ROI Definition i.e. Financial Outcomes Definition

KINDUZ

1. Why this release of ROI Definition?

Over the last decade KINDUZ has worked with Fortune 500 companies such as DB Schenker, LafargeHolcim, Pfizer, Bharat Petroleum, GlaxoSmithKline including multiple Small and Medium Enterprises (SMEs), among others and have delivered over US$ 670 million of ROI that has positively impacted their P&L, which have been signed off by their Finance Organizations.

As an organization, our Return to Investment Ratio within a span of 26 months is:

- at a target of 3 : 1 i.e. for every dollar invested on KINDUZ, we target to give back $3 to our customers
- at a median of 8 : 1 i.e. for every dollar invested on KINDUZ, we have given back $8 to our customers
- at a highest of 38 : 1 i.e. for a dollar invested on KINDUZ, at a highest we have given back $38 to one of our customers

We work towards delivering at least:

- ~3% of your Revenue as additional EBIDTA within 14 months of engaging us;
- and additional ~5% of your Revenue as additional EBIDTA between 15 months to 26 months;
- and we do it in such a way that it is repeatable each financial year.

Given the success we have had with our beloved customers and the brand we have created for delivering 'Outcomes' in the industry, there have been numerous requests from various organization for access to our ROI Definition document.

While we realize that this is one of the core part of our Intellectual Property (IP), we also realize the amplitude of benefits this document will deliver for the industry. Given our Purpose of 'Creating Universal Prosperity', we have consciously decided to release this IP into the public domain, with our Copyright being applicable.

Feel free to use the information given below. A lot of the stuff is simple and common sense (which is said to be uncommon). Yes, we have made mistakes in our engagements, and learnt from them, but never at the cost of the customer. We have burnt our fingers while protecting our customers. That's how we work, with 'True Intent'. This piece of thought leadership contains a lot of our learning, small and big.

2. Introduction

There are different ways the industry defines Return on Investment (hereinafter called as 'ROI' or 'Financial Outcomes').

Typically, ROI in the industry is defined as a ratio of (Gains – Investment Costs) / Investment Costs

Let's start by defining a few parameters first.

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1. **Gains:** Organizations work toward improvements. Improvements for better Customer Outcomes, improvements for better Financial Outcomes, Societal Outcomes and more. From these improvements come 'Gains', also called as 'Savings' or 'Benefits'
2. **Investment Costs:** In order to obtain the 'Gains', organizations usually spend a certain amount of money towards enhancing their technology, processes, people capabilities etc. These expenses are termed as 'Investment Costs'
3. **Additional Gains:** @ KINDUZ our love is to deliver 'Additional Gains' i.e. Gains in addition to what you are already working towards and what you are already delivering
4. **Success Fee:** @ KINDUZ we love to put our skin in the game i.e. share risks along with our customers. This is a core DNA of our organization and we do not back away from sharing risks. When we share risks along with the customer, the rewards are also shared along with the customer, when the customer receives them. A success fee ties the success of KINDUZ and its consultants, to the success of the Customer's Organization.
   Success Fee is usually a percentage (%) of the Additional Gains

KINDUZ prefers to keep things very simple.

In case KINDUZ is engaged on a Fixed Fee engagement, the 'ROI' or 'Financial Outcomes' is calculated as = Additional Gains – associated Investment Costs

In case KINDUZ is engaged on a Business Outcomes engagement i.e. an engagement where KINDUZ shares risks by reducing its Fixed Fee, given which a Success Fee is paid to KINDUZ on delivering ROI to our customer(s), the 'ROI' or 'Financial Outcomes' is calculated as = Additional Gains – associated Investment Costs – Success Fee. In this particular scenario the estimated ROI is comparatively lower, when compared to the Fixed Fee engagement due to the associated payments of a Success Fee.

The definition of 'ROI' is further detailed as below.

3. Additional Gains considered for ROI Calculations

Only those Additional Gains are considered for ROI calculations that can be attributed directly due to the Projects undertaken in a Program. All Additional Gains will be estimated as a part of the Project Identification Phase by ~~KINDUZ, and~~KINDUZ and will be jointly validated by the Customer's Finance team and KINDUZ during the Project Identification Phase.

The additional Earnings Before Tax (EBT) will be the base for calculating the Additional Gains for each improvement undertaken in each project. Additional EBT brought in will be calculated for each improvement, which will then be consolidated for each project, which will then be consolidated for the entire Program. This should not be confused with Earning before tax (EBT) at an organizational level, as organization level EBT will also take into consideration overall organization level expenses such as but not limited to OPEX, CAPEX, Interest, Depreciation, Amortization expenses which may not be related to an improvement Program and/or Project and/or related activities.

During the Project Initiation Phase, each project will have clearly identified metrics that will measure the Additional Gains to be delivered for the organization (for e.g. Days Sales Outstanding (DSO), Days Payable Outstanding (DPO), Days Invoice Outstanding (DIO)). Each of these metrics in each project, will have clearly defined Operational Definitions that will be mutually agreed upon between KINDUZ and the Customer. Given that each project will have different metrics, this will need to be discussed on a case-to-case basis once the Projects and relevant metrics are identified.

3.1 Cash Flow Improvement:

Any improvement and/or acceleration in cash flows due to, including but not limited to

I. Reduction in working capital requirements
II. Reduction in Cost of Capital through
   - Reducing Days Invoice Outstanding (DIO) for the Organization
   - Reducing Days Sales Outstanding (DSO) for the Organization
   - Increasing Days Payable Outstanding (DPO) for the Organization

III. Collection of outstanding cash from all relevant stakeholders

3.2 Cost reduction:

Any cost reduction due to, including but not limited to

I. Reduction in selling, general and administrative expenses [for example: Reduction in salesforce transport cost, Reduction in communication costs, Reduction in power consumption and facilities costs]
II. Reduction in cost of inventory [for example: Reduction in working capital locked in the inventory held in the warehouses, Reduction in inventory carrying cost, Reduction in losses due to expired and/or damaged inventory, reduction in Customer returns, better forecasting, implementation of Just In time for raw material]
III. Reduction in Cost of Goods Sold [for example: Reduction in raw material procurement cost, Reduction in cost of human resources, Improvement in yield of products, reduction in logistic costs]
IV. Debt Restructuring leading to reduced interest costs
V. Reduction in penalties
VI. Reduction in payments due to legal issues
VII. Reduction in Detention Fee, Demurrage Fee

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VIII. Reduction in Loss due to Ullage and/or Pillage
IX. Reduction in vendor and supplier costs (if required by working with them to reduce their costs)

3.3 Cost Avoidance

Additional Gains from Cost Avoidance due to, including but not limited to

I. Reducing losses of assets in good condition (e.g. Good spares in scrap)
II. Productivity improvement
III. Defect reduction
IV. Avoidance of Capital Expenditure [for example by improving Overall Equipment Effectiveness, improve capacity of production plant, improve storage capacity of warehouse, improve turnover of inventory, refurbishment of scrapped equipment]
V. Avoidance of Operational Expenditure [for example by reducing non-value added work of workforce]
VI. Hedging against currency fluctuation

3.4 Revenue Growth

Additional EBT generated from revenue growth is included as a part of Additional Gains. Any revenue growth due to, including but not limited to:

I. Growth in sales due to increase in production of product(s) [For example: Removal of constraints in the production of a high-selling product, thus meeting the sale demands of the external market]
II. Growth in sales by addition of new Customers [For example: Additional Sales in new markets and/or with new Customers; Additional Sales due to Customer referrals]
III. Growth in sales among current Customers [For example: Additional Sales due to us being selected as a Strategic Partner with a Customer, during the Vendor consolidation process at the Customer's side, Additional Sales generated from Solutioning]
IV. Growth in sales among ex-Customers [for example: Bringing back ex-Customers to buy again from the organization]
V. Increase in Selling price thus resulting in higher Margins [For example: Selling premium products or customized products which are sold at a higher price thus bringing in additional Margin, Increase Selling price and thus increased margin due to additional Value Added Services]
VI. Growth in sales due to increased customization [For example: Working with the Customers to create better solutions for them]

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VII. Cross selling [for example: Increased sales by selling other products of the organization to current Customers]

VIII. Growth in sales due to new offerings [For example: Selling New products, Selling New Services, Selling Productized Services, Selling Services around Products]

IX. Indirect Revenue growth. [For example, Investments in Financial Instruments, Management of Currency Fluctuations and Metals, selling excess raw materials to competitors]

X. Reduction in Revenue Losses [for example: due to penalties imposed by Customers, due to loss of Customers, due to shut down of the plant due to regulatory reasons or audit non-conformances]

3.5 Replication opportunities of all the above

Additional EBT generated from replication opportunities i.e. translation opportunities of all ROI generated improvements, but not limited to ROI as mentioned above, for the entire organization and including its parent/sister/child concerns for all their locations, departments, teams, processes as and wherever applicable, are included for calculation of Additional Gains.

@ KINDUZ we have seen numerous cases where a lot of good work is done in organization, but larger ROI is not delivered due to inefficient translation opportunity identification and execution.

In one of our engagements, we delivered over € 13 million as ROI in a span of 26 months for a Fortune 500 organization. The customer and us identified a minimum € 250+ million in ROI if the work we did is translated at the Top 10 revenue generating countries of the organization. For various reasons it never happened. Translation opportunity identification and execution is key for short-term, mid-term and long-term success of any organization.

Never miss the simple things, which can deliver a ton of value.

4. Additional Gains not included as part of ROI calculations

4.1 Soft Intangible Benefits

Only measurable tangible benefits are included towards calculation of Additional Gains. Soft Intangible benefits like increase in Brand Value, Good will, Customer Satisfaction Scores, Employee Satisfaction Scores, are not included for ROI calculations. These intangible benefits are and should be tracked separately as Soft Benefits.

5. Investment Costs

5.1 Investment Costs Allowed as Deduction:

The following Investment Costs incurred towards the improvements will be considered as deduction towards calculation of ROI:

I. All Investment Costs related to the individual improvements, individual Projects and the overall Program will be mutually agreed upon between KINDUZ and the Customer before the expense is made

II. Payments made to KINDUZ as Fixed Fee for the initiative

III. Investment Costs incurred in Travel, Boarding and Lodging, Logistics such as for Training, Coaching and Printing for the initiative as listed in 'Miscellaneous Costs' of the Program.

IV. Operational Expenses (OPEX) towards the accepted and implemented recommendations of the Projects (all such expenses should be approved by KINDUZ and the Customer mutually, else will not be accounted in expenses), from the day of starting the Program until the end of the ROI Accumulation and Sustenance Phase. Please check the detailed definition of OPEX in the 'Common Definitions' section.

V. Depreciation Expenses for capital investment towards the accepted and implemented recommendations of the Projects (all such Investment Costs should be approved by KINDUZ and the Customer mutually, else will not be accounted in Investment Costs), from the day of starting the Program until the end of the ROI Accumulation and Sustenance Phase. In no case can the depreciation of an asset in a particular year from Capital Expenditure, be more than what is allowed by the regulatory bodies and income tax laws of the applicable country, for the overall value of the Capital Expenditure. In cases where an applicable country does not have such laws or standards, the maximum depreciation of Capital Expenditure will be limited to 15% of the overall value of the Capital Expenditure, and in the cases of cleaning equipment the maximum depreciation of Capital Expenditure will be limited to 33% of the overall value of the Capital Expenditure. All Capital Expenditure irrespective of the cost involved, no matter how small or how big, on the date of purchase of the asset, will be considered for depreciation. It is important to note that for all capital expenditures, only the depreciation amount will be accounted as Investment Costs for calculating the ROI. The entire cost of the capital expenditures will not be accounted as Investment

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Costs for calculating the ROI. Please check the detailed definition of CAPEX in the 'Common Definitions' section.

VI. All Investment Costs made should be allocated to the relevant Business Units of the Customer based on the number of Projects from each Business Unit. This will help in allocating the Investment Costs to the right Business Sponsor, ensuring that the focus is maintained on the Program.

VII. Investment Costs for Projects completed successfully and for those not completed for any reason will be accounted for Expense calculation

VIII. In case the organization's cash flows are being funded through debt, a pro-rata Cost to Debt will be allocated for the cash spent towards relevant Investment Costs. Cost of Debt is the effective interest amount that a company pays on its current loans, bonds, over drafts and various other forms of debt

IX. Success based incentive paid to KINDUZ if any, from the Additional Gains generated from the initiative

X. Only the below given Investment Costs will not be allowed for deduction

5.2 Expenses not Allowed as Deduction:

The following expenses incurred towards the initiative i.e. Program will not be considered as deduction towards calculation of ROI:

I. Expenses already allocated, and/or budgeted, and/or needed for on-going OPEX and CAPEX, SG&A Expenses

II. Salary expenses of Customer Change Agents (i.e. associates who drive Projects), Customer Project Sponsors (N+1s of Change Agents), Customer Process Owners, Customer Champions, Customer Co-Sponsors, Customer Sponsor and other Stakeholders for the time they spend on supporting, monitoring, training and completing their Projects and ensuring the success of the Program.

III. Salary costs of Program Management Team appointed by the Customer involved in managing improvements

IV. Expenses incurred on specific improvements and on Projects where there is no estimated ROI (for example: Projects with soft benefits)

V. Expenses incurred to keep employees, contractors and relevant stakeholders motivated (lunch, dinners, celebrations)

VI. Any long-term investment recommendations that are beyond the scope of the Projects or the overall Program

VII. Expenses already decided to be made towards improvements, before the start of this initiative

VIII. Expenses already decided to be made towards improvements, during the initiative that are not related to the initiative

IX. Expenses already budgeted to be made, before the start of this initiative

X. Expenses budgeted to be made, during the initiative that are not related to the initiative

XI. Expenses incurred due to Force majeure events

XII. Expenses incurred beyond the purview of the improvements of the Improvement Projects or the Program

XIII. Interest paid to KINDUZ towards delay in invoices/reimbursement payments from the Customer

6. Accounting for Improvements Already Done and Improvements in Progress

I. All improvement done in the past by the Customer will be documented right at the Project Identification Phase

II. Improvements done in the past by the Customer which have delivered Additional Gains and sustained the Additional Gains will not be undertaken as a part of this Program and will not be considered for ROI calculations as a part of this Program

III. Improvements done in the past by the Customer will be accounted for ROI calculations as a part of this Program, if successfully undertaken as a part of this Program in the following scenarios:

   A) Improvement that have delivered Additional Gains but did not sustain the Additional Gains

   B) Improvements that have not delivered Additional Gains

IV. All improvement currently being undertaken by the Customer will be documented right at the Project Identification Phase

V. Improvements currently being undertaken i.e. in-progress by the Customer which deliver Additional Gains and sustain the Additional Gains will not be undertaken as a part of this Program and will not be considered for ROI calculations as a part of this Program

VI. Improvements currently being undertaken i.e. in-progress by the Customer and not part of the Program will be accounted for ROI calculations as a part of this Program, if successfully undertaken as a part of this Program in the following scenarios:

   A) Improvement that deliver Additional Gains but do not sustain the Additional Gains

B) Improvements that do not deliver Additional Gains

VII. The Customer is free to launch any additional Projects and/or improvements where there is no overlap with the scope of this Program and/or Projects. Such additional Projects and/or improvements will be first mutually discussed and agreed upon between KINDUZ and the Customer to ensure there is no overlap.

7. Return on Investment Tracking

7.1 ROI Tracking during Project Identification and Project Execution and ROI Delivery Phase

I. KINDUZ will be involved in the ROI tracking till the extent of the validity of a relevant SOW

II. All relevant metrics required in the calculation of ROI, and the ROI calculation methodology itself for every project will be put in place by KINDUZ and signed off together by the Customer's Finance team and KINDUZ before the project pilots

III. ROI estimates will be refined post Pilot (by KINDUZ with support from relevant stakeholders and validation by Customer's finance team and KINDUZ)

IV. KINDUZ will be responsible for measuring and reporting ROI from each project individually during the Project Identification and Project Execution and ROI Delivery Phase

V. KINDUZ will report the ROI estimation and ROI delivered during the Project Identification and Project Execution and ROI Delivery Phase on a calendar monthly basis.

VI. The Customer's Finance Team will review the numbers within 5 working days and approve it, failing which the numbers will be deemed accepted and approved

VII. Before the end of the Project Execution and ROI Delivery Phase, ROI delivered, and ROI estimated to be delivered by all Projects, will be signed off by the Customer's Finance team along with KINDUZ

VIII. The signed off ROI will be shared with relevant stakeholders by KINDUZ

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7.2 Monthly Cycle of ROI Tracking during the ROI Accumulation and Sustenance Phase

7.2.1 In case of a Business Outcome Model

I. During the ROI Accumulation and Sustenance Phase, ROI for all projects, will be calculated by KINDUZ within the first 5 working days of every calendar month based on the performance in the past month and communicated to the Customer's Finance Team for sign-off

II. Any recommendation(s) for corrections and / or changes in the calculated ROI will be communicated to KINDUZ Consultant(s) by the customer's Finance team within 5 working days of the intimation. If no recommendations are received in this time frame, the submitted calculations will be deemed accepted by the Customer's Finance Team.

7.2.2 In case of a Fixed Fee Model

In case of Fixed Fee Model, even though KINDUZ does not get a part of the ROI generated as a success based fee, KINDUZ still recommends that ROI is captured and reported on a continuous basis. This is important to measure the effectiveness of the initiative and builds a focus within the organization on delivering measurable outcomes from each initiative.

I. During the ROI Accumulation and Sustenance Phase, ROI for all selected Projects, will be calculated by the Project Sponsor(s) and Project Change Agents within the first 5 working days of every calendar month based on the performance in the past calendar month and communicated to the Customer's Finance Team for sign-off

II. Any recommendation(s) for corrections and / or changes in the calculated ROI will be communicated to Project Sponsor(s) by the Customer's Finance team within 5 working days of the intimation

7.2.3 Common Steps

I. Once the ROI is finalized / updated and communicated to the Customer's Finance Team, the calculated ROI will then be reviewed and, requested for revision or signed off by Customer's Finance Team, every calendar month within 5 working days after the intimation of ROI, failing which the ROI estimated will be deemed accepted and approved

II. In case of any recommendation(s) for correction and / or change in the calculated ROI, KINDUZ / Project Sponsor(s) agree to review, update where required and finalize the ROI within 5 working days of receipt of the communication from the Customer's Finance Team

III. KINDUZ Consultant(s) and/or Project Sponsors and Change Agents will continue to work with the Customer's Finance Team, offline or onsite, based on mutual convenience to monitor and track the actual ROI for the duration of this Program

IV. Once finalized, the calculated ROI will be baselined and shared with relevant stakeholders every calendar month

V. KINDUZ Consultant(s) will be given access to all relevant people, sites, information and resources by Customer to calculate and/or validate ROI during the duration of the Program

7.3 Duration for calculating Additional Gains

Additional Gains and ROI will be calculated for all improvements undertaken including translation opportunities identified and implemented during the:

- Project Identification Phase (2 calendar months)
- Project Execution and ROI Delivery Phase (3 to 14 calendar months)
- ROI Accumulation and Sustenance Phase (15 to 26 calendar months)

Financial Benefit will be calculated from the day the Financial Benefit is derived upon execution of one or more action items. Note that Additional Gains may start to be realized before a Project is formally closed.

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