personal attractors are in this facet of his or her life. Learn how strong his/her personal attractors are for your objectives. Also learn what the person's competitive alternatives are. Then, adapt your objectives (products, processes, or personal behavior) so that they have the strongest combination of personal attractors for that person. (Solution selling, or *Management by Personal Attractors*)

3. Indoctrinate the individuals to believe your objectives (products, processes, or personal behavior) hold powerful personal attractors: Conduct a massive, systematic indoctrination program that tries to produce a standard, favorable set of personal attractors for what you want. (Military training or massive advertising campaigns, *Conditioning of Personal Attractors*.)

Each of the three approaches works best in some situations, but some combination of all three of them is usually the most practical. For business, the best approach is normally Alternative 1: carefully select employees, sales professionals, and customers for whom your products and business objectives old powerful personal attractors.

Exercises

1. What are your strongest personal attractors at home, at work an in your spare time in each of these areas: process, objectives, personal relationships?

2. What are the strongest personal attractors for individuals with whom you work effectively: for work processes, for business objectives, for personal relations?

3. What are your boss's strongest personal attractors in his/her key objectives and processes? What are his/her's strongest personal attractors in working with you? (Follow up question: How can you be sure of your answer unless you discuss it with your boss?)

4. What are the strongest personal attractors of key sales professionals in your marketing system for meeting your sales objectives? (If you identify one set of personal attractors for everyone, odds are that you're wrong. Ask.)

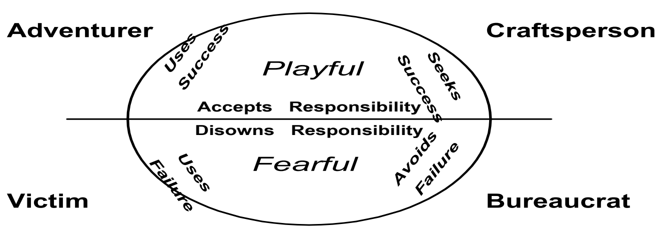
4. Decision-making Attitudes

"*Work like hell, tell everyone everything you know, close a deal with a handshake, and have fun"* Harold E. "Doc" Edgerton
"I was an abused husband" attributed to O.J. Simpson

This chapter describes four primary attitudes that all decision makers, including ourselves, adopt at one time or another. Each attitude is related to a cluster of personal attractors. We can more effectively motivate an individual or influence her decisions when we're aware of which attitude she has adopted when making them. If it is your company's policy to treat all customers the same, read this chapter and you'll learn how and why its is more profitable to treat them differently on the basis of their decision-making attitudes.

Overview

Chapter 3 described how clusters of three to five strong personal attractors tend to motivate specific actions or decisions. Most of us habitually focus on a specific cluster of needs in business, another cluster of needs in family life, another while driving, another in recreation, etc. We do this partly from habit and partly to compartmentalize and simplify our lives , a la step 3 of the Scientific Method. Each cluster of needs produces a corresponding decision-making attitude (see Fig. 4.1). In this chapter I'll describe four primary attitudes to which I've given the names: Adventurer, Craftsperson, Bureaucrat, and Victim. I'll explain these attitudes, the



specific needs they satisfy, and how they affect our decisions as buyers, sellers, and managers.

Adventurer: An Adventurer uses success and risk to satisfy fun and self-actualization needs. Success is a resource to be used to develop more risk and more success. Risk is a spice of life, a challenge to be enjoyed and overwhelmed, not something to be feared. Living with risk is a process that satisfies major attractors. An Adventurer succeeds and fails often, but assumes personal responsibility for his or her results. An Adventurer usually has a weird sense of humor about his/her adventures. Adventurers include innovator and early adopter customers, and the CEOs of most startup companies.

Craftsperson: A Craftsperson prudently seeks *success* to satisfy Ego, Social, and Fun needs. Risk is deliberately minimized, but not feared. It holds no attractors. A Craftsperson takes more time and is more thorough than an Adventurer in order to reduce risk and to produce a more certain success. A Craftsperson accepts responsibility for the outcome whether it succeeds or fails; has a sense of humor about his/her craft. The majority of consistently successful engineers and scientists are Craftspeople in their professions.

Bureaucrat: A Bureaucrat studiously *avoids failure* in his immediate future to satisfy Security, Physiological, and Social needs. Risk is frightening. He'd like to be associated with success as a buffer against failure, but that's secondary and incidental. The objective that contains his primary attractors is: "Zero risk of being held responsible for failure," in his own mind or in the minds of others. A Bureaucrat attaches himself to external systems and develops a personal thought structure that insulates him from responsibility for failure. Bureaucracies are simply external manifestations of a Bureaucrat's protective mental system. A Bureaucrat is attracted to large, well funded organizations with copious checks and balances that eliminate personal accountability for failure. Knows how to say "no" or how to avoid decisions, but has difficulty saying "yes." Usually lacks a sense of humor about his bureaucratic self and his bureaucracy.

Victim: A Victim (or as I prefer to say a *Professional Victim*) uses *past failures* to satisfy Physiological and Security needs. The Victim embroils himself in past failures but denies any responsibility for them. He uses them to demand that he be given special benefits. He is attracted to social systems that justify his behavior and reward his demands. Drinking alcoholics, drug addicts, minorities, and criminals are considered Victims in our society and are compensated in ways that reward Victim behavior and penalize Craftsperson or Adventurer behavior. Lawsuits provide financial rewards to people who assume a Victim's attitude, and to the lawyers who manage to latch on to them. The Oprah Winfrey show pays money to a parade of Victims who exhibit themselves on television. Victims have no sense of humor about their condition. They are negative and blameful.

These four attitudes are part of a continuum, like the four directions on a compass. All of us operate from each of these attitudes and from points in between at different times. We may be Adventurers in our hobbies and Craftspeople at work. Most of us are Bureaucrats when we drive[7], doing what it takes not to have an accident or get a ticket. If either one occurs, we are likely to assume a Victim's attitude in order to avoid the consequences or to derive the most financial benefit. We learned how to be Victims when we were children. When we got sick or hurt ourselves and cried (Victim behavior), our mothers gave us special attention. If we didn't whine, we didn't get the attention.

Each attitude pays off and there are conditions under which it is a helpful behavior. Sometimes we adopt one that seems inappropriate to other people. A few of us become stuck in one attitude, adopting it in most facets of our lives, unable or unwilling to shift as circumstances change.

[7] Although some teenagers are Adventurers as drivers.

Adventurers

Leaders, advocates, entrepreneurs, explorers, pioneers, risk takers, technical innovators, early adopters.
Primary motivator: Fun associated with risk and surprises. Adventure.

Adventurer technologists as customers

Adventurer technologists are highly competent innovators in their fields, prepared to take risks to be at the leading edge. They are the early adopters in their markets, ready to buy new products from new companies. They study the functional elements of a product's data sheets and schematics and figure out how to apply them. They prefer the most advanced products or product features available. They will gladly help a product's designers find and correct technical bugs in the product or its documentation if the designers will simply listen. Once they decide to use something they will make it work if that is at all possible. They will discover applications or desirable options for the product that its designers never thought of.

They take most of the responsibility (and cost) for fitting a product to their applications even if there are bugs in the product or its documentation. They highly value leading edge product functions and are willing to pay a premium for them. *(Probably don't need the product's operating manual.)*

Features

- The people to beta test a product. They will help to debug the product and still happily pay for it. Drawback as beta-testers: perhaps not thorough or picky enough to catch subtle problems.
- When Adventurer user-buyers are convinced your product is the best alternative, the economic buyers will seldom overrule them.
- Most likely to be in fast-moving, small- to medium-sized growth companies.
- Can be very profitable to a manufacturer because of their feedback and their referral sales, even if that manufacturer loses money selling to them and supporting them.
- A manufacturer must continue to innovate and stay ahead to sustain their interest and loyalty.

Downside Features

- They are less than 7% of the user-buyers in most markets.
- Because they take risks to be first, their projects (or companies) have higher than average chances of crashing and burning.
- Sometimes their opinions are persuasive but are misleading and unprofitable to the manufacturer relative to the needs of the bulk of the market.

How to sell to Adventurers

- Have products with one or more significant technical functions that are unique or state-of-the-art.
- Promote the unique technical functions to a general technical audience across all vertical markets. Adventurers will seize on the technical information and take the initiative to find you.
- Get to them early in your product's life cycle and early in their projects' life cycles.
- Supply them with data sheets and loaners.
- Connect them directly with design engineers and emphasize that you welcome their feedback. When they discover bugs, fix the bugs promptly and thank them.
- Bring them into the development process as alpha and beta testers.
- Continue to inform them first about product innovations and updates, and about other new products.
- Use them as reference sales to other Adventurers or to Craftspeople. ***Don't refer them to Bureaucrats; they will turn each other off.***
- Keep track of them as individuals over the years; **they are gold mines.**

Adventurer CEO's
CEOs who founded the companies they run are usually Adventurers. If their companies are in technical fields such as electronics, software, or biotechnology, the CEOs are almost certainly technologists in those fields. This is an asset to a company's marketing system in its early days, because the CEO and the early adopters think very much alike. The CEO's opinions about what early adopters want in a product and in its documentation are usually accurate, since he's talking about what he wants. These opinions become a liability later on as the market matures and most user-buyers are Craftspeople and Bureaucrats whose needs are significantly different. The Adventurer CEO may keep his company locked in an early-adopter selling mode.

Adventurer CEO's often run their companies by the seat-of-their-pants. Subordinates may become confused and ineffective, and a personal decision by the CEO frequently overrides all planning and logic. A manager's authority may rest entirely on how highly the CEO regards him instead of on his results, his job function or his competence.

Adventurer sales professionals
They enjoy selling new products to new markets and will sacrifice current income for the opportunity to do so, provided there's a challenge and a probable payoff. They are the best people through which to launch a new product or to open a new market. They are most effective selling to Adventurer or Craftsperson user-buyers. They are poor at dealing with Bureaucrat customers or at empathizing with their need for security. They are sometimes sucked in by Victims because of the challenge, the risk to save them, or because they mistake them for Adventurers.

Craftspeople
Professionals, sound thinkers, solid technologists, reliable achievers.
Primary motivator: Achievement, Success

Craftsperson technologists as customers
They study the product's features and systematically compare them with competitive alternatives. They expect that the product and its documentation are fully debugged, and that it will be delivered on schedule. They look for proof, before they buy, that manufacturers will meet those expectations. They take full responsibility for the product's fitness to their applications if the product meets its own specifications. They usually qualify second sources of products to improve certainty of meeting their technical objectives and of finishing their projects on schedule and within budget. Do not, knowingly, take major risks. Prefer proven products from reliable manufacturers rather than new products from new manufacturers. Look for products and solutions that maximize the chances of project success, even if it means taking more time to complete the project. They are realistic about the services required to fit the products to their applications and will negotiate realistic compensation for those services. *(Make good use of the product's manual.)*

Features
- Between 25% and 60% of user-buyers in a market.
- The pool from which most successful VPs of engineering come.
- Usually work for profitable, growing companies. Also found in "elite" teams in large companies.
- Team players or team leaders.
- Can qualify your product, but cannot assure its procurement. Their clout is on a par with the economic buyer's and can win on technical issues against competitive alternatives that are up to 10% cheaper. Won't win if an acceptable alternative is 30% cheaper.

How to sell to Craftspeople

- Promote the product's *application specific* features and its benefits in targeted markets and in general technical publications.
- Sell to Craftspeople when:
  a) Data sheets and user manuals are debugged and the product works reliably to its specification
  b) Product is consistently delivered on schedule
- Publish application notes with specific, technically detailed examples of successful use.
- Have a technical support system that is readily available with answers.
- Actively use the local salesperson to move the product's evaluation on a fast, successful track.
- Use satisfied Craftsperson technologists as references to other Craftspeople and to some Bureaucrats.

Craftspeople CEOs

Usually leaders of medium to moderately large-sized, growing companies with repeated successes. They develop business plans with their managers, and then work with them to execute the plans. They do not use plans to control subordinates, but use them to produce effective teamwork. They modify plans as required for success.

Craftspeople sales professionals

Solid account managers for established accounts. Will introduce established products to new accounts, but are reluctant to introduce new products to new accounts or to established accounts because of the overall degree of uncertainty about ultimate success. Listen well, plan well, work to plans.

Bureaucrats

Followers, risk averse, by the book, mediocre technologists, CYA.
Primary needs: Security, safety, belonging, failure avoidance.

Bureaucrat technologists as customers

They buy from the Benefits part of a data sheet but talk features. They are usually weak technically. They hold manufacturers and their sales channels responsible for a product's fitness for use in their applications. They expect the manufacturers to make them look good. They usually don't understand all the goods and services required to get their jobs done. However, they expect the manufacturers to provide whatever is needed (over the life of their applications) at no additional charge. *(Don't read the product's manual.)*

Features

- Between 25% and 70% of user-buyers (and over 90% of Technical Buyers) in a market.
- Usually found in large, hidebound, bureaucratic companies that have elaborate systems of sign-offs and approvals to prevent mistakes and spread accountability.
- Avoid personal risk at the expense of potential achievement.
- Have far less clout (to say "yes") than the economic buyers.
- If there are battles to fight within their organizations, they want and need the manufacturer to fight them. Then they expect credit for any victories.
- May be critical in buying decisions on very large orders.
- It may be difficult or undesirable to use them in referral selling. They take unnecessary risks when they give referrals so are reluctant to do so. Limit their referrals to other Bureaucrats.
- Their companies are usually large and not growing.

How to sell to Bureaucrats
- Publicize specific "benefits" in the sales literature. Paint a picture of guaranteed non-failure in the guise of assured success. You'll take the responsibility for success of his project. Be prepared to take the blame if it fails.[8]
- Take the initiative to contact them, stay in touch, and carefully manage their accounts.
- Be a large company with lots of cash in the bank and cradle-to-grave technical support.
- Develop a marketing system that holds their hands from initial contact until they meet their stated objectives. Provide lots of after-the-sale support.

Caveat: When the economic potential is marginal or suspect, send this prospect to your strongest competitor.

Bureaucrat CEOs

Bureaucrat CEOs are usually found running older, historically successful companies after getting their MBAs from Harvard and spending more than thirty years working their way up through bureaucracies of large companies like IBM, AT&T, DEC, or Motorola (etc.). Usually appointed by aging Boards of Directors dominated by financial types. As managers they make their subordinates go through motions of planning, but avoid signing off on plans if at all possible. They use plans to control, to intimidate, to blame, and to cover their own asses. Effective at managing the financial types on their board and the financial wizards of Wall Street. Probably receive enormous salaries and substantial perks, and their primary objective is not to lose them. Their secondary objective is to increase them. Have little or no sense of humor about their business or how they do their jobs. They champion cost reductions (with emphasis on travel expenses, office supplies, and personal phone calls) and give lip service to business opportunities.

Bureaucrat sales professionals

Only effective at selling tried and true products to existing customers. They work best with purchasing on re-orders. Won't introduce an unproven product to old customers or develop new markets for love or money; it's personally too risky for them; financial incentives to entice them do so are a waste of money.

Victims

Drinking Alcoholics, drug addicts, welfare addicts, lawsuit junkies.
Primary attractors: physiological
Primary focus: Failure (for which others can be blamed)

Victim technologists as customers

Victim technologist customers usually come in two flavors: they are either incompetent or extremely capable with a neurotic need to fail. The most common flavor is the incompetent people who should be in other professions but have too little self esteem to change jobs or careers. Will screw up and take manufacturers with them. *(Couldn't understand a User Manual if it were in comic book form.)* The other flavor, much rarer, is extremely capable people with either a neurotic or a temporary need to fail.

Features
- Less than 5% of user-buyers in most business markets.
- Histories of failure but have fantastic reasons why others were always responsible.

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[8]See the Tandem/ State of California DMV example in Chapter 6

- Elicit sympathy and the mothering instinct.
- Accidentally succeed from time to time, but that is a risk they have to take.

How to sell to Victims
Don't! Walk away; actively encourage them to buy from your strongest competitors. Sales to them are never profitable.

Caveat: Some sales professionals are attracted to Victim customers like other people are attracted to drinking alcoholics, practicing drug addicts or other Victims. Bureaucrats believe they can "save" them and some Adventurers like the danger of trying to save them.

Other attitudes

Sometimes it's useful to be even more specific about a person's operating point and refer to a "Craftsperson with Bureaucratic tendencies" or a "Victim with Adventurer tendencies." A *fanatic* is an example of a Victim with Adventurer tendencies.

People can migrate from one preferred operating point to another one. However, they usually do it slowly and in response to external pressures and the maturing process. Here are some examples:

Adventurer to Craftsperson: Success creates pressure for an Adventurer to be more careful. A successful Adventurer CEO acquires money, stockholders, employees, and customers who expect more dependability and less risk taking. Some Adventurer CEOs modify their attitude and management styles and become Craftspeople. Maturity that comes with age and experience may help this transition.

Adventurer to Victim: This transition is interesting, particularly among CEOs. If an Adventurer CEO becomes highly successful, the external pressures to become a Craftsperson are intense (he's accumulated responsibilities for employees, customers, investors, money, etc.). If he's unable to make the transition, what does he do? One option is to resign, convert to cash, and risk that cash for yet another adventure. (A sports example of this is found in Michael Jordan's resignation from the height of Basketball fame and fortune to pursue Baseball.) However, some individuals —Steve Jobs, founder of Apple Computer, and Philippe Kahn, founder of Borland, come to mind as possible examples— don't deliberately let go of their first successes, instead they (subconsciously?) set up situations in which they get booted out. This cleverly enables them to return to swashbuckling adventure without being responsible for a socially "irresponsible" decision of throwing away success. When they get the boot, some of them continue to play Victim in their own minds and in public. Others quickly return to being Adventurers.

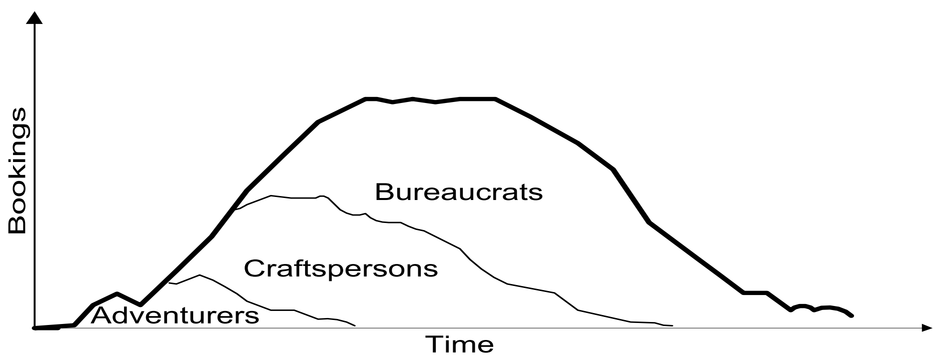
Craftsperson to Bureaucrat: A person who migrates from Craftsperson to Bureaucrat does so by becoming increasingly preoccupied with reducing the risk of failure. In the scientific method of Fig. 2.3 the person spends more and more time iterating a solution, seeking the perfect answer before releasing it. Eventually she reaches a point where she spends all her energy avoiding failure (in the guise of seeking perfection) and none of it achieving anything. As her productivity falls to zero, her self esteem and willingness to accept responsibility also decline to zero and she becomes a Bureaucrat.

Bureaucrat to Victim: An individual, for example, might migrate from Bureaucrat to Victim when he is discovered to be unacceptable by his managers. He takes a Victim position that his job wasn't clearly defined by management; therefore the performance expectations are unreasonable (or his car broke down, he was sick, etc.). The manager clarifies the job, but the employee (cleverly) finds loopholes in each clarification that make his lack of performance the manager's responsibility. If he is terminated, he claims no one ever told him there was a performance problem, and sues or demands substantial severance benefits, all with a straight face (because his internal mental system is as effective at disowning accountability as his external behavior), and a lawyer at his side.

Market timing for Adventurers, Craftspeople, and Bureaucrats

The usual market life-cycle curve groups buyers into categories such as innovators, early adopters, early major market, major market, and laggards. Unfortunately, these terms aren't helpful in deciding what motivates each group to buy when it does. Our categories provide a clearer picture of motivations and buying attractors. Adventurers are the innovators and early adopters in a market. Craftspeople begin to buy later when the product is proven, and Bureaucrats buy after the product, the manufacturer, and the market are well established. Victims show up at any time looking for a handout. Fig. 4.2 represents a typical distribution of buyers during the life cycle of a product.

When individuals buy products or services, their decision-making attitudes influence how early in the product cycle they are willing to buy and what risks they are willing to take. When companies buy products or services, several people are usually involved in the decision-making process. The attitudes of User-buyers and Economic Buyers are usually the dominant influences on timing.[9]



Impact on selling

The four attitudes are not deterministic, but they suggest what motivates a person and what he or she is most likely to do. An Adventurer CEO, Craftsperson engineer, or Bureaucrat CFO is strongly motivated to make major professional decisions in a way that is consistent with his attitude. We are more effective when we know our own business attitudes, and we can work more effectively with customers and sales professionals when we know theirs. Adventurer customers are the innovators and early adopters, Craftspeople are the most profitable segment of the market, Bureaucrats are the bulk of the market, and Victims are the most unprofitable market segment. Adventurer sales professionals are best at launching new products, opening new markets, and at selling to Adventurer or Craftsperson customers. Craftsperson sales professionals are best at

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[9] These terms come from *Strategic Selling* and are described in the next chapter.

developing and expanding proven markets with proven products and Bureaucrats do their best administering repeat business.

Exercises

1. With reference to Fig. 4.1, what decision-making attitude do you normally take in your job? Which needs are you filling? Identify situations in which you were in each of the other roles in your work. What needs were you trying to satisfy at the time?

2. How does your attitude change from when you're relaxed to when you're under constant pressure?

3. What is the decision-making attitude of your boss? Key subordinates? How do similarities and differences in attitudes affect each of these working relationships?

4. What are the decision-making attitudes of your key Sales Professionals and Key Customers?

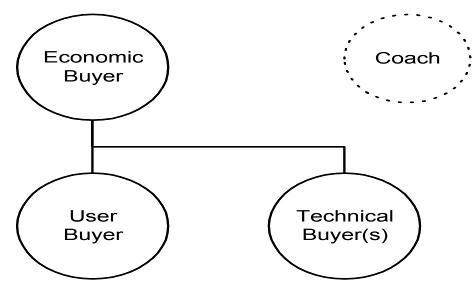
5. Customers' Buying Processes

"*People buy for their own reasons, not for yours*." Miller and Heinman

In order to design an effective marketing system, it is important to know how prospects and customers buy. In this chapter, we'll go into detail on the makeup of the buying teams in companies, their buying processes, their shortcuts, the timing of buying processes, and the goods and services that the buyer might need or want in order to use a product successfully.

The buying team

As described in *Strategic Selling*[10], and mentioned in Chapter 4, the team that makes a company's buying decision includes four significant buying influences: Economic buyer, user-buyer, technical buyer, and coach. These buying influences may involve more than four people, or they may all rest in one person, depending upon the situation.



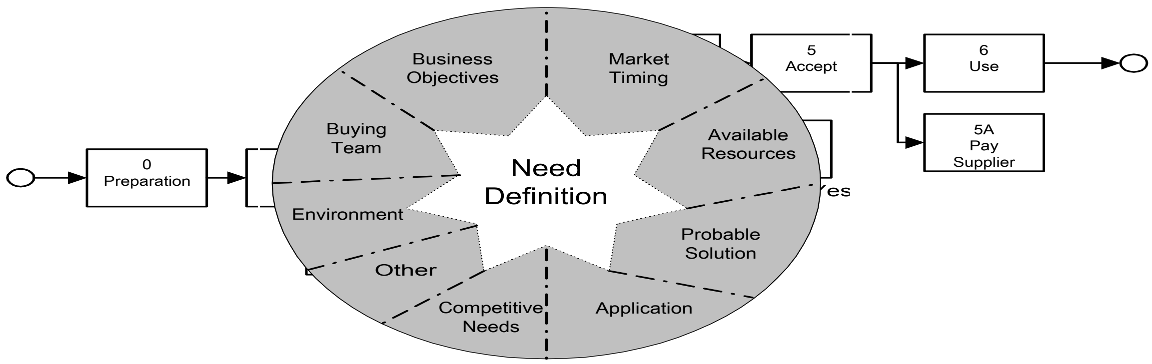
The **economic buyer** has discretionary use of the funds to buy and focuses on the economic costs and benefits of buying. This buyer is usually the most senior management person in the process.

The **user-buyer** will either use the product or be responsible for its successful use by others. This buyer focuses on fitness-for-use characteristics such as performance, ease of use, reliability, and ruggedness. The user-buyer may also be concerned with appearance or style. User-buyers may include technologists who incorporate the product into a process or design it into another product.

The **technical buyer** focuses on how well the product and its supplier meet specific qualifying technical requirements. The technical buyer screens out suppliers and products, but does not decide which one is selected from the remaining alternatives. There may be several technical buyers on a team. They might include: legal counsel who rules out sources for contractual reasons, a Quality Assurance manager who rules out sources that don't meet ISO 9000 Quality Assurance standards or products that don't have reliability data, a Purchasing Agent who rules out sources who have failed to meet commitments in the past or who can't meet price or delivery requirements now, and a representative from Finance who would rather not spend the money at all.

The **coach** is someone, usually inside the buying organization, who believes that a specific supplier is in his and the buying organization's best interests. He or she is willing to advise the supplier on how to work with the buying team. A coach may be the economic buyer, user-buyer, or a technical buyer on the buying team, someone outside the team, or someone outside the buying organization who has credibility with it.
Each team-member is expected to act rationally in the best interests of the business, but is also motivated to act by his personal attractors. In healthy buying situations the economic buyer and user-buyer act like

[10] *Strategic Selling*, Buying Influences pp 69-95.



Craftspeople or Adventurers trying to achieve organizational objectives. The technical buyers act like Bureaucrats trying to protect the organization.

The buying process

We'll examine the buying process by discussing the typical procedure a business follows the first time it purchases products to fill a specific need (See Fig. 5.2). Then we'll discuss the most common shortcuts to the buying process.

Step 0: Preparation that results in the decision to fill a particular need, form the buying team, and allocate a budget and timetable for getting the job done. What the buying team members know and believe at the conclusion of this step usually determines what the team decides to buy and from which suppliers. ***Step 0 is normally more important than steps 1, 2, and 3 combined***. However, many manufacturers and their sales organizations wait until the buyer reaches Step 2 before getting actively involved in the process!

Step 1: Specify a need in a set of business contexts like the ones shown in Fig. 5.3. The contexts determine the criteria for an acceptable solution and the conditions for sustained success. These contexts include:

- *Business Objectives* that the need supports.
- *Application in which the need exists.* The application might be an OEM product for resale or a product for use within the business. Important factors include how a solution will be used and the other equipment to which it connects.
- *Buying team.* These people define the need based on what they know and believe at the time. Their attractors, attitudes, and competencies also affect their drive to proceed with the buying process, how they will choose a specific product and source, and how much effort they will put out to make the solution and need fit together successfully.
- *Environment of the need* includes the physical, cultural, and business environments. For example the physical environment might be a cement plant, a rain forest, or an air-conditioned office. The cultural and business environments might involve workers with limited education, engineers with college degrees, or the general public.
- *Resources available* include the money, labor, and materials justified by the importance of the need. For example, the need might be important enough justify as much as $50,000 in money and three man-months of effort to choose a solution and to get it up and running.

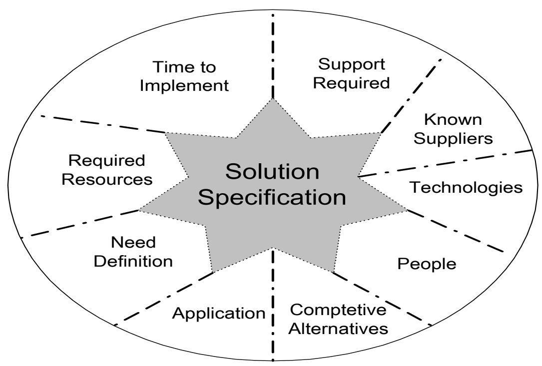
- *Competitive needs* include any alternatives for spending the allocated resources. They also include the option of leaving the need unsatisfied and keeping the resources.

- *Market timing* includes the schedule on which the need has to be met and the interval for which the need must remain satisfied by the solution. For example, an acceptable solution might have to be in place within three weeks and meet the need for another five years.

- The most *probable solution* influences the development of the need specification. What team members see as probable solutions alter their perceptions of reasonable expectations.

Step 2: Specify a hypothetical solution. The solution specification will probably include the contexts shown in Fig. 5.4. They include:

- *Time to implement:* the calendar time budgeted to get the solution, install it and make it fully



operational. It is also involves the specified useful life for the solution.

- *People:* those who use the solution, those who support its installation, training, and maintenance. Their attractors, attitudes, and competencies and the outside support required to make the chosen product work successfully during its useful life.

- *Competitive Alternatives*: any product choices **known to the decision-makers** that they believe are close to meeting the requirements of the Solution Specification.

- *Sources*: the potential organizations from which to buy the product and other goods and services they provide to support the timely delivery and successful use of the solution.

Step 3: Evaluate known competitive alternatives and select one. An alternative is chosen from among these options (or variations thereof):

a) Purchase a specific product from a specific source to meet the need.
b) Purchase two or more products solutions which together fit the need.
c) Negotiate with one or more sources to modify their products to fit the need.
d) Purchase a unique solution designed specifically to meet the need.
e) Make the solution; don't buy it.
f) Go back to step 2 (Fig. 5.1)and revise the solution specification.
g) Go back to step 1(Fig. 5.1) and reconsider the need specification.
h) Save the resources and leave the need unsatisfied.

The evaluations of products and suppliers considered in alternatives a), b) and c) are based on the factors that include: sources' product specifications (data sheets), demonstrations, and test units, quotations, product and source credibility with the decision-makers, and support products and services that will insure that the product performs its defined functions over the specified useful life. The solution of d) is evaluated from a detailed proposal from a "qualified" source. The buying team may split the order for a specific product or solution between two or more sources to qualify second sources. This usually occurs when the product or solution is critical to the business and will be reordered in the future.
Steps f) and g) are valuable feedback paths in the buying process. They enable the buying team to update its requirements based upon what it learns during the evaluation process. A prospective source may be able to coax the buying team to use these feedback paths. It would have them rewrite their requirements around its products in a way that excludes all other competitive alternatives. However, it is much easier for a prospective source to influence the initial specification during Step 0. Bureaucrats on the buying team can also use these feedback paths to delay the buying decision.

Step h) is both a legitimate alternative and a way to delay the buying decision. It may hold strong attractors for a Bureaucrat on the decision-making team because it is the only alternative for which that team member is sure to avoid accountability for "failure" within his bureaucracy.

Step 4: Order products. Once the buy decision is made and then approved by the economic buyer, a Purchasing Agent (who may or may not have been a member of the buying team) initiates a routine ordering process. He issues a Purchase Order (P.O.) to the selected supplier. The P.O. specifies what is being ordered, when it is needed, where it must be delivered, how much will be paid for it, terms and conditions, etc. The definition of what is being ordered is usually explained in the P.O. by referring to one of these documents: a) customer's Solution Specification, b) supplier's Product Specification, c) supplier's Proposal, or d) the manufacturer's part number that refers to the manufacturer's current product specification.

Step 5: Accept products. Most businesses have formal evaluation and acceptance procedures for the first shipments of new products. Payment is contingent upon acceptance, and acceptance is contingent upon the product passing tests that check to see that it meets the specifications called out in the purchase order. After the first shipments, acceptance testing becomes perfunctory or nonexistent unless earlier shipments had quality or reliability problems.

Step 5A: Pay Supplier. A business will usually pay for the product thirty to forty-five days after accepting it. Some will pay more promptly to receive a discount, others will delay payments as long as they can and force suppliers to finance their business.

Step 6: Use products. The products may be consumables used only once or they may be items that will operate in the application for many years.

When you compare Fig. 5.2 with Fig. 2.2 on page 22, you'll find that the buying process generally follows the Scientific Method.

Reorder process

The reordering process is usually faster and simpler. The specification of the need and the solution are *frozen*; the product and its source are already qualified. The customer doesn't need to re-examine the specifications or to re-evaluate the competitive alternatives. A purchasing agent simply reorders the same products from the same source and the shipment is accepted with little or no testing. If the purchasing agent has more than one qualified source for the product, he has the authority to choose among them. He commonly bases his decision upon price, delivery, and payment terms.

Shortcuts in the buying process

Individuals and companies buy lots of things. They limit the step-by-step process of Fig. 5.2 to critical decisions and adopt time-saving and money-saving shortcuts for everything else. We've discussed the reorder process, which is one widely used shortcut. Here are other widely used shortcuts:

Limit solution searches to previously qualified sources. Buyers limit solution searches to sources with which they already do business. When a need arises, they ask known sources about how to solve it and use the first acceptable solution they find. This shortcut is convenient, it is comfortable for Bureaucrats and it efficiently "reuses" the initial investment made to qualify a source.

Consolidate buying: buy from as few sources as possible. Many things that we buy are relatively unimportant and not worthy of detailed analysis. As individuals we buy most of our groceries at a local supermarket. The identical products may be available in other stores, but we don't often go from store to store to find the best brands and the lowest prices on each item. We skip detailed evaluations of each item's prices and features to deal with one store with which we feel comfortable. Companies follow much the same process. Purchasing agents consolidate requirements for hundreds of products and buy them from a single source, perhaps a favorite Distributor, rather than shop around. Occasionally they do this to the detriment of the user-buyers when they purchase "equivalent" products that aren't.

Compromise or redefine needs so that several of them are filled by a common solution. This is also known as "standardizing." Standards are two-edged swords. In the hands of Craftspeople, standards are valuable, simplifying tools that aid teamwork and success. In the hands of Bureaucrats, standards are often control mechanisms that stifle innovation and impede progress.

The reorder process and other buying shortcuts are barriers to entry for manufacturers and marketing systems in search of new customers. A customer who already has an adequate solution from a known source has little incentive to spend time and money evaluating alternatives. What is more, it's politically safer for a Purchasing Agent to buy the tried and true. The Purchasing Agent would have to drag the user-buyer and economic buyer, kicking and screaming, back into the decision-making process to evaluate a new product from a new source. He won't do that without a serious delivery or quality problem with the existing source, unless the new alternative is much cheaper, or unless a strong personal attractor is satisfied.

When a new source with equivalent or even better products vies for orders, it faces economic and personal obstacles. From the buyer's point of view:

- The existing sources have established their personal credibility; the new source may have none.
- Standardizing on one solution is easier and cheaper. Standardization reduces training and support costs.
- Dealing with a proven source and a proven solution has a more certain outcome than going through the qualification process with a second source.
- The more business you do with one source, the more important you are to it, the more leverage you have, and the better support you get.
- Dealing with as few sources as possible makes the job simpler.

- To change sources and solutions may suggest that earlier decisions were wrong and that someone made a mistake. Bureaucrats in particular do not want to suggest that they, their bureaucracy or their fellow Bureaucrats made a mistake.

Timing of the buying process

Fig. 5.5 on the next page shows four representative buying processes and typical time-scales related to each of them. Its purpose is to help illustrate how widely the buying process varies. The variations in ordering times and in the sizes of the orders significantly affects the design and management of an effective marketing system.

Simple Purchases (Fig. 5.5A)
Simple purchases are the most common ones. Each order stands alone. It does not commit the customer to buy anything more from that source.

Individual Consumers make simple purchases when they buy most things including food, clothing, appliances, automobiles, and homes. However, the time they take for a simple purchase usually increases with the cost of the purchased item. People normally take less than a day to buy $50 in food, less than two weeks to buy a $500 stereo system, less than two months to buy a $15,000 car, and more than two months to buy a home.

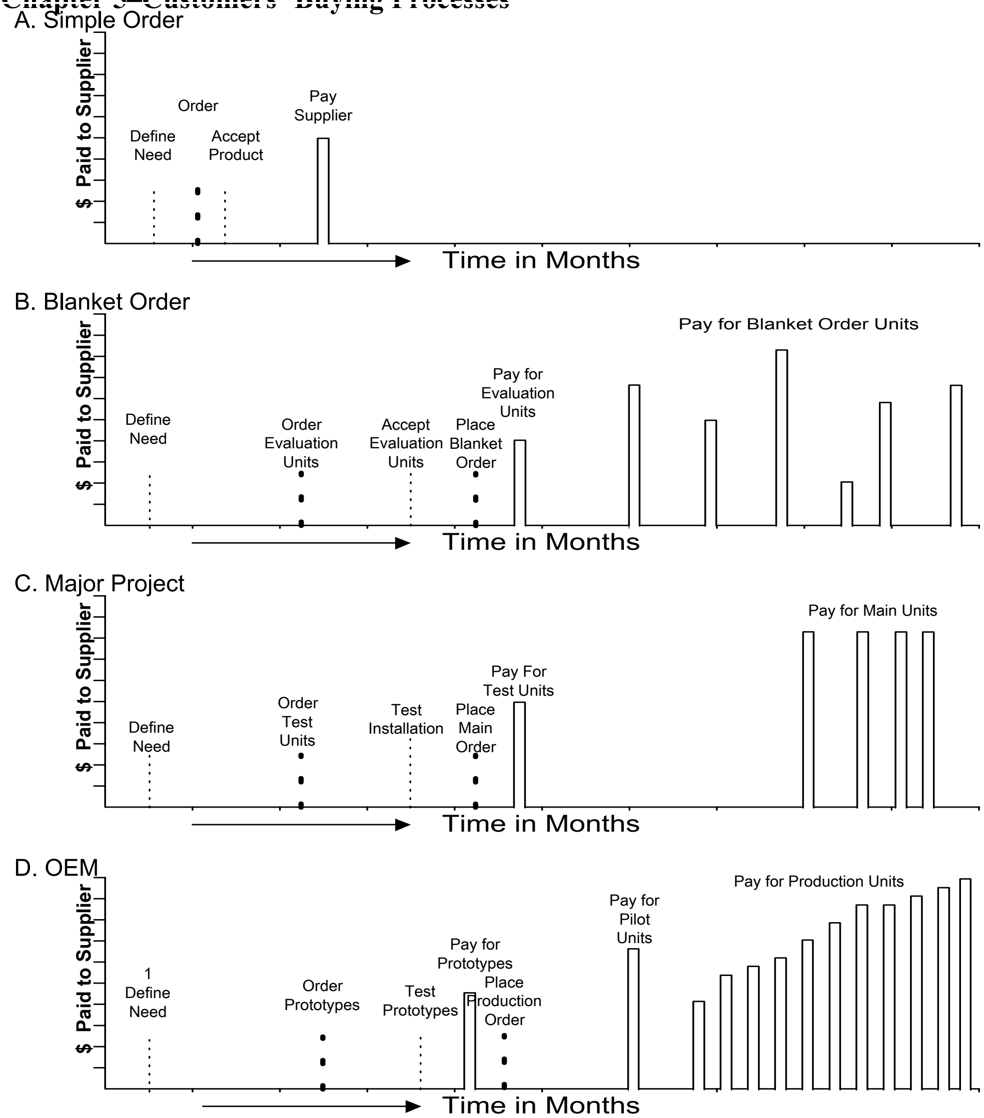
Businesses also make simple orders for some supplies, office equipment, and capital equipment. Overall, purchasing and payment times increases with order size. It probably takes less than sixty days to buy a $500 power supply for the engineering lab, and more than a year to buy a $500,000 Pick and Place machine for manufacturing.

Blanket Orders (Fig. 5.5B)
A Blanket Order is a customer's commitment to buy a specified dollar amount of products within a specified period, typically a year. The Blanket Order buying process has two phases. In the first phase the customer buys limited quantities of the product or products from one or more sources to qualify the products and to select one source. Then the customer commits to a blanket agreement with the successful source. In the second phase, the period of the agreement, the customer reorders products under the terms of the agreement.

Businesses overwhelmingly prefer Blanket Orders to Simple Orders for the reasons explained earlier in this chapter in "Shortcuts to the Buying Sequence."The dollar value of the blanket order determines the thoroughness of the customer's evaluation process and the risks the competing sources are willing to take in phase one. Competing sources invest time and money during the first phase without being certain that they will recover these costs on the second phase.

Major Project Orders (Fig. 5.5C)
A Major Project is undertaken by the customer to fulfill a specific need, either its own or that of one of its customers. For example, a customer builds a new plant to expand its business. In the process it buys and installs such things as furniture, telephones, a telephone system, computers, a computer network, and manufacturing equipment. The needs are clear at the start of the project, but the elapsed time to evaluate, order, take delivery, and pay for any of these products is dictated by the Project's schedule, not by the buying process itself. The elapsed time could be a few months or several years.

When the project involves significant technical risks, the customer is likely to use a test installation to evaluate the risky elements on a smaller scale. Based on the results, the customer might change what he buys



and whom he buys it from, or he might postpone or kill the Project. It is in the best interests of a would-be source to give superlative support to the customer beginning well before the Order for the Test Installation products.

OEM Orders (Fig. 5.5D)
OEM stands for Original Equipment Manufacturer; a customer that buys materials to include in the products it manufactures and sells to its own customers. The OEM's buying process is connected to the development and release of its own product and usually goes through several phases: Prototype, Pilot, and Production (See Fig. 2.4). In the Prototype phase the OEM builds and tests enough products to debug and prove the design concept (Step 6 of Fig. 2.4) and to chose its sources. In the Pilot phase it builds enough products to debug its manufacturing process. In the Production phase it builds products in response to its customers' demands. The duration of each phase varies widely from one case to the next. The Prototype phase can vary and take less than two months to more than a year. The Pilot phase usually takes a few months. The Production phase can go on for years.

What customers want or need

A customer buys to solve problems and satisfy needs. However, to buy and use a manufacturer's generic product successfully, a customer may need as many as two dozen other goods and services! Figure 5.6 lists these goods and services (including the generic product) and groups them into five categories: Information, Deliverables, Technical Support, Financial/Business, and Intangibles.

Intangibles
- Credibility & Trust
- Convenience

Information
(about):
- Manufacturer & Marketing system
- Deliverables
- Technical Support
- Financial/Business

Technical Support
- Application Engineering
- Product Engineering
- System Integration
- Installation and Testing
- Training
- Problem Solving
- Maintenance

Deliverables
- **Product (generic)**
- Options
- Special Features
- Updates
- Product Documentation
- Solution Documentation
- Products of Other Manufacturers

Financial/Business
- Availability
- Price
- Credit
- Terms and Conditions
- Warranty
- Spares, Safety Stock
- Contingent Liability
- Configuration Control
- Manufacturing Rights
- Quality Assurance

Fig. 5.6: Table of Goods and Services customers might need, want, or expect from a supplier

Intangibles

Credibility and Trust: Frankly, these intangibles precede any commitments by a customer, and should precede any commitments by a supplier (a manufacturer and/or its marketing system). The manufacturer, its products, and the sales agents that call on the customer all have to establish reasonable credibility and trust before the customer will book its first order. The first time a supplier works with a customer, its credibility and trust are conditional and under close scrutiny. The behavior of the manufacturer and its sales agents when providing information and in working with the buying team either builds credibility and trust, or causes them to deteriorate. Credibility and trust are fragile and conditional until the two parties complete at least one cycle of business together. After that, it still takes efforts by both parties to maintain credibility and trust.

Convenience: How easy is it for the customer to do business with its supplier? Are Deliverables readily available as required, or does the customer have to schedule deliveries far in advance? Are questions answered rapidly, information delivered promptly, or service performed quickly with no hassles?

Information

At various times in the buying process the customer needs timely **information about the Manufacturer** and **its Marketing system**, **the Product**, other **Deliverables**, **Technical Support**, and **Financial /Business.** The manufacturer or its marketing system can provide the information in various forms including advertising, press releases, application notes, fliers, data sheets, accessible computer data bases, seminars, referrals, demonstrations, loaners, evaluation tests, quotations, and proposals. A customer also develops information from previous experiences with the manufacturer and its marketing system, and from their ongoing working relationship. Some information will shape the customer's vision of its needs and options in the Pre-Buying Phase (See Fig. 5.1). Some will influence the Specification of the Hypothetical Solution. Some will critically influence the choices made from among competitive alternatives.

Deliverables

Deliverables are the quantifiable goods and documentation that the customer receives from its supplier in exchange for money. An obvious deliverable is the **Manufacturer's Product**. However, the customer may also need **Options** to the product, **Special Features**, and/or the Products of other Manufacturers to fulfill his requirements.

Products of other Manufacturers: These might be included simply for the convenience of combining orders. Or, they might be products that interact with the Manufacturer's Product and by including them the supplier takes responsibility for their successful interaction. In fact the manufacturer might be required to integrate them with his Product and create a fully tested, working Solution to the customer's need. The common theme for including the Products of Other Manufacturers is that the customer considers it more valuable to include them in his order than to buy them separately.

Other deliverables include the **Product's Documentation** such as a User's Manual, Maintenance Manual, Drawings, or descriptive literature. When the supplier configures a unique Solution for the customer, then **Solution Documentation** is also required.

Usually the customer requires the Deliverable items after he places the Order. Sometimes a manufacturer samples Deliverables (for example Product Documentation) as a way to get Information.

Technical Support

Technical Support applies specialized knowledge about the supplier's product and the customer's need to mate the two successfully.

Application Engineering fits a manufacturer's generic product to the customer's need without substantially changing either one.

Product Engineering substantially redesigns the product or designs new products to meet the customer's requirement.

System Integration combines existing products (from one or more manufacturers) into the customer's solution.

Installation and Testing get the Deliverables up and running successfully after they are received by the customer.

Training includes the planned activities needed to enable the customer to use the Deliverables successfully.

Problem Solving includes the unplanned activities to resolve technical issues such as unreliable connections between the Products and other products, or operator problems (also known as cockpit problems).

Maintenance: is the ongoing support required to keep the Deliverables working successfully over the useful life of the solution. There are generally three levels of maintenance: factory, depot, and on-site. Factory maintenance means the product is returned to the factory for repair. Depot maintenance means the product is returned to a local organization, associated with the manufacturer, that performs the repair. On-site maintenance means that someone comes to where the product is being used and repairs it.

Financial/Business

Availability is usually related to how soon after an order the Deliverables can ship. The issue of availability can be complex for major Programs or OEM orders (Figs. 5.4B and 5.4C) where a substantial quantity of deliverables is needed over an extended period. To place the Order, the customer must be confident that the supplier can and will repeatedly provide the deliverables on time.

Price usually refers to the price charged by the supplier to the customer for the Deliverables. Some suppliers and some customers get even more simplistic and focus on the unit price of the Product, assuming that everything else is included in that price. Price should include the entire amount the customer will pay the supplier. As we will see later in the book, sloppy negotiations about price and what it includes are a major source of grief and lost profits for manufacturers and their channel organizations.

Credit: The customer may lease or rent rather than buy, or pay in instalments over an extended period of time. In some cases the supplier might finance the leasing (as IBM did with computers) or a third-party might become involved.

Terms and Conditions: These are the legal protocols between customer and its supplier. A key item: *How long the customer can take to pay for Deliverables after it receives them.* Business customers are usually given "net 30" terms: payment is due within thirty days of shipment. Some customers then take as many as 60 or 90 days to pay, thereby using the Supplier's credit to help finance their businesses. Another condition is *the location at which the transfer of ownership legally takes effect.* This has tax implications. It also impacts *insurance, how deliverables are shipped,* and who pays *shipping costs*.

Warranty: The Supplier's commitment to make good for defects in materials and workmanship of its deliverables. It includes commitments as to how the Supplier repairs or replaces defective Deliverables. It's almost always a "limited warranty," that is the Supplier specifically excludes responsibility for the consequences of the product's failure.

Spares, Safety stock: Deliverables available to meet emergencies or unforseen contingencies. They may be used to replace defective parts or to allow the customer to handle additional needs quickly. These deliverables may be stored by the manufacturer or its agent and remain the manufacturer's properties unless drawn down by the customer.

Contingent Liability: This includes a liability for "fitness for use" of the deliverables in the customer's application and a liability when a manufacturer's products infringe on patents or copyrights. Here's one example of contingent liability: A manufacturer makes transistors and his OEM customer uses them in Pacemakers which they sell to surgeons who implant them in patients. A transistor fails in the Pacemaker and the patient dies. The patient's family sues the doctor, the hospital, the manufacturer of the pacemaker, and the maker of the transistor for megabucks. The fact that the customer used the transistor in a critical application created a contingent liability for its manufacturer. Had the same transistor been used in a video game and failed, it would not have created a huge contingent liability.

Contingent liability can accrue when a supplier fails to deliver on time or fails to meet its published specifications when either failure costs the customer big bucks. When a manufacturer's products violate a third party's patents or copyrights, the customer may wind up with contingent liability. Most agreements between customers and suppliers have clauses like "hold harmless" in which one of the parties agrees to defend or indemnify the other (that is, take the bullet) in case of litigation. These agreements are not bulletproof.

I'm personally amazed at how few manufacturers account for the contingent liabilities their customers create for them. At least the price of the transaction should include some consideration for this risk. The price of a doctor's services includes a hefty amount to pay the insurance premiums that cover his contingent liability. Some manufacturers blindly walk into situations that have enormous risks and minuscule rewards.

Configuration Control: OEM customers have discovered over the years that manufacturers change the design of their Products from one shipment to the next to "improve" performance or to cut costs. Sometimes those revised Products do not work in the customers' applications, or they force the customers to adjust their products or procedures. To prevent this, some customers require suppliers to notify them of Product changes in advance. Unless the customer approves the changes, the supplier must continue to ship him the old configuration.

Quality Assurance: Many large customers take an active interest in the quality and reliability of their supplier's products. They may require that certain quality policies and procedures be followed in design and manufacturing, like ISO 9000. They may even require third party certification of quality procedures, perform source inspections, and conduct Quality Audits. They may require specific, extensive testing of finished products to improve confidence in their reliability or safety.

Manufacturing Rights: The business success of an OEM customer may depend upon a Supplier's ability to make and deliver its products. The OEM may choose to protect itself by requiring the Supplier to assign it the rights to manufacture the products if the Supplier fails to meet its delivery commitments.

Few customers require all the items listed in Fig. 5.6. The items that a specific customer requires add value for that customer and may increase costs for the manufacturer or its marketing system. Sometimes an item's costs are built into the marketing system and specific customers don't use or value that item. This can put a manufacturer at a competitive disadvantage. When a manufacturer attempts to develop a "one size fits all" marketing system, it either wastes money on some customers or loses others because it fails to deliver necessary items.

Subsequent chapters discuss which items various Sales Channel Organizations can typically supply. In Chapter 13, it is all tied together in a way that enables a manufacturer to design an effective marketing system. Few purchases involve all the requirements.

Timing of goods and services

Fig. 5.7 on the next page correlates the steps of the buying process shown in Fig. 5.2 with the needs listed in Fig. 5.6. It shows when customers usually require goods and services to fulfill each need.

Some significant points related to this chart:

- It's valuable to supply Information at Step 0. It can favorably influence the definition of the need and the acceptable solution. It also builds credibility and trust between the manufacturer and the prospective customer.
- Costs incurred by a manufacturer prior to step 5 are at risk until payment is received at step 5. The interval between when costs are incurred and when they are recovered at step 5 ranges from months to years depending on the buying process. (Refer also to Fig. 5.5)
- There may be significant costs after the deliverables are accepted and paid for.

	Step in the Buying Process (Fig. 5.2)						
Goods and Services Required	0 Prepare	1 Specify Need	2 Specify Solution	3 Evaluate	4 Order	5 Accept/ Pay	6 Use
Intangibles							
Credibility and Trust							
Convenience							
Information							
Mfg. & Marketing system							
Deliverables							
Technical Support							
Financial/Business							
Deliverables							
Product							
Options							
Special Features							
Updates							
Product Documentation							
Solution Documentation							
Products of other Mfgs.							
Technical Support							
Application Engineering							
Design Engineering							
System Integration							
Installation and Testing							
Training							
Problem Solving							
Maintenance							
Financial/Business							
Availability							
Price							
Credit							
Terms & Conditions							
Warranty							
Spares, Safety Stock							
Contingent Liability							
Licenses							
Manufacturing Rights							
Quality Assurance							

Fig. 5.7: Steps in the buying process when goods and services are likely to be required. Degree of shading corresponds to relative level of support and its costs.

Exercises

1. Select a recent major purchase decision that you made as a consumer (for example a TV, computer, refrigerator, furniture). When did you decide to make a purchase to fill that need? If someone else was involved in making the purchase decision who was the economic buyer? Who was the user-buyer? Were there technical buyers? What preconceived ideas did the user-buyer have about the need and the viable solutions at Step 1? Over what period of time were those opinions formed? How much did your opinion change as you moved to Step 4? What caused any significant changes?

2. Select a recent major purchase decision that your company made in which you were involved. Answer the questions in exercise 1 for that buy.

3. Which of the goods and services of Fig. 5.6 did your company require to successfully select and use the product involved in that major purchase? What organizations and individuals, including those within your company, supplied each good or service?

6. Customer/Supplier Relations

"The customer is frequently wrong. We don't carry those sorts of customers. We write them and say: Fly somebody else. Don't abuse our people." Herb Kelleher, CEO Southwest Airlines

To sell effectively, it's important to know how customers expect to be treated by their suppliers, and how suppliers expect to be treated by their prospects and customers. This chapter studies buyer-seller relationships in our society and how they impact business objectives and successful marketing systems. We usually assume that customer are, or should be, kings in buyer-seller relationships. I'll explain where this idea comes from, how it influences our business transactions, and why it's unhealthy.

Relative importance of Customers and Suppliers

Respected gurus of business frequently remind us that "the customer is king," "the customer is always right," and "we're in business to please our customers." They don't tell us that "the supplier is king," "the supplier is always right," or "we're in business to please our suppliers." While it's true that the customer is usually more important than the supplier, that importance is not due to some immutable law of nature. It is a consequence of four economic and social conditions which happen to favor the customer in most situations in our economy:

- Supply and demand
- Cultural beliefs
- Money and competitive alternatives
- Generally Accepted Accounting Standards (GAAS).

Supply and Demand

The law of *Supply and Demand* is an observation that a product's value is set by the relationship between its supply and the demand for it. When demand exceeds supply, its value increases until supply and demand come into balance. When supply exceeds demand, its value decreases until they come into balance. I learned about this law in college. However, it was only a few years ago that I first realized that it directly affects the Customer/Supplier relationship.

In the fall of 1989, I taught a course on Project Management to business executives in Shanghai. One of my students was a very successful young woman who managed several retail stores. One Saturday we toured her crowded stores and watched bored "sales" people reluctantly and slowly serving hordes of shoppers. I couldn't pass up the opportunity to espouse western business principles. I explained the importance of customers and suggested that she might train her sales people to treat them better. She smiled and gently replied: "In China, the most important people in a business are the purchasing agents, and the least important are the sales clerks, because it's difficult for us to get products and we can resell anything [11]we can buy! It's not necessary to treat the customer well."

On that crowded street in Shanghai, it finally dawned on me that the law of supply and demand determines the relative worth of suppliers and customers as they negotiate with each other. Affluent societies have a chronic surplus of suppliers, so that suppliers usually have to work to get customers to buy from them.

[11]Actually she said "almost anything," and added that what the Chinese wouldn't buy could be exported to the Russians who would buy anything.

Developing countries have a chronic surplus of customers, so customers have to work to get suppliers to sell to them!
However, there are situations in our society where individual customers are nearly worthless to their suppliers. The following story illustrates an example. One of my cousins was studying for her MBA at Harvard and I visited her class on Organizational Change. It was analyzing the case of a New York hospital at which a reporter's daughter had died because of poor treatment. The reporter had investigated the hospital and exposed its poor medical practices and patient-hostile attitudes. He had called for change, but little had happened.

The course instructor then said emphatically: "The hospital is there to serve the patient. Patients are its customers so it *should* change to serve them better." His statement might be morally virtuous, but it is economically and psychologically unsound. That hospital had an abundance of patients who overwhelmed the supply of medical care, so that individual patients had little value to the hospital staff. The staff had no rational or economic incentive to improve service because that would have attracted more patients and increased the overload. The hospital's personnel were in the same situation as the bored sales clerks in Shanghai.

Supply and demand also influence employee-employer relationships. Normally we have a surplus of potential employees (suppliers of labor) and a shortage of employers (customers for labor). Therefore, negotiations for jobs and compensation are usually one-sided in favor of employers. Some employees unionize to control the supply of labor and drive up its value. Unfortunately, the shortage of labor is artificial so that both employers and employees retain *"I win - you lose"* attitudes towards each other.

By contrast, Silicon Valley has had a natural shortage of skilled labor for the last 30 years. Without unions or bargaining agencies, salaries exploded, working conditions improved, and management added (or tolerated) a measure of fun at work. Employers improved wages and working conditions because supply and demand made the employees valuable enough to justify the improvements.

Cultural Beliefs
In our society the law of supply and demand has favored customers for several generations. Consequently, we have transformed a rational idea into a cultural conviction that the customer should be king in all transactions. We accept this as a universal principle, ethically right and morally good. As customers, we expect to be courted by suppliers and not to care about their best interests. As suppliers, we expect to serve and adapt, and to be thankful for whatever profits we can squeeze out in return.

When suppliers do get the upper hand, customers become uncomfortable and angry because it's contrary to their cultural convictions. For example, Intel and Microsoft dominate and control the CPU and software segments of the Personal Computer market. Intel controls the supply of the industry standard CPU chips, artificially through patents and copyrights, and naturally through aggressive product development and product promotion. Microsoft artificially controls the supply of operating systems through copyrights. Both companies stick it to their customers from time to time, in part for the same reasons that the hospital staff sticks it to the patients. Both companies are enormously profitable, but their corporate customers are increasingly angry and resentful, and their consumer customers are restless. This has already opened doors of opportunity for competitive alternatives. IBM, DEC, and Apple are companies in the computer industry who once held similar lofty positions, dominated their customers, and then degenerated into also-rans.

Money and Competitive Alternatives

Customers start their buying process with money, which is itself a product that can indirectly fill a myriad of needs (see Money and Personal Attractors on page 32). On the other hand, suppliers start with products that can only fill limited sets of needs. Customers have more freedom, more competitive alternatives for spending their money than suppliers have for selling their products. Customers' choices decrease after they exchange their money for products. Suppliers' choices increase when they get customers' money. By contrast, two parties in a barter economy are simultaneously suppliers and customers, exchanging products that fill limited needs. The two parties are more equal.

Generally Accepted Accounting Standards

Generally Accepted Accounting Standards (GAAS) describe the success or failure of a business strictly in terms of money: profits, cash flow, and Return on Investment (ROI). GAAS measures these things for specific periods, usually for three months (a fiscal quarter) or a year. *Revenues* during the period minus *expenses* during the period are called *profits* for the period. Products shipped to customers are accounted for as revenues the day they ship. Most costs, other than manufacturing costs, are expensed as they occur. However, there is usually a delay of months or years between engineering and marketing expenses and the revenues they produce. Since GAAS usually don't account for these time delays, managers can show higher profits, improved cash flow, and higher ROI's by not spending money on capital equipment, engineering, training, advertising or promotion, etc. Not investing in these items may undermine future revenues, but no one can ever prove that according to GAAS.

In essence, GAAS say that revenues are good and expenses are bad. Since customers produce revenues, they are good. Since suppliers create expenses they are suspect. Later in the book, I'll show how this accounting mentality undermines successful working relationships among manufacturers, customers, and channel organizations.

Critique of "*the Customer is King*"

The idea that *the customer is king* has a certain appeal. However, unless there is reciprocity from the customer, it describes a *Customer wins and Supplier loses* relationship! As the book Conceptual Selling clearly explains, that relationship inevitably degenerates into a lose-lose one[12]. Most selling "techniques" and market strategies are procedures designed to manipulate anticipated win/lose relationships so that suppliers do not lose, at all costs. For example, the strategy of market dominance is an attempt to control customers by eliminating their competitive alternatives.

[12] See Conceptual Selling, pp 159-180

U.S. semiconductor companies and many of their customers have developed unhealthy lose-lose relationships over the past 30 years. These relationships have evolved through a series of three- to five-year cycles of semiconductor parts shortages and parts surpluses. During times of surpluses, the semiconductor manufacturers fell all over themselves to woo and to support customers. Customers took advantage of this to stick it to the manufacturers financially and to treat their sales professionals shoddily. When the shortages came, the semiconductor manufacturers got even and stuck it to the customers. They dramatically increased prices, bundled products,[13] shipped faulty products, missed delivery commitments, and generally took a "take it or leave it" attitude with their customers. When the shortages ended, customers retaliated. They canceled orders, renegotiated contracts, bought on the gray market, etc. In the mid 1980's customers switched in droves to Japanese manufacturers to get more reliable products, more reasonable prices, and to be treated with respect. The Semiconductor manufacturers then formed the Semiconductor Industry Association to solicit government protection from their Japanese competitors and to whine in the press about the disloyal practices of US customers. They acted as if the customers owed them the business. These cycles of atrocities and retaliation were partly created by the win-lose idea that "the customer is king," and its implication that the manufacturer should be a servant or loyal subject.

There are healthier relationships between suppliers and customers, like the one between Southwest Airlines and its customers. I am one of their happy customers and fly them often. Their success starts with the healthy and humorous attitudes of their people. These attitudes come from careful hiring and a positive environment in which employees are every bit as important as customers. The CEO, Herb Kelliher, fosters and supports this environment. One of his statements is worth tattooing on the head of every idiot who preaches that *the customer is always right* or *the customer is king:*

> "*The customer is frequently wrong. We don't carry those sorts of customers. We write them and say, 'Fly somebody else. Don't abuse our people.'* "

Herb's comments reflect a point that I repeatedly emphasize in this book: All prospects and customers are not the same and they shouldn't be treated the same way. Treat the profitable ones well and turn the losers over to your competitors. Then, thank God for those masochistic competitors who eagerly endure the pain and losses of serving them.

The desired outcome: Profitable Customers

Not all customers are the same! Some customers contribute to a manufacturer's success, some are marginal, and others are intrinsically unprofitable. A successful marketing system chooses profitable customers. To some managers the term *profitable* means that the manufacturer gets more money from the customer than it spends to make and sell its products. They see it strictly in accounting terms: if the transaction contributes to the quarterly profits, the customer is profitable. That definition is *too simple* and gets manufacturers into serious trouble.

The best, most profitable, customers produce these benefits for the manufacturer:

- Produce financial profits
- Use the product successfully
- Find new uses for the product
- Suggest or develop product improvements
- Find and help correct bugs in the product

[13] To get delivery of scarce parts, customers had to order additional products that they usually purchased elsewhere

- Generate repeat business
- Stimulate referral sales
- Enhance the commitment of the manufacturer's sales force

The most profitable customers are usually Adventurers and Craftspeople as user and economic buyers. Adventurers are most likely to discover new uses, to identify improvements, to find bugs, and to stimulate referral sales. Craftspeople are most likely to use the product successfully, to generate repeat business, and to stimulate referral sales. Both take responsibility for their results, whether they succeed or fail.

The worst, least profitable, customers have one or more of these characteristics:

- Have expectations or needs that:
  - a) they're not clear on
  - b) exceed manufacturer's available resources
  - c) require financial losses to support
  - d) manufacturer's product is a marginal alternative
- Lack competence to use the product successfully
- Require unreasonable or unavailable support to use the product successfully
- Lack integrity

Bureaucrats and Victims as user-buyers and economic buyers are usually the worst customers. Bureaucrats don't "buy" the product and they don't focus on successfully using it. They expect the manufacturer to do whatever it takes to guarantee that they won't be accountable for failure. Professional Victims lack integrity and more or less expect failure but will (skillfully) hold the manufacturer morally and financially accountable for that failure. Bureaucrats and Victims look for large, bureaucratic, well-heeled manufacturers to take care of them. In a few paragraphs I'll describe a case in point.

The unprofitable customers produce these liabilities for a manufacturer:

- Financial loss
- Misuse the product
- Dump the manufacturer
- Poison the well
- Undermine the commitment of the manufacturer's sales force

An unhappy customer dumps a supplier that doesn't satisfy his needs or expectations and often poisons the well by broadcasting the problem to other customers and prospects. An unhappy customer also demoralizes the manufacturer's sales force and reduces its confidence in the manufacturer and its products. Sales professionals often adopt wait-and-see attitudes after a manufacturer alienates a customer.

No matter how well a product is designed, no matter how well it is supported, there are customers (user-buyers) who will buy it and trash it. These customers undermine the product and the manufacturer in the marketplace. This recently occurred in full public view between Tandem and the California Department of Motor Vehicles. Several years ago, Tandem supplied computer hardware to the DMV as part of a system to automate the management of California driving records. Tandem was paid in full, so it showed a profit according to GAAS. However, that DMV system totally failed to do the job, the failure was broadly reported, and Tandem's reputation was damaged, even though it arguably delivered equipment that met the DMV's specifications. From what I've read, it's clear to me that the DMV project team was incompetent and couldn't have succeeded under any circumstances. It was appointed by Bureaucrats and dominated by Bureaucrats.

However, Tandem's management was apparently well aware that the project would probably fail, and yet it played footsie with consultants and managers to get the order.

A manufacturer is always responsible for having an unprofitable customer. Either the manufacturer doesn't screen out an intrinsically unprofitable customer, oversells the product, or is unwilling or unable to provide adequate support. Managers and sales professionals who have unprofitable customers and don't take complete responsibility for having sold to them, are themselves behaving as Bureaucrats or Victims.

The bottom line

Manufacturers are expected to take the initiative in the Customer/Supplier relationship. However, manufacturers have to handle this initiative carefully to develop successful long-term relationships. If they treat all customers the same, like kings and queens, their own people will resent being subservient and look for ways to get in control. One way is to achieve market dominance. But market dominance creates hostile customers who look for opportunities to get even. It also creates hostile, superior attitudes in the manufacturer's people, who decide that they know what is best for customers.

Intel, which is a well run company that dominates the microprocessor market, recently exhibited this attitude when dealing with its customers about the math flaw in its Pentium processor. Its management decided what the customer "ought to be happy with," in spite of customer feedback to the contrary. It withheld information and support until forced by market reaction to do otherwise. Intel's position wasn't technically wrong, but its arrogance about what was best for the customer was self-destructive. I'm glad for Intel's sake that its management quickly bit the bullet on the recall and thereafter increased customer involvement in its decision making.

What struck me at the time as interesting was the public reaction of Intel's key accounts like IBM, Compaq, and Dell. IBM was the most vocal about holding Intel's feet to the fire. It refused to ship Pentium based computers until the problem was fixed. The other key accounts were publicly passive. IBM has some competitive alternatives to Intel's chips, and has the money and marketing clout to stand up to Intel (and Microsoft). The others are totally dependent upon Intel for economic survival. Having no viable competitive alternatives, they are subservient to Intel. Their key people must be seething with resentment towards Intel, not because Intel is bad, but because they lack the freedom of choice to be honest and forthright with Intel and with their own customers.

Governments and government agencies are other examples of suppliers without competitors. On the one hand, they are expected to support the entire market since they're the only game in town. They wind up spending most of their time and money on society's Victims; building prisons, managing armies, and doling out welfare in its many forms. In California, for example, the State Government now spends more money on its prison system than it does on its education system. On the other hand, government employees, both elected and tenured, have an arrogance towards the electorate and believe that they alone know what's best for the people. They resent it when the people aren't passive and supportive.

The problems experienced by Intel, Microsoft, and Governments are the unhealthy results of market dominance. The key to healthy relationships is competitive alternatives for both the supplier and the customer.

- The competitive alternatives that a customer has to buying from a supplier are assets for both the customer and supplier!

- The competitive alternatives that a supplier has to selling to a specific customer are assets for that supplier and for the customer!

Competitive alternatives improve the satisfaction with and commitment to the relationship between the two parties. This is a key point to remember when setting business objectives and developing the marketing system to support them.

7. Manufacturers' Selling Processes

As we discussed in the last chapter, in a developed economy it's usually the responsibility of the manufacturers to find and attract their customers. Customers don't have to go looking for manufacturers. Most manufacturers expect their marketing systems to have systematic processes for finding and attracting prospects and then turning them into customers. However, they tend to see these processes from their own point of view instead of from the customers' buying perspectives. This chapter describes the typical marketing and selling process as seen by a manufacturer. It also describes when and how this process interacts most effectively with the buying processes of customers.

Selling sequence

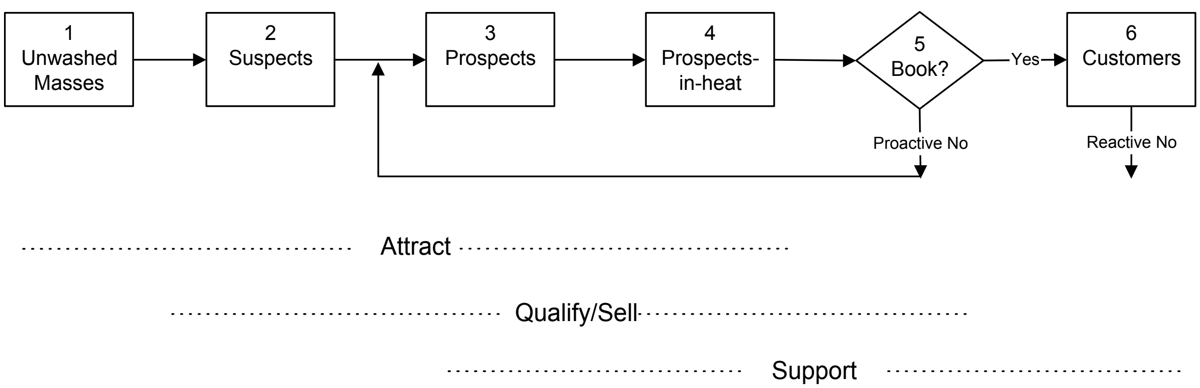


Fig. 7.1 illustrates a manufacturer's step-by-step processing of potential buyers. The processing starts with the Unwashed Masses, a large population that the manufacturer knows little about and who know nothing of the manufacturer. From this starting point a few customers are systematically identified and booked. At any time the marketing system is working with people in each of the six phases of processing. The process from Step 2 to Step 5 is often referred to as a sales funnel because lots of suspects enter at step 2 and relatively few customers are booked at step 5.

1. Unwashed Masses
There are people and companies that know little or nothing about the manufacturer, and vice versa. These are the unwashed masses. The manufacturer takes the initiative to promote its products and services to targeted audiences within this group of people and companies in a way that attracts potential customers. Typical promotions include advertising, PR, mass mailings, and exhibits at trade shows. Their objective is to elicit signs of interest from those who might eventually buy. These signs of interest, called leads, include: telephone

calls, faxes, letters, and bingos.[14] A few of these leads, such as telephone calls asking for price and delivery, may be from people who are prepared to buy. However, most leads are questionable and come from people in five categories: Uninterested, Unprofitable Prospects, Profitable Prospects, Unprofitable Prospects-in-heat, and Profitable Prospects-in-heat.[15] Usually fewer than one-in-twenty of these unqualified, leads come from Profitable Prospects and Prospects-in-heat. So the people who generate unqualified leads are only Suspects because the manufacturer doesn't know which ones are worth pursuing.

2. Suspects

An effective marketing system screens the Suspects to identify and further attract Profitable Prospects and Profitable Prospects-in-heat and to flush the others. The longer the Uninterested and Unprofitable remain in the system the more money the marketing system wastes on them. Qualification methods include: a) mailing packets of information and waiting for a second inquiry as a sign of serious interest, b) outbound telemarketing calls, and c) field sales calls. The mail approach is cheapest but is the slowest and least selective. It's usually too slow for Prospects-in-heat who are making decisions on tight schedules, and it doesn't effectively screen out the unprofitable, the students, and the literature collectors. Telemarketing is quick and can be effective at identifying prospects and prospects-in-heat, but is usually poor at screening out the unprofitable from the profitable. The field sales call can be the most effective screening tool but it is very expensive (for costs of field sales calls see Chapters 9 and 10) and takes more time to set up and execute than telemarketing qualification. Most manufacturers use combinations of all three methods.

3. Prospects

A manufacturer's legitimate prospects are all those people and companies who are in Step 0 of their own buying process (See Fig. 5.1) for needs compatible with the manufacturer's products and services. It isn't easy to evaluate who fits these criteria, because they aren't actively buying. However, it is worthwhile to do it well.

A manufacturer should systematically interact with its prospects to:

- Build its credibility with them
- Screen out the unprofitable ones
- Influence their beliefs about what they will need, when they'll need it, and how much it's worth in a way that establishes the manufacturer's products and services as the leading competitive alternative.

Proper handling of the prospect pool (apart from prospects-in-heat) is a vital part of the selling process, and one not usually appreciated by executives. For that reason I'm going to go into more detail about it.

Establish mutual credibility: When a manufacturer establishes its credibility with prospects before they start their active buying processes, it takes relatively little effort to be considered as one of the competitive alternatives. When a manufacturer simultaneously qualifies the prospects and establishes that they are going to be profitable, then it's easy for the manufacturer's people to make concerted and timely efforts to close their business when the time comes.

[14] A bingo is a response to an advertisement or product announcement in a magazine. The ad or announcement has a "bingo number" on a *reader reply card* included in the publication. The reader circles the bingo numbers of interest, fills in his name, and address and mails the card to the magazine. The magazine then forwards the reader's name and address to the appropriate advertisers.

[15] Prospects are in step 0 of their buying processes of Fig. 5.1. Prospects-in-heat are in steps 1-3 of their buying processes.

Influence perceived needs, priorities, and competitive alternatives: After a manufacturer has established its credibility with a prospect, it can influence that prospect's perceived needs and priorities by informing the prospect through advertising, PR, technical articles, trade shows, seminars, demonstrations, etc. Don't underestimate the impact of this influencing process on the ultimate definition of the prospect's needs. A manufacturer can have the most influence before the prospect goes into active buying mode.

For example, a credible manufacturer could demonstrate a unique feature of its product to a prospect and convince him of the feature's value. Then, when the prospect moves to Step 1 (Fig. 5.2) of his buying process, he will specify this feature and thereby eliminate competitive alternatives that don't have it. Some of the most successful manufacturers develop this kind of "account control" before prospects go into heat. These manufacturers get prospects to write their specifications around their products and preclude all competitive alternatives. Government contractors in the Military and Aerospace business have operated almost exclusively this way for years.

Sometimes a manufacturer can give a prospect information skillfully and thereby accelerate the start of its active buying process. It can even move passive prospects to active customers in a very short time. Just recently I was skillfully "informed" by a supplier in a way that moved me from a slightly interested prospect to a buyer of its $500 business software product in a two-hour period. I went to the supplier's free seminar to learn more about direct mail and telemarketing, issues that I knew I'd be dealing with in another six months or so. During the seminar I learned that the supplier's product fit the future need better than anything I'd used in the past, and that it offered some immediate benefits that I hadn't thought about. The product was available at the seminar and had a 60-day, money-back trial period. So I walked out of that seminar with the product under my arm, and so did more than 30 other people out of an audience of 150.

By the way, members of the audience helped sell each other the product by favorably comparing it to what they were already using, which included all the leading competitive alternatives. The seminar leader scrupulously avoided negative comments about competitive products, including do-it-yourself; he merely asked skillful questions of the audience members who used them.

Many manufacturers, those with less effective marketing systems, wait passively for prospects to go into heat and then furiously sell to them. As a consequence, they have trouble establishing credibility fast enough, have more competitors, and are much less likely to book profitable orders. Strangely enough, many executives believe that they save time and money this way.

A friend of mine, whose product is *contract manufacturing,* closes business from almost every prospect he submits proposals to because he qualifies his prospects and works with them before they become active buyers. The CEO of one of his major competitors, who simply bids on RFQ's (Requests for Quotes), couldn't believe my friend's hit rate. He felt lucky to close 20% of the jobs he bid on. In fact this fellow pays his sales people commissions for the number of quotations they make!

The contrast between those who gain credibility before the need is defined and those who wait is even more dramatic in the job market. Fewer than 20% of all job openings are ever advertised (RFQ's). Over 80% of all jobs are filled by people who are known to the employers in advance of the need. People who simply respond to ads and fill out job applications are like my friend's competitor. They typically have less than a 5% chance of being hired by a specific employer, because there are so many competitive alternatives at that point, and they have already lost out on 80% of the opportunities!

As we'll discuss in later chapters, the primary benefit that any third-party channel organization brings to its manufacturers is a pool of qualified prospects for which the channel organization has established its credibility and influence.

4. Prospects-in-heat

Prospects-in-heat are those prospects who have an immediate need for solutions. They also have authority to buy and the funds with which to buy. The manufacturer's marketing system is usually intensely involved with these potential customers with activities that may include responding to questions, making presentations and demonstrations, providing loaners, and submitting quotes or proposals. Once prospects are in their active buying modes, manufacturers are in reactive mode. That is, they must largely adapt to what the prospects have defined as their wants and needs, and meet the prospects' schedules. They have little opportunity to alter the prospects' requirements to fit their unique capabilities.

Many manufacturers vigorously pursue all their prospects-in-heat like male dogs mindlessly pursuing bitches-in-heat. They bid on every RFQ in sight. They book orders at all costs, willing to enter culturally acceptable "customer wins, manufacturer loses" relationships. CEOs and Sales Executives may be encouraging this mindless pursuit in the name of market share and meeting quarterly sales quotas. They compensate for dollars booked in the quarter (or number of quotes made) without regard to the long term profitability or success of the transactions. According to *Strategic Selling*, up to 35% of the typical sales professional's active prospects are unprofitable! [16]

5. Book orders

This part of a manufacturer's selling process corresponds to Step 4 (Fig. 5.2 on page 50) of the customer's buying process. The most successful marketing systems pro-actively convince the best prospects to order from them, the intrinsically unprofitable ones to embrace a competitor, and the others to choose a competitive alternative for this order, but to stay in the prospect pool until they can be booked and supported profitably.

Other marketing systems book everyone in sight. Later on they lose angry customers who didn't get the products or support they needed or expected.

6. Customers

Once a prospect orders, it is up to the marketing system to provide the goods and services required to satisfy the customer's needs and wants as well as to fit the customer's order.

Customers require continued support from the manufacturer (as described in Chapter 5) for as long as they use the manufacturer's products. Customers who successfully use the product are also prospects for more business because the manufacturer has cemented its credibility with them. Satisfied customers will actively seek ways to do more business. A typical example of this was described to me by a friend in the Boston area. His company successfully designed and installed a small system (under $50,000) for a major manufacturer. Almost immediately they were called in to "consult" on a major automation program for that manufacturer. They helped to specify the design and wound up with a multi-million dollar order. The successful completion of the first job established their credibility and produced a customer initiative to find more ways to do business with them.

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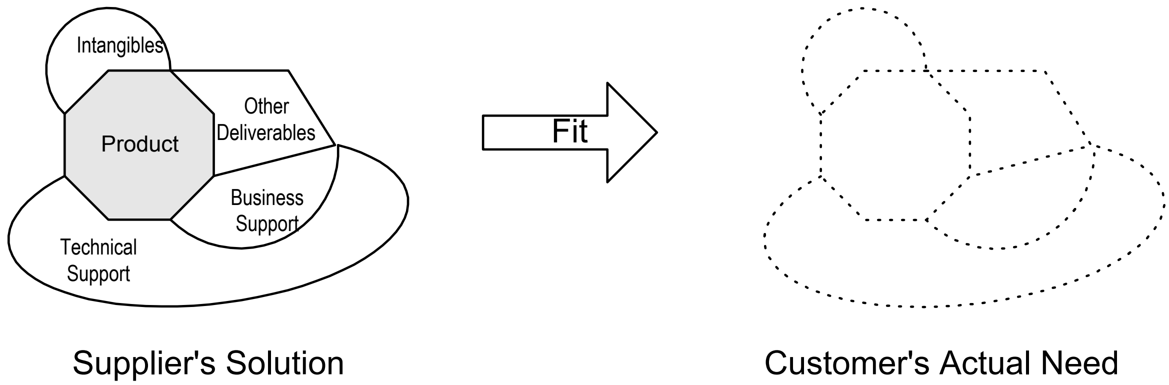
[16] *Strategic Selling*, Miller and Heiman, p 63

NB: It takes a lot of effort to build mutual trust. Neither buyers nor sellers can afford to waste that effort on trivial business relationships.



On the other hand, as discussed in the previous chapter, customers who are oversold or under-supported on one order may terminate all business with that manufacturer and its marketing system. An angry customer will devote substantial time and money to exact buyer's revenge The damage done to a manufacturer by an angry customer is typically more than five times the value of the order.

Timing of the selling process

Convincing an account to buy, supplying the deliverables, and getting paid for them takes as long as it takes. That is, the pace is usually set by the buyer, although it can be influenced by the seller in some cases. As shown in Fig. 5.5 on page 57, the active buying process can take months. The shipments and payments that result can stretch out for years. The pre-active buying process, Step 0 of Fig.5.2, can also go on for months or even years. Until a customer actually pays for the deliverables, the manufacturer and its marketing system have either wisely invested, or foolishly spent, time and money selling to that customer. When the result is a profitable customer (in its largest meaning, not just the accounting definition), the time and money were wisely invested. When the result is anything else, they were foolishly spent.

A selling process that effectively identifies and works with profitable accounts while they are in their pre-active phase (Prospects) will book the greatest number of those accounts in their active phase. However, some of the costs to develop credibility and influence may occur years before they produce offsetting profits.

A selling process that waits for accounts to enter the active buying phase (Prospects-in-heat) before working with them will book a relatively small percentage of them. Most of the time and money are spent on activities and accounts that are never profitable. However, the selling cycle is shortened and the direct selling costs attributable to specific accounts are at risk for shorter periods.

Summary

An effective selling process has five steps aimed a producing successful outcomes:

1. Find viable prospects.
2. Establish credibility with them, before they go into active buying mode.
3. Influence their concept of what they need and want (to fit what you can deliver), before they go into active buying mode.

4. Propose a conceptual fit.
5. Profitably deliver and support an actual fit.

Prospects are most apt to buy when the manufacturer and its marketing system hold attractors for them in three areas:

- **Solution** that fits the prospects need: the best fit among competitive alternatives.
- **Process** of transacting business: how the buyer and seller work together from pre-buying to customer support.
- **People** conducting the transaction: who the buyer relates to in the marketing system.

For example, a prospect may prefer to go to a store and shop around to decide what clothes to buy because she enjoys traveling to the store and the process of shopping in it. The competitive alternatives of shopping by mail or by TV, or buying from a door-to-door sales person could offer better products or lower prices and still lose out because those processes don't stimulate powerful attractors for her.

We may buy insurance from a particular sales professional because we enjoy doing business with her, or because she belongs to our Rotary or Kiwanis club. We seldom buy from a sales person we don't like or trust, regardless of the product or its price.

When a manufacturer picks channels and hires third party channel organizations, it's important to be aware of the preferred buying processes and preferred sales professionals of key prospects. Sales channels and sales professionals not only provide access to some customers, they also create barriers to other customers who won't buy from them for historic or personal reasons.

Exercises

1. Compare your existing selling process to the one shown in Fig. 7.1. In your opinion, which step in the process does your system do best? What are the activities that contribute to that step's success? How do plans, sales incentives, and personal attractors contribute to that success?

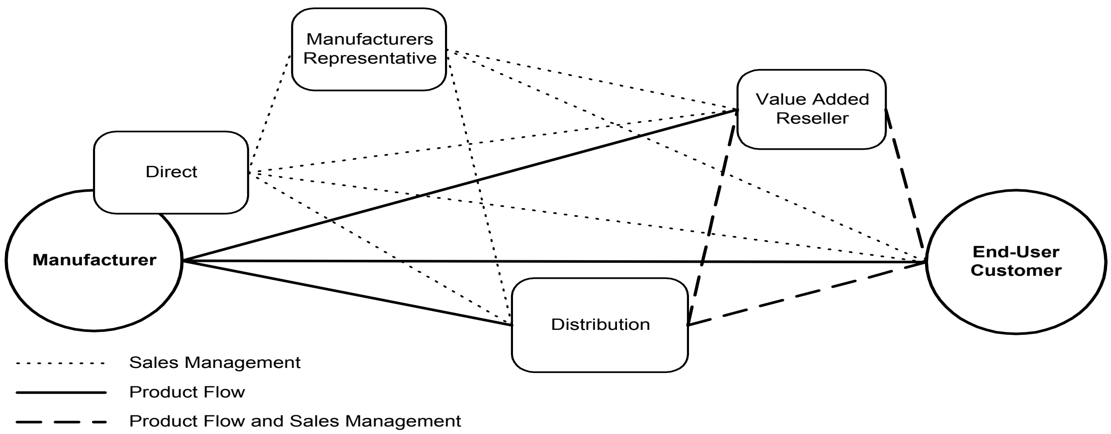
2. Which step in the process does your system do the worst? What are the activities in that step that work well? What objectives, plans, incentives, and/or resources are in need of improvements?

Section II

Channel Organizations

8. Introduction to Sales Channels

A sales channel is a specific set of resources (people, methods, and materials) with which a manufacturer sells its products to customers. A Channel is made up of channel organizations, the business entities which do the work. This chapter describes four kinds of channels and provides an overview of the organizations found in each of them. It briefly describes how each kind of channel organization interacts with its manufacturers and customers in the selling process. It also describes other individuals and businesses that channel organizations sometimes use to help them sell. The descriptions are of typical organizations and typical relationships. In later chapters, I'll suggest that you seriously consider some non-typical arrangements.



Channel organizations are generally grouped into four categories: Direct, Manufacturers Representative, Distribution, and Value Added Reseller. Figure 8.1 indicates the primary links between organizations in each channel, a manufacturer, and an end-user customer.

The Direct channel is the manufacturer's direct sales force, staffed by the manufacturer's employees. It sells directly to some end-user customers. It also selects, sells to, and manages organizations in the other three channels. An Allstate Insurance Agent is an employee in a Direct Sales channel who sells Insurance to end-user customers.

A Manufacturers Representative channel has third-party organizations that help one or more manufacturers sell their products in return for sales commissions. They may sell directly to end-user customers or to organizations in the Distribution or Value Added Reseller channels. Real estate brokers, travel agents, and mortgage brokers are Manufacturers Representative organizations that sell to end-user customers.

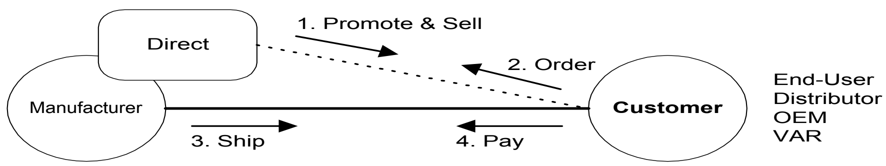
A Distribution channel has third-party organizations (Distributors) which buy the products of many manufacturers and then resell them to their own customers. Their customers may include end-user customers, Value Added Reseller organizations, or other Distributors. Distributors include Master Distributors, Distributors, Mail Order firms, Brokers, Dealers, and Retail outlets. Supermarkets and hardware stores are examples of retail outlets that sell to end-user customers.

A Value Added Reseller (VAR) channel is made up of third-party organizations that buy the manufacturer's products, turn them into application specific solutions, and then resell the solutions to their own customers.

Value Added Resellers include Systems Integrators, High-tech Distributors, and Original Equipment Manufacturers (OEMs). Plumbing contractors and roofing contractors are familiar examples of VARs that sell to end-user customers.

Direct

The Direct channel is staffed by employees of the manufacturer's Sales and Marketing organization. These people promote and sell the manufacturers products to their prospects and customers. Customers place orders with them. The manufacturer ships products to the customers who then pay the manufacturer for them.



The Customers of the Direct Channel organization almost always include end-users and may also include Distributors, OEMs, and VARs.

A Direct channel is often made up of one or more, overlapping sub-channels including Field Sales, Inside Sales, Telemarketing (or Telesales), Direct Mail, and captive Distributors. Field Sales people travel to the customer sites. Inside Sales and Telemarketing use the phone system to promote interest, close sales, and take orders.[17] Direct Mail operations send flyers and catalogs to promote interest, and may accept orders via mail, FAX, or telephone. A captive Distributor is an organization that is owned or controlled by the manufacturer and exclusively stocks and sells the manufacturer's products. A factory outlet store is a retail version of a captive distributor. Chapter 9 discusses the Direct sales channel in more detail.

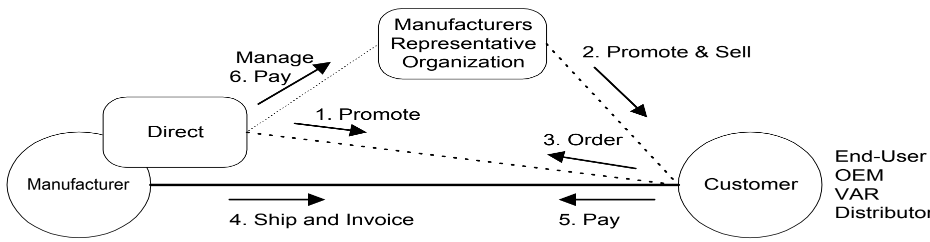
Primary benefits of a Direct channel

- Provides timely, focused contact with prospects and customers.
- Manufacturer knows who its prospects and customers are.
- Manufacturer can learn why customers buy its products and how they use them.

[17] This includes voice, FAX, and data communications.

Manufacturers Representatives

The Manufacturers Representative channel is made up of third-party sales organizations who are selected and managed by the Direct Sales organization. They help to identify prospects and close orders in return for sales commissions. These organizations are variously referred to as Manufacturer's Representatives, Sales Reps, or Reps. Each organization usually sells within a defined geographic territory: for example, New England or Southern California.



The manufacturer promotes its products (with advertising, publicity, or mailings) to the general market and generates market interest. Reps promote the manufacturer's products within their own territories. They do most of the face-to-face selling and quote manufacturers' standard prices and delivery terms to customers. Customers normally order products through the Direct Sales organization. The manufacturer fills the orders, ships to the customers, and invoices them. Customers pay the manufacturer and then the manufacturer pays sales commissions to the appropriate Manufacturers Representative organizations.

A Manufacturers Representative organization typically represents the product lines of between 7 and 30 different manufacturers and sells them to a base of customers that it has developed over time. The product lines of the different manufacturers usually complement one another so that customers for one product line are prospects for the others. When a Sales Rep makes a sales call on behalf of one manufacturer, he also promotes the products of his other manufacturers.

Variations

Some customers, particularly those who place large orders, prefer to deal directly with the manufacturer instead of with the local Sales Rep. In these cases the Sales Rep plays a more passive role and the customer becomes the responsibility of the manufacturer's Direct Sales organization. However, the Sales Rep may receive a commission anyway.

Some Manufacturers Representatives sell to Distributors and/or Value Added Resellers.

Manufacturers sometimes authorize Reps to buy their products at a discount and to stock them for resale. These organizations become Stocking Reps, a mixture of Sales Representative and Distributor. Their customers may order from them or from the manufacturer. When a customer orders from the manufacturer, the Stocking Rep gets the usual sales commission. When a customer orders from the Stocking Rep, the Rep ships to and bills the customer and gets its profit from its markup over its discounted cost. Stocking Reps set their own prices and they assume the credit risks for their customers. Customers can get immediate delivery from local stock and can buy the products of several manufacturers with one order.

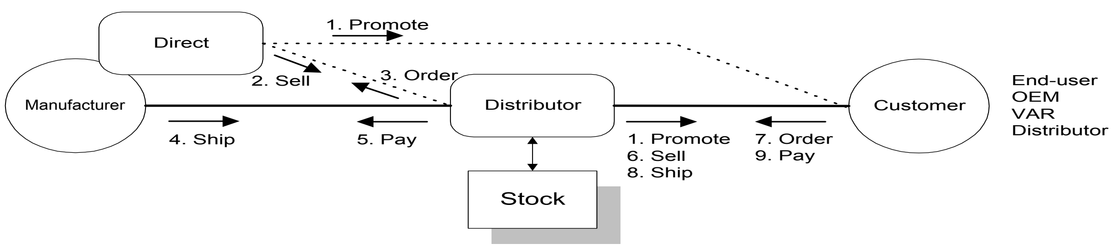
Primary benefits of Manufacturers Representatives

- **Manufacturer gets access to the Representatives' established customers**.
- **Manufacturer's cash flow improves because it doesn't pay commissions until after the products are shipped and paid for**.
- Commissions are variable expenses tied to results, rather than fixed expenses tied to payroll. The Manufacturers Representatives share the risks.
- Manufacturer can directly contact the Reps customers, learn who they are, why they buy, and what they do with the products.

You might have noticed that I didn't say that the Manufacturers Representative channel was "less expensive." That's because it is seldom less expensive than a Direct channel. The conventional wisdom for using this channel is "that it's the cheapest way to get started." In Chapters 9 and 10 we'll see what is wrong with conventional wisdom and in later chapters how conventional wisdom undermines effective management of Sales Reps.

Distribution

A Distribution channel can include Distributors, Dealers, and Retail outlets that purchase and stock significant quantities of a manufacturer's products. These organizations buy products from the manufacturer, or from one another, at substantial discounts from the manufacturer's unit list prices and resell them at whatever prices they choose. They make their money from the price markups.



Distribution organizations buy and stock the products of hundreds to thousands of manufacturers, including products that directly compete with one another. Like supermarkets, they are single sources from which their customers can buy a wide range of products. They are also independent businesses that are free to sell to customers located anywhere.

There are two overlapping selling processes with a Distributor, the process in which the Distributor buys from the Manufacturer and the process in which Customers buy from the Distributor. The Manufacturer's Direct organization selects and sells to the Distributors. The Distributor manages the transactions with the customer. However, the manufacturer stimulates the Customers by directly promoting their products through such means as advertising and publicity.

Primary benefits of Distributors

- **Manufacturer gains access to established customer base of Distributor organizations.**
- Profitably handles smaller orders for manufacturer's products

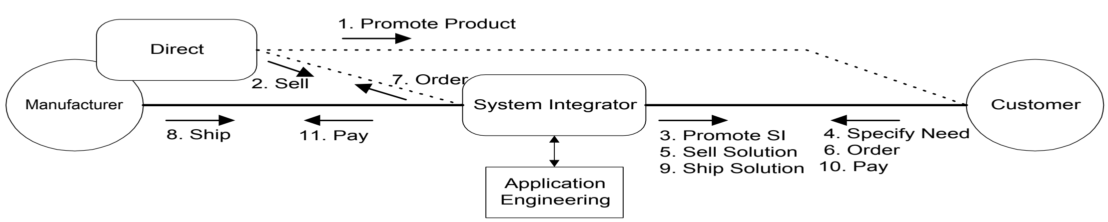
Chapters 11 and 12 describe Distribution channel organizations.

Value Added Resellers

The Value Added Reseller channel consists of independent businesses that sell customized solutions to their own customers. They buy manufacturers' products at discounts and use them in their solutions. Value Added Reseller channel organizations variously called System Integrators, VARs, High-tech Distributors, Value Added Dealers (VADs), and Original Equipment Manufacturers (OEMs). Some readers may suspect that I'm a synapse short to include OEMs among channel organizations. Everyone knows they're customers, and they are. Bear with me, there is method to the madness.

Systems Integrators

System Integrators use technical expertise, such as application engineering, to solve specific problems for customers in specific markets. Their customers are generally end-users, but on occasion they are OEMs. The System Integrator provides solutions that include the products of one or more manufacturers which they either purchase directly from manufacturers, or from distributors. They usually do business within a limited geographic territory. Roofing contractors, interior decorators, and plumbing contractors are examples of System Integrators in the consumer market.



A Manufacturer must first convince a System Integrator to use its products. A System Integrator develops product and manufacturer preferences through earlier successes with them, through discounts from the manufacturer, and through requests from customers to use specific products in their solutions.
A Systems Integrator orders products as they are needed and isn't required to stock them or order them in large quantities to get its discounts. Manufacturers often provide price guarantees that make it possible for Systems Integrators frequently to contract with their customers to provide solutions at fixed prices that might take them months or years to design, build, and deliver.

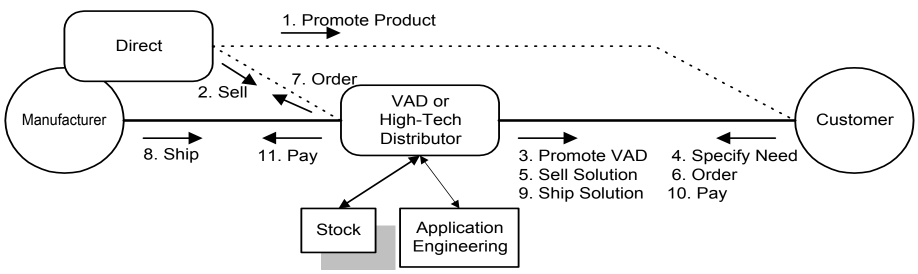
Manufacturers promote their products to the customers and prospects of Systems Integrators, especially when their products are significant parts of the solutions. Some customers specify to Systems Integrators products that must be used in their solutions. Other customers indicate strong preferences for specific products. For example, we sold Pro-Log's industrial microcomputers through Systems Integrators who designed manufacturing control systems. One of our Systems Integrators made control systems for the auto industry, including Ford and GM. However, at the time, top management at GM and Ford had specified that their manufacturing control systems had to use Allen Bradley controllers. Our Systems Integrator had already successfully done the same control applications at less than half the price with Pro-Log's products, but had to propose the Allen Bradley controllers just to be considered by GM or Ford. It was Pro-Log's job, not the Systems Integrator's, to change the customers' specified preferences.

Primary benefits of System Integrators

- **Manufacturer gains access to its customers. These customers buy solutions, not the manufacturer's products.**
- It adds unique technical values to create application-specific solutions. In effect it creates new uses for the products.

High-Tech Distributors and VADs

High-Tech Distributors and Value Added Dealers (VADs) buy and stock the products of their primary Manufacturers then resell them, primarily to end-user customers. They also use technical expertise to enhance and support these products for their customers. Customers usually buy from them to get added services such as installation, training, on-site maintenance or extended warranties. However, they may buy from them simply as a matter of convenience or to get a better price. Chapter 11 discusses High-Tech Distributor organizations in more detail.

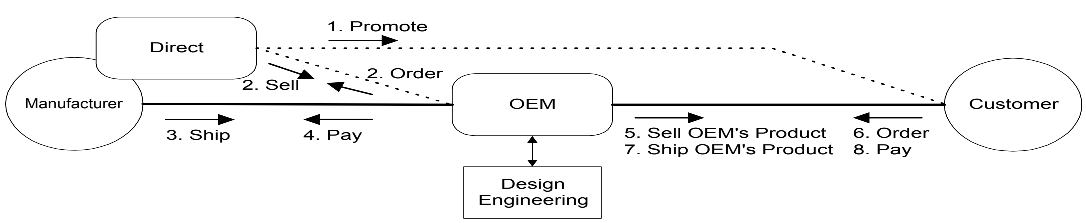


Primary benefits of a High-Tech Distributors

- Manufacturer gains access to its customers. These customers usually buy solutions or enhanced products, and would not be prospects for the manufacturer's products.

OEMs

On the one hand, OEMs are customers. On the other hand, OEMs behave like VARs. They produce large quantities of standard products designed to their specifications. They use the manufacturer's products in their designs. They expect large discounts and price protection for extended periods, but they schedule their orders from the manufacturer.



It's often useful for a manufacturer to promote its products to the OEM's market. It enhances the OEM's credibility, increases its sales, increases the manufacturer's profitability, and cements the relationship between manufacturer and OEM. A superb example of this is Intel's promotion of "Intel inside" to the general public. Intel makes microprocessors. Its OEMs, including such companies as Compaq, Dell, Gateway 2000, and IBM make computers that use these microprocessors. The "Intel Inside" campaign stimulates consumer preference for computers that use Intel's microprocessors instead of clone microprocessors with equivalent performance.

To take this example a step further, OEMs are Intel's primary sales channel for its Pentium microprocessors. Furthermore, because of its monopoly, shrewd marketing, and clever distribution, Intel makes significantly more dollars profit from the sale of any computer with a Pentium Processor in it than the OEM makes. In financial terms the OEMs are working more for Intel's benefit than they are for their own benefit.

Primary benefit of OEMs

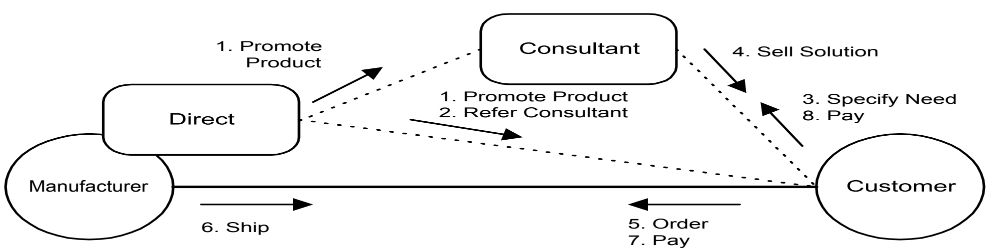
- *The manufacturer gains access to the OEMs' customers*. These customers would not be candidates for the manufacturer's products without the OEM because they only buy complete solutions or higher levels of product integration.

Other Channel Resources

Manufacturers and channel organizations use consultants and successful customers to sell their products. Service organizations sell replacement parts, provide credible technical referrals about product quality and reassure some customers that they will be conveniently supported after they buy a product.

Consultants

Consultants provide technical expertise which the customer employs to develop its product or solution. The Manufacturer's Direct organization (or any other channel organization) cultivates consultants who know how to use its products to solve specific problems. The manufacturer refers consultants to appropriate customers. The customers decide which consultants to hire. The consultant designs the manufacturer's product into the solution. The customer buys the product and pays the consultant.



Primary benefits of Consultants

- Provide technical expertise to help transform manufacturers' products to a customer's solution
- Customers assume costs of and responsibility for developing their own solutions

Successful customers
Successful customers, including OEMs, provide referrals and enhance a product's credibility without formal agreements and without receiving commissions. Furthermore, they have enormous credibility in the marketplace because they are fellow customers. What a deal! However, not all successful customers are willing or effective agents. Adventurers and Craftspeople are the most effective. Bureaucrats are often reluctant to take the risk of advocating anything and are quick to drop into Victim mode and bad mouth things when problems crop up.

Frankly, successful customers probably make more sales for manufacturers than any other channel resource, yet they are seldom deliberately managed as sales agents.

Primary benefits of Channel Resources
- Provide access and credibility to their associates, their customers, and their competitors.

Classifying organizations is tricky business
Each channel organization, like each customer, is unique. We group them into channels for our own convenience, so that we can deal with clusters of them in the same way. This is simply an example of applying Step 3 of the Scientific Method (Fig. 2.2 on page 22). It's convenient and useful to divide things into groups so that they can be managed in bite sized chunks. However, it's only an educated guess, one that each manager must verify in the real world and be willing to modify if it doesn't fit.

Most manufacturers employ the same formal agreements with all channel organizations in a specific channel. However, the unique needs and capabilities of each organization are the operating realities, not the theoretical concept of channels.

Furthermore, each organization evolves and changes in a never-ending competitive search for more revenue, increased profits, and more security. Direct organizations take on VAR characteristics. Rep organizations tend to evolve into mini-distributors and/or VARs. Distributors broker some products, add VAR support for others, or even provide contract manufacturing. VARs can act like distributors buying and stocking manufacturers' products in order to resell them without adding technical value. They may even act like brokers, first getting orders from customers, then buying product at VAR discounts, and immediately upon receipt reshipping them to the customers at higher prices. VARs can also develop into OEMs and produce standardized solutions. OEMs may become unauthorized distributors in order to unload inventories or maintain volume discounts from manufacturers.

It's incumbent upon manufacturers to use direct feedback to track the evolution of the organizations they work with, and to adopt their agreements and working methods to the changes.

Exercises
Document your answers to the following questions, then review your answers after you complete Chapters 9 – 13. You'll probably be surprised at how much your perspective changes. By the way, if you work in a channel organization, try answering these questions from the perspectives of a manufacturer you support.

1. What official channels does your marketing system currently use to sell its products? What are the primary reasons you believe each channel is useful? What are the official reasons for using each channel?

2. What drawbacks do you see in each of your channels? What are the official drawbacks?

3. If you were to add a sales channel to your marketing system, which one would it be? What are the top three benefits you would expect? What are the three most significant drawbacks or risks?

4. If you were to delete a sales channel from your marketing system, which one would it be? Would you replace it with another channel?

5. What new ideas for promoting or selling your company's products occurred to you as you read this chapter?

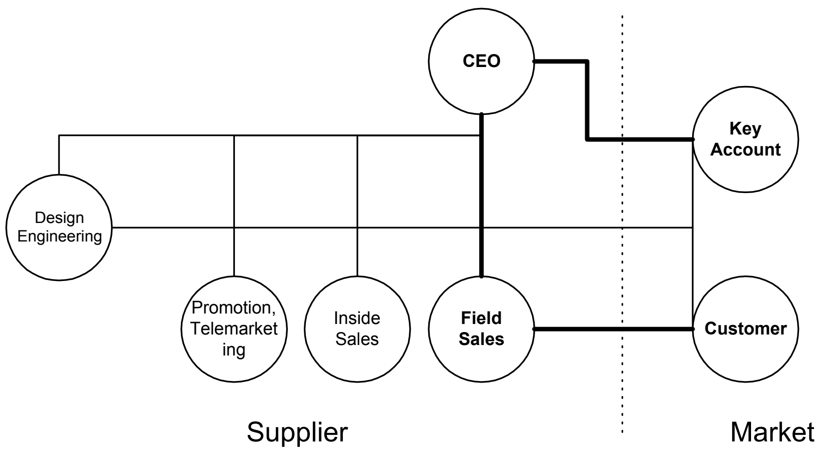
9. Direct Sales

Direct Sales is essential to any successful business regardless of other channels that business uses. This chapter covers the structures, people, economics, values, strengths, weaknesses, management issues, best customers, and worst customers for a direct sales channel. The following description is intended to provide enough information for you to make sound decisions on how and when to use your Direct Sales channel in your marketing system. It does not begin to cover all the ways Direct Sales might be organized or function.

Structures

The structure of a direct sales organization depends on the company's size. In this section we will look at typical structures found in small, mid-sized, and larger companies.

Small company

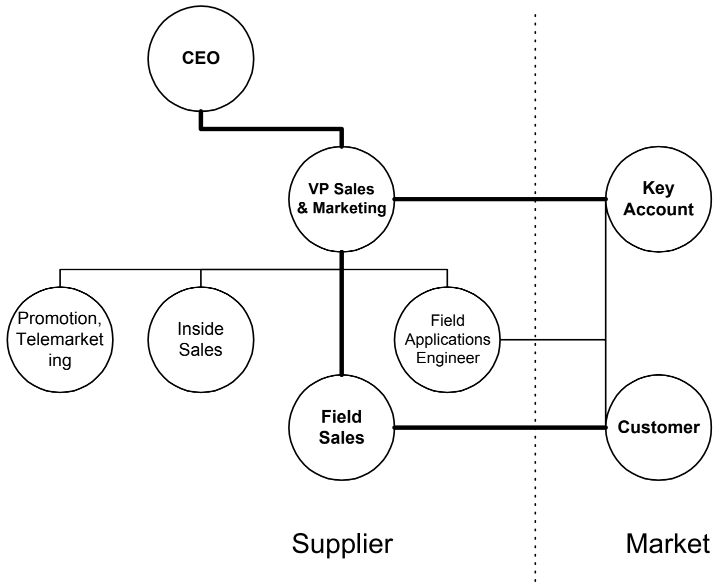


A direct sales organization is created at the founding of a company, when everyone wears many hats and the CEO is personally involved in selling. The CEO manages some key accounts. Design engineering supports the CEO and handles some technical problems, customer training, or design modifications. The CEO has hired one or more Field Sales people to take care of most of accounts and to generate new business. He hires them for technical competence, but does not know how competent they are at selling. They can answer technical questions, do most of the applications engineering, train customers, solve problems, and provide some support. Occasionally they use design engineers for technical support. The Field Sales people usually work out of the factory and periodically travel to their designated territories. Since they work directly with the CEO, they get quick decisions about resources, policies, prices, deliveries, priorities, etc.

The manufacturer's primary contacts are with the user-buyers of customers and prospects. Most of these user-buyers are Adventurers and Craftspeople, the early adopters. These buyers take the initiative to find manufacturers and identify new products. Account management for the manufacturer is primarily supportive, responding to requests for information, technical assistance, and quotes.

Mid-sized company

As the company grows, the CEO hires or appoints a VP of Sales and Marketing (or a National Sales Manager) to take over the management of Field Sales and to handle the key accounts. The VP of Sales and Marketing hires the Field Sales people and, if he is a sales professional, selects them for their selling skills rather than their technical competence. He hires Field Application Engineers to provide technical support to the customer. Design engineering is called on only when the customer requires design change to the products.

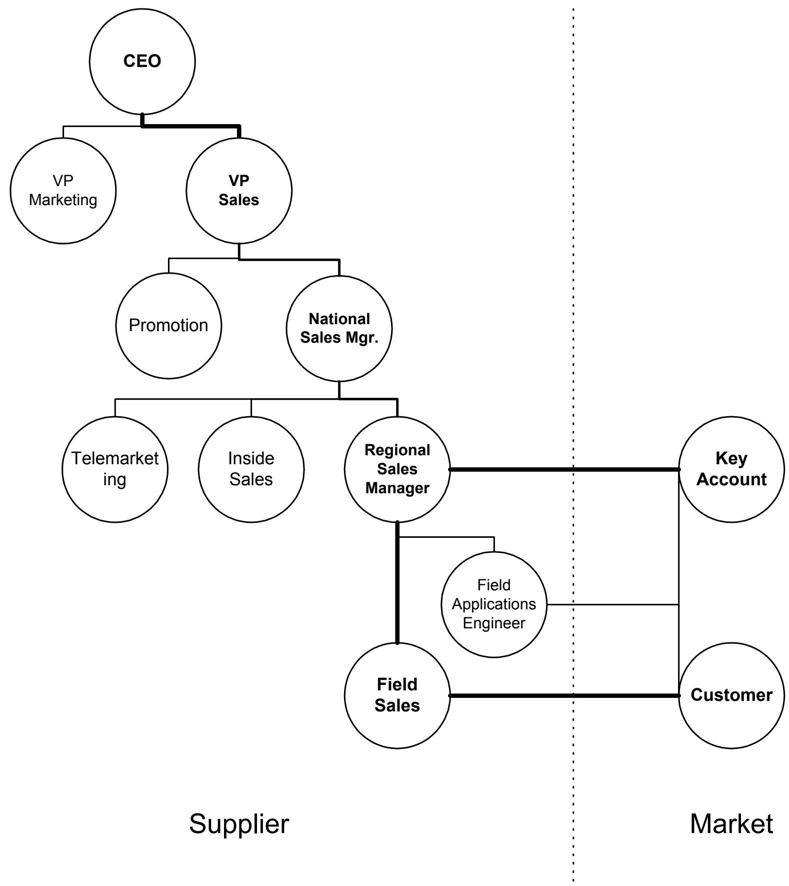


Because the Field Sales people report to the VP of Sales and Marketing, they can still get fast response on prices, and applications support. However, product design changes and product delivery issues become more difficult to deal with because their VP cannot allocate the resources of the Engineering or Manufacturing departments. Field Sales people usually have territories and sales quotas. Some of them work out of the factory, and periodically travel to their territories; others have offices in their territories and periodically travel to their factory. The ones who work out of the factory have better access to corporate resources; the ones with field offices have better access to their prospects and customers. The differences between being in the field and factory are critical, and neither location is ideal. Manufacturers often give these field sales people the title of "Regional Sales Manager" to enhance their credibility with customers and to make the Field Sales people feel better.

By this time many major selling opportunities are to Bureaucrat user-buyers and purchasing agents in larger organizations. These prospects typically have longer buying cycles, require better selling skills, and need more technical support and personal hand-holding to close than Adventurers or Craftspeople.

Larger company

As the company gets larger, its direct sales organization becomes further specialized and the VP of Sales becomes a full-time manager back at the plant. He or she may pay a courtesy visit to a customer site now and again, but doesn't personally manage accounts.



The people who interact with the customers and key accounts are the Field Sales people, Regional Sales managers, and the FAEs. Some or most of these people have territories and work out of offices that are remote to the plant but close to their customers. The company and its products are well established in the industry, its user-buyers are primarily Bureaucrats and secondarily Craftspeople. Most of its business is reorders from established accounts.

The Field Sales people seldom interact with those who determine pricing, delivery, and product changes. They work from rigid sets of directives, and must find customers who can accept these standards. Attempts to get deviations or special considerations from management are usually frustrating. Although these Field Sales people have the same title and job function vis-a-vis the customer as their brethren in smaller organizations, they have less freedom to act.

It does not take much effort to see that the executives who make the business and marketing decisions are increasingly isolated from customers as their companies grow. They work from distant memories of how the customer was, and from "data" passed up the chain of command. In later chapters we will discuss how specific problems, including lousy sales forecasts, are created by the chain of command.

Key people

The CEO
The CEO of a startup company is probably an Adventurer and a technologist in a field directly related to the company's product. He is more comfortable designing the product than selling it. However, in the startup phase he usually sells products by necessity, and discovers that he is very effective at it. He may observe, with mixed feelings, that he is more effective than the sales professionals he has hired. The reasons for this situation include:

- Customers that buy from a new company are primarily early adopters who are like the CEO: technologists and Adventurers.
- The Product is something the CEO would buy and use. He believes in it and understands its benefits to him and to the early adopter market segment.
- Adventurers buy functions, and the CEO can expertly and enthusiastically discuss his product's technical functions.
- The CEO is poorly prepared to attract, select, and hire the most appropriate Field Sales people. The people he hires probably aren't the most appropriate sales professionals to develop the market.

The CEO's field experiences can create long-term problems. As a technologist he probably had an unproductive bias about sales and selling. Field experiences reinforced a distorted view of how and why customers buy, in particular that customers are competent technologists who buy based solely on product functionality. When he hires a VP of Sales and moves out of the field, his selling experiences cease and his beliefs and expectations about customers freeze. What worked in the early market for the Adventurer segment (usually less than 10%) becomes the CEO's perception of what should work for the entire market. It colors his business decisions, his expectations of the sales organizations, and his willingness to allocate appropriate authority and resources.

CEOs of larger and older companies are likely to be Bureaucrats with no selling experience and a propensity to run the company by the (GAAS) numbers to protect themselves and the invested capital. Most of them have spent many years buried inside large organizations, and are far removed from the realities of customers and the marketing system.

VP of Sales
A Craftsperson VP of Sales is the most effective, a sales professional first and a technologist second. However, he is likely to have a credibility problem with a technologist CEO as he tries to develop a professional marketing system. The CEO is suspicious of non-technologists anyway, and the effective VP of Sales takes actions and hires people that don't fit his expectations. VPs of Sales have an average life expectancy of around two years in younger companies.

A Bureaucratic VP of Sales will accommodate the CEO's expectations (known as *kissing arse*) and won't systematically develop a professional organization. He'll tend to attract and hire Bureaucratic sales professionals. But he'll be one hell of a team player.

Regional Sales Managers
This has to be one of the most difficult jobs in any company to do well. It is equivalent to the battlefield General in the army who has to win battles and simultaneously garner support from a headquarters staff far removed from the battlefield. The Regional Sales Manager works with his customers, directly and through his field sales staff. That seems simple enough, but the context in which he is expected to close business is a management challenge second to none. He is probably in an office in his region, far away from the factory. He depends upon the National Sales Manager for resources, information, and support, but usually doesn't work with him on a daily basis. They seldom have a strong personal relationship.

Craftspeople Regional Sales Managers usually get the best results provided they have gotten appropriate management training and sales experience. They consistently meet or exceed challenging sales quotas, have satisfied customers, and have a enthusiastic and successful sales teams. They achieve this through effective planning and hard work. They support their people and help them get what the customers need. They do battle with the factory bureaucracy to get recognition and support for their people. During factory visits, they point out how the company can improve its support of Field Sales people and customers, and they have carefully developed data and plans to back up their suggestions. When a customer-hostile decision is on its way to the field, they speak up. In short, when they visit the plant they are hardworking pains-in-the-arse.

Bureaucrat Regional Sales Managers get much poorer sales results. They go back to the plant to soak up the company line, bring it back to their customers and subordinates, and indoctrinate them with it. When they are with their subordinates, they are authoritarian managers. When they are at the plant, they are cooperative, team players. They compensate for poor results with arse-kissing behavior to management. They spend more time negotiating their quota down than in getting their sales up.

Guess who usually gets promoted to National Sales Manager (and from there to VP of Sales) in larger companies? For that matter, which kind of general gets promoted to the Pentagon? (Hint: "team player" is more important than "gets results" for Bureaucrats.) Regional Sales managers who are bucking for promotion will not do the best job of building sales, a healthy sales organization, or a base of satisfied customers. In fact, this is a universal principle. We know it too well from politics: ***A Politician who does his job solely to get re-elected doesn't do the job that needs to be done.***

Field Sales Professionals
The field sales professionals who are attracted to startup companies are probably Adventurers. They are attracted by the challenge of developing new markets for new products. They enjoy selling to innovator and early adopter customers. They make decisions, take risks and assume personal responsibility for results. They thrive in fluid organizations, both their own and their customers', that are low on structure and high on action. They are willing to work hard, over extended periods for substantial emotional and financial payoffs. They do not enjoy working with Bureaucrats in large organizations over extended periods.

The Craftsperson field sales professional may take a few calculated risks in where she works, the products she sells, and the accounts to which she sells. Her strength is in systematically developing a market after it is identified and inroads have been made into it. She is more comfortable selling a product after some customers have already used it successfully. She usually has the best personal rapport with customers who are Craftspeople too. However, she is also effective at supporting Adventurers and Bureaucrats.

Many field sales professionals who work for large, well established companies are Bureaucrats. They like the security of being associated with a successful company and successful products. They like the comfort of predictable policies and procedures, the certainty of the products and customers, and the annuities produced by administering reorders from established accounts. They are most effective at protecting established business and useless at developing new markets for new products.

Economics

This discussion of the economics of Direct Sales organizations focuses upon the typical cost of planned sales calls and the cost of qualified leads. The revenues generated by a sales organization are proportional to the planned sales calls made on Prospects and Prospects-in-heat. Qualified leads are used to identify new Prospects.

Typical costs of planned sales calls

Planned sales calls are visits by a sales professional to prospective buyers at their places of business for advancing the buying/selling process toward closure. The call itself may take 30 minutes to two hours or more. Furthermore the sales professional has to prepare for the call, follow up the call, and travel to and from the call site. When the sales professional works out of a local office within two hours' driving distance of the average prospect, she might make as many as 640 planned calls a year (16 planned calls a week, 40 weeks a year). If she works out of the factory and travels to geographically dispersed accounts, she might manage as many as 260 planned calls a year (10 planned calls a week, 26 weeks a year).

For a sales professional who is paid $80,000 in salary and bonuses and who also costs his company another $20,000 in benefits, the total **costs for each planned call are approximately $230 from a local office** and approximately **$450 from the factory**. Of these costs the time and expenses related to travel are approximately $60 from a local office and approximately $280 from the factory! However, these costs do not include all overhead costs (managers and support systems) or the relative costs of a local office and its infrastructure versus the equivalent system in the factory. When these costs are included, the total costs for sales calls are much higher.

Typical costs of leads from Advertising

There are so many variations in advertising costs and numbers of leads generated that any thorough discussion of costs would quickly be swamped in detail. I will simply describe my own experiences which are typical. You can follow the same line of reasoning to determine the cost of leads for your organization.

At Pro-Log we ran full-page, four-color ads in technical magazines targeted to design engineers in our target markets. These ads cost us roughly $6000 per page (including amortized design costs). An ad would generate between 20 and 150 leads; the average was about 70 leads, mostly bingos. We would mail a packet of literature and/or we would place a telemarketing call to qualify the lead. Between 5% and 10% of the leads turned out to be valid prospects. If we assume that 50% of the cost of advertising is for lead generation,[18] then the average costs for each unqualified lead were approximately $43 ($6000 per page x 0.5 ÷ 70 leads per page). We spent another $10 per unqualified lead to qualify them. On the average then, **each qualified Prospect cost us more than $530** ($43 + $10 @ a 10% qualification rate) to attract and identify, before we even made the first field sales call on them! At this point we still didn't know how profitable these prospects might be, and our credibility with them was still very low.

[18]The other 50% is to maintain credibility and visibility with prospects, customers, and the sales force

The point of this exercise is to show the costs associated with developing leads with advertising and a direct sales organization. As I'll show in the next few chapters, the principal benefit of other channels is a base of qualified prospects! For example, **each qualified prospect a Rep or Distributor organization has for a manufacturer when they start working together would otherwise cost the manufacturer at least $600 to develop with advertising and telemarketing**. The actual value of each prospect is probably twice that amount since the knowledge and credibility that the Rep or Distributor has would take the Manufacturer's direct organization one or more field sales calls to duplicate.

Costs of Trade Show Leads
When a Direct Sales organization goes to a trade show there are three objectives: to generate leads, to see what the competition is doing, and to have fun. The typical costs for a 10' by 10' location at a three-day national trade show costs around $10,000. The trade show booth (amortized over several shows), shipping costs to and from the show, demo equipment, and literature cost another $5,000. When the booth is staffed by three people from the factory their travel and labor costs are very roughly $10,000. When things went well at a Pro-Log booth, we generated about 300 unqualified leads at a three-day show. At best, 20% of them turned out to be valid prospects. At that rate, the approximate cost per qualified lead was about $500, roughly the same as through advertising.

There are other, less expensive ways to generate leads, including the use of news releases and applications articles. The least expensive, and most effective way is through referrals by existing customers.

> ***N.B.***:*A qualified lead costs around $500 and takes months to identify and reach. When an appropriate third party sales organization joins the marketing system, it brings a customer base with it that includes many pre-qualified leads that can be reached in a matter of weeks.*

Strengths

Sales team is kept relatively well-informed about manufacturer's business.
The manufacturer's management views the Direct team as part of the company and is more inclined to share business and technical information with them than with third party organizations.

Sales team hired and trained specifically to sell manufacturer's product.

Sales team provides the most direct feedback path (compared with other channels) between customer and manufacturer.

Weaknesses

Sales professional's credibility is suspect with prospects and customers because he has only one product line to sell.
The direct sales person starts with the least trust and confidence on the part of a buyer who is evaluating competitive alternatives. The buyer expects a prejudiced presentation.

Sales professional only gets in prospect's door when prospect is interested in product.
It is relatively difficult and expensive to gain access to a prospect with just one product or product line. The direct person must usually wait to establish credibility until the individual has a significant interest in the single product he represents. The person who represents several products or solutions can establish credibility on one of them, and be in place to influence the prospect's interest in the other ones.

Sales professional effectively sells products to their specifications, but is poor at selling solutions.

Prospect assumes that the cost of all services required to make a product fit into his application is included in the Product's price.

Costly travel is required to cover small, widely dispersed accounts.
The travel costs add no value to the product.

Management issues

Management expects sales professionals to sell because they are employees.
Management in a direct organization (starting with the CEO) doesn't believe it has to "sell" its objectives and its products to its sales force before it sells them to customers. Management generally assumes that paychecks and bonus programs are sufficient motivators to sell. Because employees have nothing else to sell, no competitive alternatives, they are told what to sell and how much to sell. Management would get better results by selling to their sales organization first. This selling process is the same as it is for prospective customers. It requires managers to listen to employees, work through their objections, and find personal attractors that develop their individual enthusiasm and commitment.

Management expects sales professionals to give their employer and its products 100% share of mind.
A widely held management myth about selling is that it is desirable for the company to have a 100% share of mind from its sales professionals. The ideal share of mind is around 30% for the product and its success, another 60% for the customers and their successes, and the balance involved in a healthy respect for the customers' competitive alternatives. When that mixture of mind share, the sales professional is not a docile doer of company mandates, but an effective advocate for prospects and customers.

Most sales compensation is unrelated to producing successful business.
Sales compensation is usually based on gross order dollars and not on the order's profitability or a customer's long-term success with the manufacturer's products. It tempts sales professionals to book orders at any cost, and leaves it to others in the company to play bad-guy and to weed out unprofitable business.

Loyal employees only report culturally acceptable bad news.
I hinted at this problem in discussing the job of the Regional Sales Manager. Every CEO I know, including myself, **says** that he wants to hear the bad news. But every CEO also broadcasts unmistakable signals about which bad news he'll accept, which news he'll ignore, and which news will tempt him to kill the messenger. For most CEOs, messages like "we lost the order because our price was too high" or "times are tough and people just aren't buying" are culturally acceptable, so they become the messages the CEO is told. The true situations may be quite different, but culturally unacceptable.

Large manufacturers have a long, shaky chain of command.
The most serious problem with a long chain of command is that virtually no information makes it up the chain, and no management directives make it down the chain in any semblance of their original forms. Furthermore, the people who make strategic decisions are thoroughly isolated from the customers. The people who work with customers have little or no direct access to critical resources.

Best customers

The best customers are the ones who order more than $50,000 per year (or account for more than 0.5% of gross revenues, whichever is greater) of standardized products and services, and who take the responsibility for fitting the products to their applications (Adventurer or Craftsperson user-buyers). The standardized services referred to include: demonstration and evaluation units, product documentation, product training, options and special features, spares, updates, JIT delivery, Price/terms, factory level warranty, and repair.

Worst customers

The worst customers are the ones who order less than $10,000 per year, are geographically dispersed, have long buying cycles, expect the manufacturer to fit the product to their application (Bureaucrats and Victims), and require special services. Special services include: application engineering, products of other manufacturers, design engineering, system integration, installation and testing, solution documentation, problem solving, and on-site maintenance.

Exercises

1. Estimate the cost of a planned sales call in your Direct Sales organization. Break the costs down into labor, travel costs, and appropriate items of burden. Include the time, and costs to plan for, and arrange the call, and the time, and costs to follow up the call with appropriate actions.

2. Estimate how many planned sales calls it takes to close a typical customer. What percent of planned sales calls wind up being spent on prospects who don't buy?

3. List the five most significant ways your company generates leads. How many unqualified leads did each way generate in the last three months? How many qualified leads did each way generate in the last three months? What was the approximate cost for each qualified lead? (Don't be surprised if your company doesn't have much data on this.)

4. Select about twenty of your company's good customers. How did each of them first learn about your company, and its products? How does this relate to your present lead-generating activities?

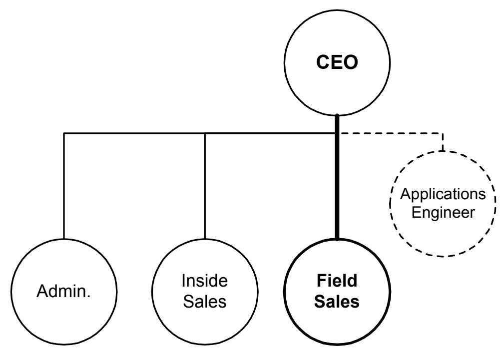
10. Manufacturers Representatives

In this chapter, we will extensively analyze the Manufacturers Representative organization. We will examine its structure, the beliefs and attitudes of its key people, its economics, its working relationships with manufacturers and customers, its strengths and weaknesses, and its best and worst customers. Much of this material also applies to other channel organizations and will be referred to in those chapters.

Manufacturers Representatives generally have a poor reputation in the world of high-tech selling, particularly among Venture Capital people. This reputation is largely undeserved. It stems from ignorance and myths about them. I worked with them for more than sixteen years, and they made critical contributions to the success of my company. This chapter replaces myths with information. I hope it dispels some ignorance and promotes respect.

Structure

The typical Manufacturers Representative organization is a small business that represents between seven and 30 different manufacturers. It sells their products in a specific geographic territory, for example New England or Southern California. It is typically organized as shown in Fig. 10.1, with an owner/manager as its CEO, Field Sales, Administrative support, Inside Sales, and sometimes Applications Engineering.



Manufacturers Representative organizations come in all sizes. The smallest one I have worked with was a one-person company that operated out of a home office. The largest had over a dozen field sales people and another dozen support people working out of formal offices in four different cities.

Key people

CEO

If you're already familiar with Manufacturers Representatives, you may wonder why I call the owner/manager a CEO. It emphasizes a critical point: Sales Rep organizations are small businesses and their leaders really are CEOs. Manufacturers who understand and respect this fact will get the best results from them. The owner/manager of a channel organization put it this way:

> " *I was a salesman, but now I'm the CEO of my own company. I hire, fire, and manage people, have to meet payroll, and I worry about long term stability and profits. I have more in common with the CEOs of my principals (manufacturers) than with anyone else in their organizations. The trouble is that Regional Sales Managers try to manage me. They are sales people who don't have my experiences and don't understand my perspective or my needs.*"

These CEOs have extensive sales experience and a degree of technical proficiency in the products they sell. Many of them are shrewd business people and decent managers. Some are not. Many of them wear Field Sales hats and continue to sell in territories or to key accounts.

A few of these CEOs are Adventurers, on the lookout for new products and new markets. Most are Craftspeople trying to develop and sustain a successful business by effectively representing a group of competent manufacturers to an established base of customers. Some are Bureaucrats who sit in their offices clipping coupons, signing up any manufacturers who cross their thresholds, and waxing on about past glories. The Victims quickly go out of business.

The Sales Rep's CEO considers his customers to be his principal business asset. As one of them told me "*It is easier for me to replace one of my manufacturers than it is to replace a major customer.*" Manufacturers come and go quite frequently, sometimes for reasons completely beyond the control of the CEO. However, customers have been carefully developed, and the key accounts can be maintained by giving effective support even as manufacturers change; consequently the CEO and his staff focus their efforts on customer support.

Another very successful CEO described how he categorized and supported his customers. His A accounts were those that generated significant annual revenues (commissions) and bought the products of at least half the manufacturers he represented. His B accounts generated significant commissions but mostly from one or two product lines. His C accounts were any other active accounts.

His A accounts were his key asset. They were given his organization's finest coverage and service. Each week he updated and distributed his list of A and B accounts to everyone in his organization. His people were trained to say "yes" immediately to a request from an A account and then to follow through without worrying about policies, procedures, or approvals. His reasoning was simple: the A accounts generated substantial revenues and they were really his customers, not the customers of specific manufacturers. He retained their business because he provided a unique combination of products and services for them that wasn't dramatically altered by the loss of a single manufacturer.

His B accounts were important because individually they generated as much or more revenues than an A account. However, the revenue from B accounts was tied to specific manufacturers. Consequently, the Sales Rep was less essential to the customer or to the manufacturer. Manufacturers could (and often did) unilaterally reduce the commission rate or terminate the relationship. The organization provided excellent support to B accounts. However, the CEO was less inclined to bend over backwards for them. Support was subject to policies, procedures, and approvals.

Field Sales people

Field Sales people are professionals at selling and may or may not have technical backgrounds. Some of them are Adventurers who enjoy the challenge of introducing new, complex products into new markets. Many of them are Craftspeople who put their best efforts to selling proven products into established markets. Many are Bureaucrats who never sell anything complex or risky and they play gofer between prospects and manufacturers, letting the manufacturers do the selling and support work for them. Successful Rep organizations will include a mixture of Adventurers and Craftspeople with a smattering of Bureaucrats. The older and larger organizations have few, if any, Adventurers, some Craftspeople, and many Bureaucrats.

The CEO hires the Field Sales people. Their educational background, competence, and attitudes depend on his selection criteria and his management skills. He measures their performance by how much commission revenue they produce, not by how well they sell the products of specific principals.

The Rep organization usually pays the field sales person's expenses and overhead costs, a nominal base salary (or an advance against commissions) and a commission of 30-50% of the commission payments his firm receives from manufacturers. A Field Sales person actively sells two or three of the product lines he represents and “takes orders” for the rest of them (the financial reasons for this behavior are described below in the economics section). He earns most of his commissions from his top three lines.

A Field Sales person has a specific territory within driving distance of his home or his office. He works in the business office once or twice a week and travels to customer and prospect sites the rest of the time. The Rep CEO generally requires all the field sales people to work in the business office Monday or Friday morning each week to plan, organize, and provide mutual support. The CEO prefers to schedule manufacturers’ training sessions for the same day to reduce interference with account calls.

The Field Sales people look upon their customers as their key *personal* assets. They work closely with their accounts, know the people, and have developed personal credibility. They believe that both their income and their job security rest more on these working relationships than on any other single factor. Each Field Sales person has his “black book” on his accounts. The black book is his personal data base, one he is reluctant to share with manufacturers or with his own management because it is a form of job security. This reluctance to share is a stumbling block to automating account information, because then the data is a company asset and the Field Sales person feels less secure in his job.

The priorities of a Field Sales person also conflict with his CEO’s priorities. The Field Sales person probably works for short-term income and deals with customers and RSMs that are personally satisfying. His A accounts are probably his company’s B accounts. The conflict in priorities is both rational and human. On the rational side, the Field Sales person could lose an account’s revenue within a few weeks or months because:

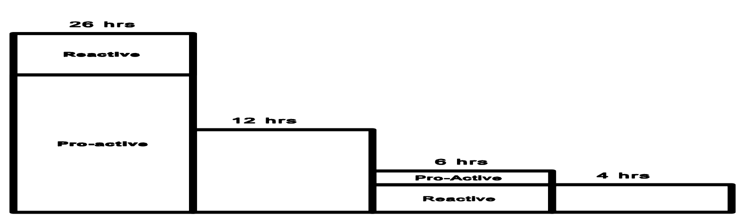
- a manufacturer terminates the Rep organization
- his CEO terminates him or changes his territory
- he voluntarily resigns

The probability that one of these events will happen within a one-year period is high, so he concentrates on short term revenues. On the human side it’s easier and more fun to sell one or two products, to support a few happy customers, to work with one or two of the more comfortable RSMs, and to get rewarded soon after putting in the effort.

A Typical workweek

One of the more interesting aspects of the lives of these Field Sales people is how they spend their workweeks. Fig. 10.2 shows a typical 48 hour work week (am I being realistic or just kissing up?) divided among activities I have classified as:

- customer proactive
- customer reactive
- travel
- manufacturer proactive
- manufacturer reactive
- organization.



Customer proactive activities include planning and making account calls, and other account management. *Customer reactive* activities include responding to customer requests or firefighting problems. *Travel* includes the time driving to and from customer sites and waiting in lobbies. *Manufacturer proactive* activities include: scheduled training and systematic study of each manufacturer's products, sales presentations, and attending manufacturers' regional or national sales meetings. *Manufacturer reactive* activities include: handling phone calls from manufacturers, processing leads, filling out reports, and visiting accounts with manufacturer dignitaries. (Please note that this is the total spent on all of the seven to 30 manufacturers he represents!) The Organization category includes reports, plans and forecasts required by the CEO as well as weekly planning and coordination with the CEO and the rest of the staff.

The relative times shown in Fig. 10.2 vary widely among Field Sales people, but what is important is to appreciate the variety of competing influences that affect their use of time.

Inside Sales people

Inside Sales Professionals handle inquiries from the customers' purchasing agents, quote standard prices and deliveries, and book orders over the telephone. They also process requests for product literature. In some organizations, the inside sales people do outbound telemarketing to screen leads provided by manufacturers. Most organizations send periodic mailings of promotional literature to their customer and prospect base. A typical mailing might be an eight-page, quarterly newsletter featuring some manufacturers, announcing new products, and introducing the Rep Organization and its people.

Applications Engineers

Applications engineers are optional members of the organization. Some Rep firms have them; others hire field sales people with technical backgrounds and expect them to answer basic technical questions and provide basic technical support. Applications engineers in a Rep organization are more likely to be technicians than degreed engineers. They work in the office and respond to technical questions from customers and field sales people. They pass complex technical issues to the field applications engineers and technical support staffs of the manufacturer.

In some organizations, applications engineers support just the one or two of the product lines, usually the ones that generate the most revenue. Part or all of their salary may be paid by manufacturers with the understanding that their time is dedicated to those manufacturers' products.

Informal Resources: Consultants

Effective Manufacturers Representatives know their territories, do business on a personal basis, and cleverly employ resources that fall outside their official organization. For example, they commonly use technical consultants, independent contractors whom they refer to customers. Rep CEO's and their field sales people know the value of design support in closing orders; the person who does the design usually decides what products are used in it. However, they don't want to be responsible for managing or paying for this support. They solve this problem by developing informal working relationships with consultants who have successfully used the products they represent.

When a customer or prospect asks for design support, a Rep refers her to one or more of these consultants. There is no charge to the customers or to the consultant for the referral. The customer interviews the consultants and usually hires one of them. The Rep and the consultants have an informal understanding that the consultants will use the Reps' products, unless competitive products are significantly better.

Human nature being what it is, this process works well without heavy-handedness or skullduggery. First, most technical consultants, like most of us, probably will use something on the next job that succeeded on a previous job. They have a natural barrier to change unless a serious problem crops up. Second, most technical consultants have a sense of fairness and feel indebted to the Rep for referring business to them. Third, the customers are already favorably inclined to the products and to the Rep, or they would not have asked for referrals. They expect the consultants to use some of the Rep's products.

This arrangement has another distinct financial benefit. When the customer selects a consultant, she automatically expects to pay the consultant for his work. When a Rep or manufacturer provides the technical support, the customer presumes that the consultant's cost is included in the price of the product.

Economics

Revenues

The top three product lines of a Manufacturers Representative organization usually generate about 50% of its commission revenues. The top one or two lines are actively sold by most of the Field Sales people, but not necessarily by all of them.

The CEO tracks two revenue numbers for each product line: commissions and bookings. Commissions pay his bills and determine the product's profitability to his organization and to his field sales people. Bookings are what the manufacturers measure to judge the Rep organization's performance. Commissions are a percentage of bookings, but the percentage varies widely from product line to product line and sometimes from order to order. The CEO's objective is to have total commissions from all product lines pay the bills (including a healthy income for the CEO) and generate a reasonable profit.

Costs of Selling

The costs and commission requirements for each Field Sales person normally fall in the following ranges:

	Bottom Quartile	Top Quartile
Field Sales person's income, benefits, and commissions	$ 60,000	$ 100,000
Overhead including facilities, support staff, management, travel, etc.	$ 75,000	100,000
Burdened Annual Costs	**$135,000**	**$200,000**
Annual Bookings required to break even at a 10% average commission rate.	$1.35 million	$2.0 million
Annual Bookings required to gross 15% pretax profits (on commissions) at a 9% average	$1.7 million	$2.5 million

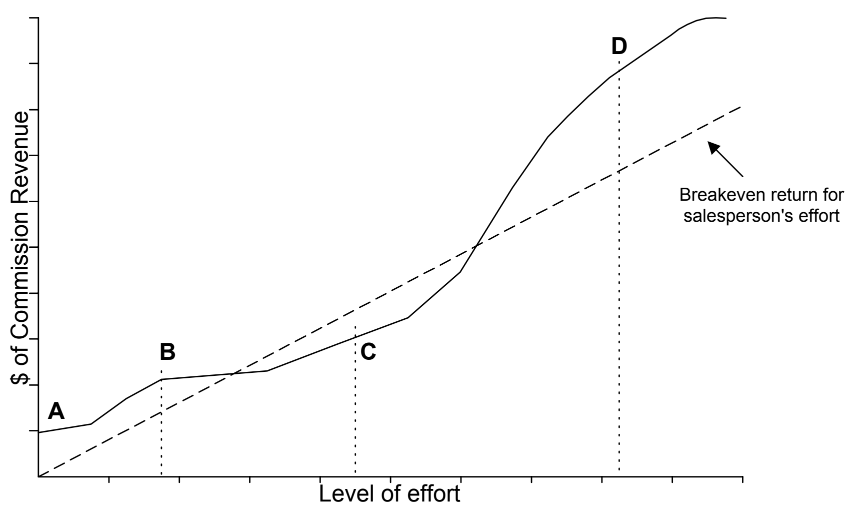
commission rate.

Average costs of a planned sales call

An important piece of financial data that comes from these annual costs is the fully burdened cost of a planned sales call by a Field Sales person. The average Field Sales person makes about three planned calls a day, four days a week (he's in the office one day a week) 44 weeks a year (he has vacation, sick leave, and must attend many manufacturer-mandated sales meetings). That comes out to about 500 planned sales calls per year. If we assume, as do most sales organizations, that these calls generate the commission revenues, then on the average each call must generate between $270 and $400 in commissions just to pay the burdened costs for the Field Sales person. Put another way, each call costs between **$270** and **$400**. This range of costs is comparable to the costs of a planned sales call in a Direct Sales Organization.

A Manufacturers Representative's profit alternatives

A Field Sales Professional can make money from a particular product line in one of two ways: either by investing either very little effort (typically less than 5% of his time) or by investing a lot of effort (more than 15% of his time). It is relatively unprofitable for him to work at sustained level of effort in between. If he handles a dozen lines he can only expend the higher level of effort on two or three lines at most. To understand this situation better, let us examine Fig. 10.3.



The curve of Fig.10.3 relates income to effort. The solid line represents the typical relationship between the sales person's effort for a specific product line and the total annual commissions that the product line generates for him in the first year. The sloping dashed line represents the break-even revenue required to pay for the effort. Of course the actual slope of either line, and the actual profitability at any level of effort, depends on such factors as commission rate, typical order size, difficulty in making sales, and competence of the sales person. However, the principles illustrated by this figure aren't changed by those variables.

Point A on the curve is the revenue an individual Field Sales person receives for doing nothing. It comes from sales that close with or without a Rep in the territory and is a result of the manufacturer's efforts and referral selling. These bookings are generated by a few Adventurers or Craftspeople customers who sell themselves on the product and then work directly with the manufacturer. Putting no effort into selling a product line is a somewhat risky behavior since the manufacturer might catch on and terminate the Rep organization.

However, when one sales person in a Rep organization actively sells a product line, another sales person can successfully operate at point A for that product line without being terminated.

Point B represents an effort of about 30 minutes to 90 minutes a week, which is the time spent by most sales people on most of their product lines. As shown, the profits per hour invested are very high. The Field Sales person spends a good part of this time interacting with the manufacturer. He has a superficial knowledge of the product line and its applications so he is selective about selling it. He drops off literature to customers he feels secure with and he responds to eager prospects with price and delivery information. He does not actively seek new business or pursue difficult prospects. This level of activity is profitable enough to keep Rep CEOs happy and it improves sales enough to satisfy most manufacturers.

Point D represents the revenues and time (about two to six hours a week) that sales people invest in each of their top two or three product lines. They spend more than 80% of this time working with prospects and supporting customers and less than 20% interacting with manufacturers. They are expert about the product lines and their applications, provide effective selling support to most customers, and actively pursue new business.

When sales people operate between points B and D they sell more and have more product knowledge but they are not fully proficient, comfortable, or enthusiastic about the manufacturer or the product line and its applications. In most of this region, they aren't sure that the added effort is paying off. For example, at point C, the overall commission income doesn't cover the expenses. Since this region is unprofitable, it is unstable. Personal attractors either draw them to D or back to B.
The curve of Fig. 10.3 is simplistic, but it accurately illustrates a basic truth:

> ***It can be highly profitable for a Manufacturers Representative to sign up a product line and then do very little to sell it*.**

If money were your only motivator, and you were an astute field sales person or the CEO of a Sales Rep organization, you too would probably sign up lines to cherry pick orders. Therefore, it is silly for manufacturers to decry this behavior and much more productive to understand it and work through it. The management question is: how can a manufacturer establish a region of mutual profits and mutual benefit where they and the Manufacturers Representatives thrive? We'll provide some answers later in the book.

Relationships between selling efforts and commissions
Field sales people invest most of their time and money on prospects before prospects buy (refer to Figs. 5.2 and 5.5). However, they usually don't receive commissions for orders until the products are delivered and paid for. The times between the efforts and the compensation are at least a few months and may be a year or more.

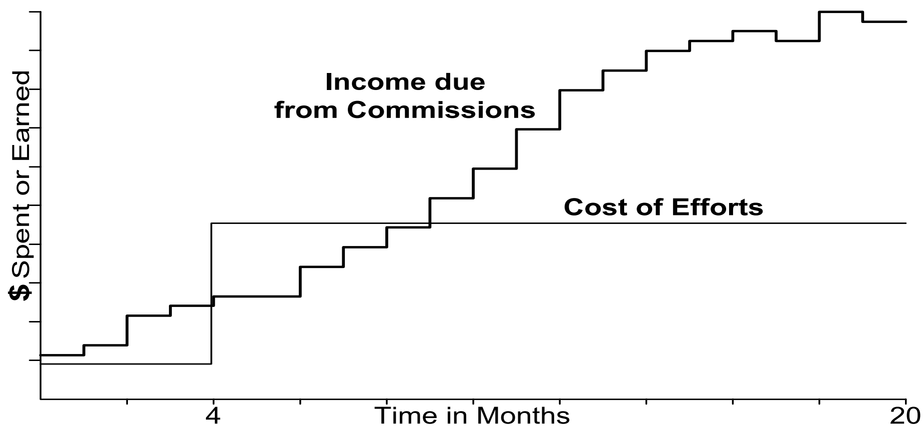


Figure 10.4 illustrates a typical relationship between the monthly costs of a field sales person's efforts on behalf of a manufacturer and monthly commissions due from the resulting orders.[19] This relationship is tracked for the first 20 months after he begins to sell for a manufacturer. The Cost of Efforts line shows that the field sales person makes a minimal effort for the first four months, then steps it up for the next sixteen months to make the line one of his top three.

After the fourth month, he works diligently on behalf of the manufacturer, learns the product line and its applications, identifies and pursues prospects and prospects-in-heat among his existing customers, and looks for prospects outside his established customer base. His Commissions increase slowly, but don't match his added costs until after the tenth month. In fact, the Manufacturers Representative and his organization do not fully recover their costs until well into the second year.

In effect, the Sales Rep organization has financed the development of the manufacturer's market for the first year to recoup a healthy profit after that. Somewhere along the line, the Rep CEO and the field sales person had to be convinced that this was a good investment. They had to be sold and had to stay sold.
Critical management issues are related to all this, so hang in there for one more timing curve.

[19]The actual payments are made to the Sales person is at least 45 days after the commissions are booked.

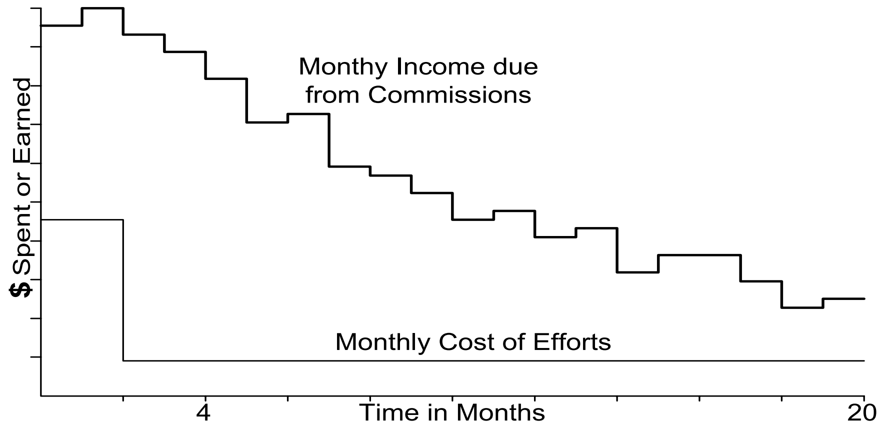


Fig. 10.5 illustrates what happens to commissions when a Manufacturers Representative who has been working hard for a manufacturer stops selling its products. In the first two months shown in this chart, the Field Sales person works hard and receives a high level of commissions. In the third month he minimizes his efforts. Sudden drop in sales efforts happen all the time. They are triggered by such things as:

- The manufacturer alienates an important customer of the Field Sales person.
- The manufacturer fails to provide timely support, and the Field Sales person doesn't book a large order he had worked hard to get.
- The manufacturer's management mistreats the Field Sales person.
- The manufacturer unilaterally decreases commissions or degrades other terms of the working agreement
- Another manufacturer convinces the Field Sales person to make its product line one of his top three, and he transfers his efforts.
- The Field Sales person's CEO directs him to re-prioritize his energies.

Although the salesperson's efforts drop sharply, his bookings and commissions continue at a high level for a few months before decreasing slowly over a period of a year or more. Old customers continue to reorder, new accounts that were well into their buying processes also order, other accounts order because of referrals by satisfied customers. Furthermore, this period is enormously profitable for the Field Sales person and his organization.

The relationships showed in Figs. 10.4 and 10.5 affect the behavior of Rep organizations when they sign up with new manufacturers and when they part company with old manufacturers.

Starting to sell for a new manufacturer

Look again at Fig. 10.4. When a Rep organization first signs on with a new manufacturer, where do the Field Sales people find the time to learn about and effectively sell its products? They reduce their work for one or more of their other product lines. To entice them to do this, the manufacturer has to sell them, one by one, on the idea that they will be better off selling its products than one of product lines they already sell. The Field Sales person is a buyer, a customer who has his other product lines as competitive alternatives to supporting the new manufacturer. The manufacturer can't direct the person to sell; it must sell him on it! In Chapter 17 we'll discuss how to get channel organizations to sell for you.

Behavior when terminated

You are managing a Manufacturers Representative organization whose bookings decline. You look into the matter and decide that the organization is not diligently selling your products. You issue a written warning: *change within 90 days or you'll be terminated*. You receive profuse assurances from the Rep's CEO and his people that they are fully committed to your line.[20] Still, bookings continue to shrink. You visit the sales people frequently, provide extra training, and make sales calls with them. Finally you terminate them. Within 48 hours of receiving the termination notice, the Rep CEO jumps on a plane and shows up in your office with a well-documented turnaround plan. He promises extensive efforts, gives you incredible stories why this trend is part of the overall business picture in his territory and not a lack of effort by his organization, etc. You rescind the termination and grant another 90 days to get results. Nothing changes and you finally end the relationship. **This is not a hypothetical situation; it happens all the time!**

What was going on? Why did the Rep's CEO bother to fight termination when he had no intention of doing anything constructive? Why the deceit? From the Rep's point of view his behavior was rational, necessary, and fully justified for two reasons:

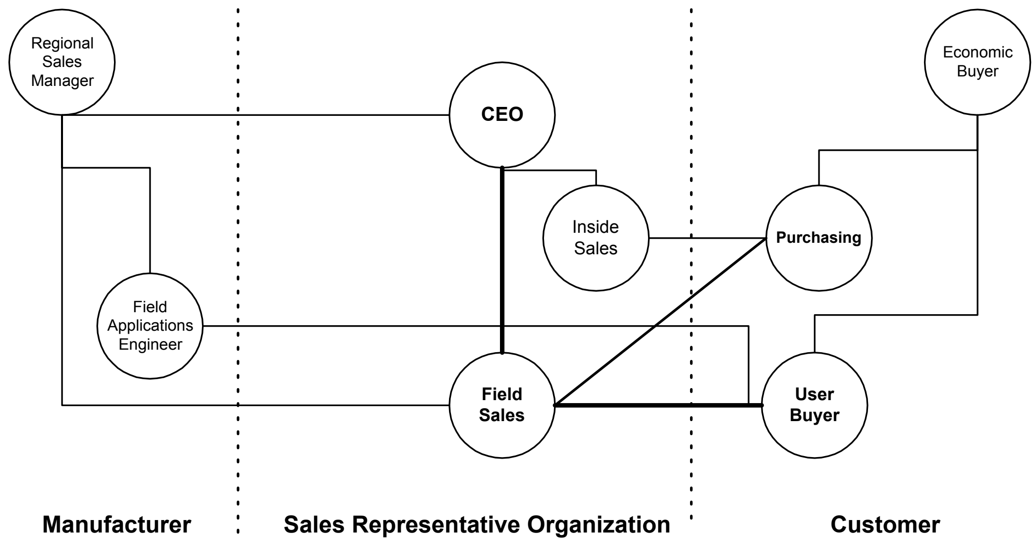
- Most of the commissions paid while he stalled and postponed termination were rightfully his; the result of his earlier investments of time and money
- According to the termination clause of your working agreement, assuming it was typical, your commission payments were limited to orders received within 30 days of termination and shipped within six months of termination. These conditions deny him commissions he has rightfully earned on long-term business.

His only viable option was to stave off termination for as long as possible, put in as little effort as possible, and recoup as much as he could.

[20] Sometimes they mean it. However, a manufacturer doesn't see a significant decline in bookings until several months after the Rep organization stops actively selling, so the root problems are already well entrenched and are likely to be irreversible.

Working relationships

Fig.10.6 shows the primary working relationships between people in a manufacturer's sales organization, a Sales Rep organization, and a Customer's organization.



The Sales Rep organization is usually managed by a manufacturer's Regional Sales Manager (RSM). This presents an interesting set of situations:

- Because the manufacturer pays them commissions, the RSM and his managers (particularly the CEO) are inclined to treat the Rep like part-time contract labor.
- Between 7 and 30 RSMs are simultaneously trying to manage the Rep organization, each for his own benefit and somewhat to the detriment of all the other manufacturers.
- An RSM does not understand the business viewpoint of the Rep's CEO.
- An RSM is often not well trained as a manager.
- An RSM's sales objectives for the Rep are seldom in the best financial interests of the field sales people or the Rep organization.

Most manufacturers and their RSMs tend to bypass the CEO. They try to manage the Field Sales people directly. One example is a sales incentive program that pays bonuses directly to the Field Sales people. I described the viewpoints of the Rep CEOs and the field sales people earlier in the chapter. In the long run it does not pay for manufacturers to exacerbate these conflicts.

I know of a situation in which a field sales person in a Rep organization was named the salesman of the year by a manufacturer and he was fired by the Rep CEO a few months later. The two events were related. The field sales person had succeeded for the manufacturer because he sold that manufacturer's products almost exclusively. His CEO had vainly attempted to keep his activities in balance so that his customers would not become just customers of that one manufacturer. After he received the award he was totally unmanageable. This story has an epilogue. The field sales person went to work for a competing Rep firm, confident that the manufacturer would transfer its business to his new firm. It did not happen.

Strengths

The strengths of a Rep Sales organization in comparison to Direct Sales organization are as follows:

Has already established credibility with customers

A successful Sales Rep organization has developed a client base within its territory that knows the Rep and has a certain level of confidence in its people, in the products it represents and in the support it will provide. The Rep's credibility can substantially shorten the manufacturer's time to market. One of the two most significant reasons to sign up a Manufacturers Representative organization is to gain access to its customer base. Unfortunately, many manufacturers sign up Manufacturers Representatives without knowing who their customers are and then expect them to prospect for new customers.

Improves the manufacturer's cash flow

Reps finance many business costs of making the sale. They may carry net investments on some customers for years before recouping them in commissions. Cash flow improvement is one of the two most significant reasons for signing up a Manufacturers Representative.

Is more important to a customer

The Rep field sales people make more calls on each of their accounts than any one of their manufacturers can afford to make. They fill several needs of each account with more than one product line. The level of business and the frequency of contacts increase the relative visibility and credibility of the Representative to the account, and vice versa. The customer expects more responsiveness to his needs on any one product because of the total level of business conducted. The customer gets more support because he represents a much larger part of the Sales Rep's business than he does of a manufacturer's business.

Is more application-focused than product-focused

The Rep's Field Sales people learn what their accounts are doing and how their products meet account needs. They study product lines in a context of actual applications. They can accurately evaluate the potential for a specific product at a specific account and then talk with the account about how the product will meet his needs.

Has access to local consultants

Local consultants can provide technical support to customers, and customers will pay for the support and not expect it to be included in the price of the product.

Sells more profitably to smaller accounts

Synergies among the Rep's product lines create opportunities for Reps to sell or support the products of manufacturers B and C during sales calls for manufacturer A. This is crucial to the financial success of Reps, and is to the overall benefit of all manufacturers. Oddly enough, many executives of manufacturers get upset when they travel with Reps and hear other product lines being discussed. This reaction is a significant irritant to Reps because it shows a lack of understanding and respect for the Rep's legitimate business needs.

A variable expense to the manufacturers

Reps get paid for results, not for their costs. They are not fixed expenses for the manufacturers like the salaries and support costs for their direct channels.

Weaknesses

The major weaknesses of a Sales Rep organization when compared with a manufacturer's Direct Sales organization include the following:

Not as versed in manufacturer's product

The typical sales person has to keep up with at least six other product lines. He is not technically proficient and must rely on the manufacturer for detailed technical answers that a direct salesperson might know.

Mind-share of Field Sales person is less than two hours per week

Unless the manufacturer is one of the top three lines for a sales person, it receives less than two hours per week of his thoughts and actions.

Can lose credibility with some of a manufacturer's key accounts because of account problems with other product lines

A customer may become alienated from a Manufacturers Representative organization when another one of its manufacturers lets the customer down.

Management issues

Manufacturer treats Rep as (cheap) contract labor

- Doesn't listen
- Inflexible responses to requests
- Manufacturer's executives lack respect and are suspicious
- Not trusted with manufacturer's latest information
- Less informed about manufacturer than are some customers
- Told (through annual forecast debacle) how much to sell

There is an intrinsic conflict of interests among four parties

- Manufacturer
- Rep CEO
- Rep Field Sales person
- Other manufacturers on the Rep's line card

The Rep CEO manages Field Sales people based on his priorities, not the priorities of a manufacturer

A manufacturer may find that a Field Sales person in a Rep organization is not selling his products and he is losing important business. However, the CEO of the Rep organization determines who calls on which accounts. He probably will not replace a Field Sales person who is doing a good job of selling the other product lines.

Territorial exclusivity

The Sales Rep organization has signed an agreement with each manufacturer that authorizes the Rep to promote the manufacturer's products in a specified territory and to quote factory authorized prices and delivery. The customary agreement commits the manufacturer to pay the Rep a commission for all sales made in the Rep's territory, whether or not the Rep helps to make the sale. It also commits the Rep not to handle other product lines that the manufacturer deems to be competitive with its own. Exclusivity, its pitfalls, and alternatives to it are discussed at length in Chapter 20.

Termination causes and length of notice

The customary agreements may be terminated by either party with 30 to 90 days' notice. The termination clause is a sore point with the Rep CEO because it makes long term commitments risky. As a result:

- He cannot afford to depend on any manufacturer for too much of his income. He must be able to recover from being terminated by any manufacturer.
- He cannot afford to pursue very many major accounts with long selling cycles on behalf of any one manufacturer.

The issue of termination is discussed at length in Chapter 20.

Manufacturer's Regional Sales Manager has difficulty maintaining credibility with both his factory and his Reps

This credibility problem for RSMs is similar to one cited for RSMs in a Direct Sales channel. However, it is even more difficult for the RSM who manages Reps because the executives at the factory see the Reps as *them*; as in *them and us*. When the RSM does battle for *them*, management suspects he's gone native and is no longer one of their loyal employees.

Best customers

The best customers are those with short buying cycles who generate more than $4,000 in commissions each year from combined sales of more than three of the Rep's product lines.

Worst customers

The worst customers are those who buy only the products of one product line, have buying cycles longer than a year, and require ongoing and varied special services to support.

11. Distributors

Distributors are key factors in most marketing systems. They are organizations that buy products from hundreds of manufacturers and resell them to their customers. They sell standard products and financial benefits; they don't sell technical solutions.[21] Distributors usually specialize in a class of products, such as electronics, foodstuffs, pharmaceuticals, clothing, etc. Some specialize further, for example in "passive electronic components." They provide a convenient means of purchasing the products of many manufacturers. They grant discounts on individual products based on the overall levels of business their customers do with them. They usually provide faster delivery, and better terms and conditions than the manufacturer.

Distributors' customers include OEMs, end-users, retail outlets, Systems Integrators, VARs, and High-Tech Distributors. Some of these customers also buy products directly from manufacturers.

Distributors are usually the largest channel organizations, and the ones with the most money. Many distributors are national, with several warehouses and sales offices. Some are international. They usually centralize their buying processes and leverage their sales volume to obtain the lowest possible prices from manufacturers. They rely heavily on catalogs and data sheets to notify customers of the products they handle.

Structures

National Distributors are large businesses with annual sales running into the billions of dollars. Many of them are public corporations. Their executives are primarily Bureaucrats, far removed from day-to-day operations, and they run their businesses according to GAAS to optimize quarterly results and cash flow. Operating decisions are influenced by pressures from a handful of their largest suppliers and customers. The rest of their suppliers and customers must accept their policies and procedures for conducting business.

Regional Distributors are medium-sized businesses. Regional Distributors have fewer customers and represent fewer product lines than National Distributors. Their executives work more closely with their customers and with their suppliers than do their counterparts at National Distributors. However, Regional Distributors often receive less-favorable pricing and less technical support from the largest manufacturers because their volume of business is relatively low. As a result they are more approachable to the less well-established manufacturers.

Distributors have Field Sales organizations, but with some exceptions their field sales people are not the cream of the selling crop and they have an average tenure with distributors of less than two years. The field sales people spend more time with purchasing agents than with user-buyers. They are usually conveyors of literature, sources of free samples, buyers of meals, and mediocre administrators of ongoing accounts. They can't be, and aren't, technically competent about the vast majority of the products they sell; there are too

[21] There are exceptions of course. A few electronics distributors have recently developed partnerships with contract manufacturers and provide the purchasing, materials management, and manufacturing solution for some of their customers. It's what we used to call "fab to print" work in government contracting; the customer supplies the manufacturing drawings (prints) for a product and the supplier buys the materials and fabricates the product to those drawings.

many products and they don't stay around long enough to become proficient. What they sell is convenience and financial benefits for consolidated orders and reorders.
Some distributors serve as "off the books" warehouses for select customers. They carry bonded stock, inventory exclusively reserved for specific customers. These customers pay a premium of course, but they have assured, immediate access to inventory which doesn't show on their books. Thus, the customer's Purchasing and Manufacturing people appear to have improved inventory turns, and they become cash flow heroes. GAAS doesn't identify the financing costs for the bonded (off-the- books) inventory, so everyone is happy. One catch is that the bonded inventory may carry with it an obligation on the customer's part to buy it even if he can't use it. For customers with cash flow problems, the off-books inventory of distributors can be a vital and valuable service that is well worth the costs. In effect, distributors help to finance the businesses of some of their customers.

Key people

Field sales people

It is not my intent to belittle any channel organization or sales professional. However, it is important to be accurate. In the spirit of accuracy I must say that, on the average, Field Sales professionals in domestic Distribution are less capable of representing suppliers than are their counterparts in other channel organizations. (Having said that I will quickly add that I've also worked with a few individuals who were outstanding and the equal of the best sales professionals in other channels.) There are several reasons for this:

> **Substandard hiring, management, and compensation:** Distributors are generally larger businesses who hire according to policies, manage by the numbers, and pay as little as possible. The individual's performance is less appreciated. The outstanding people can do better in other organizations. People who are technically competent usually work elsewhere because they can earn more.
>
> **High turnover rate:** The average tenure of a Field Sales person at a specific Distributor is less than two years.
>
> **Very broad range of products:** The Distributor represents hundreds to thousands of product lines. At best, a Field Sales professional can only be competent about a handful of lines. For the rest of them she simply passes out catalogs, data sheets, price lists, and free samples, acts as a conduit for technical questions and arranges meetings.
>
> **Emphasis on purchasing**: Distributors focus on supporting the customers' Purchasing Agents and pay relatively little attention to the engineers or user-buyers. Those who are competent to help solve technical problems become frustrated with Purchasing Agents.
>
> **Technologists are cynical about their competence:** Most engineers have a cynical attitudes about Distributors' sales people. For some, their attitudes come from bitter experiences. These engineers quickly and emphatically communicate their cynical attitudes to the rest of the engineering community. Over the years these attitudes have become ingrained in the engineering culture.

Strangely enough, much of a key customer's loyalty to a Distributor comes from the individual relationship between the Field Sales person and the Purchasing Agent. Also, most of the significant knowledge about an account rests in the mind and black book of the Field Sales person. When a field sales person of one distributor is hired by another the key question is: which accounts can he bring to his new employer.

Inside sales people

Inside sales is particularly important in Distribution. The customers' and prospects' Purchasing agents generally telephone the inside sales people for price and delivery information, and then place orders directly with them either by telephone or FAX. Purchasing agents are usually harried, with numerous orders to place and broad latitude about who to buy from. They place a high value on convenience and dependability. The inside sales person is immediately available, surrounded by product literature and operating a computer terminal, to answer questions, to quote prices and delivery, and to immediately process orders. The competence of the inside sales people and the chemistry between them and the Purchasing agents is critical. It has a direct and significant impact on the level of business and which products the Purchasing agent orders.

An executive of one Distributor emphasized the importance of Inside Sales. She noticed that the business level from one key account had declined significantly over the previous few months. A discussion with the Field Sales person revealed that the customer's own business actually growing. Their share of the customer's business was declining. She visited the customer to learn what her company was doing wrong. The customer had no particular complaints, and the Purchasing agent offered no reasons for the decline in orders placed. But something in the conversation led her to believe that the Purchasing agent had some discomfort interacting with the Inside Sales person assigned to that account. She assigned another person to the account, one she thought was more suited to the temperament of the Purchasing agent. Sure enough, over the next few months the level of orders increased substantially.

Economics

Distributors make their money on the profit margins at which they resell products to their customers. In the electronics business, the typical gross margin on sales is around 20%. They sell most products at moderate to substantial discounts from manufacturers' list prices, so they demand and get at least 30% discounts from manufacturers unit list price. Sometimes they get discounts of more than 50%.

The commissions paid to sales people are generally based on the Gross Profits attributed to the orders, not to total order dollars. This motivates the sales people to be aware of margins and to maximize the margins at which they sell their products. Products that command higher margins generate higher commissions and usually get more attention from the sales people.

Working relationships

Manufacturers deal primarily with the purchasing side of distributor organizations. Unless a manufacturer represents more than 1% of a distributor's annual business, the dealings are dictated by the distributor's policies and procedures. The best that most manufacturers can do is to keep distributors stocked with literature, make sure they get exposure in their catalogs (by helping to pay for same), and be responsive when asked for price and delivery concessions.

Strengths

Shopping Convenience.

Consolidates orders and simplifies the Purchasing Agent's job. Immediate delivery from stock.

Well financed

Uses its funds to stock products, provides bundled discounts, and special terms for customers. Can carry inventory and help finance customers' businesses.

Credible and convenient for Purchasing Agents

The Purchasing Agents of customers frequently shop around for competitive quotations on the things they buy, even when they have preferred sources. It's partly *due diligence*; they might discover a source with better prices or delivery, or discover an equivalent part that saves lots of money. It also gives them leverage to squeeze a few more dollars out of their preferred suppliers. Purchasing Agents are usually measured on such things.

Handles reorders effectively

Weaknesses

Relationships to user-buyers

Not effective at developing new customers for moderately complex or complex products.

Short term selling

High turnover rates among the field sales people causes them to focus on Purchasing Agents and business that pays commissions quickly. The distributor sales force, with individual exceptions, is not prepared to work for a year or more with user-buyers who are developing new applications and new markets.

Technical support

Technical support is usually limited to handing out data sheets and catalogs, and to relaying technical questions to manufacturers.

Management issues

Manufacturer has little visibility or clout

Unless you are one of a distributor's largest manufacturers or largest customers, you have very little visibility and clout. You have to work to their requirements.

Can be a threat to other sales channels on reorders.

Distributors can underbid everyone but the manufacturer on reorders. In fact, on reorders for small quantities, a distributor can even underbid the manufacturer's direct sales organization. Furthermore, a distributor anywhere in the country can compete for the business of an established customer. Those who developed the business, and expect to be compensated for reorders, are left out. (This is discussed further in Chapter 21.)

Manufacturer can misuse distributors' inventories to meet sales quotas

The quarter is almost over. The manufacturer's sales force hasn't reached its sales quota. Someone gets a bright idea: Get the distributors to buy more products and accept shipment before the end of the quarter by giving them a special discount (say another 5%). The idea works! Quarterly financial statements, bonuses, and commissions are salvaged. Everyone is happy.

However, how do the distributors get rid of the added inventory? They use the discount to reduce their prices and steal business from other channel organizations during the next quarter. They don't generate new business, they cut the average street price of the products. They reduce the average profits for the manufacturer and the manufacturer's other sales channels. Furthermore, they dig a hole in the next quarter's bookings, one which will prompt a repeat of the discount scenario, this time to stave off disaster. It's a bit like becoming a dope addict; it feels good the first time but then becomes a painful habit and necessary for survival.[22]

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[22]My first in-house seminar on channel selling was at a $100 million/year electronics company. When I described this discount practice the executives became quite animated. It turned out that they had been doing it for years and their situation had become even more destructive than I described. Distributors knew there would be a 5% discount for orders booked and shipped in the last three weeks of the quarter, so they held their orders until then. Manufacturing then had to produce and ship about 30%

Inventory Protection.
Distributors require price protection and obsolescence protection from manufacturers. When a manufacturer reduces its prices, it usually has to issue credits to distributors for the stock they have in inventory. When a manufacturer increases its prices, it usually has to give the distributors advance notice and allow them to stock up at the lower prices. When products are obsoleted, a manufacturer usually has to accept product returns from distributors' inventories.

> NB: Regardless of the fact that Generally Accepted Accounting Standards treat sales to distributors as real shipments, a manufacturer has not really sold its products until the ultimate user-buyer has bought and paid for them.

No exclusive loyalty to manufacturers
Handles directly competitive products as a matter of policy. May entice a customer to switch to another product that increases his margins and profits. This is not all bad. It enables the distributor to continue to support a wider variety of customers. It also makes the distributor more credible with customers; since the distributor sells competing products its recommendations are presumed to be less biased!

Trend to centralized buying

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of the quarter's revenues in the last three weeks of each quarter. The discounts were eliminated shortly after my seminar. The company went through one bad quarter (withdrawal pains) but more than made up for it in the following years.

For example, large manufacturers, such as Intel and Motorola in the semiconductor business, are driving distributors to go national and to buy from them under single agreements. This change is for the convenience of these manufacturers and does not benefit the distributors' customers, smaller manufacturers or the distributors themselves. I suspect it's a sign of unhealthy bureaucratic centralization within these manufacturers and within their distributors. Sooner or later it will create serious problems for all of them and create opportunities for competing manufacturers and distributors.[23]

***Ship and debit* arrangements with some manufacturers.**
Distributors and some manufacturers[24] have a process called "***ship-and-debit***" that customers should be aware of because it can significantly affect their costs. Ship-and-debit goes like this: A distributor has a formal pricing arrangement with a semiconductor manufacturer and sets its customer prices accordingly. However, if a specific customer shops around and finds an equivalent, but lower priced, competitive product, then the distributor can use the competitive quote to obtain a lower price from the semiconductor manufacturer. However, the lower price is limited to a specific purchase order from that customer. It is for a specific quantity of products shipped within a specified period of time. The result is that a customer must shop around and obtain a better price for a competitive product before placing each order, or he may not receive the lowest price. Ship-and-debit is intended to discourage cutthroat competition. However, it undermines the integrity of blanket agreements between customers and distributors because distributors can't quote their lowest prices in blanket agreements. Unfortunately, this pricing game has been going on for years and it will continue. **Buyers Beware.**

Best customers

Accounts that buy tens to hundreds of different products from catalogs and data sheets on the basis of collective pricing and assured supplies in distributors' stock. Accounts looking for inventory financing to improve cash flow. Can profitably handle a low dollar volume for any one product.

Worst customers

The initial purchase by a customer's technologist of a high-tech product based on its technical features where training and special technical support are required.

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[23] If you're an executive in one of these companies and disagree with my assessment, give me a call . Let's discuss it.

[24] I'm fairly sure it's more widespread than that, but I know about this one because it cost Pro-Log quite a few bucks to learn about it the hard way.

12. Retail

Retail stores are several books in themselves, books that others can do a better job writing. This chapter is merely an overview of key points. There are millions of retail organizations ranging from mom-and-pop specialty stores to national chains. Although retail outlets are generally associated with consumers, businesses of all sizes also buy from them. Traditionally, businesses have purchased office equipment and office supplies from them. In the last few years retail organizations sell businesses their computers, software, and other high-tech products.

Shelf Space

A critical concept in retail is *shelf space*. Customers usually make their final decision to buy a specific product while standing in the aisle by the shelf where the product is displayed. The product's location and its presentation, including the manufacturers packaging, are critical to its sales. Each retail outlet, whether a mom-and-pop establishment or the local store of a giant chain, has a limited amount of shelf space. Every manufacturer who sells through that outlet competes for space. New products and new suppliers must displace products and suppliers that are already there.

The retail outlet, or its parent company, determines which products are on the shelf, where they are displayed, and how much space each one is allotted. Manufacturers try to influence these decisions. The ones with brand recognition, substantial sales, and competent negotiators are successful. The rational basis for allocating shelf space is to do it in a way that maximizes the outlet's total sales and profits over many years. There are no simple formulas for this. The decisions are made through human judgment, trial and error, and factors that have nothing to do with overall sales, like personal relationships, promotional SPIFFs (Special Incentives for Sales), or kickbacks.

The allocation shelf space is a complicated and never ending process. For example, the typical supermarket has well over 10,000 products on its shelves. Fewer than 200 of these products account for more than 50% of its sales, and their allocation is a no-brainer. But one of the primary reasons a customer chooses to shop at a specific supermarket is that it carries specific items which that particular customer wants. The 9,000 plus items that sell in very low volumes, collectively influence customers to buy the top 200 items there. As demographics change, as fads come and go, and as new companies and new products vie in the marketplace, the battle for shelf space continues.

The most difficult job for a manufacturer is to get shelf space. It is less difficult to change which of the manufacturers products the store carries in that space. That is, it is relatively easy for a new product from a manufacturer to replace one of its older products on the shelf. It is far more difficult for the new product to get additional shelf space of its own. But it is a mistake to assume that once you have shelf space it is yours. There are plenty of others continually striving to take it.

Once a product is allocated shelf space, it might be purchased from distributors and put on the shelf by the store's employees, or a "rack-jobber" representing the manufacturer might be permitted to stock the shelf. A rack-jobber reduces the store's labor costs by managing the inventory and keeping the shelf stocked. A rack-jobber provides direct feedback to the manufacturer about product sales at each outlet. A rack-jobber also shmooze the store's management to wangle a little more space or a special display location. Frito Lays potato chips and commercial bakeries traditionally rack-job their products in supermarkets.

Getting Shelf Space

In order to get and keep new shelf space for a product, there must be a demonstrable demand for it from the store's customers. The manufacturer must create this demand. Customary methods are through advertising, promotions and referral sales developed through sales by other channels. When manufacturers induce customers to visit retail outlets and ask for their products, they get the stores' attention.

Retail outlets won't create a market for a new product; they will serve an existing market. Don't expect a retail outlet to generate demand for a specific brand of product, unless it is their own private-label product. It is up to the manufacturer to create a market value for its brand name. For example, Safeway sells a Safeway brand of coffees which it promotes in its own advertising. It buys these coffees from one or more manufacturers who, like Maxwell House, also sell similar (probably identical) products at higher prices under their own brand names on the shelves adjacent to the Safeway brand. These manufacturers have to induce the customer to prefer their brand to the Safeway brand, and be willing to pay more for it.

Retail is an attractive and often cost-effective way to sell for several reasons:

- **Prospects travel to the retail outlet.** They invest their own time to travel and pay their own travel costs, yet they don't even factor their time and travel costs into the cost of the product! In fact the process of traveling to a store and shopping probably satisfies strong personal attractors. When they choose not to buy, they still eat the travel time and travel costs.

- **When prospects enter a retail outlet they are usually in active buying mode**. They have self-qualified, although it is still up to the retail outlet to make sure that they're profitable. They are prepared to evaluate competitive alternatives, make a choice, take delivery, and pay for the products all within a few minutes.

- **When prospects enter a retail outlet, they attribute credibility to its sales staff.** Think about it for a moment in comparable business terms. If I go to your office to discuss something, I have acknowledged your status and credibility. If you come to my office you accord them to me. In fact, it is customary for a junior person to travel to the office of a more senior person. When a customer visits a supplier or someone its marketing system, the customer has accorded them credibility which facilitates more productive discussions.

Structures

The product's path from Manufacturer to Retail outlets can be quite varied. Chains like Office Depot may purchase directly from the Manufacturer and have the product shipped in bulk to their own warehouses. Their individual stores will order from their warehouses. Some chain stores carry products from their own warehouses, from third party distributors, and from rack-jobbers.

Smaller chains and independent stores buy through a multi-level distribution system. They may order from a local distributor or dealer, who purchased the product from a regional or national distributor, who bought it from the manufacturer.

Key people

From the perspective of a manufacturer's marketing system there are two key jobs in the path to the customers: the store's (or the chain's) buyer and its Sales Assistants who interact with customers.

Buyer
The Buyer is the person who decides which products and companies get shelf space. He deals directly with manufacturers and with Manufacturers Representatives who specialize in working with buyers.[25]
The Manufacturers Representatives can get a new manufacturer in the door to see the buyer, and can educate the manufacturer on what the buyer expects. However, the process of convincing a buyer to try a new manufacturer and new product usually involves a detailed proposal from the manufacturer that covers pricing and volume discounts, manufacturer's advertising plans, co-op advertising allowances, special incentives, packaging, displays

Sales Assistant
Once a customer is standing in the aisles ready to make a decision, the Sales Assistant and the product's packaging play the two most significant roles in his decision. It is in the Manufacturer's best interests to have a Sales Assistant who is knowledgeable about its products, enthused about them, and motivated to recommend them. There is seldom a formal way to control this, but it is worthwhile to exercise informal approaches, like having factory representatives visit outlets from time to time and help sell the products. The Sales Assistant is usually aware of three things that affect his enthusiasm and motivation: the gross margins for the products, the difficulties customers have using the products and the customers' return rates. The Sales Assistant usually receives a commission on the dollars of gross profit that the store gets from the sale. He loses selling time dealing with customer complaints, and his commission is docked for customer returns.

Product Packaging
Correctly packaging a product for retail selling requires specific knowledge and skills. A product's packaging is one of the two most important elements for success at the point of sale, and it is the element the manufacturer can control. The package has three selling tasks: to attract the prospect's attention, to encourage the prospect to buy, and to give the prospect the information he or she needs to make a selection. The first two tasks have to be accomplished within seconds. There are also packaging constraints imposed by factors that include shelf space limitations, shipping and bulk packaging considerations, safety, regulations, and packaging costs.

My strong recommendation: turn the job over to experienced professionals. Don't wing it.

Economics
Distributors and retail outlets talk about gross margins, the percent of the average selling price that is left when they pay their supplier. Retailers typically operate on a 35% to 40% gross margin. If a store earns a gross margin of 40% on a sale of $100, it means they paid $60 for the products they sold. They have to pay their costs of business and retain a net profit from their $40 gross margin.

However, a manufacturer seldom sells directly to the retail outlet, there are one or more distributors or a chain's warehouse between them. Each level of distributor operates on its margin, typically between 10% and 20%. As a result, it is not uncommon for a product's retail price to be three times the price at which the manufacturer sells it to major distributors.

[25] I deliberately left out a discussion of this category of Manufacturers Representative in Chapter 10 to keep things simple. This specialty is just one of many for Manufacturers Representatives.

In addition to that, the manufacturer is expected to pay for advertizing and promotions, and to partially underwrite costs of adding new products (Stock Keeping Units or SKUs) or opening new stores. These payments are usually in the form of credits applied to future purchases, but sometimes they are outright cash rebates.

Strengths

- Has established credibility with clientele and influences them to limit their range of competitive alternatives to choices carried by the retail outlet.
- Prospects who come to the outlets are in an active buying mode for something.
- Impulse buying, referral business
- Prospects pay travel costs and may consider it a benefit.

Weaknesses

- Poor way to build markets for new products....can't push, must pull...advertize, create store traffic
- Often centrally run, buy decisions made for general market rather than local markets.....
- Customer must self-sell based on concepts developed before coming to outlet and shelf presentation at the outlet.

Management issues

- Shelf space, product presentation at point of sale
- Knowledge of staff about a specific item...low to none...too many items, low paid staff, training is controlled by retail management...selling training more than product specific.
- Central buyers focus on discounts and margins, sales to broad market...not store by store
- Different retail chains different philosophies: discounts, service orientation, general purpose, specialists.
- Problem getting store data and working with outlet unless rack-jobbing...high labor content.

Best customers

Local individual who establishes a habit of buying a specific range of goods and services from the local outlet and becomes a repeat customer. Customer pays cash or uses outlet's specific credit programs. Customer comes to store to make decision with little sales effort on part of outlet's staff.

Worst customers

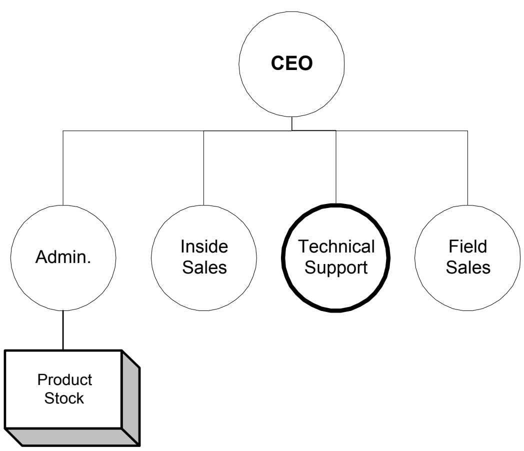
Individual or business in search of a solution to a single complex problem that requires substantial selling effort and technical support.

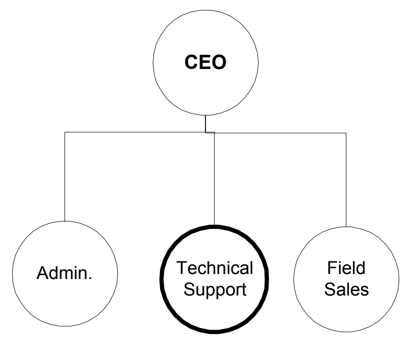
13. Value Added Resellers

High Tech Distributors, VARs, VADs, Systems Integrators

Organizations in the Value Added Reseller channel specialize in providing the technical expertise to produce customized solutions for their customers. Systems Integrators produce turnkey solutions for specific applications in specific markets, and buy products from manufacturers and distributors as they need them. High-tech Distributors, VARs, and Value Added Dealers (VADs) provide partial solutions and turnkey solutions for a wider range of applications and markets, but specialize in supporting a limited set of product lines which they stock and resell. Their inventory is much more limited than that of Distributors in the Distribution Channel, usually just a modest level of stock for fewer than twenty, non-competing but complementary product lines.

Structures





Applications engineers and/or technicians are essential Technical support resources in Value Added Reseller organizations. The Field Sales people depend on this technical support to help them sell, to produce customized solutions, and to support the customers with training and maintenance.

Value Added Resellers write *proposals*, whereas Sales Representative and Distributor organizations write *quotations*. A proposal is a solution-centered selling document that describes a unique solution that fits the customer's requirements. It commits the Value Added Reseller to provide a working solution acceptable to the customer. A quotation is a product-centered document that focuses on the characteristics and prices of products. It lists products and commits to their prices and delivery times. Here's an everyday example of the difference: A homeowner wants a new kitchen. A proposal from a kitchen contractor (Systems Integrator) describes the finished kitchen, when it will be ready, and how much it will cost. On the other hand, a quotation from an Appliance Dealer lists the prices and delivery dates for the refrigerator, the oven, the dishwasher, etc. It's up to the homeowner to get them installed and working and to put together the other materials and labor needed to create a finished kitchen.

Value Added Resellers buy products from Distributors as well as from Manufacturers. In fact some of them buy all their products from Distributors. They buy direct from Manufacturers only when doing so gives them a significant financial, marketing, or technical advantage, or when the products simply aren't available from

Distributors. Many manufacturers supply products to their Value Added Resellers through their Distribution channels and directly provide technical support.

Key people

Owner/CEO

The owners/CEOs of High-tech Distributors have similar backgrounds to their counterparts in Sales Representative organizations. In fact, many High-tech Distributor organizations were once Rep organizations. One owner suggested that he was one of the smarter Sales Reps because by becoming a High-tech Distributor he got 30% discounts from manufacturers and was treated like a customer. As a Sales Representative he was lucky to get 10% commissions from the same manufacturers and in the bargain was treated like a hired hand.

These CEOs clearly see themselves as running small businesses. They buy and sell products, set their own prices, and control their own inventories. They each manage a sales organization, administrative support, and an "engineering" group. Their people assemble systems and produce supporting documentation. Their organizations have all the elements of a small businesses.

The CEOs of Systems Integrators are usually technically competent in the industries of their clientele. They influence their technical staff's selection of manufacturers and products.

Field Sales

The field sales people are usually technically savvy about the products their company uses and the range of applications in which they specialize. They spend more time managing and supporting accounts than in selling. They call on far fewer customers than their counterparts in Sales Representative or Distributor organizations. They sell the capabilities of their organizations, and only secondarily the specific products they represent. The unique value of VAR organizations to customers is their technical competence, and that's what the Field Sales people sell.

Inside Sales

High-tech Distributors and Value Added Dealers usually have inside sales people who respond to basic questions, mail literature, do some telemarketing, and support the Field Sales people.

Technical Support

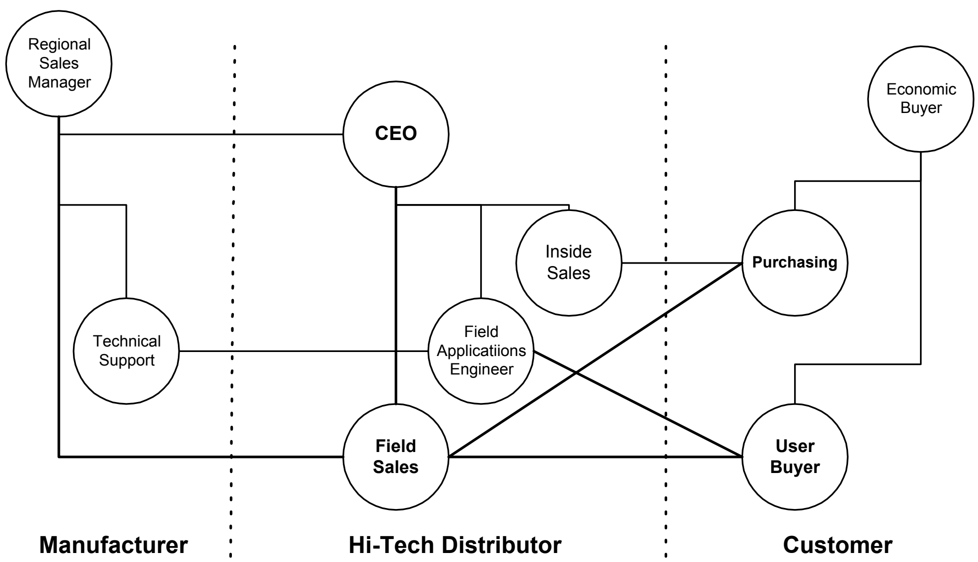
The technical support people are the key ingredient of VAR channel organizations. They are technically competent to use, modify, and service the products the organization includes in its applications. They are also knowledgeable about the applications that the organizations specializes in. For example, when a Systems Integrator specializes in test systems for the textile industry, then it is likely that the technical support people once worked in the textile industry using or maintaining this kind of equipment. They have a deep understanding of how their customers use the equipment in an industrial environment. They are also specifically trained by the manufacturers in how to use, modify, and maintain the test equipment bought by the Systems Integrator.

Economics

Costs
Value Added Reseller organizations have similar selling and office costs to organizations in other channels. In addition, they have to pay for their Technical Support people who typically cost well over $75k per year when salary, benefits, office space, and support equipment are accounted for.

Compensation
Compensation comes from marking up the prices of products they buy from manufacturers and distributors, and by specifically charging for services they perform. (See the M & D Controls brochure in Appendix A.) For example, a proposal might include a two-year, on-site maintenance agreement at a fixed price. However, most of the money will pay for the Technical Support staff who will provide the maintenance.

Working relationships



The manufacturer's regional sales manager works primarily with the CEO and the Field sales people. The Manufacturer's technical support staff works with the VAR's technical support people to keep them informed and competent. The technical support link is at least as important as the other two links in the case of Systems Integrators. An SI's technical people, not the field sales people, decide what products to include in their designs. The field sales people of High-tech Distributors have a bit more influence. The next most important link is to the CEO. The problem is that the typical RSM is unprepared to manage or support the CEO of a small business.

Strengths

Provide complete solutions to customers in their target markets.
They write proposals that say, in effect, *please sign the P.O. and leave the rest to us*.

Technical support for application-specific design, training, problem solving, and maintenance.

Weaknesses

Handle relatively few customers per field sales person.
Each customer takes a lot of field sales time for in-depth support and special services.

Probably unprepared to pursue business outside their area of customer expertise.

In other words: If you're a manufacturer who needs someone to develop a market for your product, this is among least effective channel organizations with which to do it. This is a lesson that Frank, the CEO in the book's introduction, learned the hard way.

Management issues

Sizes of discounts
The management question is: what is the rationale for the discount? Is it to give the VAR organizations an incentive to sell the products? Is it to support the training costs of their technical support people? Is it for the anticipated volume of sales they might produce? Most manufacturers attempt to tie up all compensation and incentives in a single discount formula. Management-wise, that is a too simple solution.

VAR might resell products without adding value
VAR organizations are independent businesses who can legally resell what they buy to anyone at any price. If they receive as large a discount as classic distributors, in part to pay for some of their value added technical support, there is nothing to stop them from undercutting the prices of other channel organizations without adding any value.

Manufacturers push VARs to buy unnecessary "inventory."
VAR organizations are not flush with money and aren't driven to sell by the amount of inventory on their shelves. Furthermore, the manufacturers' products aren't really sold until customers pay for them. However, since a sale to a VAR shows up on the manufacturer's books and RSM's quotas, many organizations push VARs to take more inventory than they need. In most cases that inventory carries a liability for the manufacturer when it doesn't resell, prices drop, or the manufacturer obsoletes it with newer products.

Returns and exchanges
VAR organizations that are required to carry stock expect to be able to return or exchange obsolete or slow-moving products. They expect to be able to return all inventory for nearly full credit if they are terminated. Manufacturers usually place limits on the amount of exchanges in any quarter.

Pass-through warranties
When a VAR resells the manufacturer's products, how is the product warranty supported: through the VAR or direct with the customer? When the warranty is for a limited period, does the clock start when the VAR receives the product, or when the VAR's customer receives its solution? How does the manufacturer know who the customer is and when it receives the product?

Price changes and price protection, list price and its reference value.
VARs submit proposals to their clients which may take months to translate into orders, and months or years to result in product shipments. How does the manufacturer enable the VAR to count on the price of its products for the term of the VAR's agreement with its clients?

Paying for technical expertise and keeping it up to date.
How does a manufacturer make sure that the VAR's technical competence on manufacturer's products is satisfactory and up-to-date? Some manufacturers stipulate that a VAR's technical people receive annual training. They test and certify the technical support people. They modify a VAR's discounts or limit its referral business based on its compliance with training and on the certifications of its people.

Channel conflicts on large orders
VARs may design a system using the manufacturer's products and ship an initial order to their clients. However, on re-orders, the client may get competitive quotes from the manufacturer or other channel organizations. How is the VAR compensated when follow-on business goes through different channels or how does the manufacturer work with a VAR to enable it to provide pricing that is comparable to that available to the client from other channels?

Best customers
Accounts with Craftsperson or Bureaucrat technologists looking for a "solution" that includes the products of several of the VAR's manufacturers and a significant amount of technical support.

Worst customers
Accounts which reorder moderate to large dollar-volume buys of one manufacturer's products.

Section III

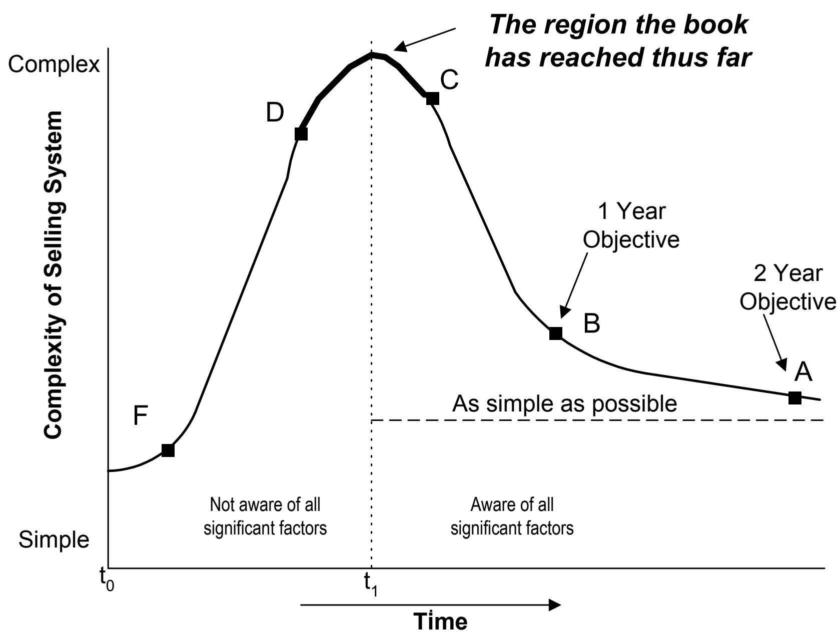
Where the Rubber Meets the Road

14. How to Design Your Marketing system

"*You can always get what you want, if you help enough other people get what they want*" Zig Zigler

Where we are in the design process

In the first seven chapters, we developed fundamental tools for evaluating and managing customers and marketing systems. In Chapters 8 through 13, we described channels and channel organizations in enough detail to know what benefits they provide and how they operate. We have reached the conceptual point where the pieces are there, but they are not effectively organized as a system. If we mechanically assemble a marketing system based on what has been described thus far, we'll get one that is overly complex, user unfriendly, riddled with bugs, and doesn't produce a competitive advantage (See Fig. 14.1). This might well describe a typical marketing system.



An objective of this book is to enable you to develop a B marketing system within a year, and to develop an A one within two years. The next step in doing that is to introduce simplifying principles.

Simplifying Principle #1:

Channel Organizations are key customers

Please consider this principle carefully. The following questions might help: How are channel organizations and key customers similar? How are their buying processes and buying characteristics similar? Who are the channel organizations' user-buyers? Who are the economic buyers? What characteristics makes channel organizations profitable or unprofitable customers? Which goods and services of Fig. 5.6 on page 57 do channel organizations expect from the manufacturers they represent? Which goods and services do specific channel organizations provide to their customers?

Here are a few, thought provoking answers: The user-buyers in channel organizations are their sales professionals and the technical support people. The economic buyers are their owners and managers. A manufacturer has to establish substantial credibility with user-buyers and economic buyers before they will commit to sell its products. The manufacturer also has to establish and maintain credibility with the managers, sales professionals, and support staff in its own Direct sales organization.

Also consider these questions:

- What competitive alternatives does a channel organization have to selling the products of a specific manufacturer? (The alternatives vary from one organization to the next.)
- What are the competitive alternatives for a sales professional in a Direct organization or a third party channel organization to actively selling your company's products?
- Since a Direct sales organization is a key customer, who is managing that customer? Is it being managed like a key customer or a hired gun?

Chapters 3 and 4, on motivation and decision-making attitudes, apply to sales professionals. Some sell as Adventurers, others as Craftspeople, and still others as Bureaucrats. Adventurers are the most eager to sell new products to new customers, because they enjoy the challenges. They are the innovators and early adopters of selling. It's a waste to expect them to effectively administer well established, large, bureaucratic accounts. Bureaucrats are at their best administering ongoing business with established, bureaucratic accounts. It's a waste of time and money to expect them to pioneer new products to new customers.

Some readers may consider the implications of "*Every channel organization is a key customer,*" as anything but simplifying. It seems more difficult to manage sales organizations like customers than to use the traditional methods of bossing them around with promises and threats. These old methods (otherwise known as "Theory X management") may be comfortable to Bureaucrat managers, but they don't work very well. They are too simple. Effective sales organizations and competent sales professionals (even employees of the manufacturer) always develop attractive competitive alternatives to selling a manufacturer's products regardless of the threats, controls, financial incentives, and official agreements that may be in place.

Simplifying Principle #2:

Help your key customers succeed at what they do

The most productive strategy towards all (profitable) customers is to help them succeed at using your products and services; help them succeed sooner, with less effort, and more dependably. That is the essence of "value added" from a customer's perspective. This strategy starts with end-user customers, but applies equally well to all the worthwhile sales organizations and sales professionals in your marketing system. Instead of shoving product into channel organizations with discounts and incentive, instead of setting quotas and then demanding that people meet them, do what it takes to help them sell products and make profits—all the way to the end-users. In fact, to effectively increase your credibility and bargaining position with the channel organizations and sales professionals, create demand for your company and its products from their established customer bases.

Here is one example of second principle in action: The manufacturers of FAX/Modem semiconductor chips, including Rockwell and US Robotics, sell their chips to OEMs, who produce the FAX/Modem plug-in cards for Personal Computers. The number of chips each manufacturer sells depends on how many OEMs buy from them and on how many cards each of their OEMs sell in the retail market. However, the chip manufacturers don't just sell design chips and sell them to the OEMs. They work with the OEMs and with end user customers (customers of their OEMs and of competitors products) to design and build working models of generic board-level products. Then they give working prototypes, design information, and the manufacturing rights to their OEMs. The chip manufacturers help their OEMs succeed by getting them to market faster, reducing their engineering costs and enabling them to focus on manufacturing and retail marketing.

In another example of the second principle, a manufacturer launched a new telephony product through a chain of retail stores. The manufacturer ran the usual product ads with tag lines that said the product was available at this chain. Shortly after the product reached the stores' shelves, two of the manufacturers sales managers traveled from store to store, stood in the aisles next to the product displays, answered customers questions, and informally trained the stores' sales people on the product's benefits and features. They also did some shmoozing and made the sales people aware that the chain's profits on this product, and therefore their commissions, were higher than for the average product of this type. The new telephony product's sales increased dramatically in the weeks following their visits.

I'd like to stress that **this principle applies just as successfully to employees in your direct sales organization** as it does to any other customers.

Eight Questions that shape your Marketing System

There are eight key planning questions, whose answers can help you define the most appropriate sales channels, identify the best organizations in those channels and determine what it will cost you to sell effectively through those organization. The questions are:

1. Which channels and channel organizations do your targeted end-users already buy from?
2. Which of the goods and services (of Fig. 5.6 on page 57) do your targeted end-users need to buy, install and use your products successfully?
3. Which organizations will provide each good or service: manufacturer, channel organization, customer, or a fourth party?
4. How much does each good or service cost you or your channel organizations?
5. How much does it cost you to select, manage, and support channel organizations?
6. When are costs incurred?
7. How are costs recovered?
8. When are profits realized?

1. Which channels and channel organizations do your targeted end-users already buy from?
Individuals and organizations develop buying patterns. They tend to buy from sources they bought from in the past and they tend to buy for the same reasons today that they bought for in the past. The channels and channel organizations your prospects now use to buy products related to yours already have credibility with those prospects.

2. Which goods and services (of Fig. 5.6 on page 57) do your targeted end-users need to buy, install, and use your products successfully?

In order to transform your Products into customers' solutions, you and your marketing system have to provide the other goods and services the prospects actually need. There are four principal factors that determine the specific needs of your prospects:

- **Customer characteristics**
  - ***Competence and attitudes of user-buyers***
  - Nature of the applications
  - Buying culture
  - Competitive alternatives
  - Geographic distribution
- **Product attributes**
  - Ease of Use
  - Role in Customer's Solution
  - Competitive Position
- **Initial order or re-order**?
- **Manufacturer characteristics**.

Customer Characteristics

Competence and attitudes of user-buyers: As a general rule the more competent the user-buyers, the less information and technical support they require. The market segment with Adventurer or Craftsperson user-buyers requires less information and technical support than the Bureaucrat segment, because they are more competent and willing to invest more personal time and energy in working things out themselves.

Nature of the application: When the application is significant or critical, the customer tends to demand more support: more information about the manufacturer and product, better documentation, more training, quality verification, etc.

Buying culture: When the customers' buying processes are complicated with buying teams and formal procedures, they require more support from the marketing system. For example, when a government agency buys, it usually drags the process out over months or years, demands libraries of paperwork, requires formal presentations, and performs all kinds of bureaucratic evaluations. A small company, buying the same thing, does it relatively quickly, demands little paperwork, prefers informal discussions, and keeps evaluations short and to the point.

Some buying cultures are win/lose. They are not concerned with whether or not the manufacturer or his channel organization makes a fair profit. This kind of buyer will typically hold out the carrot of a large production order to get favorable pricing and copious technical support during the development phase. The unwise manufacturer and/or channel organization blindly make a big investment with the intent of recouping the losses on the production order. Then the buyer re-opens the competition for the production order and goes with the low bidder, usually someone who didn't make the front-end investment.

Competitive alternatives: A customer with viable competitive alternatives is inclined to demand more goods and services than one for which the next best alternative is relatively poor. For example, Intel can get its OEM customers to do most of their own education and technical support for its Pentium CPU because they have no serious competitive alternatives.

There is a tricky point to the issue of competitive alternatives: when a manufacturer has several channels, they may become competitive alternatives for customers who can play them off against one another to get more and to pay less. Intel's many OEMs for its CPUs are competitive alternatives for end-user customers of IBM compatible personal computers. The end-user has alternatives, but the OEMs have a sole source. The end-users are happy, Intel is extremely profitable, and the OEMs undermine each others' margins to sell to the end-users.

Geographic distribution: The geographic distribution of a manufacturer's top 200 target accounts impacts costs (particularly travel costs) and convenience. Customers feel more comfortable when they have the option to deal with someone face-to-face on short notice. In spite of automation, a local presence still carries some weight. The key issues are: where are the sales activities and technical support services performed, and who pays the travel costs?

Product attributes

Ease of use: How easy will it be for the average customer to install, use, and maintain your product? It is obvious that the simpler the product is, the less technical support it will require. But there is a second, and often more important factor: how well does the product conform to ***market standards*** for use, installation, and maintenance. When market standards exist, a product that conforms to them can be technically complex but easy for the customers to use, install, and /or maintain, because typical customers know the standards before they buy.

For example: It takes a complex set of skills to drive an automobile. Yet, it is simple for most adult Americans to drive any car they buy, because all cars sold in the USA use the market standards for placement and operation of the steering wheel, accelerator, brake, and gear shift. Car buyers learn how to drive using these standards before they buy their first car. Individual manufacturers don't have to teach prospects how to drive. However the same drivers face a learning crisis trying to drive through London in a car made to British standards because they have to sit in the passengers' seats, shift with their left hands, and drive on the "wrong" side of the road.

The QWERTY keyboard is the industry standard for typewriter and computer keyboards. It originated around 1912 with typewriters. It is technically difficult to learn and there is a far simpler one available, but it is taught in almost every high school and trade school in the country. The majority of keyboard users learn how to touch type on a QWERTY keyboard before they buy their first typewriter, word-processor, or computer. The Dvorak keyboard is a technically superior and simpler alternative to the QWERTY keyboard. Tests have shown that it takes half as long to learn, enables users to type 20% faster, and enables them to type for hours without fatigue. It was introduced to the market over 60 years ago, and its current market share is microscopic! Its relative technical simplicity is irrelevant, because it isn't the industry standard to which the customers are educated.

An IBM compatible Personal Computer is another very complicated product. But for most consumers, it's fairly simple to install and use because it conforms to a set of standards for use and construction embraced by over 90% of the market. Over 100 million users already know how to operate its QWERTY keyboard, its mouse, and its Windows operating system. Users who don't know how to do these things expect to learn on their own time and at their own expense. An Apple PC is technically simpler to use than an IBM PC, but it is more difficult for most people because its hardware and software don't conform to the market standards.[26] IBM compatible PCS are comparable to QWERTY keyboards and Apple computers are in danger of becoming the Dvorak keyboards.

Use of Market Standards	**Complexity**		
	Highly Complex	Moderately Complex	Simple
Standards exist and Product uses them	**2**	**1**	**0**
Standards aren't well developed for Product category	**4**	**2**	**1**
Standards exist but Product does not use them	**6+**	**4**	**2**

0-1 Simple to use for typical users in mass markets
2-3 Moderately difficult to use, typical users require some support
4-6+ Extremely difficult to use, typical users require extensive support.

Fig. 14.2 Relative difficulty to install and use a Product as a function of its complexity and its adherence to market standards. Applies to customers' initial purchases.

Figure 14.2 illustrates the relative difficulties for typical customers to install and use a product as a function of two of its characteristics: Complexity and Adherence to Market Standards. The numbers represent the degree of difficulty for typical users to install and use the product for the first time. They also represent the relative costs of selling and technically supporting the product. This figure is a conceptual tool more than a mathematically rigorous one. It illustrates how market standards and a product's adherence to them reduce the manufacturers selling costs. They also reduce the customers' costs to install and use the product.

Automobiles, for example, are moderately complicated to drive, but conform to market standards. Potential users are already trained to these standards, so driving a car has a difficulty rating of "1." However, the same cars are very complicated to repair, and fewer repair standards exist, so the repair difficulty index is "4" or more. Most people don't service their own cars, they pay professional mechanics to service them.

[26] In Personal Computers, the most significant market standards are *open architecture* and *multiple sources.* These standards enable customers to be consenting adults. Apple's computers are closed architecture systems, proprietary to Apple, and have only one manufacturer. Apple used its software copyrights to lock out potential competitor. It maintained parent-child control of its customer, in its shrinking market share. See my editorial from 1985 "The Mind Bus" in Appendix A.

IBM compatible personal computers are highly complex to install and use, but conform to market standards, so they have a “2” complexity rating for most users.

Virtual Reality products fall into the category of complex products without market standards for installation and use, so they rate a “4.” This is a typical situation for new high-tech products in new markets.

Pen-based computers are examples of products that don’t use existing standards (keyboarding). Their barrier to acceptance is even higher than for equivalent products without market standards. The customer is being asked to ignore or to relearn skills he already has.

Product’s role in the Customers’ Solutions

- The Product is the Solution.
- The Product is a visible, critical component in the Solution.
- The Product is a minor or invisible component in the Solution.

Product’s competitive Position

- **Pioneering:** State-of-the-art features; creates a new market.
- **Established Leader**: Is value reference for the market.
- **Also ran**: one of the herd. The other goods and services are the source of product differentiation.

Initial order or re-order

Information and Technical Support requirements drop substantially for re-orders because customers have become better informed, more skilled, and more comfortable with the products. Business issues, particularly those of product availability and product price, become more important. Because of this, sales channels that supply appropriate and competitive support for initial orders may be less appropriate and less competitive for re-orders.

For example, a customer’s user-buyer might initially buy from a VAR to combine several products into a working solution and to get application engineering, training, installation, and technical support. But once that solution is installed and operating, the customer probably knows how the solution is designed, how to use it, how to maintain it, and what products are used in it. Thereafter, to save money, the customer’s purchasing agent might bypass the VAR and reorder products from distributors or from the manufacturer. When the products arrive, the customer assembles and installs the solution.

Manufacturer Characteristics
Established relationship to customers
Competitive Position in market

- *Pioneer*
- *Established Leader*
- *Also ran*: one of the herd

3. Which organizations will provide each good or service?

- Manufacturer
- Channel Organization
- Customer
- A fourth party

The typical, too simple, answer to this question is: the Manufacturer and/or the Channel Organization. After all, who "wants" the transaction to occur? Who is "supposed" to do all the work? But there are ways to induce customers or fourth parties to provide some goods and services at little or no cost to the Manufacturer. Manufacturers and channel organizations who find ways to do this have distinct competitive advantages. Here are two examples. The first example illustrates how manufacturers can design their products to get customers to do more of the work themselves. The second illustrates how to get a fourth party to provide goods and services at no cost to the Manufacturer, Customer, or Channel Organization.

Personal computers have been standardized, modularized and simplified so that consumers and businesses can decide what to buy from product descriptions, configure their own systems, install options, and perform simple maintenance tasks. Prior to the emergence of personal computers, computer manufacturers such as IBM and DEC designed all computers and computer software to their own unique specifications, personally educated and sold each customer, installed every system, and performed all maintenance. They developed huge marketing systems that did it all, and charged the customers princely sums for cradle-to-grave technical support. But they became vulnerable once their customers had the option to reduce costs by an order of magnitude with the PC's do-it-yourself standards. Their bloated marketing systems became a liability.

Home appliances, automobiles, cameras, VCRs, etc. are rated by Consumer Guide, and/or get the Good Housekeeping Seal of Approval. Many consumers use these and other independent ratings to decide which products to buy. These fourth-party ratings provide customers with competitive sales information at no cost to the manufacturers, and with more credibility than manufacturers could ever develop on their own.

There are three requirements for an independent evaluator like Consumer Guide to be available at no cost to the manufacturer and to be an asset to the manufacturer's selling process:

- The market has to be large enough, or interesting enough, to support independent evaluations.
- The manufacturer has to have competitors to be measured against (competitors are an asset!).
- The manufacturer and its product should be among the best in an objective comparison.

4. How much does each good or service cost you or your channel organizations?
This question has two parts: a) How many dollars and how much labor is actually involved? b) How much of the cost does the customer see as value added towards its required solution?

5. How much does it cost to select and manage channel organizations?
The primary costs are:

- A share of the sales dollars that is profitable for them.
- Time and money to: select them, train them, support them, and sell them on your company and its products.
- Time and money to manage channel conflicts.

6. When are costs are incurred?

- Before prospects go into their active buying processes
- During the active buying processes
- After the order is placed but before the customer pays
- After the customer pays

7. How are costs recovered?

- Bundled into the product's price
- Unbundled within the transaction's purchase price
- Outside the transaction

Two examples of bundled costs paid for in the product's price are: the selling costs and a "free one-year parts and labor warranty." Unbundled costs within the transaction are shown as line items on the P.O. They might include extended warranty, training, and spares.

Examples of costs paid outside the transaction: When we buy appliances in a retail store, we spend time and money to travel to the store and shop, but we don't attribute those costs to the transactions. At one time or another most of us learned to drive a car, but we didn't pay the car dealer or car manufacturer for the training when we bought our first car. When we service or repair our cars, we pay for it in transactions that are separate, in our minds, from their purchase prices.

8. When are profits realized?
The short answer, according to GAAS, is that a manufacturer realizes a profit at the time it ships product and invoices the customer. The channel organization realizes its profit when it receives credit for the shipment from the manufacturer. However, it takes weeks or months for the manufacturer to collect from the customer, and (usually) additional weeks to pay the channel organization. All in all, the time between when a supplier sinks costs into selling to a customer and when it gets paid by that customer can vary all over the place. Fig. 5.5 on page 57 provides a general idea of these variations.

Depending on how the selling costs and a customer's payments get divided between the manufacturer and its channel organizations, one party could come out ahead long before the other one does. More often than not, a manufacturer recoups its costs long before a third-party sales organization recoups its costs. This imbalance is one of the factors that undermines effective cooperation between them. In Chapter 20, I'll suggest terms in the manufacturer/sales organization agreements that account for imbalance and are more productive for both parties.

Summary of values added by channel organizations

Before getting down to the issue of which channels to use, let's recall the two key benefits of third party channel organizations:[27]

- **The manufacturer gains access to each channel organization's existing customer base**. When that customer base is part of the manufacturer's target market, the channel organization reduces the average time to market by months or years and increases the manufacturer's market share.

- **Channel organizations improve the manufacturer's cash flow.** Channel organizations carry some of the costs and take some of the risks associated with marketing, selling, and supporting customers.

In addition to the two general benefits, each channel provides particular value-added goods and services. Figure 14.3 on the next page shows which of the goods and services are usually provided by organizations in each channel. *NB: This match-up is a general guideline only; each channel organization is somewhat unique. What counts is what a particular organization actually does.*

How to develop a Marketing system from scratch

The following suggested general procedure for developing a Marketing system follows the Scientific Method:

1. CEO specifies three-year business objectives, defines major products, major markets, desired position in market, rough costs, and estimates resources available to develop, market, and sell products.

2. Sales executive specifies sales organizations and channels that support the product, market, and business objectives for the next three years. Specification includes definition of which channels will be in place, the markets each serves, the support costs, and the revenues generated.

3. Sales executive develops Direct sales organization into a healthy, productive channel and markets to organizations in the next channel to be developed.

4. Designated sales managers attract, qualify, and sign up the first three organizations in the second channel. They invest 90 to 180 days to get these organization up to speed and to mutually evaluate and debug their working agreements and support issues.

5. Systematically select, negotiate, close, and launch balance of organizations in second channel at a rate determined by the managerial and technical support available to support each organization effectively. If another channel will be added, begin marketing to channel organizations in that channel, but wait to begin hiring until the second channel is running smoothly.

6. Repeat steps 4 and 5 for the next channel when appropriate.

It is a legitimate part of the development process to iterate back to previous steps, including Step 1, because of results in each of the later steps.

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[27] A marketing manager emphatically suggested that I emphasize two things you probably won't get from channel organizations: cold calls on your behalf and dependable follow up of sales leads. In general I agree with this.

Always develop the Direct sales organization first because it is required to:
- Learn and appreciate what goods and services are required to sell the products to customers
- Attract, develop, manage, and support key accounts, including third-party channel organizations
- Provide continued support for customers whenever third-party channel organizations are terminated or fail to support them for any reason.

Adding a channel organization is like adding any other key customer:
- Credibility precedes commitment.
- The arrangement should be mutually profitable
- Don't add one which can't be supported or one which is marginal. It is better to get a pro-active "no" and keep it as a prospect, than it is to sign it up and then fail to support it.

	Channel Organization						
Goods and Services	Direct	Sales Representative	Distributor	Retail	High-Tech Distributor	Systems Integrator	OEM (Direct)
Intangibles							
Credibility	Yes	Yes	Fair	Yes	Yes	Yes	Yes
Convenience	Fair	Some	Yes	Yes	Yes	Yes	Fair
Information							
Manufacturer	Yes	Fair	Poor	-	Fair	-	Fair
Channel Organization	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Deliverables	Yes	Yes	Fair	Fair	Yes	Yes	Yes
Technical Support	Yes	Poor	Poor	Poor	Yes	Yes	Yes
Financial/Business	Yes	Fair	Yes	Yes	Yes	Yes	Yes
Deliverables							
Product	Yes	-	Yes	Yes	Yes	Yes	Yes
Options	Yes	-	Fair	Fair	Yes	Yes	Yes
Special Features	Yes	-	Poor	-	Yes	Yes	Yes
Updates	Yes	-	Poor	-	Yes	Yes	Yes
Product Documentation	Yes	-	Fair	-	Yes	Yes	Yes
Solution Documentation	Poor?	-	-	-	Yes	Yes	Yes
Products of other Manufacturers	Poor?	Fair	Yes	Fair-Good	Yes	Yes	Yes
Technical Support							
Application Engineering	Poor	?	-	-	Yes	Yes	Poor
Product Engineering	Yes	-	-	-	No	No	No
System Integration	Poor	-	-	-	Yes	Yes	Poor[28]
Installation and Testing	Prod. Only	-	-	-	Yes	Yes	OEM's Prod.
Training	Prod. Only	-	-	-	Yes	Yes	OEM's Prod.
Problem Solving	Prod. Only	-	-	-	Yes	Yes	OEM's Prod.
Maintenance	Prod. Only	-	Depot Level	?	Yes	Yes	OEM's Prod.
Financial/Business							
Availability	Prod. Only	-	Yes	Yes	Yes	Yes	OEM's Prod.

[28] Unless the OEM's product is the solution.

Price	Prod. Only	-	Yes	Yes	Yes	Yes	OEM's Prod.
Credit	Fair	No	Yes	Yes	Fair	Fair	Fair
Terms & Conditions	Yes	-	Yes	Fair	Yes	Yes	Yes
Warranty	Prod. Only	-	-	?	Yes	Yes	OEM's Prod.
Spares, Safety Stock	Yes	-	Yes	-	Yes	Yes	Yes
Contingent Liability	Yes	-	-	-	Poor	Yes	Yes
Licenses	Yes	-	-	-	-	Yes	Yes
Manufacturing Rights	Yes	-	-	-	-	Yes	Yes
Quality Assurance	Yes	-	Fair	-	?	?	Yes

Fig. 14.3 Typical capabilities of channel organizations to supply goods and services in support of a specific manufacturer.

How to optimize an existing system

1. CEO specifies three- and five-year business objectives, defines major products, major markets, desired position in market, and estimates resources available to develop market and sell products.

2. Sales Executive specifies sales organization at three years and five years that supports product, markets, and business objectives. Specification includes definition of which channels will be in place, the markets each serves, the support costs, and the revenues generated.

3. Sales Executive develops Direct Sales Organization into viable channel.

4. Sales management prunes marginal channel organizations, and focuses its efforts and support on best customers and best channel organizations.

5. Sales management carefully adds replacement channel organizations as resources permit.

Guidelines for adding channels

Be cautious about adding new channels or new organizations to existing channels. Some executives add them to give sales a shot in the arm, or to give the existing organizations a healthy dose of competition. Neither motive is sound. The results aren't likely to be good. The process of adding a new channel invariably diverts some resources from support of existing channels. If an existing channel is marginal to begin with, the resource diversion, coupled with channel conflicts, will create a crisis that will lose customers, channel organizations, and money. (See Chapter 21 on channel conflicts)

Whenever a new channel is added, the existing channel organizations become a bit more difficult and a bit more expensive to manage. It is practically certain that their profit margins will decrease unless the manufacturer proactively spends the time and money to avoid it. Unless the manufacturer's objective for the new channel is significant and well planned, it's not worth adding. Instead, the manufacturer should make the equivalent investment to improve the productivity of its most productive people and organizations.

Add a new channel when:

- The existing channels are operating effectively and profitably;
- Existing Channel organizations can continue to grow and prosper;

- The Direct organization has the resources to successfully launch a new channel without dropping the ball with existing channel organizations and customers.
- Within three years, the new channel will account for at least 20% of the sales and profits for the products it handles.

15. How to Hire Sales Professionals and Channel Organizations

"You never get a second chance to make a first impression."

The people in a marketing system have more to do with how successful it is than any other factor. Therefore, the process used to select sales professionals and channel organizations is crucial; yet in practice, it is often rather haphazard. In this chapter we'll discuss the selection process and practical ways to improve it. This is not intended to be a dissertation on the art and science of hiring. There are useful books on the subject and competent professionals available to train people in how to conduct interviews.

General approach

Hiring a sales executive or signing up a channel organization is a buying process like the one described in Chapter 5. The primary user-buyer is the individual who will directly manage the sales executive or channel organization. There may be other user-buyers, including those who will be peers, co-workers, or subordinates of the individual or organization being hired. The primary economic-buyer is the executive who has authorized the hiring. When hiring a V.P. of Sales, the user-buyer is the President or CEO and the economic-buyer is probably the Board of Directors. When hiring a channel organization, the primary user-buyer is usually the regional sales manager and the economic buyer is probably his boss.

Pro-Log had consistently successful results hiring individuals when it used selection teams that included the hiring manager (undisputed team leader), one peer of the hiring manager, one peer and one subordinate of the intended job position, and a representative from Human Resources. (Unfortunately, we seldom used a team approach to hire channel organizations. We should have.) Team members did more than help make the choice, they committed to help the selected person succeed. The Human Resources representative was a valuable technical-buyer, useful for finding reasons to exclude prospects, but not particularly effective at choosing whom to hire.[29] I also found it more successful to have team members interview the serious candidates at least twice. After the first pass, the selection team assessed its data, the reactions of team members, and identified specific areas to discuss in the next round of interviews. Our policy was to honor serious reservations by any team member. That is, if a concern were raised it was either resolved in the interview process or the candidate was dropped. The hiring managers had the prerogative to ignore the concerns of team members. Invariably, the results were less than satisfactory when a team member's concerns were ignored.

Benefits of thorough interviews

Well-planned and thorough interviews are well worth the time and effort to prepare for them and to conduct them. Key benefits include:

- *Mutual respect and credibility*: You impress the prospects that you know what you're doing, and you learn enough about the prospect to develop trust and confidence in them.

[29] I adamantly advise young professionals to look for companies where they are interviewed and selected by the person they'll work for and by other managers with whom they'll be working. When Human Resources plays a dominant role in the interview process, look elsewhere, because that organization's management is awash in a sea of Bureaucrats.

- *Competitive advantage*: You stand out compared with typical interviewers, and you learn what the competitive alternatives are for the prospects.

- *Negotiating advantage*: You acquire the data needed to determine areas of mutual benefit.

- *Minimize unpleasant surprises and unrealistic expectations*

Interview and hiring tips

As an engineering manager and as an executive, I successfully selected and hired scores of top notch engineers and engineering managers. But as a CEO, I hired VPs of Sales, Regional Sales Managers, and channel organizations with an overall success rate that was less satisfying. A selection criterion that works for engineers needs major adjustments to work for sales professionals. The following hiring tips have improved the success rates of others and would have improved mine had I used them.

Tip 1: Use the concepts and tools described on pages 63-156 of Conceptual Selling to conduct interviews. Prospective Sales Executives and Sales channel organizations are key customers. Interviews are a form of sales call in which you're the supplier selling them on a job. The prospects are evaluating you in the context of their competitive alternatives. You're also a prospective customer for their services, and are evaluating the prospect as one of your competitive alternatives. The concepts, objectives, and planning tools used for sales-calls also apply to these interviews.

Tip 2: Don't treat a sales professional's expressed enthusiasm for your company or its products as a sign of commitment. Technologists and sales professionals work in two different cultures. Engineers or scientists are critical, careful, and unenthusiastic about an alternative until after they commit to it. Sales professionals, on the other hand, are enthusiastic about any alternative until two weeks after they commit to something else. They use enthusiasm to keep their options open. They've learned to get the order first and then decide whether or not they want to accept it. When technologists interview sales professionals, they often mistake professional enthusiasm for commitment. However, this enthusiasm isn't "phony." It's a part of the selling culture and has integrity and purpose within that culture. In fact, if the person you're interviewing doesn't express enthusiasm for your company and its products, you should doubt that he's really a sales professional.

Tip 3: Before hiring an individual or a channel organization, negotiate and document mutual objectives, initial plans, and allocated resources that produce mutually acceptable performance on a tight schedule. Technologists are trained to gather data systematically to make rational decisions, consequently they focus on gathering data in hiring interviews. However, when a working relationship starts solely on the basis of data, the confidence levels between the parties is low, the relationship is fragile, and it is easily disrupted by problems. Highly successful people use the interview process to develop strong, positive convictions about the candidates they select and to engender strong, positive convictions in those candidates. Then, both parties start their relationship convinced that they'll succeed and ready to support one another when problems crop up.

A practical way to produce a high level of mutual confidence during the interview process is to negotiate a startup plan before making the job offer. First, solicit the candidates' proposals for how they'll solve your needs. Then develop a startup plan that covers the first 90 days. The plan should include mutually agreed to short-term objectives, resource commitments, and a clear statement of long-term objectives. One of two things will happen during this planning process: 1) you and the candidate will develop a high level of mutual confidence, commitment, and enthusiasm, or 2) one or both of you will decide to look elsewhere. Either outcome is far better than muddling into a collaboration that later fails.

Tip 4: Select a sales executive who believes in the effectiveness of the sales channels you're prepared to support. A sales executive will need to use channels (and people) in which she has confidence. If your convictions about sales channels are at odds with hers, it's a lose-lose situation.

Tip 5: Only hire those who meet or exceed your basic requirements and your standards. If you don't find a fully qualified person or channel organization in which you have high confidence, make-do with existing resources and keep looking. Hiring a marginal person or organization is demoralizing to others in the marketing system, and never profitable over the long run.

Interviewing Sales Executives

Planning checklist

- What would the individual's business results look like two years from now if the individual is successful? Develop clear, quantifiable objectives for the Sales Executive.

- What three to five attributes of the Sales Executive are essential for me to maintain an acceptable degree of trust and confidence in him/her?

- Where is my comfort range for the individual in the Adventurer/Craftsperson/Bureaucrat spectrum?

- What's the potential pay-off for the Sales Executive in terms of challenge, compensation, and relationships?

- What are my competitive alternatives to hiring this Sales Executive including other candidates and other ways to get the needs met?

Interview Checklist

The most important strategic job of Sales Executives is to attract, select, and manage competent sales professionals and sales organizations. It's worth asking prospects for specific personal examples of how they perform this job.

Management:

- How does the prospect attract, interview, select, and hire people?

- How does the prospect manage people?

- How does the prospect terminate people? (Specific questions for the prospect: What was the job of the most senior person you've terminated? Describe how you decided to terminate that person and how you went about doing it.)

- With what sales channels and channel organizations has the prospect succeeded?

- With what customers has the prospect succeeded?

- To what does the prospect attribute his/her success?

Motivation:
- What results does the prospect want within two years from successful performance in this job?
- What would a successful outcome look like two years from today?
- What aspects of earlier jobs were the most challenging? Most satisfying? Most fun?
- What incentives motivate the prospect?

Planning:
- How does the prospect develop plans? How closely does he/she work within those plans?
- What will the prospect do in the first 90 days in this job? If a prospect answers this question without asking for information in the process, you have the wrong person.

Follow-up analysis
During interviews, prospective Sales Executives are selling products: themselves. For them an interview is a sales call. How they conduct themselves is probably how they'll perform on the job. Here are some questions that you can answer for yourself by reviewing what happened during the interview:

- How skillfully did the prospect get and give information?
- Did the prospect practice win-win selling? Did he/she clearly specify his/her capabilities and requirements, learn yours, and help define the region of mutual benefit?
- Did the prospect take constructive responsibility for part of the agenda, or was he/she too passive or too controlling?
- Was the prospect's primary decision-making style: Adventurer, Craftsperson, Bureaucrat, or Victim? Was it one you respect?
- How competent was the prospect at planning, and at hiring and managing people?
- Did the prospect convince you that you would like to work with him/her?

Interviewing Reps or VARs

General Suggestions
- Conduct more than one interview of a qualified prospect organization, with at least one interview at its offices.
- During the first interview, emphasize the exchange of information and get answers to questions that determine whether or not this organization is a serious candidate.

- During subsequent interviews, get specifics about customers to which they would sell your products, how and why they would sell your products to them, and what support they would expect from you.

- During the final interview, mutually develop a 90-day startup plan.

Planning checklist

- What are the primary characteristics of target companies and user-buyers to which you want this organization to sell?

- Which three to five goods and services of Fig. 5.6 on page 57 does this organization provide to your customers? Which other ones would you like it to provide?

- What are your two-year sales objectives for this organization?

- What are your competitive alternatives to this organization?

- What support are you prepared to give and how are you prepared to supply it during the startup phase and afterwards?

- How can you help this organization succeed in selling your products to its customers?

Whom to Interview

- The owner/CEO

- The top two salespeople for your Products (as predicted by the owner/CEO)

- Technical Support person who would support your Products (when the organization has one or more)

- Three of their key customers: user-buyers and purchasing agents

- Sales manager for two of their top three product lines and for two product lines "on the way up"

Interview Checklist

The following checklist is overly detailed for any one organization. It is more useful as a menu from which to select the ten to twenty most appropriate items for each organization. Questions that are typically the most important are in bold italic.

Business

- Is this a well run business with qualified management and staff? (Specific data)

- What is its financial situation? What resources does it reasonably have to develop the market for your products?

- What territory does it cover?

- What services (Relative to Fig. 5.6 on page 57) does this organization supply? How well does it match your needs profile? How is the organization normally compensated for each service?

- What are its facilities and supporting technologies? (i.e. offices, computer systems, demonstration room, development and test equipment, communications, audio/visual, etc.)

- What are the overall annual sales of the organization? Overall annual revenue?

Ownership

- Who owns this business?

- What are the owner's long term business objectives?

- ***What are his exclusivity and longevity objectives? What is he willing to contribute to achieve them? How are they being met by current principals?***

- How current is he on what's going on in the field?

- Does he have accounts? Work on a regular and planned basis with the field sales people? Manage by remote control from his office?

Customers

- What markets does the channel organization specialize in, and what are its competitive advantages?

- Who are its top twenty customers and which of them are candidates for your products?

- At what management and technical levels does it usually interact with these customer organizations?

- What revenue might the top twenty accounts generate? What new accounts would they have to add to meet your objectives?

Line card

- ***What's on their line card? How many vendors? What synergies do the product lines give the organization?*** (Pick up their line card and marketing literature, both theirs and their principals')

- ***What are their three best-selling products? What is it about these products and their vendors that makes them the top three?***

- ***What does your company have to do to achieve a competitive advantage over any of their top 3 lines?***

- ***What does the sales manager for each of their top three product lines think of this organization?***

- ***What do key accounts expect from this organization?***

Sales and technical support people

- ***Who are the best sales and technical people relative to your product? How competent are they technically and as sales professionals (Adventurers, craftsmen, Bureaucrats, Victims) ?***

- ***How are the sales and technical support people compensated? What incentives do they get? How quickly and reliably are incentives paid?***

- How are sales and technical people matched with customers? By territory? By personal fit? As individuals? **As selling teams?**

- What has been the turnover of sales and technical support people in the last 2-3 years? Last 6 months?

- How are sales and technical support people selected and developed?

- What are the training policies and procedures for sales and technical people?

- ***Which days of the week are field people in the office?***

Information processing

- How is customer information organized and stored? Does it belong to the salesman; is it available to their organization; is it available to your company?

- To what degree do they use automation? How compatible is it with your systems? What are their prevailing attitudes about automation?

- To what information will your company have access? How timely will it be?

- What kind of leads do they prefer (how qualified)? How do they process leads? How would you close the loop?

Use the old-boy network

Tap into the informal network of personal relationships that exists between the sales professionals of channel organizations. Use it to develop and identify new channel organization prospects and to market your product and your company to them. The old-boy network is there and it operates for your benefit or to your detriment. There is nothing quite so inspiring to the channel organizations you have as having other organizations eager to represent you.

CEOs of channel organizations and their sales professionals interact with their peers in other territories at sales meetings, trade association meetings, trade shows, and when they sell to large accounts that cross territorial boundaries. They call each other when manufacturers have problems, change policies or agreements, hire or fire, etc. They are sometimes rivals, but always peers who have a pretty good handle on who is good and who isn't. Under the right conditions, some of the best ones working with you can help you find and sign up excellent organizations.

It's in their own interest for you to be well-represented in other territories. However, one caveat: don't put yourself in the position of having to hire someone they recommend. Seek their suggestions and their endorsements, but always make the decision on whom to hire after thorough interviews and careful analysis. Sometimes their personal relationships take precedence over sound business judgments.

Some trade associations, such as the Association of High Technology Distributors, encourage membership by manufacturers. If it's possible, join channel trade associations that one or more of your channel organizations is involved in. It provides networking opportunities and a window into the issues that these organizations are dealing with.

Eight common mistakes

1. Sign up a large number of organizations in a short period of time.

The motives for doing this are usually to get a nationwide (or international) presence quickly or to boost sales by "getting more feet on the street." Frank, the CEO referred to in the introduction, made this mistake. Signing a channel organization, or hiring an employee for that matter, is similar to getting a major order from a key account: it's only a tentative commitment; you still have to deliver in order to get paid. Each channel organization that's signed up requires immediate and extensive support to get up to speed. After that, it requires ongoing support to maintain its commitment and its sales momentum. Without adequate support, a channel organization will flounder and the manufacturer will lose credibility with its people.

2. Select a channel organization on the basis of an interview with its owner.

A Rep owner described the typical manufacturer's selection process to me:

> "*A Manufacturer's RSM calls me up, introduces himself, and says that he's looking for a Rep organization in my territory and wonders if I'm interested in handling his product line. We talk for a few minute; then he schedules an interview with me at my office, usually within a week or so.*
>
> *He shows up at the appointed time, spends about an hour telling me what he needs and asking me a few questions about my organization. I give him my line card, give him a guided tour, and get a packet of his sales literature. He leaves within two hours of arriving and interviews his other two or three alternatives.*
>
> *When he walks out the door, he doesn't know much about me or my organization. I'm the only person he has talked to. I'm a fairly skilled interviewer because I've done these interviews on a weekly basis for twenty-five years. I always choose to make a good impression, whether I intend to work with this manufacturer or not. If he decides in favor of my company, then about a week later I get a phone call from him telling me I've been selected.*"

3. Select the most successful organization in the territory.

The most successful organization in a territory can be a dead end for a growing company. That organization is a success because it already sells established product lines. It probably doesn't need to develop new ones. It may take on a new product line, but will probably limit its efforts to processing orders from those existing customers who sell themselves.

I learned this lesson the hard way in Pro-Log's early years. I signed up a Rep, in the Washington D.C. area, which had a great, longstanding reputation for selling large quantities of complex electronic equipment. Its salesmen all earned big bucks and drove fancy cars. I thought I'd made quite a coup to sign them up. I personally trained them. I made account calls with them. They professed enthusiasm. But over a two-year period nothing much happened in the way of business and I finally severed our relationship. I replaced them with a smaller, hungrier organization that rapidly developed Pro-Log's business.

4. Select organizations with large geographic territories to reduce the number with which you have to deal.
Some Rep or Distributor organizations cover large regions of the USA. A few of them span the nation. Some manufacturers jump at hiring these larger organizations, believing that it will simplify their jobs.

When an organization has several offices located in different cities, it's very likely that one or more offices won't actively sell your product even if the other ones do. Each office has its own characteristics and a degree of autonomy except in organizations managed by and staffed with Bureaucrats. Each office has to be individually managed and supported by a manufacturer to produce adequate results. So, a large organization really doesn't simplify the management problem; it may make it worse. When one office doesn't sell, but the others do, the manufacturer is faced with several mediocre alternatives: a) terminate the entire organization, b) work around the non-performing office, or c) accept the fact that there won't be many sales in the office's territory.

5. Hire a marginal organization because there's an urgent need to cover the territory.
"Marry in haste, repent in leisure" applies well to selecting sales organizations. Use the direct sales organization instead to buy time.

6. Hire third party organizations before making direct sales in the territory.
There are several reasons this is a mistake: a) the manufacturer doesn't know what it takes to close business in the territory, so he's going to rely blindly on the third-party organization, b) there are no successful accounts to use as credibility builders with the third-party organization, c) there is no income to fund the third-party organization's startup investment, making it less likely that it will invest much time and talent.

7. Hire without really "negotiating" an agreement.
Most manufacturers have standard agreements that they fill out, sign, and send to the channel organization. This agreement procedure is tolerated only because it's so universally practiced. We'll discuss a more effective alternative in Chapter 20.

8. Hire without having an agreed-to plan for the first 90 days.
An effective 90-day objective for a successful relationship is to build mutual credibility by closing a significant amount of business. To accomplish this requires a well thought out plan that is in place on the day the agreement is signed. We'll discuss this at length in Chapter 16.

Exercise

If you're a sales executive or a CEO of a manufacturing organization I suggest that you try the following and see what happens:

1. Review the preceding checklist of interview questions.

2. Pick out the ten questions that you consider most important to your organization.

3. Ask your sales managers those questions about one or more of the third-party organizations they currently manage.

This exercise should produce an interesting discussion, and clear away some myths. Don't be surprised if the managers don't know or guess at the answers to several of your questions.

16. How to Get Them to Sell for You

"*You can get everything in life you want if you will just help enough other people get what they want.*" Zig Ziglar

In this chapter, I'm going to suggest a 90-day plan of action that will get each channel organization in a Sales Representative or VAR channel off to a good start. It includes a step-by-step process for conducting the first training session. One premise of the plan is that sales professionals have to be sold on a manufacturer and its products before they will effectively sell those products. This means that they must be convinced that advocating the manufacturer and its products will benefit themselves and their customers. They aren't convinced when the agreement is signed.

The startup plan is described specifically for Sales Representatives. However, the principles apply to all channel organizations including Direct Sales, OEMs, and Distributors.

Background

The process of getting a sales professional, a technical support person, or a channel organization up to speed is like the process of getting an airplane into the air and up to cruising altitude; the pilot must position the plane carefully on the runway and then give it full throttle. She doesn't ease back on the throttle until the plane reaches cruising altitude. Without full throttle during takeoff, the plane probably won't get off the ground.

A sales professional doesn't reach his cruising altitude for a manufacturer and its products until he's thoroughly sold on them. That doesn't happen until one or more of his key customers tells him how wonderful the manufacturer and the manufacturer's products are. To borrow a phrase from Gen. Douglas MacArthur:[30]

> *When it comes to selling sales professionals:*
>
> ***There is no substitute for Customers***

Customers have far more credibility with sales professionals than manufacturers do. When a sales professional's best customers say a product and its manufacturer are excellent, he or she will be convinced. Until then, his or her commitment is conditional and fragile (in spite of professed enthusiasms). Any worthwhile plan to get a channel organization to sell your products must see each sales professional through the entire process of booking orders, delivering products, receiving commissions, and hearing positive comments from customers.

Fellow sales professionals have less credibility than customers; however they usually have far more credibility than manufacturers. Sales professionals who are successful with a manufacturer and its products become excellent resources for referral selling to sales professionals who are just getting started. On the other hand, when sales professionals or channel organizations' CEOs lose confidence in a manufacturer, they can and will poison the well for other sales professionals within their organizations and outside of them.

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[30] *"When it comes to war, there is no substitute for victory."*

The typical startup process

1. Manufacturer's Regional Sales Manager interviews and selects the channel organization.

2. Manufacturer fills out standard agreement, signs it, and sends to channel organization to sign. (For more on agreements and the signing process see Chapter 20.)

3. Signed copy is returned to the Manufacturer.

4. RSM authorizes shipment of literature and demo equipment. He calls channel organization to schedule the first training session on his next trip to the area.

5. Training session conducted: focuses on manufacturer's products, applications, and sales literature.

6. Sales calls scheduled for later trips by RSM.

This sequence looks good on the surface, but it is actually "business at cruising altitude" by the manufacturer. It squanders critical opportunities to develop credibility, commitment, and new bookings.

Plan Overview

- Have a negotiated startup plan in place before signing the agreement.
- Act immediately; use the "honeymoon" to set the tone.
- Bring sales professionals up to speed according to their decision making attitudes: *Adventurers first* (innovators and early adopters), *Craftspeople second* and *Bureaucrats last*. Use referral selling and the buddy system within the organization's office to get the Bureaucrats up to their speed (slow and steady).

Above all: Plan to provide plenty of timely support in the first 90 days. If you don't have the resources to support the organization, don't sign it up. The same advice applies to any other customer: don't book an order you can't deliver.

As stated in Chapter 15, I strongly encourage the manufacturer and the channel organization to mutually negotiate a 90-day startup plan during the selection process. When they wait until after the agreement is signed to develop the plan, they start off with less mutual credibility, take longer to get to market, and may not get the resource commitments they need from each other.

Plan Objectives

Objective for the first 90 days:

1. To sell at least one, and preferably two, Adventurer or Craftsperson sales professionals in each office of the channel organization on your products and your company;
2. To sell the organization's CEO and inside support people on your products and your company;
3. To have the sales people identify and effectively support all known customers (the ones you developed prior to taking on this organization) and their most significant prospects for your products;
4. To plan with the CEO and the sales professionals how to support effectively all their customers on behalf of your products within the first 180 days.

Objectives for the second 90 days.

5. To bring the rest of the organization up to speed;
6. To negotiate with the CEO and sales professional a path and a timetable for achieving, within two years, your company's relative position in their sales efforts and income.

The first objective is to identify the channel organization's Adventurer and Craftsperson sales professionals and to sell them on your products and your company.

A Sales Professional is **sold on your product** after all of the following occur:

- He understands your product and its benefits.
- He believes your product has a distinct competitive advantage in one or more areas.
- He has made a successful presentation to a customer and was able to answer questions.
- **His customer has ordered, taken delivery, and paid for your product.**
- His customer tells him that your product works well in his application.

A sales professional is **sold on your company** after all the following occur:

- He believes your Regional Sales Manager is competent, effectively supports him, and isn't a jerk.
- He has gotten competent, courteous, timely support to: solve technical questions, provide quotations or pricing, get delivery information, get service, get demo equipment or loaners, and get "exceptions" issues answered.
- He feels comfortable dealing with his contacts at your plant.
- He has received a significant commission from your company.

A Sales Professional becomes **unsold on your company and your products** when:

- A key customer who bought your products tells him your products or your company are no good.
- He repeatedly gets no response, or very slow response, to his requests for help or information.
- Demonstration equipment and literature are out-of-date, or not available when needed.
- He is yelled at by the Regional Manager or someone else from your company.
- Product is shipped late, and he hears about it first from his customer.
- His customer receives a product that doesn't meet specifications or doesn't work; then your company fails to take swift and thorough corrective action.
- His customer does not get prompt and competent service that is appropriate or as promised.
- His customer is treated rudely by your finance department.
- His commission isn't competitive or is delayed.

The CEO, owner/manager, is **sold on your company and product** when:

- His company makes money from your product line that is appropriate to the resources invested.
- His sales people and customers are sold on your products and your company.
- You and he have mutually developed a plan of action and support in his territory and you consistently work from that plan.
- You know your target market and have a Product, a promotional program, and a sales support system suited to that market.
- You have significant sales in his territory, as measured in $ volume and in number of accounts.
- You treat him with respect as a businessman and as an entrepreneur.

The CEO, owner/manager, is **unsold on your company** by any of the following:

- Reluctant or slow payment of commissions.
- A manager in your company initiates discussions about "unearned" commissions
- You stick him with obsolete inventory.
- You attempt to get his salespeople to sell for you to the detriment of his overall business.
- Unilateral changes in the Agreement, especially those that reduce his income or add restrictions to his activity; for example: reduced commissions or house accounts.
- Using the letter of the agreement to "win" at his expense.
- The coerced annual forecast, with only one "right" answer.
- Not being respected as a professional business person.

Plan Sequence

1. Negotiate a 90-day plan prior to signing the agreement.

2. Negotiate the agreement (See Chapter 20 for details).

3. Have literature, demo equipment, etc. arrive within days of receiving the signed agreement. Include information on your company and on the people in it with whom that the sales organization will deal. Send individual letters of greeting to each field sales person, each inside sales person, each technical support person, and any other individuals with whom you will deal.

4. Hold the first training session within two weeks of sign up. The specific end result of any training program, including the first one, is: "orders from customers."

5. Make customer and prospect calls with Adventurer or Craftsperson field sales people in the hours and days after the first training session.

First training session

Preparation

1. Read *Conceptual Selling pages 23-28* on how to make an effective sales presentation.

2. Manufacturers tend to focus on their products too soon and for too long. The sales people being trained start out with these questions, which are listed in the sequence they are usually thought of:
   - Is the person standing in front of me a professional, or a jerk?
   - Is his company reliable; will it support me and my customers? (The payoff for selling your products is only a commission, but the risk is that your product or your company could do something to alienate existing customers for all the other product lines.)
   - Does this company seem to know its business, its market, and its competitive advantages?
   - Is it safe to sell this company and its products to my customers?
   - Is it worth my time and effort?
   - Am I able to sell it to my customers? Why would my customers want to buy this? (At this point the sales person mentally attempts to match the product with some of his customers.)
   - Would it be FUN to sell this product for this company?

Objectives

- Identify the sales professionals who are Adventurers and Craftspeople.
- Get them to the point of committing to specific sales calls (with the manufacturer) within the next week or two.
- Leave everyone, including the organization's CEO, with the impression that working with your products and your company might be successful, profitable, and fun.

Remember: a training session only produces a temporary and conditional commitment in some of the individuals and has little or nor impact on the rest of them. If it isn't followed up quickly and effectively, that commitment will die and will be extremely difficult to resuscitate.

How to Conduct it

1. Prior to the training session, the Regional Sales Manager sets up account calls in the territory for immediately after the session. He works through the owner or someone the owner designates. The training session is scheduled at a time that minimizes lost selling time, probably the day of the week when the field people are in the office.

2. The training session is conducted by the Regional Sales Manager and at least one other person. While one of them conducts part of the meeting, the other person observes, takes notes, and records action items.

3. The Sales Manager starts the session with introductions and asks questions of each attendee in the session. (He has already studied background information on the people. He concentrates on attitudes and interests.) He learns what kind of support they appreciate from other vendors and uncovers support issues that have hurt their sales. To some extent this information should confirm what was learned during the evaluation process prior to signing up this organization.

4. The Sales Manager briefly describes his company and its history, the business it's in (a few concrete examples of who buys the products and how they use them), its products, its competitive advantages, and how it supports customers and sales people. He encourages questions. He gives the names of people in his company and some information about them that makes it easier for the sales people to contact them.

   Whenever an issue is raised that the Sales Manager can't handle effectively in the meeting, he should seize this as an opportunity! He frankly admits that he doesn't have the answer and he writes down a commitment to have an answer by a specific date. This sets a tone and establishes a process that encourages people to raise issues. It also teaches them to expect either an immediate response or a dependable commitment to respond by a specific date.

5. The product training starts with a description of how existing customers use it. The discussion, demonstration, and introduction of sales literature proceeds in this sequence:
   1) Existing applications and known markets
   2) Benefits
   3) Features
   4) Functions.

   The presenter and note taker watch and record how long the CEO and each sales professionals follow the discussion with interest and obvious understanding. It is a clue to the interest and caliber of each participant. Those who actively follow the discussion all the way through features and functions are the most likely to be Adventurers or Craftspeople. Bureaucrats' eyes will usually glaze over as the presentation moves from benefits to features.

6. The participants are asked if they see a possible match with one or more of their customers. When someone mentions a customer, ask questions about the customer and its application. Then explore whether or not a match exists. Those who volunteer customer names are probably Adventurers or Craftspeople. The Bureaucrats are not likely to risk naming an account during the first training session. They will avoid risking their judgment or their customers on your product or company until they've seen others in their organization succeed.

7. The Regional Sales Manager develops and documents everyone's follow-up action items and objectives. He summarizes the action items he'll pursue. He puts names and dates for completion on all action items. He double checks with everyone to make sure the actions are realistic and the individuals involved are committed to doing them by the assigned dates.

8. The Regional Sales manager makes the pre-arranged account calls with the appropriate sales professionals. The time is used to build one-one relationships.

After the meeting

1. Complete your commitments on or before the dates agreed to. Mail meeting minutes complete with action items to all attendees. They should receive these minutes within 48 hours of the meeting. Hold the others to meeting their commitments.

2. Make account calls with the sales professionals on the accounts they identified within three weeks of the meeting.

3. Schedule at least two more selling visits in the first 90 days.

17. Eight ways to Keep them Selling for You

"A failing of most managers is that they spend most of their time trying to make their poor performers mediocre instead of helping their good performers become outstanding." Peter Drucker

"Only mediocre people are always at their best." Sommerset Maugham

This chapter describes eight ways to build and maintain a high level of commitment and effectiveness from the best people in your marketing system.

1. Provide dependable, timely support

Dependable, timely support for sales professionals, channel organizations, and customers is essential. Without it, everything else is window dressing. When a sales professional or a customer requests literature, technical support, a quotation, special features, special pricing, a proposal, etc., respond to him immediately and do the work promptly. If your support takes a few days to complete, immediately get back to the requesting party, acknowledge the request, and commit to a deadline. Then, meet or beat your deadline. If your answer has to be "no," say so promptly and tactfully. Slow, undependable responses demoralize the people who make requests.

An executive of a startup company that wrenched a $100 million market from a firmly entrenched competitor said that timely support of customers and distributors was vital to his company's success. His people acted on requests the day they were received. When necessary, they worked after-hours and helped each other until every request was handled. He emphasized that timely field support and a reputation for integrity got his company a disproportionate share of selling effort from its distributors, and major orders from customers that had routinely bought from their less cooperative competitor.

2. Build on strength

Make it a business policy to give the best support to the most successful people and organizations; limit support to the less profitable; prune those who are unprofitable. Let's be practical: there is only so much support to go around, and demand for it always exceeds supply. When everyone is treated the same, then at best everyone gets inadequate support. Without a policy to build on strength, what usually happens is that marginal customers or marginal subordinates demand and get more support than the profitable ones. Managers who budget their level of support based on results, efforts, and competencies, deliver a clear message about their priorities and increase their own effectiveness.

Begin each sales planning process by studying your most successful customers, sales professionals, and sales organizations. Learn what characteristics make them successful, and identify opportunities to make them more successful. Next use these characteristics as templates for evaluating the potential for success of your other customers, sales professionals, and sales organizations. Then use the templates to identify and screen prospective customers, sales professionals, and sales organizations.

Instead of building on success, managers often waste valuable time and resources compensating for subordinates' incompetence or lack of effort. They are frequently directed to do so by their own managers!

Here's a typical example:

> A Regional Sales Manager who supervises five channel organizations significantly exceeded her quarterly sales quota. However, two of her channel organizations were substantially above their quotas, two met their quotas, and one stunk. Her National Sales manager criticized her for the weak

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> performance of the one organization and *spake* a profound management observation: "Just think of the potential business you're missing in that territory." Then he ordered her to get that organization's sales in that territory up to quota in the next quarter.
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> The channel organization was infested with several incompetent and uncommitted sales professionals. To improve their sales the RSM spent several frustrating weeks of next quarter trying to teach them, supporting them, and working directly with their customers. The time and support come at the cost of reduced time and support for her more successful channel organizations. The result was that she barely made her overall quota; however, all five of her channel organizations met their quotas. Furthermore, she did the selling and her incompetent and uncommitted sales professionals got the commissions! Of course her National Sales manager was satisfied, the numbers look neater, and the *obvious* failure appeared to have been corrected.

Compensating for weak performers is a poor way to get results, rewards nonperformance and penalizes success. If the RSM had invested more time to enhance the sales of her top sales professionals in the most successful organizations, her overall results would have been far better. She should have ignored the poor performers or replaced the weak organization with one that had a chance to become outstanding.

Management-by-weaknesses is a classic bureaucratic behavior. Bureaucrats want to avoid failure or the appearance of failure at all costs and over-react to weaknesses. Bureaucrats manage in a way that attempts to make everything look homogenous, balanced, bland, and well under control. They don't have significant successes or appear to have glaring weaknesses because they devote their energies to patching problems. ***Craftspeople and Adventurers produce successes in a context of evident weaknesses and some failures because they focus on enhancing significant achievements.***

In Chapter 12, I described how the CEO of one channel organization classifies his customers as either A, B, or C accounts. The A accounts are the strongest customers for his organization. For them his company's answer to any request is always "yes," regardless of company policies. B accounts are well treated but within the bounds of company policies. C accounts, the least profitable, get support on an *as available* basis. Weekly Planning starts with the A accounts, proceeds to the B accounts, and C accounts get leftovers. You can profitably do the same thing with your accounts, channel organizations, and sales professionals.

Novell, a leading manufacturer of computer networks and computer software, classifies its network resellers on the quality and quantity of their technical support. It provides them complete technical training, annually tests and certifies their technical competence, and then rates them. Novell's highest rating is "Platinum Reseller." Novell authorizes its Platinum Resellers to sell the widest range of its products and to provide the most technical services. It gives them first crack at sales leads and promotes the value of their Platinum rating to customers and prospects. As the quality of its Resellers diminishes so does the support and opportunities it gives them.

3. Have the best sales professionals visit the factory

Pay to have the most successful sales professionals visit the factory and while they're there, listen to them. Well orchestrated factory visits will increase their commitment and enthusiasm, improve field support by factory personnel, and bring in valuable new ideas. Carefully prepare for each individual's visit. Have a planned agenda and make sure that appropriate people are available and prepared to participate effectively. A typical agenda would include the following actions:

- Sales professional meets with the support people who have helped him and his customers, learns about what they do and their work environment, thanks them, answers their questions. (Takes them to lunch to say thanks and to share some fun.)
- Sales professional relates key success stories to support people, to executives, and to other factory personnel. The stories include descriptions of how the product, documentation, factory support, etc. contributed to success.
- Sales Professional briefs key executives (including CEO) on:
  - a) Manufacturer's three to five most significant selling strengths, with examples;
  - b) Three to five most significant opportunities;
  - c) Three to Five most wanted improvements, with specific suggestions or recommended solutions, if any.
- Key executives (including CEO) personally thank Sales Professional.

Optional agenda items:

- Update the sales professional's literature and demonstration equipment.
- Provide technical training,

At Pro-Log, we evolved a program like this almost by accident, yet it was a terrific boost for both the field people and the factory people. It began with an annual incentive program that we established in 1975 and ran for over ten years. Each fiscal year when an individual Sales Rep's bookings exceeded $750,000, he earned a free, expense paid trip for two to Hawaii. However, on the way to Hawaii, or on the way back, he had to spend a day at our factory in Monterey.

At first, these plant visits weren't highly structured, and the Reps set the agendas. They invariably spent time with inside sales and technical support people and several Reps brought them gifts. Some took them to breakfast, lunch, or dinner. Reps eagerly told their success stories to anyone who would listen and liberally gave credit for the help they had received from the plant. Eventually, we developed a more formal agenda and had them tell their stories, their opportunities and their needs to executives as well as to others in engineering, finance, and manufacturing. Their genuine enthusiasm for Pro-Log and its products infected the people they contacted, boosted morale, and increased the factory people's willingness to bend over backwards to support the Reps and their customers.

I must confess that it was several years before I added the executive briefing. However, it was sometimes one of the most beneficial aspects of the visit. There's a lot going to make this briefing effective: the sales professional is credible because he has produced results. His mood is upbeat and his attitude is positive. The briefing itself is about positive results: how to help someone become outstanding who is already good. (When a non-performer suggests improvements by the manufacturer, it's easy to dismiss them as excuses.)

An effective briefing process is to discuss strengths first, opportunities next, and needs last. Discuss how to enhance strengths and seize opportunities. Limit the discussion of needs to five items. Address needs in the context of strengths and opportunities. Avoid getting sucked up in an endless round of fixing problems. Management's role in the briefings should be to listen and to question for more information. Commitments to changes or additional support should be communicated to the sales professionals within two weeks of the briefings.

Most of Pro-Log's Reps were married men who brought their wives with them. The wives got a kick out of touring the plant and meeting people. At first we made no special efforts on their behalf. Later we had volunteers (usually spouses of employees) take them on company-paid sightseeing tours of the Monterey Peninsula while the Reps were in meetings. We eventually realized the impact the spouses had on the Reps' motivation and performance, and we deliberately involved them in incentive programs. In one, very successful, program we sent the spouses the monthly status reports and paid them the incentive bonuses. (Of course we were careful to do this with the Reps consent.)

4. Publicize competitive ratings among top performers.

Competitive ratings stimulate top sales professionals to do more because, like top athletes, they are highly competitive people. How they rate compared with their peers is critically important to them. Develop several performance categories that are meaningful to sales professionals and to you, such as major accounts, new accounts, new products, and growth rate in the territory. Publish the ratings monthly, if possible, but at least quarterly. Continue the ratings for at least a year. However, don't expect competitive ratings to stimulate the worst performers. Singling them out and highlighting their failures is counterproductive.

One year, we conducted a very successful, year-long incentive program to stimulate the sales of PROM Programmers, instruments that cost around $2000 each and were used to code Programmable Read Only Memory chips. We paid a $100 bonus directly to the sales professionals for every Programmer they sold. Each month, we published a list of sales professionals and their cumulative total of Programmers sold. The incentive program was a huge success and produced the largest annual growth in Programmer sales in the history of the company.

However, even though there were over 80 people selling the instruments, over 20% of the Programmers were sold by just two of them. One person was in the San Francisco Bay area. The other was in Boston! Each sold over 200 units. They were neck and neck throughout the year until the final day of the program when one of them beat the other by one unit!

They didn't sell over 200 programmers each to earn the commission. They did it to win, to beat each other. In the last months of the contest, each of them called the factory every day to track how many Programmers the other one had sold. They both made an extraordinary effort to win. Its been over 15 years since that sales program. I still keep in touch with both of them. The winner constantly reminds me that he won. The one who came in second constantly reminds me (only half in jest) that he thinks the other guy pulled a fast one on the last day. Both of them vigorously agree that they were driven to beat the other guy, and they thoroughly enjoyed the competition! *Neither of them has ever mentioned how much money he made from the bonus commissions.*

5. Conduct participative and interactive sales meetings

Participative and interactive sales meetings are far more productive than the "bring them in and lecture at them" ones. I'll illustrate this point by describing Pro-Log's most successful National Sales Meeting. There were three phases to the event: preparation, the meeting itself, and follow-up.

The *preparation phase* began six months before the meeting. It included setting the dates, picking the location, determining the objectives of the meeting, selecting the issues to be discussed, training some Pro-Log employees to facilitate small group discussions, developing and publishing the agenda, and promoting attendance. The meeting's agenda included a series of one-hour and two-hour workshops on topics that Pro-Log, channel sales people, and the CEOs of channel organizations had proposed.

The *meeting itself* was held near Pro-Log's plant so that employees could fully participate. There were over 60 participants from channel organizations in the USA and overseas,[31] and another 30 participants who were Pro-Log employees. The Pro-Log people included managers and executives such as the VP of Engineering, CFO, Director of Operations, the MIS manager, and other key people from sales support, marketing, engineering, manufacturing, and finance.

The participants were divided into teams of eight to ten people who sat together around circular tables in the main conference room. Two people on each team were Pro-Log employees, and the rest were from channel organizations. The teams were assigned in advance and worked together for the entire meeting. During the three days, they participated in eight workshops which followed this pattern:

1. The topic was presented to all the groups assembled, handouts were provided, and the key questions were posed. Some topics were presented by people from the field sales organizations, others by Pro-Log's staff. Presentations generally took less than 30 minutes.
2. Each team discussed the issue, developed and documented their conclusions and recommendations on it, and prioritized their key recommendations. One of Pro-Log's team members facilitated the discussion; the other was secretary and recorded the ideas on a flip-chart. Teams held their discussions in breakout rooms.
3. The groups reassembled, and a member of each team presented the team's conclusions and recommendations.
4. The assembly picked the top action items, and specific participants were assigned to follow up on them.

On the last day of the meeting, as Pro-Log's CEO, I was called in to listen to a summary of issues, recommendations, and action items. The action items specified who was responsible for them and when they would be completed. Then other corporate officers and I were questioned by participants who submitted anonymous written questions, or asked them from the floor.

The meeting also included presentations on Pro-Log's business and product plans, new product demonstrations, and time to rest or attend breakout sessions for product training and social events. All Pro-Log employees and their spouses were invited to the welcoming cocktail party on the eve of the meeting. All Pro-Log executives, meeting participants, board members, and other Pro-Log supporters including attorneys and bankers, were invited to the awards banquet on the second night of the meeting.

The *follow up phase* included completion of all action items within the deadlines set. Some actions simply required a yes or no decision on a policy or procedure. Others required implementation of programs and suggestions developed in the meeting.

How do I know that this meeting was a success? There were three indicators: sales growth in the following year, the enthusiastic endorsement of participants from channel organizations, and its impact on Pro-Log's staff. Of course the most important result was growth in sales and profits. However, the reactions of participants convinced me that we had succeeded within days of the meeting. The following two examples stand out in my mind.

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[31] Most of them brought their spouses and there was a spouses' program that ran in parallel with the meeting.

The night of the awards banquet, I was approached by the CEO of a Sales Rep organization that covered New York City, Long Island, and Northern New Jersey. I mention the territory because it's a dog-eat-dog region where people aren't accustomed to handing out or receiving compliments. He said "In my 20 years of business, this is the best National Sales meeting I've ever attended." He went on to say the principal reason was that he and the others had been treated with respect. His opinions and efforts counted in which issues were dealt with, what was discussed, and how they were resolved. In most sales meetings, he was simply expected to listen to the manufacturer's propaganda.

About two weeks after the meeting, I ran into our MIS manager in the hall. He had been a meeting participant. I jokingly asked him "Well Adam, are you ready to give up computers and go into sales?" He paused, thought a second and said: "If you'd asked me that question three weeks ago I'd have said 'no way.' But I found out from working with them in the meeting that those guys work hard, are serious about what they do, and are really sharp. Now I'd seriously consider selling as a profession." Adam is still an MIS manager, but he and the other participants developed mutual respect by working together for three days. A lot of cross-cultural myths and stereotypes were shattered.

6. Establish a "Top Sales Professionals" council

Establish a "Top Sales Professionals" council and listen to them. Make it a working council of six to eight field sales professionals. Appoint people to two-year terms based on selling results in the year prior to appointment. Have a written charter. Have members elect a new chairperson each year.

Members of the council can review sales training programs, help plan new product introduction plans, comment on incentive programs, write "how to sell" articles, actively participate in regional and national sales meetings, and work closely with marketing.

Membership in the council should be publicized to peers and to customers. It is appropriate to pay some of the costs to the individuals and/or their channel organizations. However, membership shouldn't take individuals out of the field more than 3 days a year.

7. Establish a Council of channel organizations

Create a channel organization council whose members are the CEOs of their organizations. Make it a working council of six to eight people and develop a written charter of responsibilities and authority. It should annually elect its own chairperson, and no chairperson should serve for more than two years. Use it to recommend or to negotiate changes in the basic agreements with channel organizations, to review pricing changes and incentive programs, to help develop agendas for national sales meetings, and to participate in their execution. Invest resources to help channel organization owners with their business issues. The Channel Council should meet with Manufacturer's executives at least one day a year to plan, to exchange ideas, and to socialize.

Limit the term of any member to 4 years and make this clear in the council's charter; otherwise the group will become frozen and useless because it might be insulting to replace one owner with another one.

Most manufacturers have some sort of Channel Council. However, these councils seldom have written charters or term limits. They serve at the will (whim) of the senior sales executive, meet once or twice a year and are expected to rubber stamp the manufacturer's policies and plans including changes to compensation. Councils that operate like this are window dressing. They are a worthless waste of time and talents.

8. Establish an effective and continuous training program

Everyone related to sales, from the CEO to the support staff, should be in constant training on how to sell, how to manage, how to listen to customers, how to evaluate customers, and a myriad of other related issues. Top athletes and world class musicians have to train every day or lose their competitive edge and their markets. Sales effectiveness requires the same dedication to continuous training on the part of the individuals and their organizations. The sales training programs of most companies, including channel organizations, are pathetic; and that's putting it mildly.

Advice to individual sales professionals: If your company doesn't have an effective sales training program, change companies or establish your personal training program and pay for it yourself. Don't wait or you're dooming yourself to perpetual mediocrity. No one is ever more interested in or more responsible for your success than you are. Others can only help you succeed after you've accepted total responsibility for your own success.

18. A Fresh Look at Classic Issues

"I come bury Caesar, not to praise him." Mark Anthony

What makes a Sales Forecast counterproductive

Most companies go through an annual ritual that requires their Sales Organizations to generate twelve- month sales forecasts. The forecasts are subsequently used to justify business plans and to set quotas for people and organizations in the marketing systems. In this section, I'll explain intrinsic defects in the Annual Sales Forecast, and suggest some productive alternatives.

I've presided over the annual sales forecast ritual more than a dozen times, and have been consistently frustrated by its results. Forecasts and actual sales were seldom within 20% of one another at the macro level. Things were substantially worse at the detailed levels; it was difficult to find any significant correlations between actual bookings and forecasts by quarter, product type, customer, or territory. In good years, it didn't matter. In bad years, there was nothing we could do about it. Year after year, I modified the process in futile attempts to improve our results. But in all honesty, they never improved. Eventually, I realized that the process itself created bad data and hurt sales. I also realized that, when total sales happened to come close to the annual forecast, it didn't mean that the sales organization had done a better job.

Forecast objectives

- Provide bottom-up data to support (validate, justify) the business plan
- Establish targets for quotas and incentive compensation (good old MBO!)
- Provide data from which manufacturing can schedule production runs and generate material requirements.

In reality, the typical forecast doesn't produce squat to support these objectives. It appears to validate the business plan because the plan is a "right" answer that permeates the forecasting process. The sales quotas are usually set from the top down with little more than lip service to the forecast. A well-managed material planning operation wisely ignores the sales forecast, generates its own forecasts based on historic trends, and then constantly adjusts them based on actual backlog and weekly orders.

Forecast process

The sales forecast is usually conducted early in the annual planning cycle. Regional sales managers are required to develop a twelve-month forecast by month, by product line, by territory, and by major customers. The regional managers in turn coax forecasts from their third-party sales organizations and from their own major accounts. They massage these forecasts by applying their management judgment and by conducting intense negotiations with their subordinates. Then they pass massaged data up through the sales organization where it is further reviewed, massaged, and renegotiated by each higher level of management.

The forecast process has intrinsic weaknesses which tend to be overlooked in the search for "hard numbers" around which to build a plan.

The forecast process is a game of *telephone*

The people in the forecasting process, starting with the CEO, are actually playing a game of *telephone* to generate the results. Telephone is a parlor game that demonstrates how information gets garbled as it goes from person to person. It's usually played like this: A person whispers a message into the ear of a second person. The second person then whispers it to a third person. The third person repeats it to a fourth and so on. By the time the message has gone through five people it bears no resemblance to the original message. The CEO's initial message may be "Develop an objective sales forecast." It gets garbled to "Show me how you'll meet the numbers in my business plan." If the business plan numbers aren't available, those doing the forecast will first decide what management wants them to be and then generate conforming forecast numbers.

Telephone has such a deleterious impact on the forecasting process, and on other planning processes, that I'm going to describe some examples of what happens. I designed a business version of telephone for management workshops at Pro-Log. During the class, five people were sent out of the room. Then they were brought back one-by-one, first to hear and then to retell a message. The rest of the class heard each retelling and noted how the messages got garbled. The original message was in writing and about two paragraphs long. It described a business situation, within the company, in familiar terms, and asked the person to do several specific things. After hearing the message, the first person could ask questions, but couldn't take notes. Then the second person was called into the room and heard the message as recited from memory by the first person. The second person could ask questions of the first person before retelling the message to a third person, and so on.

I employed this version of telephone over a dozen times in management workshops. Without fail, by the time the fifth person recited the instructions, they were hopelessly wrong. Oddly enough, the process of asking questions introduced many of the errors. Few people limited their answers to what they'd heard. They guessed what the answers should be. Only once, out of some 60 times, was an exchange from one person to another "accurate." One woman apparently had a phonographic memory. She asked no questions, answered no questions, and simply repeated verbatim what she had been told.

In one workshop, I paired people up to listen to each telling of the message, ask questions, and then discuss with each other what they heard before relating it to the next pair. The message got screwed up even faster and more thoroughly! What makes this particularly relevant to our forecast discussion is that each pair of participants were executives who frequently worked together. One of the more memorable pairs was the Director of engineering and the Director of sales. As they "discussed" what they'd heard, they disagreed on a vital point. As it turns out, the Director of engineering had remembered it correctly and the Director of sales hadn't. However, the Director of sales was more persuasive and after a brief, heated discussion, the Director of engineering acquiesced.

The annual forecast is a process that passes a request down through the organization, and passes conclusions back up through the organization. Even for a modest sized company with third-party channel organizations, there are at least six people in any path: the CEO, VP Sales, Regional Sales Manager, Channel Organization CEO, Channel Organization Field Sales Professional, Customer contact person. The intent of the forecast (which is the context which determines what numbers are generated) is communicated verbally or not at all. The CEO may say or put in writing that he wants objective data (as I naively did year after year), but somewhere down the line the intent changes to producing a forecast that is acceptable to the next person up the line. If the acceptance criteria aren't explicitly spelled out, an individual will guess what it is based on experience. The data he passes back will have been pre-filtered by his guess.

Customers' numbers aren't that reliable

Most of us pretend that our customers are sources of accurate, objective information, but they aren't. Their internal forecasts are just as faulty as our own. They also filter and fudge the projections they give suppliers. They frequently distort projected requirements to manipulate suppliers. Let me describe a typical case:

> A supplier's representative asks a customer's purchasing agent for a twelve-month forecast on how many widgets he'll need. The purchasing agent invariably overstates quantities relative to his company's actual projections. He knows that prices, delivery, and service improve as his projected quantities go up. Besides, his own "information" comes from forecasts that he knows are never right so he isn't lying, he's just modifying his data to get the most favorable results from the supplier.
>
> The purchasing agent may exaggerate even more when there are shortages of widgets. He may even issue duplicate purchase orders to two or more manufacturers or distributors of widgets, accept the first widgets he receives, and then cancel the other orders (or resell them on the gray market). This kind of double and triple ordering has repeatedly whipsawed manufacturers in the semiconductor industry from 52-week backlogs to surpluses of shippable products within a few weeks. In reality, the customers' forecasts were worthless and so were their booked orders.

The forecast process creates lose-lose situations

When the manager of a channel organization submits a forecast to the manufacturer's RSM, he knows from experience that it will be used to measure his performance and to set his quotas. That biases him to underestimate so as to maximize his actual income. However, if he forecasts too low, he'll wind up in a confrontation with the RSM (who has his own right answer) to the effect that his numbers aren't good enough, and if that's all he can commit to, there'll be a change of organizations.

To avoid all this unpleasantness, he determines the RSM's acceptable range of numbers and massages his own data until it fits. After all, the data is questionable anyway, and he's just modifying it to get the most favorable results from the Regional Sales Manager (managing the manager)[32]. One channel organization CEO flat out told me he did two sets of forecasts for each product line; the "accurate" ones from which he generated his own budgets (and beat up his sales professionals?) and the doctored ones that he gave to his principals. He further said that he wished he could trust his manufacturers enough to discuss the accurate forecasts with them and get the support he really needed.

Now if you think I've painted a pessimistic picture, you're wrong. The reality is actually worse than I've described it thus far. For example, some customer or prospect forecasts are partly based on the timing and outcome of their own new product development programs. Their programs can slip by months or be canceled at any time after the supplier is given their forecasts.

Forecast data is largely obsolete by the time its used

By the time a forecast is developed and massaged, the customers' data are already two to three months old. During the ensuing year the actual situation changes dramatically, and a healthy marketing system

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[32] For more on how subordinates massage data to manage their managers see the essay *Effective and Meaningful Jobs* in Appendix A.

responds to the latest information. However when times are tough, some managers beat up subordinates for missing obsolete forecasts (that gave the right answers) instead of helping them make the most of the latest situation. It's comparable to beating up on engineering for not forecasting a development project accurately or for revising the product specification after new customer requirements, new competitive information, or new technologies have emerged.

Other things the forecasting process doesn't account for:
- Global variables: Economic conditions, competitors' initiatives, product problems, personnel changes, new product timing
- Support required to make the forecasted bookings and shipments happen
- Incremental profitability of the forecasted business to the marketing system

Competitive Alternatives to the annual forecast
One fundamental problem with the forecast is that it violates the Principle of Three to Five (Chapter 3). It tries to satisfies too many objectives and winds up doing them all poorly. Separate sales planning from the process of setting sales quotas. Start with sales objectives that are based on ongoing planning information and work with the sales force to work out how to make the objectives happen.
- Major accounts: ongoing forecasts, relate to support budgets, use customer's marketing data
- Sample major account data: AQL by executives done at customer's places of business
- Small accounts: measure group momentum
- Separate forecasts from quotas

Individual Quotas and Incentives

My impression is that the god of many sales managers is Pavlov. Their first commandment seems to be: set quotas, dangle incentives in front of the sales professionals, drive them from the rear, and then expect them to jump through hoops to reach the quotas. One problem with this religion is that customers become an objective to be controlled and manipulated to meet the quotas. Another is that the focus is on closing orders and collecting money; not on the mutual success of buyers and sellers. A third is that this treatment of sales professionals is suspiciously similar to dog training. That's not the stuff of successful business relationships.

Two recent examples illustrate the detrimental affects of typical, too simple, incentives.

> Several years ago California and New Jersey filed charges against Sears Roebuck for consumer fraud in their auto repair shops. The shop managers were being paid hefty incentives based on the amount of repair work they sold. They were (alleged to be) selling repairs that customers didn't need. Within weeks Sears announced that it had terminated the volume based incentive program and replaced it with one based on overall customer satisfaction.
>
> Last year Orange Country went bankrupt because its financial manager had invested heavily in bond derivatives. The investigation is still in process, but it has already revealed that a risk manager in the firm which brokered the speculative transactions had tried to cut them off long before the disaster occurred. However, he was vigorously overridden by the sales department, which was receiving handsome commissions to keep the process going. So far the management of the brokerage firm hasn't shown the same wisdom that Sears demonstrated.

Now don’t get me wrong. I’m heartily in favor of setting clear objectives and seeing to it that they contain strong attractors for the people working to achieve them. Financial incentives can produce significant attractors.

Financial incentives are also an integral part of the culture and the success of Silicon valley, but they usually take the form of stock options. Stock options can be quite lucrative when there is overall growth in sales and profits over a significant period of time.

At the very least I believe financial incentives should be tied to objectives that encourage teamwork in selling and which include long term profitability for the company, customer success, and customer satisfaction. However, the starting point for developing an effective incentive plan is to discuss it with the sales professionals it is supposed to compensate and motivate. Also, remember the lessons of Sears and the brokerage firm:

> **Anyone who does a job strictly for the money, eventually does a terrible job.**

This applies to sales professionals and to executives. An executive who is primarily motivated by salary, perks and stock options will also do a lousy job. I have a sneaking hunch that if one were to plot job performance versus total compensation in executive jobs, peak long term performance would probably show up in the lower paying jobs. The reason most compensation programs work as well as they do is that so many people are also motivated by other things, including doing the best possible job whether or not they get paid for it.

Launching New Products

Most companies struggle with how to launch new products to new markets. They start with an approach that seems to be perfectly rational, but seldom works very well. They announce their new product to the entire sales force, give everyone a crash product training course, and offer special incentives (usually bonuses) to motivate everyone to beat the bushes. Out of a sales force of 100 people, perhaps ten people put in the extra effort and the others take a wait and see attitude. Management noodles the undesirable results and decides to increase the incentives (the carrots) and/or add a “new product” sales quotas to everyone’s compensation plans (the sticks). This produces a slight increase in support for new products, but not much. It usually reduces sales of everything else.

When we consider the information on Decision Makers in Chapter 4, and when we look at people in the sales force as customers, the problem takes on a new light. At least one workable solution becomes fairly obvious. There is a distribution of decision making attitudes among the individuals in the sales force just as there is among customers. The typical staff of sales professionals includes Adventurers, Craftspeople, Bureaucrats, and Victims. Adventurer customers are the innovators and early adopters of products. Adventurer sales professionals are likewise the innovators and early adopters who enjoy launching new products. They are the ones who will happily take the risks involved in finding new customers for new products. They have the self confidence to take unproven products, identify innovator and early adopter customers, and live through the process of shaking the products down. Let’s be realistic, most products have performance and delivery problems for the first six months or so. Craftspeople and bureaucrats, be they customers or sales professionals, are turned off by these problems.

The craftspeople sales professionals need to see a successful shakedown of the products and a clear vision of their key features and benefits before they can comfortably push them. The Bureaucrats are once and forever account administrators, and no amount of incentives can induce them to take risks. Fear will only induce them to go through the motions.

The problem is that most sales forces are divided by geography. A product launch through the adventurers will typically reach less than 10% of the geographic market, the regions they are assigned. What manufacturers really need are sales efforts to the innovators and early adopters in every region. To do this, **manufacturers and channel organizations should seriously consider dividing up regions among teams rather than among individuals. Each team would include at least one adventurer and one craftsperson sales professional.**

19. Automating Your Marketing system

Automation is a combination of methods and tools that leverages human actions. The tools can be as simple as a telephone, a tape recorder, or a FAX machine, or as complex as computers and computer networks. However, ***people*** are the core resource of a successful marketing system, not methods and certainly not high-tech tools. Automation can improve a person's commitment and effectiveness, or it can undermine them. It can attract competent sales professionals, prospects, and customers, or it can alienate them. The results depend on how automation is designed, how it is introduced into the system, and how it is used.

Automation can be used to reduce selling costs. However, merely reducing selling costs might reduce profits by forfeiting profitable customers or by increasing costs in other parts of the business. If the primary objective of using automation is to reduce costs, it is misguided. Cost reduction targets are attractive to Bureaucrats because they are measurable by GAAS numbers. But mere cost reduction measurements are short term and usually misleading. They ignore the longer term, overall impact on both the marketing system and the business system. In the context of Fig. 2.1 on page 20 and Fig. 2.2 on page 22, cost reduction measurements partially evaluate the results of automation at Step 4 of the Scientific Method, the detailed level, and ignore its effects at Step 5 and Step 6.

Automation can be used to improve profits. Profit improvement objectives are better criteria for investing in automation than are cost reductions. At least they call for measuring automation's impact on the business as a whole. But profit improvement objectives don't go far enough.

> **The best uses of automation enable good people to do outstanding jobs, attract more of the best and brightest people to the organization, and help make the marketing system as simple as possible.**

The best uses of automation in your marketing system will attract more of the best employees, people in channel organizations, prospects, and customers. When your best people are enabled to do outstanding jobs, they will produce years of sustained growth and profits.

In this chapter we'll discuss some practical examples of effective automation in marketing systems, indicate how to go about automating your marketing system, and suggest what an executive can do who doesn't have a personal feel for computers or networks and their role in automation.

Examples of effective automation

The following examples of automation illustrate the endless variety of opportunities to employ it in marketing systems. I've avoided rounding up the usual suspects: customer data bases and contact management systems. Most of these examples directly help customers, reduce the marketing system's labor and costs, and improve its responsiveness to customers' needs.

A manufacturer of electronic cabinets provides free **software containing detailed product drawings and technical specifications in a format that's compatible with standard CAD packages**. The software is available on discs or can be downloaded over Internet. This speeds up the customer's design, improves accuracy, makes it more convenient to use the manufacturer's products than competitive products, and reduces design and documentation costs.

Banks provide **automated teller machines** that enable us to make deposits and withdrawals without human assistance, 24 hours a day, 7 days a week at numerous convenient locations.

Audio cassettes and car phones enable sales professionals to learn and to communicate while driving. Field Sales people average more than 10 hours per week on the road. Many already listen to audio cassettes on selling and motivation. Some manufacturers supply training tapes about their own products; how to use them and how to sell them. Audio tapes could also be made available to prospects and customers. Many of them also commute several hours per week.

UPS supplies **software that enables its customers to track their own shipments**. This software increases UPS's credibility, reduces customer calls about shipments, and is fun to use. UPS workers also have a subtle incentive to perform well because they know that their handling of packages can be audited by the customers at any time. The competent workers take this as a challenge to consistent excellence. Less than competent workers see it as a threat. (Consider providing sales organizations and customers with software that enables them to track their orders through your manufacturing and marketing system.)

Individuals can **use Internet to plan flights, find the best fares, and order airline tickets**. Internet providers, such as America On Line enable free access to American Airlines Easy SAAbre reservation system. Tickets can be ordered and delivered to home or office within 48 hours. Those willing to do a little more work can note the flight and fare information, then contact one of the airline ticket discounters on Internet or advertised in newspapers, and usually get their tickets at substantial discounts. This, do-it-yourself ticketing, might eventually reduce the dependence of airlines on travel agents, one of the top four costs in the business of flying.

Remote diagnostics via telephone. Manufacturers and service organizations use telephone links to diagnose equipment such as printing presses and computers. In some cases they can upgrade and repair equipment via telephone. Doctors use a telephone link to periodically monitor patients with pacemakers. They check the pacemakers' performance and monitor the status of its battery. The patients simply place a call from home and connect the pacemaker to a monitor that is linked to the telephone.

Companies, including Hewlett Packard, have made sales and technical literature available through a third party **FAX on demand** services. A customer's request for information generates a document on the customer's FAX machine within hours. Other companies have established **Bulletin Boards and Web pages on the Internet** from which customers can download sales literature, application information, specifications, ordering information, software updates, etc.

Eight tips on how to automate

1. Treat the process of automating the marketing system as a continuing series of improvements, each of which is designed for and sold to a client base.

The best process for incorporating automation into the marketing system is nearly identical to the best process for designing and launching new products. The people who will use the automation are its prospective user-buyers, whether they are employees of the manufacturer, people in channel organizations or people in customer organizations. These automation customers have the same range of attitudes (Adventurer, Craftsperson, Bureaucrat, and Victim) towards adopting a new way of working as product customers have to adopting new products. The Adventurers make the best innovators and early adopters. The Craftspeople are the next successful adopters and the Bureaucrats follow reluctantly behind when all is proven to be safe and secure.

Automation customers often have strong personal preferences about the hardware and software they use. The automation project team should respect and value these preferences. People will succeed more often when they use the tools they are comfortable with and believe in. Standards are fundamental to a successful automation program. But, forcing everyone to use identical hardware, software, and operating procedures in the name of corporate standards does not produce the best results.

Automation customers have their own motives for how they already do their work. These motives shouldn't be ignored. For example: Field Sales people keep customer information in black books. However, they are reluctant to put the same information into a data base because the black book is their property, and data in the data base is their company's property. They consider account knowledge (and their personal credibility with customers) as vital to their own job security. Putting what they know on a data base makes them less necessary and therefore more vulnerable.

2. Give automation a significant priority, adequate resources, and rewards

At Pro-Log we formed a Process Improvement Group (they playfully named themselves the Pigs); a co-ordination and resource group made up of representatives from line organizations. The PIG's chairperson reported to the CEO. Its primary tasks were:

a) to lay the groundwork for business-wide coordination and compatibility among the processes developed by the line organizations,

b) to see that training and other resources were planned and available to support line organizations, c) to encourage sustained programs of innovation in each line organization,

d) to work with the Product Planning Committee to find opportunities to harmonize process improvement plans with new products.

As we automated our factory we immediately tied measurable improvements in productivity and knowledge to pay increases. When a new piece of automation was introduced, specific people were selected and trained to use it and as soon as they became proficient received substantial raises. Within a year the people in manufacturing went from reluctant participants to actively driving improvements into the manufacturing process. .

3. Use the marketing system's line organization to select, manage, and execute its automation projects

Don't manage automation projects through the data processing department. DP professionals are valuable as resources but the wrong people to select and manage automation in the marketing system, or in any other line organization. It's as inappropriate for DP professionals to manage automation as it is for Human Resource professionals to manage engineers, sales professionals, or executives.

4. Use automation tools that are industry standards

As you automate your marketing system (or any other part of your business) keep these things in mind:

- Your expertise is in what you sell, not in how you automate.
- Automation tools will continue to be improved by their manufacturers.
- You can't keep up with the state-of-the art with do-it-yourself automation.

Therefore, when you need automation hardware or software buy it, don't make it. Whenever possible buy industry standards from leading or emerging suppliers because they have the income streams and competitive motives to innovate their products. Avoid unproven products or software vendors' vaporware. You'll be using automation products to change significantly how people do their jobs. **Don't get in the position of debugging the automation products while debugging your changes.**

5. Adapt automation to the people who will use it, and make it pay dividends for them as quickly as possible.
Establishing credibility with the *customers* is the first hurdle in introducing automation, just as it is the first hurdle in selling products to customers. There is no substitute for *successful customers* to establish credibility with the rest of the market and to create a "pull" for more improvements.

First projects should be relatively simple, quick to implement, with significant pay-offs for people implementing them. The pay-offs should primarily come from improvements in their output and increases in their personal satisfaction, but can include recognition and financial rewards. Early projects should be chosen more on the basis of who is ready to make them succeed than on overall impact to the organization.

Banks followed this approach to introduce automated teller machines. They introduced ATM machines to reduce their labor costs. However, most of us were initially intimidated by the ATM machines and suspicious of them, so banks launched the ATM machines as devices which enabled us to get our money twenty-four hours a day, seven days a week at convenient locations. Those of us who learned to use the machines got an immediate payoff in convenience and flexibility. The banks also made ATMs easy to use by having them carefully walk us through a sequence of simple steps. They limited withdrawals to $20 increments to simplify their use and their upkeep. Once we became comfortable with ATM machines, more and more of us used them during regular banking hours and enabled the banks to reduce the number of human tellers.

Don't start with a massive automation program aimed at big payoffs for the company and no payoffs for the people who use it. This is equivalent to "push" selling. It might look good on paper, but it isn't very effective. It probably wont succeed because those implementing the program wont have strong personal attractors to pull them to success. Users who fail will breed cynicism, hostility, and resistance towards automation in general. Automation programs, especially grandiose ones, are relatively easy to sabotage.

6. Adopt phased introductions
Use enthusiastic volunteers (Adventurers) for alpha testing. They will discover the bugs and help you correct them. Once the system is reasonably sound, use Craftspeople to nail down its effectiveness and dependability in beta testing. Finally, release it to the general market which includes the Bureaucrats who will adopt it slowly and carefully after they that others use it successfully.

7. Encourage play and risk-taking while working for significant payoffs
I've mentioned the importance of fun several times in this book. I'm going to do it again. Playfulness and fun are integral to successful automation. At the concept level, using automation and playing video games are identical! That is, both are interactions between humans and machines to achieve specific human objectives. However, automation usually requires manuals and costly training, expensive mistakes, and repeated efforts to motivate users. By contrast, Video games don't have user manuals; people train themselves through trial and error and are highly motivated to correct their own mistakes and become experts. The difference: video games are fun because: they are real-time, interactive, pseudo-realistic with full color graphics and sounds that involve the operator's entire brain; they include lots of interim milestones, rewards and surprises in the process of learning; they have new challenges just beyond the user's existing level of competence; they allow the user to fail repeatedly without disaster or being embarrassed.

In essence, video games are better designed because they have been made people literate. Automation lacks playfulness and is more poorly designed. People are expected to become machine literate.

There is no technical reason why sales automation can't have the motivational and training features of video games. However, there are two human impediments: a) a puritanical view that work and fun are separate, and b) an insufficient understanding of and respect for users by some of those who design automation equipment and automation software. Technologists, particularly computer scientists, are trained to view machines as the center of their systems rather than to place people there. Sad to say, there are no required engineering or computer science courses on how the human brain, the human perceptual system, and the human motivational system work.

8. Whenever possible give people choices in the tools they use and in how to work with them.
There are certain aspects of automation that depend on standards for their effectiveness, especially data bases and communications. Where standards produce substantial gains they should be adopted, particularly if they are industry standards. However, the attitudes people have towards the tools they use also impact effectiveness. Automation tools are like any other products, when individuals have competitive alternatives to choose from, they are more satisfied with and committed to the choice they make.

Diversity also leaves the door open for users to develop surprising improvements.

Suggestions for computer-resistant executives

Use computers, communication equipment, and other tools to get a visceral feeling for what's practical and what's not.
Almost all recent graduates of engineering schools and business schools have used computers extensively. They have also used Local Area Networks, and probably used Internet to do research, lab work, and reports. They are as familiar and comfortable with these technologies as those of us over 40 are with the telephone.

Unfortunately, the majority of executives over 40 have little or no experience with these tools and have developed working habits that don't take advantage of them. I know several CEOs of electronics companies who don't personally use computers.[33] Their secretaries use them, but they don't. These executives, and others like them, are vulnerable to techno-babble because they don't have a feel for a technology that is vital to their company's competitive health. I'd bet the farm that IBM's corporate executives didn't use PC's before 1990. It would explain their incredibly bad decisions about the computer business.[34]

Let me put this another way, as indelicate as it might be: Prospective employees, customers, and investors should steer clear of organizations (including channel organizations) whose top executives don't personally use computers. Those executives are as out of touch with competitive reality as executives in the 1920s who didn't use telephones. Their companies are either in trouble or headed for it.

Buy an IBM compatible portable PC.

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[33] About half of them have computers on their desks that are either off or permanently displaying screen savers.

[34] For more on this read "The Computer as God?" in appendix A.

If you're an executive who doesn't use a computer, invest about $5,000 in yourself and get a portable PC, a laser printer, and lots of paper. Your PC should be IBM PC compatible[35], have an active matrix color display, a PCMCIA port, a V.34 data and FAX modem, at least 6 hours of battery operating time, and a quad-speed CD ROM player (external is OK). If you don't know how to type (now called "keyboarding skills"), get a typing tutor program and teach yourself. Play games on the computer, have some fun in the learning process. Get an X-rated CD ROM if that's what it takes to motivate you. Experience the frustrations of using Microsoft Windows and promise yourself and your customers that you won't force them to work with software that's so poorly designed from a human factors perspective. I suggest that you buy Quicken (CD ROM version) and use it for your personal finances. It's useful and is easy for novices to use; which is to say it's well designed.

Get an Internet account and learn to *surf the net.*

Internet, particularly e-mail and the World Wide Web, is an infrastructure tool that provides revolutionary opportunities to connect companies to their marketing systems, their customers, and their prospects more quickly and more effectively. Once you personally experience what you can do on the Web, what resources are available, and what its minor annoyances and major limitations are, you can intelligently support programs that use the Web profitably.

Sign up with an Internet access organization like Netcom and use their NetCruiser software to surf the net.[36] It costs about $20 per month for 40 hours of usage in prime time and unlimited usage on weekends. An e-mail account is included. Learn to use it and put your e-mail address on your business card. Visit Web sites of other companies in your business and download or print out samples of data and graphics they make available. Later, create your own, personal, Web page and encourage those inside and outside your company to access it. When you reach the point of having a Web page you'll have your own ideas of how to use it.

If you use your computer for at least 4 hours a week for 3 months, your perspective and your decisions about computers and automation will dramatically improve. I know of no substitute for doing this. If you think you don't have time to do it, I suggest you don't have time not to do it. Those who don't have a feel for computers and networks will continue to be swamped by an ocean of buzz words, techno-babble, and automation schemes that can cost them money and cripple their businesses.

Go wireless.

Once you are comfortable with the PC, take it on trips with you and go wireless by adding a wireless link through the PCMCIA plug-in port. Sign up with Ardis or RAM Mobile and send and receive FAX's and e-mail while traveling. You'll discover both the benefits and drawbacks of always being accessible.

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[35]Because an IBM PC compatible uses the industry standards of hardware and software used by over 90% of the market.

[36]Netcom On-Line Communications Services Inc. can be reached by calling 1-800-353-6600

20. Those Nasty, One-sided Agreements

"*We have met the enemy, and he is us.*" Pogo

How can we write, negotiate, and administer effective agreements; ones that enable manufacturers and sales organizations to enter into and sustain win-win selling relationships? What should we include in Rep, Distributor, or VAR agreements? How can we use agreements to get results and to protect ourselves? This chapter contains answers to these and other questions about business agreements with third party sales organizations.

Written agreements developed by manufacturers and imposed on Sales Reps, Distributors, or VARs are facts of business life. They are also a source of cynicism and hostility. They are signed in haste, largely ignored by both parties, and unilaterally employed by the manufacturer when the time comes to change compensation or terminate a relationship.

One-sided business agreements are not unique to manufacturers and channel organizations. Agreements between manufacturers and customers are similarly one-sided. A manufacturer's quote includes fine print with terms and conditions that fully protect the manufacturer. The customer's purchase order has fine print that ignores the quote's fine print and says in effect that the customer can do just about anything he wants. The manufacturer's order acknowledgment and shipping documents ignore the customer's fine print and contain their own fine print that says the manufacturer can do what he wants, and that the customer agrees to that when he accepts the shipment. When a dispute occurs, both parties haul out their fine print to wave at each other, but wind up settling disputes based on who-needs-whom the most.[37]

Less emphasis on legalisms and more on mutual benefit, mutual expectations, mutual commitments, and mutual plans can reduce the cost to serve and sustain mutual success. During the 1980's I learned to live comfortably with that approach to agreements in the People's Republic of China. In those days the PRC was blessed with very few lawyers and their agreements started with a standard phrase that translated roughly as: "*This agreement is entered into in the spirit of mutual benefit. If either party no longer finds the agreement beneficial, it is subject to renegotiation*." It meant that no agreement was *legally* nailed down. Yes, some people tried to renegotiate agreements to their advantage. But once our company earned credibility for its products, business ethics, and firm positions, and walked away from prospects or partners who lacked integrity, the PRC became a consistently profitable place to do business.

The contexts of any agreement include the expectations of the parties involved, their competitive alternatives, and the government. These contexts put some constraints on what can be done to adapt the agreements to the mutual best interests of everyone involved. However, those who invest the time to make their agreements and their process for negotiating them more constructive and fair, will increase commitment and sales, and reduce non-productive hassles.

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[37]Technically speaking, the last document shipped by one party and "accepted" by the other is supposed to control the terms and conditions of the transaction.

Principles of agreements

Before making significant recommendations on agreements it's probably prudent for me to make a huge disclaimer. So here goes:

> *I am not a lawyer (thank God!), or licensed to practice law. Check with legal counsel before approving the boilerplate of your agreements, or before carrying out some of my recommendations.*

Recommendation 1: Make sure legal counsel has reviewed your agreement, but don't abdicate responsibility for the content or tone of the agreement. It is as imprudent to have lawyers write agreements as it is for Human Resources to hire employees.

The following Laws of Agreements, like Newton's laws of physics, are based on years of observing cause and effect relationships.

Lee's First Law of Agreements

If one party to an agreement intends to screw the other party, there is no way to write the agreement to protect the intended screwee.

Lee's Second Law of Agreements

If an agreement is written on the basis that one or both parties lack integrity, then one or both parties will live up to that presumption.

Corollary to the First Law
The longer and more complex the agreement, the easier it is to screw or be screwed.

Corollary to the Second Law
The longer and more complex the agreement, the less likely it is that both parties have integrity.

I discovered the First and Second Laws and the corollary to the First Law early in my career as an engineering manager in an aerospace company that did contract work with NASA. Like most government agencies, NASA wrote detailed agreements and pursued stringent negotiating processes, but was readily and systematically screwed by its contractors. When NASA issued an RFQ (Request for Quote) one of the first things my company did was to study it for technical loopholes that could be used to negotiate price increases after the contract was landed. The number and magnitude of the loopholes determined how finely margins were shaved on the initial quote. The more complex the agreement, the easier it was to find loopholes, and the more justified management felt in using them.

Phil Fisher, one of the world's original Venture Capitalists, and a man of enormous personal integrity taught me the corollary to the Second Law.[38] In 1970 Phil invested a significant sum in a company I helped to found.

[38] Forbes magazine published an article about Phil Fisher in the 1980's. The article said that if Phil Fisher were Japanese, he'd have been designated a national treasure.

He once told me this: "*I prefer one-page agreements that spell out what each party will do. Longer agreements are written to protect one party from the other. If I think I need protection from the other party, I don't invest*."

Conclusions from Lee's First and Second Laws

The best protection in a business relationship is to:

a) Carefully evaluate the integrity and intent of the other party before entering into an agreement.

b) Walk away from deals with people who lack integrity.

c) Construct an agreement that is within the region of mutual benefit so that it is in the best interests of both parties to make it work.

Elements of channel agreements

These are the principal elements of agreements with Sales Representative, Distributor, OEM, or VAR channel organizations:

- Objectives of the relationship
- Responsibilities of each party
- Authority of each party
- Exclusivity
- Compensation
- Term and Termination
- Resolution of Disputes

In later sections of this chapter, we'll discuss the elements that are the most critical to each type of channel organization, and how to construct them in more competitive and constructive ways. The issues of Term and Resolution of Disputes are universal, so I'll make a few comments on them now.

Term of the Agreement

Upon advice of counsel, the term of any channel agreement should normally be for one year and renewable by mutual consent for additional one-year intervals. The idea is to define this legally as an agreement to a temporary business relationship and not a long-term contract. Most manufacturers synchronize the term to fit with their fiscal years, by adjusting the duration of the first term. Then they modify and renew all agreements together, and couple this with the annual forecasting and quota setting rituals.

Resolution of Disputes

Serious disputes that can't be resolved between the two business parties are rare. During my sixteen years at Pro-Log, we never had a dispute with any channel organization, domestic or international, that wasn't satisfactorily resolved between the two parties. However, when a dispute degenerates to the point that it has to be adjudicated by an third party, it's in everyone's best interest to have it done quickly. For that reason I included a clause in all our agreements that required binding arbitration. Our legal counsel, one of the best law firms in Silicon Valley, recommended against binding arbitration saying that arbiters might give more to a sales organizations than it could win through the legal process. However, binding arbitration can be concluded in a few months, and civil litigation drags on for years, debilitating everyone involved no matter who is "right."

On one occasion, Pro-Log became embroiled in time-consuming civil litigation with an ex-employee. We wasted nearly eighteen months, and it cost our company and our insurer over $100,000 in legal fees to go through a discovery and deposition process and to reach the point of a trial. It took this long even though we aggressively pushed for an early trial, and we were the defendants! (The case was settled out of court the day the trial was to start. The only one who came out ahead was the plaintiff's attorney, who got paid for doing a pathetic job on behalf of his client. Among other things he had failed to take key depositions.) The greatest cost to our company was the loss of time, energy, and business focus that the legal process imposed on management.

So the key principle of resolving disputes: make every effort to resolve them amicably. If that can't be done, resolve them quickly and get on with business. Getting even, getting justice, or dragging things out is Victim behavior that doesn't contribute to business success.

Objectives of channel agreements

The primary purposes of agreements between manufacturers and their channel organizations are to:

- Quantify the significant responsibilities of both parties
- Specify limits of each party's responsibility to the other party and for its actions
- Quantify the terms and conditions of compensation
- Specify how to end the relationship in a businesslike way
- Satisfy the legal requirements for a business relationship

In addition to these purposes, the manufacturers' top management usually want the agreements to be:

- Standard for all organizations in the same sales channel
- Legal protection from the actions of the sales channel organization
- A document that will prevent conflicts between channel organizations
- A legal tool that enables at-will termination of the sales channel organization

Since manufacturers write the agreements they tend to cover all these wants, even those that are unrealistic.

On the other hand, the channel organization's CEO usually wants a business relationship with

- Income and profits
- Respect
- Dependable support for its selling efforts
- Protection from predatory practices by the manufacturer or other channel organizations
- Longevity in compensation that assures a predictable return on invested effort.

From repeated personal experience, the channel organization's CEO knows that manufacturer agreements are irrelevant to these issues, regardless of what they say. The clauses in the agreements spell out the best he can hope for, not what he can count on.

Usual signing procedure

1. Manufacturer writes a standard agreement that applies to all organizations in each channel. It has blanks for the name of a channel organization, for the starting date of the agreement, and sometimes for describing a specific territory.

2. Manufacturer's legal counsel reviews and expands this standard agreement to well over ten pages of cold and hostile verbiage that require advanced degrees in linguistics and semantics to decipher.

3. When it comes time to sign up a new channel organization, manufacturer fills in the appropriate blanks in the agreement, has an appropriate sales manager sign it (not an officer of the corporation), and sends three

copies to the channel organization's CEO. A letter accompanies the agreement. It says, "Read, sign, and return two copies. Call if you have questions."

4. CEO of channel organization signs and returns two copies without comment! (Only about one in ten raises issues no matter how one-sided the agreement is. They know from experience that unless the issues are typographical errors or gross oversights, the manufacturers response is: "*That's our standard way of doing business. All our agreements must be the same. No one else has objected to that. We'll look at it next year."* This response constitutes "negotiations.")

5. Officer of Manufacturer organization signs both copies to make the agreement legal. One copy is returned to the channel organization.

6. Both parties stick the paperwork in their files until annual renewal, major flap, or termination.

This "usual procedure" is tolerable to channel organizations simply because everyone does it. There are few competitive alternatives, so they submit to this impersonal and one-sided process.

Suggested signing procedure

What I'm about to suggest for manufacturers will add work to their agreement processes. However, it will significantly increase their credibility with channel organizations, and get their working relationship off to a roaring start. When you treat the agreement like a product and the sales organization like a key account, the shortcomings of the usual procedure and the benefits of the suggested procedure become apparent.

1. Write a ***balanced*** agreement that focuses on the ***outcomes*** sought by each party. Keep it short; keep it clear. A balanced agreement spells out comparable objectives and responsibilities for each party. Minimize discussion of the *rules* of the relationship. If your agreements are as long as 10 pages (double spaced) they're probably too long. Brevity is the soul of mutual trust.

2. Negotiate in good faith. Discuss mutual benefits and the outcomes to which both parties are committed. Then allow for a unique version of the agreement with each organization.

    a) Negotiate with an unsigned document. *A signed document already has the signatory's "face" on it and negotiation is win-lose.*

    b) Review it in person. Solicit comments without rebutting them. Discuss them in context of mutual benefit and specific outcomes. Ask for examples of effective terms and conditions that the channel organization has with other manufacturers. *Manufacturer learns what's important to the other party and gains credibility as a listener.*

    c) Tailor the agreement to each organization through balanced, mutually beneficial changes. *The idea that all Reps or all VARs have to have the same agreement and same compensation is simply wrong managerially and legally. Cookie cutter agreements are a primary reason for channel conflicts and wasted management effort. What is sound managerially and defensible legally is equal treatment (including compensation) for equal responsibilities, efforts, and results.*

3. Develop a written outline of a 90-day startup program while negotiating the agreement.

4. Use the Agreement constructively in planning meetings with the channel organization and with Regional Sales Manager to focus on outcomes.

5. Negotiate updates to agreements at least 90 days in advance of renewing them.

Sales Representative agreements

The controversial issues in a Sales Representative agreement are:

- Compensation: Commissions, Other
- Exclusivity, House Accounts, Distributors, and VARs
- Termination

The three issues are interrelated as you will discover in the following discussion. Manufacturers and Sales Representatives have to resolve all three areas in order to work together effectively.

Compensation Suggestions

The Sales Representatives' questions about financial compensation are fundamental and practical:

- For what are we paid?
- How much are we paid? Is it enough?
- When are we paid?
- How confident are we that we'll be paid?

The manufacturers' question is:

- Will the Sales Representatives do what I need done and earn the money I pay him?[39]

Win-win compensation has to answer all these questions. The following are my suggestions on ways to do it.

Tie base commissions to specific standard services.

Review Figure 5.6 on page 57. Identify the specific services the Rep organization will supply and how much each one is worth.

- State quantitatively how much commission is paid for each service.
- Split the commissions when services are provided by different organizations. For example, a large customer's organization with engineering and manufacturing facilities located in different states might decide to buy a product in the territory of one Sales Representative, order it, and pay for it in another territory, and have it shipped and used in yet other territories. The commission split should be appropriate to each sales channel organization's contribution to success.

If a specific organization is not qualified to perform all the standard service, and you still want to hire it, pay a lesser commission until it qualifies. Set objective standards and a formal process for qualification.

Make base commissions large enough to generate reasonable profits for competent channel organizations.

Estimate the costs for a competent channel organization to provide the selling services to a typical buyer for a typical order. Assume for purposes of the calculation that the channel organization and the buyer

[39]Some manufacturers have a less honorable and less productive question: How can I avoid paying any more commissions than I have to?

already have a working relationship. Develop a base commission rate that is profitable to the channel organization.

Pay a bonus commission for the first $X of sales to a new account.
(For example a 5% bonus on the first $20,000 in sales). It costs more for a direct organization or a Sales Representative to land a new account (establish credibility, supply information) than it does to get additional orders from existing customers. The bonus pays for new account development and it compensates the Sales Representative for making its customer base available to the manufacturer.

- The total bonus should amount to the average cost for a competent sales professional to book the first order from a typical account.
- Establish the bonus percentage and total dollar amount so that it is normally paid out within 12 months of the initial order. For example: if the appropriate bonus is $1000, and the typical new account would order $20,000 in products during the first twelve months, then the bonus commission might be 5% of the first $20,000 in orders from a new account.

Even though two commission structures might pay the same dollars, a bonus on top of a base commission is a stronger motivator than a base commission which starts out high and declines as a customer's order size or total orders increases. I've tried both approaches and it is no contest: the dollars can be the same, but the psychology is different. The bonus stimulates enthusiasm, the sliding scale breeds complaints. This is an example of my comments in Chapter 3 that how we pay people is also important, not just how much we pay them.

Pay half of a commission within 10 working days of shipment, and the other half within 10 days of receipt of the customer's payment.
We always followed this policy at Pro-Log. It stimulated the field sales people to make more sales calls for us because they usually received half their commission within four weeks of making their first sales calls.[40]

We withheld the second half of our commission to keep the Sales Representative motivated about prompt payment by the customer. Whenever a customer took more than 60 days to pay, the first half of the commission was deducted from the next commission check and held back until the customer paid.

Make your commission payments as sacred as your payroll.
Timely, dependable payments generate greater incentives per dollar than payments made months later. Resist the temptation to lean on your Reps to improve cash flow. There are plenty of other idiots doing this, so if you earn a reputation for dependable payments, your dollars will earn more commitment.

When in doubt, pay commissions first and settle disputes later.
Once commission payments are used as a management weapon, you might as well look for another channel organization.

[40]Our leading product was a PROM Programmer which a prospect frequently ordered on the first sales call and which was shipped within a week. The first half of the commissions were paid to the Rep organizations within 10 days of shipment. However, the Rep organizations took a while to pay commissions to their sales professional.

Pay for non-standard services outside the basic commission structure after those services are performed.

Don't complain about paying commissions on bluebird orders.
Management complaints about un-earned commissions are completely counter-productive and reflect poorly on the complainer's understanding of sales and marketing systems. Either eliminate your exclusivity clause, which is what I recommend, or cheerfully accept that you're paying for exclusivity.

Exclusivity Suggestions

The traditional Sales Representative agreement stipulates that:

- The Sales Representative shall not represent any Direct competitors of the Manufacturer.
- The Manufacturer shall pay the Sales Representative the basic commission on any and all sales booked in the territory (with the possible exception of house accounts).

It is argued that the two exclusivity stipulations balance each other. However, neither party is entirely happy with the arrangement.

I'm convinced that both forms of exclusivity produce sub-optimal results and wasted efforts.

Sales Representatives would prefer to represent a range of "complementary" products that still allow them to satisfy the customer's needs when one of their manufacturer's product lines is not an adequate fit. Distributors have this option and aggressively use it to keep their customers. Manufacturers are justifiably inclined to view "complementary" products as "competitive" products, that undermine the Rep's resolve to sell actively on their behalf. Therefore, manufacturers usually reserve the right to define unilaterally which products are *competitive* and to demand that they be excluded from the Rep's line card. When a serious dispute about competitive products arises, a manufacturer is reduced to either terminating the Rep or to grudgingly accepting the "competitor." The actual choice usually depends on the overall performance of the channel organization and the impact of the decision on the other channel organizations. It is never a win-win choice.

A manufacturer dislikes paying commissions to sales agents for orders they didn't work on. Strangely enough, this issue becomes most sensitive in dealings with Sales Representatives even though it also applies to commissions for direct people and to discounts for distributor organizations. Sales Representatives dislike selective payments because manufacturers have used them to arbitrarily withhold commissions and force the Reps into endless negotiations and game-playing to establish their claims.

The heart of the problem is that manufacturers and Sales Representatives are trying to micro-manage each other. It's far more effective to plan and to manage results: judge the relationship by results and cheerfully pay for results. To follow this approach, manufacturers have to let the Sales Representatives decide what other lines to represent. In return, Sales Representatives should agree to be paid only for the results they produce. However, Sales Representative should receive significantly higher base commissions on each order they produce, roughly 10% to 20% higher than for territorial exclusivity, as part of the bargain. When either party finds the no-exclusivity, pay-only-for-results situation getting out of hand, it should first attempt to come to a mutual agreement with the other party. If that doesn't work, terminate the relationship.

Termination Suggestions

Some of the greatest misunderstandings between Manufacturers and Sales Representatives are about termination. Manufacturers are concerned with effective selling, and Sales Representatives are concerned about being paid fairly for business they produce. An agreement's termination clauses help set the tone for how much effort, and what kind of effort, the Rep organization or its individual sales people will make on behalf of the manufacturer.

Manufacturers want short termination periods. They know that when Sales Representatives stop selling their products, they have to make immediate changes. Even a 30- to 90-day termination period is too long, and can cost market share. Sometimes though, manufacturers want to terminate Sales Representatives for other reasons, including harebrained schemes to save commission costs by going direct, or because a new sales manager or sales executive wants to prove his (or her) masculinity.
Sales Representatives say that they would prefer termination periods of a year or longer. Many of them ask to be able to earn longer termination periods as incentive compensation for beating sales quotas year after year. However, what they are actually looking for is economic longevity and equitable compensation, not the continuing right or obligation to sell a manufacturer's products. They want an appropriate financial return for customers they developed who continue to buy for years after a termination. (See Fig. 5.5 for representative times between when customers book and when they pay.) It's actually fiscally imprudent for Sales Representatives to spend time and money developing major accounts, when a short termination period means that they have an uncertain chance of receiving the bulk of their commissions.

I recommend two things be done, which jointly are in the best interests of both parties.

1. Agree to a no-fault termination with 30 days' notice.

Either party should be able to walk away from the relationship with 30 days' notice. When either party really wants to end a selling relationship, it is already over. Why play "for cause" games that waste everyone's time and money, and can only add to the wealth of a few lawyers? Furthermore, I've yet to meet a Rep who said that he was ever terminated for cause. Reps, like all of us, must save face, in their own minds, for their customers and for other manufacturers. Most of them say that they decided to terminate the relationship with a particular manufacturer. Who knows, maybe they did it by not selling. When a manufacturer tries to prove cause, the Reps are cornered into defending their reputations any way they can. *For cause* is a lose-lose approach to termination.

2. Agree to pay a percentage of the Rep's commissions beyond termination for a period of twelve months or more.

Setup a termination payment schedule that:

- Compensates the Rep for having increased business in the territory
- Compensates the Rep for "longevity" earned by appropriate performance in past years
- Removes incentives for the Rep to stall the termination just to milk commissions
- Removes incentives for the Rep to torpedo your sales in the territory and to redirect them to a competitor. Remember, most of the customers buy other products from the Rep. The Rep will work to preserve its relationships with them and is capable of switching many of them to competitors.

Examples of what might be done:

a) Continue to pay 80% of base commissions for a period of 6 to 24 months after termination (based on longevity and performance) on a portion of the quarterly sales in the territory. The portion is defined as the net increase in quarterly sales from the quarter prior to the Reps hiring until the quarter prior to the date of termination. This kind of formula makes it unprofitable for a Rep to stall termination and allow sales to deteriorate.

b) Establish a key-account payout schedule based on the Rep's role in closing them and the nature of the accounts' actual and potential orders. Payout terminates on all key-accounts if and when the Rep causes the manufacturer to lose any one of them by replacing manufacturer at that account with a competitive product.

The following true story is a particularly egregious example of what Sales Representatives go through during terminations, and how poorly negotiated terminations hurt manufacturers as well. A manufacturer's CEO terminated a Sales Representative organization as part of his latest and greatest plan to cover the territory with a "captive" sales agent. Their written agreement said that commissions were only to be paid for orders on the books or received within 30 days of termination and shipped within six months of termination.

This Sales Representative had worked for more than two years on a major OEM order from a division of Dupont. The prototype order had already shipped. Dupont's project was on schedule, and the manufacturer was locked into the business. The production order was due in six months, and shipments, worth millions to the manufacturer, would be scheduled over several years. Dupont had been one of the Rep's most profitable customers for years, and the Rep had gotten this business for the manufacturer.

During the termination process, the Rep owner personally requested special consideration on commissions for just this one account. The manufacturer's CEO refused to discuss it. The customer's user-buyer wrote a letter to the CEO on behalf of the Representative; the CEO refused to reconsider. The Sales Representative then signed on with the manufacturer's principal competitor and got Dupont to switch its business to that competitor. The manufacturer lost an account that would have ranked in its top 20 nationwide for the next three to four years and its primary competitor got the business because the CEO was unrealistic (euphemism for *pigheaded*) about termination payments. In addition to that, the Rep worked diligently for the competitor to convert other customers away from the manufacturer. Part of the motivation was revenge. On top of that, the "captive" sales agent didn't work out and was eventually terminated.

Distributor and VAR agreements

The most important issues to the Distributors or VARs are:

- Compensation: discounts, other
- Price changes, price protection
- Returns
- Inventory: minimum, obsolete

Compensation

Distributors and VARs are compensated with discounts from list price. The question is, how much discount should a manufacturer give? The answer isn't simple. Distributor discounts are typically somewhere between 30% to 50% of manufacturer's suggested list price. If a manufacturer has discounts that are less than the customary ones for its product category, it has to have a good story. Distributors assume that the manufacturer has established the product's list price value in the market. They typically expect to mark up products they sell by an average of over 20% of what they pay for them. They also expect to sell products at an average price that is significantly lower than manufacturer's list price. When a manufacturer creates market "pull" for its product, it's in a position to negotiate lower discounts because distributors are willing to sell at lower markups and at prices closer to list price. When a manufacturer has to "push" the product through the distributor and expect the distributor to help develop market demand, then the distributor will dictate a higher discount in part because the manufacturer is in a lousy negotiating position.

Discounts to VARs are usually smaller than discounts to distributors. They vary with the VAR's commitments to annual orders from the manufacturer. Agreements usually state total sales dollars the VAR commits to purchase, and then sets a discount rate based on that expected volume. VARs who commit to ordering more product get lower prices. Just to be sure the VARs take their commitments seriously, the typical manufacturer includes a bill-back clause that says if the VAR doesn't buy enough product, the VAR will get an additional bill at the end of the year that appropriately increases the average price. Few manufacturers ever send such a bill, and fewer VARs ever pay it.

Connect discounts to specific services rendered.
It is important to know which services you expect the distributor or VAR to perform and how much they're worth. For some services, such as advertising, it's more effective to pay for work done rather than to cover it in the discount. In fact, the agreement might stipulate that the distributor or VAR will advertise the manufacturer's products, and the manufacturer will pay a major percent of the advertising costs.

Don't give "added" discounts to entice distributors to overstock so that you make your shipping quotas.
In the long run the manufacturer always loses from such discounts because**:**

- The orders are borrowed from the next quarter and dig a hole in it that will probably take another added discount to fill.
- Promotes shipping surges in the last weeks of each quarter which screws up manufacturing.
- Tempts distributors to wait until the end of the quarter to order.
- Discounts are used by distributors to slash prices and steal business from other channels or other channel organizations.
- Discounts end up lowering the average street price of the manufacturer's product.

Be prepared to negotiate a special discount or rebate for a major order to a specific customer.
Do this only when you know who the customer is, what the order is, and how your product will be used.

Price Protection
Distributors buy and stock products so that they can provide quick and convenient delivery to their customers. However, their inventory of products creates a financial risk for them. When a manufacturer decreases its list price, the distributor is stuck with overpriced inventory. Distributor agreements usually specify some form of price protection, such as 90-days notice for price changes or retroactive credits for price decreases. A 90-day notice can work to a distributor's benefit when a manufacturer raises prices. Distributors can stock up at the lower prices and then resell at higher margins after the price increase goes into effect.

In some cases, distributors and VARs are asked to provide their customers with fixed price quotes that are good for extended periods, perhaps as long as a year. The distributor in turn will seek a not-to-exceed price guarantee from the manufacturer to support this order.

Returns and Obsolete Inventory
In high-tech businesses, where products quickly become obsolete, inventory is deadly. Yet most manufacturers push distributors to build large inventories of their products for these dubious reasons:

- **To get the distributor committed**. The theory is that the more inventory the distributor has, the harder he'll work to sell the product. This is part of the "push" theory of marketing. Not too bright.
- **To make quarterly sales quotas**. GAAS allows companies to treat shipments to distributors as real sales. Sales management aggravates this by paying commissions on sales to distributors rather than on sales by distributors to their customers.

Manufacturers should realize that they haven't really sold their products until customers have paid for them. Most distributors require manufacturers to exchange obsolete products for current ones. Manufacturers "protect" themselves by limiting the amount of product that a distributor can exchange in a specific period of time.

Manufacturers have three alternatives: minimize distributors' inventories, notify distributors well in advance of upcoming product revisions, or be prepared to eat lots of returns with a smile.

21. Managing Channel Conflicts

Channel conflicts are customarily described as competitive disputes between channel organizations over customers. These disputes boil down to: "Whose customer is it and who gets the profits and/or commissions from this order?" They can produce squabbling that undermines profits or loses customers.

Some manufacturers attempt to eliminate channel conflicts altogether by tightly controlling which channel organization or which individual handles each customer. Their channel agreements specify which customers a particular organization can sell to based on customer characteristics such as location, industry, application, or the dollar level of business. Manufacturers may assign the largest accounts to their direct channels, and divide the smaller accounts by territory or industry among the other channels. Channel organizations in turn attempt to eliminate conflicts among their sales professionals by assigning them "exclusive" rights to specific customers.

Attempts to eliminate channel conflicts through exclusive rights are often counterproductive. They reflect a lack of understanding and respect for customers and channel organizations, and for the intrinsic and useful nature of some conflicts in an effective marketing system. Even the customary description of the conflicts as "channel conflicts" is misleading. The conflicts occur between individuals in the marketing system because of overlapping or competing interests in the same customers.

Myth:
- *All channel conflicts are unhealthy.*
- *Manufacturers are always responsible for them.*

Reality:
- *The majority of channel conflicts are unhealthy and preventable.*
- *Some channel conflicts are healthy. A marketing system without channel conflicts is probably losing a significant part of its market.*
- *Channel organizations and customers also cause channel conflicts.*
- *Channel organizations share the responsibility for managing conflicts*.

In this chapter we'll describe some typical conflicts, the reasons for them, and steps that manufacturers and channel organizations can take to manage them within sustainable win-win business relationships.

Examples of conflicts

Among sales professionals within a channel organization
Example 1: A telemarketing agent for a software manufacturer, who works on a commission basis, responds to leads generated by company mailers. She works with a specific prospect over several weeks answering questions, sending literature, and supplying a demonstration copy of the software. That prospect eventually orders 10 copies of software for $1500 and the telemarketing agent receives her commission. A field sales agent, for the territory in which the account is located, learns about the order, visits the account, and shmooze the decision makers. He discovers that they are about to place an order for an additional 250 copies of the software. He writes a quotation for price and delivery, books the order, and gets the commission that the telemarketing agent would have gotten otherwise.

Example 2: Thirty-five years ago I bought my first auto insurance policy in Pasadena California from an agent of Allstate. He just happened to be the agent on duty when I walked in the door. It turns out that Allstate had a rule that made me the "property" of that agent. I didn't know the rule existed for the first ten years because I lived within 20 miles of Pasadena and simply renewed the policy by mail each year. I learned about the rule when I moved to Northern California and tried to change agents. I was informed in writing that I couldn't do so. I was irritated, but continued with Allstate anyway. From time to time I had to call "my" agent long distance with questions and policy changes. Over the next decade the agent's attitude deteriorated and his helpfulness declined. In fact, he became churlish and critical. I suspect that he had developed physical ailments or mental problems. After one call I was so angry at his critical and inappropriate remarks, I was prepared to change to another company at the next annual renewal. Shortly thereafter I received a notice that "my" agent had retired and I was free to chose a new one. I selected the next Allstate agent very carefully.

Allstate created a rule that rewarded the agent who acquired my business. However, the rule was customer-hostile, and must have lost customers for Allstate over the years. It left me with an unpleasant choice: continue with an unsatisfactory agent or buy my insurance from another company. I still feel hostile towards Allstate for treating me like a piece of property, even though I'm happy with how they've handled policy claims.

Many Real Estate agencies and car dealerships have similar rules for "walk-in" clients. A walk-in client becomes the property of the agent on duty. Unfortunately, if the client isn't happy with that agent, her only competitive alternative is to take her business to a competitor.

Distributors vs Reps or Direct
Example 1: A Rep (or direct) sales agent has made several calls on a prospect for a $3800 projection display system. The prospect finally asks for a quote of price and delivery, and the Rep quotes factory list price of $3800 and two weeks delivery. Both price and delivery are dictated by the manufacturer. Meanwhile, the prospect receives a second quote, from one of the manufacturer's authorized distributors, of $3100 and immediate delivery on the same system. The distributor gets the order, and the Rep loses both his commission and his credibility with the customer.

Example 2: A customer with a rapidly growing business has bought its power transistors from a specific Distributor for several years. The customer will need 200,000 units of a particular power transistor over the next twelve months. The Distributor, who buys these transistors from the manufacturer at a distributor price of $2.75 each, quotes the customer $3.25 each for an annual buy of 200,000 units. The manufacturer's direct sales organization quotes the customer $2.50 each. The customer places the order with the manufacturer.

Direct vs. Sales Reps: House accounts
Example: A Manufacturer of power transistors stipulates in its Rep agreements that it can re-assign accounts that do over $100,000 per year to its Direct sales organization. These accounts become House accounts. Rep Commissions for House accounts will only be paid for orders on the books within 60 days of the time the account becomes a House account.

Distributors vs. VARs
Example 1: A VAR designs and proposes to assemble and install a sales-office automation system for a customer. The system includes IBM compatible personal computers and HP printers, which constitute roughly half the cost of the system. The VAR's proposal shows these products at the manufacturer's unit list prices. The customer asks the VAR to supply the system without the printers and the personal computers because he can buy those components from a Distributor at 20% less and install them himself.

Example 2: A VAR designs a sales-office automation system as in *Example 1*. The customer accepts the first system as proposed, has it installed, and learns how to use and maintain it. The customer decides to put the system in 50 branch offices and realizes that if she buys and installs the personal computers and printers separately, she can save 30% of their costs. She asks the VAR to quote 50 systems without these components.

Distributor vs Distributor: The Gray Market
Example: An authorized Distributor of a manufacturer's telephone headsets pays the manufacturer $55 each for a specific model of telephone headset and usually resells it at $75 each. A major credit card organization requests a quote on 10,000 headsets for its new telemarketing center. The Distributor sharpens his pencil and quotes $60 each. A second, gray market distributor quotes $53 each and wins the order. The second distributor negotiated a special 'deal' with a major OEM customer of the manufacturer, who paid $45 each, and bought 10,000 more headsets than it needed.

Origins of conflicts

Channel conflicts are caused by manufacturers, channel organizations, and/or customers. Some causes are non-productive and should be eliminated. Other causes are tied to legitimate interests and useful benefits; these are productive conflicts when they are properly managed.

Manufacturers
Manufacturers cause channel conflicts through:

1. Poorly conceived pricing
- Steep, volume based, discount curves that encourage arbitrage among channel organizations
- Inconsistent pricing: a) between channel organizations, b) between channel organizations and major customers, and c) from one order to the next
- Pricing that favors one channel at the expense of others

2. Poorly conceived compensation policies
- Compensating reseller organizations entirely with discounts
- Paying commissions to Direct people or to Manufacturers Reps for sales into reseller inventories
- Inadequate compensation for acquiring customers; too much for maintaining them

3. Improper design and staffing of the marketing system
- Too many channels
- Too many channel organizations
- Organizations with too little integrity
- Sales management structure with intrinsic conflicts of interest

4. Bloating the inventories of channel organizations
A product isn't really ***sold*** until it's working successfully in the end-user's application. Until then, it is in someone's inventory and hasn't made a real, dependable profit for anyone. It can come back to haunt the manufacturer's marketing system as a stock return, as excess or obsolete inventory, or as a gray market product that undermines user pricing and marketing system enthusiasm.

5. Hostile policies and procedures for returns
Manufacturer's return policies can be so onerous that they drive OEMs and other resellers to unload their products on the gray market. The gray market drives the street price lower and steals business from authorized channel organizations.

6. Ignorance
The interrelationships within a marketing system and between the marketing system and the manufacturer are very complex. It is easy solve specific problems in ways that unintentionally create channel conflicts. For example, management may attempt to simplify manufacturing planning and to compensate for manufacturing lead times by giving substantial discounts to large orders that have deliveries scheduled months in advance. However, if a customer who has placed one of these orders can't use all the product he commits to, his inventory can wind up in the gray market. A more appropriate solution, to this example, is to develop a just-in-time (JIT) manufacturing process that accommodates changes in customer requirements on a timely basis and minimizes inventory and inventory fluctuations.

7. Lack of integrity
When management acts unfairly, selfishly, or dishonestly towards customers, sales professionals, or channel organizations, people become hyper-sensitive and simple issues become bones-of- contention. Very frequently the real issue is lack of management integrity. The channel conflicts are simply culturally accepted scapegoats used to vent frustrations.

Channel Organizations and Sales Professionals

The manufacturer's policies and procedures may create conflicts, but channel organizations or sales professionals create their share because they:

1. Don't "sell" their value added services to customers
Most channel organizations that I've dealt with don't deliberately and systematically educate and sell their customers on all the unique values that they add to the transactions. They lump together technical support, service, account management and selling and expect to recoup all the costs from product markups. This makes them vulnerable to other channel organizations who don't provide the services, have lower costs, and undercut their prices. Unless the customers are educated to the services and their value, they see the price differentials, but don't appreciate the legitimate differences in value.

2. Play *I lose — you win* with customers
A channel organization decides to "buy the business" by taking a loss on the initial order and then expects to make it up on re-orders. A second channel organization, with no investment to recoup, underbids the first organization on the re-orders. The first organization thinks that either the manufacturer or the customer owes them something, but they only have themselves to blame because they gave things away.

A sales professional gives away samples, provides free technical support and drops prices to get orders at any cost. He becomes a gopher for his prospects, willing to do anything (for nothing) in hopes they'll feel indebted to him and give him orders.

3. Sell products at little or no profit
Distributors, VARs and OEMs are free to resell specific products at prices of their own choosing. They may use certain products as loss leaders to attract other, profitable business from their customers. They may also bomb a product's price to increase their sales rate and meet the sales volume requirements of their manufacturer's agreement.

4. Sell specific products at a loss to improve cash flow
Sometimes the most important benefit of selling is cash flow, not profits. A quick way to convert bloated inventories to cash is to cut prices and steal business from those channel organizations who are trying to maintain a legitimate markup.

5. Are ignorant
Some channel organization personnel are poor managers, poor businessmen, and poor sales professionals because of ignorance. They don't know how to do their jobs and they usually blame manufacturers or other sales organizations for problems their own ignorance produces.

6. Lack integrity
There are innumerable self-serving, destructive ways to make a quick buck in sales and distribution. Certain people, motivated only by money, unencumbered by any sense of ethics, and **unable to make it through law school**, vigorously pursue them.

Customers
Customers create channel conflicts because they:

1. Want competitive alternatives
They don't want to become the property of any channel organization or any particular sales professional when they buy specific products. Competitive alternatives are reassuring benchmarks for evaluating the organizations with which they are doing business. Customers are the most satisfied with their transactions when they can chose what to buy, who to buy from, and how to buy. When a manufacturer gives a customer only one alternative in all three areas, then the customer's competitive alternatives all involve not buying that manufacturer's products. A manufacturer might have the most desirable product, but if the customer is unwilling to buy anything from that manufacturer's authorized sales channel, the sale will be lost.

2. Change needs and wants from one order to the next
The first time customers buy a product, they usually require extensive sales, account management, and technical support. When they reorder that product, they need relatively little of those services, so they usually focus on price and delivery to determine from whom they buy it.

3. Change decision makers from one order to the next
The initial order may be driven by the user-buyer and later orders by a technical buyer, purchasing. People come and go from a particular buying process due to hiring, termination, or promotions. New people bring different understandings of what is best and who to deal with.

4. Are ignorant
Some customers don't know what they need, what it costs or what it's worth to them. Consequently they have no basis upon which to build confidence in their supplier and respect for what they do. A sure sign

of ignorance is when a user-buyer doesn't know what it really costs him not to buy and what it really costs him to make rather than buy.

5. Lack integrity
A few customers go beyond evaluating competitive alternatives to manipulating destructive relationships with their suppliers. They make a practice of playing one channel organization against another to win at their suppliers' expense. One way they do it is to get a quote or proposal from one channel organization and then shop it around to other organizations with a promise to buy from the lowest bidder.

How to manage conflicts

There are two ways to manage conflicts: proactively with consistent well-designed policies and reactively on a case-by-case basis. As in everything else, the old saying "an ounce of prevention is worth a pound of cure" applies to conflict management. This section has recommendations for how manufacturers and channel organizations can proactively manage most conflicts.

Pricing and Discounts

Be consistent with prices and discount curves.
Setup a pricing structure and stick with it. Avoid the end-of-quarter discounts, discounts to keep production flowing smoothly, and similar temporary deals. Consistent pricing enables channel organizations to plan ahead, confident that they know what the playing field is. When they suspect that prices or discounts will fluctuate, they waste time and energy trying to anticipate and take advantage of the changes instead of selling the product.

Have the same discounts for all channel organizations and then pay for special services (as they are performed) with credits against future purchases.
One reason discounts vary from one channel organization to the next is that manufacturers use additional discounts to compensate some channel organizations for specific services they provide. Unfortunately, the added discounts give them cost advantages when they don't provide the services. Their most profitable strategy is to use their cost advantages to steal customers (who don't need the services) from other channel organizations.

A more constructive approach is to issue monthly or quarterly credits or payments for services after they are performed. Whenever possible, the manufacturer should issue credits against future purchases of its products. This approach has three advantages over blanket discounts:

1. It gives the organization obvious incentives to provide the service, such as advertizing, technical support, or maintenance.
2. The organization uses the credits to order more products.
3. It gives the manufacturer a say in the planning and quality of the services it pays for. The manufacturer can also vary (or negotiate) the amount of these incentives (rather than product discounts) to encourage or support specific actions on the part of specific channel organizations.

For example, when a channel organization does advertizing on your behalf, compensate it with co-op advertizing credits or payments which amount to an agreed to percentage of advertizing costs. Also, find out how the channel organization budgets and manages its advertising. Then issue the payments or credits appropriately. That is, if their advertising department is a cost center with an annual budget, issue your payments to that department rather than to the purchasing department. It makes the advertising department look better. It also avoids having them treat the credit as a reduction in their cost of goods which they can use to bomb their prices.

When a channel organization trains technical people on your products, or provides warranty services, issue appropriate payments or credits for those services as they occur.

There are some caveats about using credits. They include:

Avoid tying strings to how they may use your credits. Don't put restrictions on when credits can be used or applied to orders. Make the credits the same-as-cash in payment for product orders.

Resist the temptation to micro-manage through credits. Keep the terms for earning credits consistent and straightforward. Let the channel organization manage how it does its job. When in doubt pay, pay promptly, and pay with a smile.

Don't overuse the credit concept. Stipulate in each channel organization's agreement no more than five services for which you'll pay credits. Leave the rest to the overall profitability of the relationship.

Avoid using large "step function" discounts, credits, or bonuses to motivate specific levels of sales.
Lump-sum incentives tempt distributors and OEMs to do things that stimulate unproductive conflicts. For example, if a distributor receives a large rebate (or avoids a large bill-back) by reaching a specified volume of annual business, the distributor may bomb prices and steal business from other resellers, or sell to other resellers (temporarily stealing their business from the manufacturer) in order to reach that volume of business.

Keep volume discount curves relatively flat to minimize conflicts, undesirable arbitrage, and a gray market.
Let's face it, volume-based discounts aren't justified by improvements in cost-of-goods. I wonder how many people have actually analyzed the cost basis for volume discounts. The reality is:

Unless a specific customer or channel organization accounts for more than 10% of a manufacturer's output, its volume of business has little impact on the product's cost of goods.

The costs that do vary with a customer's or a distributor's order volume are the per-unit costs of doing business with it. However, when volume discounts significantly increase channel conflicts, the per-unit costs of doing business increases.

Commissions

Pay more and pay longer for "acquiring" end-user customers.
If I were to choose the single compensation change that would have the most beneficial impact on selling it would be to pay more for "acquiring" each end-user customer and less for acquiring resellers or maintaining existing customers. As a part of that compensation change I would : a) continue to pay the sales professional or sales organization an "acquisition" commission on major accounts for as long as those accounts reordered products on specific projects, b) pay that commission regardless of which channel organization shipped and billed the orders, and c) normally pay that commission beyond termination of the individual or sales organization.

Getting business from a customer is like pumping water from a well. It takes a lot of pumping to get the first glass of water, but after that a steady, gentle pumping produces a steady flow of water. It might take a sales person a year or more of hard work to land a major account. However, under typical commission programs, he won't profit from his investment if: a) the customer orders from a distributor or reseller, b)the factory takes the account direct, or if c) the sales professional or his organization is terminated. The typical commissions thereby encourage activities that take little effort and have short-term results, and discourages long-term investments in developing major accounts.

At Pro-Log we compensated acquisition costs to some degree by paying a 5% bonus on the first $12,000 in orders from a new account. That front-loaded compensation helped to stimulate new account development.

Pay more commission for sales to user-customers and much less for sales to resellers. Commissioned sales people who manage resellers should be paid to generate "pull" from end-users. They should not be rewarded for "pushing" inventory onto resellers' shelves. In order to reward appropriately for "pull," a manufacturer has to develop a program with its resellers in which they periodically report their inventories and the number of units shipped to end-users. The end-user shipments should be identified by ship-to organization and zip code. The manufacturer needs to know where the shipments went and which ones went to end-users.[41] Many resellers will be reluctant to provide this information, especially if there's nothing in it for them. One way to promote cooperation in obtaining this vital data is to issue credits (equal to a 2-4% discount) for sales to end-users that are identified by company and zip code. Sometimes these reports contain surprises for the manufacturer. At Pro-Log these reports uncovered companies and individuals who were purchasing for resale in international markets.

Hiring policies

Certain individuals and certain channel organizations thrive on predatory practices that steal business from others. The organizations are well known in the industry, and easy to identify. The individuals can be identified by competent managers. Don't hire these organizations or these people. If one of these organizations is already a part of your distribution network, terminate it. There is nothing worthwhile a manufacturer can do to manage such an organization because its management lacks integrity. Similarly, there is no way to successfully manage a sales professional who lacks integrity.

Customer selection policies

It's as important to select customers as it is to select sales professionals and channel organizations. Customers who are incompetent or dishonest should be screened out. They are intrinsically unprofitable, and one way they undermine profits is by creating channel conflicts.

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[41] Inventory reports are not very useful by themselves and sales information by zip code can be misleading because many resellers buy from and sell to other resellers.

Education and Training

Customers

If a customer has access to more than one of a manufacturer's authorized channel organizations, the manufacturer can provide a neutral source of information on the benefits provided by each organization, encourage the customer to choose one, then support that organization's success with the customer. This doesn't guarantee that the customer won't switch later on, but it does increase commitment and improve customer satisfaction.

Novell, a leading supplier of Local Area Networks, does something along this line. It categorizes its VARs on the basis of proven (by periodic training, testing, and customer evaluations) technical competence as Gold or Platinum (the highest level) resellers. It clearly defines the meaning and value of these labels to its customers and prospects, it reserves some products and services to Platinum Resellers, and it gives them more and better leads.

Channel personnel

Managers in channel organizations can develop organizational marketing plans that educate prospects and customers about the costs and value-added benefits of their organization. This marketing process must begin with the first contact with a prospect and continue with each contact, mailing, quotation, or proposal. Then they have to continually educate and encourage their field sales and inside sales professionals to sell these costs and benefits to their customers.

They should also hone their quotes and proposals to make it clear what the customer gets by dealing with them. If some of their services are included in the product's price, then itemize them, specify their value in dollars and then show them as "Included at No Charge." This process is valuable in two ways: it helps sell the customer on the value of the channel organization's services, and it helps sell the channel's people on the value of the services. I've found that good sales professionals can usually sell at a higher price if they personally believe it's justified and if they can present a rational case for it.

Bob Dietz, CEO of M&D Controls Company, and founder of the Association of High Technology Distributors, implemented an extremely successful organizational marketing program for his company. He developed a Menu of Services (Reprinted with Bob's permission in Appendix A) which is supplied to each prospect and customer. It defines what his organization does and specifies the unbundled rates for the technical services it supplies, including engineering services, on-site services, non-warranty repair services, configuration services, and training services. This document establishes a reference point, early in the relationship, for services that may be quoted or included at no charge in a proposal. He typically bids some of the services at no charge, but spells them out, and their unbundled costs. That reminds the customer of what he's getting besides the product and keeps the door open for Bob's company to re-quote if another supplier should quote a major buy-out item at a lower price. This approach makes it easier for the customer to pay M&D Controls more than he'd pay the distributor. If the customer decides to buy a major item from another party, M&D Controls still makes the services available, at the quoted rates.

When Bob first introduced the concept of charging customers for technical services, his sales force resisted. They were convinced that it would cost them business not to give these things away. Now it is their accepted and successful way of doing business, has made selling easier, and has reduced the amount of business lost to low-ball prices from other sources.

22. Seven Ways a CEO Can Increase Sales

"*A desk is a dangerous place from which to view the world.*" John le Carre
"*I don't care how much you know until I know how much you care.*" A Zen Master

In the long run, the knowledge, beliefs and actions of the CEO decide his/her company's sales and profits. This chapter describes seven specific actions a CEO can take to increase sales, add profits, energize the sales organization, and improve the business plan.

1. Visit customers and channel organizations

During my first five years as CEO of Pro-Log, I also ran Sales and Marketing. I set up, hired, and managed the field sales organization, made account calls, negotiated agreements, and trained customers. I personally knew our key accounts and the owners and sales agents of our Rep organizations. I signed commission checks and included congratulatory notes with the biggest ones. Sales and profits grew substantially every year. Then I withdrew from the field to concentrate on managing the company and hired the first in a series of sales executives.

Over the following years, I continued to discuss our customers and the field sales organizations in executive planning meetings. However, they became impersonal abstractions to me and were hypothetical caricatures to the other executives who had never worked with a customer or a salesperson in his native habitat. I made increasingly poor product and market decisions based on third-hand information filtered up through the line organization, and on my fading memories of how customers and Reps used to be. It took five years of this management isolation to slow the company's growth and reduce its profitability. It took another two years before growth halted, and ten consecutive years of profits ended with a year of losses.

Belatedly, I put myself on a program like the one we'll discuss next. My first trips to the field after years as a desk jockey were a revelation: our customers had changed their expectations, skills, wants and needs; our products and marketing systems had fallen behind. It was suddenly clear to me why our results no longer matched our plans. I began to make changes that eventually salvaged the business.

Business Objective

To have a CEO systematically interact with accounts and sales organizations in a way that produces:

a) accurate, up-to-date, in-depth, visceral, working knowledge of key accounts,
b) a realistic context for business planning
c) reasons for mutual success,
d) needs for continued success,
e) an understanding of what a successful sales call requires in time and planning
f) improvements in executives' comfort with customers,

so that the executive's support of the customer and the field sales organization will be more effective and sustain success as measured by improvements in sales, profits, and performance to the business plan.

Typical Program

The CEO invests approximately eight days per quarter (including travel time) to systematically visit three to five key customers and three to five field sales organizations. The eight days includes the time to prepare for, analyze, document, and follow-up these visits. He will revisit these customers and sales organizations every six months.

Criteria for key customers

- Sales or technical leaders in their markets
- Different markets for each customer
- Already among the top 100 customers, or expected to be within two years
- Supported by a sales professional who ranks in your top quartile

Criteria for key sales organizations and sales professionals

- At least one from each channel
- Sales or technical leaders in their channel (use judgment, not just sales' $)
- Successfully selling your company's products

Suggestions on how to plan and conduct effective visits

The following suggestions hit the highlights and give an idea of the planning and preparation effective visits require.[42]

Steps:

1. Define the objectives of your visits and communicate them clearly to the sales personnel involved in helping you. *The people in your sales organization can easily misunderstand your objectives and your motives. You're learning about customers so that you can do your job better, not to do their jobs or to second-guess how well they are doing them.*

2. Select accounts and organizations with the assistance and approval of sales management, but don't abdicate the selection process.

3. Research accounts and sales organizations before initial contacts with them.

4. Plan and schedule visits at least four weeks in advance. Reconfirm one week in advance and have backups available. *Although the sales organization can help set up the initial visit, you should personally confirm it, communicate your objectives, and establish agendas. Your visits should include meeting their top executives, and you may be the only one who can arrange meetings at that level.*

5. Develop key questions and a rough agenda prior to a visits.

6. Make initial visits to accounts or channel organizations with the sales professionals that manage them. Before the visits, ask these sales professionals to brief you. Be the leader of your team during the visits. Some sales professionals take charge to demonstrate to you that they have account control.

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[42] *Conceptual Selling*, pp 63- 156, provides a splendid tutorial on how to conduct effective meetings with customers.

Unfortunately that will reduce how much you learn. Ask questions and take notes. If you are asked for a commitment, avoid the CEO syndrome of making it on the spot[43]. Promise to respond with your decision by a specific date, usually within a few days of your return to work. Check with your sales organization before responding. Length of visit: two to four hours including a tour of the customer's facility. Respect customer's or sales organization's time and follow-up with questions by phone rather than stretching meeting beyond agreed limits. Summarize agreed-to action items and timing for completion at end of meeting. Thank them for the information and hospitality. Cite something that has been particularly interesting or useful to you during your visit.

7. Complete action items on schedule. Send thanks to key individuals at customer and in sales organizations within two days of return to office.

Management issues when CEOs or other executives visit customers or channel organizations

- Not enough time to follow through on visits or insufficient preparation and follow-up because executive doesn't respect the importance of the visit.

- Executive isn't comfortable in a selling situation. Preparation, a little training, and the first few calls will usually take care of this.

- Sales might plan visits only to solve tactical problems or to help close orders.

- Sales tends to suggest model accounts that are under perfect control by the sales organization.

- Resistance from sales organization because:
    a) Fear of the unknown. Executive is not under control, could screw up account with his comments or responses, may lack street-smarts.
    b) Executive might be critical (out of context) of how account is handled.
    c) Executive might use contacts with account or channel organization to go around sales organization and undermine it or to second guess sales management.
    d) Customer or salesman might use opportunity to get special privileges. Top executives are relatively easy to talk into making exceptions to their company's policies.

[43] I made that mistake once, it cost Pro-Log $50,000, it cost me the trust and confidence of a Regional Sales Manager, and it taught me a valuable lesson. When I visited a customer in Detroit (without our account manager), the purchasing agent and a project engineer told me that we had recently shipped them $50,000 in products that they hadn't ordered and asked me to sign an authorization for its return. I hadn't heard of any problems with this account, but I signed without checking. Turns out they lied, for internal political reasons. It had nothing to do with the quality or performance of our products.

For those who would like more encouragement and more ideas on making field calls, I heartily recommend the article by Harvey B. MacKay, "*The CEO Hits the Road (and Other Sales Tales).*"[44] He is the CEO of Mackay Envelope Corporation, Minneapolis and writes from personal experience.

2. Require other corporate executives to visit the field

After my first round of field visits, I encouraged our other executives to adopt the program. There was substantial resistance to that idea! Most of them had more excuses for not doing it than you could shake a stick at: they didn't need to do it, there wasn't time, they already were meeting customers and sales people who came to visit us, they would do it as soon as 'some other' project was completed, etc. On the whole, participation was reluctant, spotty, and poorly executed. In hindsight I should have made the program mandatory and supplemented it with education and support to prepare them for field trips.

Art Pasquinelli, our CFO, was the only person to wholeheartedly embrace the program. He was thorough in his preparation, professional in his calls, and dependable in his follow-up actions with customers. As a direct result of his field visits he decided to make the Finance department an asset to the selling process. He created and implemented new, more flexible credit terms for customers and distributors. He also *adopted* one of his key customers and became its champion. He worked with its CEO and top management, learned about its business and its markets, and facilitated our support of its requirements.

3. Actively and formally listen to sales professionals

Listening to sales professionals is nearly as important as listening to (other) key customers. A CEO can use it for sanity checks and updates on his beliefs about his marketing system. He'll also hear some dynamite ideas and suggestions about customers, product, and policies. This good stuff will be mixed in with complaints and lesser ideas. He'll find that his respect for sales professionals increases. The morale and commitment of the sales professionals will improve because they are pleasantly surprised to find a CEO who listens instead of telling them what to do.

Most CEOs listen to some sales professionals from time to time. What I'm advocating is a pro-active and formal program of listening, similar to the program of account visits. Pro-active means that the CEO plans the occasions, employs active listening, and follows up each discussion with appropriate actions.

Plans the occasions: There are three opportune times to sit down with sales professionals either individually or in a group:

a) when top performers visit the plant (See Chapter 17, suggestion 3)
b) during National or Regional sales conferences (See Chapter 17, suggestion 5)
c) during field visits to customers and channel organizations.

[44] Harvard Business Review, March-April 1990 pp 32-42.

Uses active listening: Active listening is a method of listening to other people which helps them to explain their issues fully, leaves them with the feeling that they've been heard, and encourages them to solve their own problems. The material in *Conceptual Selling* on how to conduct an account call, involves some of the techniques of active listening. However, the best material I've found on the subject is described in *Sales Effectiveness Training*, pages 69 – 89.[45] The authors conduct formal training programs on active listening and other aspects of sales effectiveness. I wholeheartedly endorse their program for all executives and sales professionals.[46]

Follows up with appropriate actions: Sometimes an issue will be raised that the CEO needs to respond to in some way. The appropriate method of handling this is to commit to a time by which the response will be forthcoming, then do what it takes to meet or beat the deadline. What is always appropriate is a simple thank-you letter penned and mailed within a day or so of the meeting.

4. Convey personal thanks to top performers

Personally sign the largest commission checks and any other checks that reflect commendable results. Include brief, hand written congratulatory notes, or call to say thanks.

These contacts can be particularly productive for Sales Representative organizations. One paranoia that Rep owners share is that once they develop a territory beyond a specific sales level, the manufacturer will take it direct. Many CEO's (and CFO's) see Reps as an expense and are ambivalent or hostile about paying them large commissions. When a CEO shows genuine respect for large commissions, he reduces the paranoia and increases a Rep owner's commitment to developing his territory. Besides, it is a fun and appropriate way to say thank you and to break down barriers.

5. Review channel agreements and how they are administered

Chapter 20 describes useful principles for channel agreements that boil down to: Keep them simple and keep them fair. The difficulty is that this appears to be a risky approach, one that must be personally supported by the CEO to endure. The tendency of subordinates, from Vice Presidents on down, is to rewrite and administer agreements with creeping protectionism and ever increasing control over the channel organizations.

6. Replace win-lose forecasting with proactive planning

The annual sales forecast is a planning crutch in the vast majority of companies. As described in Chapter 18, it is a defective one. It's up to the CEO to replace it with effective tools.

7. Sponsor an ongoing sales-training program

An effective marketing system is produced by teams of skilled managers, skilled sales professionals, and skilled support people. Skilled people require systematic and continual training to remain at their best. If world class athletes or musicians stop training for even a few days, their results suffer. The responsibility for

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[45] Carl D. Zaiss and Thomas Gordon, Ph.D., *Sales Effectiveness Training*, Penguin Books, 1993

[46] Contact: Effectiveness Training Incorporated, 531 Solana Beach, CA 92075, (800)628-1197.

remaining skilled and fit belongs to each individual, but it is up to the company to supply supporting methods, time, and resources. A winning football organization, like the San Francisco 49ers, expects its athletes to have their own personal training programs and to stay fit in the off-season. Then the organization supports the individual efforts with training camp, pre-season games, and daily training regimes (physical and mental) throughout the season. Football is just another competitive business!

The traditional objectives and incentives in sales organizations pressure the managers and sales professionals to abandon training in favor of making more account calls. Training is like investing in capital equipment, there is an up front cost and a long term payoff. It takes a CEO's sponsorship and continual pressure to establish and maintain effective sales training programs.

A story about two woodcutters metaphorically illustrates the value of training. Two woodcutters continually argued as to who could cut the most wood. One was much stronger than the other, but not as bright. One day they decided to settle the issue by seeing who could saw the most wood in one day. They met early one morning at the village green, where two enormous piles of wood were stacked. The whole village turned out. When the church bell rang, the contest began. The stronger woodcutter attacked his pile of wood and furiously sawed all day long. The brighter woodcutter also sawed diligently, but he stopped from time to time to sharpen his saw, and he won easily.

Appendix A

Recommended Reading

Sales and Marketing

E. Raymond Corey, Frank V. Cespedes, V. Kasturi Rangan, ***Going to Market,*** Harvard Business School Press, 1989. An excellent book that studies distribution systems for industrial products. This book isn't currently on book shelves. It can be ordered from McGraw-Hill by calling 1-800-722-4726.

Theodore Levitt, ***The Marketing Imagination***, The Free Press, 1986. A practical book on how to develop a competitive advantage for any product in a global market. One thesis of this book, amply demonstrated by example and analysis, is that there is no such thing as a commodity. That is, no company has to compete strictly on price. Executives who think they are selling commodities simply lack an understanding of how to differentiate their products.

Robert B. Miller, Stephen E. Heiman, ***Strategic Selling,*** Warner Books, 1986, and ***Conceptual Selling***, Warner Books, 1987. Two of the finest and most professional books on high-tech selling I've ever read. I've used them in practice. I recommend them unconditionally to every CEO, sales executive, and sales professional. They are important books on the win-win strategies and tactics of selling products and services to major accounts. They cover everything from how to conduct account calls to how to develop account strategies. Hewlett-Packard and Coca Cola are just two of many companies who have incorporated the teachings of these books in their sales programs. John Young, then CEO of Hewlett Packard, wrote an enthusiastic endorsement in the Forward of Strategic Selling.

Carl D. Zaiss, Thomas Gordon, ***Sales Effectiveness Training,*** Penguin Books, 1993. Specific, critical, active listening skills for field sales professional and sales managers. Step by step method for resolving conflicts so that no one loses. Starts with active listening, a method for fully and frankly uncovering the conflict issues in a way that enables them to be resolved to the mutual satisfaction of all parties. A companion audio tape of the same title is available in most bookstores and is well worth repeated listenings. Thomas Gordon wrote the bestseller ***Parent Effectiveness Training***. I read that book, took a training course in active listening, and found that it was very helpful both at home and at work.

Rowland T. Moriarty and Ursula Moran, ***Managing Hybrid Marketing Systems***, Harvard Business Review, November-December 1990, pp 146-155. Discussion and case studies of marketing systems with several channels. Has some interesting and potentially useful graphics to illustrate functions of various channels during the selling cycle. I don't agree with much of their analysis about conflicts, but the article is still worthwhile.

General

Analee Saxenian, ***Regional Advantage***, Harvard University Press, 1994. A comparative study of culture and competition in Silicon Valley and Route 128. This study shows in hard numbers the competitive advantages of interdependent networks of businesses (Silicon Valley) over vertically integrated businesses (Route 128). The relevance to the marketing system is to confirm with hard numbers and measurable results the strategic values of partnering with third-party channel organizations.

John Briggs & F. David Peat, ***Turbulent Mirror***, Harper and Row, 1989. A study of chaos theory and self-organizing systems that is interesting, very readable, and relevant to markets and business systems. You don't

have to be a technologist to read this book. It will alter, for the better, your perspective on how a business actually operates, as a self-organizing system.

Eric Hoffer, ***The True Believer***, Harper & Row, 1951. An easy to read, yet profound, study of the nature of mass movements. Many of the issues he discusses apply to current events and to the strategies and cultures of many businesses.

Douglas R. Hofstadter, ***Gödel, Escher, Bach:*** an Eternal Golden Braid, Vintage Books, 1979. Winner of the Pulitzer Prize. Hofstadter weaves together mathematics, art, music, biology, computer science, and much more into a fun and mind expanding experience. If you know about one of these topics when you start, you can map that knowledge into the other subjects and discover that you already know a lot about them too! This book does not directly talk about business, but it does talk about self-organizing systems and degrees of coupling at low levels (components) that cause "clumped" behaviors at higher levels. This material contributes to an understanding of coherent behaviors in teams of people. In general, this book is just too good for me to pass up an opportunity to recommend it. Suggestion: When you read it, don't plod through it cover to cover. Follow those themes (there are seven) with which you are comfortable or familiar, then tackle the unfamiliar ones.