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# Using ROI as an Effective Sales Tool

## How to Highlight the Economic Benefits of Your Solution

# Contents

## Introduction

This paper presents best practices for using ROI – return on investment – analysis as a sales tool with enterprise customers, particularly in the technology industry. It offers a general introduction to return on investment, a brief discussion of ROI's importance in the sales cycle, and some pointers on developing your ROI story to help customers understand and embrace your value proposition.

Why is ROI important and why does it continue to garner so much attention? Because it is a straightforward and powerful decision-making tool.

There was a time when technology vendors could expect to close sales based solely on innovative solutions. Nowadays, spending is more constrained across the board and enterprises demand a clear timeline for realizing a return on every investment. Vendors offering technology solutions must bring a strong ROI story to the table and be able to articulate it in ways that are compelling to the customer, leverage it throughout the sales process, and offer tools that champions within the enterprise can use to sell the benefits internally.

## Defining ROI

ROI is a method of calculating the economic benefits derived from a monetary investment, measured over a specified period. The investment might be dollars spent to acquire new technology, time spent training the workforce to use a new product, or opportunity costs incurred during sales channel downtime – any expenditure to which you can assign a monetary value.
The return might be increased revenue, costs savings, enhanced investment income associated with better allocation of capital resources, tax advantage – again, it only matters that a monetary value can be assigned.

$$\textbf{ROI} = \left( \frac{\textbf{(total economic benefits over ROI period)}}{\textbf{(total investment)}} - 1 \right) \times 100\%$$

The flip side of ROI is the payback period which calculates how long it took to make back the initial investment. Once the payback period has elapsed, benefits begin to accrue.

$$\textbf{Payback} = \frac{\textbf{(total investment)}}{\textbf{(monthly benefit)}} + \textbf{implementation time}$$

A final note – when calculating ROI, it is critical to look at cash flow, not income and expense, because of the way capital expenditures are depreciated over time. If the entire cost is paid up front, then that amount of cash will be out of pocket during the first year. At the same time, if the capital expenditure is depreciated over a multi-year period, then only a portion of the cost will hit the income statement in any given year, which would not reflect the actual cash flow.

ROI is only one among many tools available to investment decision-makers. Other popular techniques include Net Present Value, Economic Value Added, and Internal Rate of Return, to name a few. While it can generate a less precise financial analysis than some of the other tools, ROI is the most straightforward approach, so it is easy to use and readily understood. That makes it ideal for enterprises evaluating technology purchases.

## ROI as a sales tool

Long used by internal project champions late in the purchase process to support a *de facto* decision, these days ROI is more often addressed in the initial stages of the sales cycle. In today's economic climate, it is not unusual to see CFO or general manager sign-off required for expenditures as low as $50,000. Investments at any scale are closely scrutinized by finance teams charged with ensuring analyses and assumptions are solid. ROI has become a key element in justifying technology expenditures, creating an opportunity for vendors to leverage it in their value propositions.

## Assembling your ROI sales toolkit

Successful sales teams rely on standardized tools and techniques to create a pitch customized to each enterprise customer. Incorporating ROI analysis in the sales approach likewise uses one or more of the tools described below.

### *ROI model*

The heart of the ROI analysis is the model, typically a spreadsheet that simulates the enterprise customer's business model. Using a series of input variables representing the factors driving the business, the model calculates projected ROI benefits.

Ideally, the vendor sits with the enterprise project champion and together they populate the model with assumptions and input. In the case of a complex model, the joint conversation is necessary to ensure the vendor team understands all aspects of the customer's business challenges and to reassure the customer of their understanding.

### *Usage Guidelines*

Written usage guidelines help sales representatives get the most mileage out of the ROI model. Designed as a convenient reference tool, this document describes the model and its mechanics; includes a list of Frequently Asked Questions (FAQs); discusses specific strengths and weaknesses of the model; and lists common objections and how to address them.

### *White Paper*

The ROI model is a consultative exercise that is effectively supported by the ROI white paper. Conceived as a stand-alone document, the white paper introduces the reader to the vendor and the product line without assuming prior knowledge. It then describes the value proposition and walks through one or two customer scenarios that showcase the product's ROI.

### *Case Studies*

One of the most powerful tools for building credibility for the ROI value proposition is the case study. Ranging from one-sheet summaries to highly detailed accounts, case studies discuss how real customers have implemented your solution and document the returns on those investments, stepping through actual ROI calculations.

Developing case studies can be challenging when a product is newly available with a sparse track record and/or because customers are reluctant to share proprietary details. Consider broaching the subject of a public case study early in the sales cycle and building a participation requirement into the contract.

### *Testimonials and third-party data*

Enterprise customers contemplating substantial investments are looking for reassurance you're your solution will deliver as promised. Testimonials from happy customers can add tremendous credibility to your ROI story. Use them whenever possible. Third-party data can provide a powerful supplement to testimonials or, when necessary, substitute for them. This might include results from independent testing labs, findings from research studies, and opinions from credible analysts.

### *Training*

One of the key success factors to effectively using ROI in the sales cycle is the knowledge and comfort level of the sales representative. For this reason, training of the sales organization is a critical, but unfortunately often an overlooked step.

The author(s) of the model should train sales staff along with anyone else who might need to discuss ROI with customers, for instance, product managers and marketing teams.

## Key success factors

With ROI playing a central role in the enterprise sales cycle, every vendor is offering an ROI story and customers can start to feel like they've heard it all before. Paying careful attention to some key factors can help you rise above the noise.

### *Whose model?*

Increasingly, enterprises are developing their own ROI models rather than depending on those provided by vendors. Still, the vendor who brings their own model to the table can strengthen their position by:

- Demonstrating awareness of the customer's business needs and specific economic benefits associated with the solution
- Helping the internal champion develop and refine their own model, identifying gaps or omissions

And of course, in situations where the enterprise does not yet have a model of its own, the vendor's model can provide a foundation for building one together.

### *Simplicity versus complexity*

An ROI model should be sufficiently straightforward that customers can grasp it easily. At the same time, it must credibly cover all aspects of the value proposition. Achieving that balance can be challenging but is a crucial part of leveraging ROI as a sales tool.

### *Soft versus hard benefits*

In developing the ROI model, it is crucial to understand distinctions between hard and soft benefits and to balance them appropriately. Hard benefits are associated with specific budget line items, driving impacts directly and measurably to the bottom line.

Examples might include:

- Reducing the number of servers required to perform current operations
- Reducing the amount of network throughput required to perform current operations
- Savings in personnel costs
- Reducing outsourcing costs while maintaining current operations
- Reducing facilities or maintenance costs

Soft benefits impact the bottom line in less direct ways, for example, by increasing productivity of knowledge workers. A solution might increase productivity for the average knowledge worker by 5 percent, but it would be difficult to credibly translate that into a measurable benefit without positing follow-on actions, e.g., to restructure and lay off 5% of the workforce.

An ROI model built on hard benefits is typically perceived as more credible than one that primarily emphasizes soft benefits. There are exceptions, of course. An example is high-touch applications such as call centers, where increased worker productivity has a direct and measurable impact on the bottom line. Nevertheless, it can be tricky to support an ROI story relying exclusively on soft benefits. Whenever possible, emphasize hard benefits and let soft benefits provide icing on the cake.

### *Shortened Payback Period*

The days of payback horizons measured in years are long gone, never to return. Enterprises look for payback over two to three quarters and, while it can be challenging to establish, that kind of aggressive timeline is often the price of entry.

### *Reducing cost versus increasing revenue*

Vendors sometimes fixate on reducing customers' costs to demonstrate a solution's ROI, neglecting the fact that driving increased revenue can also represent an important opportunity. Cost reduction is typically easier to build a credible story around. In some instances, however, the new solution could open new distribution channels or position the customer to launch new products or services, thereby creating and/or expanding revenue streams.

### *Revenue versus gross margin impact*

Shockingly, many vendors incorrectly calculate the ROI potential of their services by simply counting increased revenue and dividing it by the investment in the product. This calculation fails to account for the Cost of Goods. The true measure of economic returns associated with increased sales is gross margin impact, not straight revenue.

### *Capturing all elements of investment*

Another common error vendors make is considering only the cost of their product or service, rather than the entire investment the enterprise needs to make. For example, a software license that costs $500,000 might require an additional $1 million in implementation costs to cover new servers, hardware, and professional services.

### *Tracking and measurement*

Once the sale is closed, the value of ROI analysis shifts to tracking. Building appropriate metrics into the project facilitates monitoring to ensure that targeted benefits are achieved. This reinforces the vendor's credibility with the customer and captures data that can be used in future sales engagements.

### *IT savings is only part of the story*

The ROI story as it pertains directly to the IT department is typically straightforward and because IT Is both purchasing and implementing the solution, the sales cycle is easier. But many technology solutions have beneficial impacts not only to IT but throughout the enterprise such as increasing operational efficiencies, enhancing sales efforts, or reducing marketing overhead. While this makes for a more robust ROI story it also means multiple teams must buy into the ROI value proposition, including acceptance of reduced budgets and/or increased revenue targets associated with implementing the new solution.

## A typical ROI story

The following example is derived from actual ROI models developed for IT vendors, streamlined to serve as a high-level illustration and disguised to protect confidentiality.

The actual model considered more than a dozen distinct elements of ROI. For purposes of demonstration, this version considers two benefits: increased bandwidth throughput and reduced server load. Samples of more comprehensive models are available at www.callan-consulting.com.

In this scenario, the vendor sells a product that increases the efficiency of corporate networks. Main benefits include increased bandwidth throughput and reduced server load. The technology will be deployed in an organization running several enterprise applications centrally on a server farm and will reduce the number of servers and the corporate network bandwidth required to run the applications.

Table 1 provides key inputs to the model and Table 2 provides an overview of the economic benefit calculation.

**Table 1. Scenario Inputs**

| *Model Inputs – Server Savings* | |
|---|---|
| Number of employees in enterprise | 100,000 |
| Number of server-based enterprise applications | 5 |
| Cost/incremental server | $20,000 |
| % of servers needing to be replaced annually | 25% |
| % of employees who access each application | 20% |
| % of concurrent use at peak, for employees using each app | 10% |

| *Model Inputs – Bandwidth Savings* | |
|---|---|
| Total first-mile bandwidth in MB/sec (w/out VENDOR) | 200 |
| Monthly cost for first-mile connectivity in MB/sec | $500 |
| % bandwidth utilization rate without VENDOR | 60% |
| % bandwidth utilization rate with VENDOR | 80% |

**Table 2. Economic Benefits Calculation**

| | *Non-VENDOR Solution* | *VENDOR Solution* |
|---|---|---|
| *Server Savings* | | |
| Concurrent users/application server | 40 | 400 |
| Concurrent users/VENDOR server | NA | 400 |
| Max. concurrent application users | 100,000 | 100,000 |
| # application servers needed for enterprise apps | 250 | 25 |
| # VENDOR servers needed for enterprise apps | NA | 25 |
| Incremental servers needed for enterprise apps | 250 | 50 |
| Annual incremental server purchase needs | 63 | 13 |
| Incremental server cost | $1,250,000 | $250,000 |
| ***Annual economic contribution of VENDOR*** | | ***$1,000,000*** |
| *Bandwidth Savings* | | |
| Total first-mile bandwidth provisioned in Mbps (no VENDOR) | 200 | NA |
| % bandwidth utilization rate | 60% | 80% |
| Actual throughput rate in Mbps | 120.0 | 120.0 |
| Required bandwidth provisioned to realize throughput | 200.0 | 150.0 |
| Monthly cost for first-mile connectivity in Mbps | $500 | $500 |
| Total bandwidth costs across organization | $100,000 | $75,000 |
| ***Annual economic contribution of VENDOR*** | | ***$300,000*** |

Table 3 illustrates the ROI profile of the solution. For simplicity the benefits are assumed to accrue linearly over time, but a real-world example would take into account the ramp-up time associated with the solution deployment along with other timing issues.

With a one-time solution cost of $1,000,000, inclusive of all incremental hardware, software and service components, the ROI is 30 percent in the first year of operations and the payback period is nine months.

**Table 3. ROI Summary**

| | *Monthly Contribution* | *Annual Contribution* |
|---|---|---|
| Server savings | $83,333 | $1,000,000 |
| Bandwidth savings | $25,000 | $300,000 |
| **Total Economic Benefits** | **$108,333** | **$1,300,000** |
| One-time cost of VENDOR solution | $1,000,000 | |
| **1st year ROI, %** | **30%** | |
| **Payback Period, Months** | **9** | |

## Conclusion and Recommendations

Gone are the halcyon days when technology vendors could survive and even thrive on innovation alone. Enterprise customers want to know how much and how soon they will see an economic return *before* they invest in new solutions. This puts ROI analysis front and center in the sales process. The successful vendor will make a credible ROI story part of their pitch.

To get the most leverage from your ROI story, embrace these guiding principles:

- Always bring an ROI model to the table, even where the enterprise is conducting ROI analysis internally. It builds your credibility and helps you guide the project champion's thinking.
- The ROI model is a tool to move customers through the sales process. Keep it simple enough to understand, yet comprehensive enough to tell the complete story.
- Equip your team with a complete set of ROI tools: the model, internal usage guidelines, case studies, testimonials and third-party data, and a white paper. And train them well to use the toolkit.
- Avoid common pitfalls that undermine the credibility of your ROI story, e.g., focusing on revenue rather than gross margin impact, or failing to account for all elements of the investment.
- Emphasize hard benefits over soft.
- The shorter the payback period you can demonstrate, the better.

Like any other aspect of business, effective use of ROI in the sales process requires a measure of expertise. Given its potential to reinforce your value proposition, it's well worth the effort and attention required.

To learn more about ROI and how to leverage it in your sales cycle, Callan Consulting offers additional resources including full ROI models and white papers developed for technology vendors, available free of charge or obligation at www.callan-consulting.com.