Multi-dimensional Salesforce Contracts with Negotiated Prices

Pranav Jindal
Indian School of Business
Minkyung Kim
CMU Tepper
Peter Newberry
University of Georgia

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Abstract

In settings where pricing is delegated to salespeople, firms may provide the salespeople incentives to not only sell more, but to do so at higher prices. In this paper, we study the relative importance of sales and pricing incentives, and quantify the profitability of different aspects of the pricing incentives. Utilizing data from a large durable goods retailer in the U.S., we outline and estimate a structural model of a multi-tasking salesforce where a salesperson jointly makes selling and pricing decisions (through negotiation) for multiple product types. The overall disutility from negotiating is comparable to that from selling, which makes salesperson effort allocation across selling and negotiating under each contract design nontrivial. Eliminating pricing (sales) incentives lowers the retailer's profit by 31% (8%) pointing to the relative importance of the pricing incentives. Additionally, eliminating different aspects of the pricing incentives, which vary in the extent to which they incentivize higher markups, results in lower profits for the retailer. Finally, we find that the salesperson's ability to reallocate effort across selling and negotiating hurts the retailer, but a move to fixed pricing, which eliminates negotiation effort completely, further lowers the retailer's profits.

Subject Areas: *Pricing, Retailing, Sales Force*

Track: Pricing & Promotions