Barrett Business Services, Inc. Fourth Quarter 2024 Earnings Call

Good afternoon, everyone, and thank you for participating in today's conference call to discuss BBSI's financial results for the fourth quarter and full year ended December 31, 2024. Joining us today are BBSI's President and CEO Mr. Gary Kramer and the company's CFO, Mr. Anthony Harris. Following their remarks, we'll open the call for your questions. Before we go further, please take note of the company's Safe Harbor statement within the meaning of the Private Securities Litigation Reform Act of 1995. The statement provides important cautions regarding forward looking statements. The company's remarks during today's conference call will include forward looking statements. These statements, along with other information presented that does not reflect historical fact, are subject to a number of risks and uncertainties. Actual results may differ materially from those implied by these forward looking statements. Please refer to the company's recent earnings release and to the company's quarterly and annual reports filed with the Securities and Exchange Commission. For more information about the risks and uncertainties that could cause actual results to differ from those expressed or implied by the forward looking statements.

I would like to remind everyone that this call will be available for replay through March 26, starting at 8 p.m. Eastern Time tonight. A webcast replay will also be available via the link provided in today's press release, as well as available on the company's website at www.BBSI.com. Now I would like to turn the call over to the President and Chief Executive Officer of BBSI, Mr. Gary Kramer. Sir, please go ahead.

Thank you. Good afternoon, everyone, and thank you for joining the call . I am pleased to report that we had a strong fourth quarter capping off an equally strong year. Our financial results exceeded our expectations and we are optimistic for the future. We continue to execute our short and long term objectives, and we added a record number of worksite employees from new clients. Before I speak about our financial performance, I would like to recap some of the key operational and strategic accomplishments for the year. We are successfully selling and servicing BBSI benefits in every one of our markets. We entered into an additional strategic, multi-year partnership with a new carrier that set us up for a great 1/1/25 selling season. Of the new clients, we are seeing success in white collar verticals that we previously had a difficult time penetrating. Our strategic sales initiatives have been operationalized and are resulting in a greater velocity at the top of the sales funnel, resulting in record WSEs. We have more referral partners that understand and appreciate our value proposition and are referring more business to BBSI. We continue to invest in our asset light model and have successfully expanded into new geographies and continue to gain momentum. We continue to invest in my BBSI and in our tech stack, which resulted in multiple product releases in 2024. And we are executing on exciting new product releases in 2025. We also made further advancements on our Employer of Choice initiative and earned the great place to work designation for a fourth year in a row.

Every year we conduct a survey of our clients to evaluate customer needs and satisfaction, and I am pleased to report that our Net Promoter Score increased 5 points to 69 points. This gives us great confidence in the value our clients place on the service and solutions we provide. Our clients love what we do and they are ready and willing to spread the word about BBSI. This is further illustrated in our record client retention rate for the year. 2024 was a great year with great results and I am proud of what our teams accomplished. Moving to our financial results and worksite employees. During the quarter, our gross billings increased 10% over the prior year quarter, which is greater than we expected. We continued to execute various strategies to increase the top of the sales funnel and we achieved a record number of worksite employees from new client adds during fourth quarter and for the full year. Our client retention set a record and exceeded our expectations in both the fourth quarter and the full year. I like to attribute that to the work we do with our clients and the value our teams provide. The result of all these efforts, or what I refer to as our control overgrowth, is that we added approximately 4,000 worksite employees year over year from net new clients, while our client growth remained below our historical averages, our clients workforce continue to grow modestly in the fourth quarter and was up sequentially and year over year. We anticipate these hiring trends will continue into 2025.

To summarize for the quarter, we grew our worksite employees by 5.2% as we sold and retained more business and benefited from our client net hiring. For the year, our gross billings grew 8%, driven by 4.2% growth in average WSEs. Moving to our staffing operations. Our staffing business declined by 9% over the prior year quarter and 7% for the year. Please note the rate of decline in our staffing business has slowed significantly compared to the previous year, and we are forecasting our staffing business to modestly grow in 2025 as our higher value recruitment offering for our PEO clients commands a higher share of the business. In fact, we continue to execute our strategy to recruit for our PEO clients and placed 103 applicants in the quarter. Moving to the field operational updates. We are very pleased with our entrance into new markets, with our asset light model. We have 21 total new market development managers in various stages of their development. These folks have been gaining traction and consistency. January was a big month. Our MDMs added over 500 new WSEs to three of the markets we hired additional local talent to support our clients. We anticipate having ribbon cutting ceremonies for our new brick and mortar branches by the end of second quarter. We continue to see positive results from our investments in new markets and are actively recruiting additional new market development managers.

Regarding product updates, we continue to execute on the sale and service of BBSI benefits. Our New Health Insurance Offering. To recap, we started off the year with 275 clients on our various plans with more than 6,800 total participants. Our plan was to double the book in 12 months, and I am pleased to say that we have exceeded our plans. At the end of January, we have approximately 575 clients on our various plans with more than 16,000 total participants. As a reminder, we partnered with Kaiser Permanente and added their best in class HMO product to our offering mid-year. We saw strong momentum in Q4 that carried into Q1 of this year due to the attractiveness of a national PPO side by side with Kaiser HMO in California. I'm very pleased with our teams, our progress, and our financial results. As we look forward to 2025, this product is now a profit center for us and we reap the benefit of leverage through scale. Our value proposition resonates well and we are having success with small and large clients in white and blue collar industries in every state we operate and with a diverse distribution channel.

Next, I'd like to shift to our 2025 IT product objectives. I previously mentioned that we have been investing in our tech stack on the product side to service and support our clients better. Over the last couple of years, we've made additional investments in myBBSI to support our BBSI Benefits offering learning management systems and to integrate with additional third parties. As we evolve and look forward to 2025, we will be making additional investments to round out the employee life cycle experience. We think of the employee life cycle from a client perspective, permanent employees hired to win the employee retires and everywhere in between. We will be replacing or bolstering attributes of the life cycle with additional product launches throughout the year. On Monday, we issued a press release for our first new product launch of the year BBSI Applicant Tracking System. This cutting edge tool allows for our clients to create job postings from our centralized system, which integrates with various third party job boards. Clients can manage the interview process in our system, and then when employees are hired, they integrate seamlessly with our payroll and timekeeping systems. This will help our clients with organization and create multiple efficiencies. You may ask, why are we doing this now? Simply put, our clients are asking for it. With our benefits offering, we are seeing larger clients. We are also seeing more white-collar businesses. This product will help support those clients and it's designed for the employer who has multiple hires per month. This does not replace BBSI Recruiting, which is our product that is utilized by our PEO clients for hard to place candidates for clients who don't have much velocity in hiring. We are excited about this launch and the future launches as we execute on our product roadmap in 2025. We are also making investments in systems and AI that will launch in 2025 to better support our employees and create efficiencies that Anthony will discuss in his prepared remarks.

Next, I would like to shift to my view of 2025. We have consistently achieved strong controllable growth by focusing on the needs of our clients and by adding new clients. Furthermore, we have also seen improvements in client hiring in 2024, especially in Q4, and we expect these hiring trends to continue in 2025. We have been executing on the sale and service of BBSI benefits this has become one of our core competencies. In IT product enhancements, rolling out more products to sell, more folks selling and more referral partners recommending BBSI. We will execute on our additional IT initiatives that are going to increase our efficiencies and also increase our financial results. We have a culture of taking care of our clients and for executing to a plan and I will be looking forward to 2025. Now I'm going to turn the call over to Anthony for his prepared remarks.

Thanks, Gary. And hello, everyone. I'm pleased to report that we finished the year with strong results and are off to a strong start in 2025. For the quarter, our gross billings increased 10% to $2.25 billion versus $2.05 billion in Q4 2023, while diluted earnings per share increased 17% to $0.63 compared to $0.54 in the prior year quarter. For the full year, gross billings increased 7.9% to $8.3 billion in 2024, versus $7.7 billion in the prior year.

While diluted earnings per share increased 7% to a $1.98 compared to $1.85 in the prior year. Looking at the quarterly results more closely. PEO gross billings increased 10% in the quarter while staffing revenues declined 9% to $20 million. Our PEO worksite employees grew by 5.2% in the quarter, which, as Gary noted, was driven by a record number of WSEs added from new clients in the fourth quarter. This continued a strong trend of controllable growth during the year and was once again combined with positive and improved client hiring in Q4. The pace of client hiring exceeded our expectations in the quarter, but still remains below our long term historical averages. We continue to see consistency in client hiring across most regions and across industries. Looking at wage rates and hours worked, total hours remained stable in the quarter, while overtime hours increased modestly year over year. Wage rates continue to increase and average billing per WSE increased 3.3% in the quarter.

Looking at year over year, PEO gross billings growth by region for Q4, East Coast grew by 21%, Southern California grew by 11%, Mountain grew by 10%, Northern California grew by 5% and the Pacific Northwest declined by 4%. Southern California represents our largest region and has improved to double digit growth through a combination of consistent client adds and stable customer hiring. The strong East Coast performance represents the 15th consecutive quarter of double digit growth in that region, also driven by a combination of strong controllable growth and above average client hiring. The Pacific Northwest region is our smallest region, comprising about 5% of our gross billings and continued to have the weakest client hiring. However, those trends have begun to stabilize and the region had a successful year in selling season. As such, we expect the Pacific Northwest region to return to growth in 2025.

Turning to margin and profitability, our workers' compensation program continues to perform well and benefit from favorable claim frequency trends and favorable claim development. This strong performance has once again resulted in favorable adjustments for prior year claims. In Q4 2024, we recognized favorable prior year liability and premium adjustments of $2.4 million compared to favorable adjustments of $5.4 million in the fourth quarter of 2023. As a reminder, our client workers' compensation exposure is now primarily covered by our fully insured program, with no retained claims risk by BBSI. As with past quarters, a cost savings we recognized in workers' compensation expense continue to offset pricing pressure and the workers' compensation insurance market, which continue to move overall rates lower.

Moving to SG&A, fourth quarter SG&A expense increased 7% on a year over year basis, primarily due to increases in variable employee compensation and incentive pay really the stronger financial results compared to the fourth quarter of 2023. For the full year 2024, SG&A expense increased by approximately 6%. We continue to see efficiencies from our operating investments in 2024 and prior, including investments in technology and new product support. As such, we expect our SG&A growth rate to slow in 2025 compared to 2024. Moving to investment income. Our investment portfolios earned $2.5 million in the fourth quarter, down approximately $300,000 from the prior year due to lower average interest rates. Our average investment balance is expected to remain stable in the year ahead, but average book yield will come down with short term rates decreasing year over year, leading to lower investment income in 2025. As a reminder, our investment portfolio continues to be managed conservatively with an average quality of investment at AA. Our balance sheet remains strong with $122 million of unrestricted cash in investments at December 31 and no debt. Our approach to capital allocation remains consistent, and that includes first making investments back into the company where we can. In 2024 these investments included several initiatives that Gary mentioned, including technology investments related to ongoing product development as we continue to invest in and expand our value proposition and investments in our sales team, including our asset light expansion in 2024. In 2025, we expect to continue these investments and we will launch additional systems and initiatives that will make our internal operations more efficient across our teams, including leveraging modern systems, AI tools and streamlined processes. We're also excited about the launch of additional sales technologies that should further improve our sales velocity, increase our operating efficiency, and help accelerate the success of our new sales team members. After investing in the company, we continue to generate excess cash flow and we continue to distribute excess capital to our shareholders through our dividend and stock buyback plan. Under our $75 million July 2023 repurchase program BBSI repurchased $7 million of shares in the fourth quarter at an average price of $43 per share, with $30 million remaining available under the program at quarter end. In total, in 2024, we repurchased over 3% of the company's shares outstanding through purchases of more than $29 million. We also paid over $8 million in dividends for the year, bringing total capital returned to shareholders in 2024 to $37 million.

Looking ahead to 2025, we expect to continue to generate excess available cash and to continue these capital allocation strategies. Now turning to our outlook for 2025. We expect gross billings and average WSEs to strengthen from 2024 with 2025 gross billings expected to increase between 7% and 9% and average WSEs to increase between 4% and 6%. As a reminder, 2025 includes one less business day, which equates to about a 0.5 percentage point lower billings growth. However, we expect that to be more than offset by continued growth in our net client adds a trend that has continued throughout 2024 and from continued but modest improvements in client hiring. For 2025, we expect gross margin to remain generally consistent with 2024 and range between 2.85% and 3.10%. There are two variables that I would like to call out. First, client payroll tax rates have increased in 2025, similar to the increases we saw in 2024. These rates are being reflected in our pricing, but may have some lag impacting the shape of our earnings. Second, we expect continued softness in workers' compensation pricing, offset by savings in our workers' compensation costs. And finally, we expect our effective annual tax rate to be between 26% and 27%.

I will now turn the call back to the operator for questions.

Thank you, sir. Ladies and gentlemen, we will now be conducting a question and answer session. Our first question comes from Chris Moore with CJS Securities. Please go ahead.

Hey, good evening, guys. Thanks for taking a couple questions and congrats on a good year and on the NPS score. Maybe we'll talk about obviously higher wages in a vacuum positive for you guys. What are you hearing from clients in terms of being able to continue to grow in the current environment, it sounds like hiring is picking up a little bit, but just any further thoughts there?

Yeah. Thanks, Chris. This is Anthony. We're really seeing stability and recovery in those metrics. So, first of all, you mentioned, wage inflation. We've continued to see consistent wage inflation every year. And that's a baseline driver of growth for us. And we're seeing that rate remain stable. We continue to see on a year over year and sequential basis, wage inflation remain consistent. In terms of hiring, we've seen that trend improve during the year and notably in Q3 and Q4. We also saw overtime hours improve in the year, also indicating kind of increased activity at our clients. So as I mentioned in my remarks in our outlook, we're cautiously optimistic. We're expecting only modest improvement for the purposes of our outlook. But we see the trends are favorable.

Got it. I appreciate that. Average WSE growth is targeting around 5% this year. Just want to – the majority of those are coming from new clients, correct?

Yeah. That's going to be the lion's share of our growth is going to come from our controllable growth, which is the clients we had, the WSEs they have and the clients we retain.

Got it. And maybe one more on the healthcare side. Can you just maybe talk a little bit about the mechanics of how you get paid on healthcare, like reseller fees versus admin fee expansion and where that looks to go over time in terms of that split?

Yeah. We had a very – I mean, when we were last quarter when we were giving our earnings call and we kind of talked about how we saw 2025 shaping up. It was going to be similar to the 2024 that was before we had a really good close of the year, a really good start of the year. So we closed out the year really strong and we had a great January selling season, the best January selling season we've ever had by far like 20% more new business than we did in any other January. So we really finished strong and started strong and because of that we moved up our gross billings estimate by like 200 basis points from what we originally thought, if you would ask me a quarter ago. So a portion of that was allocated to the strength in how we closed with our benefits products. So we doubled the number that we wanted for one business. So we crushed our floor plan for 1/1 and we crushed our plan for the back half of the year. So if you just think of getting that finishing strong and starting strong, you get the compounding effect of having that earned through your financials for the full year. So for the earn through the financials for the full year, on the healthcare, number one, we don't take any health insurance risk, right. We don't take any risk on the on the workers' comp or marginal small risk on the workers' comp and no risk on the health insurance. But the health insurance, we get a – we get as a seller's fee. So we get like a commission from the market for selling the product, number one. And then number two, because we handle the administration, the compliance, the enrollment, the IT and we're able to provide good value with that product. We're able to charge a little more for our PEO. And so we get a little bit from the market and we're able to charge the clients a little more because of the value is there.

Got it. And I'm sorry, last one on the healthcare revenue side. Is that something that you would eventually break out on the financials to give investors a look, couple of years down the line, what's being generated there?

Yeah. It's something we've talked about and we want to make sure we're disclosing the right metrics for understanding the business. One of the nuances of disclosing a revenue number for benefits is just from the question you asked, is really our kind of income generated from that program is twofold, right. It's kind of the reseller fees, but it really is packaged together with our overall admin fee that represents the value we're providing to our clients right. And a big part of that now is health benefit. So kind of that is we think about the profitability of that program. The income is more than just the reseller fee. It's also that admin fee expansion. So we're being thoughtful about how we present that and disclose that. But absolutely, we'll continue to expand those disclosures.

Okay. I appreciate it. I'll jump back in line.

Thank you. Our next question comes from Jeff Martin with Roth Capital Partners, LLC. Please go ahead.

Thanks, Gary Kramer, Anthony, how are you doing?

Good.

So, Kramer, I wanted to drill down on the tech investments. It sounds like this is in part I mean, I'm sure this is part of a roadmap that have been planned for quite a while. But just curious if you've enhanced your technology initiatives or your technology product initiatives as a result of starting to attract, non-traditional clients in the white collar space and larger clients?

Yeah. So we have – when you're running a company, the biggest decisions you have to make is strategy and allocating capital. And if you think of how we've shifted over the years, right. We've repositioned the product to sell health insurance, to have a learning management system for all these different things. And those all have an IT component to them right. So we have been really investing in bolstering up our IT tech stack for the last three years to support the business. And that was really designed for the products that we were trying to launch. Now we're really thinking at of using software as a I don't want to say software as a service, but using software to help support our business and to help support the business. The first one we've launched is the applicant tracking, right. And it's pretty cool because if you're a client and you hire a lot and it could be anything from a franchise to you name it right. It doesn't need to be just like an office worker. It could be anything in the – in that space. And there's a lot of volume in the hiring. But the basic idea is you can come into our system. We have a bunch of job descriptions that are curated. You can take the job descriptions. You can then modify it to better fit your company. You can post it, post out the different job boards. People go in and apply. When they apply, they come into our system. When they come into our system, depending upon how the client has set up, they can ask them questions, do screening, do the interviews in there or push out e-mails and calendars and all those things. Okay, now we want to hire the person. Hire the person, boom. We push out the I-9, the background checks, the different forms through our system. Okay , now they passed all that boom, we want to hire them. And then they go right into payroll, into our payroll platform and into our timekeeping system today if they buy our timekeeping systems. So, that's the front end and that's what we talk about on the employee life cycle right. So it's how do you attract clients, how do you bring them in, how do you hire them? That's the first step. I would say that we're building out in 2025 and we launched it this week and we're going to start selling it in March. But the idea is that the front end and then throughout the year, we're going to have additional products that come out that support that employee, that client employee life cycle. So you'll see more of this coming out in the back half of the year. We've got a roadmap that's going to be a couple of years until we get to what I would call best in class.

Okay great. And on the payroll tax side, I think you were I think rates were due for a catch up was that – what did the rate come in in line with your expectations, did it surprise you, to the extent that it cost you a little bit of margin relative to your initial budget for the year? And is there an ability to recapture some of that, if that's the case with pricing?

Yeah. Jeff, it's Anthony. You're correct that rates were due for a catch up to some extent right. They have been coming down for multiple years in a row. Last year they went up. This year they went up as well. But I would say very much in line with expectations. We saw that trend coming. We see that unemployment activity and that was in line with our expectations. That said, every client in our client reporting states like California has at their own rate. And so we need to wait till those rates come in to effectively reprice most of them. So we have processes to do that. But as I mentioned, there is some lag in that at the end of the day that will be captured. But there may be some change in the shape of our earnings, a little bit more of a loss in Q1. We saw that trend last year as well. But overall, especially over a rolling 12 months, we're not expecting margin degradation.

Okay, great. And then one more, if I could. It's a two part question. One, any signs of a turnaround in the pricing side of the workers' comp market? And then secondly, what is your exposure to businesses that have been affected by the California wildfires?

Kind of the joke in the organization is I've been trying to call the bottom for workers' comp for six years and I've been calling it wrong, you're seeing a deceleration in rate decreases now. It hasn't flattened. It's still trending downward, but at a much smaller rate. So I would think workers' comp is going to decelerate slower from here and we're seeing that in the market. But it's still – there's still pressure if it's a good account and attracts a lot of buyers. And when there's a lot of buyers, it drives down the price, if that makes sense. So we don't see the bottom yet. We're hopeful that we're going to see the bottom soon. But ultimately, it's the market doing what the market does. And I think it's going to turn sooner than later. But I don't – I can't pinpoint when it's going to turn. For the California wildfires, directly for us, I'd say for our employees, there was a minimal employee that were affected. There was minimal branches that were affected. We did have evacuated a couple of times. But no, there is no loss of property on our branch side when we think of our clients, the Palisades and Malibu per se, they are not big grounds for our clients. So we had minimal client effects. I think we had one client who had his facility burned down, but out of, call it 8,500 clients have one that was affected by it. Like we would call it, almost nothing. The real question that we think is, unfortunately, when there's a tragedy the way it was, it's got to get rebuilt. And when it gets rebuilt, we think of our clients being prone in position to capitalize on the – especially in our blue collar, to capitalize on the rebuild. So we think a lot of our clients will get business from the rebuild. We've seen it with our restoration companies already. I think if the restoration types of companies that go in and do the rehab for the water damages or the fire damages, we've seen them boom already. What we haven't seen yet is the construction uptick. But ultimately that will follow. I don't know if that's going to be a 2025 event or if that's going to be 2026 by the time all the permitting and everything shakes out. But we definitely think that that business specifically is going to have a tailwind in California for us.

Great. I appreciate the thoughts.

Thank you. Our next question comes from the line of Marc Riddick with Sidoti & Company LLC. Please go ahead.

Hey, good evening.

Hi, Marc.

Hello. I wanted to follow up on your comment of the strong finish to the year and strong beginning to the year. I was wondering if you could talk a little bit about maybe if you're seeing any particular client industry verticals that are kind of leading the way there. You touched a little bit on construction, but are there any sort of call outs that you're seeing that might be leading away in that activity?

Marc, I would say it's not so much related to any one geography or any one industry. I would say broad based. The company just did well in Q4 and the company did well in January. The one call out I did give in my script was our asset light, our market development managers. They added over 500 WSEs in January, which is a really good accomplishment for them. We're starting to see consistency out of that group and I'm looking forward to watching that grow.

Great. And then I was wondering if you could maybe sort of discuss with benefits the – I know it's sort of early into a new year or what have you, but maybe can you sort of talk about where you are currently from a competitive positioning standpoint, maybe some of the call outs that give you confidence in the strength of the of the adds that you've seen to date, which are and I appreciate the detail and update on that data. But maybe some of the things that you think sort of are helping you sort of stand out in that area, particularly with the pickup on the white collar side that you alluded to earlier in your prepared remarks?

Yeah. If you just kind of take a step back and look at our value prop right. We're going to – we've got more products now with benefits and with other things in IT. We're going to have more IT products coming out, but they will never replace our core product, which is our people right. So people are our products. They will always be our product. That's our differentiator in the local market. So if I can have a local team that is second to none and then I've got all of these additional products and if those products are even if they were equal to the different marketplace, if you can be equal to the marketplace, plus have that killer team there, it's going to be hard to beat us, right. If it's – if the price is the same and you get our teams, it's going to be hard to not go BBSI. And that's why we're seeing the uptick in sales.

Great. And then congratulations again on the net promoter progress that you made there as well. That's certainly a positive as well. Thanks.

Well, thank you.

Thank you. At this time, this concludes the question and answer session. I would now like to turn the call back over to Mr. Kramer for closing remarks.

I want to thank everybody for dialing in and thanks, everybody all of our BBSI professionals for a great Q4 and a really for a great start of the year. I'm looking forward to 2025. Thank you.

Thank you. This concludes today's teleconference. You may disconnect your lines at this time. Thank you for your participation.