

# Business Performance Management

## Part 1a

### The Basic Equation Cost per Order

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## The Basic Equation

$$\text{Operational Result} = \text{Sales} - \text{Cost of Sales} - \text{Expenses}$$

$$OR = (S - COS) - EXP$$

Expenses: labor costs (salary),  
rental, stationary, traveling cost,  
depreciation, etc.

Cost of Sales,  
Cost of Goods Sold (COGS)

Sales, Revenue or Turnover

Operational Result, Operational Income  
Profit, Earnings before Interest and Tax (*EBIT*)

## The Basic Equation

**Operational Result =  
Sales - Cost of Sales - Expenses**

$$OR = (S - COS) - EXP$$

**Gross Profit (GP), Gross Margin (GM)**



## The Basic Equation

**Operational Result =  
Sales - Cost of Sales - Expenses**

$$OR = (S - COS) - EXP$$

Example:

<b>Sales per month <i>S</i></b>	<b>\$20,000</b>
<b>Cost of Sales <i>COS</i>:</b>	<b><u>- \$12,000</u></b>
<b>Gross Profit <i>GP</i>:</b>	<b>\$ 8,000</b>
<b><u>Expenses per month <i>EXP</i>:</u></b>	<b><u>- \$ 5,000</u></b>
<b>Operational result <i>OR</i>:</b>	<b>\$ 3,000</b>

## The Basic Equation

**Operational Result =  
Sales - Cost of Sales - Expenses**

$$OR = (S - COS) - EXP$$

**Sales  $S$  is the result of booked orders.**

**There is a **time delay  $t$**  between  $O/$  and  $S$**

**Because of manufacturing time, delivery time ...**

**We will neglect it in our model at the moment.**



**For simplification we replace **sales  $S$**  by **order income  $O/$**  in our model**

## The Basic Equation

**Operational Result =  
Sales - Cost of Sales - Expenses**

**$OR = (OI - COS) - EXP$**

**Sales  $S$  is the result of booked orders.**

**There is a **time delay  $t$**  between  $OI$  and  $S$**

**Because of manufacturing time, delivery time ...**

**We will neglect it in our model at the moment.**



**For simplification we replace **sales  $S$**  by **order income  $OI$**  in our model**

## Key Ratios

### Key Ratios and Key Performance Indicators

- 1 **Cost per Order *CPO***
- 2 **Profit per Cost *PPC***

For key performance indicators, we use preferable *ratios* instead of absolute figure

Ratios make it easier to compare organizations of different size

## Key Ratios

**Operational Result =  
Sales - Cost of Sales - Expenses**

$$\frac{OR}{OI} = \frac{(OI - COS) - EXP}{OI}$$

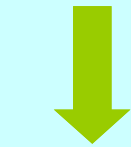
**As we want to come to ratios,  
we divide the equation on both sides by *OI***



## Key Ratios

**Operational Result =  
Sales - Cost of Sales - Expenses**

$$\frac{OR}{OI} = \frac{GP}{OI} - \frac{EXP}{OI}$$



**PR**

Profitability



**GMP**

Gross Margin  
Percentage



**CPO**

Cost per Order

## Key Ratios

**Operational Result =  
Sales - Cost of Sales - Expenses**

$$\frac{OR}{OI} = \frac{GP}{OI} - \frac{EXP}{OI}$$



$$PR = GMP - CPO$$

**Profitability = Margin - Cost per Order**

Key ratio:  
Cost per Order

**CPO**

=

$\frac{EXP}{OI}$

Order income per month:	\$20,000
Expenses per month:	\$ 5,000

**Cost per Order  $CPO = \$5,000 / \$20,000 = 25\%$**

**$PR = GMP - CPO$**

**Profitability = Margin - Cost per Order**

Key ratio:  
Cost per Order

**CPO**

=

$\frac{EXP}{OI}$

Order income per month: \$20,000

Cost of Sales: \$12,000

Margin **GMP** =  $\frac{\$20,000 - \$12,000}{\$20,000} = 40\%$

**PR = GMP - CPO**

**Profitability = Margin - Cost per Order**

Key ratio:  
Cost per Order

**CPO**

=

$\frac{EXP}{OI}$

Profitability  $PR = GMP - CPO$

= 40% - 25%

Profitability  $PR = 15\%$

$PR = GMP - CPO$

Profitability = Margin - Cost per Order

Key ratio:  
**Cost per Order**

***CPO***

A lower *CPO* is better than a high *CPO*

*CPO* should be lower than your gross margin percentage *GMP*, otherwise the company will make losses

*CPO* is always positive (as you have always certain costs and expenses)

Increasing your order income *OI* (with given operating expenses) will lower your *CPO* and increase your operating result

Doing “cross country business” with order income in foreign currency, *CPO* will reflect changing FX rates

For more visit <http://bpmsg.com>