

# Demonstrating the ROI of an ERP System

## WHAT YOU CAN EXPECT FROM INVESTING IN AN ERP SYSTEM

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# Demonstrating the ROI of an ERP System

What kind of tangible (hard dollar) return can you expect for your investment in ERP software? The answer is: a lot more than you might expect. In this article you will learn how ERP software pays for itself within the first year and goes on to generate hundreds of thousands of dollars in cost savings each year thereafter.

## FEATURE/BENEFIT ANALYSIS

The first step in determining the ROI of a software system involves a feature/benefit analysis. In other words, examining various features of ERP software to see what they do and how they generate a positive return on investment. The following features, which are an integral part of Global Shop Solutions software, can be found in most good ERP systems:

**FEATURE:** Integration of all business processes, including estimating, quoting, sales orders, inventory, routing, work orders, invoicing, purchasing, accounting and shipping.

**BENEFIT:** Lean management of all processes. This allows management to focus its time, energy and resources on continuous improvement, sales growth and diversification.

**FEATURE:** Scheduling/capacity planning.

**BENEFIT:** On-time delivery rates of 97 – 100 percent. Reduced cycle time.

**FEATURE:** Shop floor online touch screen.

**BENEFIT:** Reduces paperwork and indirect time. Improves accuracy.

**FEATURE:** Shop tracking (instant tracking of a job or all jobs by customer).

**BENEFIT:** Improved customer service and an impressive site visit of your facility for customers and/or prospects.

**FEATURE:** Indirect labor measurement, which enables daily accountability, balancing of all direct/indirect labor and performance measurement by employees.

**BENEFIT:** Reduction of indirect labor, in some cases by as much as 50 percent.

**FEATURE:** Automated purchasing.

**BENEFIT:** Frees up purchasing personnel's time to improve pricing, quality and on-time delivery. Obtain better pricing from consolidation and standardization. Reduce inventory.

**FEATURE:** Direct labor measurement, including performance reports and estimate versus actual.

**BENEFIT:** Improved direct labor performance.

**FEATURE:** Lean setup, including measurement of estimate versus actual and average time to make a setup.

**BENEFIT:** Helps focus on classic lean setup goals, such as reducing all setups to 10 minutes or less.

**FEATURE:** Quality/linking documents.

**BENEFIT:** Reduction in quality costs. Documents are displayed right on the shop floor. Operators can do their own QC.

**FEATURE:** Cost accounting.

**BENEFIT:** Improved margins by changing the mix to the most profitable levels.

**FEATURE:** Multiple training methods, including on-site classroom training, on-site consulting, annual users' conference, one-on-one virtual training on the Web and subscription training on the Web, including Lean Training.

**BENEFIT:** Continuous improvement.



## THE HARD DOLLARS

Purchasing ERP software represents a significant financial commitment, especially for smaller companies. However, in most cases, the software more than pays for itself within the first year. More important, when properly implemented, ERP software continues to generate annual cost savings of several hundred thousand dollars year after year after year.

At Global Shop Solutions, the typical customer has about 70 employees and does about \$10 million a year in annual sales. Companies in this range will pay \$60,000 to \$70,000 to initially purchase the software, with annual licensing fees of \$15,000 each year afterwards. However, our experience has been that these customers typically generate cost savings of more than \$300,000 a year. Even if it takes six to 12 months to begin experiencing the efficiency gains, the software still pays for itself within the first year. Thereafter, the software continues to generate \$300,000+ in annual savings at a cost of only \$15,000 a year, for a remarkable 500 percent return on investment.

Where do the cost savings come from? It depends on the company, but in most cases indirect labor yields the greatest percentage of savings, often generating nearly half of the total cost savings. Why so much from one area? Because many manufacturing firms have no idea how much indirect labor actually goes into their products. As a result, they do a very poor job of managing indirect labor costs. ERP enables these companies to track, measure and adjust indirect labor costs while work is still in progress, which leads to substantially improved indirect labor practices and significant reductions in cost.

Other areas that contribute most to the cost savings are on-time deliveries, direct labor, shop floor tracking, quoting, purchasing, and efficiency gains in other processes throughout the company.

## ERP PAYBACK CALCULATOR

The screen shot below shows is captured from the Global Shop Solutions payback calculator. It shows in detail how the typical Global Shop Solutions customer obtains annual cost savings of \$326,000.

The screenshot displays the 'Global Shop Solutions Payback Calculator' interface. It features several sections with input fields and calculated results:

- On-Time Delivery:** Increased Sales by improving on-time delivery from 75% to 85% or more. Total Sales: \$4,000,000.00. Increase: 10%. Cost: \$10,000.00.
- Reduce Indirect Labor:** Decreased Indirect Labor from 22% to 12%. Total Indirect Labor: \$1,500,000.00. Payback: \$150,000.00.
- Reduce Direct Labor:** Increased Direct Labor from 50% to 55%. Total Direct Labor: \$1,500,000.00. Payback: \$75,000.00.
- Shop Floor Tracking:** Daily input to shop floor: 75% to 75%. Minutes spent: 140 days per year. Cost per hour: \$10.00. Cost per hour: \$0,000.00.
- Improve Processes or Whole Company:** More On-time, Customer who really ask a need of general category, job status information, and use of current technology. Sales personnel can provide job information instantly while on the phone, resulting in lower call-backs. Allow better use of time to take personal calls or creating new business. Total Sales: \$2,000,000.00. Increase: 10%. Cost: \$1,000.00.
- Partially to more automated, less time to spend on order of work, more time to spend on reducing overhead quotes, request for quotes, and actual removal of orders through the internet.** Annual Purchases: \$7,000,000.00. Savings: \$326,000.00.
- Quotes are generated quicker which increases the amount of quotes that can be created. Stand out competition with better quotes, a fast quote, to use of estimates and for work order generation, reducing service information with customer.** Total Sales: \$1,000,000.00. Increase: 5%. Cost: \$1,000.00.

**Total Payback: \$326,000.00**

## WHEN REVIEWING THE SCREEN, KEEP IN MIND THE FOLLOWING:

- The Indirect Labor fields represent the amount of time spent by direct labor employees engaged in doing something other than running parts. In other words, non-productive time. There are multiple causes of Indirect Labor that can include looking for tooling, checking with the shop manager on which job is to run next, and many more. Some of these activities, such as knowing which job to work on next, are automatically handled in a streamlined ERP system. In most cases, the single most important factor is that each employee quickly learns that they are being measured each day on indirect labor and they seek to improve their performance.
- The Direct Labor fields represent the increase in efficiency realized from monitoring an employee's time spent running a job (actual) against how long it should have taken them to do the work (estimated). Although typically less than the reduction in indirect time, direct labor savings for most companies can still be a significant figure.
- The Purchasing field will typically contain both materials and outside process purchases. Cost savings are realized through group or bulk purchase, longer lead times, better inventory turns (due to tighter management of inventory levels), fewer physical inventories required, and an overall improvement in the efficiency and organizational level of the purchasing department.
- The Cost field represents the overall manufacturing cost, leaving the gross profit to reach 100 percent. Depending on your company's current manufacturing processes and management practices, you may save more or less than the amount shown in this example. However, the payback calculator clearly demonstrates how even small improvements in critical areas like direct and indirect labor and on-time deliveries can lead to huge cost savings and additional dollars to the company's bottom line.



**DIRECT LABOR SAVINGS FOR  
MOST COMPANIES CAN BE  
A SIGNIFICANT FIGURE.**



## INTANGIBLE BENEFITS

Although harder to measure in quantifiable terms, ERP can also lead to important changes in employee attitudes and the overall culture of the company. In addition to generating direct cost savings, ERP also enables companies to:

- Make better management decisions. ERP functions as a powerful management tool that allows the owner/CEO to get a daily snapshot (in graphical format) of sales orders, work in progress, inventory, receivables and all the critical areas of the business. With timely and accurate information at their fingertips, the business owner/CEO can make better decisions.
- Do more with less. In medium to large companies, ERP enables one person to do the work of several, particularly in an area like purchasing. In smaller companies, individuals who perform several functions can do them in far less time and have more time to devote to other areas of the business.
- Enhance teamwork. ERP makes every process in the system more visible. As people begin to see how all the different processes are interconnected and how their jobs affect each other, they become more open to sharing information and working together to resolve problems and improve processes.
- Improve morale. ERP raises the professionalism of a company. It also lessens the pressure and frustration employees feel when forced to work with outdated and inefficient processes. ERP users feel more competent and professional, and they gain a real sense of accomplishment from learning new skills. When people feel good about themselves and the work they perform, they inevitably do better on the job.
- The bottom line is that ERP will make a real difference in your bottom line, both in terms of hard dollars and in developing the people who run your business. The initial investment to purchase and implement ERP may seem steep, but it's a drop in the bucket compared to the return on investment the software will generate for years to come.



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**WHEN PEOPLE FEEL GOOD ABOUT THEMSELVES AND THE WORK THEY PERFORM, THEY INEVITABLY DO BETTER ON THE JOB.**





## **WE SIMPLIFY YOUR MANUFACTURING.™**

Since 1976, **Global Shop Solutions** has been the exclusive provider of One-System ERP™ Software designed to make lean manufacturing a reality in countries around the world. The efficiency delivered through their ERP software provides real-time inventory accuracy, improved on-time delivery, lower administrative costs, increased sales and improved customer service. Real-time data with high-level accuracy empowers business leaders to be proactive in their decision making. Global Shop Solutions customers enjoy a significant ROI to their bottom line. Headquarters in The Woodlands, Texas includes a state-of-the-art R&D facility and their Global Shop Solutions University training center. Through its offices in the U.S., Mexico, Indonesia, Singapore, Australia, New Zealand and the United Kingdom, it maintains its place of prominence in the ERP manufacturing software industry.

**To learn more about Demonstrating the ROI of an ERP System, call 1.800.364.5958 or visit [www.globalshopsolutions.com](http://www.globalshopsolutions.com).**

