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Adecco Group AG (ADEN.CH)

Q4 2017 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Ladies and gentlemen, good morning. Welcome to Adecco Q4 and Full Year 2017 Results Analyst Conference Call. I'm Mirona, the Chorus Call operator. I'd like to remind you that all participants will be in listen-only mode and the conference is being recorded. After the presentation, there will be a Q&A session. [Operator instructions] the conference must not be recorded for publication or broadcast.

At this time, it's my pleasure to hand over to Mr. Nicholas de la Grense, Head of Investor Relations, accompanied by Mr. Alain Dehaze, CEO; and Mr. Hans Ploos van Amstel, CFO of the Adecco Group. Please go ahead.

Nicholas de la Grense
Head of Investor Relations, Adecco Group AG

Good morning, everyone, and welcome to Adecco Group's Q4 and full year 2017 results conference call. To present to you today, I am joined by the Alain Dehaze, Group CEO; and Hans Ploos van Amstel, Group CFO. Before we start, please have a look at the disclaimer regarding forward-looking statements in this presentation.

Let me give you a quick overview of today's agenda. Alain will first briefly present the highlights of the quarter. Hans will take over to review the financial performance and comment on the outlook. Alain will then discuss our strategic and operational progress and initiatives. We'll then open the lines for your questions.

And with that Alain, I hand over to you.

Alain Dehaze

Chief Executive Officer, Adecco Group AG

Thank you, Nick. Good morning, ladies and gentlemen and welcome to our fourth quarter and full year 2017 results investors call. I will start on slide 5 with the key highlights. Looking at the fourth quarter, revenue momentum has accelerated 7% organically and trading days adjusted, and this despite a 3% tougher comparison base.

We see that the growth was mainly driven by France, Italy, Spain, the Benelux, and the Nordics. Also to be noted for this fourth quarter, it is our solid performance in the perm business, 18% gross. The EBITA margin excluding one-offs was 4.6%. In fact, a good underlying operating leverage with a 3% FTE increase to support 7% revenue growth.

We did also in this quarter strategic investment in digital and IT for 25 basis points. The underlying gross margin trends remained unchanged. Reported gross margin was impacted by the timing of bank holidays and the impact of year-end accruals, which were positive in the fourth quarter 2016, but negative in the fourth quarter 2017.

Now, looking at the full-year 2017, we show an improvement in revenue growth to 6% organically, up from 4% in 2016. The profitability leadership was maintained with an EBITA margin at 4.9%, down 10 basis point year-on-year, including strategic investments.

In 2017, we made significant progress with the implementation of our strategic initiatives. With GrowTogether, we are transforming the core of our business to provide a better service in a more efficient way. And we are also adding new digital first solutions to expand into attractive adjacent markets. After the launching of Adia and YOSS, both digital marketplaces co-created with Infosys and Microsoft, respectively, we have announced last week the acquisition of Vettery, a digital professional recruitment platform. With Vettery, we are adding valuable talent and technology to the Adecco Group, and gaining a strong platform to grow our market share in professional recruitment. We will talk about Vettery more later on the call.

For 2017, the board of directors will propose to the general assembly to increase the dividend by 4% to CHF 2.50, which corresponds to a payout ratio of 46%. We remain committed to paying at least a stable dividend every year, supported by the Group's strong through-the-cycle cash flow. And for 2017, the board will also propose a new share buyback of €150 million.

Coming to the outlook, revenues in January and February were up 5% organically and adjusted for trading days. In 2018, we will continue to drive our strategic agenda. As a leader in our industry, and as you can see, we continue to perform and we invest to transform and innovate.

And with this, I hand over to Hans for on more insights on the financials [Technical Difficulty] (00:05:31).

Hans Ploos van Amstel

Chief Financial Officer, Adecco Group AG

Thanks, Alain. Let's start with sales. Sales growth improved to 7%, and this is on the back of 6% growth in the fourth quarter of 2016. France accelerated to 9%, and we're closing the gap to the market in January.

In North America, in UK General Staffing, we see continued challenging conditions in North America. This was offset by strong growth on the client wins we made at the beginning of the year in the UK. As discussed before, we're working to drive the sales growth in North America by implementing our proven segmentation strategy.

Professional Staffing in North America delivered solid growth with continued outperformance versus the peers, the UK market remains more difficult and challenging.

Turning to Germany, Austria and Switzerland; we see continued strong results in Professional Staffing, and permanent recruiting. In General Staffing, the integration of Adecco and [indiscernible] (00:06:39) is on track and as we communicated before, we expect to return to market growth in the second half of 2018. We're pleased with the continued growth momentum in Southern Europe.

EBITA margin is down 50 basis points in Q4, 40 basis points is explained by the timing of bank holidays and favorable accrual releases in Q4 of 2016 versus higher accruals in Q4 of 2017. Adjusting for those two items, this leaves a net 10 basis points decrease, 30 basis points coming from pricing and mix partly offset by a 20 basis point improvement in SG&A, strong operating leverage even after making the investments for the future.

Important to note that, when you cut through the noise of the holidays and the accruals in fourth quarter, the full-year 2017 EBITA margin was broadly stable year-on-year, organically, even while we invested an additional 25 basis points in our strategic initiatives.

A couple of remarks on the country level. As mentioned before, Q4 was impacted by bank holidays and changes in accruals. Second, the strategic investments are impacting the country profitability. France, North America, the UK and Japan are impacted by the strategic investments in IT and driving the growth agenda.

In North America General Staffing, we also had the favorable accrual release in Q4 2016. The EBITA margin in Germany, Austria and Switzerland would have shown an increase when adjusting for the bank's cost due to the less favorable bank holidays in Q4. Benelux is also impacted by the working days, plus we had a negative impact from subsidies and accruals. Italy remains strong, while the business mix was a little less favorable in the fourth quarter.

Let's look at our gross margin and SG&A productivity in more detail, starting with the gross margin. The divestiture of Beeline negatively impacted the gross margin, but had a positive impact on the EBIT margin. Currencies had a negative impact of 10 basis points, temporary staffing gross margin was down 70 basis points, 40 basis points of the decrease is due to the timing of bank holidays, and the changes in accruals in the 2016 to 2017 comparison for the fourth quarter, the balance is explained by pricing and mix.

Our strong growth in permanent recruiting is helping the gross margin by 20 basis points. This is offset by lower sales in LHH; as you know, this business counter-cyclical. We're pleased with the market share gains and the improvement in profitability at LHH.

We continue to drive strong productivity, while investing for the future, 3% increase in head count delivering 7% sales growth. SG&A increased 5%, organically including 2% from investments in GrowTogether, IT and the Digital Ventures. We remain on track to deliver €50 million in productivity with GrowTogether in 2018, and are on our way to €250 million annual productivity savings by 2020.

Cash conversion remain strong, DSO is stable at 52 days. Conversion was solid at 80%. The cash conversion reflects strong revenue growth and consequent working capital investment following the same pattern as we have seen in previous years of growth acceleration. We have already repurchased €279 million from the €300 million share buyback program, which will complete in March this year.

Net debt stands at 0.8 times EBITDA at the end of 2018 or 0.8 times adjusted for the recent acquisition of Vettery. This brings me to the capital allocation for 2017. We propose a dividend of CHF 2.50 per share. This is a 4% increase versus last year, and a payout ratio of 46%. We remain committed to the progressive dividend policy, and will provide a stable dividend even in a recession. For 2017, we proposed a new €150 million share buyback to return the excess cash to our shareholders in line with our capital allocation policy.

Turning to the outlook; January, February combined show 5% sales growth. Some notes on the margin for the first quarter. The gross margin in Q1 will be impacted by the timing of bank holidays because that's less favorable in Q1 of 2018. This will have a 30 basis point negative impact. Also for your models, remember that, CICE has gone from 7% to 6%, which has about a 15 basis points impact at the Group level. Currency impacts also continue in Q1.

Back Alain to talk about our strategic and operational progress.

Alain Dehaze

Chief Executive Officer, Adecco Group AG

Thank you, Hans. And indeed, now, let's look at our strategic and operational progress during the fourth quarter. As we discussed doing our Capital Markets Day last September, we are aiming at combining performance and transformation and innovation to accelerate our growth and enhance our margin. And during the fourth quarter, we made further progress with this agenda.

First, the transformation of IT infrastructure continued and our new integrated front office system is in the process of being rolled out in France, Spain, the UK and the U.S. The so-called InFO for integrated front office will enhance productivity, customer engagement, and deliver a differentiated service in the quarters to come, supporting our target of €50 million of savings in 2018.

As part of the innovation agenda, we have launched in Switzerland, in May 2017, Adia, an online staffing marketplace. And in the meantime, Adia has expanded in the UK, and now, Germany. And we will launch in another country during the first half of this year.

YOSS, our marketplace for freelancers, completed its successful beta phase and went live in France, as planned in early February. And finally, last week, we announced the acquisition of Vettery, a digital platform for online professional recruitment.

So you see, we are building a portfolio of digital solutions. And at our recent Capital Markets Day, we updated you on how much opportunity the changing world of work is offering us, thanks to the mega trends, and our multiple competitive assets. We talked about capturing growth opportunities in new frontiers, providing solutions and services that are complementary to our existing portfolio, and where we can build real competitive advantage.

[ph] It's last year (00:15:26) we added to our portfolio Adia and YOSS, we also highlighted in the Capital Markets Day in London, the gaps in our portfolio, including in digital professional recruitment. I am very pleased that at the very beginning of 2018, we filled that gap with the acquisition of Vettery.

Let's now zoom in on Vettery. The €25 billion professional permanent recruitment market is today, highly fragmented. In this market, we have less than 1% market share. The current professional recruitment process is highly-transactional, allowing artificial intelligence to leverage productivity and efficiency.

This is the rationale behind the acquisition of Vettery, a company which has been created in 2012 by two entrepreneurs in New York, Brett Adcock and Adam Goldstein. And in the meantime, Vettery is growing fast and has already expanded in seven U.S. cities. And together with Adam and Brett, we will continue to expand in 2018, first in the U.S., and then in the U.K. So we now have best-in-class platforms in online staffing, freelance, and now permanent recruitment.

Coming to the concluding messages, we are on track to make the world work for everyone. With the recent acquisition and ongoing strategic progress, we have the building blocks in place for a successful 2018. In the fourth quarter 2017, we made significant progress on our strategic agenda to perform, transform and innovate through the GrowTogether initiatives and the investments in our digital portfolio.

We continue to perform with positive growth momentum and another quarter of strong productivity. And in January and February, growth continues with 5% organic growth. Finally, I would like to thank our more than 34,000 colleagues for their hard work and dedication during 2017. And I take the opportunity also to welcome into the Adecco Group family, our new colleagues from Vettery.

I thank you for your attention, and now, I would like to open the line for the questions.

QUESTION AND ANSWER SECTION

Operator: We'll now begin the question-and-answer session. [Operator Instructions] The first question comes from Anvesh Agrawal from Morgan Stanley. Please go ahead.

Anvesh Agrawal
Analyst, Morgan Stanley & Co. International Plc

Q

Hi. Good morning, I have a couple, but first, can I ask in continuation to your rationale for Vettery, and if you think about the end markets that could be disrupted or will change the way they are sold because of the technology, is the lower volume professional perm market will be among the earlier ones to be disrupted?

And second, can you just give some color on the expected operational leverage in FY 2018 now you have CICE negative. The pricing probably still remains challenged, but you've got some savings coming in through your plans. So is it fair to assume some margin expansion in FY 2018 or a more realistic number would be flat year-on-year? Thank you.

Alain Dehaze
Chief Executive Officer, Adecco Group AG

A

Good. On Vettery, you have seen that this €25 billion market is highly fragmented, we have 1% market share, the market leader has 2.5% market share. So it is for us a huge opportunity.

On your specific questions regarding disruptions and so on, you know that technology, yeah, is making its inroads, but gives also a lot of new opportunities. So we see the two models continuing in. Vettery today is concentrated on mainly IT with some profile in sales and finance.

So we are in seven U.S. cities. We will now expand into other U.S. cities and then in the UK. For sure Vettery is one of the leading – brand leading organizations in this digital professional recruitment platform. I don't see a disruption. On the contrary, I see a huge opportunity to expand in this market, take market share and expand also for customers having still an [ph] in-shop (00:20:58) solution.

Anvesh Agrawal
Analyst, Morgan Stanley & Co. International Plc

Q

Yeah. So just to clear, what I mean by disruption is essentially, it's very clear that the way these end markets are served by agencies is going to change. So do you see the perm professional market being a first one to be in that line or is it going to happen parallelly across all end markets? That's the question.

Alain Dehaze
Chief Executive Officer, Adecco Group AG

A

No, I see professional recruitment as one being indeed first leveraged by technology, why? Because it is – that's what I said in my comment, it is very transactional business, it is a lot of processes. And you'll see that, thanks to artificial intelligence, thanks to deep learning, you can automate this process of candidate curation that you can automate in a better way, the matching between curated CV and the needs of the customers. So for sure, that's where we see technology making first it's inroad.

Anvesh Agrawal
Analyst, Morgan Stanley & Co. International Plc

Q

Okay. And on operational leverage, please?

Alain Dehaze
Chief Executive Officer, Adecco Group AG

A

Yes. On the CICE, two things, I will start and then Hans will continue. So first of all, the CICE is going this year from 7% to 6%, it has been communicated. For us, it means a €30 million impact in France. Now, with all the measures we have in place, being pricing disciplined, being also expanding in value-added services such as the [ph] CDITT (00:22:45) the segmentation, apprenticeship, we are doing our best to mitigate this €30 million.

Hans Ploos van Amstel
Chief Financial Officer, Adecco Group AG

A

Yeah. Hans here.

Anvesh Agrawal
Analyst, Morgan Stanley & Co. International Plc

Q

Yeah.

Hans Ploos van Amstel
Chief Financial Officer, Adecco Group AG

A

Just so your question on the margin. First, if we look back at this year, at the full fiscal year, we have seen a continuation of that around 30 basis points of gross margin, and we have offset that about with operating leverage even after making the 25 basis points of investments. We're in a period where we're making investments to strengthen the core of our business and into the Digital Ventures, that will continue into next year.

The good news is that, next year, we'd grow together. We'll start to deliver €50 million of true savings. So, we're coming out of the investment period of GrowTogether. And next year, we'll invest more in Vettery, is one example into the Digital Ventures. So global level operating leverage, but we are also in a period where we see, we need to Transform and Innovate, and with the Transform and Innovate [indiscernible] (00:23:49), we're making the right relevant investments so that we position our business for profitable growth in the future.

Anvesh Agrawal Q
Analyst, Morgan Stanley & Co. International Plc

That's clear. Sorry, can I just have one follow-up on the CICE for next year. We know the form's going to change, and it remains difficult to assess the financial impact of that. But is it fair to assume that it could accelerate the pricing pressure in France, because right now you receive the subsidy on a deferred basis, but with the change in the form you're going to receive it in year one itself, so could the large clients can demand more discount or this model play become more aggressive?

Hans Ploos van Amstel A
Chief Financial Officer, Adecco Group AG

No. I wouldn't say so, because in the end, next year, it goes from 7% to 6%, so it would give them less reason...

Anvesh Agrawal Q
Analyst, Morgan Stanley & Co. International Plc

I mean, I was saying for FY 2019 when the form changes?

Hans Ploos van Amstel A
Chief Financial Officer, Adecco Group AG

If you look, 2019, I think that's further away. Things are still [indiscernible] (00:24:42). There's a lot of change so – but I would not draw you a conclusion from that.

Anvesh Agrawal Q
Analyst, Morgan Stanley & Co. International Plc

Okay, cool. Thank you so much.

Alain Dehaze A
Chief Executive Officer, Adecco Group AG

You're welcome.

Operator: The next question comes from Konrad Zomer from ABN AMRO. Please go ahead.

Konrad Zomer Q
Analyst, ABN AMRO Bank NV

Hi, good morning, gentlemen.

Alain Dehaze A
Chief Executive Officer, Adecco Group AG

Good morning, Konrad.

Konrad Zomer Q
Analyst, ABN AMRO Bank NV

If you look at all the Digital Ventures that you've started in the last few years, particularly talking about YOSS, Adia online, but also now Vettery. What's the percentage of your overall sales that you think will be impacted by these digital changes that you're putting through once it's all settled? And my second question is, can you comment anything on the underlying market trends that you're seeing in the U.S. Professionals business at the moment? Thank you.

Alain Dehaze
Chief Executive Officer, Adecco Group AG
A

Okay. Good. Now, coming to the Digital Ventures, I would like to first of all to make it clear that, yeah, all these initiatives are less than one year old. We launched Adia in May 2017. As I said, YOSS is now since February with the first version after the beta version up and running in France. And we had bought last year, Vettery.

So the point is for sure, we are at the beginning of our journey. We are convinced that digital human resources solutions will be important going forward. And looking at the future, we would love to build the kind of new LHH with all these solutions being in online, job staffing, being in professional recruitment or being in the freelance business. There is a huge market in this.

Hans Ploos van Amstel
Chief Financial Officer, Adecco Group AG
A

So, if you look, yeah...

Konrad Zomer
Analyst, ABN AMRO Bank NV
Q

No. Please go ahead?

Hans Ploos van Amstel
Chief Financial Officer, Adecco Group AG
A

No, I think to couple on that, I think, they're all relatively early in the development, but we were pleased with the progress. But really the objective is, is that we add – yeah, like the LHH, our ambition is to add relevant and meaningful profitable businesses. But also – and that's the case with these business with a higher gross margin structure, because these type of businesses are having a good margin structure, they're in the [indiscernible] (00:27:22). And I'm also very pleased with what we did successfully because these type of – and we know it, when you talk to candidates and clients that you can fill orders faster for clients, it's very exciting, it's early, but it's exciting.

If you look at Professional Staffing in U.S., we see 3% growth there. It's modest growth. We were ahead of the peer group. We're pleased with performance. We have a good segmented approach with our Professional Staffing portfolio, and we're investing also there with new front end tools to strengthen our sales ability to drive the growth continuously.

Konrad Zomer
Analyst, ABN AMRO Bank NV
Q

Okay. Thank you.

Alain Dehaze
Chief Executive Officer, Adecco Group AG
A

Thank you, Konrad.

Operator: The next question comes from Tom Sykes from Deutsche Bank. Please go ahead.

Tom Sykes
Analyst, Deutsche Bank AG

Q

Yeah. Morning, everybody. Firstly, just on the onsite business, because you had, if I remember, very fast growth at the beginning of last year, and the end of the previous year from onsite. So, I'm just wondering how much the annualization of some of that high-growth is a factor in both the margin move, because there presumably is some mix in the 30 basis points. And then, on the growth step-down at the beginning of this year, please?

And then, maybe could you make some comments on when we should expect the larger restructuring charges to start coming through again, please? And just could you remind us, is there any front office staff you're expecting to let go or would this large lease – or is this just back office staff, please?

Alain Dehaze
Chief Executive Officer, Adecco Group AG

A

Okay. Yeah. Numerous questions, so I will share them with Hans. Now, regarding the onsite business, yes, we are pleased with the development of the onsite business. If I think the fourth quarter, we had a growth of 25% in this business. You know that, we have a segmented approach, and this onsite business or the growth of this onsite business was indeed much higher than the small and the medium.

Now, I think your second question was about the growth, no? In January, February, I if I understood well?

Tom Sykes
Analyst, Deutsche Bank AG

Q

Yeah. It was just that you had very strong growth in onsite, I thought in Q1 2017 and just how much of the step-down in growth from the sort of 7% to the 5% run rate now is due on an annualization of that onsite or is it due to other factors?

Alain Dehaze
Chief Executive Officer, Adecco Group AG

A

No. I shouldn't – I think it's much too premature to read something from there in the 5% we have communicated.

Tom Sykes
Analyst, Deutsche Bank AG

Q

Okay.

Alain Dehaze
Chief Executive Officer, Adecco Group AG

A

No, it's too premature, I said, the 5% reflects the January, and you know, January is never easy to read. And then, part of February, we see all the macro trends being confirmed. We see also from our weekly that the momentum is also continuing. But for sure, we had last – a very strong first quarter with 7% organic growth. So that's also – can give some more color on the 5%.

Hans Ploos van Amstel
Chief Financial Officer, Adecco Group AG

A

On your question on the restructuring, first and foremost, the objective of GrowTogether is to drive more productivity across the organization. And that will be in sales, in recruiting, but also in the back offices. With that we'll provide better technologies to equip our people and [indiscernible] (00:31:36) reorganization for the downside, it should give our people more options to drive for profitable growth, and drive market share wins.

On the reorganization, when we had the Capital Markets Day, we said, the whole GrowTogether we announced in the amount of around €200 million. That will have a good payout, because we'll deliver annually more than – almost €50 million of savings. We're not in the position to give forward-looking statements on these because every time we have, when we implement the piece, there's work to be done. It's the logical work we need to do in these areas, because it relates to people. But you will be reassured that we'll have productive use of money there to make sure we drive the savings and the growth. I wouldn't forget the growth element.

Tom Sykes
Analyst, Deutsche Bank AG

Q

Okay. So just importantly on that, you're expecting that to have zero negative impact on growth when those occur, and if anything, you're expecting those to have a positive impact in the year those occur?

Hans Ploos van Amstel
Chief Financial Officer, Adecco Group AG

A

Yes, that's the objective. That's why we call the initiative GrowTogether, because that, I know is important that it's not a restructuring and that's why we do it in a phased approach, because – yeah, I think in any business like in our business, we have seen people, if you do that, and we're bringing better technology and tools for a successful sales drive.

And some of the pilots we're doing are confirming that. So we're pleased with the progress [indiscernible] (00:33:14) comment yet, because some are in pilot phase, but you see that we're also implementing new front office solutions, so those should give us towards 2018, maybe a little bit more in the second half, some good momentum.

Tom Sykes
Analyst, Deutsche Bank AG

Q

Okay. All right. Thank you very much.

Alain Dehaze
Chief Executive Officer, Adecco Group AG

A

Thank you, Tom.

Operator: The next question comes from Alain Oberhuber from MainFirst. Please go ahead.

Alain-Sebastian Oberhuber
Analyst, MainFirst Schweiz AG

Q

Good morning, Alain. Good morning, Hans.

Alain Dehaze
Chief Executive Officer, Adecco Group AG
A

Good morning, Alain.

Alain-Sebastian Oberhuber
Analyst, MainFirst Schweiz AG
Q

I have two questions. The first is just to come back again to gross margins. Did I get it right that Hans said, he's expecting an impact of 50 basis points? Obviously, the €30 million is minus 70 basis points, but you can recuperate 20 basis points, so it's minus 50 basis points. And then on the top of that, if we expect that gross margins remain on pressure of this 30 basis points throughout the year, so do I look at it right that we could see a decline of gross margins of 80 basis points for the year? And the second question is regarding price pressure. Do you currently see in any of your larger markets, any price pressure?

Alain Dehaze
Chief Executive Officer, Adecco Group AG
A

On price pressure, what we have just said is, and I confirm that, is that the underlying price pressure we had in the previous quarter is, let's say, stabilized at the level we have seen in the previous quarter, which is a 30 basis point impact from price pressure and mix, and this in all the big geographies and all the geographies, not really a change of pattern in one direction or the other.

Hans Ploos van Amstel
Chief Financial Officer, Adecco Group AG
A

If we turn more specifically to the numbers, we gave some color for the first quarter. As we said, the bank holidays is impacting in the first quarter, have a negative impact but not for the fiscal year. So bank holidays next year will not have a negative impact for the fiscal year.

And CICE is around 15 basis points at the group level, and we're looking to find the offsets. And the reason why we launched GrowTogether is that, this is a competitive market. The pricing we have seen over the years [indiscernible] (00:35:42) we have offset and operating numbers, and we grow together.

We're adding new tools to drive – new ways to drive that operating leverage so that we have positive margin development, while we would see [indiscernible] (00:35:57) a continued competitive industry. And if I look this year again versus the industry, you look at the numbers, we're in line with what you see, and this is consistent.

Now, we also, with our new businesses, want to mitigate that, driving more segmentation into the mix, adding our Digital Ventures, higher margin businesses, so we bring those as well. But I think the key with GrowTogether will find the right ways to drive the operating leverage going forward.

Alain-Sebastian Oberhuber
Analyst, MainFirst Schweiz AG
Q

Okay. You said 15, 5-0 or 1-5?

Alain Dehaze
Chief Executive Officer, Adecco Group AG
A

1-5, 1-5.

Hans Ploos van Amstel
Chief Financial Officer, Adecco Group AG

A

Sorry, [indiscernible] (00:36:36).

Alain-Sebastian Oberhuber
Analyst, MainFirst Schweiz AG

Q

Okay. Thank you very much. Thank you very much.

Operator: [Operator Instructions] The next question comes from Matthew Lloyd from HSBC. Please go ahead.

Matthew Lloyd
Analyst, HSBC Bank Plc

Q

Good morning, gentlemen. I too am going to rather boringly return to the gross margin questions. I wondered if you could give, if not numbers, a feel for how much of that 30 bps of underlying gross margin pressure in temp you think is mix, industrial has been growing faster. You seem to be doing well in that sector as well. And how much you think is underlying pricing pressure? Because I think the two things seem to get rather blurred.

And then, a sort of – I'll put the follow-up question in straighter way, a number of your peers have talked about a sort of stabilization in gross margin trends, and they've also done quite a lot of work on sort of dynamic pricing giving salesmen a clue as to what different skill sets can be charged at in terms of gross margin or markup. And that seems to be the sort of the hottest subject amongst the IT vendors to your industry at the moment.

Have you made any progress on dynamic pricing, I mean, in the old days a salesman just place the candidate where he'd get the biggest commission check, which was normally where they got paid the most, and where he got the biggest markup. But that's a bit harder these days. So are you doing anything on dynamic pricing?

Alain Dehaze
Chief Executive Officer, Adecco Group AG

A

We are, we – without going into the details also for competitive reason, we have already since many years, because I started dynamic pricing, I think in 2004, four or five years ago, really dynamic pricing based on artificial intelligence. So meaning that we are treating every week millions of data to see at what kind of pricing we have concluded transaction the week before by role, by region.

For sure you cannot apply dynamic pricing everywhere; why? Because you need sufficient amount of data, it's always the same issue with artificial intelligence. So we are applying dynamic pricing in big geographies, but not in small geography, because we don't have enough data to have an effective model.

Now, regarding the question of 30 bps, and yes, it is a mix of a lot of influences being the regions where we are growing fast, the type of business we are growing fast or less fast. And Hans can give more color on that.

Hans Ploos van Amstel
Chief Financial Officer, Adecco Group AG

A

Sure. I think on the gross margin, I want to make a couple of points. First, I think, we have always been more transparent about that, and the reason why we have, because that shows that we know what's going on, and that was the foundation of our GrowTogether initiative to drive more operating leverage and new ways to drive operating leverage, grow our margin, while that's going on.

[indiscernible] (00:40:10) at the industry, and I think it's better to look at the year, because the quarter always has, quarter four is a year-end quarter there are some things into that. Our gross margin is similar to the industry, it's not like [indiscernible] (00:40:28). So we're bringing, like Alain said, similar tools to the market to improve our pricing, and I think we're doing that.

If I look at onsites, yes, onsite place, I wouldn't want to give you a precise number on that, because if we give you the volume and the pricing, then you see, but that is, in that 30 basis points, a relevant part. So it's not just pricing, the move to onsites, which we offset with cost leverage place into that 30 basis points, I think. So I'll leave the conclusion that, that's not all pricing, there's also that mix and that mix plays.

Matthew Lloyd
Analyst, HSBC Bank Plc
Q

Okay. Thank you very much. Just one other question, because people seem to be a little concerned about, I think Tom called it a sort of fall-off in growth or something suitably dramatic. When you're looking at numbers in the middle of February, presumably you don't have very much perm in that mix, because that tends to be very heavily March, and that's been growing faster. Would that be accurate to say that, any perm growth is likely to hit a bit later?

Alain Dehaze
Chief Executive Officer, Adecco Group AG
A

A good question. I must say without giving figures that I was very pleased by the perm development in January.

Matthew Lloyd
Analyst, HSBC Bank Plc
Q

Okay. Thank you.

Operator: We have a follow-up question from Tom Sykes from Deutsche Bank. Please go ahead.

Tom Sykes
Analyst, Deutsche Bank AG
Q

Hi, thank you. I'm trying to be quick. But just on the Italy business and growth outlook there and the outlook for leverage. And then also just on LHH. Obviously, your growth was down, but margin was up a lot, and could you just remind us – you were going through some integration in Q4 last year, but would you expect to be able to hold your margin if margins are a little bit – sorry, growth is a little bit weaker in LHH, please?

Alain Dehaze
Chief Executive Officer, Adecco Group AG
A

On LHH, you know that this business is counter-cyclical and it's career transition, it's old placement. So when we look at all figures, whether high-single-digit decrease you see that, it's published. But when you benchmark with all figures with some of order-listed peers, you will see that we can be very pleased with this performance. We are gaining market share. And the decrease of this business is typical from the current economic environment in which we are in. So on the top line, we are pleased with the performance of LHH.

You see also that on the bottom line, thanks to our business model, we are able to adapt very rapidly our cost structure. We have a variable cost structure, and that's what we have done, and that's why you see the profitability we have delivered in Q4. On Italy, I didn't catch the point on Italy at all.

Tom Sykes
Analyst, Deutsche Bank AG

Q

No. It's just that you're growing quite rapidly, but you said the mix was slightly negative to – for your operating margin and leverage. And so, therefore, I was just wondering what the outlook for whether we would get operational leverage in 2018, if you continued to grow, whether that would happen if you continued to grow at quite a strong rate in Italy?

Hans Ploos van Amstel
Chief Financial Officer, Adecco Group AG

A

Yeah. Hans here, we did drove good operating leverage into Italy, and we always have. It's a good – A, it's a very health margin to start with. But you also have seen the mix of business shifting a little bit with the level of growth there. And you have a little bit still coming out of the [indiscernible] (00:44:31) subsidies and all that, that has helped in the past also, the margins.

So that comparison base also is a little bit impact how some of the subsidies have played over the last years. We're continuously pleased in Italy with the growth momentum, strong margin leadership, and we're driving operating margin with a strong margin, while you see some shifts of mixes and the way these subsidies are playing into the mix.

Tom Sykes
Analyst, Deutsche Bank AG

Q

Okay. But does mean you still – you'd expect your operating margin up in Italy in 2018, when you take into account the mix and subsidies?

Hans Ploos van Amstel
Chief Financial Officer, Adecco Group AG

A

Yeah. We're here to drive profitable growth, but we report every quarter how we do in that statistic.

Tom Sykes
Analyst, Deutsche Bank AG

Q

Okay, fine. And then, actually one shorter follow-up on the tax side, I believe you put Mya into your larger retailers in Q4 or the contracts you had with large retailers in Q4. I think, you mentioned at the time, something like 12 was your largest retail accounts in North America in Q4. Just wondered if you could give us some of your experiences with Mya as you rolled it out, please?

Alain Dehaze
Chief Executive Officer, Adecco Group AG

A

Yes. We have in the meantime; we are working with 11 customers in the U.S. so we have expanded the first pilot phase to another one, quite promising. And we see that, for example, with one large client where we're able to reduce the number of [ph] STE (00:46:14) on the account by 3% and improve the fill rate by 1%. So we see good potential to roll out more widely for high-volume clients.

And what you see also is, Mya is an example of how we are putting artificial intelligence, deep learning at work. We're applying artificial intelligence now in various business. Vettery will be another example where we will put artificial intelligence at work to do the curation of the candidates. But also within InFo that we have developed together with Salesforce.com, we are also looking at putting artificial intelligence at work to increase the efficiency, automate repetitive transactions so that we can focus on candidates and customers, value-add and increase our productivity.

Tom Sykes
Analyst, Deutsche Bank AG

Q

Okay. Thank you very much.

Alain Dehaze
Chief Executive Officer, Adecco Group AG

A

You're welcome, Tom.

Operator: The next question comes from Hans Pluijgers from Kepler Cheuvreux. Please go ahead?

Hans Pluijgers
Head of Research, Kepler Cheuvreux SA (Netherlands)

Q

Yes. Good morning, gentlemen. Two questions from my side. First of all, going back on the gross margin and SG&A leverage that we indicated onsite is quite – is significant impact of that 30 basis points, but in principle it should be logical that, the impact on the gross margin should be offset by the same amount or same impact on the SG&A. So I'm making a quick calculation, I come to 20 basis points. Of course, also the SG&A should have a positive impact of 20 basis points, so the underlying leverage is quite limited. Is that a fair assumption?

And secondly on free cash flow generation, yeah, beside of course the increase in gross, but also on the timing impacts in the cash generation on Q4, could you give some [indiscernible] (00:48:13) on that?

Hans Ploos van Amstel
Chief Financial Officer, Adecco Group AG

A

Yes, I think what you take as onsite into the mix is probably a little bit more optimistic than what I would see. But you're right that onsites, the gross margin reduction should come one-on-one out of the SG&A, because onsite has a better delivery model.

If we look at our operating leverage this year, we held the margin about stable, while we're making 25 basis points of investments. So we are driving operating leverage while we have the 30 basis points headwind into the gross margin. But we're also going through a period of investing. We're investing in front offices, we're investing in our digital tools, so we have a period of investment.

If I look at the FTEs versus the sales growth, we did 3% – 7%. So, yes, the onsite plays, but not to the amounts – when I say relevant, probably it's not as relevant as you did the calculation. If I look at the cash flow, for the year, we had strong cash flow ahead of the profitability, so it's ahead of the EBIT. So we continue to drive a very good operating metrics there.

DSO was stable. If you look in the last quarter, you have from Q3 to Q4, last year we drove down the receivables, and this year, they're stable. So we had a more favorable Q4 last year than this year, because receivables quarter-over-quarter was down last – stable this year. But if I look back at the fiscal year this was a better fiscal year cash flow than last year.

Alain Dehaze
Chief Executive Officer, Adecco Group AG

A

And if you were asking about the impact of having the 31st of December on a Sunday, yes, to have the last day of the quarter in a weekend is never favorable.

Hans Pluijgers
Head of Research, Kepler Cheuvreux SA (Netherlands)

Q

Okay. Thanks.

Alain Dehaze
Chief Executive Officer, Adecco Group AG

A

You're welcome.

Operator: The next question comes from George Gregory from Exane BNP Paribas. Please go ahead.

George Gregory
Analyst, Exane BNP Paribas

Q

Good morning. Yeah...

Alain Dehaze
Chief Executive Officer, Adecco Group AG

A

Hi, George.

George Gregory
Analyst, Exane BNP Paribas

Q

Just following up on that last question, just to sort of clarify some of the points. So the 25 basis points investment, which you explained at your Capital Markets Day year-on-year in 2018 should be neutralized by the gains.

I think, you suggested maybe 15 basis points or so of operating leverage. There is a 15 basis points drag from CICE, which you'll try to offset. Telling all that together, should we therefore be expecting margins to be flat to up based on the fact that bank holidays are neutral or are there any other moving parts that we should be accounting for? Thanks – as operating margins?

Hans Ploos van Amstel
Chief Financial Officer, Adecco Group AG

A

No, I think, I'll let you add up the individual components, but what we said and we continue to say is that, GrowTogether is coming out of the investment phase. We're delivering €50 million of true savings, which will offset some of the investments we're making in the strategic IT agenda. So that's coming out of an investment phase. Most of the investment this year was in GrowTogether.

Next year, digital enters the investment phase of that 25 basis points. And then, we have the CICE we need to offset, [indiscernible] (00:52:00) many things, but yeah, I think, you summarized the key components, and how they quarter-by-quarter pan-out, that's what we report. But I think you got the gist of it.

George Gregory
Analyst, Exane BNP Paribas

Q

Okay. Thank you.

Alain Dehaze
Chief Executive Officer, Adecco Group AG

A

You're welcome, George.

Operator: We have a follow-up question from Matthew Lloyd, HSBC. Please go ahead?

Matthew Lloyd
Analyst, HSBC Bank Plc

Q

Hello again, gents. Just two questions, really. One, I just wanted to understand, in France, has the CICE enabled more price competition from smaller players, because if they've got that cash inflow, can they afford to be [ph] cuter (00:52:44) on gross margins? Is there a potential pricing pressure offset as CICE reduces?

And then second question, there's a lovely Harvard Business Review article pointing out just how many people work in call centers pretending to be chatbots in Bangalore, in Indonesia. Can you confirm that you don't employ lots of people pretending to be Mya, pretending to be people?

Alain Dehaze
Chief Executive Officer, Adecco Group AG

A

This is a very creative question. No, when we – and I was mentioning the people we have been able to – for efficiency, we have been able to save. So the chatbots we have are real chatbots, and I can tell you, we are looking at that, the same with Vettery and so on. So it's really technology at work. We look into detail, various companies, various technology, and that's why we choose, for example, Vettery in this field. So, it's real chatbots.

Matthew Lloyd
Analyst, HSBC Bank Plc

Q

Good.

Alain Dehaze
Chief Executive Officer, Adecco Group AG

A

And then, they are based in New York. Now, regarding France, the point is, if I try to – if I have understood well your question, is yeah, this is true for big companies who have given away in the past the CICE to the customers in a way [indiscernible] (00:54:32). For sure, they had been impacted, and they are impacted especially as they assured there is no other compensation from the 7% to the 6%. In 2019, we will get social charges decreased and so on, we don't know the details, yet, but that's the situation, today.

Hans Ploos van Amstel
Chief Financial Officer, Adecco Group AG

A

Yeah. I think – but I think for 2018, that definitely is from the perspective on pricing. I think, there's no reason to say, because you get last CICE that, that could potentially be an offset to the last CICE.

Your question on the people who work for us who can be replaced by – we also, I think, get new customers, which I wanted to add, which asked us to do flexible labor solutions in new businesses. I'll give you an example. For one company in the car industry which does e-cars, we install at home all their trucks, and I can continue.

We do new store, staff solutions for customers. So yes, this will happen. I think that's a good change for us, because company structurally will use, and that will more flexible labor. But we also see newer businesses that are coming to us for new solutions. So I think we'll see both.

Matthew Lloyd
Analyst, HSBC Bank Plc

Q

And one follow-up question because my colleague will kill me if I don't ask it. Your GDPR costs. Are they – how much is it costing you to become GDPR-compliant?

Hans Ploos van Amstel
Chief Financial Officer, Adecco Group AG

A

I know that. I might not tell you. But in our cost of business and I think it's good, also cost of increasing compliance. One thing you see, and it's not just GDPR, cyber security risk, more and more costs. And those are not in the 25 basis point [indiscernible] (00:56:37) we just see those need to be offset with all those savings. But we are having very solid programs on GDPR. We have them on cyber security.

And those are good for us, because smaller players going forward might not be able to [indiscernible] (00:56:52) we're going a little bit through a period of transition as industry, but I keep telling you and [indiscernible] (00:56:57) that this will drive true growth for us because with GrowTogether, we can access data better than the smaller players, we can scale technology better [indiscernible] (00:57:08) for our customers the re-assurance be it on cyber security, global data protection. We're now in an investment phase, but I think these are all good investments to strengthen the cash flow profile of the business.

Matthew Lloyd
Analyst, HSBC Bank Plc

Q

Okay. Thank you very much.

Alain Dehaze
Chief Executive Officer, Adecco Group AG

A

You're welcome.

Operator: Gentlemen, there are no further questions.

Nicholas de la Grense
Head of Investor Relations, Adecco Group AG

Thank you, everyone [indiscernible] (00:57:30) I appreciate, it's a very busy results morning for a lot of you, and thank you for your questions. Also, we look forward to speaking to you again either during the roadshow or otherwise when we report our Q1 results on the 8th of May. Thank you.

Alain Dehaze
Chief Executive Officer, Adecco Group AG

Bye-bye.

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.