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# UNIT 15 SALES FORECASTING AND SALES QUOTAS

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## Objectives

After studying this unit you should be able to :

- suggest the importance of sales forecasting and sales quotas for territory management
- describe some of the managerial issues concerning sales forecasting
- explain the importance and types of sales quotas, and how they are established
- discuss some of the attributes of effective sales quotas.

## Structure

- 15.1 Sales Forecasting - Introduction
- 15.2 Sales Forecasting : A Quick Recapitulation
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## 15.1 SALES FORECASTING - INTRODUCTION

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The following discussion on sales forecasting is an extension of Unit 6 of Ms-6 on sales forecasting. Besides a quick recapitulation of the aspects covered in the referred unit, managerial practices of refining the sales forecast are given next. This is followed by discussion on sales forecasting for new products.

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## 15.2 SALES FORECASTING: A QUICK RECAPITULATION

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Sales forecasting is an estimation of projected sales for a time period. Simply speaking, the process of sales forecasting involves reviewing performance, history of the product or service, and relates it to the marketing and sales effort of the firm within the anticipated market environment (economic, competitive, technological, public policy etc.) and buyer behaviour.

Sales forecasts are time span related and therefore are termed as, short term forecast - covering time period of upto a year, medium term forecasts-for a time period of around five years. The exact time period for which a forecast is developed is dependent on the product/ market characteristics as well as the purpose for which it is developed and hence may vary from company to company. Notwithstanding thus the longer the time span covered, the more qualitative will be the forecast, and the shorter the time span covered, the more quantitative the forecast.



Time series (trend fitting, moving average), correlations and regression, customer/dealer surveys and executive judgement are the most commonly used methods for preparing sales forecasts. The selection of the appropriate forecasting method(s) depends upon (i) its purpose (ii) availability of reliable and relevant data and (iii) market conditions. For increased usefulness, the overall sales forecasts should be broken down by product, month, territory, geographical area, and segmentwise as per the needs of the company.

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### **15.3 MANAGING SALES FORECASTS**

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The pay off of sales forecasting lies in the accuracy of the forecasts made. Since the attainment of sales forecasts require the deployment of resources in its anticipation, the manager must do his best to make the forecast come true. Evaluation of the approach and methods used for sales forecasting as well as monitoring of the actual and its comparison with the estimated performance form part of the regular activities of the manager.

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### **15.4 WHAT TO DO WHEN SALES FORECASTS DIFFER?**

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Many a firms in order to minimise the error factor in sales forecasting, use multiple experts and approaches. At times this results in varying levels of sales forecasts under the circumstance, the manager may examine the differing forecasts by :

- Probing into the methodology of sales forecasting adopted by different experts.
- Looking into definition and scope of the terms used in the construction of the forecast.
- Pooling of wisdom of the experts and arriving at the most agreeable level of forecast.
- Conducting retrospective-prospective analysis of the suggested levels of sales forecasts using fine tuned historical data and executive judgement.

Experience brings out that the sales managers who have detailed market knowledge, and their companies the comprehensive marketing information system providing data on product, customer and segmentwise basis of their competitors sales, succeed in making more accurate sales forecasts.

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### **15.5 MONITORING THE SALES ECAS'T**

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As the sales realize for the operating period these should be monitored at a regular periodicity. The unfolding of market reality often creates the need to adjust the sales forecast. Business prudence desires that in the case of annual sales forecast, these be thoroughly reviewed at least on a quarterly basis and if need be corrected too. A similar review on an annual basis in the case of long-term forecast is felt necessary. In the process of carrying out corrections in the sales forecast emphasis should be laid on diagnosing the causes warranting such corrections so that the accuracy level of sales forecasts be improved. In any case a strong justification must be made for modifying the sales forecast so that suitable adjustment in the marketing and sales strategy be also carried out

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### **15.6 SALES FORECASTING FOR NEW PRODUCTS**

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Unlike the established products, forecasting of the sales for new products is more difficult. Depending upon the degree of similarity/dissimilarity with the existing products, sales forecast for new products are based on :

- Past records and experience
- Study of competing product's demand



- Market research findings Test market results
- Demand behaviour of substitute products and rate of substitution.

In addition, sales curve of such a new product in foreign markets and its analysis on a product life cycle basis provides meaningful insights.

In the case of a totally new product, a close watch on the actual sales along with the experts opinion, lessen to some extent the otherwise impossible task of developing reliable forecasts for such products.

### Activity

Check whether the following statements are true or false :

Statement	True/False
1) A firm's sales potential and its sales forecast are normally identical	.....
2) Projecting past sales is totally unreliable for use in sales forecasting	.....
3) The key limitation of all past-sales projection methods lies in the assumption that past sales history is the sole factor influencing future sales	.....
4) Deriving a company sales forecast from an industry sales forecast requires an appraisal of company strengths and weaknesses against those of competitors	.....
5) Sales forecast of totally new products can be developed with equal degree of accuracy as of established products	.....

#### Check Your Answers

1 (True) 2 (False), 3 (True), 4 (True), 5 (False)

## 15:7 SALES QUOTAS - MEANING AND IMPORTANCE

A sales quota is a quantitative goal assigned to a sales unit relating to a particular time period. A sales unit may be a sales person, territory, branch office, region or distributor. Sales quotas are used to plan, control and evaluate selling activities of a company. They provide a source of motivation, a basis for incentive compensation, standards for performance evaluation of sales person and uncover the strengths and weaknesses in the selling structure of the firm. For example, a company manufacturing electronic office equipment discovered that it took twice as long as to sell an electronic typewriter than to sell other similar products in the product line. Since the electronic typewriter was considered more important by company, quotas on the electronic typewriter were set for each sales person. The result was that a sales person in a control group having a rigid electronic typewriter quota outsold the uncontrolled quota group. This example shows that generally speaking sales persons are quota achievers and their motivation may fall off if easy or no quotas are set for them to achieve.

## 15.8 WHY QUOTAS?

Sales quotas serve several purposes. The principal purposes include.

**Providing Goal and Incentives :** Quotas provide sales persons, distributive outlets and others engaged in the selling activities, goals and incentives to achieve certain performance level. Many companies use quotas to provide their salesforce the incentives of increasing their compensation through commissions or a bonus if the quota is surpassed and/or recognised for superior performance. Needless to mention,



to be true motivators sales quotas, set should be perceived as being realistic and attainable.

**Controlling Sales Persons Activities:** Quotas provide an opportunity to direct and control the selling activities of sales persons. Sales persons are held responsible for certain activities of customer per day, calling on new accounts, giving a minimum number of demonstrations and realisation of company's account. If the sales person fails to attain these quotas, the company can take corrective action to rectify the mistake.

**Evaluating Performance:** Quotas enable the company to evaluate performance of its sales person, territory or distributive network. Performance against quotas also helps identify the strong and weak points of the sales persons.

**Controlling the Selling Expenses:** Quotas are also designed to keep selling expenses within limits. Some companies reimburse sales expenses only upto a certain percentage of sales quota. Other tie expenses to the sales person's compensation in order to curb wasteful spending. Expense quota helps companies to set profit quotas.

**Making Effective Compensation Plan:** Quotas play an important role in the company's sales compensation plan. Some Indian companies follow the practice that their sales person will get commission only when they exceed their assigned quotas. Companies may also use attainment of the quotas in full or in part as the basis for calculating the bonus. If the sales person does not reach the minimum desired quota, he/she will not be entitled for any bonus.

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## 15.9 HOW QUOTAS ARE SET?

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Having understood the meaning, and usefulness of sales quotas let us now learn how quotas are set.

There are four types of quotas :

- i) Sales volume quota
- ii) Financial quota
- iii) Activities quota
- iv) Combination of the above quotas.

These quotas alongwith the approach used for their determination are discussed below :

**Sales Volume Quotas:** The most commonly used quotas are those based on sales volume. This type of quotas are set for an individual sales person geographical areas, product lines or distributive outlets or for any one or more of these in combination. Sales volume quotas are also set to balance the sales of slow moving products and fast moving products or between various categories of customers per sales unit. The sales volume quotas may be set in terms of units of product sales, or rupee sales or both on overall as well as productwise basis. Some companies combine these two and set quota on "Point" basis. Points are awarded on the attainment of a certain specific level of sales in units and rupee terms for each product/customer. For example : A company might consider Rs. 1000 equal to 1 point, Rs. 2000 equal to 2 points and so on. At the same time company may award 3 points for unit sales of Product A and 5 points - for unit sales Product B. Companies use this type of approach generally because of problems faced in implementing either Rupee sales volume or unit sales volume quota. Unit sales volume quotas are found useful in market situations where the prices of the products fluctuate considerably or when the unit price of the product is rather high. Rupee sales volume quotas are found suitable in the case of sales force selling multiple products to one or different types of customers.

### **Methods for Setting Sales Volume quotas:**

**Past Sales :** One of the earliest methods of setting sales volume quotas is to base them solely on past sales experience. The method in this case would be to determine the percentage by which the company's market share is expected to increase and then add this into last year's quota. For example, if a company expects an increase of 8 per cent this year then the new quota for each marketing unit would be last year's quota plus 8 per cent or 108 per cent of last year's quota. This method assumes that



the preceding year was a typical year, and if not, it suffers from the limitations of being based on unrealistic figures. An improved method is to take the average of say past three years and then add to it to the planned rate of growth.

**Total Market Estimates:** The other method is to derive sales quotas from the total market size estimates made by the company for the year. Two approaches are used to arrive at such market estimates. One approach is to estimate the market size in an aggregate manner as per the data available as well as the judgement of the executive at the head office. The other is to build estimates based on projections made by the field staff at each territory office of the companies. In either case the market estimates need moderation to be realistic as well as to match with the company's sales objectives.

**Financial Quotas:** Financial quotas are determined to attain desired net profit as well as to control the sales expenses incurred.

**Net Profit Quota :** Net profit quotas are particularly useful in multiproduct companies where different products contribute varying level of profits. It emphasises on the sales force to make right use of their time. The following figure clearly depicts a selling situation in which a sales person optimally balance their time between high and low profit yielding products. Let us look at the following figure.

Figure 1

Ratio of Sales Volume to Net Profit

Product	Sales Price per unit	Profit Margin per unit (%)	Volume per month		Net Profit per month	
			Mr. A	Mr. B	Mr. A	Mr. B
Product X	Rs. 200	Rs. 140 (70%)	20,000	60,000	14,000	42,000
Product Y	Rs. 100	Rs. 40 (40%)	35,000	25,000	14,000	10,000
Product Z	Rs. 50	Rs. 10 (20%)	75,000	10,000	14,000	2,000
			125,000	95,000	42,000	54,000

This figure illustrates how important it is for the management to ensure that its sales persons do not spend more time on less profitable products, because the sales persons are costing the company the opportunity of earning higher profits from their high margin products. In other words, it should ensure that its sales persons spend their maximum time on more profitable customer. The objective can be achieved by setting a quota on net profit for its salesforce, and thus encouraging them to sell more of high margin products and less the low margin products.

**Expense Quota :** In order to make the salesforce conscious of the need to keep selling costs within reasonable limits, some companies set quota for expenses linked to different levels of sales attained by their salesforce. And to ensure its conformity they even link compensation incentives to keeping expenses within prescribed limits. Since sales are the result of the selling tasks performed which vary across sales territories, it is not easy to determine expense quotas as percentage of sales in a uniform manner. Also very strict conformity to expense quota norms result in demotivation of salesforce. As such expense quota is generally used as a supplement to other types of quotas.

**Activity Quotas:** Good performance in competitive markets requires the salesforce to perform the sales as well as market development related activities. The latter activities have long term implications on the goodwill of the firm.

To ensure that such important activities get performed, some companies set quota for the salesforce in terms of the various selling activities to be performed by them within a given periodicity. Finally the company must set a target level of performance for the sales persons. Some of the common type of activity quotas prevalent in Indian companies are as under:

Figure 2

Common Types of Activity Quotas

- Number of prospects called on
- Number of new accounts opened
- Number of calls made for realising company's account
- Number of dealers called on
- Number of service calls made
- Number of demonstrations made

The chief merit of activity quota lies in its ability to direct the salesforce to perform the "urgent" selling activities and "important" non-selling but market development related activities in a balanced and regular manner.

**Combination Quotas:** Depending upon the nature of product market selling tasks required to be performed as well as selling challenges facing the company, some companies find it useful to set quotas in combination of the two or three types discussed above. Rupee sales volume and net profit quotas or unit sales volume and activity quota in a combined manner are found in common use in a large number of consumer and industrial products companies in India.

**Activity 2**

A) Check whether the following statements are true or false :

Statement	True/False
1) Quotas are quantitative objectives assigned to specific sales units	.....
2) The only ingredient necessary for effective quotas is sound executive judgement	.....
3) Usually, the smaller the selling unit for which a quota is set the more effective it is as a device for directing and controlling sales operations	.....
4) One reason for not using quotas is that the product is in such short supply	.....
5) Activity quotas are appropriate when sales personnel perform important non-selling activities	.....

B) Tick the most appropriate answer

- I) Financial quotas are particularly appropriate when :
- 1) Management wants to emphasize the inspirational value of quotas.
  - 2) added sales volume is obtainable only at greatly increased cost.
  - 3) sales people perform important non-selling duties
  - 4) new products are being introduced.

- II) Sales volume quotas specify the sales level management expects to attain under :
- a) the worst possible circumstances
  - b) the most favourable conditions
  - c) somewhat less-than-ideal conditions
  - d) the average conditions existing in the past.

- III) If it is important for a company to maintain contacts with the customers who buy infrequently but in large quantities. Serious consideration should be given to using.....quotas.
- a) sales volume
  - b) expense
  - c) net profit
  - d) activity

- IV) Which of the following is NOT a reason for setting and using quotas.
- a) to motivate desired performance

- b) to provide more effective budgetary control
- c) to guarantee the attainment of objectives
- d) to provide quantitative performance standards.
- V) One of the crudest procedures for setting sales volume quotas is to base them solely on
- a) past sales experience
- b) expenses
- c) the sales forecast
- d) the market potential

**Check Your Answers**

A) 1 (True), 2 (False), 3 (True), 4 (True), 5 (True)

B) 1 (b), 2 (c), 3 (d), 4 (c), 5 (a)

**15.10 ATTRIBUTES OF A GOOD SALES QUOTA PLAN**

Usually, the sales department is responsible for establishing the sales quota, and no review or approval of a higher executive is needed. Within the sales organisation, the task may rest with any of several executives, depending on the size of the company, the degree of centralization in the sales force management, and the method used to determine the quotas. The chief sales executive may be responsible for setting the total company quota, but the individual breakdown may be delegated down through the regional and branch district managers. Or territorial sales potentials may be given to the branch or territory managers, and they set the salesmen's quotas.

There are several characteristics of a well-designed quota structure. Many of these attributes are the same attributes found in good compensation plans, territorial designs, organisational structures and other aspects of sales management.

**Realistic attainability :** If a quota is to do its intended job of spurring a man to the efforts management wants, the goal must be realistically attainable. If it is too high or out of reach, the salesmen may lose initiative.

**Objective accuracy:** Regardless of whether a firm is using volume, profit, expense, or activity quotas, they should be related to potentials. Obviously, executive judgement is also required, but it should not be the sole factor considered. If the men are to have faith in the performance goal, they must be convinced it was set impartially and based on factual, qualitative market assessment.

**Ease of understanding and administering:** A quota must be simple and easy for both management and the sales force to understand. A complex plan probably will cause friction and make the men resentful and even suspicious. Also, from management's point of view, the system should be economical and cost effective, to administer.

**Flexibility:** No quota ordinarily is a good one unless there is adequate flexibility in its operation. Particularly if the quota period is as long as one year, management may have to make adjustment because of changes in market conditions. At the same time, caution must be exercised to avoid unlimited flexibility, which may result in confusion and destroy the ease with which the system is understood.

**Fairness:** A good quota plan is fair to the men involved. As much as possible, the work load imposed by quotas should be comparable, but this does not mean that quotas must necessarily be equal for all men. Differences in potential, competition, and salesmen's abilities exist and, therefore, the performance goals may not be comparable by absolute measures. They can be compared but only in relative terms.



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## 15.11 SUMMARY

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### Relating Sales Forecast to Sales Quota

A sales forecast constitutes a critical component of the sales planning task of the company. To do this with desired accuracy, a detailed market knowledge and the existence of the comprehensive marketing information system are required.

Development of sales forecasts on product, segment, customer and geographical area basis enables a company to keep sales as planned. This lead to establishments of a quantitative goals relating to an identified sales unit for a specific period to time. The sales quotas also determined facilitate the carving of profitable sales territories and their management in the most in the most productive manner.

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## 15.12 KEY WORDS

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**Sales Forecast:** An estimate of Rupee or unit .sales for a specified, future period, under a proposed marketing plan or period.

**Market Potential:** The expected sales of a commodity, a group of commodities, or a service for an entire industry in a market during a stated period.

**Sales Potential:** The share of a market potential which a company expects to achieve.

**Sales Quotas:** The share of the company's overall sales job, which is assigned as a performance goal to some marketing unit in an effort to aid in the planning, control and evaluation of sales activities and effectiveness.

**Financial Quotas:** Financial quotas are those which set for desired net profit as well as to control the sales expenses incurred.

**Sales Efficiency:** A measure of performance to evaluate the relationship between sales volume or value and individual and total selling cost.

**Sales Volume Planning:** A means of allocating targets, expressed in quantitative terms, to individual sales persons to achieve overall sales volume objectives.

**Sales Targets:** A performance standard against which the degree of achievement can be measured. Targets are usually set on a geographical, product or customer basis in either selling quantities or sales performance terms. '

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## 15.13 SELF-ASSESSMENT QUESTIONS

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1. Discuss how sales forecasts, and sales quotas relate to each other.
2. What are the distinct advantages of sales forecasting. In your opinion does forecasting helps even when there is a recession in the industry. Discuss.
3. Give a comparative account of various types of sales quotas and identify the attributers of a good sales quota plan.

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## 15.14 FURTHER READINGS

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William J. Stanton and Richard M. Buskirk, 1905, *Management of the Sales Force*, Butterworth.

Richard R. Still, E.W, Cundiff, N.A.P Garoni, 1998, *Sales Management: Decision, Strategies and Cases*, Prentice Hall, New Delhi.