

It's All About the ROI (Return on Investment)

Customers frequently ask about ROI when migrating to IP Telephony and IP applications. Very often this is part of their standard business process – they have to be able to present an investment justification to their CFO (or the customer is the CFO). In order to support this process, providers have built elaborate ROI tools and offer support to help with the analysis. While one can debate the accuracy of these predictions, the opportunity to go through the assumptions and look at the resulting yearly cash flows is undoubtedly a valuable exercise to at least get a rough sense of the financial values and orders of magnitude involved. It also provides a tool to hold the appropriate managers responsible for the results of the investment.

But how does this apply to internal decisions on investments in your equipment provider business? Is ROI used to compare opportunities or are decisions just based on intuitive need and anticipated results for each individual investment? How are the benefits of small dollar investments versus large dollar investments evaluated? Are large dollar investments always assumed to have the biggest returns? In other words, given the opportunity to invest in your business how do you know you are using your investment cash most wisely?

Consider three very different types of “investments” and the ROI of each:

- Hiring an additional sales person
- Investing in a remote monitoring system to offer new service to existing customers
- Subscribing to a competitive database service to increase competitive win rates

An ROI analysis for each potential investment is provided below. While each vendor's results will be different based on costs and volumes, the intent is to compare the relative orders of magnitude of profit and ROI of each investment.

New Sales Person Investment		
Fixed Costs		
Base salary	\$50,000	
Loading for taxes, benefits, etc.	30%	
Total fixed costs		\$65,000
Variable Costs		
Commission rate (applied to total revenue)	10%	
Revenue from average sale (assumes 50 stations, \$600/station, 12% for installation)	\$33,600	
Expected number of sales per year for new salesperson	15	
Total new revenue	\$504,000	
Total commission costs		\$50,400
Total cost of investment		\$115,400
Profit		
Gross profit margin on sales	30%	
Profit on additional sales		\$151,200
Net profit (sales profit - investment cost)		\$35,800
ROI of Additional Sales Person ((return-investment)/investment)		31.0%

Remote Monitoring System Investment		
Costs		
System up front costs (one time)	\$30,000	
Technical staff (annual) to monitor and manage (assumes 1/2 person at loaded salary of \$80,000)	\$40,000	
Cost per customer system for interface port on monitoring system	\$50	
Installed base of systems to monitor	200	
Total cost of interface ports	\$10,000	
Revenues/Profits		
Annual charge per system for monitoring (assumes 50 ports, \$1/month per port)	\$600	
Annual revenue from monitoring	\$120,000	
Three year net present value of costs		\$139,474
Three year net present value of revenues		\$298,422
Net present value of improved cash flow (profit)		\$158,948
Average annual profit (3 year NPV divided by 3)		\$52,983
ROI of Remote Monitoring System ((revenue-cost)/cost)		114.0%

Competitive Database Subscription Investment		
Number of system sales per year (status quo)	50	
Revenue per system sale (assumes 50 stations, \$600/station, 12% for installation)	\$33,600	
Gross profit margin per sale	30%	
Average profit per sale	\$10,080	
Percent increase in sales with competitive database*	10%	
Annual increase in profits due to competitive database		\$50,400
Cost of competitive database subscription (annual)		\$2,000
Net profit		\$48,400
ROI of Competitive Database ((profit improvement-cost)/cost)		2,420%

* TelecomTactics users reported win rate improvements averaging 14% in Jan/Feb survey.

In summary, the three investments are expected to produce the following annual results:

Investment Opportunities	Profit (\$)	ROI (%)
New Sales Person Investment	\$35,800	31%
Remote Monitoring System Investment (average annual results)	\$52,983	114%
Competitive Database Subscription Investment	\$48,800	2,420%

It is reasonable to assume that these comparative results were not intuitive, meaning that managers would not have been able to guesstimate all of these values and the rank order of the ROI values unless they had previous experience with each type of investment. While there are always strategic issues associated with investment decisions that are not captured in the numbers (although some would argue that the only strategic issues are the numbers), there is no substitute for this type of comparison. Given this set of investment options, the clear winner is the competitive database subscription.

Readers who are interested in improving their ROI can take the **TelecomTactics ROI Challenge**. If anyone can demonstrate a better ROI than **TelecomTactics** for a similar investment amount (using an ROI analysis such as those shown above) the **TelecomTactics** team will provide the service free for one year. If you are interested in more information, including a web-based demonstration, contact **Bonnie Fairbrother** by email at <mailto:bfairbrother@t3igroup.com> or by phone at (973) 602-0181 or contact **Dennis Kelly** at <mailto:dkelly@t3igroup.com> or by phone at (973) 602-0180.



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