This is an edited version of the English translation of the Q2 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 Q2 FY2023 Earnings Call

November 8, 2023

Shen: Welcome to Recruit Holdings Q2 FY 2023 earnings conference call.

This call is a simultaneous translation of the original call in Japanese and translation is provided for the convenience of investors only. I am Mizuho Shen, group manager of Investor Relations and Public Relations.

And joining me today is Junichi Arai, Executive Officer of the Corporate Planning Division. The second quarter financial results presentation video and its transcript were uploaded to the IR website at 3pm today, so all 50 minutes of today's session will be used as a Q&A session. This time we've decided to start the call at 4pm which is one hour earlier than in the past. This change is intended to speed up the process of uploading the Japanese and English transcripts of the calls for the benefit of global investors.

Jun: Thank you very much. I appreciate your attendance today.

We uploaded the transcript to the IR website at 3pm today and so I think you have seen it already.

Let me briefly summarize.

For the consolidated full year outlook the numbers will still be not disclosed because the market environment is still uncertain and many things could happen. So we will not disclose the outlook.

On the other hand, in the financial results briefing in May, we said we expected both revenues and profit to decline.

Revenue decline will remain unchanged but we changed the outlook of the adjusted EBITDA will be a slight decline or flat, and net profit will increase as long as no one-off extraordinary loss is incurred in the fourth quarter.

And for the segment views, HR technology full year outlook will not be disclosed because it's still uncertain.

But when I and Idekoba talked in the May earnings announcement at Fireside Chat, my question to him was if the US dollar-basis revenue hypothetically falls 20%, what the margin would be? And the answer was adjusted EBITDA margin would probably be in the mid 20%s.

But given the tight cost control, and results shown in the first half and the outlook for the second half, the expectation will be more like upper 20%s, which is higher than mid 20%s. So we are changing our outlook. But to repeat myself, we're not saying that our revenue outlook is minus 20%.

Even if something significant happens in the fourth quarter results and revenue will result in that kind of level, we can generate adjusted EBITDA at that level. So let me repeat that message.

We disclosed the result of the second quarter, and we just announced the segment outlook and the consolidated outlook for the third quarter.

For Marketing Solutions revenue in Matching & Solutions a detailed disclosure was not provided for a long time but we will now give the revenue breakdown in line with how we operate the business and our business strategy on a biannual basis.

That is one special item this time. We shared that information with you one hour ago.

We will be happy to answer your questions as well in regards to those topics.

Shen: First of all, UBS securities, Fukuyama-san, please go ahead.

Fukuyama: Thank you as always, and we really appreciate reconsidering the disclosures. So one question from me is related to the change in the pricing model of Indeed. How much has it penetrated after six months, especially in the US?

And, regarding your customers who have switched to the new pricing model, has there been any changes to how they consumed their budget? Thank you.

Jun: Thank you for your question.

Penetration wise, as we mentioned previously, we believe we have been progressing steadily, especially for existing customers.

And in terms of the pace of budget consumption, we have been implementing multiple changes. So we cannot give you any uniform answer, but if you look at our revenue situation, of course there are economic drivers, but as we described, there are multiple factors which impact the number of job, paid job numbers, and unit price to change.

As we mentioned previously, short term revenue is not something we're going after by increasing the unit price significantly.

We are trying to offer our customers with the same budget, the same or larger impact with our strategy. We are offering incremental value. And if this is understood and promoted properly, revenue would be somewhat neutral and not decline. And I would describe it as a very smooth transition. Thank you.

Fukuyama: The unit price for a job has not decreased? Is that the correct understanding?

Jun: I believe it was in the FAQ or in my script, but we have revisited our minimum budget. So as Fukuyama-san said, overall nothing changes but there is a positive impact on unit price per job. This is not only driven by the impact of PPSA, but it has been progressing smoothly.

Fukuyama: Thank you, that was encouraging.

Jun: Thank you.

Shen: Goldman Sachs securities Munakata san, please.

Munakata: This is Munakata from Goldman Sachs. Thank you very much.

I have two questions. So should I go one by one?

Shen: You can ask two questions first.

Munakata: They're both on HR Technology. First is on minimum budgets. I don't really understand your strategy, so sorry to ask the basics. But what is the advantage of minimum budgets for the clients?

And my second question is on HR Technology regarding the third quarter outlook. While revenue on US dollar basis declines 18% YoY, revenue declines quarter on quarter, and the amount of operating expenses is about the same as Q2. I understand your Q3 margin declines versus Q2, but is this because of seasonality or any planned investment? Thank you very much.

Jun: Thank you for the question. So let me answer your second question first. In Q3, revenue is expected to decline 9% quarter on quarter, equal to a decrease of 18% year on year. And as I disclosed, revenue in October declined 18% year on year. These are the numbers we presented.

As I mentioned, regarding expenses, we are tightly controlling costs and the personnel is flat including natural churn, resulting in a slight decline in headcount. Margin forecast is 27%. Given the October status, we're seeing around 27%, but we think that the possibility of below 27% is not high, in other words, 27% margin might be a bit conservative.

It's not that we are thinking of making any new investments or incurring any other costs that we have not communicated to you. So did I answer the second question?

Munakata: Yes. thank you.

Jun: Regarding your first question about the minimum budget, what it means is that if the lower limit is set too low, results will not be achieved, but this does not mean that Indeed's functions are not working well, but rather that the budget level is not appropriate.

So by setting a minimum budget per job, the expectation and the outcome will be more aligned and a more desirable result will be produced for the client. And we know, that will be the case. That's why we are setting this minimum budget and we understand the current situation as being well received by paying customers.

Munakata: I understand. so you made the appropriateness of the budget setting more clearly. Thank you.

Jun: Yes. The level can be around $20 or $25 or something like that, but clients can choose not to pay this and just post for free and such clients will still have a return from not paying. The return is much lower than for free postings. So the return on paid jobs will become clearer, more visualized, that’s how we set the minimum budget.

Munakata: I understand. Thank you.

Shen: Nagao san from BofA please.

Nagao: Up to how many questions may I ask? My name is Nagao. May I ask two questions at a time? Then my first question is on Matching & Solutions. I would like to get your view on the third quarter outlook.

When we look at Matching & Solutions from a slightly different angle, considering the seasonality of the segments, I can imagine that revenue in Dining, Beauty, and Travel in the third quarter, could be larger. In such a case, margins could expand proportionately. What is the context of setting margin at 23% for Q3? That is my first question. Thank you.

Jun: Thank you. We are looking at the past numbers, but the margin is slightly high in the third quarter. However, there isn't a significant difference over the past four years. Of course, it could be much lower in Q4 intentionally, but it doesn't necessarily mean that we have an exceptionally high margin in Q3.

For example, in 2019, before COVID-19, Q1 margin was 26.7% and the Q3 was 27.4%. Last year, the Q1 was 17.4% and the Q3 was 16.5%. Q2 is slightly lower, but there is no significant dip or jump. So 23% margin, it's what we should naturally reach.

Nagao: Understood, thank you. My second question is on the pie chart page 9.

I would like to make some basic clarification of the numbers. This dark blue area consists of Beauty, Travel, Dining and SaaS solutions, does this mean that revenue in Beauty, Travel, Dining and SaaS solutions all together add up to 120 billion yen?

Jun: Yes.

Nagao: Okay. Then If I subtract each of the businesses from 120 billion yen, I would guess that revenue in Saas solutions has grown to already a 10 billion sized business which is sizable as a business. Am I right?

Jun: I can't say if this is sizable or not as we have other sizable businesses, but if you look at the past numbers and subtract them, I can see why you would have that impression.

Nagao: I see the revenue of SaaS solutions is clearer now. So I really appreciate this disclosure. Thank you very much.

Shen: Citigroup Securities Yamamura-san, please.

Yamamura: Hello, this is Yamamura from Citigroup Securities speaking. Thank you.

Two questions. First question is on HR tech regarding US and Non-US business.

Looking at your numbers, it appears the US decline is supported by the regions outside of the US. Is this due to the impact of the macro environment, further PPSA penetration or the minimum budget setting? Does that have an impact? Could you please elaborate?

Second question is regarding the collaboration between HR Solutions in Matching & Solutions and Indeed. We have heard that you would like M&S and Indeed resources to be consolidated and the place to post an advertisement is unified so that the advertisements are more efficiently distributed to the right media.

Do you plan to integrate the US Indeed office with Japan, or not? And are any upfront investment this fiscal year planned. Thank you very much.

Jun: Thank you for the question. So let me answer your second question first.

So the full year business direction, the upfront investment was not considered like Kitamura mentioned. Of course we have many plans. But we do not have a full year plan that includes your point.

There are many possibilities. So we cannot clearly say: This is not included or this is included. But we are thinking of the most possible and promising actions for our business and the biggest lever to increase business efficiency.

So we're thinking of various measures, and trying to judge whether it works or not as we move forward. So it's not something that will happen today or tomorrow. But as you rightly said, we will continue pursuing a more productive, efficient, better job for our clients.

Regarding your first question, compared to the market share in the US, we have other overseas businesses and there are some countries where our competitors are very strong. The European economic environment is as difficult as the US, but there's still significant potential for continued growth.

So there are some European countries where we are gaining market share. On a dollar basis, and local currency basis, there are two ways of looking at it. In some cases, overseas businesses on a local currency basis, revenue may be stronger and growing more or revenue is flatter than Yamamura-san sees.

In case we would disclose more about individual non-US countries, it would be clearer. Generally, we see non-US is doing well while the dollar is very strong.

Shen: Mizuho securities Kishimoto san please go ahead.

Kishimoto: This is Kishimoto speaking. Thank you for your explanation. I have one big question regarding Matching & Solutions. Specifically, I have a question about the financial results of HR Solutions.

In the earnings release, you mentioned that some business clients are cautious to hire. Can you give us some color on the hiring situation in terms of industries or any type, recently?

For the third quarter 2% growth is projected for HR Solutions. In the second quarter, some clients were hesitant to hire and maybe those clients expected to increase. Or is it going to be a high hurdle to achieve, year over year growth?

What is the assumption for the momentum change from the third to the fourth quarter? That's my big question.

Jun: Thank you for your question.

We explained for the second quarter, that results are slightly lower than revenue projection and that the third quarter is projected at around 2%. So in terms of growth rate, it is more moderate.

That's what the numbers tell you.

Some clients are cautious but other clients are active.Whether they post job ads on the job board or post job ads into the placement service, depends on the industries of the clients and what type of category they are looking for. That is what makes a lot of difference and the future is unclear.

Software engineers, for example, will continue to have high demand regardless of industry or type of employer. Of course, demand from service sectors continues to be high. On the other hand, manufacturing may be weaker. So depending on the industry, there are differences. So it's a mixture including the very strong demand in some industries and roles mentioned earlier.

Kishimoto: Understood. Thank you. Do you think this trend is going to continue in the fourth quarter? I'm sorry, I'm asking about the future.

Jun: Well because of the given situation, full year projection is less than what we originally disclosed.

Kishimoto: So I would like to estimate Q4 by subtracting between the outlook for the full-year and the third quarter.

Shen: Macquarie Securities, Tanioka-san, please go ahead.

Tanioka: Thank you. This is Tanioka from Macquarie. Thank you. One question regarding HR technology. Sorry in case you have already explained this but you've been doing good cost control in HR Technology for personnel and advertising and making good profit. Even if the underlying basis changes from what Idekoba-san said, you can achieve a higher 20% margin.

But if the top line does not drop that much, do you resume your hiring? You have frozen your hiring and taken restructuring measure. Do you plan to resume your hiring? If you resume hiring, what will be the trigger?

Jun: In the May results call or in February, Idekoba said the difficult situation will continue for one year or more, and that is the case for this fiscal year. So this led to questions about what will happen next fiscal year, or in the calendar year 2024? So I think that is where your question is coming from. So it's not just the fourth quarter numbers, but it is even beyond that, we are trying to cautiously ascertain the outlook and how we spend. As of today, we do not think the economy will turn upward and lead to a significant revenue increase.

Even if the fourth quarter revenue is stronger than we anticipate, that will not be a substantial uptick. So for now we will steadily invest where necessary in a low-key manner and prepare for the next upturn or downturn. So our view remains unchanged.

We don't know what the revenue will look like in the fourth quarter. But short term, even if the margin hits 30% or 35%, we will keep that behavior in managing our business. If we can clearly see the bottom we may take such action, but we don't know where the bottom will be. So we're not thinking of such action yet.

Tanioka: Thank you.

Shen: CLSA Kato san, please go ahead.

CLSA Kato: This is Kato speaking. I also have a question on HR Technology. Minus 18% is projected in Q3 and the second quarter result was the same and also for October. So I think you see it in the same way in November and December. Is that because last year's comparable is going to be lower or is PPSA contribution expected to be more, resulting in minus 18%. What is the assumption here?

Jun: As I responded earlier, the pricing model change is neutral. That is the basic assumption. Supply and demand imbalances are easing and the economic situation continues to be tough. These are the two main factors.

Kato: Understand. What are the KPIs for you to identify the bottom? Is it, for example, the increase in job openings for three consecutive months?

Jun: Well, macro economic indicators are something we're focusing on. Idekoba is looking at those indicators to paint a picture of the future. So there is no one magic indicator. We are taking into account a combination of multiple factors. Of course, we have internal data and we also have public indicators like JOLTS. The increasing or decreasing job openings trends or something like that are important and what will happen from there. These are examples we pay attention to.

What is difficult to define is, what triggers our clients to think about restarting hiring.There may be a gap with the actual economic situation. Maybe some people will make a leap or some people are more cautious. So it's a very difficult decision, but we are referring to basically the same indicators that you are looking at. It's not something automatic, for example, if job openings increase for X months consecutively.

Kato: Understand. So in terms of the number of paid jobs, I think it was minus 50% for the second quarter, but how should we look at this in the third quarter?

Jun: I think it was a question from Munakata san that I responded to earlier. We have been carrying out those measures. So the drop or change of paid jobs as volume is no longer relevant to our revenue trend. So in my script earlier, we mentioned that we're no longer going to be disclosing that information. So I recommend that you shouldn't rely too much on that number. And going back to the original topic, according to Deko, the number of job postings is data for us to know what companies are starting to think. Thank you.

Shen: SMBC Nikko securities Maeda-san please.

Maeda: Hello, thank you very much. My question is on HR technology. Like you said earlier it will take some time for the labor market to normalize. The speed towards normalization seems to be mild, not plunging or declining rapidly. So it may take some time towards normalization. It may linger and may take a long time. So next year, if the top line does not bottom out, how much cost control do you have next year? You started reducing costs in the second half last year. So it may be more difficult for you to control your costs further. Please tell us your view on how long it will take to normalize and your cost control measures. Thank you.

Jun: So normalization, meaning the supply demand balance?

Maeda: Yes, supply demand tightness from the extraordinarily tight supply demand is now relaxing.

Jun: Thank you very much. At the moment we don’t have an assumption that the economy will suddenly turn upward and hiring will progress next year. I think you know better than me. Well, maybe you are assuming several scenarios: a hard landing or a deep dive or slow decline. We're also thinking of all these scenarios as we consider our next step. We don't know when the timing will be but when the market recovers we need to become stronger and bigger. So that is our only focus. No matter how long or shallow or deep it is, we are doing what we need to do.

But as we mentioned in March or May this year, we need to keep our discipline as a listed company, and demonstrate to the capital market what we are doing. So we must do what we need to do. But there are things we can do or we do not do in the short term and other things that we can do but not do for the long term. We have to hit the right balance.

Like we said last time, we will continue to invest in the talent and assets that will contribute to our future growth. Of course we take into account the short term view, but the biggest focus is how to grow when the economy recovers, that is the sole focus. And so whether the time is long or short, we will do what we need to do, we will not do what we should not do. We will not push ourselves too much to control our costs.

Maeda: Thank you. This may be a similar question. If the environment deteriorates, will you keep the discipline as a listed company and keep the margin at a certain level?

Jun: Like I say every time, we do not take certain steps to keep the margin at a certain level every quarter. But at the same time, we have a margin level that we have to keep as a listed company. So we have that perspective too. But we will not do everything to keep that level.

Maeda: I understand Thank you.

Shen: BofA securities Nagao-san, please?

Nagao: This is my second turn. So for the Matching & Solutions, I have a question about your view regarding the adjusted EBITDA margin for this segment.

In the second quarter in Marketing Solutions, adjusted EBITDA margin is approximately 30%.

And for HR Solutions, it's approximately 23% for the second quarter. Last year on the full year basis it was 25% for Marketing Solutions. So the margin has significantly improved for Marketing Solutions. What is the driver here?

And for HR Solutions, the margin in the second quarter was 23%. and last year on the full year basis, it was 12%. So this is again a significant improvement.

I believe this is not only coming from cost reduction, but also due to revenue growth, resulting in margin improvement for both segments of Matching & Solutions. What is the mechanism for this margin improvement? What is the most recent situation?

Jun: The revenue mix has been changing. In HR Solutions we have media and the placement service. The revenue breakdown is not disclosed. So I cannot explain what is the mechanism of the margin growth there. And I cannot say the same for Marketing Solutions.

But I hope you will remember from back in May. Last year, we made strategic investments in Matching & Solutions. And for that year, we didn't really mention the specifics of this investment, but in May we announced that the investments were made more in HR Solutions and we are not going to be making the same level of investment this year. I think that's what we explained back in May.

In HR Solutions, the gap of the margin comes from how we spend money. And of course in Marketing Solutions, we are using less money for investments compared to last year.

In Matching & Solutions, adjusted EBITDA margin was 14.4% last year.

But this year’s target is 20%. Marketing Solutions was around 30% and HR solutions was 23% for the first half of the fiscal year. That is the level of the margin. When we deduct the headquarter costs, the overall margin was around 22%. When we take into account the headquarter cost, there is a certain level of performance we need to achieve in order to realize 20% margin. So we have to control our spending and on the business side have to scrutinize the need for hiring so we can achieve a 20% margin on a full year basis.

Nagao: Thanks. One follow up. Adjusted EBITDA for Marketing Solutions disclosed in the past was around 27% at maximum. But in the first half, it finished at around 30%. So the cost is being controlled and revenue mix is improving, and you have been working on the SaaS solution business. Can I assume that its profitability improvement is also contributing here? Can you give us more color? Thank you.

Jun: The cost allocation has changed quite a bit from when we disclosed in the past. You cannot compare the margin from the past on an apple to apple basis with the current margin.

We had our headquarters cost allocated but to only a small degree in the past.

In the past, headquarters cost was smaller than today because the headquarters cost existed in each subsidiary and then we consolidated. So it is not an apples to apples comparison.

Still, we are taking various measures so that we can come closer to that level. We should be disclosing the margin on a consistent basis so that you can make a fair comparison. But that is currently not the case.

So what we are presenting today is lower than the previous basis. I'm sorry I cannot give you specific numbers, but I just wanted to call out that not a simple comparison can be made.

Shen: So the next and last question will be from JP Morgan securities Mori-san, please.

Mori: Thank you. I have two questions. First, on a consolidated basis, advertisement expenses for the first half was down by around 40 billion.

Usually you invest more in the fourth quarter. So the investment in the second half tends to be bigger than the first half. But last year, because of Indeed, the second half was smaller. Will this year be the usual year where the second half is bigger than the first half? In that case on a year on year basis, the advertisement expenses will not decline that much YoY.

Could you please elaborate?

Do you have any particular focus in your advertisement expenses this year? Last year, Recruit Direct Scout was the focus. Do you have any particular investment focus this year? That's my first question.

Jun: For Japan this year we are not investing with a particular focus, as I answered Nagao-san’s question, and that is why the margin is improving.

So that is my short, straightforward answer.

For the second half, as we mentioned, for the Japan business we think it's most effective to invest like we do every year. So it may not be as much as last year, but still we will have a bigger investment in the fourth quarter.

I'm not looking at these numbers on the consolidated basis, but rather on the segment basis.

The consolidated number is just a simple sum-up, but where the amount differs when comparing the first half and the second half is Matching & Solutions, so Matching & Solutions will have a bigger second half.

For Matching & Solutions, you are looking at the current margin and third quarter margin of 23% and multiply it by the revenue percentage. So, you can calculate the fourth quarter margin based on that and the full year forecast of 20%. So that is the amount we are planning to use.

Mori: The operating expenses are expected to remain stable, maybe with some increase due to FX. For advertisement expenses, there are not that many swing factors this year and there will not be much increase or decrease from quarter to quarter.

Jun: We are investing in a disciplined manner. Personnel is also being controlled. Because of the economy the return on the advertisement expenses may not be big. And so we naturally reduce the advertisement expenses.

Mori: The second question is related to Indeed FutureWorks.

You spoke a lot about AI. So there are things you've done in the past and new products are being launched in Spring. When we think of AI utilization in HR Technology as a one big theme, is it being used to improve the surface or, new products that will be launched next Spring are asking clients to pay a fee for the added value. Is it for enhancing usability or, by using AI, can you increase TAM? Could you share your view on that?

Jun: As you correctly said, by offering better service to the users and the business clients, we hope to benefit in the long run. This is what we are doing through various trials and errors. We have done many things and analyzed the numbers.

People at Indeed are thinking how to evolve and improve the services by training the machine with language. Beyond analyzing the numbers, what can we achieve?. That's what Idekoba and I talked about yesterday.

I expect Idekoba will have such discussions with you in the future. We can do more things, more new things in the future.

In HR hiring business, the personnel cost to total cost ratio is high, because the processes are being done manually to match people. So more people are needed to increase revenue. So it has been a high personnel cost business for higher revenue.

By improving the clients' convenience, we also improve our efficiency. The traditional industries will have higher potential while more advanced industries may not have so much room for improvement.

Hiring used to be slow or lagging behind in automation and we can do more. And that's what Idekoba is talking about. Our business has a very promising discussion and as we announced before, we want to do many things. It's very exciting. So to answer your question, despite good or bad economic situations we want to and we should invest in this area no matter what. We have this strong commitment because we think we are the only ones who can do this for the future in this HR industry. I hope we can share with you more specifics in the future.

Mori: Thank you very much. I look forward to it.

Shen: Last but not least, let me announce an upcoming IR event. Coming Friday December 15. Svenja Gudell, Indeed Chief Economist and head of the Indeed Hiring Lab, will host a webinar session to discuss global labor market trends. The event will last approximately one hour, with a presentation followed by a Q&A session. Details about this event will be posted on our IR site tomorrow. We hope that you can attend this event and take advantage of this opportunity.

[END]

Forward-Looking Statements

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.

Please note that significant differences between the forecasts and other forward-looking statements and actual results may arise due to various factors, including changes in economic conditions, changes in individual users’ preferences and business clients' needs, competition, changes in the legal and regulatory environment, fluctuations in foreign exchange rates, climate change or other changes in the natural environment, the impact of the spread of COVID-19, the occurrence of large-scale natural disasters, and other factors.

Accordingly, readers are cautioned against placing undue reliance on any such forward-looking statements. The Company has no obligation to update or revise any information contained in this document based on any subsequent developments except as required by applicable law or stock exchange rules and regulations.