

Recruit Holdings Q4 FY2021 Sell-side Analyst Call
May 16, 2022

Question & Answer

Shen: Our first question comes from Mr. Kinoshita from BofA Securities.

Kinoshita: I have two questions.

The first question is about the share-based payment expenses. For this time, you will use your treasury stock that you have now as resources, but I think you said that you would also consider buying stocks from the market when you announced this stock incentive plan. Even if you don't have an answer to this question, I would like to ask you to explain your thought between buying stock through the market or making use of the treasury stock that you presently own.

Arai: Actually, I would like to ask Deko to answer questions as much as possible, but since this is kind of a technical question, let me answer. Every year from February to May, we consider and decide on how to allocate capital.

As of today, we have 86 million shares of treasury stock, and when we think of ways to use them beneficially, one of them is to allocate them to share-based payment expenses.

Of course, if the stock price is very low and the stock price is lower than when we bought the treasury stock, it may be appropriate to buy the treasury stock from the market and use it for share-based payment expenses. However, in a situation where there is an abundance of treasury stock, I think that in many cases, using treasury stock is the right thing to do.

However, on the other hand, there may be a business that would like to use the treasury stock to acquire a Japanese company.

In that case, the priority would be on the demand from the business side, but the timing of the actual issuance of shares is much later.

So, as I mentioned earlier, it does not mean that the 86 million shares will be depleted immediately. We will consider how to collect shares either using treasury stock or purchasing from the market, depending on the stock price of each time.

Kinoshita: I understand. If possible, I would like to ask Deko to answer.

Since the issuance of new shares is moderate, you are saying that treasury stock will be fine as resources, but the impact on ROE and other factors will be basically limited, so you think that is fine?

Deko: As Arai just mentioned, I think the impact on ROE will be limited, and we are also benchmarking with US technology companies and others to see the level of compensation or stock compensation. We are still trying to make sure that the level of compensation is still at an acceptable level compared to the past.

Kinoshita: I understand. The second question is also a technical one, but I would like to ask about the increase in share-based payment expenses, because you introduced a large amount of share-based payment expenses this fiscal year, and the full-scale introduction of stock-based compensation will have a serious effect on the increase. Is it correct to understand that the increase will be gradual?

Arai: As a mechanism, there is a considerable time lag between what is recorded as an accounting expense and the increase in stock grants as you asked about earlier. So we are assuming that the increase in the number of shares will be about approximately 0.3 percent of the current net number of shares for this stock compensation.

Therefore, the increase in the number of shares is not going to be so sudden that we will use all of the current treasury shares.

As for your first point, the system is like an inverted pyramid, where the time line flows slowly, and the expenses are processed slowly.

If employees stay with the company longer, if they do not quit during the course of their employment, and if the number of employees increases, the expenses will naturally increase. As the company grows, the cost will increase, and the cost of the benefits granted last year or this year will be applied to a certain part of the company next year.

Although I cannot make any assurances since it depends on the exchange rate, I think the increase will be at that level, such as approximately 70 billion yen this year will probably exceed 100 billion yen next year.

Kinoshita: You give a little bit each year to those who are there.

Arai: We don't give it to those who quit. The incentive package is like that, so now you get it for 4 or 5 years, but if you quit, the right is gone.

Kinoshita: Thank you very much.

Shen: Next question comes from Mr. Takeuchi from Jefferies Securities.

Takeuchi: I'd also like to ask two questions.

Based on the data you disclosed, I was wondering if you could give us a look back at Indeed's growth to date. Thank you very much for the additional data.

Compared to March 2019, I think your revenue has increased by 2.5 times, but what was surprising was that the number of monthly unique users was 250 million, which was not that much change from 3 years ago. On the other hand, the average number of recruits per minute has probably doubled since then, so it seems to me that the growth in sales to date has been driven more by conversions from the site to recruiting than by the site's overall traffic, and the growth has been in a unit-per-job kind of way. Is this understanding correct? And what do you think will happen to the content in the future?

This is the first point. Thank you very much for your cooperation.

Deko: The number of unique users is a bit of a tricky indicator on the Internet, especially in recent years when it has become difficult to obtain cookies, and many companies have stopped using the number of unique users.

What we look at as an important indicator is not so much the number of unique users, but rather a deeper level of engagement. For example, the number of logged-in users is steadily increasing, especially for apps, because logged-in users are able to use many additional functions.

Conversely, in the United States, for example, there are many developed countries, such as the United States, Canada, and the United Kingdom, where a huge number of people are using the application. We have been doing this for the past three to four years without assuming that this will be the case. In other words, we are working to increase the depth of engagement.

As a result, users who are logged in to our apps, for example, are receiving search results and recommendations that are more relevant to them, and as a result, the number of recruitment signals is increasing.

Takeuchi: I have an additional question. Is the ratio of app users going up?

Deko: I don't think we disclose the percentage of app users, etc., but it is steadily increasing. I understand that this is due to the increase in mobile users rather than the increase in Internet users.

Takeuchi: Thank you very much. Secondly, I would like to talk about the investment and changes you are trying to make in the area of human resources for media solutions.

What impressed me was that you are planning to spend about 40 billion yen this fiscal year on upfront investment in the human resources area of the media solutions business. What kind of changes are you planning to make through the investment in this area? Could you tell us about your strategy in this area and your current situation? That is my second point.

Arai: First of all, before Deko answers, this 40 billion yen is divided into three components. One is the marketing expenses for the human resources area that you just mentioned. The other is marketing expenses in the area of sales promotion. I mentioned 30 billion yen for these two components, and 10 billion yen for the system investment. The total of these is 40 billion yen, so I would like to first confirm that not all of it is for human resources.

Deko: The speed of recovery in the human resources field in Japan has been quite slow compared to other countries. I believe that the additional marketing expenses are based on the expectation that the human resources field will recover in the future.

In addition, we are currently deepening our partnership with Indeed and other HR tech companies in the HR domain and M&S in the HR domain, mainly in the area of recruitment technology. We are currently deepening our partnership in this area. We have seen in various test results that matching can be done quite efficiently mainly in this area. If we can achieve this level of success in this area as well, we will invest a little more. Since the matching efficiency is increasing, we are increasing the investment that we expect to be able to recover.

These two points are the reason why we are increasing the size of our investment plan.

Takeuchi: I understand very well. Thank you very much.

Shen: Next question from Mr. Kishimoto from Mizuho Securities.

Kishimoto: Thank you very much for your explanation. I would also like to confirm one point about Media & Solutions.

In the current fiscal year, you said that the margin would be 20% on a normal basis, but that it would be pushed down due to the prior investment you mentioned earlier. Or, since marketing, system renewal, and other issues must be tackled over multiple years, next fiscal year's costs will be commensurate with the next fiscal year, and should we expect margins to be a little lower than before Covid-19, at around 10%?

We can still expect the top line to recover in the next fiscal year, so just tell us how you think about the margin when sales recover after this period. This is one question.

Arai: What do you mean by next fiscal year?.

Kishimoto: The fiscal year ending March 2024. I'm afraid it's a little ahead of schedule.

Deko: We would like to look at the situation over the medium to long term and make investments based on whether the position is working out well.

As I mentioned earlier, we have been investing in the dining, travel, and bridal businesses. As I mentioned earlier, the recovery of these businesses, which have had very high profit margins in the past, is still lagging behind. We should take advantage of the recovery timing to acquire the user base and customer base, as these businesses have high repeating users and customers.

As a result, we do not know how much profit we will make in the next fiscal year compared to the current fiscal year, since there are still some uncertainties, including the economic situation. However, we are spending marketing costs based on the number of users and the lifetime value of each user or customer. I hope you understand that we are thinking in terms of a larger framework of medium to long term investment, and profit will recover after revenue recovers.

Kishimoto: Okay, one follow-up question: the marketing costs that are expected to be incurred this fiscal year, can we assume that they will have the effect of boosting the top line to some extent during this fiscal year? Are you talking about a little bit further ahead, meaning after the next fiscal year, after the fiscal year ending March 2024?

Deko: It depends on the business. For example, for users, traveling and dining are relatively frequent, but bridal is not so frequent. These businesses are expected to recover to a certain extent in the short-term, so some level of marketing expense is planned. The other way of thinking is "lifetime value" which we think for medium- and long-term rather than short-term, and is expected to be more than 2020, pre Covid level.

Of course, we do not yet know what will happen with the government-led campaign, but we will monitor the situation and strengthen our marketing activities accordingly.

We expect to be a little more flexible this fiscal year, including in this area. Did I answer your question?

Kishimoto: Yes. I understand very clearly. Thank you very much.

Shen: SMBC Nikko Securities, Mr. Maeda, please.

Maeda: Thank you very much for your time, I have two questions.

The first question is a technical one: how should we rethink the impact of exchange rates? There are various types of currencies such as the dollar-yen, euro-yen, pound-yen, and Australian dollar, etc. I think there are some areas where you can be helped by exchange rates this fiscal year. This is the first point.

Arai: Let me first answer the technical aspects of this question. First of all, we are assuming 120 yen on a dollar basis, which will change if the current situation continues, but if we make a rough estimate, we can assume that a 1 yen change in the dollar-yen exchange rate will naturally lead to changes in other exchange rates, and this will have a roughly 3 billion yen plus or minus effect on profits. This is a rough image of the effect on profit.

Since we don't manufacture anything and do not import or export anything, we do not expect a large change in adjusted EBITDA margin due to rate fluctuations. However, if it is possible that sales will increase or decrease in real terms, and that adjusted EBITDA margin will increase at the same levels .

Therefore, 1 yen change in the dollar-yen basis will result in a 3 billion yen change.

Maeda: Thank you very much. The second question is about HR technology. I think that client's costs are rising in this environment, but do you feel that the level of satisfaction with your company is increasing when compared to your competitors?

There is a possibility that this kind of environment will continue structurally. In the U.K., I think that the mismatch of human resources and supply and demand is further progressing, and in the U.S., too, it is not going to be resolved for some reason, so I think that there may be some structural aspects to the situation. Could you tell us about your clients' current reactions and future prospects?

Deko: Thank you very much. It is very difficult to raise the level of satisfaction in an environment where there is a mismatch. In our various surveys, it is not that we are the only ones who are suffering, but rather that the overall situation is deteriorating.

For example, in the case of dispatching workers to countries such as the U.K. and Australia, where they used to rely heavily on immigrants for essential workers, the number of requests from clients has increased

tremendously, but we have been unable to fill those requests at a cost that clients accept. However, they are not able to fill these requests in a way that is cost-effective.

In the end, there are situations in which orders are being cancelled if the satisfaction level of the customer is lowered.

There are various studies on the future, but in the medium term, most of the studies indicate that the problem cannot be solved immediately, and we ourselves agree. The main problem is the aging population of workers in developed countries.

Also, although it would be wrong to say that this is particularly true of young people, through the Covid-19 pandemic, there is a growing diversity of views on work-life balance in many countries. As a result, I think the current situation is that no matter what they pay, not all customers will be able to fill their hiring demand as in the past, and I understand that this situation will continue for a while longer.

Maeda: Thank you very much.

Shen: Next question comes from Ms. Mori from JP Morgan.

Mori: I would like to ask two questions, both relating to HRT. I would like to confirm what you intend with the growth in revenue per paid job advertisement.

I understand that you are changing from CPC to CPA, but I would like to know more about the trend of revenue per paid job advertisement as Mr. Arai explained earlier.

Deko: I would like to talk about that part.

For example, we are expanding the scope of our testing. For some of our clients, we are now offering a cost-per-application (CPA) service, in which applicants are checked within 48 hours by them and we charge them if they are satisfied with the applicants. This is what is called "cost-per-application," or CPA.

It is very rare that a large client who has 100 or 1,000 jobs and 2,000 applicants per day needs to judge within 48 hours. The number of CPA clients, mainly small businesses, is increasing.

Therefore, it is no longer easy to disclose how much the CPC has increased as a unit price, as is done by other Internet companies. We are looking at if the amount paid per job is increasing.

Mori: Thank you very much. I apologize if I misheard you, but sales revenue per paid job advertisement increased by 16%.

Arai: That is correct.

Mori: This is the actual results for the period that ended, and that will be the main driver of revenue growth for this fiscal year?

Deko: That is how we intend to do it.

Mori: I understand. You do not expect it to fall, at least.

Deko: We expect that the volume of paid job advertisements will be slightly lower to some extent than last year's peak level.

Mori: I understand.

The second point is about the recruitment automation market. I think it is a fairly large market, but how much revenue do you recognize in your HRT business from this market?

I have a rough idea of the scale of Indeed Flex sales, and I think it is around 30 billion, but is it close to this figure or is it much larger depending on how you define it? This is the second question.

Deko: The figures here were calculated by a third-party organization. To put it simply, for example, Indeed has several hundred employees in its talent acquisition team, or so-called "recruiting team". These people perform a variety of manual tasks, and the third-party organization's figures are based on the assumption that there will be a certain amount of automation to replace these manual tasks in the future.

This is a figure that can be reasonably considered that the work process will change without increasing the number of talent acquisition teams through automation.

Therefore, it is not so much a question of who is taking the market now, but who will be able to take the market in the future. This is also difficult because it is close to the so-called productivity index, which is similar to the SaaS market. I am not sure who is taking the money, but I think it will go to various places in a way that it will somehow blend in.

We are close to the upstream process of hiring. We actually check the resumes of applicants, set up interviews for them, and conduct assessment tests, and this kind of automation is actually used by many companies. We know that our clients who use such functions as SaaS generate many times more revenue per job.

We hope to increase the percentage of such customers, and as a result, we hope to take a certain market size.

Mori: Thank you very much.

I think you are mainly referring to Indeed Hiring Platform, but when you talk about revenue per job for companies using Indeed, do you think that increasing advertisements through Indeed would be the biggest contribution to raising revenue per job? Or is it more effective to receive payment for the functions like SaaS services that you mentioned earlier?

What you are thinking about now and in the future may differ, but I would like to ask you about your thoughts.

Deko: IHP is a product for large enterprise clients who use various types of SaaS, and each contract is large. A similar version for small- and medium-sized companies can be used as SaaS platforms that directly post jobs.

So, in the end, I think it will probably be both. However, in terms of the speed of penetration, the so-called self-serve type for small and medium-sized companies, where the customers themselves decide to use this or that, is usually faster than the type for large companies. In the short term, I think this will have a larger impact on overall revenue.

Mori: Yes, I understand very well. Thank you very much.

Shen: Next question comes from Mr. Tsuruo from Citigroup Securities.

Tsuruo: First, I would like to ask you how you incorporated risks such as the macro environment and competition into this fiscal year's performance. Of course, you are discussing various issues by segment, but as macro risks and conditions are changing and your company operates globally and has touch points with many employers, how much of a risk do you see from macro environment such as interest rates, geopolitical risks, and rising input costs, and how much do you put the risk into your guidance this year?

I would like to know what the key issues are now that you have been CEO for a year.

I assume that the hiring and the costs associated with that is a very big issue, which is why the definition of adjusted EBITDA has been changed.

Deko: To answer your first question, thinking to what extent we and probably as well as other companies can incorporate the changing elements of the macro environment into the figures, the basic premise is that we do not assume that something like the Lehman Shock will occur during this fiscal year.

For example, the forecast of the number of job openings in the U.S. that some companies and we are assuming is based on that there will not be an extremely severe recession like the Lehman Shock during the current fiscal year, and that the current tight labor market will gradually ease in terms of changes in the labor participation rate and the number of job openings.

Therefore, if I were to answer your question, I would like you to draw a linear line based on the trend over the past six months or so.

As for your second question, in terms of what I consider to be the most important issues at the moment, the answer may be slightly opposite to the answer I just mentioned. I still think that the situation is overwhelmingly uncertain, and various people are saying that the probability of entering a recession this year or next year is "X" percentage points.

The most important thing for me as CEO is that we have survived many recessions in the severe economic environment over the past 60 years. Each time, we have been able to increase our market share. We believe that it is very important to make use of the experience we have gained over the years to continue to make investments to a certain extent in areas where we can gain market share over the medium to long term precisely because when the economy is in a bad condition, the same conditions occur for everyone.

I am aware that I may be criticized by various people if the economy should take a turn for the worse, but I think it is important that we continue to make medium- to long-term investments.

Tsuruo: Thank you very much.

Shen: Next question comes from Mr. Watanabe from Mito Securities.

Watanabe: My name is Watanabe from Mito Securities. I have two questions.

The first question is about the concept of HR technology for FY2022 and FY2023. You expect the revenue will increase by 10 to 20% in FY2022. Since we can see some increase in sales revenue per client, is it correct to say that you should be able to achieve about 20% growth, if the current favorable market conditions do not slow down?

For example, your company will hire a large number of new employees in FY2022 and will engage in a variety of other businesses. While we have seen growth of about 30% due to market conditions, are you aiming for even greater growth in terms of the business for FY2023?

Deko: I would like to answer that question myself.

First of all, the guidance of revenue in FY2022 should be based on the same concept as you mentioned. For medium to long term, we are transforming the pay-for-performance model from CPC, CPA, to CPQA, which means that if the applicant is a good candidate, we ask clients to pay for our service.

In the domestic and global HR market, there are many companies that are making hundreds of billions of yen in sales by charging 25%, 30%, or 35% of the total cost per hire for recruitment and staffing services.

Compared to them, we are still not charging even 1% of salary. For example, as I mentioned earlier, we are gradually learning that if we ask clients to pay us in case they like the applicants, we can gain more than charging for the clicks.

Ultimately, I think it is important in the medium to long term to change our way to charge if the clients are satisfied, like Cost Per Hire.

In order to put this into practice, we need to know various insights of users, what kind of trends the companies are adopting to hire, or what kind of jobs each individual wants to get, to increase the accuracy of matching.

This is what a human recruiter is doing in the end. The recruiters assign a person as they know the staff well. As the level of automation increases, and as a result, for example, if we can get 2% or 3% of the salary instead of 1%, our revenue will increase by 2 or 3 times.

We know that we are not yet at a level of matching accuracy that can compete with humans, so it will be important to further evolve this area by combining humans and AI, and if we can do this successfully, we will be able to increase revenue to some extent. I hope I have answered your question.

Watanabe: I understand very well.

My second question is in the area of domestic HR Solutions in the Media & Solutions segment. I would like to confirm that your company's competitiveness is not declining amid the emergence of various new companies.

Deko: We are engaged in a very large number of HR businesses in Japan, so it is difficult to say which service or product is losing competitiveness.

However, when we look at the overall market share, I think the companies you are referring to are emerging Internet companies, but the size of their sales is quite small in comparison. The data that we are checking, looking at the overall market size, does not show that we have lost much sales share at all.

I have a feeling that there is a difference between sales of hundreds of billions or sales of about 500 million or 1 billion growing at double the rate, but I am not aware of any overall decline in market share at this point.

Watanabe: I understand. Thank you very much.

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