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ADEN.VX - Q4 & Full Year 2013 Adecco SA Earnings Conference Call

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PRESENTATION

Operator

Ladies and gentlemen, good morning. Welcome to the Adecco Q4 results 2013 analyst conference call. I'm Selena, the Chorus Call operator. I would like to remind you that the conference is being recorded. (Operator Instructions). The conference must not be recorded for publication and broadcast.

At this time, it is my pleasure to hand over to Mr. David Hancock, Head of Investor Relations; accompanied by Mr. Patrick De Maeseneire, CEO of the Group; and Mr. Dominik de Daniel, CFO of the Group. Please go ahead, gentlemen.

David Hancock *- Adecco S.A. - Head of IR*

Thank you and good morning. Welcome to Adecco's fourth quarter and full-year 2014 results conference call. Patrick De Maeseneire, Group CEO; and Dominik de Daniel, Group CFO, will lead you through the presentation today, followed by a Q&A session.

Before we start, please have a quick look at the disclaimer regarding forward-looking statements in this presentation.

So let me give you a quick overview of today's agenda. Patrick will present the operational highlights, then Dominik will review the financials and, finally, Patrick will make some comments on the outlook. We will then open the lines for your questions.

With that, Patrick, I hand over to you.

Patrick De Maeseneire - *Adecco S.A. - CEO*

Thank you, David. Good morning, ladies and gentlemen, and welcome to our full year and Q4 2013 results conference call.

First, a few remarks on the results for the full-year 2013, which was marked by a difficult, but improving economical environment.

Revenues for the year were EUR19.5 billion, down 5% or down 1% organically. Professional staffing revenues held up well, increasing 1% organically.

General staffing revenues declined by 2% organically, but there was a clear improvement during the year, led by the industrial business which grew by 6% in constant currency in Q4.

Geographically, we saw an improving trend in all European regions and in the emerging markets, and solid growth in North America. Our gross margin improved strongly in 2013; up 40 basis points to 18.3%. We benefited from our strict price discipline, a better business and country mix and the impact of the French CICE.

Our focus on cost control was maintained. SG&A was down 1% year on year organically and excluding restructuring and integration costs.

Despite the revenue decline, we improved profitability. We achieved an EBITA margin, excluding restructuring costs, of 4.4%, up 40 basis points.

For 2013, the Board of Directors proposes a dividend of CHF2, an increase of 11% over the prior year and a 47% payout ratio of adjusted earnings. This reflects our solid balance sheet, our strong performance in 2013 and our confidence in the outlook.

We continue to be very focused on reaching our EBITA margin target of above 5.5% in 2015. Based on the good progress on our six strategic priorities, recent trends and more favorable economic conditions expected going forward, we are convinced that we will achieve this target.

Let me now focus on the highlights of the fourth quarter, where my colleagues worldwide delivered an excellent performance.

We had revenues of EUR5 billion, up 4% in constant currency. Gross profit grew by 7% in constant currency and the gross margin was 18.3%, up 50 basis points year on year.

Costs continue to be well controlled. SG&A in constant currency and excluding restructuring costs, was up 1% year on year and up 3% sequentially, driven by seasonality and some limited investments.

This resulted in EBITA, excluding restructuring costs, of EUR238 million, an increase of 30% in constant currency. The EBITA margin, excluding restructuring costs, was 4.8%, up 90 basis points on the prior year.

Coming into 2014, we have maintained our momentum. In January and February, revenues were up 5% in constant currency and adjusted for trading days.

We now have a look at the fourth-quarter revenue development by region in constant currency. In North America, growth was solid, up 3% year on year. Both general and professional staffing contributed to the good growth trends.

In Europe, revenues were up 5% in the quarter, with all regions either growing or showing flat revenue development. This is in clear contrast to the beginning of the year, when in Q1, all our regions in Continental Europe declined.

Rest of world was up 2%. In Japan, the rate of revenue decline eased further to 3% in the quarter. Australia and New Zealand remain difficult; Here our revenues declined by 22%, impacted by the contract losses that we mentioned last quarter.

By contrast, emerging markets revenues grew 11%, with further acceleration in Eastern Europe.

We go through our main markets now. In France, revenues were EUR1.2 billion, flat year on year after two years of decline. From an industry perspective, we saw a significant improvement in our largest cyclical sectors and solid growth in manufacturing.

Our perm revenues were down 1% in the quarter compared to minus 15% in Q3. As we have previously indicated, we have taken additional restructuring actions in 2013 to optimize our cost base. In the quarter under review, we incurred EUR10 million restructuring cost.

EBITA margin, excluding restructuring costs, was strong at 6% compared to 2.8% in the same period last year. This improvement was driven mainly by cost efficiencies, price discipline and the impact of CICE.

In addition, Q4 2013 included several one-time items, which together added approximately 50 basis points to the EBITA margin in France.

For January and February, revenues were flat year on year adjusted for trading days.

We turn now to North America. Growth rates are in constant currency year. Revenues were up 3% to EUR928 million, with growth of 4% in general staffing and 2% in professional staffing.

Within general staffing, we saw strong acceleration in the industrial business, with growth of 14% in Q4 after 7% in Q3. This was driven by good demand from the automotive, logistics and chemical industries.

The office business remained soft, declining 6%, primarily due to less demand in the financial services sector.

Within professional staffing, IT and engineering and technical are our two largest businesses. The North American IT business grew 5% year on year, driven again by good growth in the US of 8%. In engineering and technical, revenues were up 2%.

In perm, we continue to deliver a very strong performance, with revenue growth of 17%. EBITA margin, excluding restructuring costs, was 5% in the quarter, up 70 basis points year on year.

At the start of 2014, our business was impacted by the adverse weather conditions. Revenues for January and February were up 2% in constant currency and adjusted for trading days.

Revenues in the UK and Ireland amounted to EUR501 million, up 7% in constant currency. We delivered solid growth in both general and professional staffing, with 7% growth in professional staffing and 5% growth in general staffing.

Perm revenues were positive in the quarter, with 2% growth on a constant currency basis. The EBITA margin, excluding restructuring costs, was 2.5% compared to 2.9% in Q4 2012, partly driven by mix effects. Revenues for January and February were up 8% in constant currency and adjusted for trading days.

In Germany and Austria, revenues were up 10%, a good acceleration compared to the 4% growth in the third quarter. This was driven by a pickup in our industrial business, which grew by 14% in the quarter.

In the manufacturing sector, we saw very strong double-digit growth and growth in automotive continued to be good.

EBITA was EUR16 million, given an EBITA margin of 3.9%, down 40 basis points compared to the adjusted margin in Q4 2012.

During Q4 2013, a new collective wage agreement took effect from November 1, leading to higher payments during vacation and sickness, and salary increases as of January 2014.

This negatively impacted profitability in Q4 2013 by approximately 90 basis points, of which approximately 60 basis points is due to a catchup of existing accruals.

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For January and February, revenues were up 12% adjusted for trading days.

In Japan, revenues were down 3% in constant currency. Our business in Japan is focused on clerical, which is typically later to benefit from a pickup in economical activity. That said, our early cyclical engineering business did see continued solid growth.

Despite the revenue decline, profitability improved further thanks to solid growth in perm and in professional staffing and continued cost reductions.

As a result, the EBITA margin was 6.4%, up 90 basis points compared to Q4 2014. For January and February, revenues were down 2% in constant currency and adjusted for trading days.

Finally, we turn to our revenue development by business line on a constant currency basis. In Q4 2013, revenues in general staffing were up 4% compared to flat in Q3. This improvement was driven by the industrial business, up 6%. The office business was up 1%.

Revenues in professional staffing grew by 2% in Q4, driven primarily by growth in IT. Our solutions business increased by 16%. Revenues at Lee Hecht Harrison, our replacement business, were up 12%, continuing to outperform the market. Revenue growth was strongly double digit in MSP, RPO and VMS.

And with this, I hand over to Dominik to discuss the financials in more detail with you.

Dominik de Daniel - *Adecco S.A. - CFO*

Thank you, Patrick. Good morning, ladies and gentlemen. I will start with the overview of the P&L.

In Q4 2013, revenues were EUR5 billion; this was an increase of 4% in constant currency. However, on the reported basis, revenues were down 1% and we continued to have a significant currency headwind.

Gross profit grew by 7% in constant currency and the gross margin was 18.3%, up by 50 basis points year on year.

SG&A was down 7%, or down 3% in constant currency compared to the prior year. SG&A, excluding restructuring cost, was 1% higher year on year in constant currency.

Sequentially, the cost base was up 3% in constant currency and when excluding restructuring costs, partly due to seasonality.

EBITA was EUR221 million. Excluding restructuring cost EBITA was EUR238 million in the quarter under review.

The margin was 4.8% in Q4 2013, excluding restructuring costs; an increase of 90 basis points year on year.

Net income in the quarter under review was EUR174 million.

Let's have a look at the year-on-year gross margin evolution. The Group's gross margin was 18.3% in Q4 2013; up by 50 basis points year on year.

Temporary staffing had a 40 basis points positive impact on the gross margin in the quarter under review, and the outplacement business added a further 10 basis points. Outplacement and other activities had a neutral effect on gross margin this quarter.

Now, let me discuss how our cost base developed in the fourth quarter. We continued to monitor revenue development closely and managed the cost base accordingly.

SG&A in Q4 was up 1%, compared to the same quarter last year, in constant currency and excluding restructuring costs. This mainly reflects mix effects and higher bonuses, resulting from the strong performance in Q4 2013.

In the quarter, FTEs were down 3% and the branch networks decreased by 7% compared to the prior year.

Our Q4 2013 results included EUR17 million restructuring costs compared to EUR46 million restructuring costs in the same period last year.

Sequentially, our cost base was up 3% in constant currency and excluding restructuring costs, due to seasonality and some limited investments in businesses where productivity is already at a high level.

SG&A for the first quarter this year is expected to be slightly up compared to Q4 2013 in constant currency and excluding restructuring costs.

Moving onto the balance sheet. Our cash position was EUR963 million at the end of the quarter.

DSO was 54 days in 2013; the same as in 2012.

Goodwill and intangible assets amounted to EUR3.9 billion at the end of December, and Adecco's shareholders' equity was EUR3.6 billion.

In September 2013, we completed our EUR400 million share buyback program, and launched a new program of up to EUR250 million. This is also being executed on a second trading line, with the aim of subsequently canceling the shares. So far, we have bought back shares for EUR25 million under this second program.

At the AGM, the Board of Directors will propose the cancelation of all shares that have been repurchased on the second trading line until the end of 2013. The total number of shares to be canceled is 10.2 million, representing a reduction of share capital of 5.4%.

Turning to the cash flow statement. In 2013, cash flow from operating activities was EUR520 million compared to EUR579 million in the same period last year. This year-on-year reduction was partly driven by higher working capital requirements towards the end of the year, as growth picked up.

In 2013, the Group invested EUR81 million in CapEx. We expect to spend in 2014 approximately EUR100 million as we further invest in the consolidation of our IT platforms.

During the year, we paid EUR297 million related to the purchase of own shares, and the dividend payment in May was EUR266 million.

Let us look for a moment to the dividend. Strong cash generation is a key focus for Adecco. This supports our dividend policy, which is for a payout ratio of 40% to 50% of adjusted earnings, and each year a dividend at least at the level of the prior year, barring seriously adverse economic conditions.

For 2013, the Board of Directors proposes a dividend per share of CHF2. This is an increase of 11% over the prior year, and a payout ratio of 47% of adjusted earnings.

The total amount of the dividend distribution for 2013 is intended to be paid out from Adecco's reserve from capital contribution, and is, therefore, expected to be exempt from Swiss reporting tax.

Net debt at the end of December 2013 was EUR1.1 billion compared to EUR1.3 billion at the end of September 2013.

Our financial guidance for the full-year 2014 is as follows. CapEx for the year is expected to be around EUR100 million.

Interest expenses, excluding interest income, are expected to be around EUR65 million for 2014. We anticipate corporate costs of approx EUR100 million. And amortization of intangible assets is expected to be approx EUR35 million.

The underlying tax rate for Q1 is expected to be around 28%.

In 2014, we also expect to incur restructuring expenses of approx EUR20 million. This is for the move to a single headquarter in North America, and several smaller projects in other countries.

With this, I hand back to Patrick.

Patrick De Maeseneire - *Adecco S.A. - CEO*

Thank you, Dominik. Ladies and gentlemen, let me finish with the outlook for our business. Most European countries has begun to recover. In Q4 2013, we delivered particularly good growth in Benelux, Iberia, Germany and Austria and Italy. In fact, revenues in all our European regions grew, or were at least flat.

We also saw a strong pickup in the Group's early cyclical industrial business, driven by double-digit growth in the manufacturing sector. In 2014, we expect the amount for flexible labor to increase to increase.

For January and February, revenue growth in constant currency and adjusted for trading days was 5%.

In general, revenue trends by geography remain similar to Q4 2013, although North America had some impact from the adverse weather conditions. And we saw a further improvement in the Nordics, in Iberia and the emerging markets.

We continue to be very focused on reaching our EBITA margin target of above 5.5% in 2015. And as said, based on the good progress on our six strategic priorities, recent trends and more favorable economic conditions expected going forward, we are convinced we will achieve this target.

With this, I would like to open the floor for your questions.

QUESTIONS AND ANSWERS

Operator

We will now begin the question and answer session. (Operator Instructions). Paul Sullivan, Barclays.

Paul Sullivan - *Barclays - Analyst*

Just a couple from me. Can you -- is there an easy way just to describe, or give us the dynamics, around the margin impact from CICE in France this year, and also the CLAs in Germany? I don't know if you can simplify the dynamics there for us. That's the first question.

And then the second question --

Dominik de Daniel - *Adecco S.A. - CFO*

Shall I take it directly, before the second question? So, for the CICE impact, you cannot look any more isolated to CICE, because it's part of the business. It's fully integrated and part of it, we spent in training. Then here and there we have difficulty to pass on indirect labor costs, so you cannot look isolated at it.

But what I can give you as a kind of guidance, and this is for me the right way to look to it, if you look to our margin increase in France in Q4, you could basically say that a bit more than half of this margin increase is thanks to gross margin increase, which is obviously then related, to a large extent, CICE, or it is CICE; and the other, little bit less than half, is operational leverage, as we restructured and benefit from this restructuring.

Regarding Germany, we clearly indicated that 90 basis points of our German margin in Q4 is related to this new collective wage agreement. Now, out of this 90 basis point, 60 basis points is a catchup for two reasons.

What are the changes with the new collective wage agreement? On the one hand, we will have wage inflation as of January 1 in Western Germany, but also in Eastern Germany. And furthermore, we have the new calculation what we have to pay to our temps during vacation, during sickness.

Up to now, or up to, let's say, November 1, it was done in the way that we paid the normally hourly rate, and now we have always to go back the last 12 weeks to look what was the average rate, and we have to apply this kind of rate. And the rate is different because often people do overtime. In the industrial business people work on shifts, or work on weekend, and have with these surpluses.

On top of that, people who are, for a certain time, in different clients have surpluses, or surpluses for how long they stay with the client. With the new collective wage agreement, all these things are considered also now for sickness and for vacation.

So what does it mean? We have to adjust our existing accruals in terms of vacation, but also in terms of overtime. And overtime is a big chunk in our balance sheet, because we want to have a lot of overtime on the balance sheet in order to manage the bench.

So from the 90 basis points, 60 basis points is a catchup; the other 30 basis points is the normal ongoing rate, fair to say, for two months, because this new calculation is effect as of November 1. And, of course, we're aiming to pass this on with price increases over time, as this is normal wage inflation.

Patrick De Maeseneire - *Adecco S.A. - CEO*

The second question was?

Paul Sullivan - *Barclays - Analyst*

Yes. No, it's following on from that. In Germany, the 12% in January and February, can you break that down between volume and price?

Dominik de Daniel - *Adecco S.A. - CFO*

Let's say, the price increase is high single digit, and the volume increase is, therefore, low single digit.

Paul Sullivan - *Barclays - Analyst*

Thank you very much.

Operator

Anasuya Sarma, JPMorgan.

Anasuya Sarma - *JPMorgan - Analyst*

My question is on margin. How much of the margin improvement was due to productivity, and how much do you think was due to the leverage to organic growth?

Secondly, is there any upside to your margin target? And if so, what would we need to see to see that further upside?

Dominik de Daniel - *Adecco S.A. - CFO*

If you look to the margin increase, the EBITA margin before restructuring costs was up 90 basis points. 50 basis points is gross margin and 40 basis points is productivity.

Patrick De Maeseneire - *Adecco S.A. - CEO*

And as far as the target is concerned, we always said that the 5.5% is a minimum target. We never achieved it in the past, so the 5.5% is clearly our target. If we can do more, we will do more.

Anasuya Sarma - *JPMorgan - Analyst*

Okay, thank you.

Operator

Alain Oberhuber, MainFirst Bank AG.

Alain Oberhuber - *MainFirst Bank AG - Analyst*

I have two questions. The first is about CICE coming back again. Are we still going for the year 2015? And after that, we do not know if it's continuing? Probably you could just give a little more insight in that?

And the second question is what happened to the medical business because it was down single digit?

Patrick De Maeseneire - *Adecco S.A. - CEO*

Okay. On the CICE, Alain, we -- this is a law which is implemented and there is not a time limit for it. We go out of the assumption that it's at least for three years, but there's not a time limit for it.

It was introduced with 4%; and for the current year, it's 6%; and also for next year, it's 6%. It's not supposed to change afterwards but, of course, laws can always change, so we don't have control over this.

Having said this, as you might have heard, President Hollande has started to look into attract more companies and more investments into France and united a number of CEOs a couple of weeks ago from international companies.

I was there as well and he clearly said that this, going forward, he wants to lower taxes on especially lower salaries, in order to make France more competitive.

So I don't expect any changes on the CICE, but again, it's not in our hands. It's in the hands of the politicians, but it's clearly going forward, the French Government wants to do something about the competitiveness in France.

Dominik de Daniel - *Adecco S.A. - CFO*

Alain, regarding the medical and sciences, it's a small business for us and the biggest business in the US. In the US, we have a pretty flattish development for the time being, but the second biggest business is in France. The French market in the medical business is materially down as hospitals, which are the end clients for this business, are cutting back spending.

Alain Oberhuber - *MainFirst Bank AG - Analyst*

Thank you very much. Just an add-on question coming back to IT. Can you just elaborate a little bit on the US IT business, as well as on the UK IT business?

Patrick De Maeseneire - *Adecco S.A. - CEO*

In the US, our business was up 8%. For the whole of North America, it was up 5%, so which means that we are still down in Canada. We see that now also Canada in the first months of the year is improving, so the situation is there now also under control I would say. And so going forwards, yes, this will be a good development.

Dominik de Daniel - *Adecco S.A. - CFO*

On the IT side in the UK, the IT business is growing the last quarter 10%. It's a further acceleration where we basically accelerate from quarter to quarter.

It's mainly demand in financial service industry for replacing systems, but also the case that we won a nice MSP account where we deliver now the IT skills there.

Alain Oberhuber - *MainFirst Bank AG - Analyst*

Thank you very much.

Operator

Tom Sykes, Deutsche Bank.

Tom Sykes - *Deutsche Bank Research - Analyst*

Just going back to the CICE, sorry, again, was the -- could you say on the gross margin, whether the CICE benefit was more than 100% of the change in the French gross margin; i.e., if you exclude the CICE benefit, would the French gross margins been up, down or flat? And could you just confirm, was there actually any CICE benefit in Q4 2012?

Then also in -- for the outplacement business, could you maybe describe what the outlook is for the outplacement business please, because obviously, that's been quite strong growth?

And then, just on your US industrial revenues, you're obviously growing at 14% and at -- or sorry, your North American industrial revenues. I think you said that, in the appendix, your North American revenues are down about 11% from peak.

Could you just say where your industrial revenues are relative to peak and maybe give some view on where the market's industrial revenues are relative to their previous peak please?

Dominik de Daniel - *Adecco S.A. - CFO*

Tom, Dominik speaking. So if you're going to look to CICE, you cannot look isolated any more. And what we always said is that we protect CICE and I think you see this in the profitability because I don't recall a quarter where we have 5.5% if you take the one-offs out in France in the history, I would say at least not the last 10 years.

So, from this point of view, of course, we protect this very well, but it's fair to say that we have situations where indirect labor costs going up or where RPs coming in, where we cannot pass fully on the indirect labor costs. So it's fair to say that the gross CICE impact would be higher than the real gross margin. This is very normal.

We said also at the beginning of last year, we have to see how much is not directly but indirectly, competed away. If we now look one year later and look to the profitability of our French business, it worked out, in our view, better than we maybe thought one year ago.

So, from the margin increase, which you had in Q4, you can say a bit more than 50% is because of gross margin, which CICE is the driver, and a bit less than 50% is the productivity increase.

We had last year in Q4 2012 no CICE impact. This started -- we recognized this as of January 1. In December 2013, we had, however, already the 6%. So the 6% which is applicable for 2014 is already applicable for December 2013. So the Q4 is a quarter with two months 4% and one month 6%.

Patrick De Maeseneire - *Adecco S.A. - CEO*

Because these salaries are paid in January.

Dominik de Daniel - *Adecco S.A. - CFO*

Because the salaries are paid in January and that's the reason. It's a cash flow problem -- look -- cash flow [in this case].

Patrick De Maeseneire - *Adecco S.A. - CEO*

So on Lee Hecht, revenues are indeed up 12%. You know we are taking market share there, so I would say that this is now the total picture for the industry, but we've clearly seen an acceleration in Europe and mainly in France and in Germany.

Also in the US, it's still holding up pretty well and especially in the financial services and pharmaceutical companies. But again, we are gaining market share there because we are a true global organized Company and this is what our customers really appreciate us with the quality of the services and this is clear with the 12% growth.

Dominik de Daniel - *Adecco S.A. - CFO*

Yes. We are optimistic for this business because even if we have a moderate economic environment, there will be still a lot of companies who have to restructure, they have to become more competitive and we benefit from it.

Will you see now the next quarters double digit? I don't think so, but we believe we will have solid growth in this business going forward.

Patrick De Maeseneire - *Adecco S.A. - CEO*

And on your third question on the industrial, Tom. I don't know how much you can compare because, of course, every cycle and every drop-off has been different in the past couple of years, but you know we have had growth rates.

If I look in the past, 2010, we had growth rates of 23%, 24% in the industrial business. In the second and in the third -- sorry, in the first quarter of 2011, we even had a growth rate of 27% in the industrial business.

But again, you have to compare that also to the base. We have now growth, at 6% we see that there's clearly still room for further acceleration there.

Tom Sykes - *Deutsche Bank Research - Analyst*

Yes, it's not really the Group's industrial business, it's just specifically on the US. And I know you've obviously made acquisitions and I don't know whether your appendix includes the acquisitions or not, but one presumes that clerical is probably down a bit more than 11% from its peak. But one wonders where perhaps the professional is, maybe as well given the IT that just the rebound in industrial. I'm assuming you're closer to your previous peak in industrial than maybe clerical or professional is.

Dominik de Daniel - *Adecco S.A. - CFO*

This is the right assumption. Yes, that's correct.

Tom Sykes - *Deutsche Bank Research - Analyst*

Okay.

Dominik de Daniel - *Adecco S.A. - CFO*

And then, of course, no acquisitions included; this is pure organic outperformance, yes, particularly is arising from (inaudible), yes.

Tom Sykes - *Deutsche Bank Research - Analyst*

Okay. And just the immediate outlook for US industrial would continue to be positive, given the plus 14% growth that you're seeing now?

Dominik de Daniel - *Adecco S.A. - CFO*

Let's say the 14% is, of course, very strong and we continue to be positive also into Q1, very positive for the industrial business. But the industrial business had a bit of weather impact also, especially in the (inaudible) business, so -- but the growth will be still very solid in the start into Q1 in the US.

Tom Sykes - *Deutsche Bank Research - Analyst*

Okay, sure. Okay, thank you very much. Thanks.

Operator

Rolf Kunz, Bank am Bellevue.

Rolf Kunz - *Bank am Bellevue - Analyst*

I have a question on professional staffing again. I'm actually wondering here a bit why professional staffing is not also showing sequential growth improvement and actually growing faster than the 2%. Many times in the past and in general, I thought that professional staffing is actually higher growth than general staffing.

And with regards to your EBITA margin target, what should we expect from professional going forward? What assumptions do you expect from professional with regard to the achievement of the EBITA margin target? Thank you.

Dominik de Daniel - *Adecco S.A. - CFO*

If you look to professional staffing, professional staffing is, in general, later cyclical and it's not that we now have several quarters of growth in industrial. We have now 6%. We were before just plotting the growth line in Q3. Office is now, after a decline the quarter before, also just back to growth a little bit.

So, from this point of view, we are still rather early in the cycle because industrial was up in Q3 1% and now, it's up 6%. So it takes a half-year or so, it depends always on different circumstances and different economies when the professional recover.

But it takes -- there's always a time lag of around six months and then it depends also on the skill set. Normally IT and engineering is more cyclical, they actually see it a little bit earlier; in other areas, you see it a little bit later.

Now that said, if you look to the US, we have seen quite solid growth rates in our professional starting business, especially in the IT over the last 18 months and US was not in this kind of downturn; and in Europe, it's just too early.

Patrick De Maeseneire - *Adecco S.A. - CEO*

And you see that also in Germany, Rolf, that the growth there, we said it this morning, also in the press release, it's mainly driven by industrial and where it -- which is more than -- which is fairly solid double digit. And so, on your question what will it do to the target, we expect professional staffing to have higher growth. But like Dominik is saying, there is always a time lag and this will take a couple of quarters before this comes really through.

Rolf Kunz - *Bank am Bellevue - Analyst*

Okay, thank you.

Operator

Hans Pluijgers, Kepler Cheuvreux.

Hans Pluijgers - *Kepler Cheuvreux - Analyst*

A few questions from my side. First one looking at the gross margin. You indicate it's 40 basis points improvement coming from the temp side. If I exclude for the CICE, that means it might be in that the other operations on average are also about flat in gross margin?

Could you give some color on that and what do you see that on pricing and business mix? What's the driver? Because in the previous quarters, the underlying, still the gross margin, excluding CICE, was still about down about 20 basis points. Could you give some feeling there and what do we expect in the near future on business mix and pricing?

Secondly, looking at the SG&A, you indicated that on constant currency basis, the SG&A was up 3%. Is that a little bit also what you see going forward for the coming quarters?

And lastly, on the UK, EBITA was down from 2.9% to 2.5%. You already indicated some business mix impact. Could you give some feeling also what the other impacts were and are you taking some additional measures there? And what do you see for profitability levels going forward in the UK?

Patrick De Maeseneire - *Adecco S.A. - CEO*

Maybe I'll take that question on the UK. Indeed, we have done 40 basis points business mix. It's mainly client mix, because the business growth, the 7% growth comes mainly from large accounts.

You've also seen that the perm growth is 2%, so which is below the temp growth. So, as long at the perm growth is not accelerating, which over time we expect, of course, for the UK, this will be the kind of profitability that we're having.

We need stronger perm growth, especially in the UK market, which is a very, very competitive market as you know, to increase our profitability there.

Dominik de Daniel - *Adecco S.A. - CFO*

So if you look -- I don't want to say excluding CICE, because it makes no sense. It is fully integrated. What I can say is if you take what I said before on France, that a bit more than 50% of the margin increase from France is because of gross margin and take this as a combined effect of CICE and related effect that we are not able sometimes to pass on indirect labor costs or other things, then you could say, yes, the gross margin, overall the temp gross margin is stable, or maybe 10 basis points down. So this is the kind of area if you take this as a conclusion.

Now, from a mix point of view, for the time being, the industrial is the driver. So in industrial, in the short term, of course, has also here and there done a slight negative mix effect on the gross margin, but a positive mix effect on the cost base, because it has lower costs to serve. This has to be considered, because it's now the industrial business who recovers.

And from the cost base, the sequential increase, if I understood your question right, because you said 3% cost increase, so the sequential cost increase from Q3 to Q4 is just, to a larger extent, from a seasonal point of view. And then, we had some limited investments and here and there also higher bonuses, given the performance in Q4.

Patrick De Maeseneire - *Adecco S.A. - CEO*

And going forward on the costs, because that was also part of your question, we say a slight increase into Q1. Why? Because we do some limited investments, like in Italy where already in Q4, people who were on temporary unemployment, our own people, came back full time, considering the growth and the high productivity we're having there already.

So we do that also in Belgium. So that is adding some cost. And, of course, in a number of countries, we also have some wage inflation. So there will be a slight increase Q1 over Q4, sequentially.

Hans Pluijgers - *Kepler Cheuvreux - Analyst*

Yes, I understand. But with respect to the SG&A, I understood that that was a 3% increase year on year in constant currencies.

Dominik de Daniel - *Adecco S.A. - CFO*

In where you have seen this?

Hans Pluijgers - *Kepler Cheuvreux - Analyst*

Oh sorry, then maybe I misunderstood you in your remarks.

Dominik de Daniel - *Adecco S.A. - CFO*

No, let's say in Q4, adjusted for restructuring cost, the cost was up 1%.

Hans Pluijgers - *Kepler Cheuvreux - Analyst*

Okay. Thank you.

Operator

Konrad Zomer, ABN AMRO.

Konrad Zomer - *ABN AMRO - Analyst*

Two questions. The first on your CapEx. At the start of last year, you were guiding towards EUR120 million. You explained throughout the year why that was going to be lower. But as late as November, you were guiding towards EUR90 million and the reported number was even lower than that. Can you maybe explain why your CapEx year on year was down?

And my second question is on the tax rate. There is an explanation in your press release on page 4 why your tax rate or your effective tax rate was 7% for the quarter. I've read it several times, but it makes no sense to me at all.

So maybe you could give some guidance, not just for Q1, the 28% you mentioned, but also maybe for the full year 2014 as far as you can tell now? Thank you.

Dominik de Daniel - *Adecco S.A. - CFO*

Okay, if we look to the CapEx guidance. When we have done the CapEx guidance, at the time, we were working on the data center consolidation in several areas, the biggest one in the US and at the moment, it was not yet decided and clear how we structure the deal with our provider. Whether we own the asset, whether we rent the service, because this has the impact what is recognized as a CapEx, what is recognized as a cost.

And our assumption at the time when we had done the CapEx guidance was rather that we rather own assets, but we -- and this what I explained when we reduced the CapEx guidance, that we now rather rent the service. So basically, it's more on the direct cost than over CapEx and over the depreciation.

This is the main reason that the CapEx guidance was somewhat down. Then when we guided for EUR90 million, I said also on the call, the EUR90 million will maybe a little bit lower; this was more on the safe side. So, therefore, I think we are in line with the EUR85 million in this respect.

Regarding the tax rate, you have to see you have an underlying tax rate. And the underlying tax rate, it was last year in the area of around 30%. But then you have, from time to time, discrete events, you have statute of limitation, which sometimes kick in and then you can release a provision or you have resolution of tax audits of prior years. This happened basically in the last couple of quarters and this is what we explain here.

Now, what is the tax guidance for Q1 and for this year? It is 28% assuming there are no discrete events, but there will be always some discrete events. But the underlying tax rate for Q1 is 28%; and assuming no discrete events, it would be also for the whole year.

Konrad Zomer - *ABN AMRO - Analyst*

Okay. Do you have any influence on the timing of these discrete events? Is that something that your accountants come up with or is it something that you can, well, influence throughout the quarters?

Dominik de Daniel - *Adecco S.A. - CFO*

No, let's say this is not -- my accountant's not coming up with this, these are audits, so these are audit for the tax authorities. But you see the discrete events are often positive. There you see my accounts; they make a very good job to manage this.

Konrad Zomer - *ABN AMRO - Analyst*

Okay. And two final questions, small ones. Can you tell us what the permanent placement business represented in terms of your gross profit? I may have missed that in the press release.

And my second question is any indications on headcount growth for Q1 please?

Patrick De Maeseneire - *Adecco S.A. - CEO*

But if we look at permanent placement as part of our gross profit, it's about 9% for the quarter of the gross profit.

Dominik de Daniel - *Adecco S.A. - CFO*

Now headcount, headcount additions into Q1 are very limited. It's, on the one hand, for example, in Italy, because in Italy, it's not really more headcount, it's more our people in Italy, they were still on a program called economic unemployment, so they worked less than the normal working time. And into Q4 and into Q1, we bring them back to normal employment.

This is related to the very high productivity which we have today in Italy. The same is true for Belgium. And then we have for perm, here and there, a couple of people, but it's very limited.

Konrad Zomer - *ABN AMRO - Analyst*

Okay. Thank you very much.

Operator

Nicholas de la Grense, Merrill Lynch.

Nicholas de la Grense - *BofA Merrill Lynch - Analyst*

A couple from me. Just the first one, following on from Paul's question on the impact of the CLA in Germany. I wasn't quite sure what would and wouldn't be passed on.

Were you saying that the 30 basis points underlying impact on the margin, you did expect to pass on over time; or is it just the wage increases from January 1 that you expect to pass on?

Dominik de Daniel - *Adecco S.A. - CFO*

Let's say that we expect to pass on the wage increase and the 30 basis points over time. It may be here and there a bit challenging, but this is, of course, our expectation because the 30 basis points is normally about cost. The 60 basis points, you cannot pass on because this is a catchup for the history, but the 30 basis point is normally about cost.

Please consider also the 30 basis points represent two months because this new collective wage agreement is effective as of November 1. So into Q1, we have three months to consider but, of course, this is normal wage inflation; we should pass this on.

Nicholas de la Grense - *BofA Merrill Lynch - Analyst*

Okay, thank you. And one more please. I was a little bit surprised that you were taking more exceptionals in 2014. Obviously, you've said of the EUR20 million, most is going to relate to the US. I was wondering can you say how much is going to relate to the US and what exactly is going to be involved there?

Dominik de Daniel - *Adecco S.A. - CFO*

It's -- 60% is the US. To move to one single headquarter, that's the situation. Also, a part of it is also France, but not in the network; it's also there that we move to a headquarter and if you reduce headcount like us in France, you do not need any more such a big headquarter, so you can also save there going forward money. This is what we're doing there and then, here and there, some smaller projects.

Patrick De Maeseneire - *Adecco S.A. - CEO*

A little bit in Germany as well.

Dominik de Daniel - *Adecco S.A. - CFO*

Germany, for example, yes.

Nicholas de la Grense - *BofA Merrill Lynch - Analyst*

And can you give us an idea of the payback around those restructurings?

Dominik de Daniel - *Adecco S.A. - CFO*

If we -- in general, it is around 12 months now for the US. You have to consider that half of the amount for the US is a non-cash item adjustment, which basically has not really a payback. So only the half of it comes back of it, but the other half is a non-cash item.

Nicholas de la Grense - *BofA Merrill Lynch - Analyst*

Okay, thank you very much. Thanks, guys.

Operator

Laurent Brunelle, Exane BNP Paribas.

Laurent Brunelle - *Exane BNP Paribas - Analyst*

Two questions on my side. First on France, could you give us a bit more color about the churn trends and by sector and market please? And are you gaining market share? And when I look at your flat performance in Jan and Feb, can you please split between the volume and prices?

And second, a follow-up on the restructuring costs. So you're basically saying that you will get a EUR50 million payback if I understand well, as half of the US restructuring is on cash, is that correct? Thank you.

Patrick De Maeseneire - *Adecco S.A. - CEO*

If you look at our development in the French market on the top line, Laurent, we came in, as you've seen, flat and we have a similar development in the first two months of the quarter. This is indeed in line with the market; some are down now, one is slightly more up.

But if we look at the markets, we are in line and we are particularly happy with that because we have done an enormous restructuring, closing 265 branches, having 1,200 people less. So for being now in line in the market after eight quarters where we really were a bit behind, not in the third quarter, but all before we were behind, we are particularly happy with that development.

What is driving it? We already said it. It's mainly manufacturing, the industrial business; also, automotive turned positive although it's from a low base, but at least it turned positive, it was heavily double-digit down before and now it turned positive. Construction was still slightly negative at minus 1% in the fourth quarter; we also expect this to turn positive.

As far as the French market in general is concerned, we always said this will be the last market to turn positive in Europe because of the lack of reforms. We said it will only turn positive in the course of the first half of the year and we are sticking to that. Again, we are happy with the flat development, but to really turn positive, it will happen in this first half of the year.

Dominik de Daniel - *Adecco S.A. - CFO*

Turning to other two questions, I think the EUR50 million is a good estimate; when you reconcile the numbers, that makes sense.

And the volume in France is still slightly down and the wage inflation runs -- price inflation is around 1.5%/2%.

Laurent Brunelle - *Exane BNP Paribas - Analyst*

Okay, great. Thank you very much.

Operator

Andy Grobler, Credit Suisse.

Andy Grobler - *Credit Suisse - Analyst*

Just a couple of quick questions from me. Just your thoughts on M&A into 2014 and potentially a bit longer than that given the leverage is down and growth rates are back?

And then secondly, just what your thoughts are in the US on the impact of the Affordable Care Act during the year. I've heard some of your competitors are a bit less positive about that potential impact than they may have been a few months ago. Thank you.

Patrick De Maeseneire - *Adecco S.A. - CEO*

On the M&A, Andy, you -- we clearly said several times that we wouldn't do any acquisitions, and this until at least the end of 2015 and we are sticking to that.

So we are comfortable with the platforms that we are having to grow organically from. We are focusing on our six priorities. This requests all of our attention, all of our time and so we won't do any acquisitions at least until then.

I'm not saying that we're now going to start on January 1, 2016; I'm just saying until the end of 2015, we won't, for sure, not do any acquisitions.

On the health care reform act, so far, there is not a lot of news. You know this is on and off and being postponed, and if it comes through in the previous thinking, we think this is going to have a positive impact, especially on the small and medium-sized companies. Because it would only be applicable up to 50 employees -- as from 50 employees, so meaning that a lot of small companies would not go for that level because then they have to apply it on their full workforce.

But it's also going to increase for larger companies, where it would have a more limited effect because of the salary levels. And the number of hours worked would only have a limited effect on temporary labor.

So we still think if it comes through, that it's going to have a positive effect. But since it's under discussion all the time and postponed all the time, we indeed take it off the table for the moment.

Andy Grobler - *Credit Suisse - Analyst*

Okay, thank you very much.

Operator

Toby Reeks, Morgan Stanley.

Toby Reeks - *Morgan Stanley - Analyst*

I've got a few as well if I can. First is could you go through the one-offs in France, just let us know what they are?

Secondly, the SGA slight increase into Q1, is that -- it sounds like we should think about seasonality and then, also to an increased cost. I think you talked about Italy and Belgium. Is that the right way to think about it?

And then the final question is could you talk about any sort of data we could have in terms of the benefits from integration of the front and back offices in Europe and the US? And do you have any productivity improvement things that we could think about? And how much is that contributing towards that 5.5% margin target? Just try to give us a sense of what that is helping. Thank you.

Dominik de Daniel - *Adecco S.A. - CFO*

First up, the first two questions, so the one-offs, there were several one-offs in France in a positive and a negative way. We had litigation costs. Then we had the release of pension cost. But in sum, there was a 50 basis points positive impact; some were negative, some were positive in this respect.

Then, regarding the SG&A development, the majority is a seasonal impact. We have some countries where wage inflation kicks in into Q1. It's how it is. Then you have in Q1 normally the kick-off meetings of the countries, so you have some more cost in this respect.

And then we make very, very limited hirings, but it's very limited because we really want to drive productivity. But if I look to a country like Italy and also Belgium, it's fair to say that that is what would make sense, to add limited headcount to support the growth.

Dominik de Daniel - *Adecco S.A. - CFO*

And the last question was related to --?

Patrick De Maeseneire - *Adecco S.A. - CEO*

Can you repeat your last question please?

Toby Reeks - *Morgan Stanley - Analyst*

The benefits of the integration of your front and back offices in Europe and the US. I think you've given some -- I think about a year ago, you were -- or certainly you just gave us some data on the improvement of productivity, like the number of clients being seen, which has been enabled by integrating the front and back office. So can you give us any more information about that?

Dominik de Daniel - *Adecco S.A. - CFO*

So basically, if we look to this whole IT area, we defined eight any different key areas or work streams where we work on it, like recruiter workplace, like search image engine, like CLM and so on. And the benefits, the big benefits, they will kick in, I would say especially 2016. There will be some benefits, maybe 30 basis points, 40 basis points also in the year 2015, but the big benefits come later.

Why? Because today, we have to invest to build a foundation; today, we have to invest in order to develop the new systems. And the benefits will basically come on the one hand, when people using the system with higher productivity, but at the same moment, when we have the opportunity to decommission the old systems. Because, for the time being, we have to develop the new systems, but we have to support the old systems.

And investments like in the data centers, they are basically fundamental investments. We have a foundation for this benefit and everything is on track on this. Our goal was develop for each of these eight different work streams the prototype in the second half of last year, which we have done. And now, we start to roll them out in the different units.

Toby Reeks - *Morgan Stanley - Analyst*

Okay. And just to be clear, did you say 30 basis points, 40 basis points benefit in 2015? And then, could you also give us an idea of if you shut the old systems off now, what would the margin benefit be, just so we know what that is?

Dominik de Daniel - *Adecco S.A. - CFO*

This could double this, of course, but again, this cannot happen so quickly because you can -- you have to just roll your things out and then stop the other things afterwards. Therefore, I said the real benefit of this one is really after 2015.

Toby Reeks - *Morgan Stanley - Analyst*

Okay, that's clear. But you would be able to double that benefit you think if, just for the sake of if, you shut it off tomorrow. So we're looking at 60 basis points to 80 basis points effectively?

Dominik de Daniel - *Adecco S.A. - CFO*

You have to see this as a huge thing; that is you do not in a couple of years. So to really do this, you need until 2017 for all the countries. This is not something which you do in one year or two years.

Toby Reeks - *Morgan Stanley - Analyst*

Yes. No, sure, I was just getting a quantification of it. Okay thanks, guys.

Operator

Matthew Lloyd, HSBC.

Matthew Lloyd - *HSBC Global Research - Analyst*

Just a quick more general question from me. You've talked about industrial picking up, the Benelux picking up. It feels like an early cycle pickup, which is good. But I wondered if there are any clues as to how far we were towards wage rate inflation and things starting to move.

So are there any pockets where you're seeing wage rate inflation, US construction exposure or bits of IT, things that make you feel like we are moving through the traditional stages of a cycle?

Dominik de Daniel - *Adecco S.A. - CFO*

First of all, this is Dominik speaking, we have no construction at the moment in the US so -- because, from a risk point of view, we are not in this area, in this respect.

It's not that we're seeing the US today in our starting business wage inflation. The wage inflation which we have in our business is primarily driven more by, let's say, union agreements or regulatory things like equal pay, like Germany with the CLA, but not demand-driven wage inflation.

Matthew Lloyd - *HSBC Global Research - Analyst*

Okay, so we haven't seen any pickup. I think manufacturing wages in the States have moved up from about 2% to 2.5% wage rate inflation. That's yet to come through in your business?

Dominik de Daniel - *Adecco S.A. - CFO*

Yes, you're right, but this is a rather normalized wage inflation. I look more in channel because you said you want more the big picture. It's not that we've seen a significant change but, yes, there is underlying a bit of wage inflation but not material.

Matthew Lloyd - *HSBC Global Research - Analyst*

Okay. That's probably for the best. Too much hyper-wage inflation might scare everybody off. Thank you very much.

Patrick De Maeseneire - *Adecco S.A. - CEO*

Thank you, Matthew. Ladies and gentlemen, this closes our call for today. Thank you very much for your interest, for attending, for your interest in our Company.

We are looking forward to meet some of you tomorrow at our breakfast in London. And if not, we'll talk again for sure on May 8, when we announce our first-quarter results.

Thank you again. Have a good day or a good evening.

David Hancock - *Adecco S.A. - Head of IR*

Thank you very much.

Operator

Ladies and gentlemen, the conference is now over. Thank you for choosing Chorus Call and thank you for participating in the conference. You may now disconnect your lines. Goodbye.
