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RETURN ON INVESTMENT (ROI) FOR EQUIPMENT PURCHASES

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In the previous article, "The Relationship Between Your Balance Sheet and Your Income Statement", we determined that assets generate sales. However, to fund these assets we must spend cash or create liabilities. This brought up the question of whether assets were good or bad. The conclusion was that assets are good if they provide more income than it costs to fund them.

How do we determine if an equipment purchase is a financial benefit or a financial drain on the practice? The Equipment ROI Analysis tool allows for the calculation of positive or negative cash flow from equipment purchases as well as the payback period and return on investment. The tool is available under the resources tab on our website (www.wellmp.com) for only $119.

Whether you are looking to spend $25,000 or $75,000 on a new piece of equipment, $119 is a low-cost investment to determine the return expected from your purchase. Simply enter information into the blue cells and the results appear in the green cells. Run the tool as many times as you like. You can look at multiple options, such as different equipment purchases and varying loan terms. This "what if" analysis allows you the ability to customize multiple scenarios.

The graphic below provides two scenarios. In the first example, we analyze the purchase of a laser for $25,000 at an interest rate of 6% for a three-year loan term. In the second example, we analyze the purchase of an ultrasound for $70,000 at an interest rate of 6% for a five-year loan term.

Which piece of equipment would you buy if you could only make a single purchase? The $25,000 laser is a clear winner, offering an excellent 468% return on your investment with a payback period of only 1.2 years. The $70,000 ultrasound is still profitable, assuming no assignment of fixed practice costs. However, it will take you 5.1 years to get your money back and you realize only a 36% total return over the life of the equipment.

As with any analysis of this type, the output is only as accurate as the inputs. However, if you can make an educated guess about how often you will use the equipment, this is an excellent tool for determining the viability of equipment purchases.

Equipment ROI Analysis
in a Well-Managed Practice®

Assumptions

	Lucky Dog and Cat Hospital		Lucky Dog and Cat Hospital	
Item purchasing	Laser		Ultrasound	
Purchase price	$ 25,000		$ 70,000	
Amount financed	$ 25,000		$ 70,000	
Interest rate - yearly	6.0%		6.0%	
Loan term - years	3		5	
Total interest over loan term	$ 2,380		$ 11,198	
Installation Cost	$ -		$ -	
Initial training cost	$ 1,200		$ -	
Direct cost per time used:	$ 3,000		$ -	
Payment at end of lease	$ -		$ 1	
Fixed, payroll, and facility costs allocation or increase per $ of revenue generated	39%		39%	
Estimated useful life of equipment (in years)	7		7	
		% of Total Revenue		**% of Total Revenue**
Practice annual revenue	$ 2,800,000	100%	$ 2,800,000	100%
Practice annual medical revenue (includes services and products)	$ 2,380,000	85%	$ 2,380,000	85%
Variable expenses	$ 672,000	24%	$ 672,000	24%
Fixed expenses	$ 224,000	8%	$ 224,000	8%
Staff compensation	$ 644,000	23%	$ 644,000	23%
Facility expense	$ 224,000	8%	$ 224,000	8%
Doctor compensation (% of medical services; also consider allocation of doctor/staff time involved)	20%		20%	

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Increase in Cash Flow (May Be Used to Service Debt)

	Lucky Dog and Cat Hospital	Lucky Dog and Cat Hospital Fixed Costs Incl. In Calc.	Lucky Dog and Cat Hospital Direct Costs Only Incl. in Calc.
1. Estimated number of times you will provide this service in the next 12 months	1,250	60	60
2. Fee or additional fee for this service	$ 50	$ 330	$ 330
3. Projected increase in revenue (#1 times #2)	$ 62,500	$ 19,800	$ 19,800
4. Allocatable portion of operating costs (from Assumptions times #3)	$ 24,375	$ 7,722	$ -
5. Profit before veterinary compensation (#3 minus #4)	$ 38,125	$ 12,078	$ 19,800
6. Veterinary comp. (Comp. % times #3)	$ (12,500)	$ (4,000)	$ (4,000)
7. Projected annual profit available to cover cost of equipment (#5 minus #6)	$ 25,625	$ 8,078	$ 15,800

Years to Recapture Investment (Payback Period)

1. Cost of equipment (includes interest on the loan)	$ 27,380	$ 81,199	$ 81,199
2. Plus: Cost of installation, training, maintenance contract	$ 4,200	$ -	$ -
3. Equals: Total cost of equipment purchase	$ 31,580	$ 81,199	$ 81,199
4. Projected annual profit available to cover cost of equipment	$ 25,625	$ 8,078	$ 15,800
5. Payback period in years (#3 divided by #4)	1.2	10.1	5.1

Investment Return

		Fixed Costs Incl. In Calc.	Direct Costs Only Incl. in Calc.
Projected profit available to cover cost over life of equipment	$ 179,375	$ 56,546	$ 110,600
Divided by total cost of equipment	$ 31,580	$ 81,199	$ 81,199
Return on Investment (ROI)	468%	-30%	36%