THIRD QUARTER 2022 HIGHLIGHTED HOLDING: RANDSTAD

Economic uncertainties have staffers on high alert; we believe there's no agency better positioned to weather a potential downturn and continue expanding its market share than global HR giant Randstad.

Randstad is the world's largest staffing and HR services agency[1]. As brokers for the job market, staffers' earnings are naturally tied to the employment cycle, generating higher profits when demand for labor is strong and wages are rising. On the surface, Randstad may appear interchangeable with staffing peers; however, we believe the market is overlooking the company's differentiated technology and scale advantages — the result of a multi-year, full-cycle investment campaign intended to grow the business organically.

WELL-POSITIONED AND RESILIENT

As we laid out in our Commentary section, Europe (Randstad's largest region) is dealing with a deteriorating economic outlook, and most market prognosticators believe that a recession is on the horizon, if not already here. Should this be the case, we believe Randstad is much better positioned for a European downturn than the market gives it credit for; not only because of its geographic diversification (~36% of EBITDA[2] is generated outside of Europe), but because management has shown a penchant for seizing market share from marginal players at the bottom of economic cycles. Investors have nonetheless pushed down sector valuations — specifically Randstad's, which is trading at a forward EV/EBITDA[3] multiple last seen during the GFC[4].

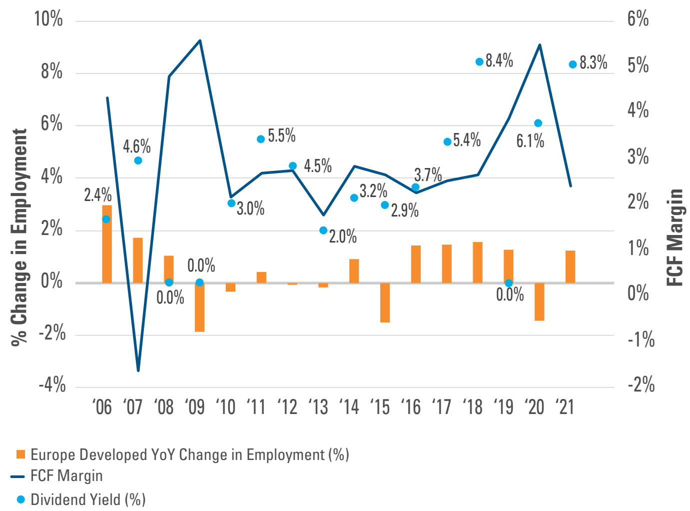
A recession clearly is not ideal for any staffer; however, from a risk perspective, Randstad is as sound as a company can be entering a downturn. An asset-light business model, counter-cyclical cash flow profile, and a pristine balance sheet with almost zero net debt (excluding leases) means the risk of capital impairment is extremely low. The stock also boasts a near 5% dividend yield, with potential upside from a supplementary special dividend[5], providing added cushion for investors. During prior periods of labor market stress in Europe — namely 2009, 2015, and 2020 — Randstad's cash flow countercyclicality was evident, as the company was able to generate positive free cash flow and flex its dividend as needed (Figure 1). Randstad also exhibits notable earnings

		Earnings Per Share			Price/Earnings		
	Price	FY22E	FY23E	Normal*	FY22E	FY23E	Normal*
Randstad	€44.58	€4.55	€4.19	€6.49	9.8x	10.6x	6.9x

*Fiscal year-end September 30. *Pzena estimate of normalized earnings. Source: FactSet, Pzena analysis. Data as of September 30, 2022*

stability, generating positive EBITA[6] in each of the last 19 years, with margins bottoming at 2.5% during the GFC versus a historical average of 4.1%[7].

Figure 1: Randstad's Countercyclical Cash Flow Profile



Source: FactSet Economics Standardized Database, FactSet Fundamentals, Pzena analysis

"TECH AND TOUCH" IS A WINNING FORMULA

What is particularly compelling, is the long-term revenue growth opportunity available to Randstad because of its differentiated business model and financial strength.

Randstad operates in a highly fragmented industry with scores of independent mom-and-pop conventional recruiters mostly servicing small and medium enterprises, as well as a few large, global players — namely Manpower and Adecco. Management's strategy to outgrow rivals was to develop a modernized "tech and touch" approach without abandoning its core identity as a temporary staffing company. This required years of investment

1. Company filings, Pzena analysis, 09/30/2022
2. Earnings before interest, taxes, depreciation, and amortization (Adj. EBITDA); company filings, Pzena analysis
3. Enterprise value/EBITDA
4. Monthly EV/EBITDA – FY1, FactSet
5. Randstad typically pays a special dividend (at management's discretion) if net leverage remains under 1x EBITDA
6. Earnings before interest, taxes, and amortization (EBITA)
7. Company filings, Pzena analysis

in digital transformation to enhance the customer experience (both candidates and employers) and better utilize candidate data. To accomplish this, CapEx[1] spending increased beginning in 2016, growing at a 12.5% CAGR[2] through 2021[3]. Most of the cash was diligently spent on building software to enhance Randstad's value for large clients requiring data-driven insights into global talent pools. Two examples include:

- A pre-screening chatbot using AI with human oversight, allowing Randstad to effectively respond to 100% of applicants around the clock. This software, developed in-house, led to a 76% year-over-year increase in interviews scheduled while raising the speed of presenting talent to hiring managers by over 50%[4].

- The company's proprietary interactive labor market dashboard, Randstad Market Insights, aggregates troves of data from third parties, governments, and Randstad itself, providing hiring managers with a detailed and exhaustive rundown of precisely where the available talent is, what they need to pay for it, and what the market demand is for that talent.

According to Randstad Sourceright's 2022 Talent Trends report, 73% (highest level on record) of hiring managers today are investing in analytics — a valuable resource that less IT-equipped traditional staffers are unable to provide.

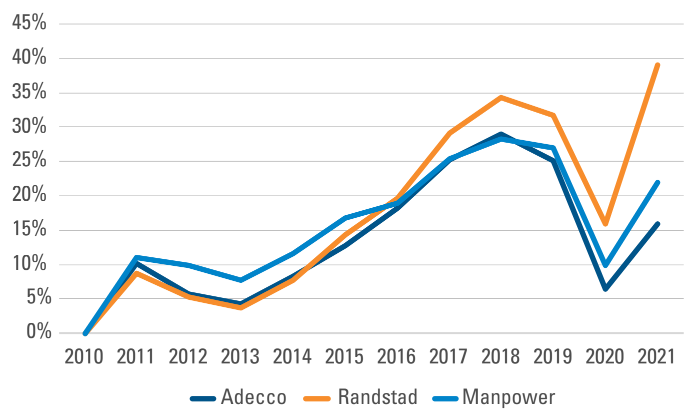
On the "touch" side of the equation, Randstad was quick to realize that embedding itself within the client's day-to-day operations, effectively acting as an outsourced HR consultant, creates customer stickiness and a higher level of value-add. As part of its In-house Services offering, Randstad sends its consultants to work on-site at a client's location, exclusively for that client, providing and managing a large number of candidates — particularly useful for companies needing to hire a high-volume workforce with very similar profiles. Currently, Inhouse Services constitutes 24% of Randstad's sales, and the business grew 13% organically year-over-year in 2Q22 versus 9% for the entire company[5].

1. Capital expenditures (CapEx)
2. Compound annual growth rate (CAGR)
3. FactSet, Pzena analysis
4. May 2021 company presentation: responsible AI for Labour Market Matching
5. Company filings

Randstad has also been exceptionally forward-thinking in capturing opportunities to support the "gig economy", for example through "employee compliance as a service", which leverages their ability to process candidates, screen for work eligibility, and perform other onboarding functions at scale. Management views the estimated EUR 61bn gig staffing market[6] as a major long-term growth driver for the company.

These are just a few examples of the investments Randstad has made to scale its portfolio of services and offerings to chip away at its rivals' market share. The benefits of these investments started off small; however, minor, tangible differences in growth rates compound over time. In fact, from 2011–21, Randstad grew 3.3% organically per annum versus 1.6% and 2.0% for Adecco and Manpower respectively. Presently, Randstad is 14–20% larger organically than those peers than it was a decade ago, and those growth differentials have continued to widen in the past five years (Figure 2).

Figure 2: Outgrowing Rivals
Cumulative Organic Revenue Growth



Source: Company filings, Pzena analysis

UNRIVALED SCALE, BREADTH, AND REACH

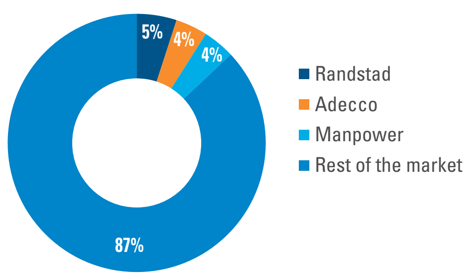
It is worth detailing exactly how Randstad measures up in the context of the massive global talent acquisition market. The staffing giant maintains operations in 37 countries, manages over 660,000[7] temporary employees globally, and offers everything

6. Randstad 2021 CMD slides
7. Company filings

from traditional staffing functions to professional recruitment (headhunting), to HR services (recruitment process outsourcing and consulting). Independent agencies, which make up the bulk of the market (Figure 3), rely on their intimate knowledge of local customs and languages to generate business. This serves them well with small, private clients in localized settings; however, they lack the presence and expertise in multiple disparate geographies that larger corporate multinationals source talent from, as well as sophisticated IT infrastructure for onboarding and administrative purposes. This is where Randstad excels, and a space where mom-and-pop shops simply cannot be competitive.

Figure 3: Global Market Share 2021

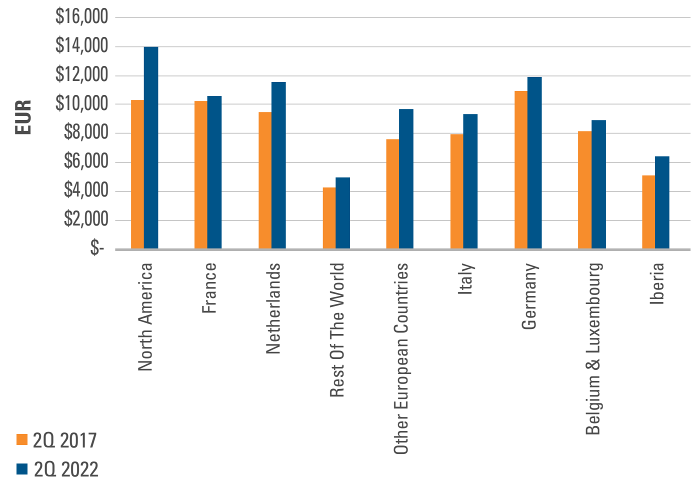
Total HR Services Market: EUR 476 Billion



Source: Randstad estimates, 2021 Bloomberg consensus and 2021 SAI reports

The reality is that Randstad is one of only three truly global staffers — along with Adecco and Manpower — with the ability to serve multinational corporations, who currently make up approximately 25% of company sales. In addition to management's focus on internal investments to spur growth and boost efficiency, the C-suite has organized Randstad's culture and sales incentives around promoting whichever service offering maximizes their value-add to the customer. These initiatives are yielding results not only in Europe or the United States, but worldwide (Figure 4)[1]. Today, Randstad is profitable[2] and growing organically in every one of its reported regions — a feat its rivals cannot claim. Assuming modest revenue growth and a more normalized mix (as above-trend high-margin permanent placement fees mean revert), we still arrive at a current valuation of just ~7x our normal earnings estimate.

Figure 4: Randstad's Revenue per Employee



Source: Company filings, Pzena analysis of Rev. by region per employee (corporate + temp. staffing)

CONCLUSION

Investors are fixated on macroeconomic headwinds instead of the idiosyncratic value proposition for a uniquely positioned market leader. We believe a downturn, although painful in the short term, can be an opportunity to gain market share for a structural winner such as Randstad.

In the early days of the COVID-19 pandemic when global GDP plummeted and unemployment spiked, Randstad responsibly dialed back its operating expenses — not only because it was the correct thing to do fiscally, but because it could afford to. Randstad had already made its investments in prior years, taking action ahead of its rivals, and it is manifested in superior organic growth and higher profits. These initiatives have today resulted in a full service, multinational talent acquisition giant with clear advantages over both pure online recruiting platforms and smaller mom-and-pop competitors. We believe Randstad is operating in the perfect space to exploit appreciable long-term share gains, which the market is not recognizing, given the stock's valuation.

1. Company filings, Pzena analysis
2. Adj. EBITDA per region, 2Q22

FURTHER INFORMATION

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