by Bob Dust

Understanding Financial Terminology

WHAT TERMINOLOGY DOES management use when allocating resources and how can you speak their language?

Two terms should concern you the most—return on investment (ROI) and profit margin (PM). What are they? How do these affect you?

Many for-profit organizations strive for between a 10 to 20 percent return on their investments. Some want even more. Often, within the same organization, different areas will have widely different ROI objectives. The ROI on older, established products will usually be higher than for products that are under development or newly released.

Know what your reorganization's ROI goal is. Map a plan to illustrate how your training meets or exceeds that ROI.

For some training, it's easy. Sales training is a good example. Imagine that you spend (invest) $10,000 in a sales training program, and sales per sales rep increase by 10 percent, from $1,000,000 to 1,100,000 the first year. You can document that your training ROI was 1,000 percent, just for the first rep [($100,000 ÷ $10,000) x 100]. What other department can document those kinds of returns?

Other courses can be more difficult to measure. For example, how do you measure the ROI on your stress management course?

It's not easy, but it can be done. Find ways to measure the impact that stressed employees have on your organization—missed days from work, missed projects, wrong shipments, high turnover, and so forth. Document and measure the costs of these problems the year before you offer the course. A year later, measure the costs again. Divide the savings by the cost of the course and you have your ROI.

You may be thinking that no one, including management, will buy into the notion that your course on managing stress is the sole cause of all these improvements. They may be right. If you do this for each course, you will have the attention of management. They will now look at the big picture of training that you presented. It will be up to the other departments (your "competitors") to prove you wrong.

If you really want to make an impact, have a statistician calculate the "correlation coefficient" of your cause-and-effect theories. Who can argue with a statistician?

The profit margin is the percentage of money that remains after all expenses have been allocated. These include not just the initial expenses, but also allocations for overhead (such as rent, equipment, postage, and so forth). Profit margins generally run in the two to eight percent range. Did you know that sometimes decreasing your profit margins can increase your profits (by increasing your sales at higher volumes)?

There are two types of profit margin

EFFICIENCY MEASUREMENTS

There are several measurements of training efficiency. If you can, use previous training records to determine the following for previous years:

Average training hours per employee. This measures the quantity of training and tells how productive your training has been as a function of time. Some certification programs are interested primarily in how much training was performed.

Average training cost per employee. This measures the average "benefit" of training for all employees. You may also want to break this down further by EEO class, job status, job title, and organization structure.

Total instructor hours. This measures the supply of training hours and tells you how productive your instructors have been as a function of time. This measurement can help determine instructor load and requirements for future training.

Total classroom hours. This measures the supply of classrooms and tells you how much you have used your classrooms. This measurement helps you plan classroom load and requirements for future training.

Total class hours. This measures how many hours were spent in all training, including instructor-led training, self-study, and outside training.

Average student hours/instructor hours. This measures instructor load. If this number is too high, the effectiveness of training will decrease. In other words, students may not be getting the attention that they need. If it is too low, the effectiveness will also decrease because there were students who were not in the classroom who might have benefited from the training. In other words, the instructor had attention to give and no one to receive it.

Cost of student absences. This measures the cost of students who registered for a course but did not attend. In the business world, this is considered spoiled inventory. Spoiled inventory is inventory that has been paid for, but was discarded because it spoiled, rotted, evaporated, and so forth.

Student enrollment/class capacity. This measures a form of excess inventory. If the optimum size of your class is 10 students, and the class costs $4,500 to present, your cost is $450 per student. However, if only nine students show up your cost jumps to $500 per student. You had the capacity to teach 10 students, but only taught nine. Your ROI will be less.

Wait listed/student enrollment. This measures unsatisfied *demand*. If you continually have students who are wait listed for your classes, that is, they want to enroll but cannot, your *supply* of training is not sufficient to meet your demand. (A good time to ask for more resources.) The higher this number, the higher the amount of unsatisfied demand. As this number approaches zero, you have an indication that your supply may be too high. (Not a good time to ask for more resources.)

that you should examine.

Gross profit margin (GPM) shows the percentage return that is earned over the cost of producing products. The gross profit is used to cover operating expenses. GPM is calculated by dividing gross profit by total sales:

GPM=sales-cost of goods sold÷total sales.

Net profit margin (NPM) shows the percentage of net income generated by each dollar of sales. The net profit is used to support future operations (retained earnings) or is distributed to the stockholders (dividends). NPM is calculated by dividend net income after tax total sales:

NPM=net income after tax÷sales.

ROI and PM are two controls that management uses for overall organizational efficiency. You will want to examine others that are more training specific.

Controls keep training focused on objectives. Your controls should be indicative of the success (or problems) of your training. Refer to Dr. Holton's article on training evaluation and to *efficiency measurements* in this article.

But how do you determine the optimum numbers for the measurement controls?

That's one that you will have to determine yourself. We already mentioned the review of past figures as one guideline. Your goal is to improve on those previous year's numbers. If those numbers were efficient before, you will be able to document how effective your training has become—that is, how it has improved.

One mistake that many businesses make is not knowing when to say 'NO!'

Another good source is your local community of trainers. Join training associations (such as ASTD) and ask your colleagues what measurements they have available. Also be aware of how well others in your industry are performing. This will be of more concern to your management than anything else.

Know what your capacities are to deliver your services. One mistake that many businesses make is not knowing when to say, "No!" They over commit, causing problems for themselves and their customers. That tarnishes their reputation in the process.

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