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Adecco Group AG (ADEN.CH)

Q3 2016 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Ladies and gentlemen, good morning. Welcome to the Adecco Q3 2016 Results Analyst Conference Call. I'm Selena, the Chorus Call operator. I would like to remind you that all participants will be in listen-only mode and the conference is being recorded. After 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. David Hancock, Head of Investor Relations, accompanied by Mr. Alain Dehaze, CEO; and Mr. Hans Ploos van Amstel, CFO of the Adecco Group.

Please go ahead, gentlemen.

David J. Hancock
Head-Investor Relations, Adecco Group AG

Thank you, Selena. Good morning, everybody, and welcome to the Adecco Group's third quarter 2016 results conference call. To present to you today, I'm joined by Alain Dehaze, Group CEO; and Hans Ploos van Amstel, Group CFO. Before we start, as usual, please have a look at the disclaimer regarding forward-looking statements in this presentation.

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

With that, Alain, I hand over to you.

Alain Dehaze

Chief Executive Officer, Adecco Group AG

Thank you, David. Good morning, ladies and gentlemen, and welcome also from my side. Thanks to the engagement of our colleagues and associates, the Adecco Group delivered another good performance in Q3 2016. Before going into the numbers in more detail, I wanted to mention that while delivering these results, we made further progress in deploying our strategic priorities. We are strengthening our competitive positions, working with leading partners to streamline all processes and upgrade all customer-facing and back-office IT. We are also acting on areas of underperformance, improving the performance of businesses currently operating below their potential and exiting those that structurally cannot achieve all goals. I want to take this opportunity to thank my colleagues for the efforts and progress during the last quarter.

So, turning now to the highlights of the third quarter, on this and the following slides, I will give all growth rates organically unless otherwise stated. In Q3 2016, we had revenues of €5.8 billion, an increase of 3%. Trading days had a slightly negative impact this quarter. Excluding this effect, revenues grew by 3.5%. The gross margin was 18.7%, down 20 basis points year-on-year. SG&A, excluding one-offs, was up 3% year-on-year or down 3% sequentially. This resulted in EBITA excluding one-offs of €320 million. The margin was 5.5%, down 30 basis points year-on-year. Revenues in September were up 4% organically and adjusted for trading days.

Let's have a look at the third quarter operating performance in more detail and I will start the revenue redevelopment by region. In Europe, revenues grew by 3% in the quarter. A decline in Germany, Austria and Switzerland was offset by good growth in Italy and Iberia. In North America, revenues declined by 1%, the same as in Q2. Growth in the rest of the world, including Japan, was 7% in Q3. Revenues were up 2% in Japan and up 10% in the rest of the world.

We look next at the revenue development from a business line perspective. In Q3, revenues grew by 3% in Industrial and by 4% in Office and in Professional Staffing. Growth rates in Q3 were similar to Q2 when excluding the positive effect of trading days in Q2.

Let's also have a look at the third quarter revenue development by service line. Temporary staffing is our largest service line. Growth here was 3% this quarter, the same as in the previous quarter. Revenues from permanent placement grew by 5% in Q3 compared to 9% growth in the previous quarter. In outplacement, revenues were up 8% this quarter compared to 1% in Q2.

Next, I will go through our main markets by geography. Turning first to France. Revenues were up 3% in Q3, in line with Q2. Revenue growth continued to be good in construction and logistics and was, again, very strong in automotives.

General Staffing revenues grew by 3% and Professional Staffing growth accelerated to 14%. Permanent placement revenues were again strong, up 22%. The EBITA margin was 7.2%, down 10 basis points year-on-year. In September, revenue growth adjusted for trading days accelerated slightly compared to Q3.

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We turn next to North America. Revenue decreased by 1%, the same as in Q2. In Professional Staffing, revenues were flat. Medical & Science was up 16% and Finance & Legal was up 3%. IT and Engineering & Technical, both declined by 4%.

In General Staffing, revenues were down 1%. Office grew 2% and Industrial was down 3%, reflecting the softening in the U.S. economy this year. In Perm, revenues were flat. The EBITA margin, excluding restructuring cost, was 6.2% in the quarter, down 20 basis points year-on-year. In September, the revenue decline, adjusted for trading days, was similar to the quarter overall.

In the UK and Ireland, revenues were up 4%. In our large Professional Staffing business, revenues were up 2%. IT was up 5%, partially offset by Finance & Legal, down 12%. Our General Staffing business is mainly exposed to Office which was up 6%. Perm revenues were down 3% in the quarter. This reflects uncertainty or increased uncertainty following the vote to leave the EU, impacting especially the London area.

The EBITA margin was 2.5% compared to 2.7% in the same quarter last year. In September, revenue growth adjusted for trading day accelerated slightly compared to Q3. In Germany, Austria and Switzerland, revenue declined by 2%. Revenues in Germany and Austria were down 2%. This was driven by mid-single-digit decline in automotive. In Switzerland, revenues declined by 3%, negatively impacted by reductions in the export-related and medical sectors. The Q3 2016 EBITA margin, excluding restructuring costs, was 7.2%. This is a decrease of 160 basis points compared to Q3 2015, negatively impacted by an increase in bench costs in Germany. In September, revenue growth, adjusted for trading days, was similar to Q3 overall.

In Benelux and Nordics, revenues increased by 2%. In Benelux, revenues were down 2%. We outperformed the market in Belgium with broad-based growth, while in the Netherlands, our price discipline negatively impacted growth in a competitive market. In the Nordics, revenues were up 8% with good growth in all countries. During the quarter, we made an acquisition in Finland to reach critical mass in this market. The EBITA margin for Benelux and Nordics was flat at 4.6%. In September, revenue growth, adjusted for trading days, was similar to the quarter overall.

Finally, in terms of segment performance, I will touch briefly on some of all the markets. In Italy, growth accelerated to 13% and the EBITA margin improved by 90 basis points. Japan delivered another good performance. Revenues grew by 2%, with continued strong growth in Professional Staffing and permanent placement and an improvement in profitability.

In Lee Hecht Harrison, revenues were up 5%. We continued to see contrasting trends in the largest businesses. Strong growth in the U.S.A. and good growth in the UK offset the decline in France ahead of the election next year.

And with this, I hand over to Hans to take you through the financials in more detail.

Hans Ploos van Amstel

Chief Financial Officer, Adecco Group AG

Thank you, Alain. I will start with an overview of the P&L. Alain already mentioned the operating highlights in his introduction with revenues of €5.8 billion and EBITA, excluding one-offs, of €320 million. Below EBITA, other income and expenses was negatively impacted by non-cash losses on disposals in Russia, Ukraine and Venezuela. Net income attributable to Adecco shareholders was €173 million. In the prior year, we reported a net loss as we recognized an impairment of goodwill of €740 million.

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Now, we look at our sequential revenue growth analysis. This slide shows the sequential growth adjusted for currencies, acquisitions and trading days for each quarter compared to the long-term trends. In this way, we show the sequential growth adjusted for seasonality. For Q3 2016, we were in line with the long-term growth trends just as we were in Q1 and Q2. This shows that we're seeing a continuation of the growth trends in Q3.

Next, let's have a look at the year-on-year gross margin evolution. The group's gross margin was down 20 basis points to 18.7% in Q3 2016. Normally, we showed the gross margin to one decimal place, but we have some slightly unusual roundings this quarter, so we added the more precise numbers from the slide.

Compared to last year, acquisition and currency movements each had a positive impact of 10 basis points. On an organic basis, the gross margin was down 40 basis points, outplacement added 10 basis points to the gross margin, while permanent placement had a neutral impact. The temporary staffing gross margin was down 50 basis points. This decrease is higher than in the first half due to workers' compensation charges in North America and an increase in bench costs in Germany this quarter.

Now, let me discuss how our cost base developed in the third quarter. SG&A, excluding one-offs, was up 3% organically compared to the prior year. This was largely driven by a 2% increase in head count. Sequentially, our cost base was down 3% organically and excluding one-offs, better than our guidance of approximately flat.

Turning to the cash flow statements. In Q3 2016, cash flow generated from operating activities was €217 million compared to €293 million in Q3 2015. The difference is mainly due to three effects. First [ph] EBITA (13:35) was lower in Q3 2016 compared to Q3 2015; second, working capital increased as the stronger sequential sales growth more than offset the better DSO performance. And thirdly, we had some negative impact from the timing of tax payments.

DSO in Q3 was at 52 days, 1 day less than in the prior year. This quarter, CapEx was €18 million compared to €25 million in Q3 2015. This mainly reflects lower capital expenditure on IT.

Finally, net debt at the end of September 2016 decreased to €1.2 billion compared to €1.4 billion at the end of June. Our net-debt-to-EBITDA ratio was at one times at the end of Q3 2016.

And with that, I hand back to Alain.

Alain Dehaze

Chief Executive Officer, Adecco Group AG

Thank you, Hans. And let me now comment on the current trading. Organic revenue growth adjusted for trading days was 3.5% in Q3 2015 and 4% – in 2016 and 4% in September. Volume growth in October was similar to September. In Q4 2016, SG&A, excluding one-offs, is expected to increase organically compared to Q3, in line with the normal seasonal increase of approximately 3%.

And with that, I would like to open the line for your questions.

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QUESTION AND ANSWER SECTION

Operator: We will now begin the question-and-answer session. [Operator Instructions] The first question comes from Denis Moreau from UBS. Please go ahead.

Denis Moreau
Analyst, UBS Ltd. (Broker)

Q

Hi. Good morning, everyone. Denis Moreau, UBS. Two questions, please. First, one on the gross margin. I let my colleague raise a question regarding the 50 bps drop for temps and I would like to focus actually on the decline – on the stability actually for perm. We have no improvement in the – no positive effect on the gross margin from the good growth in perm hirings. It's been good in Q3. It was good as well in Q2. So, what is the rationale behind that? Why don't we see any positive impact from this good performance in perm hirings? That's my first question.

My second question relates to the one-off charge of €26 million. I'd like to better understand why we should consider this charge as a one-off? The comments you made, for example, regarding Australia were sales grew by 9% and you mentioned some cost optimization measures, which does not exactly sound to me like a one-off, but rather ongoing discipline on costs. And so, to follow up on [ph] this idea (17:04), if these costs are truly one-off, does that mean that there will not be any further one-off restructuring charges in Q4 relating to the geographies impacted in Q3? Thank you.

Alain Dehaze
Chief Executive Officer, Adecco Group AG

A

Thank you, Denis. I will take the first question and Hans will take the second question. Regarding the perm, what you see overall that the perm growth declined from 9% in Q2 to 5% in Q3. When you look at in more details, you see that the decline is mainly concentrated on two geographies: North America and the UK. That's where you see – America, we had a Q2 of [ph] plus 5% (17:55), and we are now at 0%; and the same in UK where we had minus 3%. But if we exclude these two geographies, you will see that the perm business is remaining very strong. If I take France, plus 23%; if I take Italy, fourth quarter in a row, about 40% and so on. So, there is – I think I have answered your questions by showing also the mix where this perm growth and decline is coming.

Denis Moreau
Analyst, UBS Ltd. (Broker)

Q

Okay. So, that means you do normally a better margin in the UK and in North America [indiscernible] (18:37)?

Alain Dehaze
Chief Executive Officer, Adecco Group AG

A

That perm is here.

Hans Ploos van Amstel
Chief Financial Officer, Adecco Group AG

A

What you saw – Hans here – just to add a little bit to gross margin because indeed there were quite a few things. First, you mentioned the 50 basis points reduction. What was – there are two things into the quarter which are important to mention? One, in Q3 2015, we had a favorable gross margin which was driven that we had some favorable items like in the workers' comp in North America and this quarter, we had an unfavorable item into the workers' comp. So, that quarter-to-quarter, played.

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On top of that, in the outsourcing business in Spain, we made some reorganization which flows through the gross margin. There are a few other items which were favorable last year that if you just do the real comparison on the gross margin, we see a continuation of the mix and pricing in line with what we saw in the first half, around [ph] that 20 or 30 (19:42) basis points and the rest is just the comparison base because of the items I mentioned. The perm business has a positive impact on our gross margin. But given that we have this quarter 5% growth, it was a small plus which rounded up to a zero into the total. But, yes, the perm business has a positive gross margin, but with 5% growth, it just doesn't weigh enough of the total results to have that impact.

When we go to organization, there was a lot into the quarter, you talked about Australia. We're very pleased with Australia on the progress we've made. We have diversified the business away from the oil and gas exposure, so we have a much better mix of business. We have some [indiscernible] (20:36). Australia has been underperforming for a long time. We're addressing that given the significant changes we're making and there are some one-off costs, but we have had a few of those, but that's all geared to deliver profitable growth going forward.

And if you look at the underlying profitability, it has improved this quarter. We just have to – we had one unfortunate [indiscernible] (20:58) of an old customer which happened, and then we made this reorganization cost to make sure that the cost base of the business and the infrastructure is shifting with the new business we're pursuing and is adjusted for the size of the business. Business is well under control and the team is making good progress.

Denis Moreau Q
Analyst, UBS Ltd. (Broker)

Okay. So that means no big restructuring charge number or one-off in Q4, right? I mean, generally speaking.

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

We should not be in the business of one-offs, but I hope you see that we are acting on some of the underperformance which was in the business for a longer period and have not been addressed. We are addressing that and are not shying away from taking the cost to make sure we get the business to the profitability we want perhaps in Australia. And similarly in Germany, and we can talk more on Germany. Last year, we had the goodwill impairment and we anticipated that we needed to make changes in the business model of Germany. And we were also acting there on the integration and reorganization to make sure we [ph] come to a (22:12) profitable growth also in Germany going forward.

So, it's a lot that I acknowledge and recognize, but it's driven by the actions we're taking to improve the overall performance of the portfolio. And we're doing that in Germany, we have done it in Australia. We exit the business in Russia, Venezuela and Ukraine, the rest in Holland. So, it's just an outcome of our performance management.

Denis Moreau Q
Analyst, UBS Ltd. (Broker)

that's very clear and very helpful. Thank you.

Alain Dehaze A
Chief Executive Officer, Adecco Group AG

Thank you, Denis.

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Operator: The next question comes from Mr. Chris Gallagher from JPMorgan. Please go ahead.

Christopher Charles Gallagher
Analyst, JPMorgan Securities Plc

Q

Good morning.

Alain Dehaze
Chief Executive Officer, Adecco Group AG

A

Good morning, Chris.

Christopher Charles Gallagher
Analyst, JPMorgan Securities Plc

Q

Three questions from me. Just first, kind of continuing on the €23 million restructuring, that would give you a bit of a help from an SG&A perspective going into Q4. So, why do you not expect this slightly lower-than-normal increase and what payback do you expect in these different sections over the next year?

Second then, around the gross margin. Let me talk a little bit about your pricing strategy and how much of the pricing decline is you trying to move back to market versus actually underlying pressure in the market and maybe where that is.

And then the third question just around CICE, we're seeing that may well be increased for next year to 7%. Maybe any discussions you've had around that. Thank you.

Alain Dehaze
Chief Executive Officer, Adecco Group AG

A

Thank you, Chris. I will start with the CICE and the pricing strategy and then Hans will answer your third question on the – your restructuring. Regarding the CICE, there has been an announcement in July from Poland saying that it was finally willing to increase the CICE from 6% to 7%.

This statement is reflected in the budget proposal that we – from – everybody has heard about it. So, it is in the budget draft and this has been – or this has to be voted in December by the parliament. So, that's the situation today. But it is in the budget draft, increased from 6% to 7%.

Regarding the gross margin annual pricing strategy, we continue to maintain the pricing strategy and the cost discipline we have. The pricing pressure is not more, not less than it was in the previous periods. That's what we see also in the results. We have said, yes, we want to grow in line with the market and we want to do that in a profitable way. That's – for example, one of the reason we are pushing the segmentation. And we see that in some of our key markets, this segmentation is bearing its fruits, being France, being Japan, being Iberia.

For example, in France, we grew with 15% on the small segment in Q3, 15% on the small, 5% on the medium, and 1% on the large. So – and we continue to push to be in line with the market, but in a profitable way.

Hans Ploos van Amstel
Chief Financial Officer, Adecco Group AG

A

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Chris, Hans here. On the restructuring, three elements. Germany, which is €13 million out of that €23 million, because of the legislative environments and the notice periods that the savings will start to come in and the head count reduction, early 2017. So, the notice period.

In the U.S., we executed the restructuring and that you will see already in the margin this quarter. Because this quarter, we have that mix impact because of workers' comp. If you take that away, the U.S. margin would have been up. And the underlying conversion ratio improved, so you see the productivity already into the quarter.

Australia, what we see on the cost restructuring, we saw that the underlying margin is already improving and we'll see a continuation of that. So, it goes at different levels into the P&L.

Christopher Charles Gallagher
Analyst, JPMorgan Securities Plc

Q

Okay. Thank you. And then just should we expect an ongoing restructuring? [ph] I heard a (26:38) comment you made around working with partners to streamline about your customer-facing activities as well?

Alain Dehaze
Chief Executive Officer, Adecco Group AG

A

Yeah. We are focusing on four main areas. We are working on the branch network and especially moving to the digital, physical and hybrid relationship that we have to develop with all candidates and clients. We are working on the front office, mainly improving the order fill rate. We are working on the back office and central functions, digitizing the processes. You have seen also, in Germany, we are consolidating the back office. And last but not least, we are working also on the procurement. We improved the transparency of all figures to leverage all sites. And we do that, we've partnered with, let's say, the competencies and the track record of successful similar projects such as Heinz or AB InBev and Mondelez.

Christopher Charles Gallagher
Analyst, JPMorgan Securities Plc

Q

Okay. Great. Thank you very much.

Alain Dehaze
Chief Executive Officer, Adecco Group AG

A

Welcome, Chris.

Operator: The next question is from Mr. Toby Reeks from Morgan Stanley. Please go ahead.

Toby W. Reeks
Analyst, Morgan Stanley & Co. International Plc

Q

Hello. I've got two questions. Could you just talk a little bit about the working capital? I didn't quite catch all the elements you're talking about where we saw the deterioration in Q3.

And then secondly, when you say you're acting on areas of underperformance, I appreciate you've gone through Australia and Russia, for example, as markets that you'll be exiting, and oil and gas. Is it just regional and in the customer base or are we seeing any sort of [ph] exiting (28:24) around delivery model or anything like that? Thank you.

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Alain Dehaze
Chief Executive Officer, Adecco Group AG

A

I will start with your second question and Hans will continue on the working capital. Acting on the underperformance, so, some operations like Australia and Hans has already elaborated on it. We are pleased with the way it is progressing. Another country where we are focusing on our watch list is Norway. And there also, we are very pleased with the rebound of Norway.

And – but for economic reason and for regulation reason, we have taken the decision to exit Venezuela, Russia and Ukraine. Why? Because the conclusion of our analysis that in these three countries, it was unable, let's say, structurally impossible to reach – or ambition to reach at least 4.5%, 5% on average through the cycle. That's point one. And second, yeah, country like Croatia especially has a very difficult regulation for our industry. And the conclusion was for us to – it was better to exit and reinforce our portfolio in this way.

Toby W. Reeks
Analyst, Morgan Stanley & Co. International Plc

Q

Okay. So, it is just about those specific end markets where you don't think you're going to get to that margin level?

Alain Dehaze
Chief Executive Officer, Adecco Group AG

A

Exactly.

Toby W. Reeks
Analyst, Morgan Stanley & Co. International Plc

Q

Okay. Thank you. And then the working capital point?

Hans Ploos van Amstel
Chief Financial Officer, Adecco Group AG

A

We had – Hans here. The DSO was down one day. So, continued good progress on the controls and oversight on the receivables. But because the sequential sales growth was higher, there was a net investment in working capital. That would have been more if we wouldn't have take the DSO down. But it was a net investment because of our growth. So, that's – we should take that to the positive because we're growing our business with good DSO oversight.

Toby W. Reeks
Analyst, Morgan Stanley & Co. International Plc

Q

All right. Did you mention one other thing? That was the thing I didn't really get.

Hans Ploos van Amstel
Chief Financial Officer, Adecco Group AG

A

There are three elements driving the cash flow. One is – and that's the EBITDA is below last year and that's also impacted by some of the reorganization changes we made. So, that investment of reorganization impacted profitability. The working capital [indiscernible] (30:54) then were some timing, smaller one, of tax payments into the quarter. But that was just timing-related.

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Toby W. Reeks
Analyst, Morgan Stanley & Co. International Plc

Q

Okay. Great. Okay, thanks, guys.

Hans Ploos van Amstel
Chief Financial Officer, Adecco Group AG

A

But still good cash flow return, and the cash flow will come to the 90%...

Alain Dehaze
Chief Executive Officer, Adecco Group AG

A

Cash conversion.

Hans Ploos van Amstel
Chief Financial Officer, Adecco Group AG

A

...conversion.

Operator: The next question is from Mr. Paul Sullivan from Barclays. Please go ahead.

Paul D. Sullivan
Analyst, Barclays Capital Securities Ltd.

Q

Yeah. Good morning, everybody. Just a couple from me. Could you give us any more color on the exit rates in Italy, Iberia, rest of the world? Sometimes, you give a bit more granularity on those exit rates. And that's the first question.

Secondly, on the gross margin and the impact in Germany in bench risk, do you see that as sort of a – is that fairly temporary? Is it skewed to one auto customer in particular? How do you see it sort of working through the fourth quarter?

And when it comes to the overall development of the gross margin into the fourth quarter, sounds like you're indicating we go back to that underlying decline of sub-25 bps, 30 bps. I know there's some comp issues from the fourth quarter of last year, but if you could give us any moving parts there, that would be helpful. Thank you.

Hans Ploos van Amstel
Chief Financial Officer, Adecco Group AG

A

Yes. If we look at the exit rate, it's very consistent with what we see it at the global level. So, we see across the markets [ph] hub (32:24) that the exit rates confirm that we ended the quarter on a solid note and we saw that – it was actually quite broad-based across the market. So, the trends you see in the quarter are very much reflective of the exit rates.

If we look at gross margin going into the fourth quarter, we think sequentially, the gross margin will stay about the same, which means year-on-year, the 50 basis points reduction versus Q4, but recall last year, we had some releases in France, the German days trade and that's around, I think, 35 basis points. So, the big part is explained by the German days and France releases, which we mentioned last year in Q4.

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That means, that implies that we will improve on the bench cost in Germany. So, we anticipate to do better on that. But we're, obviously, watching that carefully because of the visibility we have, but we are planning to improve on the bench cost in Q4.

Paul D. Sullivan
Analyst, Barclays Capital Securities Ltd.

Q

Great. And is it skewed to one customer in particular or is it more widespread in Germany?

Hans Ploos van Amstel
Chief Financial Officer, Adecco Group AG

A

It's across different customers and [ph] back deals that some portals they got temps (33:41) and they hire them permanently and that weighs in to the quarter and that you cannot always predict.

Paul D. Sullivan
Analyst, Barclays Capital Securities Ltd.

Q

Great. Thank you very much.

Hans Ploos van Amstel
Chief Financial Officer, Adecco Group AG

A

Thank you.

Operator: We have a question from Mr. Alain Oberhuber from MainFirst. Please go ahead.

Alain-Sebastian Oberhuber
Analyst, MainFirst Schweiz AG

Q

Good morning, gentlemen. Alain Oberhuber, MainFirst. I have three questions [indiscernible] (34:07).

The first is regarding France. Will you talk a little bit more about the development? Although we saw in – statistically in the market an improvement in the momentum, you haven't really experienced one as the organic growth in France is similar to Q2.

The other question is regarding the mix. The Professional Staffing grew 4% as well as General Staffing. Isn't there – if you could talk a little bit more about professional staffing, what could we expect? Because I remember in H1, you said you expect a positive mix effect from higher growth in professional staffing at year-end. Have you already seen it or could we see it then in Q4?

And the last question is regarding the cash generation we currently see. As I understand you, you're still doing bolt-on acquisitions and your financial leverage has declined significantly. Could we expect a higher dividend payout?

Alain Dehaze
Chief Executive Officer, Adecco Group AG

A

Okay. I will start with France, take the cash generation, the high dividend; and Hans will come back on the mix – your mix question, Alain. Now, regarding France, what – if we start with the figures, indeed, we had 3% growth in Q2, 3% in Q3. We have an exit rate in September which is higher than the figure of Q3 and which has been

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confirmed also with the volume of October. What we see, to give more color on this, is that the growth we are still double-digit growth in automotive. We have good high single-digit in construction and logistics.

I told you the growth by segment, 15% in small, 5% in medium and 1% in large. So, we are very pleased with this segmentation. What is also strong is deferred business. So, we stick now to the 20%-plus. It was 23% in Q2, 22% in Q3. And also, we see also the start of Professional Staffing becoming strong. Revenues increased with 14% in the third quarter.

Now, when you benchmark this performance, let's say, to the peer group, yeah, we are closing the gap with – the last one we had to close the gap. But we do it in a profitable way and that you can see again in our results. We have an EBITA margin of 7.2% in Q3, let's say, more than – even more than 100 basis points gap with the other peer groups. So, that's the situation in France. And on your point regarding cash generation and high dividend, we stick to what we have told you during the IR Day. We are applying, let's say, a progressive dividend policy with the previous year dividend considered as floor and we'll stick to our words.

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

Quickly, on the mix of Professional Staffing, that's broadly in line, hasn't really moved material within the year [indiscernible] (38:03) mix. But that's not driven by – we have good Professional Staffing business this year. But if we look in last quarter in the U.S., we have improved the trend in General Staffing by the new client wins. So, that does help the mix also on the General Staffing.

In the UK, we had a new client win also in General Staffing and that sort of – both have improved. So, the mix hasn't, but that's more driven – that also, on the Other business, we made good progress. And in Japan, Professional Staffing was up 11% and we had also good margin progress into the quarter.

Alain-Sebastian Oberhuber
Analyst, MainFirst Schweiz AG
Q

Thank you. Just a follow-up question on debt. So, could you still expect in Q4 a positive mix effect?

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

As you see, what we have seen in the mix of this year, it would be hard to say that in one quarter, we would materially move that mix.

Alain-Sebastian Oberhuber
Analyst, MainFirst Schweiz AG
Q

Okay. Thank you very much.

Alain Dehaze
Chief Executive Officer, Adecco Group AG
A

You're welcome, Alain.

Operator: The next question is from Mr. Tom Sykes from Deutsche Bank. Your line is open.

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Thomas Richard Sykes
Analyst, Deutsche Bank AG (Broker UK)

Q

Yeah. Morning, everybody. Just on the U.S. gross margin, would you be able to say – if you were to look at [indiscernible] (39:21) workers' comp and medical, or if you like, all non-wage-related costs in the U.S. and just compare where those are now versus where you were in sort of the previous periods when unemployment has been this low. Where are they as a percentage of sales at the moment, please?

And then, just on the – so further on the restructuring comments. I think if you look back, if one looks back, most of the EBIT growth, if not 100% of the EBIT growth over the last five years has kind of come from France, Italy, U.S. and LHH added together. And so, therefore, the remaining 50% of sales have not really grown EBIT. But you're alluding to ongoing restructuring benefits or at least optimization. What's the scale of what you think can be achieved here? Are we underplaying what might be some more material profit improvements and that's the tail of the business, if you like, please?

Hans Ploos van Amstel
Chief Financial Officer, Adecco Group AG

A

If you look at the U.S. margins, the workers' comp had an impact this quarter. And if you take that away, our margin would have gone up. So, we saw operating leverage and a good margin structure continuing into the U.S. business which we're pleased with.

If you look at the operating leverage into the total business, that continued. We had a 5.5% healthy strong EBITDA margin this quarter. Whereas, that included some additional things, the workers' comp, we had the Spanish reorganization, we had the receivables write-down, we have Argentina, so there were some unfavorable things. And if you look at the FTE investment versus the sales growth, we had good operating leverage into the business. So, we continued to drive productivity and have made some investments to lay the path of future productivity as we discussed. When we look at our productivity initiative we launched, we are going into implementation phase into selective targeted countries. And with evolution, we will build in the right productivity to deliver on our margin improvement objective which we said will be 50 basis points through the cycle. So, we're pleased with where we are in the implementation phase of those initiatives.

Thomas Richard Sykes
Analyst, Deutsche Bank AG (Broker UK)

Q

Okay. And just coming back, the question really on – was just on the U.S. and non-wage costs in the U.S. because obviously you're at a high margin and I was just wondering whether where [indiscernible] (42:24) where your – in total your non-wage costs which will affect your gross margin, where they are as a percentage of sales when you look at the U.S. business now compared to when, I don't know, 2007-2008 at similar levels of unemployment today because obviously medical has gone up a lot, one would assume. And so, just wondering whether that has been actually a negative – those have been a net negative to gross margin or in total a net positive to gross margin versus where you were maybe at 2007-2008, please?

Hans Ploos van Amstel
Chief Financial Officer, Adecco Group AG

A

If you're okay, Tom, I'll come back to you on that separately.

Thomas Richard Sykes
Analyst, Deutsche Bank AG (Broker UK)

Q

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Okay. Yeah. That's fine. That's fine. Okay. I'll leave there. Thank you.

Alain Dehaze
Chief Executive Officer, Adecco Group AG
A

Thank you, Tom.

Operator: The next question is from Mr. Hans Pluijgers from Kepler Cheuvreux. Please go ahead.

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

Yes. Good morning, gentlemen. A few questions from my side. First of all, looking at SG&A and operational leverage potential. You've taken a lot of – some additional measures. But this quarter and also in the previous quarter, operational leverage has been relatively limited. Let's say, considering that the current framework, the current footprint remains intact, what kind of top-line growth do you need to get to some operational leverage next year? What's your base of thinking on that?

Secondly, on price competition, you indicated there was some negative impact on the margin. Could you elaborate a little bit on which countries you view price competition or see any change in environment compared to previous quarters?

And thirdly, on Germany, you've taken some charges optimizing the network. What are you precisely doing and was the background just purely efficiency-related or also, commercial effectiveness? Could you [indiscernible] (44:18)?

Alain Dehaze
Chief Executive Officer, Adecco Group AG
A

Okay. First, I can start with the – sorry, on Germany, Hans, what was your question?

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

What's the background precisely of the measures you are taking? It's purely efficiency-related or there are some other, let's say, strategy behind it?

Alain Dehaze
Chief Executive Officer, Adecco Group AG
A

Okay. I will start with the question three and the question two and Hans will eventually elaborate on also the question two and come back to do SG&A and the operating leverage.

Now, Germany, as you know, we have acquired TUJA in 2007. And now, we have decided to really have the leverage of the combination TUJA-Adecco, both in the General Staffing. Since the 1st of November, we have now a new combined leadership and we have also not only the leadership of [indiscernible] (45:15) in Germany, but we have also a combined operation leadership. So, it means that both the branch of TUJA and Adecco are led, let's say, by area managers combining the two brands.

And as a result of this transformation, yeah, we are consolidating the back office. We have closed and might merge some of the branches to increase the efficiency. Basically, we are doing in Germany what we had done in

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2012 in France when we worked out the combination of Adia and Adecco. That's the background of what is happening in Germany.

Now, regarding the price. What I've said, some questions before, is that, yeah, the price pressure is remaining the same as it was before. There is no significant transformation. The price pressure is mainly concentrated in large accounts. I would say no significant difference, absolutely not. We have mentioned the case of the Netherlands where there we are suffering right now of the losses of customers that – for which we took the decision to exit for price discipline.

Hans Ploos van Amstel
Chief Financial Officer, Adecco Group AG

A

So, that's a continuation of mix and pricing we have seen in the first half. And as we mentioned, there were some special events which impacted the comparison versus last year. If we go back to your question on SG&A, this quarter, we had 2% increase in head count with 3.5% sales growth. That has improved our productivity and that was the same as we did in Q2 because in Q2, we also saw an improvement in the productivity. We're pleased with that forecast. While we also make investments in new client wins in the UK, we're investing in strengthening our business. In the U.S., we said on the General Staffing, we needed to move the client base and we have moved that and that has impacted the results on our General Staffing positively in Q3. The small and medium segment, which are a focus area, we're seeing progress in [indiscernible] (47:54) markets.

So, we're delivering continued growth; we're investing in that. And we should not forget this in an economic environment, which is lower than we started the year. So, we see a continuation of growth in the lower-growth environment. That takes a good investment. But while we're making those investments, we're coming through on the FTE productivity.

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

Q

Going back on that, because in Q3, both top line and SG&A growth were 3% organically. Is that something, let's say, talking also about investing in growth, is that something which you need to keep the current growth going on or, let's say, due to the fact that [ph] you've taken also some restructuring, you expect that (48:35) next year, SG&A growth should be less worse if you look at – to get to sales growth of 3%? How do you see that leverage developing? And on Germany, you're talking about TUJA and Adecco branded. Also, of course, in the Professional side, you have different brands. Is there also [ph] something that plans (48:56) you're having to integrate those into making more, let's say, efficient and commercially stronger?

Alain Dehaze
Chief Executive Officer, Adecco Group AG

A

Regarding Germany, no. In the Professional Staffing, we have two brands. We have DIS and we have euro engineering and then we have – or the new branch, let's say, international branch we are launching with Badenoch & Clark. So, there is no real change foreseen there. It's a different situation there.

In the General Staffing, we have really two organization, let's say, in the General Staffing that's different than what we had in Professional Staffing in Germany. You can draw the parallel with France what we had in 2012.

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

Q

Okay. On the SG&A?

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Hans Ploos van Amstel
Chief Financial Officer, Adecco Group AG

A

Yeah. Hans here, I'll [ph] take that (49:46). So, what we see from the FTE productivity, you see that we have operating leverage in the business. The SG&A was 3% up on the FTE of 2%. What's important to mention that the Australia write-down of the receivables played a big part of [indiscernible] (50:07). We had some reorganization costs in Spain and in Argentina. So, the core SG&A and the core productivity, SG&A is in line with the FTEs. So, you see the operating leverage and we continue to work against that matrix.

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

Q

Okay. Thanks.

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

Konrad Zomer
Analyst, ABN AMRO Bank NV (Broker)

Q

Hi. Good morning.

Hans Ploos van Amstel
Chief Financial Officer, Adecco Group AG

A

Good morning.

Konrad Zomer
Analyst, ABN AMRO Bank NV (Broker)

Q

Apologies for asking another question on Germany. But I was wondering if you could tell us if the competitive landscape in the German market has changed for Adecco because obviously, there are the smaller French companies making inroads in Germany. There are several other local players that have become a bit more aggressive. Is part of your decline in revenue growth due to the internal focus because of the integration of TUJA and Adecco or is that because of the competitive landscape has changed?

Alain Dehaze
Chief Executive Officer, Adecco Group AG

A

So, clearly, the point in this quarter is you know that more than 30% of our revenues are coming from the auto segment. And more specifically, in this segment, we had two of our major customers with, let's say, a specific event. One of the two has hired our temps. So, that's point one. And the other one has a significant reduction of activity, and as a consequence of this, reduced the number of temps used to order with us. And you know, in Germany, the people are on our books, so it's a kind of double pain, lack of revenues and you have the costs.

Now, to your point regarding the competitive landscape, French company and so on, no, we don't see kind of new companies gaining customers or – no, absolutely not. It's actually competition as usual with a specific event we had in the auto.

Konrad Zomer
Analyst, ABN AMRO Bank NV (Broker)

Q

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Right. And on Germany, last year, you obviously had the goodwill impairment. Is there any goodwill left that could potentially be impaired in the next few years if things were to deteriorate in Germany or has everything been impaired already?

Hans Ploos van Amstel
Chief Financial Officer, Adecco Group AG

A

Hans here. When we made the impairment last year, we made a thorough analysis of the German business. And the results of today are exactly what we anticipated back then. So, there's no surprise into the number. It's a big movement quarter-on-quarter. But if you look at our results, it is exactly what we had anticipated. As Alain pointed out, the automotive exposure [indiscernible] (53:12) something we're going to work on, but that was down in the quarter. If you take away automotive, we have modest growth in Germany in the balance of the business. So, there was modest growth in Germany.

Switzerland is a normal area where we need to improve and [indiscernible] (53:32). But therefore, we're making these changes because we recognize we need to work on the competitive position in Germany and therefore, we're making the changes Alain talked about because the German market over the last years has structurally changed, became more of, what I would call, a normal market, [indiscernible] (53:53) benefits in the past which they are no longer in the future. And therefore, we're making the reorganization to drive the competitiveness and similar than what has been done on other markets.

Konrad Zomer
Analyst, ABN AMRO Bank NV (Broker)

Q

Okay. That's very clear. Thank you both.

Hans Ploos van Amstel
Chief Financial Officer, Adecco Group AG

A

Thank you, Konrad.

Konrad Zomer
Analyst, ABN AMRO Bank NV (Broker)

Q

Thank you.

Operator: The next question comes from Mr. Nicholas de la Grense from Bank of America Merrill Lynch. Please go ahead.

Nicholas de la Grense
Analyst, Bank of America-Merrill Lynch

Q

Good morning, guys. Two questions for me, please. The first one, just on North America, I guess, it's a multi-part question. Apologies. I was surprised to see that you've been taking more restructuring charges there given that you reorganized that business relatively recently, I think it was 2014. Is there – is the further reorganization, is it kind of a recognition that that market has now, if not gone X growth, we are kind of late cycle, and you need to be kind of positioning the business for that or was it other things entirely? And I'm thinking of kind of [indiscernible] (54:55) growth data in particular with regard to where we are in the cycle?

And then the second question which is a shorter one, you mentioned the Spanish reorganization was relating to the outsourcing business. So, I was wondering if you could elaborate on exactly what's going on there because, I

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think outsourcing in the past has been an area where you were quite positive. And obviously, the Spanish market itself is growing quite nicely. Thank you.

Hans Ploos van Amstel
Chief Financial Officer, Adecco Group AG

A

Let me start with the outsourcing and then Alain will give some more color on the U.S. business. The outsourcing business has worked very well for us and continues to work very well for us. One part was that we were running call centers. Call centers is a business which is evolving with the technology. Therefore, we made adjustments into the cost base on the outsourcing of this business, so it's predominately call centers. And even with that, we made very good money on it. So, it's a good business model, but things are moving forward.

Coming on North America, before I give it to Alain to give some more color, the $6 million was a cost optimization program. So, not like a big restructuring which already benefited the margin into Q3. We made some efficiency and effectiveness improvements in the corporate head office, into our branch optimization and with that, continued to secure a few just for that workers' comp [indiscernible] (56:22) margin.

Alain Dehaze
Chief Executive Officer, Adecco Group AG

A

Yeah. I would say the beauty of the North American market is that you can run it easily, adapt your capacity to the reality of the market and make sure you are remaining very productive. So, the payback is quite short, so it's very attractive to do it.

Now, to give some more color about the conditions. We have stable conditions over there in North America. You will have seen minus 1% in Q2, minus 1% in Q3. The major difference was in the perm business. That's where we saw a deceleration from plus 5% to zero.

On the General Staffing, I would say that the situation has even improved. We had a minus 3% in Q2. We have now minus 1%. We want some new customers and normally in Q4, this will gain traction. We see also that the oil and gas is bottoming out. Also to mention that Canada has returned to growth, up 6%. So that's what I can say about the U.S.

Nicholas de la Grense
Analyst, Bank of America-Merrill Lynch

Q

Okay. Thank you. Just two quick follow-ups. When you say that oil and gas is bottoming out, is that something that you're seeing in terms of demand for temps in those industries or is that more a comment on the oil price having stabilized in [indiscernible] (57:59)?

Alain Dehaze
Chief Executive Officer, Adecco Group AG

A

The comment is made – if you see, for example, Canada which is really related to the oil and gas development, you see that we have returned to growth to 6%, and I think we are not the only one in this industry, so that's a positive signal. If you see also our activity in Engineering and Technical which relates also to the oil and gas sector, we see also that the situation is improving, so that's why I gave my comment on this.

Nicholas de la Grense
Analyst, Bank of America-Merrill Lynch

Q

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Okay. That's very clear. And just one quick follow-up on the Spanish reopening as well. Are you saying you're scaling down your call center business there or was it that you're having to invest in additional technology? I didn't quite understand.

Hans Ploos van Amstel
Chief Financial Officer, Adecco Group AG

A

We are adjusting the cost base to how call centers are evolving on technology. So, it's just they need less labor into the call centers because these things with the technology are becoming more digital.

Nicholas de la Grense
Analyst, Bank of America-Merrill Lynch

Q

[indiscernible] (59:04). Thank you.

Alain Dehaze
Chief Executive Officer, Adecco Group AG

A

I'm looking at the time and we will take, if any, a last question.

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

George Gregory
Analyst, Exane Ltd.

Q

Morning everyone. Just a few points of clarification. Apologies if these have already been addressed and I've missed them. But on the CICE or French tax credit impact next year, is that still expected to be neutralized by other tax costs? Secondly, I think you had a €21 million net other expenses in the P&L in the quarter. Just wondered what those were? And finally, will the exit of the contracts have any sort of impact on revenue or profit, please? Thanks.

Alain Dehaze
Chief Executive Officer, Adecco Group AG

A

I will take your third question and your first on the CICE and then Hans will come back on the €21 million. Regarding the exit of the three countries, we speak about €70 million revenues. So, quite limited and with a, let's say, a breakeven situation. So, a very limited impact.

Then, regarding the CICE next year, indeed, there is also, in the draft of the budget, the creation of a local new tax, but nobody has really details about that. So, we have no transparency about this potential new local tax. And does it mean that we will be affected by it? That's point one. And second, as you know, part of the – you cannot take the [indiscernible] (1:01:13) growth. We have to invest also regarding employment competitiveness and so on. And that's what we have done during the last year.

Hans Ploos van Amstel
Chief Financial Officer, Adecco Group AG

A

And the other expenses related to the closure of Russia, Ukraine and Venezuela, where we're stopping the business.

George Gregory
Analyst, Exane Ltd.

Q

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The €21 million is on top of the €26 million which you booked as one-offs.

Hans Ploos van Amstel
Chief Financial Officer, Adecco Group AG

A

They're two different thing. We have, in EBIT, €23 million for Germany, Australia, Spain and the U.S. And then, the Spain number is another one-off. So, we had separated one-off. But – and then, below EBIT, we have the cost for Russia, Ukraine and Venezuela. So, in total, around €50 million.

George Gregory
Analyst, Exane Ltd.

Q

Okay. And the distinguishing factors are presumably below the line write-offs, impairments?

Hans Ploos van Amstel
Chief Financial Officer, Adecco Group AG

A

Yes.

George Gregory
Analyst, Exane Ltd.

Q

Thank you.

Alain Dehaze
Chief Executive Officer, Adecco Group AG

Thank you very much. So, thank you for joining this call and for your questions. And we hope to see many of you over the coming days and weeks on the road shows. Otherwise, we look forward to talking to you again with our full year 2016 results on March 2, 2017. Bye.

Hans Ploos van Amstel
Chief Financial Officer, Adecco Group AG

Bye-bye.

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