HR Mixtape
Transcript

Profit Doctor: When Revenue Grows but Profit Doesn't

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Host: Dr. Shari Simpson, Thought Leader, Paylocity

Guest: Ben Hansen, CEO, Profit Doctor

[00:00:00] **ANNOUNCER:** You're listening to The HR Mixtape, a podcast for leaders who want to understand people, strengthen culture, and navigate change with clarity. Today's conversation starts now. Joining me today is Ben Hansen, CEO at Profit Doctor. Ben helps CEOs diagnose profit problems fast and build healthier, more sustainable businesses that can invest in their people.

[00:00:34] **DR. SHARI SIMPSON:** Ben, thank you so much for jumping on the podcast with me today. So we're gonna talk about an interesting topic today called profititis. I'd love if you could start by helping define that term for our audience.

[00:00:37] **BEN HANSEN:** Oh, happy to be here, Sherry. So think profititis, like tendonitis, which might mean sick profitability. The way we look at it is companies that have strong or solid top-line revenue sales, but weak, declining, sick bottom-line net profitability.

[00:01:05] **DR. SHARI SIMPSON:** Love that. Super simple, easy for us to understand. And you bring a really interesting perspective. You built an eight-figure staffing firm. When did you first realize that growth can hide a profit problem?

[00:01:25] **BEN HANSEN:** In many cases, it is growth that is hiding your profit problem. So many business owners are so focused on growth, customer acquisition, getting more revenue, that sometimes they set aside profitability, margin, contribution margin. We'll just call them efficiency and profitability metrics. And in fact, often it's that push for rapid growth, or just focus 150% on growth, that results in too little focus around profitability.

[00:02:00] **DR. SHARI SIMPSON:** What are some of the signs that you've seen leaders ignore until it's really, really painful in this area?

[00:02:22] **BEN HANSEN:** Some big ones. The most obvious is looking at their P&Ls on a monthly basis and being able to chart how revenue and profitability may be diverging. That is the biggest and most obvious one. Also just keeping track of net profitability as a total dollar figure, and then as a percentage of revenue. For those who are a little deeper into the P&L, a level below: margins, gross margins, contribution margins, the spread between the revenue of something and the true cost of delivering those services or products.

[00:02:53] **DR. SHARI SIMPSON:** Is there any one area where you see this the most exaggerated? I'm thinking about areas like pricing, your cost of goods, operations, leadership habits, or is there something else that you see as the common root causes of profititis?

[00:03:14] **BEN HANSEN:** We have a little tool that helps people triage, of the 10 biggest profit problems, which ones might apply to their organization the most. But some big common issues are beginning to serve more and more customers that are kind of outside your sweet spot, and to offer more and more products and services that are outside your sweet spot. Almost like the opposite of having a niche play.

[00:03:56] **DR. SHARI SIMPSON:** If a niche play is focusing on Main Street, serving who you're best at serving with what you're best at serving, profititis is often linked with getting off Main Street or getting out of your niche and serving those customers with those products and services that you're not as good at. How do you balance that with the drive for innovation? As you're talking, I'm thinking about that growth focus, which probably leads you to want to innovate and develop other offerings and services. But if you get away from your niche, you're going to dilute that. So how do you find that balance?

[00:04:37] **BEN HANSEN:** There's a difference between being opportunistic and organic growth, and being strategic, paring away things that are not working. I think it's a healthy tension. There are probably two ways to go about it. One is more cyclical, where for a period of time you're exploring new avenues, being organic, being opportunistic, and then on some regular cadence, quarterly, semi-annually, annually, taking stock of what's really going on. And then you might think, "We've been at this opportunity for three years. It's not really paying off. Is it the kind of thing that takes six years to incubate, or is it really that we're just not very good at it?" It takes that ability to look at yourself with very critical eyes on how you're working through things.

[00:05:35] **DR. SHARI SIMPSON:** How does the people side or the people spend help or hurt profitability? Where does it kind of quietly kill things?

[00:05:42] **BEN HANSEN:** There's so much you could get from Googling that question at a level-one answer. Obviously as payroll goes up, the question is: is payroll going up at a faster or slower rate than revenue or the total margin pool? And if you're adding more payroll dollars faster than revenue or contribution margin as a pool is going up, that's going to dilute your earnings. That doesn't mean it's not an important point, but to go one level deeper: I think it's very valuable to think through the quality and caliber of the people working there. It's a quality question and then a fit question, whether it's fit for the role or fit for the company. If the average talent level of your talent is high, theoretically you're getting a lot of bang for your buck, and you should have a lot of opportunity to deliver a lot of value for clients, hopefully recoup a lot of revenue and margin from that, and therefore profitability.

[00:06:57] **DR. SHARI SIMPSON:** And if that talent level is lower, whether at some absolute level or maybe fit for your company, your vision, your market space, your customers, then the reverse is going to happen. Payroll is going to go up as a percentage or ratio of what you can deliver. HR often finds themselves at the table when we're having these conversations, and they're being asked to cut costs, and that usually means people. I really liked the example you gave about how to evaluate your talent to make sure you're continuing to increase profitability. What approach should HR be taking in that room when they're bringing their people perspective to conversations about cutting costs? Let's say if we cut this one program, we know that 50% of our population participates in it, and it could impact our culture, which could impact how our employees treat our clients, which has downstream effects on everything. How can HR bring a strategic business mindset to those cost-cutting conversations when there are real stakes about the impact that might not be as obvious as introducing or removing a product?

[00:08:28] **BEN HANSEN:** It sounds like we're now talking about bigger company stuff. I used to work at Dell and Microsoft, and I have a fair appreciation for large company benefits packages, not just direct benefits like healthcare, but all the other programs and services. I would probably say that even before you're in that room, it would be great to have already taken a very close look at those costs, in the sense of cost-benefit. Everything is opportunity cost. So before adding, keeping, enriching, or paring down any program, what is the cost and benefit? I'll take a little story from my own experience. When we had 100 employees, there was a common question that would sometimes come from employees: why not 401k matching, or why not these other benefits? And I was always thinking, we have a certain amount to spend per employee on their total comp package, to kind of balance out our P&L. And then the question was often: would you rather have more benefits, like richer healthcare or 401k matching, or would you rather have more salary? Because from a P&L impact, a dollar spent on one versus a dollar spent on another still costs me a buck. The question is, which buck do you value more as a typical employee? What we found, and I can't say that's the same for everybody, is that our employees valued a dollar of salary more than a dollar of 401k matching. And so that tended to guide the way I went about it. But obviously a $13 million company is a lot different from a $13 billion company. Being smart about your money all the time makes sense, and I would recommend doing that work even before that meeting. Everything's a trade-off, and I think ultimately when you're communicating to employees that we had to make a cut somewhere, was it salary, headcount, benefits, we gathered some insight from employees, management, and customers, and it felt like the least valued place we were spending dollars was, say, free sodas in the break room, as compared to payroll.

[00:11:05] **DR. SHARI SIMPSON:** So now we just have water in the break room instead of Red Bull. That is such a good example because it touched on a couple of things. One, it's taking that very strategic approach and looking at where you spend your dollars. The other thing you talked about was that investigation into your employee population and being really transparent about the trade-offs. "Hey, we do have to make some trade-offs here. What would you like? What feels best to you?" We did this during COVID, but that's six years ago now, and maybe we've gotten out of this habit of having these open, transparent conversations about profit and making cuts and making decisions. I love that you shared that.

As you work with different types of leaders, how do we incentivize our leaders, especially that middle management group, to help impact profitability so that we can maximize profit and find that balance, rather than just chasing revenue or cutting all expenses?

[00:12:19] **BEN HANSEN:** Incentivizing is a great word, but the complementary notion that goes with it is how do you track, report, and what are your metrics? If you're hoping that someone is taking action on one thing but measuring and incentivizing them on something else, people tend to do what you reward them for. So many businesses are truly incentivizing employees and managers on revenue rather than some flavor of profitability. A little story from my past: I used to work at Dell in the late '90s. One of the things that was very powerful at that time is they could look through to the end of what they were doing to determine the margin dollar or contribution margin impact of almost everything. If they were trying to upsell a customer on a bigger hard drive on 10,000 machines, the sales rep was looking right there on the screen that going from a one-gig hard drive to a two-gig hard drive added 35 margin dollars to the sale for every machine. They were very driven by margin dollars, a metric very closely associated with net profitability. If you're trying to get your management team dialed in around profitability, are you measuring and tracking things around at least some proxy around profitability? It's not always the case that everybody gets a clear look at your P&L. I've got a client in retail who's trying to figure out how to get their payroll cost to be 28% of revenue, trying to push payroll as a percentage of revenue down. But that's not a very effective metric to share with everybody in the company. Maybe the flip side of that is: for every hour worked, we need to hit $100 of revenue. So when you look at a shift of eight hours, how do we get to $800 of sales? Maybe that's the equivalent of "can you supersize this" or "would you like to take one to go." That's a metric that would be more rank-and-file friendly. Hey, you're there for eight hours, we need to hit a certain amount of sales for this whole thing to work out. You could imagine a mid-level manager running a $20 million P&L, thinking: you've got a cost picture, how do you hit a certain revenue target or margin pool target based on the budget you have available? That's not a big change to ask your employees.

[00:15:38] **DR. SHARI SIMPSON:** I love that you gave the McDonald's example. I cut my teeth at 14 there, and kind of learned the ways of business. In that environment, that little question about the upsell or the supersize was a big thing, and we had a lot of fun doing it together. There was a little bit of camaraderie and competition amongst the employees as to who could upsell the most. So it's a great example for that kind of space. As you think about different industries, maybe healthcare and nonprofits, both of those industries have either very small margins or very high budget constraints. Does your advice to those groups flex differently?

[00:16:25] **BEN HANSEN:** I don't know that retail, healthcare, and nonprofit all follow the same rule book. In healthcare and nonprofit, there may be an important consideration for many people. Many people who work in nonprofit, and I'm going to hypothesize that many people in healthcare as well, are mission-driven. And sometimes they think, "Focusing on the money is the opposite of being mission-driven, so I don't want to do that." A lot of times in nonprofits, we started kicking around this concept: no money, no mission. It's great to be mission-oriented, but somewhere in that whole mix, things have to get paid for. We're not going to be able to expand or attract donor dollars if our cost picture or our service delivery per dollar contributed isn't hitting some kind of benchmarks. Big donors looking at two nonprofits delivering the same service, one for $1,000 per person and the other for $5,000 per person, will often go with the more cost-efficient one. So the net of that, and I'm hypothesizing this flows through to healthcare as well, is trying to get your whole team, from the bottom to the top, on board that there is money associated with this mission, and you have to keep an eye on costs or cost efficiency, and in some cases revenue and upsell. A lot of nonprofits are taking on partially capitalistic models where they're getting some revenue to help offset some of their costs. If you can get people on what I call the profit bus, which is rank-and-file and middle management thinking about the profitability, efficiency, and cost of things, it allows the whole organization to be more successful.

[00:18:53] **DR. SHARI SIMPSON:** Such great advice and such a great perspective, especially in that nonprofit world. The second word is "nonprofit," so talking about money seems counterintuitive, but you're right. You can't do the work unless you have the funds to do the work. As we wrap up our conversation, Ben, what's the one hard truth you want our listeners to walk away with that they can implement today to really increase profitability in their organizations?

[00:19:27] **BEN HANSEN:** On our website, there's a video with a client of ours in construction services and business services. What happened is they would bid for projects, as is often the case with construction. We'll do this work for, say, $25,000. And then a team goes in and delivers that work. There was a communication gap. The people who delivered focused on: we need to deliver with excellence. What was missing is: we need to deliver with excellence profitably. In their case, if it's bid at $25,000, maybe the labor budget is $20,000, let's say 100 labor hours. By communicating to the team, "Not only do you need to deliver with customer excellence, it needs to be delivered profitably. And in this case, profitably means 100 labor hours. We want you to keep an eye on your time." What we found was so interesting: just that change in perspective, in communication, and then tying it back, "Hey, this project was bid at 100 hours. It ended up being delivered at 125. We lost our shirt. What can we learn from that to apply next time?" This client went from basically break even, low single-digit profitability over literally 20 years, to more than 20% net profitability within a space of about nine months. And I think that is the power of shifting thinking among rank-and-file employees, middle management, and business owners. Very often, maybe two-thirds of the time, business owners in the $1 million to $100 million range are not business background people. They used to be plumbers, now they have a $50 million plumbing company. They used to be attorneys, now they've got their own firm. That doesn't mean none of them are dialed in on profitability, but it tends to shake out that about two-thirds of them are not. And shifting to think, "We need to keep a close eye on profitability, and communicate how we can look at that across the team," can make a huge difference.

[00:22:00] **DR. SHARI SIMPSON:** Ben, all really great advice, great stories. Love hearing the different perspectives in the different industries you're working in. Thanks for sitting down and going through this with me today. I appreciate it.

[00:22:13] **BEN HANSEN:** Absolutely, Sherry. Thanks so much for your time.

[00:22:22] **ANNOUNCER:** Thanks for tuning in to The HR Mixtape. Like, share, review, and subscribe to support the show and help more people discover these conversations. Until next time, keep the conversation going.