What is the value of a lead?

Every firm needs customers, and every customer begins as a lead. So leads are fundamental to business success. But too many executives don't understand what leads are, or how to value them well enough to make smart investment decisions.

Leads are blocks of information connecting seller and prospect. Unless your business makes all its sales during a first inbound contact, you are going to have leads. But how you handle them—that's where the profit lies.

Leads are valuable. Firms invest a lot of money generating or buying them. But what should you pay for a lead? What is the price at which are you equally willing to purchase the lead or let it go to a competitor? Sales and marketing managers must understand a lead's value to avoid over-paying or under-buying sales leads.

Several approaches to lead value calculation are available, based on your firm's primary sales objective. Are you going for growth, market share, or profit? Your answer to this question will influence not only how you pursue sales, but also how to evaluate your sales leads.

Companies Going for Growth

Growth firms typically set their growth strategies by planning to generate a fixed number of sales. For example, a 1,000-customer firm targeting 30% growth wants 1,300 customers. Adding a few hundred to account for lost sales or cancellations, this firm may determine that it should try to acquire 500 new customers in the period.

To back your way into the number of leads required, divide the number of new customers by your close rate. If this hypothetical 500 new customer firm has a close rate of 10%, they need 5,000 leads. The marketing department's mission is to acquire them at the lowest possible cost. The value of a lead to this firm is the next highest price from any alternate lead source until the 5,000 lead target is met, and then zero once the full 5,000 leads are purchased. In short, the value of a lead for a growth firm is a step function: The lead value is very high until the growth target is reached, and zero thereafter.

When Your Objective is Market Share

Market share oriented firms are looking for their slice of the industry; it's not a fixed number of new customers. They will approach leads similarly to a growth-guided firm, but the target number will shift periodically as the market size shifts. Thus, the market share firm's goal will differ month to month.

The calculation is similar to the growth firm scenario, but it requires some fancy footwork to apply. Lead value will still be a step function, but the step size moves very quickly. You will still divide the number of new customers desired by the close ratio, but you'll be working with a very short term lead target. Because this target moves, the marketing department needs considerable flexibility to keep adjusting the lead requirements.

Firms That Strike a Balance

Most firms seek the highest number of profitable customers, irrespective of whether they are going for growth or share. These firms purchase leads to the point at which customer acquisition cost equals customer lifetime value. When these two goals reach equilibrium, the firm stops buying leads.

In such situations, you can compute the value of a lead by knowing your salesperson costs, your close rate, and the value of an account, and applying the following formula.

Lead Value = (Account Value – Salesperson Cost) * Close Rate

This is the lead pricing formula. With this in hand, plus an understanding of your primary sales goal, you will be well on your way to an accurate assessment of how much to pay for a lead.

Source: Jeff Feuer