



Opening the Kimono: Financials and Motivation

By Jason Bader

Several years ago, was doing some private consulting work with a plumbing supply company in the Midwest. During the course of the day, I was exposed to the company profit sharing program. Essentially, each full time employee was entitled to a monthly bonus based on the profitability of the organization. This was a very generous program put forth by the owners of the company. In fact, I am a huge proponent of these types of profit sharing plans. Unfortunately, there was one little drawback that impeded the effectiveness of this motivational strategy. The recipients didn't understand where the money came from.

I discovered this road block when I was speaking to one of the new employees in the warehouse. We talked a little about the structure of the company and how his first couple of months had been. I tend to get the most unbiased information from the newest members of any team. Eventually, I asked him about the profit sharing program. His eyes lit up and he told me how great it was. He told me about getting a check each month. I asked him what the bonus was based on. He explained, "When the company makes more money, we get a bigger bonus." I agreed that it was a pretty cool deal, but then I asked him what he could personally do to affect the size of the check. He looked at me and smiled, "I don't really know, but I keep on getting them." Herein lies the disconnect between company profitability and employee motivation.

I have always loved the expression *Open the Kimono* when referring to disclosure of company financials. It conjures images of forbidden, magical secrets known only to executive management. For those of you who spend time around financials, I am sure that you would agree that there is nothing mystical or thrilling about an income statement. They may have the ability to initiate a cardiac event; but beyond that, they just aren't that eye popping. It is a shame that many distributors hold their financials so tight to the vest because these documents do hold a little magical power – the power to drive net profit.

I have never really understood why owners are so fearful of sharing something as simple as an income statement with the people who work with them and for them. I think that all financial documents tend to get lumped in together. I get why we might not want to disclose a balance sheet, but why not carve out the income statement? Some distributors have a fear that a monthly income statement might fall into enemy hands. I struggle to get my mind around what a competitor might be able to accomplish with your income statement. As long as the document is relatively simple, I believe that these fears are unfounded.

As I have worked with a few next generation owners, I believe that the fear of disclosure might come from another possibility – the fear that someone might ask you to explain the numbers. Look, I am not trying to throw anyone under the bus here. It took me years to understand what the financials represented in my family business. Financial education was not something we discussed in the company. If you sold it for more than you bought it for, that was a good thing. If that difference paid for the expenses, that was a better thing. Not a whole lot of detail discussed. Unfortunately, a lack of financial understanding makes it difficult to direct others in

the hunt for cash. We need to be more transparent with the people who can exact real change in our expenses.

When I speak about hunting for cash at events, I often explain that our shoulders are broad but they aren't broad enough. We need to bring everyone in on the hunt. This starts with helping everyone understand what net profit is and how we find more. Handing people income statements and expecting them to gain insight from this document is unrealistic. We need to show how money moves in a way that makes sense.

I have always liked the dollar bill demonstration. Without getting into too much detail here, the concept is relatively simple. Hold up a dollar bill. Explain that we are selling a product for a dollar and we bought it for 70 cents. How much money did we make? The audience answers 30 cents. Tear off approximately 70% of the bill and throw it on the floor. If you really want their attention, try using a \$100 bill. Explain that the remainder of the bill you are holding in your fingers is what we call gross margin. This is where we start to pay for operating expenses. Have the audience tell you what these expenses are. Keep ripping off bits of the bill until you end up with a small piece in your fingers. Explain that this is what net profit looks like in your company. Drop the remaining piece on the ground and ask, "what if net profit goes to zero or less than zero – who is effected?" Essentially, we are explaining why it is so important that everyone helps hunt for net profit. I suggest that you also explain all the good things that happen when net profit improves. I know that some of you are not ready for a profit sharing program, but there are several other positives that come from increased net profit. We can invest in better equipment and software. We can continue to fund health care and other benefits. We can invest in new products. The list goes on. You must sell the team on the value of higher net profit. If you can do that, your shoulders just got a little broader.

Once your team is in a net profit state of mind, show them what happens if we can lower expenses by 1%. Explain how product damage diminishes net profit. I love to show warehouse employees how much additional sales volume we have to generate in order to make up for a \$100 error. By the way, it's approximately \$3,300 if your net before taxes is around 3% of revenue. I also love to share what happens if we can improve gross margin by 1%. Watch what happens to your inside sales team. I suspect that they will be more reluctant to discount prices by 5 or 10 percent. They may start understanding how 3 and 7 percent discounts can be just as effective.

For those of you who may still be a bit shy about handing out monthly income statements, I have an alternative. Instead of handing out a document with actual dollars, use percentages to represent different expense categories. You can either express them as a percentage of gross sales or as a percentage of gross margin depending on the audience. Tracking these numbers and discussing ways to improve them will generate creativity within the team. We have to start giving our people the benefit of the doubt. Go ahead, open the kimono just a little bit and prepare to be amazed.

About the Author:

Jason Bader is the managing partner of The Distribution Team, a firm that specializes in helping distributors become more profitable through strategic planning and operating efficiencies. The first 20 years of his career were spent working as a distributor. Today, he is a regular speaker at industry events and spends much of his time coaching distribution executives. For more information, call (503) 282-2333 or contact him by e-mail at Jason@Distributionteam.com. Also visit The Distribution Team's website at www.thedistributionteam.com.