Optimizing Pricing Delegation to External Sales Forces via Commissions: An Empirical Investigation

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Abstract

In this article, we develop a model of external sales representative (ESR) behavior in the context of indirect lenders that sell auto loans through auto dealerships. Using this model, we examine the behavior of ESRs, focusing on the demand allocation and pricing decisions made by ESRs and the impact that commissions have on these decisions. The results indicate that ESR's decision to allocate customer demand is influenced by commissions provided by competing providers; however, the effect is smaller than suggested in the literature. Also, ESRs use a sequential decision-making process, first selecting a lender to allocate customer demand to and then choosing an option from the selected lender's menu of prices, rather than a simultaneous process, whereby pricing options from all providers are compared at the same time. Finally, optimal commissions increase exponentially with price to ensure that lender profits are maximized.

Keywords: *sales force compensation; sales force pricing delegation; consumer lending*

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