June 2017

McKinsey Quarterly

Landing the megadeal: Seven keys to closing big sales that make money

Your salesforce needs help to remain objective, build trust, get the price right, and keep selling until the deal is done.

by David Levitch, Aditya Pande, and Brian Selby

It all started out so well. A long-time, valued customer of a networking company put out the word that it was planning a massive purchase of equipment. The supplier assembled a deal team, submitted a bid, and made the sale. But not at a profit. The customer loved the extra scope the supplier had built into its proposal but wasn't willing to pay for it, leaving the supplier with a choice of walking away or taking a hit. It chose the latter. Of still more concern was a contract clause stipulating delivery milestones. The deal was signed three months later than expected, but no one thought to change the delivery dates accordingly. Within a matter of weeks, the supplier found itself liable for penalties.

This networking company had just experienced the downside of banking on megadeals. Winning them is the holy grail of many a sales organization. Among the companies we have examined, it is not uncommon for 40 percent of projected revenues to come from just 1 percent of deals in the pipeline. A big government IT project, a contract to build and operate oil-production facilities, or an agreement to run retail outlets at sports stadiums can run into the hundreds of millions of dollars. But while losing a megadeal can mean missing revenue targets, winning one on the wrong terms can destroy value, either because of poor pricing—we often see margins that fall 50 to 75 percent below the typical target—or terms and conditions that put companies on the hook for risks they haven't fully understood or quantified.

The potential pitfalls increased as buyers improved their procurement processes, centralizing them to raise their bargaining power and deploying big data and analytics tools to gain deeper insights into suppliers' costs. Although some companies on the supply side—particularly high-tech ones—are seeking to redress the power imbalance, many deal teams still find themselves behind the curve, ill-equipped to win the big deal on the right terms.

There's no single fix. It's about more analysis and discipline when companies decide which deals to pursue and which to let go, how to manage relationships, and how to price. It's about supporting teams to shape proposals to consistently high standards. It's about incentives. And, crucially, it's about more involvement from CEOs looking at megadeals through a shareholder lens to ensure that they create value. Here are seven measures companies can take that can help them win more value-creating megadeals.

1. USE DEAL FORENSICS TO ELIMINATE DEAL FEVER

Deal fever is like summit fever, when fuzzy thinking brought on by exhaustion and altitude sickness convinces climbers they have come too far to turn back. Oxygen is in short supply on a tall peak, and so is objectivity—which also eludes salespeople fighting to keep alive what might be the biggest deal of their careers, whatever the cost. And because pursuing big deals eats up resources, the longer one is on the table, the more difficult it becomes to walk away.

To clarify the pros and cons of potential megadeals, some companies use a deal-forensics scoring system. Here's how it works: the team chooses a handful of factors deemed essential to winning a good deal, such as client engagement, the strength of the solution, the price, and the strength of the sales team. A series of questions then gauges the bid against each of these, at every stage of the bid, from submitting qualifications through the negotiations. For example, what relationship does the seller have with key decision makers? The answer might range from none to being a trusted adviser, and it is scored accordingly on a predetermined scale. Other questions the seller might ask include these:

- Do other bidders have stronger relationships?

- Is there any evidence that competitors have better solutions?
- Will the client follow through?
- How does the price compare with those of competitors?
- Will the deal be profitable?
- Can we staff the sales team properly?
- Could the contract be a game changer for how we are perceived in the market?

The weighting of scores for each answer is based on patterns revealed by analysis of past deals that were lost or won, as well as strategic considerations, which might, for example, change the relative weight of a deal's profitability as opposed to breaking through with a critical customer. The answers—and overall score—will change as the deal progresses and information accumulates.

In effect, the scoring system enables a stage-gate review, helping executives to decide where people and money need to be allocated to improve the prospects of certain deals, which deals to back away from because they have little chance of success, or what action is needed to improve the odds at different stages of the process. For example, deal forensics revealed to a large outsourcer, at the outset of its bid, that it had very little chance of winning a financial-services deal, because of poor relationships. Rather than give up or continue in vain, it chose a third option: with nothing to lose, it told the buyer's procurement group it would drop out of the bidding unless it could engage with the decision makers every week. Procurement, fearing a less competitive landscape, agreed, and the outsourcer went on to win the deal.

Deal forensics also flashed red on a megadeal that the sales team of a high-tech company had been working on for nearly two months. Relationship building had lost momentum, and the solution seemed weaker than that of competitors. Faced with this realization, the supplier's CEO suggested that his CFO meet with the buyer's CFO in a last-ditch effort to uncover the key to winning the deal. Within days, the two CFOs had come up with an alternative deal arrangement that kept the supplier in the running and ultimately secured the sale.

2. TO AVOID OVERENGINEERING A SOLUTION, PRICE FIRST

Many deal teams still respond to a request for tender by first scoping out the best technical solution. Only then do they determine the price. The result: deals lost before the conversation even begins, because the price is too high.

To win more good deals, the starting point has to be a minimum viable solution (MVS) that strips out any scope not included in the customer's request for tender, as well as features that may be valuable for some customers but make little business sense for this one. The result is a solution that meets the customer's needs and indicates, when priced, whether it also meets initial profitability criteria. The customer's budget, pricing norms in a given region or industry, and information gathered on competitors will then help decide what margin is possible and, hence, the target price of a tender—as well as the advisability of continuing to pursue the deal. This does not mean that the scope cannot be expanded later through customer feedback, but it is better to add in scope than to try and strip it out, as the networking company found out to its cost.

It's important to scrutinize all of a deal's key economics, which can extend beyond the seller's corporate borders. One company discovered that though its business units were willing to collaborate and to abandon bells and whistles for an MVS, the margins some external partners required were going to make it very hard to assemble winning bids. The sales team therefore began taking a harder look at each partner's contribution and decided whether it was a crucial component of an MVS. The answer was not always yes.

3. THINK ABOUT RELATIONSHIPS IN A MORE SCIENTIFIC WAY

From dentistry to real estate, relationships drive sales, but many top executives rely too little on their relationships or assume too much about them. This issue persists because most sellers "manage" such a relationship in their heads and rarely assess its strength. A business-unit leader we know became aware of just how poor a relationship his key-account manager had with an executive at a major customer when the account manager couldn't find the executive's office for a key in-person meeting!

Companies that manage relationships well use deal-relationship maps to understand who matters, as well as what matters to each party: price, quality, service. The map can then be used to develop the right solution, to pressure-test and refine pricing terms and conditions, and to ensure that the right messages reach the right people throughout the deal cycle.

The map should identify not just the usual suspects—that is, the CFO, CIO, and COO—but also those who hold informal power for awarding specific sales contracts, such as the procurement lead or the customer's external partners. One deal was won because the supplier's pricing team developed contacts with the customer's engineers, who were helping to model the deal. The engineers' rich insights into what their company was looking for would otherwise have gone undetected.

Senior leaders need to be involved if relationships are going to deliver. One company we know augments its sales approach on big deals by assigning senior pricing executives to meet their counterparts on the customer side. After each meeting, the pricing executives update the stakeholder map to reflect new insights.

4. APPOINT AN OVERALL LEADER AND STANDARDIZE PROCESSES

A frequent complaint from senior leaders is that they lack people with the full range of skills required to win big sales contracts. It's easy to see why: there are relatively few such deals to apprentice on, and training people to lead sales of, say, trains or aircraft can take a decade or more as they rotate through various roles. Companies therefore find themselves competing for the same handful of people—or relying on the regional team that unearths a deal (and often lacks the necessary expertise) or on the head of sales (who might not have the bandwidth). When the sales chief at a fintech player stepped out of his day-to-day role to run a major deal, the company duly won the business but also missed other quarterly targets through management inattention.

One thing that can help is to identify one or more high-caliber sales-team leaders to manage all big contracts and to help junior salespeople learn the ropes. One CEO we know held out for six months to find the right person to fill the team-leader role, such was the standard he set. Strong support processes are a second important enabler. Each deal is different, but not so much that it defies any systematization. Frankly, it is far too risky for sales teams to be creating—deal-by-deal, with limited oversight—complex bid models that can run to hundreds of spreadsheet tabs or specialized terms and conditions.

Components of the process can be standardized to help a sales team shape proposals quickly, efficiently, and to a consistently high quality. Strategy sessions that pull in the right people to decide how best to approach and execute a bid, stakeholder mapping to understand which people matter and how they should be engaged, competitive-response sessions to understand where competitors' weaknesses might lie and how to exploit them, and solution reviews to identify opportunities for integrating products and services—all these can be organized in a way that supports the team and the best possible outcome.

5. ALIGN INCENTIVES TO MATCH SHAREHOLDER VALUE

The networking company mentioned earlier found itself owing millions of dollars because of terms and conditions it could not meet. The salesperson, who had already been fully compensated on the basis of the contract's sales value, did not suffer financially. Shareholders did, however—as they often do when incentives are misaligned.

Overlooking risky terms and conditions is not the only hazard. Without some skin in the game, salespeople can keep working for too long on deals they know they are unlikely to win. Companies can inadvertently encourage such behavior when a proportion of any commission is due at various stages of the deal, such as winning a request for information or a request for proposal (RFP). The salesperson will press to pass as many milestones as possible in search of reward.

Misaligned incentives also destroy deal margins. Companies may put a huge effort into setting a target price, but time and again we see salespeople negotiating away the profit margin to bag a deal. Discounting a price from $350 million to $320 million could still mean a hefty bonus for salespeople rewarded according to revenue targets, but that $30 million reduction comes straight out of the company's profit.

We've seen a number of companies stretching to do better by setting long-term incentives that reflect not just revenues but shareholder value too. One technology player has started adjusting compensation to the operating income that a contract generates or to the achievement of strategic objectives. But companies must go into compensation overhauls like this with their eyes wide open: some individuals with strong track records in closing big deals may walk away if their incentive schemes change and they fear losing pay. The CFO at the above-mentioned technology company had to work hard to counteract perceptions that the adjustments were unfair and would leave salespeople worse off. Pointing out that the size of the compensation pie was the same, she won over most, though not all, of the strongest performers.

More data and better analytics can help companies encourage salespeople to focus on the value, not just the volume, of a deal. A number of companies we know are using advanced-analytics tools to help the salesforce stay firm on price. They identify deal archetypes according to the type of customer, the product, and the size of the deal, and then let salespeople clamoring for discounts know when similar deals have been won on less generous terms. Information like this makes it much harder for salespeople, even stars, to justify megadeals that don't create much value and can help them accept that new measures of compensation are fair.

6. KEEP SELLING EVEN IF YOU LOSE A DEAL OR CHOOSE NOT TO PURSUE IT

Deal teams should not walk away from potentially valuable relationships just because they fail to secure a deal. By staying engaged, it is sometimes possible to pick up adjacent business. Occasionally, a deal that seemed lost can be rescued. One large software company, on learning it had lost a deal on a Friday, flew its CEO to meet the buyer's people over the weekend. By Monday, the buyer's CEO and board had reversed their decision.

More commonly, continuing to invest in relationships built over the course of a tender raises the likelihood that future bids will succeed. Our experience is that about 20 percent of lost deals produce significant dividends over the next two to three years.

Sometimes expectations should be reset at the outset of a bid, to acknowledge that the chances of winning are low but that the bid process is an opportunity to build commercial ties in the longer term. One telling example: a healthcare RFP was declared a "must win" by the sector sales leader of a technology service provider. However, the deal forensics indicated a very low starting score. The CEO let the deal progress for a short while, but when the score failed to improve, he cut back the sales team's resources, effectively extinguishing any hope of winning the deal (and saving what would probably be wasted costs). At the same time, though, he insisted that senior salespeople and technical experts continue building relationships with the potential customer and make sure his company's capabilities were well understood. This proved an excellent strategy. The service provider lost the RFP, as expected, but won the next one.

7. RETHINK THE ROLE OF THE CEO

The six measures described above would surely have helped the networking company avoid its sales fiasco. But winning megadeals is not just about tactics—it entails a new way of thinking that values the long-term health of a company over winning a megadeal. That can be a difficult message to embed within a sales team long focused on how much it will earn. The job of doing so falls to the CEO.

One newly appointed CEO felt that his task of transforming the company's performance hinged on transforming the sales team, a challenge he threw himself into. He determined never to miss the weekly meeting of the deal team when a large contract was at stake. His intention was partly to support the team—listening carefully to learn more about how the deal was progressing, where the risks lay, and where help was needed. But he also wanted to demonstrate a different approach, nudging the team out of its default setting.

For example, some team members were always keen to keep on selling the old, familiar products they were more comfortable with. But the CEO insisted that they consider which products suited the customer. And he made sure that they scrutinized every deal from a shareholder's perspective. Were the financial implications of all the terms and conditions clearly understood, and was the right balance struck between near-term profit and long-term growth potential? In an important move, he would not allow these meetings to begin until all senior team members were present. No delegating was allowed.

This is far from the traditional role CEOs have taken in managing large deals. That is partly understandable—they are busy, after all, and sometimes it's enough to enter the scene toward the end of the process to help close a deal. One CEO we know is typical: "I usually meet with the buyer's executive team and approve final pricing, but I don't see a role beyond that." By then, however, it can be very hard to make changes that boost the attractiveness of a deal to the seller or buyer.

More often than not in our experience, companies benefit when CEOs imagine a broader role for themselves in megadeals. They should always be asking tough questions about whether effective controls are in place to manage pricing and profit. Above all, it is the CEO who can be most effective at helping teams caught up in the exhilaration of a megadeal to focus, front of mind, on their ultimate purpose: creating value for their companies. Q

David Levitch is an associate partner in McKinsey's Chicago office, **Aditya Pande** is a partner in the Silicon Valley office, and **Brian Selby** is a partner in the Seattle office.