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ADEN.VX - Q3 2012 Adecco SA Earnings Conference Call

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PRESENTATION

Operator

Ladies and gentlemen, good morning. Welcome to the Adecco Q3 results 2012 analyst conference call. I'm Goran, 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 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 Mrs. Karin Selfors, Head of Investor Relations, accompanied by Mr. Patrick De Maeseneire, CEO of the Group, and Mr. Dominik de Daniel, CFO of the Group.

Please go ahead, ladies and gentlemen.

Karin Selfors - *Adecco S.A. - Head of IR*

Good morning and welcome to Adecco's third-quarter 2012 results conference call. Patrick, Group's CEO, and Dominik, Group's CFO, as always will lead you through the presentation today, followed by a Q&A session. Before we start, have a look at the forward-looking statement in this presentation please.

Let me give you a quick overview of today's call. Patrick will give you the operational highlights, Dominik reviews the financials. And after that, Patrick will give you the outlook for our business before we open the lines for your questions.

Patrick, I hand over to you.

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

Thank you, Karin. Good morning ladies and gentlemen. Welcome to our Q3 results conference call. First the highlights. Our revenues were flat at EUR5.3 billion. Organically, revenues were down 5%. Price discipline and cost control remain the key focus for us, leading to strong profitability. In France, despite double-digit sales decline, we achieved solid profitability. Growth in North America further accelerated year on year. UK held up well. Japan weakened further as last year's results included a few large projects. In Germany, we continue to outperform the market. Southern European markets remained weak. The gross margin was up 70 basis points, year on year, to 17.9%. Our price discipline and the business mix led to a strong organic 50 basis points increase in the gross margin in Q3.

Costs continue to be very well controlled. SG&A was down 2% year on year and sequentially, both on an organic basis and before restructuring costs. This resulted in EBITA before restructuring cost of EUR232 million and a margin of 4.4%, up 10 basis points compared to last year. In the first nine months of 2012 we have proven to be price disciplined and cost conscious and we have been able to protect profitability despite declining revenues.

Net income was at EUR118 million in Q3. The operating cash flow was EUR284 million in the first nine months of 2012 compared to EUR270 million in the same period last year. We exited the third quarter with revenues down 3% organically and adjusted for business days.

Let us have a look at the organic revenue development by region. In North America, including LHH, revenue growth slightly accelerated and was up 4% year on year. Both General and Professional Staffing contributed to the good growth trend. Within Professional Staffing, growth in the IT segment accelerated to 6% this quarter.

Revenues in Europe were down 8% in the third quarter. In France, revenues declined 16% year on year. I will discuss France in more detail in a bit.

Germany and Austria was down 1% but still ahead of the market. In Benelux, we also performed slightly better than the market. In Italy, revenues were down 14%, and in Iberia, revenues were down 12%. The positive trend in the Nordics continued as revenues were up 6%. While Sweden was slightly down year on year, all other Nordic countries increased double digit. In the UK and Ireland, revenues were up 9% in Q3, also driven by the Olympics were Adecco was the official supplier of temp employees.

Rest of world, including emerging markets, was down 4%. In Japan, revenues declined by 15%. In Australia and New Zealand, revenues were down 11%. The emerging markets grew a solid 9% mainly driven by Latin America.

We go to our main markets now. In France, revenues were down 16% year on year to EUR1.3 billion. Despite our strong focus on profitability, the gap to some of our main peers clearly narrowed during the third quarter. From an industry perspective, revenues in automotive, logistics and manufacturing were weakest. Our perm revenues were down 15% in Q3. We incurred EUR19 million restructuring cost in the quarter under review. These were related to our plans in France to combine the networks of Adecco and Adia under the single brand of Adecco. The EBITA margin before restructuring costs was 4.1%, an increase of 10 basis points year on year. This is a solid achievement thanks to a higher gross margin and strong cost control.

Revenues in September were down 13%, adjusted for trading days. We are pleased with the progress on the voluntary social plan. Until the end of October, over 350 employees have left the Company and we are fully on track to achieve the planned 500 plus FTE reduction by year end.

In hindsight, taking into account economic developments in France, it was absolutely the right decision to be proactive in addressing the cost base early.

In North America, revenues were up 3% organically to EUR977 million. Demand held up well in technology, logistics and consumer goods. Revenues in General Staffing increased 2% in constant currency and Professional Staffing revenues were up 5% organically. The North American IT Professional Staffing business grew 6% year on year with the US being up 8%. We are pleased with the progress there since we have now closed the gap to the market.

Revenues also continue to develop solidly in Finance & Legal with a growth of 6% and Medical & Science where revenues were up 20%. Engineering & Technical revenues were flat in Q3. Perm revenues continued to develop very well, up 15% organically. The EBITA margin increased by 20 basis points year on year to 4.3%. Excluding EUR2 million restructuring cost for the consolidation of data centers in North America, the adjusted EBITA margin increased 30 basis points year on year to 4.4%. Revenue growth slightly accelerated during the third quarter. In September, revenues were up 6% adjusted for trading days.

Revenues in the UK and Ireland increased 9% in constant currency, also driven by the Olympics. In the quarter under review, perm revenues were down 31% in constant currency but compared against a strong Q3 2011. The EBITA margin was 0.7% in the third quarter this year. Profitability in the UK and Ireland was impacted by the sponsoring cost of the London Summer Olympics.

In Germany and Austria, revenues declined 1% on an organic basis, again performing better than the market and compared against the strong base last year when revenues still grew 23% year on year.

Demand from automotives still held up well in Q3 but the outlook is becoming more challenging. The EBITA margin was 8.3% down 130 basis points compared to Q3 last year. The third quarter this year includes EUR1 million of restructuring costs. Excluding this cost, the Q3 EBITA margin was at 8.5%. In September, revenues were up 1% organically and adjusted for trading days. But first indications in October point to a weaker development.

In Japan, revenues were down 15% organically to EUR379 million. Last year's results included several large projects which no longer contribute this year. Despite the revenue decline, profitability in Japan continue to be strong because the EBITA margin was 6.1%, up 60 basis points compared to Q3 last year. VSN added 20 basis points to Japan's EBITA margin in the third quarter.

And finally we turn to Adecco's development by business line on a constant currency basis. In Q3, revenues in our General Staffing business were down 7%. Industrial business was down 9% and 10% organically in Q3. In Germany and Austria, revenues were down 2% organically year on year. In France, revenues declined 16% organically, and Italy was down 15%. Revenues in North America were up 1% year on year.

The Office business was down 2% this quarter. While revenues in North America held up well and grew 4%, revenues in Japan were down 17%. The UK and Ireland was up double digit, helped by the Olympics.

The revenues in Professional Staffing increased by 2% or 1% organically in Q3. UK and Ireland continued to do well with growth of 5%. Also revenue growth in North America further accelerated to 5% organically. France, on the other hand, was down 9%.

Our Solutions business increased by 26% or 8% organically. Revenues at Lee Hecht Harrison were up 9% organically. The integration of DBM progressed very well during the last 12 months and has been successfully completed. No further integration costs were incurred during Q3. Revenue growth in MSP and VMS also continued to develop very well with revenues up double digit.

And here I would like to hand over now to Dominik, who will discuss the financials in more detail with you.

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

Thank you, Patrick. Good morning, ladies and gentlemen. I will start with the overview of the P&L. In Q3 2012, we have revenues of EUR5.3 billion, down 5% in constant currency and organically. The gross margin was 17.9% in the third quarter this year, up 70 basis points. Organically, the gross margin increased 50 basis points year on year.

SG&A went up 2% in constant currency compared to prior year. Organically and before restructuring cost, SG&A was down 2% year on year. Sequentially, the cost base was also down 2% on an organic basis and when excluding restructuring cost. EBITA was EUR210 million. Excluding restructuring cost, EBITA was at EUR232 million and the margin was 4.4% in Q3 2012, up 10 basis points year on year compared to Q3 last year. Net income in the quarter under review was EUR118 million.

Let's have a look at the year-on-year gross margin evolution. The Group's gross margin was 17.9% in Q3 2012, up 70 basis points year on year. Temporary Staffing had a 30 basis points positive impact on the gross margin in Q3 2012.

Perm placement had a neutral impact on the Group's gross margin in Q3. Perm revenues were down 10% organically in the quarter under review. The Outplacement business had a positive impact of 10 basis points on the Group's gross margin, while other activities also had a positive impact of 10 basis points in Q3. The net impact of acquisitions and divestments added 20 basis points to the gross margin this quarter. We continued to be disciplined in our approach towards pricing, and this is shown in our results.

Now let me discuss our cost base development in the third quarter this year. We continued to look closely at revenue development and manage the cost base very tight. SG&A in Q3 for the Group was down by 2% compared to the same quarter last year on organic basis and before restructuring costs. Sequentially, our cost base was also down 2% organically and before restructuring cost. On an organic basis, FTEs were down 3% year on year. The brand (inaudible) was decreased by 2% organically compared to the prior year. Our Q3 2012 results included EUR22 million restructuring cost, of which EUR19 million related to France and EUR1 million related to Germany, in North America with restructuring cost of EUR2 million for the data centre consolidation in North America.

SG&A for the Group in the fourth quarter this year is expected to remain approx at the same level as in Q3 2012 on an organic basis and before restructuring cost. Given current trends, we need to continue to align the cost base to revenue developments. We therefore anticipate to invest additional EUR15 million to further accelerate the optimization of the cost base.

Please have a look at slide 17 for an overview of actual and anticipated restructuring cost for 2012. September year to date, we have invested a total of EUR37 million in order to further optimize the business, of which EUR27 million related to France, EUR8 million for other countries and EUR2 million for the data centre consolidation in North and South America. We had initially anticipated to invest a total of EUR65 million during 2012 of which EUR45 million was planned for France, EUR10 million for other countries and EUR10 million in total for the data centre consolidation. Given recent revenue developments, as said, we anticipate to invest additional EUR15 million to further optimize the cost base, which leads to a total of approx EUR80 million in 2012. Therefore, we anticipate an approx investment of around EUR43 million in Q4 2012.

Moving on to the balance sheet. We July, we issued Swiss franc bond to finance the previously announced up to EUR400 million share buyback program. The share buyback started in mid of July and to date we have acquired 2 million shares for a total consideration of EUR76 million. Our cash in short-term investments were EUR980 million at the end of Q3 2012, DSO was at 55 days in the third quarter this year compared to 56 days in Q3 2011. Goodwill and intangible assets amounted to EUR4.2 billion at the end of September 2012. At the end of the third quarter, Adecco's shareholders' equity was at EUR3.9 billion.

Turning to the cash flow statement. The operating cash flow generated in the first nine months of 2012 amounted to EUR284 million. This compares to an operating cash flow of EUR217 million in the same period last year. Cash used in investing activities was impacted by the purchase price consideration for the acquisition of VSN in Japan at the beginning of this year. The Group invested EUR87 million net of cash acquired for VSN. CapEx was EUR71 million in the first nine months of 2012.

Cash flow from financing activities was EUR268 million. It included payments of dividends of EUR256 million, net inflows of EUR579 million related to the net increase in short- and long-term debt, and EUR57 million related to the purchase of own shares.

Net debt at the end of September 2012 was EUR1.1 billion compared to EUR892 million at the year-end 2011. In the first nine months of 2012, we paid dividends of EUR256 million and bought back shares net of disposals for EUR57 million.

As per the end of September 2012, we had short- and long-term debt of EUR2 billion and cash and short-term investments of EUR908 million. This resulted in a EUR1.1 billion net debt at the end of September 2012. As mentioned earlier, in June we launched a share buyback program of up to EUR400 million with the aim of subsequently canceling the shares. The CHF250 million five-year bond and the CHF125 million eight-year bond were issued in July 2012 and are reflected in the quarter under review. Our balance sheet remains very healthy.

Our financial guidance for the full-year 2012 is as follows. CapEx for the year 2012 is expected to be around EUR100 million. Interest expenses, excluding interest income, are expected to be around EUR80 million for 2012. Our corporate cost for 2012 are expected to be approx EUR100 million. And amortization of intangible assets is expected at EUR50 million for 2012. The underlying tax rate for Q4 2012 is expected to be around 35%.

With this, I hand back to Patrick.

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

Thank you, Dominik. Now, let me finish with the outlook for our business. Revenue developments continue to be very diverse across the different geographies. We exited the third quarter with an organic revenue decline of 3% in September, adjusted for business days. Revenue growth at the beginning of the fourth quarter slightly weakened from the minus 5% organically that we saw in the third quarter.

This was mainly driven by the UK, Germany and the emerging markets. In France and Japan, the revenue decline rates stabilized. In North America, revenue growths continued to develop well, driven by both General and Professional Staffing.

In the current environment, prize discipline and a proactive approach to cost management remain key. The gross margin improvement and the solid EBITA margin in Q3 2012 reflect our focus on profitability and value creation.

As Dominik said, SG&A for the Group in Q4 is expected to remain approximately at the same level as in the third quarter on an organic basis and before restructuring costs.

We continue to focus our efforts on improving our HR solutions, delivery models and the cost base. And we are convinced that we will achieve an EBITA margin of over 5.5% midterm.

And with this, I would like open the floor for your questions.

QUESTIONS AND ANSWERS

Operator

We will now begin the question-and-answer session. (Operator Instructions)

Toby Reeks, Bank of America Merrill Lynch.

Toby Reeks - *Bank of America Merrill Lynch - Analyst*

Can I ask a couple? The first is on SG&A. Can you talk a little bit about how much seasonality there was in Q3's cost base sequentially and what we should expect just from seasonality into Q4? And also has there been an impact from holiday accruals and will there be one in Q4?

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

The seasonal impact in Q3 is always a little bit less than 1% lower cost base on Q2 and Q3, which goes then back into Q4. It's a little bit less than 1%.

Toby Reeks - *Bank of America Merrill Lynch - Analyst*

Thank you. Okay, cool. And then just the final question I guess is on, in Germany. Could you give us an update on how you're getting on with negotiating with clients?

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

If we look to Germany overall, I mean, there are two components to consider. First of all, we have an increase in the collective wage agreement of 3.8% in Western Germany and 7% in Eastern Germany. This is the normal wage inflation and which we will, yes, pass on to our clients like we always do to a big majority.

That said, for 40% of our business this is not even relevant because roughly 40% of our German business is today already on equal pay as clients decided to go in this direction.

Then when we talk about the new surpluses, so which will kick in for the metal industry, for the electronic industry, they will kick in as of November 1st. And we are on a good way to, yes, to pass this on to the clients. Does it mean we can pass this on with the same gross margin? That's not the case. So the gross margin will be slightly negatively impacted from this equal pay. But we are positive when it comes to the absolute gross profit level, absolutely euro.

Toby Reeks - *Bank of America Merrill Lynch - Analyst*

Can you give us an idea of what sort of an impact on the gross margin you're expecting in Q4 '12 and into next year?

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

It will be not -- it will be really not significant, because you have to consider the following. If you look to our, how long the temp staying by our clients, it's very interesting to see by the clients who use temping, let's say to bigger extent the temps staying of course longer, they are mostly likely already in equal pay, so they are not impacted.

Whereas the population where we have to make this surpluses, they're on average, I would say, less than four months by a client. So you have then temps on average less than four months by a client and the surpluses kick in after six weeks, for example, for the (inaudible) of 15%. So I'm -- from this point of view, I'm not expecting a significant change. But the gross margin will drop a little bit.

Toby Reeks - *Bank of America Merrill Lynch - Analyst*

Okay. Thanks so much, guys

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

Next question, please?

Operator

Tom Sykes, Deutsche Bank.

Tom Sykes - *Deutsche Bank - Analyst*

Just on your comments of stability in France. And I think you mentioned some stability, potentially, in Italy and Spain. What are you seeing in more export-exposed clients and their order books? And what are you seeing in the more domestically exposed clients?

And then on -- please, on LHH, where is the growth coming from in LHH? And is it disproportionately US, maybe from HP, or are you seeing some growth out of Europe in LHH, and what's the sustainability of that, please?

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

Okay, Tom, I will take your first question on the decline rates in France and Southern Europe. We've seen Italy and Spain moving 1 percentage point slower compared to Q1 to relatively minus 12%, minus 14% now or respectively minus 12% and minus 14%. And in France, what we're seeing now, the minus 16%, we stay around this rate. And we see also recently that the market is coming closer, so that we are narrowing the gap to a number of main peers.

So in France it's across all businesses, I would say, this decline, so it's really equally spread. What we see is that sequentially construction is more or less at the same level. But if we look at the manufacturing, if you look at consumer goods, if you look at technology, logistics, the drop is equally spread along our industries.

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

Coming to the -- to your question regarding Lee Hecht Harrison, so Q3 is normally a seasonally weak quarter. And this year it was quite strong with this plus 9% growth. And this is related to the fact that we had two bigger projects where normally because of occasion and other things they would rather come in an October-November, and they were basically done in August-September. And this is one reason why we had a strong acceleration of the whole Lee Hecht Harrison business with organic growth rate of 9%.

And then looking to the geographic development and taking this into account, we see that the growth in North America is decelerating. It was double digit in Q2, it's now single digit in Q3. And this is close to 50% of our Outplacement business.

Whereas, we see a strong growth, let's say, Europe, excluding France, I would say. Because in France, even though that there is a new government, basically clients are still hesitating to make this step, there's a lot of pressure not to make restructuring. But outside France, strong growth, Asia is growing strongly, Brazil is growing strongly.

But I would say, overall, to the growth of 9%, a couple of big projects, they're moved more to Q3, into Q4, so the number of plus 9% is little bit, I would say, inflated in this respect if you look going forward.

Tom Sykes - *Deutsche Bank - Analyst*

Okay, thank you. And just in terms of France, have you annualized out now, sorry, I can't remember, the exit of the large autos contract that you have? And if you have, do you think you can get to a point where you can outperform the market in the next, let's say, three to six months?

And what's your view now on peak profitability in France given the highly creditable performance of slightly up margins when your organic growth was minus 16%?

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

Indeed, Tom, if you look at the automotive sector in France, we were still quite affected by this in the third quarter. It was now down 37%, it was down 27% in the second quarter. So it further decelerated. It's less than 10% of our business, fair to say, but still it's quite a decline.

And that's why I also think that you have seen some difference in gaps because we were first affected and more exposed to the automotive sector and certainly to one player in France than other players. That's why you're seeing the gap coming a bit closer.

But that we now going to overcome this in a couple of quarters and do better than the market, I don't see because our focus clearly stays on this profitability. And you see now our profitability being, relatively speaking, 60% higher than other players. I think we should continue to do this and show that it's also possible in France to make this money. So this is going to be our primary focus, not the market share gains. Dominik?

Tom Sykes - *Deutsche Bank - Analyst*

Okay. And in terms of peak profitability could go to in France. I mean, what sort of levels, I mean, I know you've always spoken about it being lower than the medium-term target of 5.5%, but do you feel like, be it the success of the restructuring means that your internal budgets may be shifting a little a bit higher in terms of France now?

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

I mean, what is definitely the case that when we worked on the plan and decided on the plan, we have [understood] the ambition that the gap to the Group target is narrowing somewhat. This is definitely the case, and we are on a good way in terms of this execution.

So do I believe it comes to 5.5%? I don't think so. Because I think this market is far too competitive to have a 5.5% margin. But it's definitely upside there. But we need one [stage closer], this is definitely also the case, yes.

For Q3, you have also to consider profitability in Q3 is very strong. We see the cost savings already, we have a very good gross margin, but we have also releases of vacation because people are on vacation, so this is just Q3 is tend, from a seasonal point of view, also a good profitability, but we are very pleased. And if then the re-restructuring where we are currently going through kicks in and then once the sales coming back, yes, definitely a lot of potential of leverage. And as you know, one reason of this restructuring is also to work on segmentation, the strength the small and medium-sized clients where higher gross margins are possible. There will be a gap, but the gap will be not significant to the Group in the mid-term.

Tom Sykes - *Deutsche Bank - Analyst*

Okay, great. Thanks very much. Thank you.

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

Thank you, Tom. Next question, please?

Operator

Andy Grobler, Credit Suisse.

Andy Grobler - *Credit Suisse - Analyst*

You noted in the management outlook that the emerging markets had slowed some into October. Which parts of the -- of your emerging market business are -- have weakened?

And then the second question, just on your additional restructuring cost, the extra EUR15 million, which areas is that going to be focused upon?

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

Okay, Andy, the EUR15 million will be mainly France, Germany, and then the remaining smaller parts for some other countries, also southern Europe. And then on the emerging markets, it's clearly Eastern Europe that is now also affected by what is going on in Western Europe. And growth is still solid in Latin America. It's okay in Asia, but it's clearly Eastern Europe that is now also affected by Western Europe, like I said.

Anything you want to add?

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

I think in Northern -- like everything, Latin America is still doing very well, but growth rate comes a little bit down because last year we had a very strong ramp up into Q4. And so, sequentially, there is still good improvement in Latin America but the speed is not anymore that strong like than last year, so the growth rate is still only little bit in North -- in Latin America.

Andy Grobler - *Credit Suisse - Analyst*

Okay, thanks. And -- just one further one on Germany. You mentioned the impact of subsidies and so forth, what are your clients saying back to you about volumes as the cost of temping relatively goes up? Are any of them looking to reduce volumes?

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

I mean, there is -- these are the surpluses, they are not -- it's not subsidies, it's surpluses.

Andy Grobler - *Credit Suisse - Analyst*

Surplus, sorry.

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

Which we have to give our temps. So we have -- let's say if we now see that our volume goes little bit further down, I think this is just from an economic point of view. We're not thinking this has to do with the new surpluses because we have to consider first of all we have no client who said I stop now temping because of this one.

Secondly, a big part of the clients is already in equal play, it's plus 40% of the business. And they really increased temporary workforce because why they have done it, they have not done it because they want to have equal pay, they have done it because this was the way to convince the workers' council to support a higher penetration of temping. And this was the growth driver of the last couple of years of the German market.

And then we should still consider even though that we have now the surpluses, this is not yet equal pay on the cross (inaudible) like we had it in other European countries, yes. And I think a lot of clients will maybe also look how long is a temp with them and maybe change temps from time to time to optimize this. But we have not the feedback that now our client is saying, hey, because of this this is not anymore interest to use temps.

And, finally, look to penetration rates. Even if Germany has now a little bit higher penetration rate than other European countries, we have to see to the German economy as a whole. The German economy is much more volatile, much more cyclical than other economies given the export exposure, given the exposure to machinery industry, to automotive. You have seen this in the downturn '09 how strong Germany suffered, but on the other hand how strong they recovered in '10 and '11 from a GDP point of view. And there is definitely a higher need for flexibility than in other European countries. So we not have the impression that this will limit our possibilities to increase penetration rates in Germany mid-term.

Andy Grobler - *Credit Suisse - Analyst*

Okay. Thank you very much.

Karin Selfors - *Adecco S.A. - Head of IR*

Thank you.

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

Thank you, Andy. Next question, please?

Operator

Alain Oberhuber, MainFirst Bank.

Alain Oberhuber - *MainFirst Bank - Analyst*

A question on North America about the gross margin mix. Clearly we see now better growth in the Professional Staffing which is mainly the reason why we see better gross margins in North America. Do you think that the strength of positive gross margin development will continue in Q4 at more or less the same magnitude, and if that also be the case in Q1 or at the beginning of next year?

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

If we -- if I maybe answer this question regarding gross margin. The gross margin trend is positive, and we see no reason that it should not continue. However, the gross margin trend was much stronger in the first half this year compared to Q3, so the positive trend decelerated somewhat. This has to do with the fact that we had experienced in Q3, and this will be most likely also the case in Q4, more, let's say, health care claims, a couple of health care claims with higher amounts, and this we have to consider.

But the underlying mix, the underlying pricing is going in the right direction, but that because of more health care claims, medical claims we have a little bit impact on the gross margin. The gross margin increase is less strong than before.

Alain Oberhuber - *MainFirst Bank - Analyst*

In Q4 as well as next year?

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

No, I mean we will -- we can look for the first six months, and then we have to reassess this. But, in general, the thing is going in the right direction.

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

It's the case, Alain, that we are insuring ourselves and that have had in Q3 and Q4 a couple of exceptional cases and expensive cases and, of course, victims. And, of course, this is affecting the gross margin. But these are the things, okay, you insure yourselves, you cannot predict, and these things happen, and we take them then in the course when they happen.

Alain Oberhuber - *MainFirst Bank - Analyst*

Okay, thank you very much.

Karin Selfors - *Adecco S.A. - Head of IR*

Okay, next question, please?

Operator

Michael Foeth, Bank Vontobel.

Michael Foeth - *Bank Vontobel - Analyst*

Just one question from my side. On the UK, what kind of impact on revenue trends and profit should we now expect post the Olympics effect, or are there still any contributions from that after the Olympics? And also what was the exit rate in the UK in September, and the trend in October?

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

We said that on the exit rate, to come first to that point, that October went a little bit slower than the minus 5% in the third quarter driven by the emerging markets, driven by the UK and Germany. So you can imagine that it's a bit slower there.

Now, the growth of 9%, if we wouldn't have had the Olympics, would have been 3%. So the impact of the Olympics is 6%. And the profitability without the Olympics would have been clearly above 2% in the third quarter, and we're aiming at a profitability like we have had in the quarters before the Olympics.

Michael Foeth - *Bank Vontobel - Analyst*

Excellent, thank you.

Karin Selfors - *Adecco S.A. - Head of IR*

Okay, next?

Operator

Jaime Brandwood, UBS.

Jaime Brandwood - *UBS - Analyst*

Just to come back to France, could you actually tell us what the benefit from the restructuring savings was in the Q3. So I understand you're targeting EUR45 million of savings or roughly EUR11 million to EUR12 million per quarter. How much benefit was there already in Q3?

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

Around EUR5 million.

Jaime Brandwood - *UBS - Analyst*

Around EUR5 million. Thanks.

And then just turning to the temp gross margin, apologies if I missed this during the actual earlier prepared remarks, but the 30 basis point temp gross margin increase, can you be a bit more granular as to which countries saw the biggest increase and which countries saw the biggest decline and, I guess, how much of the 30 basis points was just mix?

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

I mean, it's definitely a mix impact in this respect because the Professional Staffing is, of course, doing better than the channel staffing business, and this helps, of course. Above the 30 basis points, we have definitely France because France, if you have 16% sales decline and even if you have -- make a good job on the cost side to have a 10 basis points margin increase, you need a good gross margin. So France is definitely one of them, one of the key drivers in this respect.

Also if you look to Japan where we have 15% decline and increased our profitability, this is also only possible if you increase margins of Japan, it's also an important driver in this respect. And then, overall, we see a positive trend in the emerging markets. It's more from the mix point of view. Latin America is outgrowing. In Latin America, we have strong temp margins. And then there is also a small impact which is, in my view, for the whole year the same, but it's just how the quarters develop.

If you look to the results, you see Switzerland has in Q3 a very strong EBIT margin. Normally our EBIT margins in a single quarter are below, let's say, between 9% and 10%, and this time it's clearly higher. If you look historically, often we had in Q4 higher one. This time it's already in Q3. This is just the timing. It had to do with the methodology how we basically see some insurance benefits. And this is of us change this methodologies has also the impact in Q3.

Jaime Brandwood - *UBS - Analyst*

So this means Switzerland is going to be weak in Q4, I guess, or weaker.

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

It will be -- let's say, it will be not weak, but it will -- what you normally see this clearly double digit margin have now in Q3 and you have then -- you have in Q4 a normalized margin, I would say, yes.

Jaime Brandwood - *UBS - Analyst*

And other than Germany where you've already spoken about a possibly slightly weakening percentage gross margin trend, what were main countries to see temp gross margin pressure? I mean, I understand that UK gross margin is probably down because perm is down 30%, but the actual temp gross margin in countries which saw pressure.

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

I mean, this is nevertheless the UK because you have to see that this Olympic business, of course, has not very good gross margin, yes. So this also brought the UK temp margin, I would say, clearly down. Then the negative trends you see also in Germany. Why? Because our automotive business even though that it, may slows now was still growing 9%, and if we have 1% sales decline but 30% of your business is growing 9%, and this automotive business because its equal pay already it's a very large account, you have lower margins that has impact on the mix. These are the markets where temp margins, let's say, a little bit under pressure.

Jaime Brandwood - *UBS - Analyst*

Okay. And then just very lastly, this might be too early to ask this question. But for this year, I can't remember, was that the beginning of this year or at the end of last year you had a scenario analysis where you were basically saying, look, as long as our revenue organically is not down more than 5% we should be able to maintain margins. And it looks like you are now going to deliver on that.

I'm just wondering, have you started to think about the scenario analysis for FY '13 and what kind of tolerance level you have on revenue decline in terms of being able to maintain or even improve margins in FY '13?

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

Jaime, I think in -- like you said, we have proven in the first nine months that we are delivering on that promise that if revenues go down that we protect profitability and we will continue to do so if it would be the case.

In the current economical environment, you have to go into the year with different scenarios. If it would grow again, we're going to have a very good leverage with this cost base. If it doesn't grow, we will protect profitability.

Jaime Brandwood - *UBS - Analyst*

Okay. Thanks very much.

Karin Selfors - *Adecco S.A. - Head of IR*

Next question?

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

Next question?

Operator

Matthijs Van Leijenhorst, Kepler Capital Markets.

Matthijs Van Leijenhorst - *Kepler Capital Markets - Analyst*

Sorry to bother you but it's a follow up on Germany again. I'm a little bit surprised because it appears that you're not that worried about Germany. But one of your competitors last week mentioned that in worst-case scenarios, he expected a drop of 20% in the top line, and he was also saying that it could be that jobs being moved to low-wage countries such as Eastern Europe. And another company mentioned that companies were putting temps on permanent contracts by the companies that hired them. So I'm a little bit worried about Germany. Could you please elaborate on that one?

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

I mean, first of all, it's true that one or the other automotive company takes some temps to perm, that's definitely the case and this is also not new, yes. But I mean, this is very normal, this is part of our job to provide temps, temporary job and finally they are taken over to perm. So this is a very normal development.

And it's the case that in Germany some of this car makers, they really have high flexibility and they have a couple of temps who are very long with them and they want to honor that they are so long with them and then give them a perm contract, some partly also driven by workers' council who want to vote for this. That's definitely the case. But this is, I think, normal development. And I think -- I'm not commenting what many competitors say about Germany, I just believe people should be careful to differentiate between economic development and structural development.

Matthijs Van Leijenhorst - *Kepler Capital Markets - Analyst*

Is it fair to say that companies in Germany are more willing to pay for low-wage employees than for flexibility?

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

I don't think so because if you look to Germany today, we haven't had equal pay. Of course, it is then -- it's in a process that people have to learn and have to get understand that we have now soon something like equal pay. To be honest, it's not really equal pay, it's still cheaper. Even with the collective wage agreement it's still cheaper than equal pay, yes.

So -- and we have so far no clients indicating to us to say, hey, now I'm moving away from temping. And we think that it goes to Romania or other Eastern European countries, how should this work? You want to outsource 2% of your temps to Romania, I think this doesn't work. Then you have to close the whole factory.

So I think this is -- this argument I really don't understand. The temping becomes somewhat more expensive, yes. But again, a lot of the countries use already equal pay agreements. And there is still a lot of flexibility. In the first six weeks, you pay no surplus. Afterwards you pay 15%. So is this more expensive? Yes, it is more expensive, yes. But this is how it works, but it's still cheaper than having six temps each. And I think our clients are smart enough to remember 2009 when they had not enough temps. What they said, we want to have more temps because we need more temps to manage cyclicality in this country.

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

And maybe this is different from one company to another but because of our exposure to the automotive, we said that also in the previous quarter, we already have close to 50% of our temps, including the Professional Staffing and the automotive we already have close of 50% of our temps on equal pay. So the maximum [effects] we could have is on the other 50%. And there you have to make then a distinction how long are they staying in the company, how long are they there, at what salary level are they already. So there is going to be an impact like Dominik already explained, especially on the percentage. But in absolute terms we don't see that impact as being very substantial.

Matthijs Van Leijenhorst - *Kepler Capital Markets - Analyst*

Okay. Just one more question. Is it possible to get the exit rates for the Benelux?

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

We don't give exit rates for the Benelux, but let's say we are staying at similar levels as we were in the third quarter.

Matthijs Van Leijenhorst - *Kepler Capital Markets - Analyst*

Okay. Many thanks.

Karin Selfors - *Adecco S.A. - Head of IR*

Okay, next question, please?

Operator

Konrad Zomer, Berenberg Bank.

Konrad Zomer - *Berenberg Bank - Analyst*

A question on your US operations. You added something like 200 people to your Professionals business in the second half of last year. Can you update us on how productive these people have become in the meantime? And what are your headcount plans for particularly your US operations in Q4, please?

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

I mean, the -- if we look to the -- our US business, there we have had in the US business now 8% growth. We hired of course more people, so the productivity increased, but they are not fully yet productive which was also not expected. You have also to see that a lot of the hiring were related to perm, and our IT business is doing very well in perm, so it's not only temp business.

So from this point of view there is currently only selective need of hiring for IT people, but we still see a good trend in our IT business. So we are optimistic that this good trend is continuing in the IT business where we had to -- where we added a little bit of headcount but in General Staffing because in General Staffing in the last two-and-a-half years during this uptick we hardly added headcount, so we really leveraged the business. And there was here and there a need to add some headcount in the US because the outlook there is still pretty good. We have very strong demand in the logistics sector, in consumer goods. And there we added some headcount for the US.

Konrad Zomer - *Berenberg Bank - Analyst*

Right. And then one more, please, on the Group level, can you tell us what your natural attrition rate is at the moment? And how that is developing? Do you think that will go down, or has it come down?

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

It's more or less stable, around 15%.

Konrad Zomer - *Berenberg Bank - Analyst*

Thank you.

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

This is the voluntary, I must say the voluntary leavers, of course. This is excluded of the people that we are laying off in France and in some other parts to adapt our cost base to the revenue development. So the 15% is the natural attrition.

Next question, please?

Operator

Paul Sullivan, Barclays Capital.

Paul Sullivan - *Barclays Capital - Analyst*

Just a couple from me. First of all, do you see scope for gross margin improvement going into the fourth quarter?

And then secondly, Professional trends in Germany into October, perhaps some more color there. Thanks.

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

I mean, I think that the gross margin will be very similar from the Q3 level into Q4. And there are a couple of items which you have to consider when it comes to Q4.

First of all, in France you have always the highest temp margin in Q4. That's now since one year ago the case since we have the new way of calculating the social tax rebates whereas last year, in Q4, it was extremely strong which had to do with the calendar days because the last working day in November was the mid of the week. Now it's at the end of the week. This has some impact on social tax rebate. So this year it will be less than last year. This we have to consider.

We had also in Q4 last year very strong workers' comp in North America, and we have to see whether this is -- again so strong achievable or not, but it was very strong. So the base there was a little bit high. And what I said before on the question of timing with the move in Switzerland, which the positive impact now in Q3 and last year it was in Q4, this we have to consider.

On the other hand, yes, the business mix is still improving, Professional Staffing is doing relatively good and the Outplacement business is outperforming. So we believe similar gross margin is achievable.

Paul Sullivan - *Barclays Capital - Analyst*

Great. And Professional trends in Germany into October?

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

I mean, if we look to Professional, like our Professional brand DIS has had a growth of 5% after 7% the quarter before, and this is pretty similar into October.

Paul Sullivan - *Barclays Capital - Analyst*

Excellent, thank you very much.

Karin Selfors - *Adecco S.A. - Head of IR*

Okay, next question, please?

Operator

Teun Teeuwisse, ABN AMRO.

Teun Teeuwisse - *ABN AMRO - Analyst*

Few questions from me. First of all, on your overall Group gross margin, can you indicate what the impact of the fewer working days this year was?

Second question is on the profitability in Lee Hecht Harrison business. I saw that Q3 was a bit weaker than Q2 and Q1. Will you come back to the Q2 and Q1 profitability again in Q4? And why was it lower? Because I think I understood in Paris that profitability should remain relatively stable throughout the year. Thanks.

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

I mean, the -- if you look to the working day impact, there are a couple of less working days overall, but it's really not significant with the exception of the second quarter. And we outlined this in the second quarter that Germany, Sweden, where we have the people on the book, it had a negative impact on the gross margin around, yes, 10, 15 basis points. But for the whole Group overall, I think with the exception of this Q2 effect it will be not that significant.

If you look to Lee Hecht Harrison, you have to see Q3 is normally seasonally always a weak quarter, yes, because it's vacation time in France, it's always in the US less activity. So that margin this year in Q3 was actually very strong with more than 23%. Normally it should have been slightly below 20% because Q3 is the quarter with the low margin.

Now, this year it was actually strong because, I think Tom asked the question regarding Lee Hecht Harrison, because we had projects which normally would from a seasonal pattern come in October-November, they were executed in August-September. So it was actually a strong quarter.

Teun Teeuwisse - *ABN AMRO - Analyst*

Okay, so we can expect that Q4 will still come back towards Q1, Q2 levels?

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

Yes, yes, we have to see. I mean, the margin will be very high and we will beat our competitors strongly, like always, with Lee Hecht Harrison, yes. Now, of course, we have also to consider Q1, Q2. As I said before, North America starts to slower little bit, there is growth but it slows a little bit down. And as 50% of the business is in North America it has also some impact, but we are -- we will state again a very strong profitability also in Q4 on Lee Hecht Harrison.

Teun Teeuwisse - *ABN AMRO - Analyst*

All right. And then I have one final question on your German gross margin. Are you able to enter discussions with clients where you share the price increase and you get a bigger piece of the pie, so you can still protect your revenues better?

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

You mean in the background of the new equal pay agreements or --?

Teun Teeuwisse - *ABN AMRO - Analyst*

Yes, exactly, so you make an agreement with your client that you share the pay increase and in exchange you get more revenues from that client.

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

I mean the increase of the surplus, yes, we have to pass on. Why should we subsidize this? Yes, we can discuss then whether there should be a gross margin on it or not, yes, but we are not willing to give up by increasing the surplus because the surplus is a cost for us and we should just increase it, there should be no discussion. So -- and we have no intention to become there aggressive, yes.

Teun Teeuwisse - *ABN AMRO - Analyst*

Okay, thanks a lot.

Karin Selfors - *Adecco S.A. - Head of IR*

Okay, let's take one final question.

Operator

Olivier Lebrun, Natixis.

Olivier Lebrun - *Natixis - Analyst*

Question is about Australia. Is the decline of business coming from the mining industry slowdown? And what is your exposure to this sector?

Second question is regarding Japan. Could you give us an update of the new legislation on staffing and which impact do you anticipate on the business? Thank you.

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

On Australia, it's indeed the mining business that has suffered most. As -- so we see this decline, it's about 20% of our business, and most of the decline came there, and we see it is more or less in line with what's happening in the market. We don't see it further declining, by the way.

Olivier Lebrun - *Natixis - Analyst*

Okay. And in Japan?

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

On Japan, on this new law that passed already, now, it was on the table for October with a clear definition on the 26 categories and the minimum length of temps that we -- that have to stay at the customers, the minimum length that the temps have to stay at the customers. These are the main changes. We don't see really an impact for our business if we have looked at our portfolio of temps and our portfolio of customers. We don't see a material impact on our business of this at all.

Olivier Lebrun - *Natixis - Analyst*

Okay, thank you.

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

Okay. Okay, so ladies and gentlemen, thank you for attending this call and for your interest in our Company. If not sooner, we will talk certainly again on the 13th of March when we announce our Q4 and full-year results. I would like to wish you all a very good end of the year and a very good new start into the -- in the year although it's still very early. Thank you very much.

Karin Selfors - *Adecco S.A. - Head of IR*

Thank you.

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

Thank you.

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.
