

Marketing & Sales Practice

Solutions Selling

Is the Pain Worth the Gain?

McKinsey & Company

Overview

“Solutions selling” has been all the rage over the last 5 to 10 years, yet 75 percent of the companies that attempt to offer solutions fail to return the cost of their investment. Our work with a wide variety of companies suggests that solutions selling does offer a considerable prize, but that it does not come easy.

First, you have to understand how a solution is positioned in terms of two key variables, customization and integration. This positioning drives the basis of your competitive advantage and – most crucially – the “pain/gain” trade-offs you need to understand.

Then, you have to execute quite differently from a standard product-based go-to-market model in at least the first two – and preferably all – of five key dimensions:

- Create distinctive solutions value propositions using customer business metrics, not product price/performance metrics.
- Radically change the selling approach and, if necessary, the sales talent.
- Price solutions based on total business value delivered, not component features.
- Align the entire organization, not just sales, with the solutions opportunity.
- Maintain control of all aspects of implementation to ensure end-to-end value delivery.

Solutions selling is not for everyone. But for those who understand and can implement these imperatives, there is tremendous upside.

“Solutions selling” has been perhaps the most overused marketing buzzword of the last decade. Unfortunately, our discussions with over 60 solutions sellers suggest that three out of four companies selling solutions fail to see sustainable economic impact. Simply, for most companies, the pain has not been worth the gain. Why, then, do companies embrace the idea? Because those who do win enjoy significant margin and revenue improvements, as well as other benefits (see Exhibit 1).

Exhibit 1 Examples of solutions success

	Solutions transition	Impact
	<p>Global hardware provider transitioned to hardware/software/services “consultant” with well-integrated solutions across the entire spectrum of offerings</p>	<ul style="list-style-type: none"> • \$36 billion services company built from scratch • Gross profit for overall services business grew at 9.7% CAGR from 1996 to 2001
	<p>Private software provider achieved superior customer value delivery by transforming to solutions provider targeting four vertical industry segments</p>	<ul style="list-style-type: none"> • 25% uplift in pre-tax profit • Customer retention ~10% higher than industry • Project success rate tripled to 3x industry average
	<p>Multi-business industrial/high-tech U.S. organization, with 100% of revenue from siloed business units, created independent solutions BU to facilitate sales to select major opportunities (e.g., airports, stadiums, entire hospitals, high-tech campus)</p>	<ul style="list-style-type: none"> • \$380 million in incremental revenue in Year 1 • Access to customers previously outside addressable market
	<p>Traditional chemicals company, with a BU providing commodity chemicals to very large independent customers, created an independent BU to provide total chemicals solutions, thereby also serving smaller, less sophisticated customers</p>	<ul style="list-style-type: none"> • More than double the margin % for solutions than product business • Access to new markets

In general, companies enter the solutions melee for one of two reasons – ambition or anxiety. Some are drawn by the promise of increased margins, win rates, share of wallet, customer retention, or access to new markets – or even by favorable press. Others fear rapidly commoditizing core markets, the increasing sophistication and power of buyers, and competitive disintermediation.

Solutions providers who fail typically do so because they:

- Pick the wrong solutions game (or games) to play, whether by targeting the wrong customers or by failing to offer a solution sufficiently more compelling than their customers' alternatives;
- Make uneconomic “pain/gain” trade-offs, either because they don't understand the true basis for winning at their chosen solutions game, or because they don't possess the attributes necessary to win; or
- Fail to execute differently from their traditional product-centric go-to-market model in at least two of five key dimensions.

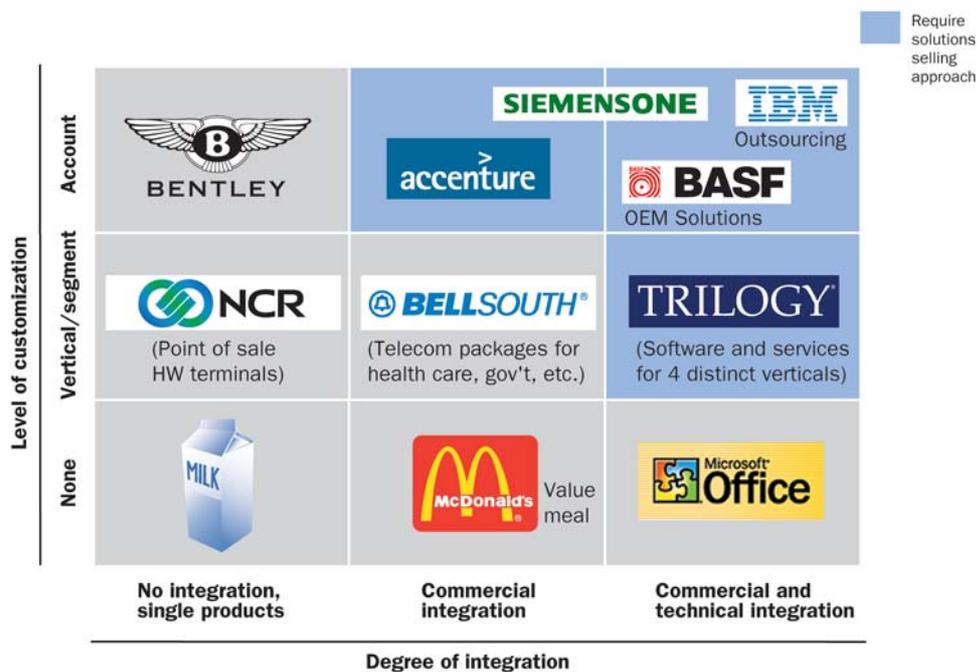
In contrast, winners consistently get these three things right.

Which solutions game (or games) should you play?

Most vendors and customers can agree on what a product is. Few companies share a common definition of a solution, beyond a vague notion that it is a combination of products and services which solves customers' business problems. In our work, we discovered that products and solutions are most critically differentiated by the degree of customization a solutions provider can deliver, and the degree of integration across multiple products and services (see Exhibit 2).

The vast majority of solutions providers offer some degree of customization to industry verticals or customer segments, ranging from superficial differences in marketing brochures to major differences in technical specifications, pricing and service

Exhibit 2: **Understanding what you offer in terms of customization and integration**



levels. Some provide highly tailored, customer-specific solutions, typically for their very largest accounts.

Integration is the degree to which products and services within a single offer are interrelated to deliver value beyond the sum of the parts. *Commercial integration* (i.e., bundling) combines multiple products and/or services into a single transaction. The products do not naturally have to be sold together to deliver useful value to customers. In combination, however, they provide some incremental billing and customer service convenience and consolidated vendor accountability. Providing local and long distance phone service on one bill from one company is an example.

Technical integration, in contrast, requires the physical interoperability of components to create value beyond the sum of the parts. For example, good call-center IT solutions vendors integrate physical end-user equipment, data and voice

communications, application software and server hardware and storage, along with customer and end-user training, to deliver an integrated call receiving, routing, handling and disposition capability.

Many companies, especially larger, established ones, have offerings across several cells of the customization/integration matrix in Exhibit 2. Judging the extent to which you want to and can participate in each type of solution offering is crucial to ensuring solutions success. Why? Because the basis for winning, the pain/gain trade-offs, the go-to-market models and the execution challenges are very different for each cell – just as they are different for standalone product businesses. Offering the “right” solution with the wrong model will be an expensive, failed experiment – and it will likely also take your focus off executing your non-solutions business successfully.

Understand the basis for winning and the “pain/gain” trade-offs

What is your basis for winning?

If you want to win based on your ability to *customize*, you must have distinctive insight at the account, segment, or vertical level into specific business problems that your solutions can solve demonstrably better than the alternatives; identify enough customers to more than offset your incremental cost of customization through higher revenue (or revenue you can retain over a longer period); and develop a sales force that has credibility with both technical and business-unit-level decision makers – often two or three levels higher in the customer hierarchy than buyers of your traditional standalone products.

Winning based on the degree of *integration* your solutions deliver depends on whether you want to stop at being a commercial integrator or bundler, or whether you want to deliver both commercially and technically integrated solutions. To win at commercial integration, you must be a market leader for at least

one component product or service in your bundle; you must achieve a combined cost of acquisition, contract management, fulfillment, billing, and service across all components of the bundle that is lower than both the expected customer discounts and the equivalent costs for your competitors; and your sales processes, product factories, and back office must be capable of delivering the promised convenience and one-stop accountability.

The bar for winning in both commercial and technical integration is at once higher and different. In addition to meeting these criteria for commercial integration, you must have distinctive technical expertise in integrating multiple products into a useful business solution (such that your integrated solution simply “works better”); lower costs of product or service integration than either your customers or competitors; and an established base of customers that already buy one or more of the un-integrated solution components from you.

Clearly, the more customized and integrated your solution, the fewer your competitors, and the higher your gains. So where is the catch?

What “pain/gain” trade-offs should you expect?

The hoped-for gains from selling increasingly customized and integrated solutions rather than products are clear: increased margins and win rates, access to new markets, increased share of wallet or deal size, and improved customer retention. However, these potential gains must be rigorously balanced against the pains: the cost of transitioning the sales force to a solutions model, and perhaps of replacing it; longer sales cycles; the increased interaction and governance costs implicit in the cross-functional nature of solutions; and, of course, the incremental investment necessary to develop and deliver a distinctive solution in the first place (see Exhibit 3).

Consider the example of a chemicals company with a business unit that provided commodity chemicals to very large industrial customers. The company recognized that by creating an

Exhibit 3: The pain/gain trade-off

Potential gain

- Value created by solution above and beyond the sum of the components or reduced cost of delivery creates **increased margins**
- Ability to create greater business value for customers results in **increased win rates** and/or reduces competition
- New solutions enable you to address **new markets** that would not previously have been addressable
- Ability to serve customers more broadly provides **increased share of wallet/deal size** with them
- Becoming a more strategic business partner delivers **improved customer retention**

Potential pain

- Cost of **transitioning sales force** to solutions model or replacing it altogether
- More strategic and consultative selling demands **longer sales cycle**
- Additional people and greater skill requirement implies **higher sales and marketing costs**
- Need for distinctive solutions and execution excellence drives **incremental investments in solution development and delivery**
- Cross-functional nature of solutions mean **higher interaction and governance costs** (both internally and with business partners)



independent business unit to provide a total chemicals solution, they could also target smaller, less sophisticated customers who needed, in addition to the raw materials, counsel on chemical mixtures and technical services.

Creating the new business unit was costly: a new combined sales and technical-services role increased sales costs, and the sales cycle was longer. SG&A rose from 9 to 14 percent. But gross margins went up from 9 to 20 percent, resulting in six additional points of margin. Further, the expanded services allowed the company to serve a new, previously unaddressable market segment.

Each customization/integration cell shown in Exhibit 2 has a different set of pain/gain trade-offs, and you must understand which combination you are dealing with. The most common

mistake we see is a company either in the right cell with the “wrong” model, or vice-versa.

Execute differently from your traditional go-to-market model

Picking the right types of solutions to deliver and making realistic pain/gain trade-offs are necessary, but not sufficient. You must also execute *differently* from your traditional product strategy. In particular, solutions winners consistently change their model in two dimensions, by:

- **Creating distinctive solutions value propositions using customer business metrics**, not product price/performance metrics. Solutions value propositions must be based on how customers measure success, not how vendors measure performance.
- **Radically changing the selling approach and, if necessary, the sales talent**. Successful solutions organizations often replace more than 50 percent of their existing product sales force in the first 12 months.

Some go beyond these two imperatives to ensure value capture in three additional dimensions:

- **Pricing solutions based on total business value delivered** relative to the customer’s next best option, not based on component features.
- **Aligning the entire organization, not just sales, with the solutions opportunity** – but without disrupting the core business.
- **Maintaining control of all aspects of implementation** to ensure end-to-end value delivery and accountability, often by limiting or eliminating the use of partners.

Create distinctive value propositions using customer business metrics

You cannot create a uniquely powerful value proposition without investing in a deep understanding of customer needs.

Consider this example of an excellent value proposition. One automotive commodity supplier of paints to OEMs transformed itself into an integrated provider of painted cars. The supplier's expertise allowed it to take over its customers' paint shop operations, one of the most expensive elements in automotive assembly. In doing so, the supplier changed the value metric from the traditional, product-oriented dollars per gallon of paint to the customer-oriented dollars per painted car. It drove paint consumption down 20 percent, and became the leading provider to automakers worldwide, garnering 70 percent of the market.

Companies that fail consistently underestimate the investment required to craft a distinctive value proposition driven by a deep understanding of customer needs. Consider the contrast between the investment two Tier 1 automotive suppliers made in understanding their customer in the early 1990s. Both sought to establish a relationship with a large German OEM. One went to the OEM's headquarter city, opened an office across the street, dedicated sales and engineering resources that were 100 percent committed to cracking the account, and spent 2½ years working with the OEM's technical people to develop specific applications. The other maintained its product-centric approach (which was actually more focused on another large OEM) and did not dedicate any specific resources to this particular target customer other than some time-shared engineering support. The customer recognized they wouldn't get the same level of dedication from this supplier, and that they were unlikely ever to get access to its proprietary technology (unlike the other OEM). Not surprisingly, this supplier was unsuccessful.

Radically change the selling approach and, if necessary, the sales talent

In order to sell solutions instead of standalone products or services, winners focus on the key senior decision makers at a manageable number of target customers, and change – often quite dramatically – their selling style, the mix of talent required to deliver the sales message, and the performance measures by which they track, manage, and compensate.

Target customers and decision makers. Winners target a finite number of customers with similar core business needs in a certain segment and spend time working directly with senior executives with business P&L responsibility, as well as with the “usual suspect” product or category buyers. A solutions account team typically must call on three or four times as many people – in different functions and business units – at a single customer as they do for a product sale. This is partly why sales cycles are usually longer for solutions – solving bigger problems and closing larger deals requires convincing more and different people.

Talent and roles. Strong solutions sales people possess deep industry knowledge, develop partner-like relationships, and can articulate a solution’s value relative to the customer’s next best alternative. Typically, less than a third of a product-oriented sales force can make the necessary transition. Consequently, the majority of the required talent has to be imported, whether to replace existing sellers or to create a separate sales structure. Often, this talent comes from within the industry verticals the company is targeting; or they may already be “stars” in another part of the organization. Once in place, they must be deployed optimally. Winners typically structure an account team around a single customer-relationship owner, supported by a much richer mix of industry experts and technical specialists, to ensure value delivery from sale through installation to service.

Governance and performance management. Top solutions performers manage performance by tracking business value delivered and customer satisfaction, in addition to sales revenue

and contribution. They also pay particular attention to quotas and incentives to ensure sellers are motivated to work through longer sales cycles and unfamiliar decision makers to get the larger deals, instead of pushing quicker and easier product sales to meet their sales targets. Winners also consciously manage both internal interfaces (across products, functions, and business units) as well as external ones (with partners), with clear rules of engagement and incentives that maximize the overall benefit to the company.

Consider the example of one large technology provider that moved from delivering products and bundles to become a solutions provider across the entire spectrum of offerings. First, management selected 48 target accounts for a pilot and hired or transferred-in 60 experienced, top-performing sales people to serve them. To focus the team on solving the customers' problems rather than pushing individual products, the company revamped the incentive system to provide team-based compensation based on total sales to the account, regardless of product group. The company understood its customers' needs to the point that when a customer asked for a bid, it would submit two – the bid it had been asked for, and the bid it thought would really meet the customer's needs.

Price solutions based on total business value delivered

Most companies invest far too little time in understanding the total economic impact their solutions have on their customers' business systems before establishing pricing. Getting this right is hard, and requires technical and operational people to work in collaboration with customers, not just sellers and marketers. This is quite a different exercise from the vast majority of product-pricing decisions, which are made on a cost-plus or competitive-product-comparison basis.*

For example, an optical networking company wanted to reprice its flagship solution by better articulating its true value to the customer. We worked with the company to build a model that

quantified the impact to the customer of more than 20 separate elements of the solution in three broad categories: capital savings, operational savings, and revenue enhancement. The proposed solution yielded a 6-year NPV gain of *twelve times* the incremental investment cost over the system the customer would otherwise be using. Using this fact, we demonstrated that the software component was badly underpriced. The client increased the price of its software packages by a factor of about fifty – and overall pricing by 25 percent.

Align the entire organization, not just sales, with the solutions opportunity

Three factors determine which organizational structure works best in your solutions context: How big is the solutions opportunity compared to your existing business? How integrated does your company need to be to create, sell, and deliver the solution? What is your tolerance for organizational disruption? Consider two companies that matched very different kinds of organizational structures to different situations.

Trilogy, a privately held software company, saw an opportunity to deliver superior customer value at a level that would powerfully differentiate it from the competition. It leveraged a private company's freedom to transform its entire organizational structure – from product development to sales to management – from a product-aligned organization to a vertically-aligned solutions provider targeting four vertical industry segments.

Siemens recognized an opportunity to capture between five and ten major projects a year – airports, stadiums, hospitals, and high-tech campuses – previously outside its addressable market, requiring a high level of coordination among its largely independent business units. Despite the size of these projects, 95 percent of U.S. revenue would still be driven by the individual business units, so the company simply put in place an overlay group to play a facilitating and sometimes a project management role in solutions selling, with minimal disruption to existing business.

Maintain control of all aspects of implementation

The implied promise of value delivery is much higher when you sell a solution than when you sell a product, because you are now partly responsible for customer business outcomes, not just isolated product performance. In order to deliver on the promise (rather than just promising to deliver), successful providers typically assume responsibility for coordinating all other parties involved, be it the customer's own staff, internal product units, or solutions partners – thus giving the customer “one throat to choke.” Counter-intuitively, we found that some of the best solutions providers prefer not to partner extensively with third parties to deliver solutions, given the added governance complexity, coordination costs, and delays in ensuring quality implementation.

Solutions selling is not for everyone. For some, however, it can be very profitable. Companies that wish to profit from solutions selling must rigorously address the following questions: Where are our solutions customization/integration “sweet spots”? Are the investment pain/gain trade-offs worth it? What distinctive strengths do we have, and what execution capabilities must we build to execute well? For those with compelling answers to these questions, there is tremendous upside to selling solutions. Others will be better off eschewing the solutions hype and seeking profitable growth elsewhere.

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* For a more in-depth discussion regarding solutions pricing, please refer to “Effective Solutions Pricing: How to Get the Best Premium from Strategic Collaborations,” *McKinsey Marketing Solutions*, May 2001.

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