

This is an edited version of the English translation of the Q1 FY2023 earnings call which was conducted in Japanese. Please note there are differences between the simultaneous English audio translation during the Q&A session and this summary.

Recruit Holdings Q1 FY2023 Earnings Call August 10, 2023

Shen: Welcome to the Recruit Holdings Co., Ltd. Q1 FY2023 earnings conference call. This call is the simultaneous translation of the original call in Japanese, and translation is provided for the convenience of investors only. I'm Mizuho Shen, Group Manager of Investor Relations and Public Relations. Joining me today is Junichi Arai, Executive Officer of the Corporate Planning Division.

The Q1 financial results presentation video and transcript were uploaded to the IR website at 3:00 PM today. So, all 50 minutes of today's session will be used as a Q&A session.

Shen: Jefferies Securities, Takeuchi-san please. Just a moment, please.

Jun: We're just adjusting. Thank you very much for your attendance. Some large listed companies are announcing their results today at the same time. Nevertheless, you are here with us. Thank you very much.

Shen: Takeuchi-san, thank you very much.

Takeuchi: First question, PPSA. Regarding PPSA in HR Technology is my first question. What is the impact and the hint to ascertain the potential going forward? 50% down in the paid job ads. Sales per paid job ad potentially increased by 60%, I calculated. By shifting to PPSA, how much per application will it go up in PPSA? What is the penetration of this in the US customers? The scale and your potential going forward, please? That's my first question.

Shen: Could you also ask the second question first? Thank you.

Takeuchi: This is also about PPSA. It started in the US, but what is the roll out plan outside the US? Thank you very much.

Jun: Thank you for today. PPSA has been tested and introduced in a few other countries, too. As Idekoba-san said last time, increasing the per application spend is also important, but the first priority is how to provide more added-value services to our clients so that it can be used more. We are doing trial and error, and this Pay Per Started Application is part of that effort.

If you visit the site, you can watch the clients' tutorial for US business clients and it explains what PPSA is about. If you have time, please take a look. But just briefly, it used to be pay-per-click. With certain budgets, clients looked for people through pay-per-click. With PPSA, in contrast to PPC, business clients will be charged when those who are really interested apply as opposed to being charged for a simple click. That is the structure.

In some cases, there may be no one who applies, which means no payment. This is different from PPA which we explained last time. PPSA is based on a budget. When the button to start an application is clicked, the business client is charged. So it is like pay-per-click which charges based on a budget. That's why the shift of business clients from PPC to PPSA is natural and correct. Many business clients have already shifted to PPSA from PPC and we are also asking the business clients to consider this payment model. As Takeuchi-san just rightly said, paid job ads decreased by 50%, but the revenue has not declined as much because of this reason. There are other things we are trying, other factors come into play, but that is one impact.

For your second question, we started in the US and we have been testing in other countries and PPSA has been started in some developed nations, too.

Takeuchi: Thank you very much.

Jun: One more point, if I may add regarding the PPSA, it is based on a budget. If one client has a budget of USD 100 per day or USD 300 per month, the budget of USD300 remains unchanged and the business client has shifted from PPC to PPSA. That's the simple way to understand this. Business clients are not paying more.

Takeuchi: Thank you very much. One follow-up question. Will there be a complete shift from PPC to PPSA in the US in the near future ?

Jun: Well, we are initiating that change, but it's not like everything is going to shift completely right away because it depends on the business clients.

Takeuchi: Thank you very much.

Shen: Citigroup Securities, Yamamura-san. Please go ahead.

Yamamura: Thank you. I also have two questions. This is a follow-up on the previous question and answer. Until Q4, implementation of PPSA model seemed rather challenging. But, in Q1, I saw that you explained that promotion of this PPSA model was promoted pretty significantly. What changed? Is it because of better penetration of your measures, better understanding in the market? Can you give us some more color on that? That is my first question.

Shen: Can you please also ask your second question as well?

Yamamura: Right. My second question is regarding Q1 results and the Q2 outlook. When I look at them, as long as there is no rapid change in the environment, EBITDA is expected to be flat or go up. But, from your flash report, I could see that there are signs of a better environment. Although the environment is uncertain, if profits increase, will the company withdraw its cost-cutting measures and return to a growth track during the current fiscal year? Can I expect a further improvement in profit if that happens?

Jun: Thank you for your questions. To your first question, it was related to Takeuchi-san's question. As I responded to Takeuchi-san, PPSA is something clients shift from PPC. PPA is a completely different product. When someone applies, it is monetized and charged a certain amount. PPSA, just like PPC, is consumed using the same budget. That is how this pricing model works.

Imagine that you are the HR person, then it would be good. Even though you see the pricing system shifting to PPSA from PPC, your budget would not change. With PPC, you don't know who is good or bad, who is serious or not, and who just clicked on your ad.

With PPSA, however, you will have the people who applied, which we consider a high-value-added service for our clients.

Also, in terms of cost, it is client friendly. That is why we are promoting this pricing model. Yamamura-san mentioned promotion seemed rather difficult. I think you were looking at PPA, not PPSA. They are similar, just with an "S", but they are totally different products actually. The shift from PPC to PPSA has been promoted among a number of clients. I believe that is a natural shift, and I hope you can understand the situation.

To your second question, my simple answer would be, we're not sure yet. If we have better visibility of the external environment, well, we are expecting a decrease in revenue and profit at this moment. We have uncertainties with regards to the external environment, so we're not announcing the full year guidance. So up to Q2, we are giving you certain visibility. Regarding Q3 and Q4, we still have a lack of visibility, and we're not sure what can happen. That is a better way to describe how we are feeling as of today.

As of today, well, when you say growth track, if you're referring to hiring more people, I would say we do not have a plan to implement such measures soon. For the time being, we will have a rather sensitive phase for

our revenue. Now is the time to take on different challenges and wait for the next recovery phase while we control the cost. That is the view we continue to have since six months ago.

Yamamura: That was clear. Thank you for correcting my misunderstanding.

Shen: Next is from Goldman Sachs Securities, Munakata-san please.

Munakata: Munakata here from Goldman Sachs. Thank you very much. I have two questions regarding the difference between PPSA and PPA.

Please correct me if my understanding of the difference between corporate clients using PPA and those using PPSA is incorrect. Is PPSA a service for large corporations that post jobs on their own systems, and if that's correct, PPSA has a larger revenue scale than PPA because it is for large companies with larger budgets? That's my first question.

My second question is regarding HR Technology costs. When you did the recent full-year financial results briefing, you disclosed the breakdown of SG&A that advertising expenses accounts for 13% of sales and that the first and second half trend is quite different. If you have the results for Q1, I'd like to know that, as well as your forecast for Q2, thank you.

Jun: For your first question, if you could remember, PPC has been used by large companies and SMEs, and PPSA is the shift from PPC as I just said, so it's not weighted towards one or the other. PPA is used more by SMEs, but depending on the purpose, large companies do use it, too. There is not a clear line between large and small and medium-sized companies. Within their budget, they use a certain portion for this or that.

Regarding the SG&A breakdown. Looking back on the past year, H1 and H2 last year, the cost and the content were different. That's how we explained it.

Of course, we did this in Q4, and we implemented cost reductions in March, and you can see the result in Q1. Personnel cost is close to H1 last year, while promotion and advertising expense is close to H2 last year. That, I think, will be the appropriate allocation. We want to provide you with an image of the allocation and the breakdown of the cost going forward, not on a quarterly basis, but on a half year or full year basis.

Shen: JPMorgan Mori-san, please.

Mori: I am also interested in this topic of PPSA. You mentioned the shift to PPSA and PPA. When we think about the revenue of HR Technology, how much is the impact from this shift? In Q1, the revenue was close to the higher range of the guidance, or perhaps above. The macroeconomic environment perhaps was simply better than your expectation, but how much was the impact from this change in the pricing model?

Within the same amount of budget, you said that you shift from PPC to PPSA, and that's understandable, but because of the higher value add or better convenience, does it lead to better wallet share and increased budget from your clients? Or do you see any signs of that happening? From the second half to the next fiscal year, the macroeconomic environment is still unclear. I imagine the shift of the pricing model was expected to bring about a positive benefit later in your journey, but how has the progress been?

Shen: Yes. And, your second question is?

Mori: That's all I had to ask.

Jun: There were many things, so it's difficult to analyze and quantify the impact in terms of percentage from different elements, but that is difficult. The macroeconomic environment is never flat. There is always a certain level of impact.

Even though the macroeconomic environment is deteriorating in the short term, our intention is not to just raise prices in order to survive during this time. We want to make sure that the measures we take today will lead to enhancing value in the future for our clients, even though it may impact our performance in the short

term. We will always consider going forward, what we should continue and what we should stop. The main focus is not increasing wallet share or increase of budgets.

On the other hand, it is possible that an originally paying customer could temporarily become a non-paying customer. Clients with smaller budgets may experience difficulties. If you just focus on the unit price, it may seemingly increase, but we're not looking for our sales to prosper in the short term, but rather, we are focusing on the longer-term cycle, and this comes from taking a long term perspective to hire people among the clients. That is our philosophy.

Of course, we may face difficulties from a short-term perspective, but from a longer-term perspective, we just hope that we can bring about more benefits for clients, job seekers, and ourselves.

Mori: Well, rather, you need to downsize the budgets and clients would want to allocate budgets to more effective products. That is how I see this. The PPSA shift is something you told us that you will never know what would happen unless you implement it. I think you just found out that you have seen a positive effect.

Jun: Well, it is a shift from PPC to PPSA. To simply put, it's just neutral. It is not charging significantly more, but clients will receive more candidates with serious intentions to apply. That means we can offer more added value to our clients. As you said, of course, we would be grateful if clients decide to allocate budgets more to this product, but comparing against the previous year, maybe clients would feel that they are spending their money in a better way this year because of this effective product. With this lack of clarity, it's difficult to foresee a future where clients would increase the amount of the entire budget. Well, if we can continue this, I think it is going to be a positive thing.

Shen: SMBC Nikko Securities, Maeda-san please.

Maeda: Thank you. I have two questions. First is the same as the others, PPSA. From a client's perspective, there's not much advantage to going back to PPC. In the next year or so, will the shift from PPC to PPSA continue to move forward, including your promoting them? Or will they coexist in the near future? That's my first question.

Second question is about the Staffing results. Overall revenue increased 4.1% and adjusted EBITDA decreased 2.0%. The profit went down, but I cannot understand why profit went down in Q1. Why did it go down?

Jun: Thank you. The revenue trend in the Staffing business is opposite in Japan compared to Overseas. As you can see revenue is down in Overseas, but our internal personnel costs went up. That was a big factor that pushed down the profit. But we are continuing to control our margin, so a mid-6% level margin is maintained for Staffing overall. Personnel cost and the associated social security cost, including Japan, that is the incremental cost, but that could not be fully offset by the increase in revenue.

Let me go back to the first question. Under PPSA pricing, money does not come to us by just clicks on the job posting, which is how it works under PPC, even if there are no started or completed applications. Those clients who enjoy the advantage of PPSA will not go back to PPC. They will enjoy the current service, I think. Once this takes root, they will not go back.

As PPSA is established, we cannot go back to PPC because as you can see on our site, we say that we will charge based on PPSA pricing, so it is unlikely that those two will coexist going forward. We've said pay-per-click, and then explained budget-based. Maybe this part was not fully communicated. I'm sorry about that. But, PPSA, is another alternative as a budget-based product. We think PPC will be mostly replaced by PPSA. Of course, there will be some exceptional customers that come through agencies, but I think the majority will shift to PPSA.

Maeda: When do you think this shift will be pretty much complete? Within a year or will it be more drastic or quick? Within a quarter or so?

Jun: Within a year, it will be pretty much replaced. In other words, there's no option to go back.

Shen: Thank you. We have taken all the questions that we have so far. Are there any questions from other participants or any second round of questions?

Jun: I would like to have questions about the Matching & Solutions SBU.

Shen: Then, Arai-san, please.

Katsumi Arai: This is Arai from Mitsubishi Morgan Stanley Securities. I would like to ask a question about the HR Technology, non-US business. In Q1, it was minus 1.8% YoY. Excluding the impact of foreign exchange, it was minus 0.9%. In Q1, I think this is a larger decline compared to other quarters. Can you give us some more color on that? In Q2, what is your outlook for the non-US business?

My second question, this is not related to the financial results, but about Indeed job posting. On your website US development of job listings is disclosed until the 28th of July. Compared to February of 2020, it is 135,136, so it is declining. How do you see the situation?

Jun: Well, regarding job posting, it includes jobs that are aggregated. There is no significant decline. Regarding paid job ads, there is a change as we have explained. As I said in my previous answers, some clients stay free while some clients pay more. When we look at six or nine months, compared to the decline of the volume jobs, a larger number of clients are paying for the product. That is going to lead to future results. The entire pie is seemingly coming down, but there is also a possibility that this can decline further. That is why we are not disclosing a full year guidance because of such uncertainty.

To your second question, US and non-US business. Regarding the performance forecast, we are disclosing based on US dollars for the HR Technology business. As always, the situation in the US is followed by Europe, but there is a delay. Then, much later, Japan follows the same path. That is the typical pattern. People are terminated; people are hired. There are more and less reactive markets. Compared to the US, the magnitude or the liquidity of the HR market is not as high as in other countries, including Japan. I believe that is the key difference between the US and non-US markets as I have always explained.

Even if there is a significant decline in the US, other regions don't decline as much. But, the revenue from the US accounts for 75%, and the rest of the world accounts for 25%. The ratio of non-US business is expected to increase eventually, which is what we've been seeing over the past three years. In the most recent disclosure, it was 70% to 30%. That means the US is decreasing, and the non-US has increased to 30%.

We are hoping a recovery will happen in both parts of the world. Maybe this ratio will change to 60% to 40%, but that is not what we are seeing today. The US is weakening, and the rest of the world remains flat or is slightly declining. That is the situation we base Q2 projections on. In Q3 and Q4, as we have discussed, it is still not clear. In November, we hope to have better visibility to share with you. As of today, the situation has not changed.

Shen: Macquarie Securities, Tanioka-san, please.

Tanioka: In the script you said Indeed and Glassdoor's traffic number is up YoY. How should I look at this? Is the competitive position changing? Could you elaborate, please?

Jun: The trend is that more people are coming to the site to look for new jobs. That is the trend right now. Of course, those who lost jobs are increasing, and those who are not satisfied with the current job are looking for new jobs, so it is a mixture of those two. Compared to the past, more are coming to look for new jobs. This is increasing.

On the other hand, with the slowdown of the economy, the number of jobs available are decreasing. The supply and demand is easing, which is something we've been saying for 10 years now. If you're looking for a job, go to Indeed, go look at the data on Glassdoor. We are happy to see that there are many people who do that, and that is the value we deliver. It is like this until today, and we think this trend will continue.

Shen: Citigroup Securities, Yamamura-san please.

Yamamura: Thank you for your kind suggestion. I have two questions regarding the Matching and Solutions business. My first question: M&S revenues continue to increase yoy. The increase in profit is due to the cost reductions communicated at the end of the fiscal year, including advertising expenses. Did cost reductions in advertising expenses have no negative impact on revenue growth? Is it also due to the impact of the centralization of the advertising contact points in the HR Solutions? Or is it going to happen over a longer timeline?

My second question is regarding Marketing Solutions. Some of the other companies were seeing weak ad placements in the food and beverage area. Is there any difference in how the different verticals in marketing solutions are performing recently?

Jun: Well, you mentioned the restaurant business, so I would like to talk about that first. Compared to housing and beauty, the size of this restaurant or dining business is small. Percentage changes tend to appear larger than in absolute growth numbers. In Q1, there was actually a large recovery in this restaurant sector. Compared to pre-COVID-19, in Q1 FY2019 it was still at a higher level than today. We haven't recovered to that level, but in these eight or nine quarters or in the three years, I believe we are at a relatively high level in terms of quarterly revenue for this restaurant sector.

As we've discussed previously, in our marketing solutions business, housing & real estate and beauty are the two largest verticals. In marketing solutions, we will continue to have about slightly over 50% revenue coming from those two verticals. These two will be enjoying a stable revenue growth. Compared to that, the size of the restaurant vertical is smaller, but revenue is actually significantly increasing YoY.

Coming back to your first question on revenue increase and cost reduction measures. When you look at Q1, overall revenue was JPY200 billion. We will not be cutting costs if it negatively impacts our revenue. We will make sure that we maintain the revenue while streamlining our cost. That is our business strategy. Therefore, our revenue was growing by 10.8% as a whole in Q1.

Both, Marketing and HR Solutions were in line with our expectation in terms of cost reduction and growing the business. Especially in HR Solutions, we had a large promotion and marketing spend last year. This year, the amount has decreased, and that is leading to better profitability of the business. We will be revisiting our strategy on a regular basis to make decisions on how to spend money. Throughout this year, we are looking at 20% overall. We like to continue to work on strict cost management to achieve 20%.

Shen: Next, CLSA Securities. Kato-san, please.

Kato: This is CLSA, Kato speaking. One simple question on the overseas Staffing business. QoQ growth is slowing down in Europe, US and Australia. Could you provide us more details on those three regions, please?

Jun: As I said earlier, the other regions have a time lag compared to the US. The biggest slowdown is in the US. The US is the most difficult market, followed by the UK, Europe as they will come, followed with a certain time lag. Australia has been difficult all along. This, I think, will provide some context. I hope this answers your question.

Kato: Okay. So the slowdown is not that different among regions?

Jun: The US slowdown is the largest. That's the rough image. It's a mirror image from the scale of TAM, as a total market, the market by country, it's almost a mirror image.

Shen: Are there any other questions from the participants? Well, we can talk about the follow-up on numbers in the analyst call. If you have questions about the big picture, we can use the remaining five minutes to answer your questions. If there are no additional questions, okay, then, we would like to close this session.

Thank you very much, everyone, for your attendance.

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This document contains forward-looking statements, which reflect the Company's assumptions and outlook for the future and estimates based on information available to the Company and the Company's plans and expectations as of the date of this document or other date indicated. There can be no assurance that the relevant forecasts and other forward-looking statements will be achieved.

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