Recruit Holdings Q2 FY2021 Earnings Call November 15, 2021

Shen: Welcome to the Recruit Holdings Q2 FY2021 earnings conference call. I'm Mizuho Shen, from Investor Relations, and joining me today are Junichi Arai, Executive Officer of Corporate Planning Division and Yasushi Hashimoto, Executive Manager, Disclosure and Individual Investor Relations Department.

Jun will briefly go through the Q2 FY2021 results we announced at 3pm today, then proceed to the Q&A session.

We recommend that you refer to the Highlights on page 5 of the earnings release and the FAQ posted on our IR website.

This call is a simultaneous translation of the original call in Japanese and translation is provided for the convenience of investors only.

Also, please note that all comparisons during this conference call are year over year unless otherwise stated.

Now I'll turn over the call to Jun.

Arai: Thank you for your participation today.

I am Junichi Arai, Executive Officer of the Corporate Planning Division of Recruit Holdings.

During Q2 FY2021, a continuation of elevated hiring activity led to continued competition for talent particularly in the US and Europe where vaccine rollouts progressed and the economic activity continued to improve.

In Japan, despite the progress of vaccine rollouts, the negative impact on economic activities remained as the state of emergency and priority preventative measures remained in place until the end of September.

As a result, the economic recovery was gradual in Japan.

Under this business environment, revenue and adjusted EBITDA in HR Technology increased significantly.

As we have mentioned before, the hiring activities of business clients and job search behaviors are greatly affected by changes in the economic environment, and as a result, our HR Matching businesses are largely dependent on trends in the global economy and corporate activities.

Although COVID-19 related restrictions have variously been relaxed in many countries, our business environment is anticipated to continue to evolve rapidly as restrictions could be reintroduced due to the emergence of variants.

We do not believe that the current unique labor market conditions impacting our HR matching businesses will continue for an extended period and it is unclear how the future rebalancing of the current unique labor market will impact our HR matching business environment.

It continues to be difficult to clearly predict the business environment in the second half of this fiscal year and beyond.

Having said that, based on the results for the first half of this fiscal year, FY2021, and information available as of today, we announced the outlook for our three SBUs for the second half of FY2021, and revised upward our consolidated financial guidance for FY2021 from the guidance announced on August 12, 2021.

We will not be swayed by ups and downs in the business environment and will steadily implement our most important management strategy,“Simplify Hiring”, and operate our business without losing sight of our long-term objectives.

First of all, I will explain the Consolidated Results of Operations for Q2 of FY2021.

Consolidated revenue increased 23.2% primarily led by significant revenue growth in HR Technology, which exceeded 200.0 billion yen for the first time as significant hiring demand combined with limited supply of job seekers looking for work continued to increase competition which positively drove our results.

Adjusted EBITDA margin was 20.1%, an increase from 12.3% of Q2 of FY2020 primarily due to the performance of HR Technology. Adjusted EBITDA increased by 101.0%.

Adjusted EPS was 56.95 yen, an increase of 133.9%.

Interim dividend is 10.5 yen per share, and year-end dividend forecast is unchanged at 10.5 yen per share, making the full year dividend per share to be 21.0 yen.

Next, I will explain the financial guidance, which we have revised upwards.

Our long-term outlook remains cautious and the FY2021 guidance is based on the assumption that stagnation of economic activities caused by new large scale lockdowns and states of emergency will not occur during FY2021.

We revised the assumption for the US dollar exchange rate in the guidance for the second half of FY2021 from 108 yen to 111 yen per US dollar, while we did not update the exchange rate assumptions for the Euro or Australian dollar.

Our revised consolidated revenue guidance for FY2021 is a range of 2.7 to 2.8 trillion yen, which was previously a range of 2.6 trillion to 2.7 trillion yen.

For consolidated adjusted EBITDA, revised guidance for FY2021 is a range of 440 billion to 470 billion yen, which was previously a range of 360 billion to 430 billion yen.

For consolidated adjusted EPS, revised guidance for FY2021 is a range of 172 yen to 184 yen, which was previously a range of 136.32 yen to 166.92 yen.

The revised guidance by segment will be explained later, along with the Q2 results.

Next, I will talk about the results of operations and financial guidance by segment.

First of all, I will talk about HR Technology.

Revenue continued to exceed our prior expectations, increasing 100.1% on a US dollar basis to $1.94 billion, as a continuation of elevated hiring activity globally led to increased demand for sponsored job advertising from new and existing customers.

The relatively limited supply of job seekers looking for work combined with significant hiring demand continued to increase competition for talent on Indeed and Glassdoor.

Due to our auction based pricing model, this competition was a significant driver of revenue growth in Q2.

On a US dollar basis, revenue in the US increased 95.9%, supported by both small and medium sized businesses and large enterprises. Revenue outside of the US increased 114.2%, primarily led by Europe and Canada.

In contrast, in Japan, revenue growth has been slower due to the lack of layoffs at the outset of the pandemic and the repeated states of emergency, both of which have continued to dampen overall hiring demand.

Adjusted EBITDA was 86.4 billion yen, an increase of 485.7%, which was the highest adjusted EBITDA ever recorded, driven by the significant increase in revenue.

HR Technology increased investments in sales & marketing year over year which had been impacted by cost control measures in the second quarter FY2020, while increasing investments for growth focused on product and technology initiatives to simplify hiring and significantly reduce the cost and time to hire for employers.

However, revenue growth continued to outpace investments, resulting in adjusted EBITDA margin of 40.3% for the second quarter of FY2021.

The competition for talent remained elevated in Q2, resulting in a significant increase in revenue and adjusted EBITDA year over year, which exceeded the Company's prior expectations for the first half of FY2021.

Our US dollar based revenue for the first half of FY2021 increased 118.5% and adjusted EBITDA margin was 39.1%, driven by a significant increase in revenue while costs increased to a lesser extent.

As we explained in our updated guidance last quarter, we had previously expected the competition for talent on our platforms to ease at some point during the second half of FY2021.

At this time, it remains uncertain if there will be any particular catalysts that will result in job seeker interest and activity increasing to a level matching the increase in the number of available jobs.

However, we do expect the imbalance in the labor market to lessen more gradually over the second half of the fiscal year and beyond, as these factors become less impactful, which in turn may put downward pressure on revenue growth as finding qualified hires for available jobs becomes less challenging.

Therefore, our US dollar based revenue guidance for the second half of FY2021 is an increase of approximately 60% to 70% year over year, and as a result, revenue for the full year is expected to increase upper half of 80%.

In HR Technology, we began to significantly increase our investments to grow headcount in Q2 and plan to continue such initiatives in the second half of the year, in order to support future revenue growth through product and technology innovation.

These investments will be in addition to continued considerable investment in acquiring new users and customers.

As a result, adjusted EBITDA margin guidance for the second half of FY2021 is in the high 20% range, and, therefore, adjusted EBITDA margin for FY2021 is expected to be in the low 30% range.

The HR Technology forecasts for the full-year revenue growth rate and adjusted EBITDA margin are higher compared to pre-pandemic, but as I have said previously, this is largely due to the extremely unique environment we are currently experiencing, and we do not expect these levels to continue for the long term.

Next, I will talk about the results of Media & Solutions.

In Q2, COVID-19 and its related preventive measures in Japan continued to impact the overall Japanese economy, and the daily activities of individuals and business clients.

Revenue in Media & Solutions decreased 8.7%. However, excluding the FY2020 revenue from the Rent Assistance Program, revenue increased 10.1% as revenue in both Marketing Solutions and HR Solutions grew year over year.

In Marketing Solutions, Housing & Real Estate and Beauty continued to be the primary drivers of revenue growth while revenue of Bridal also increased.

Revenue in Travel improved compared to Q1, but decreased compared to the second quarter of last year, which was positively impacted by the Go To Travel campaign initiated by the Japanese government in July 2020.

Revenue in Dining also decreased as a result of continued weak demand for advertising by restaurants due to the state of emergency and priority preventative measures.

In Air BusinessTools, the number of AirPAY accounts increased 40.3%, as of September 30, 2021. Of the approximately 240,000 AirPAY registered accounts as of September 30, 2021, approximately 155,000 accounts also subscribed to other Air BusinessTools solutions.

In HR Solutions, revenue increased 18.4% benefitting from the significant revenue decline experienced in FY2020.

The recovery of the job advertising business has been especially limited by the COVID-19 related restrictions on restaurants, bars, and other hospitality businesses.

Revenue in the placement service increased year over year, as well as compared to Q2 FY2019 due to strong hiring demand for highly skilled talent, such as IT professionals.

Adjusted EBITDA margin in Media & Solutions for the second quarter in FY2021 was 20.5%.

Revenue in Marketing Solutions in the first half of FY2021 increased 10.8% year over year excluding the impact from the Rent Assistance Program, and revenue in HR Solutions for the same period increased 10.0%.

During the first half of FY2021, we cautiously invested in marketing, primarily advertising, as well as strategic investments aligned with our long-term strategy, while remaining focused on cost efficiency, as the business environment remained uncertain primarily due to the state of emergency lasting longer than expected.

As a result adjusted EBITDA margin in Media & Solutions for the first half was 20.6%.

We expect the recovery of economic activities to accelerate in the second half of FY2021 as the state of emergency was lifted on September 30, 2021, although the timing of the acceleration is still uncertain.

Revenue in Marketing Solutions for the second half of FY2021 is expected to be in the range of a decrease of approximately 8% to an increase of approximately 3% year over year excluding the impact from the Rent Assistance Program in FY2020.

While we expect the business environment for the second half of FY2021 for Housing & Real Estate, Beauty, and Bridal to remain similar to that of the first half of FY2021, the business environment for Travel and Dining is expected to improve compared to that of the first half of FY2021 when the state of emergency by the Japanese government was in effect.

The reason for including the negative revenue growth outlook for the second half of FY2021 is revenue for Travel, especially, in the same period in the prior year was positively impacted by the Japanese government's Go To campaign.

At this moment, we do not expect a one-time positive impact from any potential government programs during the second half of FY2021.

Revenue in HR Solutions for the second half of FY2021 is expected to increase in the range of approximately 17 to 22% year over year.

We assume that the revenue recovery from the job advertising business will accelerate as the restaurant and hospitality sectors resume their business activities.

The placement service is expected to see continuous demand from business clients for highly skilled talent.

Based on the second half guidance, full year revenue for Marketing Solutions is expected to grow low-single digits, excluding the Rent Assistance Program in FY2020, and full year revenue for HR Solutions is expected to grow in the mid-teens.

In the second half of FY2021, we expect to invest more aggressively compared to the first half.

We will proactively invest in marketing and product development in line with our long-term business strategy for future growth in response to the evolving business environment.

As a result, adjusted EBITDA margin for the second half of FY2021 is expected to be approximately 12% and adjusted EBITDA margin for the full year to be approximately 16%, similar to last fiscal year.

Last but not least, I will talk about the results of Staffing.

Revenue increased 12.4%, or 9.4% excluding the positive impact of foreign exchange rate movements, primarily driven by the increase in Europe, US, and Australia with additional growth from Japan.

Adjusted EBITDA margin decreased to 7.2% due to the decrease in adjusted EBITDA margin in Japan that was partially offset by an increase in margin in Europe, US, and Australia.

In Japan, after the number of temporary staff decreased in Q2 of last year when the impact of COVID-19 was significant, it has gradually recovered along with the recovery of economic activities and as a result, revenue in Japan in Q2 increased 4.9%.

Adjusted EBITDA margin declined to 8.7% as a result of an increase in paid vacation time taken by temporary staff and increased advertising expenses to attract temporary staff, both of which were impacted in the prior year by COVID-19.

Revenue in Europe, US, and Australia in Q2 increased 18.9%, or 13.3% excluding the impact of foreign exchange rate movements.

This revenue growth was due to increased demand for temporary staff overall, along with continued demand for logistics roles to support e-commerce, particularly in Europe.

On the other hand, while there was a positive impact from healthcare roles to support COVID-19 mitigation efforts until Q1 FY2021, its impact was diminished in Q2 FY2021.

Adjusted EBITDA margin was 6.0%.

During the first half of FY2021, revenue in Japan increased 2.8%, and revenue in Europe, US, and Australia increased 31.2% and 21.9% excluding the impact of foreign exchange rate movements.

Adjusted EBITDA margin was 7.5%.

In Japan Staffing, the number of temporary staff on assignment in Q2 FY2021 exceeded the level of the same period in the previous year and the business environment of the first half of FY2021 is expected to remain largely unchanged in the second half of FY2021.

Therefore, revenue in Japan for the second half of FY2021 is expected to increase approximately 3% year over year.

In Europe, US, and Australia Staffing, revenue for the second half of FY2021 is expected to increase approximately 5% year over year, continuing to benefit from the reopening of the economy, especially in Europe.

Adjusted EBITDA margin for Staffing for the second half of FY2021 is expected to be lower half of 6%.

Based on the second half guidance, revenue in Japan is expected to grow low-single digits for the full year, and revenue in Europe, US and Australia is expected to grow in the mid-teens for the full year.

Based on our guidance for the second half, adjusted EBITDA margin for Staffing overall for the full year is expected to be higher than last year’s margin of 6.4%.

That concludes my explanation of the financial performance and guidance by segment.

We will continue to steadily implement our most important business strategy, “Simplify Hiring” with a long-term perspective, without being constrained by short-term changes in the business environment or business results.

We are grateful for the understanding and support of our shareholders, other capital market participants, and all of our stakeholders.

Please refer to the earnings release and the materials on our website as appropriate, which include the contents of today's presentation.

Question & Answer

Shen: Now we would like to take questions. The first, Jefferies Securities, Mr. Takeuchi, please.

Takeuchi: This is Takeuchi from Jefferies Securities. Thank you. First is in this last 3 months, HR Technology, products, services and sales mix, do you have any conspicuous changes that you could share with me? And pay-per-click, is that the main revenue format? Or is there any other prominent growth that you saw other than pay-per-click? Thank you very much.

Second question is about the forecast for the sales of the second half. You are anticipating 5% growth, so on a quarterly basis, it seems like second quarter is the peak and then declined significantly. Is this just you being conservative or are there any signs that led you to this forecast? In HR Technology, it seems like you are seeing continuous growth. In the Overseas staffing and HR marketing, what is your outlook?

Arai Thank you. Do you think that HR Technology will continue increase in the second half? Is that your outlook?

Your second question, the sound was a bit unstable, so I may ask you to repeat, but let me start with the first question.

As we mentioned earlier, in the US, especially in the US and Europe, there's a big gap between the supply and demand. The client focus is indeed traditional or original business, the online job advertisement. Our business clients are utilizing this traditional part of the business. Of course, from a long-term perspective, we are continuing various efforts and initiatives. But at this point in time, the business clients' needs, demand is advertisement, job advertisement. Compared to the previous quarter, there is no big change. This job advertisement area is the main revenue source, so that is the answer to your first question.

Takeuchi: And the second question, you mentioned 5% in the second half. This is about the Overseas Temporary Staffing outside of Japan. You mentioned 5% to that, right?

Arai: Yes.

Takeuchi: It seems like the sales revenue will peak in second quarter and decline there onward. I want you to share with me the actual situation. And HR Technology is on the uptrend, and it seems like there's a little gap. And so if you could give us some more highlights, more color to it.

Arai: I see. Whether we look at 5% as conservative or not, this may be different from us looking at it from internally and from your external viewpoint, but the Temporary Staffing in Europe from the second half of last year, the demand under COVID, the health care personnel and the staff, so the supporters in the vaccination venues, there was this one-off extraordinary demand in those areas. But this decline in the more general industries, general area recovered. This is what we are seeing. We are looking at the decline and formulated our numbers.

If there are future lockdowns or restrictions, it may change the scenario. We cannot say for certain that this will be the case. But when we formulated the numbers, this was one side of the mix. We anticipated the decline in this extraordinary demand.

Takeuchi: I understand.

Shen: Thank you. Next, Tsuruo from Citigroup Securities.

Tsuruo: Thank you for this opportunity, and congratulations on your wonderful performance. First, in HR Technology, second half you expect 60% to 70% increase in revenue. That is a significant decline compared to the first half. Is there any seasonality or other factors that you considered when you develop this forecast?

And I believe you already have results for October. According to that, in the main market, for example US, what has been the trend? That is my first question. Thank you.

Shen: Please move on to your second question.

Tsuruo: Thank you. Second question is the type of question asked by one of the investors, but I'd like to ask a progress of 51 in China and of your outlook as Recruit Holdings. Thank you.

Arai: Thank you for your questions. In the first half, based on US dollars, it was 118.5%. And when it comes to 60% to 70% in the second half, you may be able to say that growth is rather muted in the second half. But on the other hand, in the second half of FY2020, especially in the fourth quarter, since then, we have grown significantly already. Therefore, the denominator is large in the second half. In terms of growth numbers, it's seemingly declining, but in this second half, continuing from the first and second quarter, we are expecting a similar trend.

Perhaps the significant gap between supply and demand is going to ease a little bit. But basically, similar trend is going to continue. In August, we announced our forecast. And back then, we expected a control of COVID pandemic and also the end of restrictions by the government and the local government, and that was our prior expectations. But today, we factor in other elements other than this too. We do have uncertainty as to when this situation is going to end, but we do not think that is going to end immediately. And that is the basis of forecasting 60% to 70%, based on the previous year's second half and in the range of 85% to 90% or in the high 80% range is what we expect as of today based on the latest conditions.

And as for seasonality, if you look at past figures, especially in the US market, in the holiday season, obviously, job seeking activities will be slower as well as the hiring activity. Therefore, in the US during the fourth quarter, we tend to see lower activities, but it is not visible yet for this year. We do expect a certain level of such seasonality, but that is just an expectation as of today.

And as for your second question, we see the progress as receptive, meaning that we have been just monitoring the progress. We are not taking proactive measures. Environment has been changing and people involved in transactions, they may have different thoughts. But from our point of view, we are waiting for the phase where the conditions decided in the contract will be implemented and executed. We are waiting for that phase.

Tsuruo: Thank you very much.

Shen: We answered the questions we received so far. Any other questions? Mizuho Securities, Mr. Kishimoto, please.

Kishimoto: This is Kishimoto speaking. HR Technology margin is my question. The second half is the higher half of 20%. If the supply-and-demand gap is resolved, what do you think is the margin level for the second half? The way of thinking is with aggressive hiring, there may be some cost increase. The first and second quarter was very strong, and therefore, maybe you are anticipating a bit lower level than that. If you could give me your view. Thank you very much.

Arai: Thank you. For next year, there is nothing we can say about next year. It's not appropriate to say anything at this point in time. I hope you could understand. But increasing margin or lowering margin, we're not intentionally trying to lower or raise margin excessively. We want to accumulate enough capability and hire people appropriately and invest in marketing activities appropriately. We are taking steady measures. Sometimes margin is high like the second quarter and not so high in other quarters. It's not that we have the numerical target for the margin. That's not how we operate the business. Our forecast of margin next year is something we are not projecting yet.

Kishimoto: Thank you very much. Another follow-up question. Engineers, the technicians, recruitment, how is it going? Is it progressing well? I'm sure there is competition for talent for high-skilled engineers. Is it going in line with your plan? Or after the first half, are you spending your hiring costs as planned or?

Arai: Our hiring is not that different from other companies' hiring. When there is a supply-demand gap, we are struggling as much as the others are. But in the second quarter, we worked hard on hiring people and continue doing that in the third and fourth quarter. We have that in our plan. And this is not for this year or for early next year. This is for a longer-term objective to simplify hiring. The people will be the engine to achieve our objectives. Regardless of the profit margin level, we are working steadily making investment to achieve our long-term goal.

Kishimoto: Thank you very much.

Shen: Thank you. Now Mori-san from JPMorgan.

Mori: Thank you. This is a similar question to the one before. But in HR Technology business, in the second half, operating expenses, marketing needs to be increased to a certain extent in order to spend this much money. And together with gradual recovery of job seekers' activity, are you expecting to spend more marketing cost? Or even if you cannot expect much recovery are you willing to invest in marketing at this timing actively? That is the first question.

Second is Indeed hiring platform, in March it was launched, and it's been over 6 months. The monthly fee structure has been tested. And as of today, what do you set as KPI? I believe monetization is not something that you're focusing too much today, but is it the number of interviews? What is the KPI that you focus on the most today? Those are the 2 questions. Thank you.

Arai: As for your first question, as you say, what can we do towards the future to build foundation and there is something that we can take as measures when we are being profitable now. We want to make sure to have right people in the right place at the right timing, and that is why we need to make investment at certain timing. Timing differs between countries and regions. This is what we're trying to begin.

At some point, we may be aggressive than the other timings. And at some point, we may be less aggressive. It's not that we are trying to use this much money for unnecessary purpose, but we do believe that this is the right timing to invest into marketing, and this is the preparation for the future growth. That is the intention behind.

And to your second question, as I've been saying, in addition to advertising, in the broader Recruiting business, we would like to realize better environment for those seeking jobs and those trying to hire. We'd like to develop better services and environment for those people.

Regarding this initiative, we do not focus on short-term KPI, but we always consider how we can bring down the hiring cost of our customers' clients, and looking for people and trying to hire them is the top priority in this business. A lot of our clients are setting top priority as hiring people rather than the cost itself. But cost per hire is one concept we need to think about, and we are trying to offer added value through our service. Today, clients are willing to pay for advertising and once situation becomes more normalized, how customers would appreciate our added value, meaning that lower cost per hire will be realized for customers in the end.

This is one of the processes to realize that vision. Bringing down cost per hire is the biggest KPI ultimately for us.

Mori: Thank you.

Shen: Thank you. SMBC Securities. Mr. Maeda, please?

Maeda: Thank you very much. The second quarter ended and you are accumulating cash. Dividend, you have full year unchanged. Your cash and balance sheet, I think you will accumulate more cash in the second half. I want to ask you for your view on the cash allocation, if you could update me.

Arai: Yes. Cash allocation has not changed from the past. The order of priority remains unchanged. The business, we will use what we need to use in the P&L and then a stable dividend, steady dividend, and M&A. Our surplus capital, if the condition is right, then we may consider the possibility of share buyback. This priority remains unchanged.

Of course, strategic M&A, acquisition tends to be the focus. Business development, M&A team are working hard to identify good partners every day. That remains unchanged.

Maeda: Thank you very much.

Shen: Thank you. Now Fukuyama from UBS Securities.

Fukuyama: I have one question related to Air Business Tools. The KPI for every quarter has been disclosed. Compared to your internal targets, what is the progress? Sales activities are restricted to some extent. Has it been progressing less than your expectation? Or are your internal KPIs are progressing positively? Can you please comment on that? Thank you.

Arai: Thank you for your question. Air Business side, it is true that there are still some restrictions on our sales activities. Our internal targets cannot be shared with you all, unfortunately, but even under such circumstances, we would like to offer convenience for customers, and we have been acquiring a lot of new customers. We are going to continue such measures and cashless environment will be developed and supported in Japan going forward, and we would like to be at the front line of such initiatives.

Therefore, we would like to continue to make efforts so that Air Business Tools will be used by many shops and companies. We believe the progress has been steady and positive.

Fukuyama: Thank you.

Shen: It is time, so we would like to take one last question. CLSA, Mr. Kato.

Kato: This is Kato speaking. Thank you very much. HR Tech, second-quarter profit margin. First quarter, you had more sales growth, so it was 37% higher. But second quarter, I think you anticipated a big growth in sales. And so I thought margin will decline, but it improved even further. What was the background? For example, USD1.5 billion sales, it will decline to 30% margin? Or what is your line of thinking?

And second question. In October, US, the subsidy in some states were ended. What is the status of the supply and demand?

Arai: Let me start with the second question first. It's linked to my first part of the answer. Those who are away from work are receiving subsidies and this period will end. Once the period ends, many workers will start searching for jobs. That was our original projection.

But there are other factors. It is difficult for the parents to send their kids, have their kids looked after, have to look for where their kids have to be kept. And because of COVID, some are refraining from working actively. The progress in vaccination and the end of subsidy are not the only 2 trigger events. There are variabilities from state to state. The job seekers activity has not returned to the original level. That is our current view.

And the first question, as I mentioned earlier, for the revenue increase, the second quarter last year had quite some savings. But this second quarter was not. Compared to second quarter last year, we used various expenses more aggressively, but our revenue growth was even bigger, bigger than we thought. That is why margin increased from the first quarter.

Kato: Thank you very much.

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