5.7 Sales Activity Metrics - Part 3

Sales Funnel

Now we are going to look at an essential metric in the world of SaaS called Lead Conversion Rate. Before we jump into the numbers and percentages, we will discuss the Sales Funnel that you can see in the image.
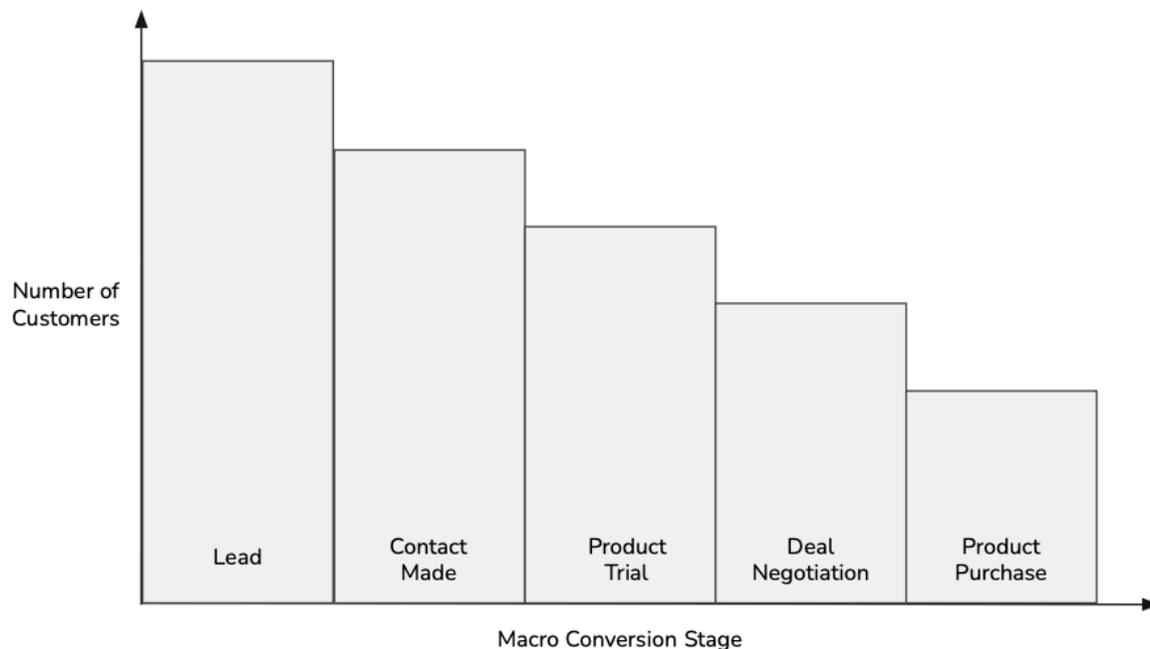
Sales funnel is a step-by-step process that describes the journey of a potential customer becoming an actual customer. It is divided into several stages, while each represents a closer step toward making a purchase.

- At the start of the funnel, we have our potential customers called 'leads.' These are the people who have shown some interest in our product.
- The first key stage after becoming a lead is making contact. These are the individuals we've reached out to, and because of this contact, they're now more likely to consider buying our product.
- Next comes the product trial stage. At this point, customers are trying out our product, usually through a free trial or a limited version, known as 'freemium.'
- Following that is the deal negotiation stage, where discussions about the potential

purchase take place. This might involve negotiating prices or terms of the service.
- The final stage is the product purchase. This is where leads who have gone through the previous stages decide to make a purchase and become paying customers.

As we look at this process from beginning to end, from a lead to a paying customer, we call these different stages "micro conversions'.

Each of these micro conversions gives us valuable information. We are able to calculate **Lead conversion rate** at each stage of the funnel meaning the percentage of leads moving to the next stage. Thus we can understand where in the process potential customers decide to move forward or drop out. Or in other words, we are able to identify where in the sales funnel we are the most effective and where we lose potential customers. Based on the findings, we can continually refine our sales process.

Lead Conversion Rate
- *the percentage of leads moving to the next stage*

Let's see how we can calculate the Lead Conversion Rate at each stage using a simple formula. We divide The total number of people who are moving to the next stage by The total number of leads at a current stage and multiply it by 100 to get a percentage:

$$CR = \frac{\text{Number of Leads Moving to Next Stage}}{\text{Total Number of Leads at Current Stage}} \times 100$$

Now we look at some scenarios from our imaginary Saas company. Take the Product Trial Stage as an example.

Product Trial stage:
- made contact with 300 leads
- 120 signed up for a product trial

$$CR = \left(\frac{120}{300}\right) \times 100\% = \boxed{40\%}$$

We managed to make contact with 300 leads from which 120 signed up for a product trial. The conversion rate for this stage is 40%.

Next, suppose we entered the Deal Negotiation stage with 10 000 leads and only 1 ended up purchasing the product.

Deal Negotiation stage:
- 10 000 leads
- 1 purchase

$$\text{CR} = \left(\frac{1}{10,000} \right) \times 100\% = \boxed{0.01\%}$$

The conversion rate for this stage is 0.01% which indicates significant issues and that something in this stage isn't working well. It could be the price, the way we present the final offer, or another factor that we need to investigate.

In general, a high conversion rate suggests that leads are positively responding to our efforts at that stage. Conversely, a low rate might indicate an issue that needs addressing.

The sales funnel offers us much more than just numbers - it can be a powerful planning tool. Take the overall conversion rate. If it's at 3%, it means that we successfully convert 3 out of every 100 leads into paying customers. By knowing this rate we can forecast and set achievable revenue targets.

Consider this scenario: Our goal is to generate 1,000€ in monthly revenue. Given that each customer contributes 100€ each month, we'll need 10 customers to meet this revenue target.
Our current conversion rate is at 3%. This means that for every 100 leads, only 3 become paying customers.

To find out how many leads are needed to secure 10 customers, we use a straightforward formula based on our conversion rate. We divide the number of paying customers by conversion rate:

$$\text{Required Leads} = \frac{\text{Required Paying Customers}}{\text{Conversion Rate}}$$

$$\text{Required Leads} = \frac{10 \text{ customers}}{0.03} \approx \boxed{333.33}$$

Rounded up, we'll need to engage with at least 334 leads to achieve our revenue goal of 1,000€ per month.

But that's not all. If we track conversion rates over successive months, it allows us to effectively measure our strategic progress. For example, if we notice a slight increase in our conversion rate from 3% in January to 3.2% in February, this change, though modest, indicates our sales tactics are improving.

Tracking conversion rates over months:
- January: 3%
- February: 3.2%

In summary, the sales funnel not only points out where we need adjustments, but also shows us the effectiveness of our efforts.