



Leveraging the Power of ROI to Boost IT Sales

An IDC White Paper

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THE POWER OF ROI

The power of return on investment (ROI) analysis lies in its ability to quantify the business benefits of an investment in terms that CFOs and other executives can readily understand — the cost savings realized as a result of the investment and the additional revenue generated. ROI analysis allows decision makers to compare investments in different elements of the business plan and make informed judgments on where to spend the budgeted dollars for optimal effect.

To sell into this business environment, IT vendors must be able to demonstrate the ROI that customers can expect from deploying their particular solution. When vendors try to make this business case during the sales cycle, they commonly base the ROI analysis on a series of assumptions of what the cost savings and additional revenue will be.

IDC has a better way. Instead of using questionable assumptions, we use the actual cost savings and additional revenue realized by existing customers to determine the ROI a prospective customer can expect from deploying a particular IT product or service.

For our ROI analysis, we use a proprietary methodology and model, which we have refined over the past 10 years in conducting more than 70 ROI studies for clients. To populate the model, we interview a number of customers, asking a series of questions about cost, revenue, and specific IT processes, including associated time and staffing requirements before and after deploying the IT solution. From the interview results, we can calculate the average cost savings and additional revenue resulting from the deployment as well as the average payback period and ROI for the investment.

Because the ROI analysis is based on actual customer experiences, it makes a far more compelling case than an approach that uses unverifiable assumptions. Additionally, IDC's reputation for objectivity and authenticity adds considerably to the credibility of the ROI analysis.

ROI: Today's Number 1 Buying Factor

The Web changed everything. In the old days, before ebusiness and certainly before March 2000, justifying IT projects was often driven by steady upgrade and replacement mingled with occasional bouts of panic, the last being Y2K. Technology choices were usually limited to at most three to five products each. Decision making was driven by compatibility, best of breed, or price. The value of the technology was often obvious and operational. The Web led to ebusiness, and ebusiness became important to every company's business and ultimately dragged IT and IT executives into the boardroom.

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For a time it was easy. IT acquisitions that directly led to building a Web presence were self-justified. Everyone had to have an ebusiness strategy to be competitive even if the business value of that strategy was fuzzy. In addition, the emergence of a dizzying array of technology, software, and services led to a Web presence without seeming to cost too much. The new companies that offered this new IT world were lining up behind each other to lead the way, hoping that the big enterprises (where the real money is) would follow once they had established themselves as the standard. IT products needed to be cool. In our first five years of conducting ROI studies, 90% of IT products revolved around management or collaborative software. It was plumbing, and had a great ROI.

With the growth in dot-coms came a desire to differentiate and brand around delivering business value. We all know what happened next. It became obvious to all, even Wall Street, that only a few of these companies were going to be profitable. When the growth slowed, these marginal companies started failing, and the companies that had sold a lot of gear to these companies (on credit, as investment) started to lose money as well. The big enterprises slowed their spending, and the down cycle deepened.

However, ebusiness lives on. Despite the hype and the early failures, companies benefit from ebusiness initiatives. The difference today is that cool doesn't count; we are back to the bottom line. All aspects of IT now benefit from a strong ROI story. IDC is conducting studies of the business value of a wide range of IT solutions, including storage, appliances, enterprise resource management, business-to-business and business-to-consumer ecommerce, Web services, management, and using application service providers. IT buying decisions must be based on compelling business criteria. Today an IT project, ebusiness or otherwise, is not considered viable unless it can show a substantial ROI.

WHAT BUSINESS VALUES TODAY

Businesses have returned to the basics. Slowed growth means less room for mistakes. Fewer customers mean each customer is more important. Lower profits mean less discretionary spending. Strategy is no longer an irrelevant factor; it has replaced coolness as the primary corporate value. For investors and prospective employees, the following strategic values are key today:

- **Vision.** Companies must quickly show a profit as well as a strategy for sustaining the advantages that make them profitable.
- **Growth.** The great thing about a recession is that it allows companies to have an acceptable excuse for not growing, but they better be able to identify when they have hit bottom because they will be expected to grow from that point on.
- **Control.** Executives who pin their companies' failings on the market, the economy, or some other external cause are passé.

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ROI BASICS

ROI is a technique that allows companies to evaluate uses of capital. The idea is that a company can then compare its capital investments based on which investment is most profitable. It is the same criteria a board uses when it is deciding how to best use its profits. It enables rational decision making by putting everything in terms of a common factor — namely dollars. In this way, ROI also quantifies the impact on the organization's business as a result of implementing change. It thus enables CEOs to compare the impact on their companies of purchasing two new trucks to conducting companywide sales training to launching a Web-based, supply-chain management application.

The following criteria validate an ROI analysis:

- **ROI must capture all costs, direct and indirect, associated with the project/technology.** This includes products and services devoted to direct support.
- **ROI must be based on quantifiable results.** The baseline metric is the dollar. Often we get there by calculating time saved; time is money.
- **ROI must be based on observable results.** Automation has business value only when we can see the results — faster production, higher quality.
- **Each company will experience a unique ROI.** Despite identical investments, no two companies will reap identical returns.
- **Each product yields a unique ROI.** Technology is too complex and changes too quickly to expect uniform results from even the most standardized or commoditized products.
- **ROI methodology must be consistent.** Quantifying changes and establishing a set of assumptions for growth, salary loading, and time value of money should follow a consistent approach.
- **Companies should always lean toward the conservative when estimating savings.** This approach helps when companies are being challenged.
- **The numbers tell the story, but not the whole story.** Some benefits may not be quantifiable today in terms of dollars (e.g., ease of use, competitive advantage, and customer loyalty). However, these benefits are still worth including in the value story and creative thinking process as to how to quantify in the future.

How ROI Delivers the Three Most Important Business Values

The power of ROI is that it enables the IT vendor or the IT vendor's customer, the IT executive, to win in the boardroom. A proper ROI analysis elevates a vendor's argument from "We can do cheaper or better" to "We can help you maximize your assets, increase profitability, and grow your business. Not only that, but we can help you convince your executive management that buying our product is good for the business."

How Do I Maximize My Assets?

Despite the recent economic downturn, U.S. productivity continues to rise. Is this a result of IT delivering on its promise? IT was supposed to enhance productivity. One of the key values for evaluating ROI then is productivity, which we define as increasing the percentage of time employees spend in activities contributing to the success of the business. The measure of productivity is employees' time and the value of that time based on the employees' salary.

Web-delivered software and services will have the most positive impact on productivity once standards enable widespread adoption. Examples include software that automates administrative functions, such as filling out forms, ordering materials, and documentation.

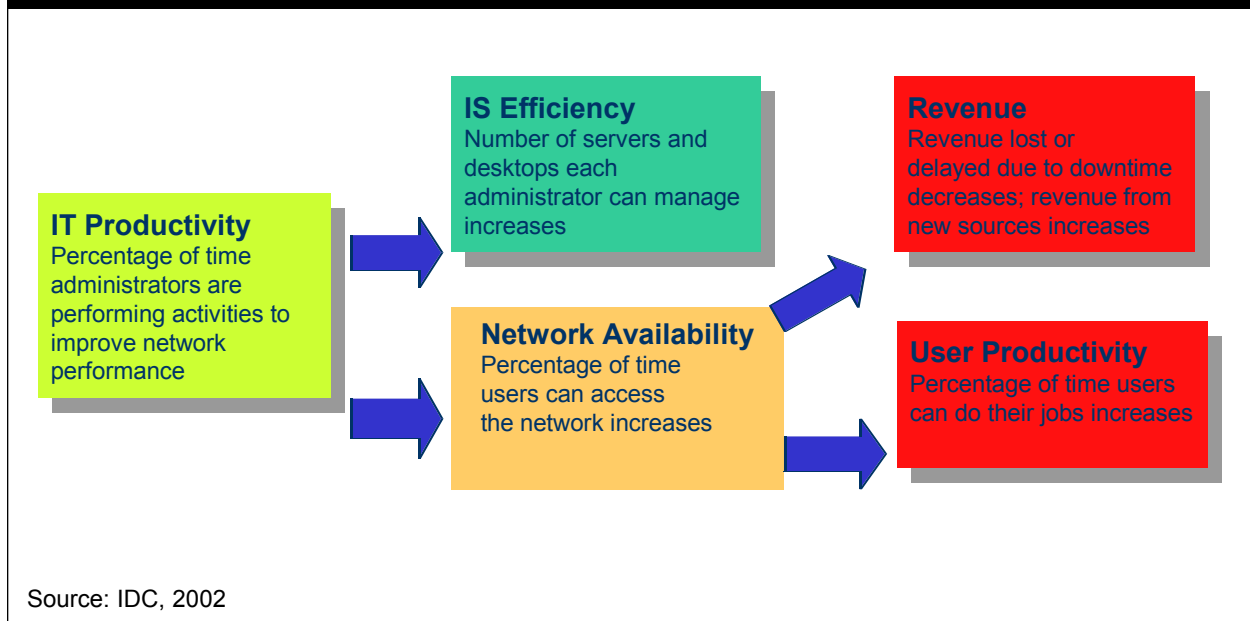
The new generation of content delivery technologies enables employees to attend meetings and training without travel time. Our studies have shown that companies have enjoyed from 2% to 5% across-the-board increases in productivity.

While technology becomes more distributed because we want those closest to our customers to be the best-informed and best-equipped members of the corporate team, there has been a move to centralize the creation, distribution, and control of information. Centralized control allows all those involved with the administration and management of information to reduce their travel time as well as the time spent on nonproductive activities. Over the past 10 years, our studies have shown that the implementation of network and system management tools has shifted 24% of IT staff time from nonproductive activities, such as software upgrades, server and client configuration, troubleshooting, and help desk operations, to more proactive activities, such as network upgrades, capacity planning, applications creation, Web-site creation, and ebusiness implementation. The result is a proactive IT staff, which lowers downtime, employee turnover, and training costs and boosts customer satisfaction.

Increasing productivity creates hours in the day, adding an average of 18.4 hours per year per employee. Another benefit is that the employees are more satisfied doing what they were trained to do; this satisfaction results in reduced employee turnover and the cost associated with recruiting and retraining staff.

Productivity applies to all parts of the company. The sales force should be in the customers' face, not filling out forms. Having more time to devote to business-productive activities results in more sales calls, faster turnaround of orders, shorter billing cycles — all quantifiable benefits that contribute to ROI (see Figure 1).

Figure 1: Productivity Leads to Financial Benefits



Source: IDC, 2002

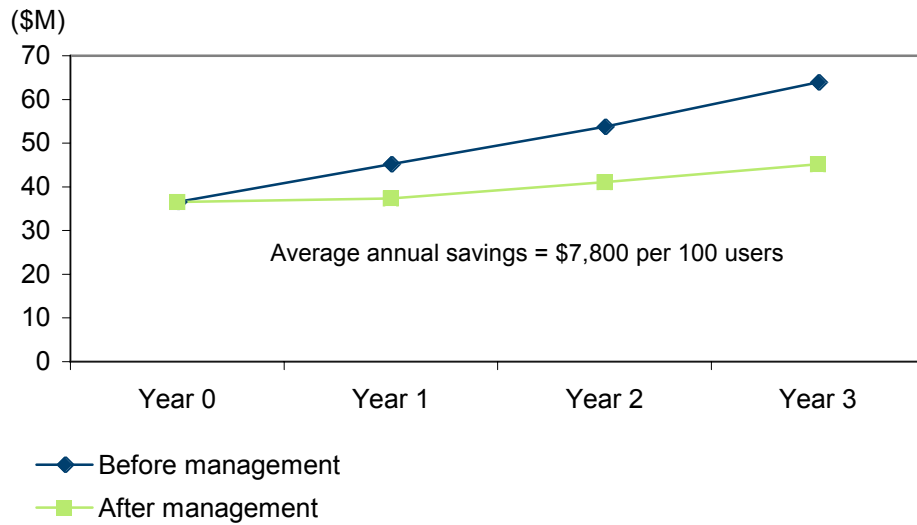
How Do I Increase Profitability?

The dramatic change in the economy from 2000 to 2001 has revised the yardstick for success. Growth is out, and profits are in. In times of flat growth, companies look to reduce costs to retain profits. This makes the funding of any new projects doubtful. However, if by investing in technology companies can reduce the real costs, they have a very good chance of getting the funding. Implementation of IT reduces costs in three ways:

- It reduces the cost of ownership by extending the life span of equipment, increasing scalability, and reducing the maintenance costs or consolidation.
- It reduces travel, which decreases the real dollar cost of airfare, lodging, and meals.
- Most significantly, by increasing productivity, support staff can support more with less. In other words, companies can save the total salary of staff through layoffs, growing staff more slowly than revenue or reallocation (again optimizing utilization of assets). This tends to create the greatest reductions because people usually make up the largest single budget item (62% of total IT spending on average).

In our studies, we found that companies were able to grow their IT staffs at only 10% per year while extending their networked assets to 19% more IT users per year and enjoying 82% increased annual demand on their Web sites (see Figure 2).

Figure 2: IT Staff Savings Due to Increased Efficiency



Source: IDC, 2002

How Do I Grow My Business?

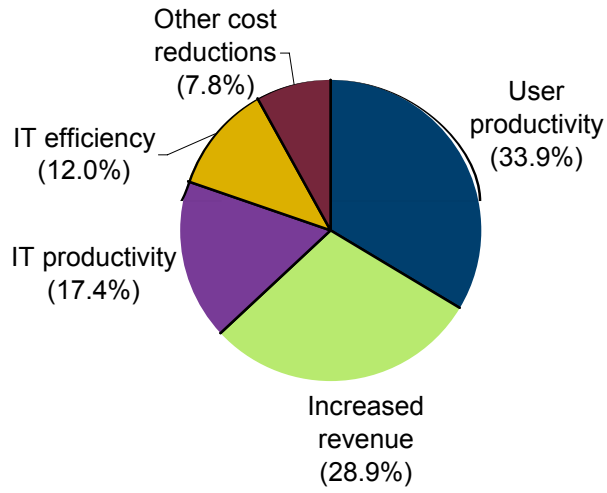
What will a more productive employee base supported more efficiently do? Generate revenue. This takes two forms.

Revenue Protection

The primary source of lost revenue is unplanned network downtime. On average, increasing availability by .1% generates \$1 million per year in a large enterprise. As ecommerce becomes more prevalent, the value of downtime becomes more expensive and accounts for a larger portion of a company's revenue. While we tend to quantify downtime as simply lost revenue proportional to total revenue (one hour of downtime per day means a loss of between 4% and 12% of the revenue for that day), downtime also results in lost future revenue, as customers tend to gravitate to more reliable competitors.

For network service providers, downtime is even more costly. Excessive downtime is the number 1 reason for switching service providers. Over the last 10 years, nearly 30% of the savings generated by products that IDC has evaluated has been related to reducing lost revenue. Our study of the ROI for Web hosting revealed that lowering downtime was the primary reason enterprises outsourced their Web centers and the only reason for switching service providers (see Figure 3).

Figure 3: Financial Benefits of Managing Networks



Source: IDC, 2002

GENERATING REVENUE

The true bonus in ROI is earned when companies can create revenue at a faster rate by reducing time to market or shortening production cycles. Where IT is directly associated with the corporate business operations, it can be shown that IT speeds the business processes of design, production, distribution, billing, and collection. IT allows business to produce more revenue over time without adding overhead.

Change the Business Model, Turn Overhead into Revenue

The lure of ebusiness is not only to create additional sources of revenue but also to change the business altogether. This is not restricted to designed revenue centers; any operational function can be turned into a profit center by being very efficient and developing excess capacity (e.g., developing the best online billing department in the world and then offering outsourced billing services to other companies).

TELLING THE STORY

The best ROI story is useful only if the right audience hears it. The highest ROI for developing a strong story is achieved by those companies that employ the right communication vehicle and put everything behind it. It cannot be an isolated or limited marketing approach but rather a public commitment to enhancing business value. Educating the buying public on the business value of a particular technology requires a widespread campaign, spearheaded by white papers, Web presence, analysts, and customer events. Taking that message to specific customers is optimized by the use of ROI sales tools, which provide a full range of support to every phase of the acquisition process — from proof of concept to configuration and cost comparison to complete investment justification.

Five Things a Strong ROI Story Will Do

The following list details five things a strong ROI story will do for IT vendors:

- **Deliver financial justification to customers** — Provide customers with justification for choosing the product rather than reasons why the product is better than competitors' offerings.
- **Shorten the sales cycle** — Cut out the comparative bells-and-whistles pitch and line item evaluation and cut right to the business reasons for deploying the product.
- **Turn the sales force into ROI consultants** — Elevate the salespeople by enabling them to make a strong business case for the product.
- **Project the value of the product** — not simply the cost.
- **Establish objective evaluation for benchmarking** — A standardized rigorous approach to ROI based on logical results provides a compelling and objective argument for the product.

CONCLUSION

We no longer have to spell out ROI to describe what it means to information technology. CIOs and IT managers have to prove how their departments deliver value to the company. IT technology providers want to compete as partners to the CIOs, to tell the ROI story.

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