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## RIEKHOF ON PRICING No 59

When Sales Incentives make Price Strategy Implementation impossible

## When Sales Incentives make Price Strategy Implementation impossible

Many well-conceived pricing strategies often fail because incentive systems in sales hinder their implementation. Corporate leaders should pay much closer attention to this issue.

In our Pricing Newsletter No. 59, we explain where the greatest opportunities lie in aligning pricing strategies with incentive schemes of your sales team.

### Implementing Pricing Strategies: The six execution levers

Let's first take a look at the levers used to implement strategies in general. This is one of my favorite research topics: why do strategies fail? In my book (see below) I identified six main reasons why strategy implementation does not work:



**Hans-Christian Riekhof,**  
**The Six Levers of Strategy Implementation.**  
**Schäffer-Poeschel Stuttgart**  
**2010, ISBN 978-3791026251**

These are the six execution levers – the top management should use them for a review when the implementation of strategies shows limited success:

#### 1 **Strategy Roadmaps (Pricing Roadmaps):**

A clear strategy roadmap for each business unit, division, and affiliate. In pricing, we call them Pricing Roadmaps.

#### 2 **Resources for Strategy Implementation:**

Strategy-related allocation of necessary resources is a MUST. Strategies will fail when resources are not available. Strategic (pricing) projects require budgets aligned with the strategy. And keep in mind that management attention is a crucial and often scarce resource.

#### 3 **Strategy (or Pricing) Scorecards**

Strategy scorecards resp. pricing scorecards will measure implementation success, emphasizing the principle "What gets measured gets done."

#### 4 **Strategy-based Management Competencies and Incentive Systems**

Managers do need deep theoretical as well as practical know how in pricing. They need fundamental training and development in this area. And very often sales-based incentive schemes are one of the main reasons why sales people do not care so much about pricing strategies. This is the focus of our current Pricing Newsletter No. 59.

#### 5 **Organization Structures and Business Processes aligned with (Pricing) Strategies.**

(Pricing) strategies will fail when organisational structures do not support them, and when pricing processes are not aligned with pricing strategy.

#### 6 **Urgency and Commitment: C-level Support for the Strategic (Pricing) Agenda**

Last but not least, a sense of urgency must be created and demonstrated by the company leaders (as discussed in my Pricing Newsletter No. 44).

These six execution levers are a framework for implementation, and they can be used as a checklist when you want to assess shortcomings and obstacles in the execution process.



Fig. 1: Pricing strategies will not work when incentive systems are not aligned with strategic intentions

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#### Negotiating Prices with Customers based on your Price Strategy: The Role of Sales

In most companies, the sales team has a decisive influence on the final price paid by customers. In B2B, the sales team and key account managers negotiate final prices, order details, payment terms, and delivery and service conditions.

In B2C, store managers decide on discount promotions, special offers, placement of promotions, special conditions for specific customers, and price communication. Certainly, the influence of sales on the price is ultimately variable in each company and industry, but generally quite significant.

#### Increasing Revenue as the Key Motivation in Sales

Both sales management, key account managers, and the sales team are usually highly motivated to achieve their revenue goals, as a substantial part of their compensation usually depends on these targets. This means that the sales team places great emphasis on ensuring that:

- No order is lost due to price
- Existing customers are retained - given the significantly higher cost of acquiring new customers.

This ultimately implies that the consistent enforcement of higher prices may be only half-heartedly supported by the sales team. Losing revenue due to prices is something they want to avoid – sometimes at all costs.

“When Pricing strategies do not show the intended results, you better have a look at the incentive plans for your sales team.”

Prof. Dr. Hans-Christian Riekhof



**Fig. 1: Using a pricing role model for your product portfolio offers the chance to connect pricing objectives and sales incentives**

### Sales Incentive Systems: Short-term vs. Long-term Orientation

A fundamental challenge in designing incentive systems for your sales team lies in the fact that it is much easier to incentivise short-term actions and goals. Establishing incentive systems that span multiple periods is much more challenging. Annual salary and bonus discussions, as well as corresponding planning and budget rounds, are firmly established. Setting a three-year development goal for specific customers, industries, or product groups is conceivable but not easy to implement. So a long-term incentive might be an additional option, but it will not replace a short-term bonus system.

### Sales Incentive Systems: Revenue vs. Contribution Margin

Another difficulty lies in the fact that many incentive systems are, for simplicity, oriented toward revenues. In my own management career, as a general manager, I once tried to switch from a revenue-driven incentive system to one based on contribution margin for my sales team.

This was more challenging than expected. A customer's or a sales region's contribution margins are significantly influenced by manufacturing and raw material costs – factors beyond the control and responsibility of the sales team. Therefore, we stuck to our traditional revenue-based incentive scheme. But we introduced some innovative elements into it which will be distributed below.

## Solution 1 Product-related Incentive Systems for Price Strategy Implementation

In Pricing Newsletter No. 48, we outlined how we assign strategic roles to certain product groups. Think of categories such as:

- Commodity Items
- Product Launch Items
- Recommended Items
- USP Items
- Specialized Items
- Customized Items
- Validated Items
- NOS Items (Never Out of Stock)
- Services
- Hidden Items, among others.

These categories are associated with different price strategic guidelines, objectives, and revenue potentials. In my Pricing Newsletter No. 77, I interviewed Dorian Rieger from Sartorius in Göttingen about how Sartorius uses pricing roles for their product portfolio in order to reduce complexity.

The sales management can use these categories, setting sales targets for each category (e.g., prioritizing Recommended Items for growth or providing high incentives for Customized Items). This aligns sales

“When you want to connect pricing strategies and sales incentives I strongly recommend to use price-based product roles. They are a pragmatic way to pay your sales team for pricing performance.”

**Prof. Dr. Hans-Christian Riekhof**

incentives directly with the goals of the price strategy. For these roles or categories, a marginal contribution as well as a pricing strategy has been defined; therefore, objectives for these categories are aligned with pricing targets.

I personally experimented with how closely product-related guidelines from product management could work in sales many years ago when I was the head of an operational business unit. At that time, we selected three products with high contribution margins for a growth initiative, we actively promoted them, and provided the sales team with bonuses. The results exceeded our expectations, surprising us all.

## **Solution 2** Product-related Incentive Systems for Price Strategy Implementation

Various studies have shown that organizations tend to fully exploit the maximum allowable discount levels. For instance, if a quantity discount of 15% is possible (though not mandatory) for certain sales volumes, in practice, these 15% are granted in most cases. The same applies to other types of discounts.

It is advisable to integrate the minimization of discounts or the reduction of discounts, during customer discussions and sales work, into incentive systems. In our pricing projects, we regularly identify significant potentials for reducing customer discounts that are no longer justified (e.g., due to unmet quantity thresholds or changed conditions).

Within an incentive system, it is possible to determine the total discount volume of all types in a sales region, and to define targets to reduce granted discounts.

## **Solution 3** Independently plan quantities and prices, and implement them into target objectives.

In the first semester of a business administration studies for a bachelor's degree, one learns that revenues result from the multiplication of unit price and quantity. However, this fundamental concept hasn't yet permeated all architects of ERP systems.

Planning and budgeting systems should independently represent quantity and price effects. In practice, we often encounter companies in our projects that stick to merely reporting total revenues. Consequently, it becomes challenging to incorporate and accurately track targets for price increases in the systems and match them with actual figures.

### **Our Conclusion: Align Incentives with Product Categories Related to Pricing**

It should be clear that in many companies, incentive systems are geared towards achieving revenue goals. Enforcing price increases or, more broadly, implementing the price strategy then has limited chances of success.

We see the greatest opportunities for embedding price strategic goals in the sales team through the introduction of a product category system for the entire product range. Categories like Recommended Items, Commodity Items, Hidden Items, and Specialized Items can be differentiated. Price strategies are formulated for these categories and translated into sales targets, creating a cohesive pricing process from product management to sales organization – a good foundation for shared success.

If you are interested in further aspects of managing pricing strategies and their implementation, I recommend these Pricing Newsletters – available for download on [www.unicconsult.com](http://www.unicconsult.com):

- Pricing Newsletter No. 77 (2023): Mastering Portfolio Complexity.
- Pricing Newsletter No. 75 (2023): The 11 Most Common Strategic Pricing Mistakes.
- Pricing Newsletter No. 70 (2023): How to Succeed in Commodity Pricing – Escaping the Commodity Trap.
- Pricing Newsletter No. 65 (2022): Do you have a Handle on your Rebate Strategy?
- Pricing Newsletter No. 48 (2021): Creating Pricing Categories for your Products.
- Pricing Newsletter No. 42 (2020): Can the Sales Team be Utilized for Pricing Research?
- Pricing Newsletter No. 39 (2020): Is Centralization the Way forward in Pricing?

[www.unicconsult.com/pricing-newsletter/newsletter-abonnieren/](http://www.unicconsult.com/pricing-newsletter/newsletter-abonnieren/)



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