Automatic Data Processing, Inc. (ADP) CEO Carlos Rodriguez on Q1 2020 Results - Earnings Call Transcript

Oct. 30, 2019 3:12 PM ET
by: SA Transcripts

FQ1: 10-30-19 Earnings Summary

Press Release SEC *10-Q* *Slides*

EPS of $1.34 beats by $0.01 | Revenue of $3.5B (5.19% Y/Y) misses by $-21.76M

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Automatic Data Processing, Inc. (NASDAQ:ADP) Q1 2020 Earnings Conference Call
October 30, 2019 8:30 AM ET

Company Participants

Christian Greyenbuhl - VP, IR

Carlos Rodriguez - President and Chief Executive Officer

Kathleen Winters - Chief Financial Officer

Conference Call Participants

Ramsey El-Assal - Barclays

Kevin McVeigh - Credit Suisse

David Togut - Evercore ISI

Bryan Bergin - Cowen

David Grossman - Stifel

Jason Kupferberg - Bank of America

Steven Wald - Morgan Stanley

Bryan Keane - Deutsche Bank

Operator

Good morning. My name is Crystal, and I'll be your conference operator. At this time, I would like to welcome everyone to ADP's First Quarter Fiscal 2020 Earnings Call. I would like to inform you that this conference is being recorded and all lines have been placed on mute to prevent any background noise. After the speakers remarks, there will be a question-and-answer session. [Operator Instructions]

I will now turn the conference over to Mr. Christian Greyenbuhl, Vice President, Investor Relations. Please go ahead.

Christian Greyenbuhl

Thank you, Crystal. Good morning, everyone. And thank you for joining ADP's first quarter fiscal 2020 earnings call and webcast. With me today are Carlos Rodriguez, our President and Chief Executive Officer; and Kathleen Winters, our Chief Financial Officer.

Earlier this morning, we released our results for the first quarter of fiscal 2020. The earnings materials are available on the SEC's website and our Investor Relations website at investors.adp.com where you will also find the investor presentation that accompanies today's call as well as our quarterly history of revenue and pre-tax earnings by reportable segment.

During our call today, we will reference non-GAAP financial measures, which we believe to be useful to investors and that exclude the impact of certain items. A description and the timing of these items along with a reconciliation of non-GAAP measures to their most comparable GAAP measure can be found in our earnings release.

Today’s call will also contain forward-looking statements that refer to future events and, as such, involve some risk. We encourage you to review our filings with the SEC for additional information on factors that could cause actual results to differ materially from our current expectations.

Before turning the call over to Carlos, you would have noticed in today’s earnings that we made a correction this quarter to certain PEOs zero margin pass-through revenues that we have previously reported on a gross basis and which going forward will be reported on a net basis.

For consistency, we also revise prior periods and the total impact to fiscal 2019 revenues and operating expenses was $65 million. This does not materially impact our previously reported growth rates and does not impact consolidated earnings before income taxes, net earnings, consolidated financial condition or cash flows. To better assist you, we have also included the details of these adjustments in the appendix to the presentation that accompanies today’s call. Our supplemental schedule of quarterly history of revenue and pre-tax earnings by reportable segments also reflects the impacts of these changes.

Accordingly, our reported results and full year outlook and the following commentary from both Carlos and Kathleen also fully reflect the impact of these adjustments. As always, please do not hesitate to reach out should you have any questions.

And with that, let me turn the call over to Carlos.

Carlos Rodriguez

Thank you, Christian. And thank you everyone for joining our call. This morning we reported our first quarter fiscal 2020 results with revenue of $3.5 billion for the quarter, up 6% reported and organic constant currency. We are pleased with this revenue growth, which despite some higher than expected unfavorability in FX was in line with our expectations.

Our efforts to enhance our operating efficiency along with your focus retention on transformation help us deliver 60 basis points of adjusted EBIT margin expansion for this quarter. This margin expansion was in line with our expectations and we are happy to see the progress that our associates continue to make in helping to improve our productivity, while also improving client satisfaction, particularly given the difficult margin compare given our strong performance in the first half of fiscal 2019.

Together with share buybacks and a slightly lower than expected adjusted effective tax rate these results help us deliver 12% adjusted EPS growth this quarter, which was slightly ahead of our expectations.

Moving on to Employer Services new business bookings, this quarter we saw solid growth across our US markets, which helped drive 6% growth in the quarter. With regard to our international and multinational sales opportunities, we did see some impact from timing as certain deals that were expected to close this quarter are now expected to close slightly later in the fiscal year. Nevertheless, we are maintaining our full year Employer Services new business bookings guidance of 6% to 8%.

Now turning to Client Service. We continue to drive improvements in our client satisfaction scores across our businesses. And this quarter, we were especially pleased with our progress in the upmarket with improvements in both our implementation and overall client satisfaction scores.

We continue to take positive steps to transform our service organization and enhance the client experience, and with this continued progress in mind, we remain confident in our forecasted full year fiscal 2020 retention increase of 10 basis points to 20 basis points.

We are pleased with our start to fiscal 2020 and with the continued momentum in advancing our strategy to simplify how we do business, deliver innovative solutions for our clients and associates and drive sustainable long-term growth for our shareholders.

We understand that a key element of building our success in the market is in the capacity to be agile and to anticipate and adopt to change. Innovation is at the core of this need and it’s a job that's never done. While we are incredibly excited about the solutions, we are delivering in the market today to help clients meet the needs of an evolving workforce, we're even more excited about the future. As the workforce continues to evolve, organizations are looking for ways to manage their entire workforce through a single user experience.

Today companies of all sizes are using a variety of applications to get work done. What they need is an open HCM platform that allows easy integration with third-party solutions and is also flexible enough to handle the increasingly dynamic nature of work, one where workers are organized around how work happens in teams, often with individuals working on multiple teams at the same time. Aided by insights from the ADP Research Institute, our Next Gen HCM platform is designed at the core to address these needs.

A few weeks ago I had the opportunity to attend the HR Technology conference in Las Vegas where our Next Gen HCM platform and used innovations took center stage. As I met with clients and HR professionals, I was incredibly proud of the reception and recognition that we received for delivering innovative solutions that address how and where work is done today.

I was especially proud when our Next Gen HCM platform won both the HR Executive Top HR Product of the year award and the Awesome New Technology award, a remarkable achievement and a testament to ADP's commitment to innovation.

Back in September, we also had the opportunity to showcase some of the differentiating features of ADP's Next Gen platform to HCM industry analysts when we hosted our 2019 Industry Analyst Day. At this event, we spent time sharing some of the more meaningful and differentiating elements of our technology, such as, the use of graph database technology that powers the unique ability to dynamically configure teams while enabling actionable data and insights around relationships or our meta data driven design approach that allows solutions to be tailored by the client via local rapid development through a drag-and-drop interface.

In addition, our solution was designed from the beginning to be public cloud native. This among other advantages helps improve resiliency and uptime.

Finally, our solution is designed to be global. Companies that are expanding globally, or that would like to more effectively manage their existing global workforce are an ideal target for ADP Next Gen HCM.

We were equally proud and excited to see, the recognition our efforts from industry experts, at this event. And while it is great to receive these awards and to recognized by industry experts.

It is even more rewarding when we see our efforts translate into recognition and acknowledgment from our clients and prospects. As we work to scale our solution and its capabilities, our Next Gen platform is also building momentum in the market and continues to progress in line with our expectations.

As an example, earlier this quarter, at our Industry Analyst Day, we shared details of a successful go live with a 6,000 employee U.S. company that chose ADP's Next Gen HCM platform for its talent capabilities. And the ease of the ease of integration with the client's own internally developed on-boarding tool.

At the same events, we were also pleased to share that we have recently signed a 65,000-employee global enterprise that was looking for an HCM platform, capable of handling its growing workforce.

With that said, our focus on innovation is not limited to our Next Gen HCM platform. We have also increasing the leverage, machine learning to enhance our core strategic advantages in payroll and big data. As an example, we simplified 21 million raw job titles from our unmatched data like, and normalized them down to 2,400 job categories, ultimately enhancing both this functionality and accuracy of our ADP data cloud benchmarking.

Customers are using our compensation and HR benchmark data to make substantial changes to their business. For example, one of our clients was able to leverage our turn over benchmark data, to identify opportunities for improvement, and ultimately to reduce their turnover by 20%.

While another saw its front line managers use our Executive and Manager Insight’s mobile solution, to help reduce overtime cost by 6%. These equate to real multimillion dollar operational savings that are being enabled by ADP's data and products.

Also to enhance the efficiency of our implementation organization, we are designing our NEXT GEN payroll engine to automatically recognize, convert and classify different formats, an input, from prior payrolls and so payroll policies.

We believe that this will give us an advantage when we on board new clients, because it will enable the automation of various elements of the implementation process. And allow us to share best practices with our clients.

And finally, we also continue to drive innovation for our frontline associates, in an effort to transform how we work, by reducing low value, client contacts, while still delivering value-added service.

With this in mind, last year, our support organization and the downmarket rolled out expanded checkbox functionality, which today is capable of handling over 100 different inquiry types for our more than 640,000 small business clients.

ADP's unique ability to meet the needs of clients and their workers today while anticipating their needs in the future, have been hallmarks of our success over the past 70 years. And I believe will driver sustained growth in the years to come.

And with that, I’ll turn the call over to Kathleen, for commentary on our results and fiscal 2020 outlook.

Kathleen Winters

Thank you, Carlos. And good morning, everyone. As Carlos mentioned, we're pleased in transforming our business, in order to simplify, innovate and grow. Our strategy is working, and we are off to a solid start to the year.

This morning, we reported first quarter revenue growth in line with our expectation, at 6% on a reported and organic constant currency basis, which includes a slightly greater amount of FX unfavorability than we previously anticipated.

Our adjusted EBIT increased 8%, also in line with expectations. And adjusted EBIT margin was up 60 basis points compared to the first quarter of fiscal 2019. We're pleased with this margin improvement, which benefited from cost savings related to our workforce optimization and procurement transformation initiative as well as continued efficiencies within our IT infrastructure.

These benefits were partially offset by incremental brand spend as well as selling, amortization and PEO pass-through expenses. This margin performance is particularly gratifying given the difficult margin compare that we faced in the first half of the year.

As a reminder, this resulted from the very strong performance in the first half of fiscal 2019, resulting from the outside benefits related to our voluntary early-retirement program due to slower than anticipated plan to backfill at that time.

Our adjusted effective tax rate decreased by 100 basis points to 21.2% compared to the first quarter of fiscal 2019. The decrease was mainly due to an increase in tax incentives related to lower R&D efforts and decreasing reserves from certain tax positions.

Adjusted diluted earnings per share were 12% to $1.34. And in addition to benefiting to our benefiting to our revenue growth, margin expansion and a lower effective tax rate was also aided by fewer shares outstanding compared to a year ago.

Let’s move now to our Employer Services segment and interest in funds held for client. Employer Services revenues were in line with expectations and grew 4% reported and 5% organic constant currency.

Interest income on client funds grew 13% and benefited from a 10 basis point improvement in the average yield earned on our client fund investments to 2.3% and growth in average client fund balances of 7% to $23.7 billion.

This growth in balances was driven by a combination of client growth, wage inflation and growth in our pays per control partially offset by lower SUI collections. Our Employer Services same-store pays per control metric in the U.S. grew 2.4% for the first quarter.

Employer Services margins saw an increase of 50 basis points from the quarter. The increase in margins this quarter which enabled by the same factors I mentioned earlier when discussing our consolidated results.

Our PEO segment revenues grew 8% for the quarter to $1.1 billion with average worksite employees growing 7% to 563,000. Revenues excluding zero margin benefits pass through grew 7% to $358 million and continued to include pressure from lower workers' compensation and SUI costs and related pricing.

Margins decreased about 70 basis points for the quarter largely due to changes in ADP Indemnity loss reserve estimates, which drove about 60 basis points of pressure resulting from a smaller benefit in the first quarter of fiscal 2020 compared to fiscal 2019.

As a reminder, with ADP Indemnity results not reported in the PEO, it is normal to expect some volatility in our quarterly PEO margins as a result of changes in our workers' compensation loss reserves.

Let's turn to the outlook for the full year and start with a consolidated view. We continued to anticipate total revenue growth of 6% to 7% in fiscal 2020. This revenue outlook assumes a more elevated level of FX on favorability for the remainder of fiscal 2020 relative to our previous expectations.

With the recent volatility and overlying fixed interest rates, we now assume interest income on client funds of $570 million to $580 million and interest income from our extended investment strategy is now expected to be $575 million to $585 million.

With the continued negative interest rate environment in the Eurozone, we made the decision this quarter to wind down our two Eurozone related client money moving activities in France and the Netherlands.

As a result, we have liquidated our Dutch client funds portfolio and we will be liquidating our French client portfolio by the end of fiscal year 2020. We therefore now anticipate our growth and average client funds balances to be about 4%, as compared to our previous forecast of 4% to 5%. This decision is excusive to France and the Netherlands.

We continue to anticipate our adjusted EBIT margin to expand basis points 100 basis points to 125 basis points. And we now anticipate our adjusted effective tax rate to be 23.3%. The rate includes this quarter's unplanned tax benefit from stock-based compensation related to stock option exercises.

It does not however include any further estimated tax benefit related to potential future stock option exercises given the dependency of that benefit on the timing of those exercises. With these slight adjustments to our outlook, we continue to expect adjusted diluted earnings per share to grow 12% to 14% in fiscal 2020.

Moving on to the segments, let's take a look at Employer Services. We continue to expect 4% to 5% revenue growth in our Employer Services segment. This outlook includes the anticipated impact from my previous remarks regarding changes in FX and adjustments to our interest income on client funds outlook. We continue to anticipate pays per control growth of about 2.5%.

We also continue to expect Employer Services new business bookings growth of 6% to 8% and for our Employer Services revenue retention to improve 10 basis points to 20 basis points. I'd like to remind you as I commented in the prior earnings call that there is volatility inherent in the quarterly Employer Services bookings metric from larger international and upmarket deals.

And I’d also like to remind you the difficult compare in the fourth quarter of fiscal 2020 resulting from our strong performance in the fourth quarter of fiscal 2019 due in part to a client list acquisition.

Moving onto margins. We continue to expect our margin in the Employer Services segment to expand by 100 basis points to 125 basis points. As a reminder with a difficult compare resulting from our strong margin performance in the first half of fiscal 2019, we continue to expect a much stronger margin increase in the latter half of fiscal 2020.

Regarding our PEO segment, overall, our outlook remains unchanged. We continue to expect 9% to 11% PEO revenue growth in fiscal 2020 and 7% to 9% growth in PEO revenues excluding zero margin benefit pass-throughs, both driven by an anticipated growth of 7% to 9% in average worksite employees.

Because of the slower growth in the fourth quarter of fiscal 2019, we continue to expect the growth in our average worksite employees to be at the lower end of our guidance range in the first half of the year with a gradual reacceleration of our growth rate as the year progresses.

As we also discussed last quarter, we continue to expect lower workers' compensation and SUI cost and related pricing to pressure our total PEO revenue growth. For PEO margin, we continue to anticipate margins to be flat to down 25 basis points in fiscal 2020, which continues to include approximately 50 basis points of pressure from smaller favorable reserve adjustments in ADP Indemnity in fiscal 2020, compared to fiscal 2019.

Before I hand the call over for Q&A, I'd like to share that on February 11, we will be hosting an Innovation Day, focused on technology, strategy and showcasing some of her latest innovations.

A few of you have had the opportunity to see some of those developments during HR Tech. Others may have had a glimpse from some of the industry analyst notes, and tweets following our September Industry Analyst Day.

The February 11th event would be specifically for the investment community, to share our product and service innovation, and have a dialogue around the progress that we continue to make, including how these innovations help to differentiate ADP in the market.

We look forward to welcoming you then, and please be on the lookout, for further details in the near future.

With that, I'll turn the call over to the operator to take your questions.

Question-and-Answer Session

Operator

Thank you. [Operator Instructions] And our first question comes from Ramsey El-Assal from Barclays. Your line is open.

Unidentified Analyst

Hi, good morning. This is Damien on for Ramsey. I wanted to ask on the Employer Services bookings guidance. I know you both talked about it at lengths. But I just wanted to see if you could give anymore color on just the quarterly cadence.

I know Kathleen you mentioned difficult comps coming up in Q4. But maybe just any granularity that you could give would be great. And then, just overall level of confidence to kind of get to the midpoint of that 6% to 8% guidance?

Carlos Rodriguez

I'll let maybe Kathleen make a comment as well. But again, I think if you that last year's pattern, our second quarter last year was soft. So that would be the easier compare. And the fourth quarter because of the acquisition of the client base acquisition from Wells Fargo, I think, it'll be a little more difficult.

But we obviously try to apply some judgment on these things. And we obviously have information about individual unit performance and kind of what's happening across regions.

And I think what we try to provide in some of the color our comments is that this quarter we had very strong, what I would call strong results in our core US businesses, SBS, major accounts and national accounts. And we really had some weakness with international and multinational. And we'll look into the details of that. There were a few large deals in prior year, as well as some deals that didn't close in the first quarter as expected. So that would give us some confidence that I think, we're still on track for the year, despite these kind of quarterly fluctuations.

Because I think as Kathleen's said, and we said many times for us bookings is certainly more volatile than revenues. Obviously, we have the recurring revenue model. But on bookings the clock goes back to zero at the beginning of every quarter.

But we see some underlying strength that gives us some optimism. But we did have some weakness in the international multinational and that is something that we're looking at. I don't think that it's any major change in the economy, because it's been kind of a difficult in the economic climate for a while in Europe where we have a large business. So, again as I look at the detail, it just looks like, typical lumpiness in our bookings.

Kathleen Winters

Yeah. I mean just to follow-up on with that. Look you're always going to have some degree of lumpiness in your quarterly bookings number right, from at least a couple of things, right?

If you've got larger multinational type deals, that's going to cost some lumpiness. And then you've got the year-over-year comps issue and you've got a tough comp or an easier comp. So you'll always have a little bit of that going on. And so importantly, while the quarterly numbers obviously important I think even more important to look at a longer term trend, right?

When you look at how we've been doing in particular with last year having a really strong and I think record, right, number of $1.6 billion for last year and then 8%. And then on top of that another what we think is a really solid number of 6% in Q1, when you look at that longer period of time, we're actually feeling pretty pleased with the start to the year.

Now there is of course always pockets that are stronger and others that are maybe a little slower out of the gate and Carlos mentioned on the outside of the US having a little bit of lumpiness there, but net-net we're pretty pleased with the start to the year.

Unidentified Analyst

Yeah. That makes sense, and great. Then maybe I'll zoom out a little bit and ask on overall sort of product strategy at the large enterprise level. I just wanted to dig in and see how you see your products suite revolving there just sort of in the context of you continuing to invest advantage over time and then your strategy - your new strategy around the Lifion offering.

Carlos Rodriguez

Don't forget we also again one of the highlights for the quarter and frankly it's been a highlight in trying to kind of signal this. I am not sure how it has landed yet, but our decision to use Workforce Now with the lower end of the upmarket, so call it that 1,000 to 3,000 even though frankly it can go higher. We have a couple of clients that have 8, 9,000 employees that are on Workforce Now. But that decision has been great competitively in growth wise. So we are selling a lot of units in that kind of lower end of the upmarket.

So the ability to use Workforce Now for - and it fits certain types of profiles clients and you can probably imagine generally speaking they are large, but simpler and Vantage clients would be more complex and have more complex needs like complex benefits and talent requirements and so forth.

And Lifion it's still obviously an early adopter type of product, even though we're getting great traction and we told you what - how we've done in terms of new sales given the size of ADP, it's really Workforce Now and Vantage Now that are affecting the numbers in terms of the bookings and the revenue. And I think again in case I wasn't clear like that we had a good quarter even in national accounts in the upmarket primarily as a result of really good results from Workforce Now.

So the strategy is the same strategy we've had all along, which is I think we've figured out that we have a really great solution for a segment of the market. I think last quarter, I mentioned that we have an external third-party do some analysis for us and in terms of segmenting the market, and as usual one solution doesn't fit the entire market. And what we found was that a pretty good size percentage of the market can be addressed by our Workforce Now solutions and that's what we're doing.

And we were right. And the analysis was right. And we think the Vantage still addresses another segment of the market and Lifion is more kind of the emerging solution that we obviously have placed a lot of confidence and a lot of a - and a big bet on for the future. But as of today it's really not having a big impact on the numbers.

And I also just in terms of just your question about market dynamic when we had this meeting in Las Vegas at the HR Tech Conference that I mentioned in my comments again, early positive signs we had for anyone who was there, I think some of our – some industry analysts and some financial analysts were there, I think, it was pretty clear that we are making an impact in the market. So our lead flow was multiples of what it has been in the past in the upmarket because of the interest in Lifion.

But I just want to be cautious in terms of pace here because relative to our $15 billion in revenue, this is not next quarter or three quarters from now. But the signs are very, very positive in the long-term as Kathleen mentioned. If you focus on the long-term, I think, Lifion - the traction we're getting in Lifion is very, very encouraging.

Unidentified Analyst

Yeah. That's, that's really good. We'll keep watching. Thanks.

Operator

Thank you. Our next question comes from Kevin McVeigh from Credit Suisse. Your line is open.

Kevin McVeigh

Great. Thank you. Hey, you’re able to reaffirm the revenue despite the lower client interest on kind of funds and extended investment. Was there any kind of offset there particularly given the incremental headwinds and FX? It seems like you're able to reaffirm the guide despite those couple of headwinds.

Carlos Rodriguez

You know, I think, it goes back to what we're saying about the some of the underlying performance of the business. So as an example, even though we don't give quarterly guidance on retention, you could tell from our comments, I hope that we felt pretty good about it this quarter, so that you could probably read into that it improved prior to - compared to last year's prior first quarter.

And as I mentioned before retention if you do the math has a pretty outside impact on our business bookings in terms of revenue and frankly big impact on margin because for equal growth you don't have to implement as much business.

And so there's a lot of different moving parts that go into the pot here, but I would point that one out as an area of strength. I think we've talked about the strong performance in our core U.S. businesses.

So for the first quarter we had kind of our three core businesses performing very well in terms of bookings as well. So it's a process from the ground up of us building this forecast, first of plan and now the forecast and I think we have some optimism that we're still in that range.

And but I just want to point out the retention story because three or four years ago when it was going the other way, I pointed out that it takes four to five points of sales growth of new business bookings growth to offset one point of retention just because of the way the math works. And so - now as retention - as you get a little bit of improvement in retention that helps a lot in terms of our growth rate.

Kathleen Winters

Yes. So as Carlos mentioned there's a couple of things that obviously gave us some headwind or unfavorably versus what we would have been expecting particularly the FX and the interest from client funds. However, when you look at operationally the fundamentals things look really good.

As Carlos said retention is on a steady track upwards now gets harder and harder the higher up you go. But we're happy to see some level of increase in the first quarter here, and bookings were solid for the quarter.

Carlos Rodriguez

And I would just add on the client funds interest, we do have some of this - for the year it obviously has an impact as we guided - we gave you the information in terms of we are slightly below what we expected to be, but it's not a huge number for this fiscal year.

Kevin McVeigh

Great. And then just Carlos to highlight the retention a little bit more because obviously really nice progress there. Any sense of just the success across the enterprise versus the mid-market versus kind of downstream a little bit the range on those?

Carlos Rodriguez

Yes. I do have some sense. My sense is that, we're improving a lot. So we show some signs in terms of the win-loss, what we call balance of the trade, some encouraging signs particularly in our mid-market business.

So again the mid-market now is performing - you got to be cautious because there's definitely a forward-looking statement. But it's performing according to the script, in the sense if you remember we took a lot of pain and lot of effort to migrate all of our clients on to one single strategic platform which is Workforce Now.

And when you look at the history of what happened in our SBS downmarket business. When we did that, we were optimistic and hopeful that we would have the same kind of traction in our mid-market business. And it's beginning to show now.

So we have improving retention now for it feels like six or seven quarters somewhere in that range. I am being told more. So once we kind of finish the migration and got through that difficulty. I think we have steady improvements in retention.

This quarter was the second highest retention we've ever had, in our mid-market business. And in this quarter what was very encouraging is to see the level of activity in new business bookings. So, the combination of those two things gives us a feeling of optimism for what is - one of biggest and more profitable businesses.

Kevin McVeigh

Awesome, thank you.

Operator

Thank you. Our next question comes from David Togut from Evercore ISI. Your line is open.

David Togut

Thank you. Good morning. Could you comment on, the drivers that you expect to move your PEO revenue growth up from 8% in the recent quarter to 9% to 11% which is your guide for this year?

And then, just as a follow-up at your Analyst Day last year you gave a multiyear guide of 12% to 14%, CAGR for your HRO business, and you're trending well below that now. Did you anticipate the time that the growth rates in the earlier year’s double-digits effectively, would slow towards the end of that period? Let's say, mid- to high single digits?

Carlos Rodriguez

Well if I can start with the second one first, since I was there in the analysts and not fair to ask Kathleen. I think we have built the guidance for or I guess the estimates for are three years. We had as I think we've mentioned this couple of times, we had certain expectations around our pass through revenue and inflation of those numbers that had some historical precedent, both around workers compensation and health care.

And I think literally within two months of that, the picture changed, and we communicated that very clearly and very transparently and frankly, without any anxiety because it doesn't have any impact in our EPS. So if you remember the Investor Day, I think it June and I think when we had our August earnings call, I think, we brought down significantly for that year at least, the growth rate for the PEO mainly - primarily close to almost based on lower inflation.

Now on top of that, we have had some slowdown in worksite employee growth, which is the core driver underneath of the real growth of the business. But I think a main driver of this differential from what we communicated at our Investor Day has been has been the lower inflation of the pass-through, which again doesn't concern us, in a big way because it’s zero margin and doesn't really affect our profitability in terms of in terms of dollars.

In terms of your question about the behavior of the quarters and so forth, probably beyond the scope of this call but, it's just kind of math in terms of when we have our open enrollment for healthcare in kind of May, June timeframe which we’ve again communicated very transparently when that happens and what happens when that occurs, you tend to have some client churn.

So that drops your worksite employee growth and obviously revenue growth for the PEO. And then as bookings continue to - assuming they continue to be robust, you start to build that up again. And then at the end of the calendar year-end, you have another event at year end where you have some churn in the client base in terms of clients that choose to leave at the end of the calendar year because that's more natural, but we also have historically a lot of bookings in January as well.

So we've been doing this for 20 years and we see a difference or a change we would obviously communicate that. But I think we're just kind of dropping the numbers in as they are supposed to come in terms of -- based on historical trends.

And David I would just add, so last quarter we did say that we would expect to start a year from the lower end of the range and then grow into the range as the year progresses because obviously, we started with a somewhat of a weaker ending worksite employee number in the fourth quarter last year.

Christian Greyenbuhl

And I think it's probably worth asking I mean, adding just again in full transparency, I think we said it last quarter our health care renewal was slightly higher than the previous year. So I wouldn't - it wasn't anything out of norm in terms of historical, but it was higher than the previous year

And when that - when we have that happen you tend to get more shoppers and more -- health care cause is a large part of what a small business pays in their overall cost structure of their workforce. And so they tend to shop and look around and so forth, and so we have a little bit more churn than I think that we have had in the prior year.

The good news is for us is that we have that issue, but we've been dealing with that for 20 years, but we don’t think any risk on health care. So whatever we get in terms of price increases through the carriers, we pass those through 100% which is why we call zero margin pass-through.

So that eliminates any risk or any surprises in the future, but it also means that you have to have frankly the courage to just pass those costs through and let the chips fall where they may.

And the chips fell and I think you can see from the numbers that the chips didn't fall off the table, because there wasn't a collapse in the because of a huge slowdown, but we definitely had our speed bump and now it's really through new business bookings that we have to regain the momentum and kind of have that ramp up again and reacceleration of the growth rate.

David Togut

Understood. Thank you very much.

Operator

Thank you. Our next question comes from Bryan Bergin from Cowen. Your line is open.

Bryan Bergin

Hi. Good morning. Thank you. Carlos, wanted to ask your macro outlook on the current employment market. It sounds encouraging based on the performance of the business, but I'm curious how much of that is due to the improved competitive product position versus the underlying demand you might be saying?

Carlos Rodriguez

It's a great question because it's an important one for us to keep kind of asking ourselves, we do have some things that you know if they turn on us would put pressure on us, interest rates obviously is one of them, pays per control, et cetera.

But we're also feeling pretty good about our product situation and I think our competitive situation in the marketplace going forward here. So it is -- that's going to be a very important question for us to stay focused on here for the next few quarters

But as of today, when you look at our lagging indicators so pays per control, it doesn't look like there's a slow down or a big issue, but if you look at the same things that everyone else would look at that we have access to and you have access to in terms of leading indicators like confidence indexes or NFIB/ISM - those types of things Michigan confidence.

You know those, there's some concern there and some reason for caution. In our numbers, the only place where we have seen some little bit of softness and pace for control and it doesn't get reflected in our and what we report because as we've disclosed prior this is our Autopay base which is a very large base of both large employers, midsize employers and smaller employers.

But we have most of our employer in our run platform and there we've seen a slight down tick in pays per control growth over the prior year. It doesn't - when you look at over the 10-year history, I don't think it's anything to be alarmed by, but - when you look at other factors it certainly a cause for caution. I just happened to look I think, in the last couple of days at NFIB and that's softened significantly, but it's still well above recession levels.

And so I think we're all kind of trying to figure out the same thing here which is a soft patch or is it kind of a trend line. But with - the Fed easing and the consumer still strong like right now our plans are that we kind of work our way through this soft patch.

Bryan Bergin

Okay. That's helpful. And then Kathleen on just margin expansion progress, any further details you can share on the various transformation initiatives? And as you look across the various resources were you seeing the most yield, and anything surprising you as you've had just more time in the seat?

Kathleen Winters

Yes. Thanks for the question. Obviously, something that I'm really focused on in the organization is really very focused on as well. I mean just to kind of get some context and kind of big picture when you step back and take a look at what we've done in the last couple of years.

I mean remember back in 2018, we were at margin rate of 20.7%, with a small amount of margin expansion in that year and then in 2019 when -- fiscal 2019, when we were executing on some really big and meaningful transformation initiatives.

You saw that really outsized margin expansion of 160 basis points, and know -- as a reminder the guide for another 100 basis points to 125 basis points for fiscal 2020.

So a track record here really consistent margin expansion. And as we start in fiscal 2020 with Q1 that 60 basis points of margin expansion we're really happy to see that and very happy that we're on track with how we planned the year.

Now there's a lot of execution and a lot of work behind the scenes going on but I'd point out that number one as I started my comment there's a lot of energy around it and a lot of alignment. And that energy and alignment is around both executing what I call in-flight projects as well as developing the pipeline for the future. So that's really exciting.

I talked about on the previous call that most of the margin expansion from a transformation perspective this year is coming from what we're calling workforce optimization and procurement initiatives both are very much on track from a workforce optimization standpoint.

Think about that in terms of spans and layers exercise if you will and particularly targeted to management layers. So that's kind of on track and already executed with most of that benefit being in fiscal 2020 not much from that coming beyond fiscal 2020.

And then procurement transformation there's a lot of projects there as we look at - across all parts of the organization and spend as we look at volume and we look at policy and we look at our ability to negotiate smartly with vendors and suppliers. There is opportunity there and there is a lot of execution going on.

So a lot of work execution going on. So, a lot of work by the organization, we're happy with what the teams are currently doing and happy with the progress, but more to do.

Bryan Bergin

Thank you.

Carlos Rodriguez

Hi, Brian. I just - one thing just to add, as you think about the margin because your question I think was related to margins in particular. And obviously what's driving those. But last year, the first and second quarter but particularly the second quarter was a very strong growth in margin in that time.

And just a reminder, we also had pressure from M&A at that time. So, just layer that one on to it as well when you think about margin cadence last year versus this year.

Bryan Bergin

All right. Thank you.

Operator

Thank you. Our next question comes from David Grossman from Stifel. Your line is open.

David Grossman

Thank you. Good morning. I wonder if I could just follow-up with a couple of questions on the PEO. Each of your kind of larger peers in that space have identified some type of incremental issue with their health insurance book in their most recent reports.

And I know you mentioned, just higher health premiums and obviously you pass everything through in your model. But is there anything else, you're seeing in the market place that may be impacting the cost of delivering health insurance in the PEO industry?

Carlos Rodriguez

No.

David Grossman

All right. So for you, it's just the straight higher premium and not seeing anything else? I guess, you don't really see the claim that is around in terms of how claims may be impacting on a cost?

Carlos Rodriguez

You will see individual employee, claims data but we of course very, very carefully looking at claims data to get some sense with our carriers and partnership with our carriers, what's happening in terms of trends.

Maybe I should be a little bit more, clear on this, premium increase issue. So, I'm not going to give you the exact numbers. I don't think we want to get down that rabbit hole. But the change from this renewal to the prior renewal was call it one to two percentage points higher, on average than the prior year. So if, the previous year the average renewal increase was 6% then the next year it was it was it was 7% or 8%.

And that increase that year that was slightly higher was completely in line with the prior six or seven years. So it wasn't -- so there are some ups and downs. But the prior year was one that was actually exceptional. I think we were very clear about that. I think we talked about that in our calls, that we had a really great renewal on our health care on average I remember this is not one carrier. These are multiple carriers.

We use a number of different carriers to make sure we have good coverage across the entire country. And so, that was unusual. And it helped us competitively. But I think this renewal was not out of line with historical norms and has nothing to do with any of that.

I think anything that's happening around health care this probably has to do with people's underwriting policies and their own approach to bringing in business and repricing business, because it's not just about the business you bring in.

But every year if you're self-insured or you're taking risk, you have the opportunity or the option of passing through or not passing through health care costs. And you actually have some judgment with your underwriters on what those costs are.

And so that's generally typically what could create a problem in health care. But it doesn't appear to us that there's really anything happening broadly in the health care industry around PEOs.

David Grossman

And then just on your, just based on your commentary on workers comp. I mean I think the whole industry had a tailwind. So, if you look at this year's health increase plus the workers comp at a more normalized level, this is really a more typical year for you then right, I mean in terms of the PEO, in terms of those two items?

Carlos Rodriguez

I think that's right. That's fair. And I think on the workers comp, just again to be clear was a -- I think we were clear, but why don’t we say one more time, a smaller positive. So we're not having big surprises in terms of losses in workers comp or any kind of. And by the way we have very tight ship there in a sense that we have as we disclose in our 10-K, a collar that limits our risk in a fairly significant way. Caps are down side on workers comp. So we have reinsurance an individual claim and then we have a collar around overall loss estimates. So it's quite limited in terms of the volatility.

I think the other thing that I would mention is that our business mix hasn't changed, so we look at that very carefully as well. So we looked at the mix of we call it white collar versus gray collar, but within those categories you have a lot of different industries and a lot of different categories of people and we don't see any major change there as well.

David Grossman

Got it. And just as a follow-up, is kind of a bigger picture for you question Carlos is that given a relatively low penetration rates for the industry and that you get a lot of your new clients from a client that is already using you for payroll.

What are the major objections to somebody enrolling in the PEO particularly if they're an ADP payroll customer and you already have the payroll records so it kind of disruption and transition cost time and effort are substantially lower?

Carlos Rodriguez

I think it's - it goes back to like my first year marketing class in graduate school, which is high involvement decision, right. So the PEO to go to a small midsize business and tell them that you're going to create a co-employment relationship, you're taking over there healthcare plan, there’s workers' compensation remember all along the way there are as an example that could be a relationship with insurance agent or a broker that's been providing to health care in the workers comp for the last 10 years that gets this intermediated.

You have to - payroll is hard enough to convince some of the payroll because people worry about – are you sure you are not going to make a mistake and make sure that it's going to go accurately, we obviously have an incredibly strong reputation on payroll that helps us.

But the traditional business is you're trying to convince someone to give you your payroll, now you're also trying to convince them to give you everything around their HR department.

And so it's with a higher level of trust and it's again what I remember being taught is called a high involvement decision, which takes longer to make and is more difficult to make.

So I honestly don't think that there is really anything that prevents clients from becoming PEO clients. And I think we've demonstrated over 20 years that we've convinced a lot of them.

And so our board asks the same question you're asking, which can't you convince even more. And we're trying. Like, we continue to add improvements in the product. We continue to provide better tools. We continue to enhance our product. We continue to do all the things we can to make it more compelling and easier to use.

As an example, I think we've kind of talked about this in the last 18 months, all new business now and the PEO starting in our Workforce Now platform which has higher functionality and provides the ability to satisfy slightly larger clients than we could before because it's a mid-market platform.

And so there is a lot of things that we're doing to try to convince as many clients to come over to our PEO solution as possible. I think it's good for them and it's good for them and it's good for us but there's really nothing that I can point to other than kind of the difficulties of the convincing of the sale.

David Grossman

I got it. Very helpful. Thank you for that.

Operator

Thank you. Our next question comes from Jason Kupferberg from Bank of America. Your line is open.

Jason Kupferberg

Hey. Good morning, guys. I just wanted to pick-up on some of the margin commentary. I mean, as you rightfully pointed out the comparison there gets quite a bit harder actually in the second quarter. So just so that our expectations are properly calibrated. I mean do you expect margins to be up in the second quarter year-over-year?

Kathleen Winters

Yes. It's a really tough comp in Q2. Remember last fiscal year Q2, we had over 300 basis points of margin expansion. So it was going to be tough to expand in Q2. Maybe it's flat to slightly up slightly down. You know, hard to say exactly because there's so many moving parts.

But the way I would think about is that the bulk of the expansion to come this fiscal year will come in the second half of the year.

Jason Kupferberg

Yes. Okay. That's fair. I mean just on the bookings front somewhat similar question except in reverse right? Because you’ve got the easy comp there in the second quarter. So do you need to be above the full year guidance range in the second quarter just to make sure that you stay on track to achieve the full year outlook? Because then obviously the comparisons here get a bit harder in the second half?

Kathleen Winters

Above the bookings guidance number in the second quarter?

Jason Kupferberg

You need to be above the full year range in Q2 just to keep yourself on track?

Kathleen Winters

Mathematically, yes. So you're absolutely right. I mean it’s to stay on that for the full year you’ll have more growth in the second quarter and then much less in Q4.

Jason Kupferberg

Right, right okay. And then just last quick one from me. What would be the drivers of the anticipated acceleration in the WSE growth during the balance of fiscal 2020?

Carlos Rodriguez

Selling more new clients than losing clients. It really goes back to the - I mean, I hate to I'm not trying to be a smart [indiscernible] but the it's really the pattern, I think, I talked about it a couple of questions ago that when we tell our open enrollment in May and June, we tend to experience some client turn. The sales don't accelerate necessarily at the same necessarily at the same time.

And so you have seen that phenomenon happens sometimes at the end of the calendar year where you may lose a group of clients and then you bring on new clients at the beginning of the year, but then you also bring on - so clients tend to not leave at other times of year other than calendar year end and open enrollment which is May and June.

That doesn't mean non leave, I'm just saying that the skewing is cued towards those two periods. And the sales are skewed differently. And the combination of those two things is what causes either growth or deceleration in worksite employee growth.

Kathleen Winters

Yes. Look on - any of the not any but like a lot of these metrics when you look at a very short period of time one quarter – you could have some one-off things happening. I saw - as I said earlier looking at these trends and a track record over time for things like bookings and worksite employee growth and even margin, right? Looking at the trend over time is helpful I find.

Carlos Rodriguez

But again in this case we also have - we have to hit our plan, obviously. I guess as usual when we have these calls, if we are giving you the numbers based on what we expect right now. So if we hit our new business bookings plans and retentions stays when we expected to stay then you would get the outcomes that we're talking about.

But as Kathleen said, there's a lot of moving parts if three to six months from now, the economies in the tank and pays per control is declining, it's going to in the PEO in addition to ES and it less than ADP and that would create a headwind. But in the absence of any new information I think, we feel pretty good about the forecast we have.

Jason Kupferberg

Okay I appreciate it. Thank you.

Operator

Thank you. Our next question comes from Steven Wald from Morgan Stanley. Your line is open.

Steven Wald

Hey, good morning. Just maybe a follow-up a on the margin expansion path, looking beyond, sort of the next few quarters or even this year, I just wanted to talk about the messaging. And make sure we were getting a proper sense of the drivers there.

I think a lot of the talk has been around workforce optimization and procurement over the next 12 months or so. But I think, one of the things you guys try to talk about is the tech improvements or your investments.

As you build more this into your platform, as you're add even more into what you are doing on a day-to-day basis. Can you talk a little bit about, how that scale to you're adding or that scalable expense base that you're adding will show up in terms of cost reductions or margin improvement?

Carlos Rodriguez

Well, I think again back to like what Kathleen was talking about in terms of the math, some of it was really comparisons rather than anything that we're doing. And but we have to help people. We understand that it's important for you guys to understand that.

So, just as a reminder last year what happened was, we had with the voluntary early retirement program, we had a good number of people taking that. And then the back fills that we had planned which was all planned, certain percentage of back fills were delayed.

And so that impacted that year. We also got off to a very strong start for a couple of other reasons. We had other what we called quick wins at a time around transformation that help us get off to a strong start in the first half.

And I think Kathleen talked about -- we had for us, like incredibly strong margin improvement. And so it's just a very difficult compare mathematically. As we've been going along, regardless of how the math works, we continue to work on a number of initiatives.

And this year obviously we executed on this expand the layers initiative, and then we have a number of other projects around procurement is one of them but we also have a number kind of automation and digitization project that I think we're making some progress on. And when we have our industry - sorry our Analyst Day in February, we'll probably share a little bit more around some of those things that we're doing, because those are around transformation and innovation as well. So it's not just about innovating on the product side. But it's also innovating on the implementation and on the service side.

And we’ve gotten some good traction in some of our businesses which are allows our productivity to improve while, still for our associates. While still improving our NPS scores and our client satisfaction which by the way were up again this quarter and no surprise the retention is improving.

It’s usually a sign that client satisfaction is still high. So again trick here is you want to transform your cost structure, but you don't want to like lose all the clients in the meantime. And for now, we've been able to balance both of those and that's our plan here for the next year or two.

Steven Wald

Yes. Fair enough. And then, maybe just one quick follow-up, I noticed the buy back a little bit higher than we’ve seen last year or so. Just could you provide any commentary on how you're thinking about the pace there going forward?

Kathleen Winters

Yes. So really no change in terms of how we're thinking about that. And our strategy we talked about the intent to buy back 1% of the share base. And we've been executing along those lines, so, really no change.

We look all the time at the market conditions and look if there is some opportunity where there is a big downturn in the market and we want to become more active. Maybe we'll do that, I don't know. But constantly we watch that, we look at it, we talked about it all the time, but as of now no particular change.

Carlos Rodriguez

Again, one little statistic, because we happen to notice these things when we prepare for these calls. Because now I get like seems like 20 years of information, so we've reduced our share count by 30% since the early 2000's, and so we intend to continue to stay on that pace.

And so obviously it's a marathon for a company like we're kind of proud that it's a marathon we've been around for seven years. And at 1% per year it adds up. And it certainly has added up in the last 20 years to the tune of a 30% share reduction.

And I think that companies are in the different stage of development whether they're getting dilution and adding shares to their share count. We think we're going to win this marathon.

Steven Wald

All right. Great. Thanks.

Operator

Thank you. And we'll take our final question from Bryan Keane from Deutsche Bank. Your line is open.

Bryan Keane

Hi, guys. Just a quick - two quick clarifications. On the PEO margins it was below street, but it didn't sound like it was really below your expectations. And it sounds like there was a tougher comp to the ADP Indemnity. So could maybe just talk to that and how that looks going forward on the margin side?

Carlos Rodriguez

Yeah. No, I think that's a fair characterization. I think that as usual there's – and we try to obviously be as straight as we can be because sometimes there is a slight disconnect between what we're expecting versus since we don't give quarterly guidance. But the results I think were on that specific topic, I think we're in line with our expectations.

Kathleen Winters

Yeah. It was definitely in line with how we expect to start the year.

Bryan Keane

And then just the cadence how we think about that going forward on the margin for PEO?

Carlos Rodriguez

That's a good question. I think that when you look at the annual guidance, I think it was down flat to 25 down…

Kathleen Winters

Down 25 basis points.

Carlos Rodriguez

Down to 25 basis points. I think that was the guidance. If you take our first quarter number, I would for now assume ratably margin improvement over the course of the rest of the year because these quarterly fluctuations in ADP Indemnity are not something that is - something that we can have a - we don't have any real visibility into that.

And again, just as a reminder, part of why we've done this is, if you remember a couple of years ago, we had some criticism around our disclosures. So we had our client funds interest and Indemnity being handled in the kind of other category, which allowed us to not have these questions and not kind of makes up the results of those businesses.

But as usual, there are two sides to every story. And so I think the criticism was those things really belong and the results of the business unit. Fair enough. So we made that change and now we are saddled with every quarter having to explain any kind of fluctuations here, because what really matters is the underlying health of the business.

We don’t take enough risk in that business for it to matter. But you can get because of the size of the business, if you get a $5 million fluctuation which is what we had this quarter up or down, it affects the numbers, but it doesn't really say anything about what's happening in the underlying business.

But it is what it is. We now report Indemnity in the PEO and we’re going to have to every quarter be able to give you that kind of color. And likewise in Employer Services we now have client funds interest. And so now that creates some variability in that business as well.

Kathleen Winters

Yeah, so with the down - with the flat to down 25 basis points and down 70 in Q1 you'll see that just mathematically it ramps. But again it's going to depend on the ADP Indemnity and how that comes through during the balance of the year.

Carlos Rodriguez

It was certainly easier when we didn't have ADP Indemnity in the PEO. But because nothing -- we've been doing that for 20 years. We've handled it. We’re not by the way we are handling exactly the same way we’ve always handled it. It’s just a different accounting report. That's all.

Operator

Thank you. And this does conclude our question-and-answer portion for today. I'm pleased to hand the program over to Carlos Rodriguez for any closing remarks.

Carlos Rodriguez

Well, thanks very much. You can tell we feel pretty good about the start to 2020. We're obviously trying to change a lot of things. We've talked a lot about transformation. We'll share more with you when we have our Innovation Day here in February.

But we're focused on execution as I think Kathleen alluded to this there's still a lot of execution in front of us. But we still - we try continue to be focused on our clients and our associates. And our associates are doing a phenomenal job as evidenced by our continuing improvements in our NPS scores.

Obviously, we felt good about what happened with HR Tech, with our Lifion debut. So I think that gives us some optimism. We're very excited about what's happening in the mid-market business here in the first quarter.

So I - continue to be very proud of our organization and the resiliency of the organization and the transformation efforts that they continue to execute on. So we look forward to giving you more updates in the time to come. And we thank you for joining our call today. Thank you.

Operator

Ladies and gentlemen, thank you for participating in today's conference. This does conclude the program. You may all disconnect. Everyone have a wonderful day.