

ADP

# F2Q brings some relief; maintain Neutral

Maintain Rating: NEUTRAL | PO: 243.00 USD | Price: 238.59 USD

## Solid 2Q with no negative surprises; multiple is full

We are a little surprised at the degree to which ADP shares are trading up following the F2Q print. Both the top and bottom line modestly beat Street expectations, however the full year revs/EPS guide was unchanged. A few metrics were tweaked slightly but overall there were no material negative surprises in the print and the PEO business finally stabilized. Fundamentals are fine, but employment and rates could flip from tailwind and to headwind, and we believe valuation is full at ~26x C24E P/E. Maintain Neutral.

## Top-line slightly ahead on ES and PEO segments

Revs in both the Employer Services and PEO segments of \$2,899M/\$1,544M, respectively, came in slightly better than BofA and consensus estimates of \$2,857M/\$1,544M and \$2,883M/\$1,539M. Adjusted diluted EPS came in at \$2.13 vs. BofA/Street at \$2.11/\$2.10 despite a \$0.04 tax headwind.

## PEO stabilizes following some recent challenges

PEO revs grew 2.8% YoY reflected stability and in-line performance following some disappointment in recent quarters. F24 PEO revs guide of 3%-4% growth was unchanged. Any F2H acceleration is likely to be modest, as modest in-year benefits from strong PEO bookings is offset by softer PPC. ADP narrowed the full year PEO margin guide to the lower end of the range (now expect y/y decline of 80-100bps vs. 50-100bps prior) mostly due to diminished benefits from works' comp reserve releases.

## ES performance remains solid

F2Q Employer Services (ES) revenues grew 8% YoY (7% constant-curr), in-line with Street and slightly ahead of BofAe. Core ES revenue growth of 7% was in-line, while float income growth of 20% trailed BofA/Street at +27%/24%) as rates softened. Mgmt maintained the F24 ES revs growth guide of 7-8% as comps are more difficult in 2H. Based on YTD performance we think the higher end has become more likely. ADP slightly improved its F24 ES retention guide to down 40bps-60bps from down 50bps-70bps. ADP suggested ES bookings were solid in F2Q, but F24 guidance of 4-7% was maintained.

## A couple of small F24 guidance tweaks

The F24 adjusted EBIT margin guide was narrowed to 60bps-70bps of expansion vs 60bps-80bps prior, implying pressure in 2H as rates have moderated. ADP lowered the outlook for client funds revenue to \$985M-\$995M from \$990M-\$1,010M to reflect the evolving rate environment.

31 January 2024

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### Stock Data

Price	238.59 USD
Price Objective	243.00 USD
Date Established	17-Jan-2024
Investment Opinion	B-2-7
52-Week Range	201.46 USD - 256.84 USD
Mrkt Val (mn) / Shares Out (mn)	98,681 USD / 413.6
Free Float	99.6%
Average Daily Value (mn)	395.68 USD
BofA Ticker / Exchange	ADP / NAS
Bloomberg / Reuters	ADP US / ADP.OQ
ROE (2024E)	105.8%
Net Dbt to Eqty (Jun-2023A)	25.8%
ESGMeter™	High

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Timestamp: 31 January 2024 12:57PM EST

## Price objective basis & risk

### ADP (ADP)

Our \$243 PO is based on a 50/50 combination of a 24x PE multiple to FY25E EPS and our DCF model. Our 24x PE multiple represents a premium of nearly 30% premium to the S&P 500, consistent with ADP's long-term average. We think this is appropriate as we balance the general stability in ADP's core business with the current cycle for employment and rates. Our DCF uses an approximate 3% terminal rate and a 9% WACC.

Upside risks to our price objective are: 1) stronger than forecast economic / employment backdrop - ADP's business model is tied to cyclical swings in US private sector employment. 2) better than expected margin / new bookings performance and 3) ADP is perceived as a high-quality company than can comfortably endure the unprecedented pressures from the pandemic.

Downside risks to our price objective are: 1) while ADP has a defensive business model, its shares have been tied to cyclical swings in US private sector employment, 2) potential for new competitive entrants or disintermediation through technical innovation, and 3) potential regulatory changes.

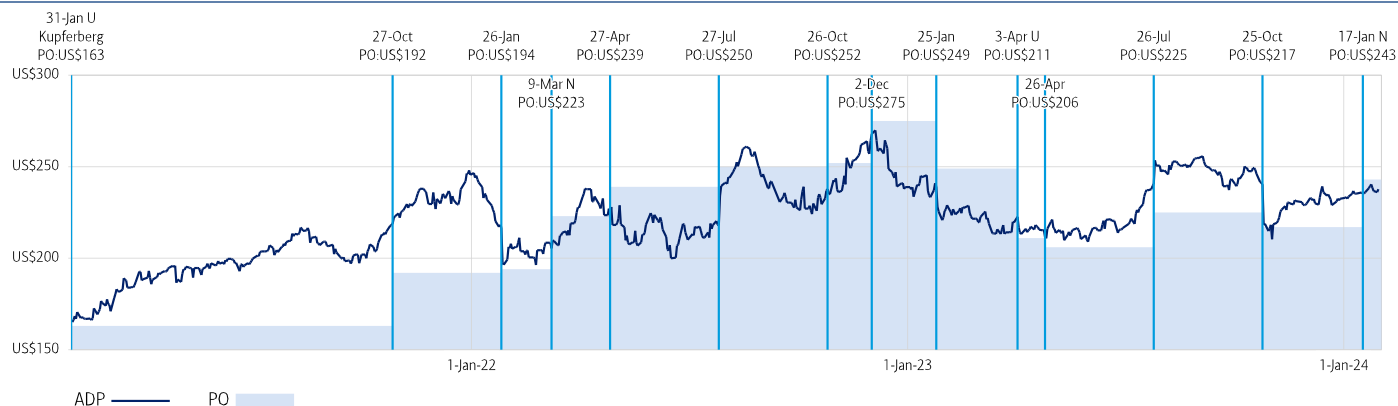
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Coverage Universe	Count	Percent	Inv. Banking Relationships <sup>R1</sup>	Count	Percent
Buy	215	53.09%	Buy	111	51.63%
Hold	97	23.95%	Hold	45	46.39%
Sell	93	22.96%	Sell	24	25.81%

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Sell	807	22.84%	Sell	383	47.46%

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