



## Return on Investment (ROI)

Most companies use Return on Investment (ROI) or its reciprocal, Payback, as a standard measure to compare one initiative to another. Given two similar opportunities, or when deciding whether or not a project is viable, management will usually use an ROI calculation.

$$\text{ROI} = \text{Profit} / \text{Investment}$$

There are differing definitions of ROI. Some companies use Net Income as the numerator (income after interest charges and taxes) and others use Operating Income (which does not include interest or taxes). Either of these definitions will work, so long as you apply it consistently.

Although the definition of ROI is fairly straightforward, capturing the quantitative data needed to calculate the ROI for a specific initiative is often very difficult.

We have attempted to simplify this process for you with an ROI Calculator. This calculator is designed to force you to think about all of the possible costs and benefits associated with each project.

Input all of the necessary data for each project. It will be very helpful to have the project sponsor complete this analysis because they are going to be more familiar with the expected costs and savings.

Not only will the ROI Calculator help you prioritize projects, but it will also force stakeholders to think through the project and identify potential risks.

All else being equal, initiatives with the highest return on investment should be of the highest priority. Closely scrutinize or eliminate initiatives that do not meet the “2:1” Rule of Thumb.

### “2:1” Rule of Thumb

*If the benefits of your proposed solution are not at least double the expected costs, then the project is not worth doing.*

There is a lot of information that you will need about each project before you can begin plugging numbers into the ROI Calculator. These include:

- Calculating the Total Cost of Ownership (TCO). **This is the total cost of the technology over the course of its lifecycle that identifies what you will spend.**

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- Calculating the benefits. **This step lays out all benefits and associated money gained or saved by these benefits.**
- Mapping out your project plan. **This process will reveal all of the hidden or overlooked costs that will affect your TCO, benefits, and your final ROI calculation.**

Listed below is the comprehensive list of costs and benefits that Info-Tech has included in our ROI Calculator. Not every one of these costs or benefits will apply to every project and we encourage you to add additional categories where needed.

### List of Items included in the ROI Calculator

#### COSTS:

- **Costs – Operating System**
  - Direct Cost – Purchased, Leased or Upgrade
  - Support and Maintenance Costs – In-House or Outsourced
- **Costs – Applications**
  - Direct Cost – Purchased, Leased or Upgrade
    - Packaged
    - Development Tools
    - Backup Applications
  - Support and Maintenance Costs – In-House or Outsourced
- **Costs – Hardware**
  - Direct Cost – Purchased, Leased or Upgrade
    - Servers
    - Desktop Computers
    - Backup Hardware
  - Support and Maintenance Costs – In-House or Outsourced
- **Costs – Other Capital Assets**
  - Direct Cost – Purchased or Leased
    - Communications Equipment – Phones, Internet Lines
    - Ancillary Items – Furniture, Power Supply, Cable
    - Building and Land Renovations or Leasehold Improvements
  - Support and Maintenance Costs – In-House or Outsourced
- **Costs – Consumables (Diskettes, CD-ROMs, Printer Cartridges, etc.)**

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- Direct Cost – Purchased or Leased
- **Costs – Staffing**
  - Management
    - IT Staff
    - Non-IT Staff
  - Planners and Analysts
  - Development Staff
  - Programming Staff
  - Data Conversion
  - Testing
  - Recruitment
  - Training and Tutoring
  - Consultant
  - Contractor
  - Support and Maintenance
  - Incentives
- **Costs – Other Project-Related**
  - Additional Insurance
  - Benefits Lost If Project Delayed

### **BENEFITS:**

- **Benefits – Increased Revenue**
  - Additional Sales
    - Better availability
    - New market
  - Sales That Would Be Lost Without the Project
- **Benefits – Staffing**
  - Staff No Longer Required
    - IT
    - Non-IT

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- Staff Time Saved that Can Be Used Elsewhere in the Company
  - IT
  - Non-IT
- Management No Longer Required
- Maintenance and Support Reduction
- **Benefits – Other Costs Saved**
  - Reduced Direct Materials Costs
  - Reduction in Interest Charges Due to Reduced Debtload
  - Office Space Saved
  - Other Office Expenses
- **Benefits – Inventory Reduction**
  - Reduced Interest Costs
  - Reduced Obsolete Inventory
  - Reduced Carrying Costs, Including Power and Land/Building Usage
- **Benefits – Improved A/R**
  - Reduction in Bad Debts
  - Increased Interest Earned by Faster Payment from Customers
- **Annual Benefit**
- **Annual ROI**
- **Payback**

### **Tips to Make ROI Work at Your Company**

- *ROI is a process. Establish a baseline upfront and come back to these calculations as you begin work on each project.*
- *Be prepared to tweak the ROI Calculator. Every business is different.*