Value: How to Project & Measure ROI in an Outsourcing Engagement

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Return on investment, or ROI, is one of the most recognized of all the financial measurements and ratios in the world of business finances and accounting. It's the standard that's used by business owners and entrepreneurs to determine how they will utilize their limited resources in order to maximize their business opportunities and profits.

The main resources available to any business are money and time. In order to save both, many Los Angeles and Southern California business owners and executives today are choosing to outsource many tasks that they have traditionally performed in house. These tasks typically include things like payroll processing, marketing and advertising, research and development, computers and IT, and CFO services.

Perform a Cost-Benefit Analysis

Before deciding to outsource tasks like these, though, a business should determine what kind of ROI can be expected from the investment they make in the outsourced services provider. Doing so involves carefully analyzing both the costs and anticipated benefits of the outsourcing engagement in order to ensure that they will receive the most value from the engagement.

Analyzing the cost of an outsourcing engagement is fairly simple: Prior to the start of the engagement, the outsourced services provider should provide you with a firm price quote. Be sure to ask whether this quote is all-inclusive or if the provider will be adding on other costs that you might not be anticipating, as well as re-billing you for expenses incurred during the engagement.

Keep in mind, though, that in addition to a financial cost, there will also be a time cost to your business when you engage an outsourced services provider. You and your team will need to spend some amount of time bringing the provider up to speed on the workings of your business so he or she can perform the task adequately, and continue working alongside the provider throughout the course of the engagement.

Quantify the Anticipated Benefits

On the other side of the ROI equation, you and your team should sit down and quantify all of the benefits that you expect the outsourcing engagement to bring to your firm. These may include:

Greater cost control — Outsourcing can help you control capital costs by converting fixed costs to variable costs. At the same time, it can free up capital that can be invested in other more productive areas of your business.

More efficiency — There's often a high price to be paid for trying to do everything internally. Most small and mid-sized companies don't have the structure or scale to perform tasks as efficiently as an outsourced service provider can.

Lower overhead — Doing everything internally requires a lot of overhead — office space, salaries, benefits, etc. When compared with these ongoing overhead costs for the performance of non-core functions, the cost of outsourcing is usually a bargain.

Staffing flexibility — This is especially beneficial for companies that experience seasonal and cyclical fluctuations in sales and workflow. By outsourcing, they can tap into external resources when needed without committing to them on an ongoing basis. As an added benefit, internal staff can learn new skill sets by working alongside outsourced service providers that they can put into practice after the engagement is complete.

A more level playing field — Outsourcing may enable small and mid-sized firms to access the same high-level expertise that big companies can retain on their staff. While large firms are often able to hire the best marketing experts as full-time employees, for example, a smaller firm can tap into the expertise of an outsourced marketing specialist at a fraction of the cost of building an internal marketing team.

A focus on your core competencies — While difficult to quantify, this may be biggest outsourcing benefit of all. Payroll, for example, was one of the first non-core business functions that companies commonly started to outsource. Payroll is an essential but non-core business function, so companies in the '80s and '90s started turning to payroll service providers to perform this task for them. This freed up resources to spend more time focusing on the things that add value to the business.

Where possible, place a dollar value on each of these benefits, even if it's just a subjective estimate. Then perform a standard cost-benefit and ROI analysis by subtracting the costs from the benefits, assuming that the benefits outweigh the costs, to come up with a dollar value to your business of the outsourcing engagement. Conversely, if the costs outweigh the anticipated benefits, you'll need to reexamine whether the outsourcing engagement is wise for your company.

Concluding Thoughts

Many Los Angeles and Southern California business owners and executives today are choosing to outsource many tasks that they have traditionally performed in house. Before deciding to outsource tasks, a business should determine what kind of ROI can be expected from the investment they make in the outsourced services provider. Doing so involves carefully analyzing both the costs and anticipated benefits of the outsourcing engagement in order to ensure that they will receive the most value from the engagement. An outsourced CFO services provider can help you perform a cost-benefit and ROI analysis to determine the value of an outsourced engagement to your firm.

About CFO Edge

CFO Edge, LLC delivers enterprise-class financial and operational performance solutions to executives throughout Southern California. Based in Los Angeles, our formerly-seated chief financial officers engage on demand as part-time CFOs, single-project CFOs, and interim CFOs to help business leaders successfully resolve pressing challenges and realize their financial and operational goals. At CFO Edge, we're passionate about helping our clients create, grow and sustain value. For more information, visit www.cfoedge.com or call 800.276.1750 Ext 101.