



The Relationship between Discount and Win Rate

*An examination of the true relationship between discount and win rate,
and a more complete quantified view of the ultimate impacts of
discounting on revenue.*

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Winning by Design

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Abstract

The invention of SaaS and in particular the Recurring Revenue model, reduced what once required upfront investments of up to millions of dollars into a \$1,000 to \$50,000 monthly payment. As SaaS services became popular, the Recurring Revenue Model itself essentially was the discount! However, neither the buyer nor the seller fully understood the model's impact, and the buying and sales behavior stayed the same: they continued to extend the same discount strategy and execute the same processes without knowing or understanding the implications of doing so.

Fast forward to today, in November 2022, where we anticipate that the SaaS industry will experience the largest revenue churn event in its history. We are entering a time when discounts will be used to force a decision.

Discounting is based on the assumption that the increase in discount will be compensated by the increase in win rate, thus increasing bookings and, subsequently, revenue.

Thought #1: Will a discount actually increase the win rate?

Thought #2: What is the true relationship between discount and win rate?

In the analysis below, we present answers to these questions.

Research via Scenario Analysis

To run scenarios, we use a baseline Growth Formula based on the Winning by Design Bowtie Data model. The Data Model is published at www.TheScienceofRevenue.com.

	VM1	CR1	VM2	CR2	VM3	CR3	VM4	CR4	VM5	CR5	VM6
Scenario	Prospects		MQLs		SQLs		SALs	Win Rate	Wins	Discount	ARR(new)
Baseline	500	10%	50	20%	10	80%	8.0	20%	1.60	0%	\$32,000

Table 1. Baseline Growth Formula

The baseline of this Growth Formula says that it takes 500 prospects per month to generate eight opportunities each month. We will refer to these opportunities as Sales Accepted Leads (SALs), also known as Qualified Opportunities. The product is sold at a list price of \$20,000. These 8 SALs in this example convert at a win rate of 20%

into 1.6 wins. This generates \$32,000 in ARR(new) from 500 leads. The table below shows the impact of a discount on revenue. Unsurprisingly, it depicts how a 5% incremental discount results in a 5% reduction in ARR.

VM4	CR4	VM5	CR5	VM6
SALs	Win rate	Wins	Discount	ARR(new)
0.0	20.00%	0.00	0.0%	\$32,000
8.0	20.00%	1.60	5.0%	\$30,400
8.0	20.00%	1.60	10.0%	\$28,800
8.0	20.00%	1.60	15.0%	\$27,200
8.0	20.00%	1.60	20.0%	\$25,600
8.0	20.00%	1.60	25.0%	\$24,000
8.0	20.00%	1.60	30.0%	\$22,400
8.0	20.00%	1.60	35.0%	\$20,800

Table 2. Impact of discount on revenue (establishing a baseline)

How much would we need to increase the win rate to compensate for the revenue loss? In other words, with \$32,000 being the baseline, how much would be required to improve the win

rate? To examine this, we manually tweak the win rate until the ARR is getting close to \$32,000; that is, we increase the win rate to the point that it compensates for the loss in revenue.

VM4	CR4	VM5	CR5	VM6
SALs	Win rate	Wins	Discount	ARR(new)
8.0	20.00%	1.60	0.0%	\$32,000
8.0	21.10%	1.69	5.0%	\$32,072
8.0	22.23%	1.78	10.0%	\$32,011
8.0	23.47%	1.88	15.0%	\$31,919
8.0	25.00%	2.00	20.0%	\$32,000
8.0	26.65%	2.13	25.0%	\$31,980
8.0	28.60%	2.29	30.0%	\$32,032
8.0	30.80%	2.46	35.0%	\$32,032

Table 3. Improving the win rate manually to compensate for the loss of revenue due to discounting.

In the example, you will notice that when a 20% discount is given, we need to increase the win rate from 1-in-5 to 1-in-4. At a 35% discount, you need to improve to a win rate of 1-in-3 to compensate for the loss in revenue.

It is an incredible feat to make such improvements in win rate (typically, after an extensive training program and diligent implementation, an organization can improve the win rate by 10%, e.g., from 20% to 22%). This tells us that the increase in discounts can NOT cover the revenue gap created, as the win rate generally stays the same. In other words, organizations are just giving away money.

EXAMPLE

- | A platform sale with an ACV of \$24,000/year.
- | Ten sellers sell five deals a month each, on average.
- | They are across the board extending (extra) a 10% discount/deal.
- | Ten sellers * 5 deals/mo * 10% * \$24,000 are giving away \$120,000 in ARR/mo.

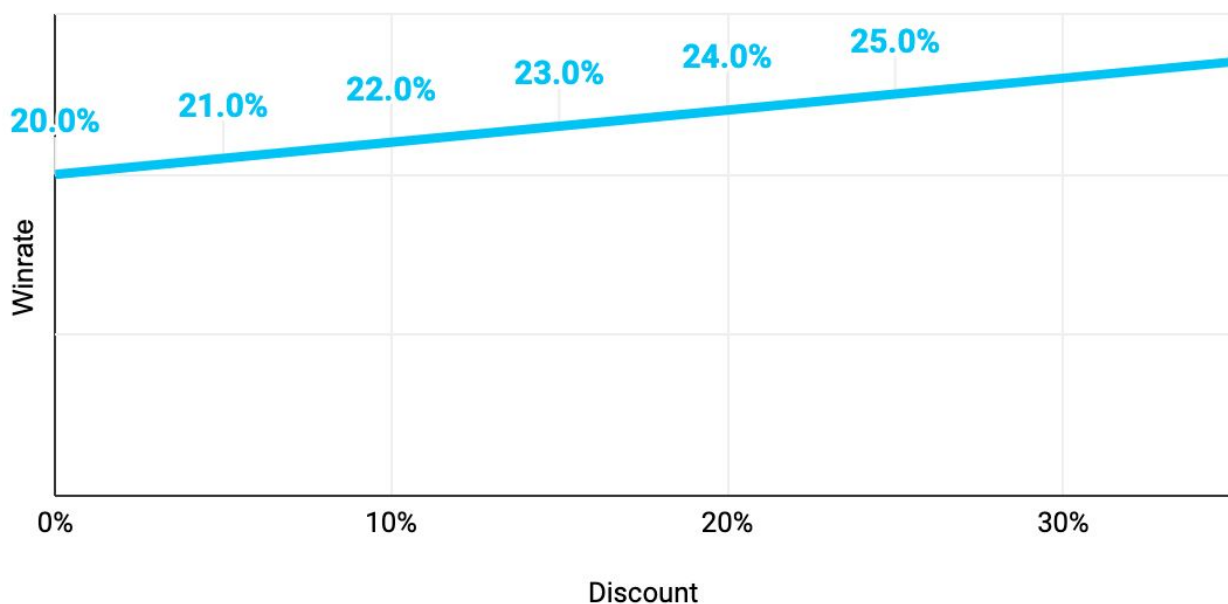


Figure 1. Visual example of the relationship between discount and win rate.

This model allows us to get an idea of the relationship between discount and win rate, through which we learn that for an increase in discount of 10%, you must improve the win rate from 20% to 22%, or an average win rate improvement of 10%. This sounds logical, right? But here's the rub: although we anticipate a

significant increase in the use and size of discounts over the next 60 days, we do not have any evidence that we can expect an increase in win rate.

The JOLT Effect

Recent work from the DCMi research team, based on the analysis of thousands of sales calls, shows that using a critical event, such as a discount, is more likely to *decrease* the win rate. In other words, discounting actually hurts the win rate. We know that ARR(new) results from multiplying multiple times using the Growth Formula. When you multiply a multiplication, the mathematical nature turns from a linear relationship to an exponential relationship. An exponential relationship indicates a disproportionate impact, in which several small changes cause a significant impact. The effect of this is demonstrated in table 4.

Increasing the discount to create a critical event causes a lower win rate. When combined, they accelerate the decline in revenue precipitously.

In this example, providing the client with a 20% discount results in a 10% decrease in win rate, resulting in a 28% decrease in revenue (from \$32,000 to \$23,040). For more information on the adverse impact of discounts on win rate, we refer to the research presented in the book “The JOLT Effect”.

VM4 SALs	CR4 Win rate	VM5 Wins	CR5 Discount	VM6 ARR(new)
8.0	20.00%	1.60	0.0%	\$32,000
8.0	19.50%	1.56	5.0%	\$29,640
8.0	19.00%	1.52	10.0%	\$27,360
8.0	18.50%	1.48	15.0%	\$25,160
8.0	18.00%	1.44	20.0%	\$23,040
8.0	17.50%	1.40	25.0%	\$21,000
8.0	17.00%	1.36	30.0%	\$19,040
8.0	16.50%	1.32	35.0%	\$17,160

Table 4. The JOLT Effect shows how discounting actually hurts the win rate.

Insights from Ted McKenna, co-author of “The JOLT Effect”

Discounts are a common tactic for combatting perceived indecision. In other words, discounts will rise not just because customer budgets are shrinking. Discounts make the deal cheaper, but reps misinterpret buyers using budget objections as indecision. Buyers say they want the discount, but more likely, they are stuck and posturing. Thus, the sales rep will mistake indecision as something that spreading Fear, Uncertainty, and Doubt will solve - represented by a discount. If the discount does work in closing a deal, when used in moderate to high indecision moments, the evidence shows an increased risk of post-decision regret from the buyer. For example, "I was still unsure about this, but took a chance on it because of the discount." Those situations create significant churn risk, initiating a separate set of costs for the organization.

A Simple Test

Ask your Finance department to provide you with the number of wins over the past month/quarter, the average selling price, and the discount applied to each deal. An example is at right (Table 5).

What you see is that the discounts given are high and rounded numbers, with an average discount of 20.8%. This is indicative of an untrained or undisciplined sales organization. Compare this to a more disciplined organization (Table 6).

What you will notice in a more disciplined organization is:

- Lower discount levels, often measured in single (not double) digits.
- Discounts are aligned to the size of the deal; smaller deals get less discount.
- The company got something tangible in return for the discount.

In the example above, across six deals, an average of 4.5% discount was given, which equates to \$39,331.

Deal	ACV	Discount
ACME Corp	\$19,600	20%
Amazing Blz	\$21,600	10%
Awesomeness LLC	\$39,200	25%
DeppSter Co	\$72,000	30%
MakeItHappen	\$19,600	20%
SaaSMaze	\$19,600	20%
	\$191,600	

Table 5. Overview of discount given per deal by an undisciplined organization.

Deal	ACV	Discount
ACME Corp	\$24,000	0%
Amazing Blz	\$22,800	5%
Awesomeness LLC	\$45,000	6.25%
DeppSter Co	\$92,571	10%
MakeItHappen	\$23,040	4%
SaaSMaze	\$23,520	2%
	\$230,931	

Table 6. Overview of discount given per deal by a disciplined organization.

Discount	Trade	Impact on Seller
2%	Payment terms N45 -> N15	Reduce DSO
3%	Commit by date x	Focus on other deals
4%	10 Reference Calls	Improve win-rate/reduce discount
4%	LinkedIn Post on Best Practices	Lead Generation
5%	Multi-year contract	Reduce churn

Table 7. Example of a Discount/Trade menu

Trade, not Negotiate

We encourage sellers to think of negotiation as trading and to think of discounts as price adjustments, thus making these price adjustments small. In trading, both parties give up something of value to be better off. By definition, trading is win-win. What do they trade for? There are many things a customer can do or say that will significantly help a business. References, case studies, social media mentions, PR quotes, and other items can form a menu of trading options at

different price adjustment levels (refer to Table 7).

Trading puts a price on discounts. Everyone knows what happens when we pay attention to the price of something – its value becomes apparent. So, when a customer isn't willing to make a PR mention and turns down the discount, the average discount rate across all sellers goes down.

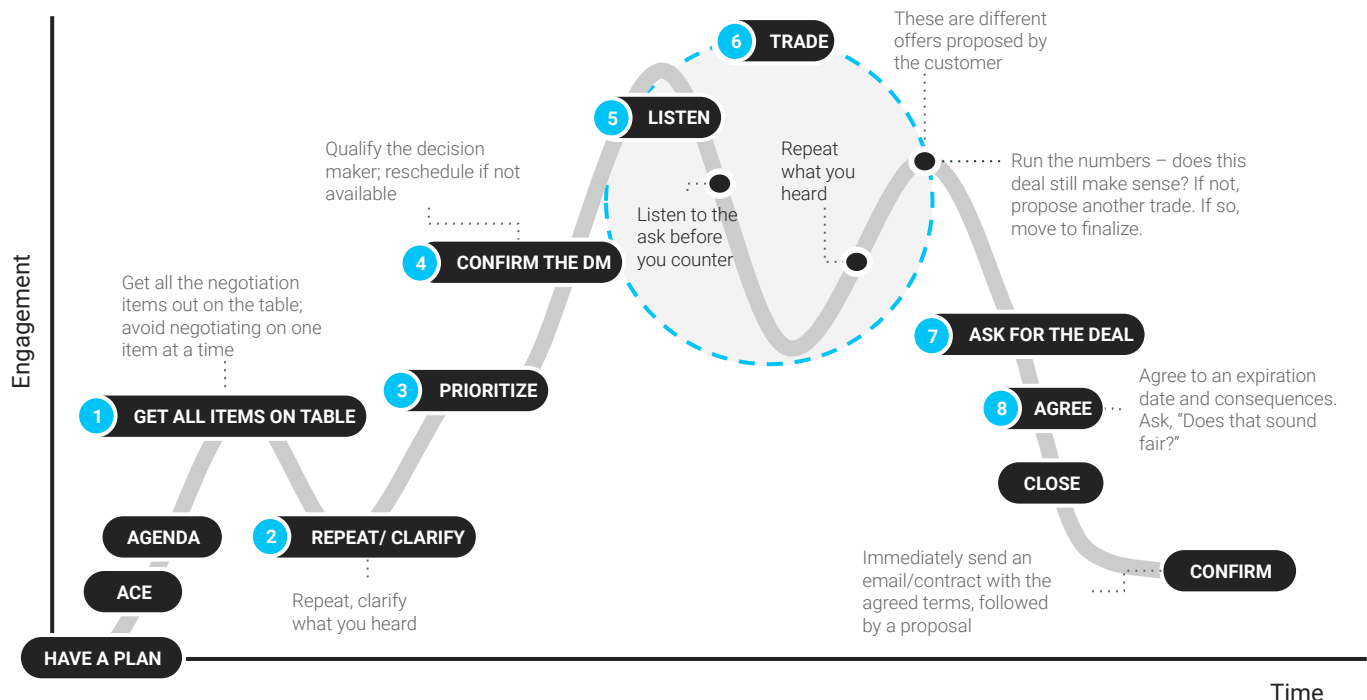


Figure 2. Blueprint: How to trade items of value.

Conclusion

Unless your team is trained on when and how to use discounts, it is very unlikely that the win rate will compensate for the loss in revenue. In fact, discounting ends up causing additional issues for the business down the road (e.g., churn) that have a negative impact far greater than just the initial loss in revenue from the discount.

Suggested Actions

1. Measure the average discount per quarter across your team, in order to understand the true impact of discounting on your revenue.
2. Train your sales team on the proper use of discounts via trading, and when to apply them.
3. Investigate and apply best practices from “The JOLT Effect” as a means of overcoming customer indecision, rather than using discounting as the solution.

About Winning by Design

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