# Paychex, Inc. (PAYX) CEO Martin Mucci on Q1 2020 Results - Earnings Call Transcript

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FQ1: 10-02-19 Earnings Summary

*Press Release* SEC *10-Q* *Slides*

EPS of $0.71 beats by $0.02 | Revenue of $992M (14.97% Y/Y) beats by $1.72M

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## Earning Call Audio

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Paychex, Inc. (NASDAQ:PAYX) Q1 2020 Earnings Conference Call October 2, 2019 9:30 AM ET

**Company Participants**

Martin Mucci - President and Chief Executive Officer

Efrain Rivera - Chief Financial Officer

**Conference Call Participants**

Ramsey El-Assal - Barclays

Kevin McVeigh - Credit Suisse

Rayna Kumar - Evercore ISI

Jim Schneider - Goldman Sachs

James Berkley - Wolfe Research

Lisa Ellis - MoffettNathanson

Bryan Keane - Deutsche Bank

Andrew Nicholas - William Blair

Tien-tsin Huang - JPMorgan

Steven Wald - Morgan Stanley

Bryan Bergin - Cowen

Samad Samana - Jefferies

Mark Marcon - Baird

Jason Kupferberg - Bank of America/Merrill Lynch

**Operator**

Good morning and welcome to Paychex First Quarter Fiscal Year 2020 Earnings Conference Call. [Operator Instructions] Thank you. I would now like to turn the call over to Martin Mucci, President and Chief Executive Officer of Paychex. Please go ahead.

**Martin Mucci**

Thank you, and good morning and thank you for joining us for our discussion of the Paychex first quarter fiscal 2020 earnings release. Joining me today is Efrain Rivera, our Chief Financial Officer.

This morning before the market opened, we released our financial results for the first quarter ended August 31, 2019. You can access our earnings release on our Investor Relations webpage and our Form 10-Q will be filed with the SEC within the next few days. This teleconference is being broadcast over the Internet, will be archived and available on our website for about approximately 1 month. On today's call, I will review business highlights for the first quarter, Efrain will review our first quarter financial results and discuss our guidance for fiscal 2020, and then we will open it up for your questions.

We are pleased with the solid start to the fiscal year 2020. Our financial results reflect good progress in operations and sales. Total revenue growth was 15% for the first quarter, including the incremental results from Oasis Outsourcing Group, which we acquired back in December of '18, Management Solutions revenue grew 5%, while PEO and Insurance Services revenues grew 56%. And not only are we off to a solid financial start, but our client retention and satisfaction continue to be at record high levels and sales continues to perform well as we start this fiscal year. We are excited to introduce several new technology enhancements and solutions at HR Tech, which is happening this week in Las Vegas, and as a longstanding leader in this human capital management space, we have insight into the needs of our clients and their employees and see trends in our markets. These new solutions address key developments in payments, wearable devices, integrations, and data and analytics. Our new wearable solutions allow Paychex Flex time users to track time worked on with their smartwatch, employees can clock in and out with a simple tap of the watch. It also makes time and attendance tracking easier for the increasingly remote workforces with enhanced geofencing capabilities, which remind employees the punch out as they leave their work locations. This is the first of many potential use cases utilizing wearable solutions that we will be making available to Flex users.

We are also excited to be introducing pay-on-demand and real-time payments by the end of calendar year 2019. Paychex clients can allow employees to access a portion of their earned pay before the scheduled check date. With many Americans living paycheck to paycheck, this advancement in technology allows financial flexibility when needed. Following this enhancement, then in early 2020, we will be offering the option to have earned funds deposited in an employee's bank account in real time. Real-time payment is an extension of our market-leading innovative technology. We will be one of the first providers to offer real-time payments or employee direct deposits, continuing our position as a tech leader in this space. While Paychex offers the full breadth of services across the HCM spectrum integrated into our Flex platform, we understand that clients may prefer to keep some solutions they use in place. Our Paychex product integration is a private marketplace that takes the company's integration partner strategy a step further, continuing to simplify the process for customers looking to connect Paychex Flex with some of the most popular HR, accounting, point-of-sale, and productivity applications on the market today.

Clients can determine how and when an integration deploys with the ability to – for it to happen real time, regularly scheduled or based on an action within their Flex platform. Our robust and continually evolving set of APIs allows clients the flexibility to choose how they receive their services through one integrated provider or by using various HR solutions. Data and analytics are areas of increasing focus. Paychex has a rich and reliable depository of data gathered from interactions with clients. We are pleased to introduce the Paychex Flex intelligence engine. One aspect of this feature is the Paychex Flex Assistant, which we have discussed before. This is our customer service chatbot introduced last year, which continues to evolve and be enhanced. Our users in-app interactions with Flex Assistant allows them to elect a preference for their learning via written how to documents, tutorial-style video, vignette short videos, or a guided interactive tour. Coming in December, the chatbot will offer these options during every customer interaction, providing the ultimate and learning flexibility. At any time, a live Paychex agent is just a click away to provide personalized service experience based on the context collected through the bot 7/24/365. Paychex is the only company to offer that personalized service option in our space, 7/24/365 days a year. Through machine learning, our chatbot continually expands its knowledge base and provides a more robust data set to leverage and formulate answers to frequently asked questions.

During the past quarter, we approached 0.25 million sessions interacting with the Flex Assistant, the bot is able to address approximately 200 commonly asked questions, and that number is growing. In addition to these exciting introductions during HR Tech, during the quarter, we also provided a set of enhancements to our solutions designed to help common – solve common HR and payroll challenges including Paychex Solo, a bundled offering designed to meet the specific needs of sole proprietors, which includes a payroll, incorporation services, and a solo retirement plan, a new customizable, new grid entry view for payroll, electronic app Form I-9 and E-Verify processes that is integrated with our paperless onboarding, HR conversations, this is a tool in our performance management module that enables collaboration between employees, managers, and HR staff; and document management, a centralized and secure digital file repository for company forms, policies, references, and employee documents and certifications.

We are singularly focused on continued innovation to meet not only our customers but also their employees' evolving needs, simplify HR complexities and offer solutions to help them thrive and grow. Also, we are offering cyber – cyberattacks are a growing threat to businesses of all sizes. We are now making cybersecurity liability protection available to our clients through our Paychex Insurance Agency and Access Insurance Company, a leading cybersecurity insurance carrier. This solution helps business owners mitigate, and the potential impact of financial – impact of data breaches, hackers, and ransomware and online banking fraud. It is particularly critical for businesses with fewer than 1,000 employees since 60% fail within six months of the cyberattack due to a lack of resources to offset the breach.

Shifting to our PEO business, the acquisition of Oasis was the largest acquisition in our history and double the number of work site employees we serve in our PEO. We are making steady progress on our integration plans and we are now focused on completing the integration of our sales and service teams. Through all of these efforts, we remain focused on what is most important, serving our clients and their employees and growing our PEO. We launched new branding for our HR outsourcing solutions including our Paychex PEO and ASO solutions. This new product brand Paychex One conveys the power of a comprehensive, flexible, total HR solution that can scale and meet the needs of any business at every stage of their development. We're also very proud that for the ninth consecutive year now, Paychex has earned the distinction of being the retirement industries leader number one in the total number of defined contribution plans. This ranking was announced as part of the annual 401-K record keeping survey published by PLANSPONSOR Magazine. We provide solutions to remove the complexity of saving for retirement and this is an integral part of the package for our clients to use as part of the recruitment for new talent, as well as retaining talent. Recent enhancements to our mobile app make enrollment in the retirement plan possible with only four clicks. This is already led to an increase in participant enrollment, which will lead as well to improved client retention. We also ranked number three on sellers Selling Power 50 best companies to

Sell For list in 2019. This is the seventh consecutive year we have appeared on the list and our ranking reflects our commitment to providing our sales teams every opportunity to succeed. We continue to return exceptional value to our shareholders, and in May, we announced an increase in our quarterly dividend of $0.06 or 11% to $0.62 per share. Our dividend yield remains of approximately 3%, a leader in this market. And during the first quarter, we repurchased 2 million shares of common stock.

In summary, we continue to focus on the growth of our business, providing great value and convenience to our client our state-of-the-art technology allows our service to our clients and their employees the way they want, when they want, where they want. We're focused on providing technology-enabled service to improve business efficiency and meet our clients' needs. Our full suite of HCM product offerings and world class service is a powerful combination that positions us for sustainable growth. The continued efforts of our employees and their commitment to our clients, is making a difference.

I will now turn the call over to Efrain Rivera and Efrain is going to review our financial results for the first quarter. Efrain?

**Efrain Rivera**

Hey, thanks, Marty and good morning. I would like to remind you that today's conference call contain forward-looking statements that refer to future events and as such, involve risks. Please refer to the customary disclosures. In addition, I'll periodically refer to non-GAAP measures such as EBITDA, adjusted net income and adjusted diluted operating – diluted earnings per share, sorry. Please refer to our press release and investor presentation for a discussion of these measures and a reconciliation for the first quarter to their related GAAP measures.

I will start by providing some of the key highlights for the quarter and then follow up with some greater detail in certain areas. I will wrap with the review of our fiscal 2020 outlook. As you saw, total revenue and total service revenue both grew 15% for the first quarter. Our growth excluding Oasis was between 5% and 6%. Expenses increased 18% for the first quarter to $643 million. Increases in compensation-related costs, PEO direct insurance costs and amortization of intangible assets contributed to total expense growth for the first quarter, primarily driven by the acquisition of Oasis. Operating income increased 9% to $349 million. Operating margin was 35.2% for the first quarter. EBITDA increased 13%. And EBITDA margin was approximately 41% for the first quarter. Margins were moderated by business mix due to growth in the PEO business and accelerated investments in sales, technology and operations.

Other expense net for the first quarter of $5 million includes interest expense of $8 million related to our long-term borrowings. As a reminder, we used $800 million of private placement bonds to fund a portion of the Oasis purchase price. Effective income tax rate was 23.3% for the first quarter compared to 24.5% for the same period last year. Net income increased 8% to $264 million and adjusted net income increased 6% to $258 million for the first quarter. Diluted EPS increased 9% to $0.73 for the first quarter and adjusted diluted EPS increased 6% to $0.71. We received approximately $0.02 of benefit from stock-based compensation payments during the first quarter, which we exclude in our adjusted diluted EPS.

I will now provide some additional color in selected areas. Management Solutions revenue increased 5% to $724 million for the first quarter. The increase was primarily driven by increases in our client bases across many of our services and growth in revenue per client, which improved as a result of price increases net of discounts. Retirement Services revenue also benefited from an increase in asset fee revenue earned on the asset value participant funds and we had a strong quarter in Management Solutions, if you recall the guide I gave you for Q1.

PEO and Insurance Services revenue increased 56% to $247 million for the first quarter. In addition to the acquisition of Oasis, the increase was driven by growth in clients and client worksite employees across our combined existing PEO business. Insurance Services revenue was moderated by softness in the workers comp premiums. This was partially offset by an increase in the number of health and benefit clients and applicants. Interest on funds held for clients increased 20% for the first quarter to $21 million, primarily as a result of higher average interest rates earned. Average balances for interest on funds held for clients increased 1% for the first quarter compared to the same period last year. Investments and income, we continue to invest primarily in high – not primarily, but in high credit quality securities. Our long-term portfolio has an average yield of 2.1% currently and an average duration of 3.1 years. Our combined portfolios have earned an average rate of return of 2% for the first quarter, up from 1.8% from last year.

I will now walk through the highlights of our financial position. It remains strong with cash, restricted cash and total corporate investments of approximately $700 million as of August 31, 2019. Funds held for clients were $3.8 billion, consistent with the balance as of the end of last fiscal year, May 31. I'll remind you that funds held for clients vary widely on a day-to-day basis and averaged $3.7 billion for the first quarter. Total available-for-sale investments including corporate investments and funds held for clients reflected net unrealized gains of $53 million as of August 31, compared with $20 million as of May 31, 2019. Stockholders' equity was $2.5 billion as of August 31, reflecting $222 million in dividends paid and $172 million worth of shares repurchased during the quarter. Our return on equity for the past 12 months was a robust 42%.

Cash flows from operations were $295 million for the first quarter, an increase of 8% from the same period last year. The increase was driven by higher net income and non-cash adjustments offset by changes in operating assets and liabilities. The increase in non-cash adjustments was primarily due to higher amortization expense, largely driven by intangible assets acquired through the acquisition of Oasis.

Now, let me talk about guidance for the balance of the year. I remind you that our outlook is based upon current view of economic conditions and trends and business trends continue with no significant changes. So we have reflected the impact of the two interest rate cuts that have already occurred this fiscal year. So we are not at this point including additional guidance on further rate cuts; we're uncertain about what will happen in the balance of the year.

I will provide our current outlook and then add color in a couple of areas. We provided updates to the guidance. As you saw, on the strength of a strong quarter in Q1, we now think Management Solutions revenue is anticipated to grow 5% above the range of previous guidance of approximately 4%. We thought that first quarter would be a sequentially a little weaker; we actually got out of the gate a little bit stronger. PEO and Insurances revenue is now anticipated to grow approximately 30% at the lower end of the previously provided range of 30% to 35%, more to come on that but we started a little slower than we had originally contemplated. Other expense net, which was previously referred to as net interest expense, is anticipated to be in the range of $18 million to $20 million, a modest change from previously reported guidance of $15 million to $18 million here due to interest rate changes. And if you remember what that is, is a combination of interest income and interest expense. So the decrease in interest rate changes effects what we will earn on the corporate portfolio.

Net income and diluted earnings per share are both now anticipated to grow 9% above the range of our prior guidance of approximately 8% and adjusted net income and adjusted diluted earnings per share are both expected to increase approximately 9% above the range of our previous guidance of growth in the range of 8% to 9%. Other guidance remains unchanged. Interest on funds held for clients anticipated to grow in the range of 4% to 8%, that’s what we said at the beginning of the year and that’s what we’re sticking with. We assume that there was a good probability that there would be a second rate cut it happened and that was contemplated in the guidance. Total revenue anticipated to grow in the same range of 10% to 11%. Operating income as a percent of total revenue anticipated to be approximately 36%, although inching ever so slightly up. EBITDA margin for the full year fiscal 2020 is expected to be approximately 41%. And the effective income tax rate for fiscal 2020 is expected to be in the range of 24% to 24.5%, although we anticipate that now will be toward the high-end.

As I indicated PEO and Insurance revenues are now anticipated to grow approximately 30%. We anticipate that growth for the second quarter will be in the range of 56% to 60% and growth in the second half of the fiscal year will be within the range previously provided of 11% to 14%, but at the lower end of that range. PEO and Insurance revenues growth was partially impacted by change in classification of an immaterial Oasis revenue stream out of PEO and Insurance services into Management Solutions after we last provided guidance. So make sure when you look at the presentation we posted that you got the right beginning number; it’s not a big difference, but make sure you’re working off that number as you look at updating your models.

Management Solutions, in addition, we have experienced lower workers' compensation insurance rates that moderated our insurance services growth. It was a little softer than we had anticipated in Q1. We anticipate the trend eases as we go through the year, but started a little bit slowly there and we are also anticipating modestly lower at risk insurance attachment in our PEO business based on current trends and the number for us, if it's not at risk insurance, we don't recognize it as revenue. So our business can do very well without having significant at risk insurance attachment. We looking at the trends, think it will be a little bit lower than we had originally projected.

Now in contrast, Management Solutions guidance was increased to approximately 5% growth from our previous guidance of approximately 4% growth due to favorable trends we've seen during the first quarter. In addition, Management Solutions has increased partially due to the change of classification of the immaterial Oasis revenue stream and had a negligible effect in the first quarter and will have a negligible effect for the remainder of the year. For the second quarter, we expect growth at approximately 5% and then between 4% and 5% in the back half of the fiscal year. Operating margins, which for the full year are anticipated to be approximately 36%, very quarterly as you probably captured in your models for Q2, we expect margins to be in the range of 33% to 34% and for the second half of the year, we expect to see them at approximately 38%. So in the second half we are anticipating at this point approximately 38% margins. I got asked a lot after the guidance that we expect to see higher margins in the back half of the year and the answer is yes.

Now, I refer you to our investor slides on our website for more information. And with all of that, I will turn it back to Marty.

**Martin Mucci**

Thank you, Efrain. Maria, we will now open the call to questions, please.

**Question-and-Answer Session**

**Operator**

[Operator Instructions] Our first question comes from the line of Ramsey El-Assal of Barclays.

**Ramsey El-Assal**

Hi, guys. Thanks for taking my question. I wanted to ask you kind of a general question about your pricing strategy. Marty, you walked through a lot of really interesting kind of product innovation that's happening. When you are able to raise prices, is it always in conjunction with a new enhancement or in addition to value, or are you still able to just raise prices on a renewal just due to the underlying kind of stickiness and competitive moat of the product? I am just trying to understand whether pricing is kind of tied to innovation or really it's just something you can leverage due to the underlying kind of competitive moat you have?

**Martin Mucci**

Yes, I think it's still both. I think we are seeing not only for the innovation in bundling more things together, but also the normal price increase that we have given guidance on pretty consistently, is held up pretty well. So, we had our kind of normal annual price increase, and we have seen that hold up pretty well. And I think that's part of where you are seeing management solutions -- is holding is better than we originally projected, it's because of that. So, actually we have the pricing power both ways, I feel at this point.

**Ramsey El-Assal**

Okay. And then on the PEO and insurance segment in the quarter, so the deceleration there – there are few puts and takes there that you mentioned, both of you mentioned, the softness – is the implied sort of deceleration in the quarter in PEO and insurance just really solely or more due to the softness on the insurance side. Can you just sort of speak to the underlying growth rate of PEO sort of ex-Oasis in the quarter and kind of disaggregate the insurance from the PEO performance for us?

**Efrain Rivera**

Yes, thanks, Ramsey. So, I would say, just to be clear, the PEO business has been growing solid double-digits. So, it grew very well in the quarter. We knew that workers' comp was coming up against a tough compare because much of the softness in workers' comp occurred in the back half of last fiscal, and so it was a little bit more pronounced than we anticipated; that's part one. And then part two is, in the PEO, the attachment of at-risk insurance impacts the revenue; it has no impact, there is very little impact I should say on margins. So, we saw a little bit less at-risk insurance attachment in the quarter. I would just mention that, that varies widely from quarter to quarter. So, you can find a big client that has a lot of work – I am sorry, that has a lot of healthcare attachment, the revenues go up. It really does – it changes your margin, but it doesn't do much for the bottom line. So, we saw a little bit of softness on both of those.

**Ramsey El-Assal**

That's great color. Thanks so much.

**Martin Mucci**

Okay.

**Operator**

Our next question comes from the line of Kevin McVeigh of Credit Suisse.

**Kevin McVeigh**

Great, thank you. Hey, Marty. Hey Efrain. Nice job on the Management Solutions. Can you give us a sense of how much of that was better retention as opposed to just any thoughts around kind of what drove that upside?

**Martin Mucci**

Yes. I think I will let Efrain speak to some of it, too, but the client retention has continued to be at our highest level. So we are feeling very good. We ended last year with a record high, and we continued right through the first quarter. So, we feel very good about the client retention piece of it and then there were a few other changes that Efrain wants to speak to.

**Efrain Rivera**

Yes. So, Kevin, we saw, as Marty mentioned, strong retention in the quarter. We had strong rate meaning combination of discounts and price increases sticking those were good. We had increases in the client base. We had a lot of good things happen in the quarter that make us incrementally more bullish. I would say two other things that are important relative to the results in the quarter, the first is that we saw very good performance coming out of our mid-market segment on the sales side, which also helped. It was really not a significant contributor, but it made us incrementally more bullish going into the back half of the year. And the other thing I would say is that we saw strong performance coming out of our PEO business from a sales standpoint that also even though the revenue was a little softer, we feel pretty good about where we are at. By the way, just a final point on that, worksite employees – before I get the question, worksite employees – worksite employee growth was strong in the quarter.

**Kevin McVeigh**

Great. And then it's interesting because obviously you are seeing overall payroll slow, it seems like your business fundamentally is accelerating. Marty, is that kind of the benefit from the investments the last couple of years or you are kind of repositioning the company or just any thoughts on that?

**Martin Mucci**

Well, yes, I think we definitely have been repositioning the company from a couple of standpoints. One is from a tech perspective, the company is much more – Paychex is much more of a technology company now providing service as well than it has been in the past, and all the investments are really paying off like the things that I listed out. This is and it's impacting not only the clients in their retention and their value and satisfaction, but also the employees of the clients. So, our business and the products that we are introducing very much focuses on the employees, and it's kind of perfect timing for a market that's difficult to hire and retain employees for small and midsized businesses. So, the fact that you have a 401(k) for example is that you can sign up for – participants can sign up for clicks on a mobile app that's a 5-star rated app and makes it easy to sign up.

That participation is up double-digits as that drives better retention of 401(k). That also drives retention of the employees and it's better for the clients. The other positioning of the company is certainly more to HR. The sales process today is very much about an HR overall need than it is for payroll by itself and we have been positioning the company that way whether it's through PEO or frankly through the power of kind of over 3,000 sales people. We use the power of those 3,000 sales people to not necessarily the old way sell payroll then call them back for other services, but basically look at their needs upfront and sell the value of HR in the full product suite that Paychex can offer upfront. So definitely the company has been – we have been repositioning the technology side of it and the HR side of it and that has made a big difference as payroll has become more or less – more of a commodity type of thing and the need of the client has been much more about HR retirement, the HR generalist. We have 600 HR generalists now out there serving the worksite employees that we serve either PEO and ASO. It's a huge need now given the changes in regulations in complexity.

**Kevin McVeigh**

Thanks so much.

**Operator**

Our next question comes from the line of David Togut of Evercore ISI.

**Rayna Kumar**

Good morning. This is Rayna Kumar for David Togut.

**Martin Mucci**

Hi, Rayna.

**Rayna Kumar**

Hi. You called out another strong sales bookings quarter, could you maybe discuss in which products and segments in the market you saw the best growth?

**Martin Mucci**

Well, we don't break it down too much that we get past selling season in the next quarter or so when we have a better sense of the year, but definitely, as Efrain mentioned the mid-market sales in particular, we saw very strong growth and this has been more of a challenge in the last couple of years for us. Once we got the investments in technology and product out there, we also have very solid leadership team in that mid-market and we performed extremely well in that first quarter. So, I would say certainly the PEO, the retirement business, etcetera, but when you look at the mid-market stands out certainly from the start of the year and actually as we ended last year as well, but this first quarter was really strong in the mid-market. And that's a real positive to us because we had, certainly over the last couple of years, hadn't been quite as strong as we thought we needed to be and we are very pleased with where we started out.

**Rayna Kumar**

Great. That's very helpful. You called out a number of real-time payment products, can you maybe discuss the timeline for rollout and the revenue model associated with these products?

**Martin Mucci**

Well, the end of this calendar year, we will have the kind of pay-on-demand so to make sure that we are clear on that. So the pay-on-demand obviously offers employees of clients the ability to take some wages out earlier than waiting for their 2-week period or etcetera, real-time payments we see coming in early 2020. We think we will be one of the first, if not the first, to offer real-time payments. This is really more of a accelerate – we offer same day ACH today. If you have a last minute change in your payroll, if you need to make some changes, if you need to do something at the last minute and be sure the funds are there and there is some charges for that and we expect there will be some charges for real-time payments which takes that to the next level of making it immediately available. Real-time ACH has – ACH same-day has some limitations from a timing perspective depending on banks and so forth and real-time payments will really kind of wipe out most of those limitations and you will be able to get funds in your employees' accounts basically in real-time.

**Rayna Kumar**

Great. Thank you.

**Martin Mucci**

Okay.

**Operator**

Our next question comes from Jim Schneider from Goldman Sachs.

**Jim Schneider**

Good morning. Thanks for taking my question. I wonder if any follow-up on the improvement that you called out both in Management Solutions and also the mid-market, is that more a function of the enhancements you have made with Paychex Flex, any color you can put around that? And also maybe just talk about how much of that's being improved by the sales force enhancements and channel strategy? Anything in terms of color you could provide around that will be great?

**Martin Mucci**

Yes, sure. I think it's a little bit of both. I think certainly the product is the enhancements to Flex have been pretty significant, not only from the payroll side, but the integration side at all, some of the products and features that we discussed today even like the payroll grid offering many more options and making it just easier for them to use from a payroll standpoint, but the integration of the HR and I think the sales team and sales, so their effectiveness and the sales approach being much more about HR first instead of leading with payrolls coming in and offering the full suite of products that we offer. And then also as I mentioned today in the comments offering others to have – we have a full set of APIs to other providers of on-demand services and HR products and accounting products and that is getting broader and I think we see that as well. We certainly offer a one solution set. That's the great thing about Paychex. We can have it all fully integrated into Flex if you want it, but if you are on an HR or an accounting system that you want to make sure you keep an interface into Flex, you can do that as well. So I think it's that approach. I also think the employee approach, Jim, that I mentioned earlier, really doing things with the mobile app that is making self-service more available to their employees, not only their check stub, their W-2s, signing up and signing off on time in attendance, changing schedules, setting up your 401(k), all of that is adding a lot of value to the mid-market in particular and we are seeing that pay off for us. So we are very pleased with the first quarter start.

**Jim Schneider**

Great. And then maybe as a follow-up, on the PEO, the reduced guidance you called out several of these idiosyncratic factors on the insurance side, but I want to make sure that I am clear in terms of what you are seeing in the core PEO business. Is there any slowdown there either in terms of market demand or from a competitive positioning standpoint and maybe just talk about how the Oasis expected growth is doing relative to what you thought was going to be?

**Efrain Rivera**

Yes. So, Jim, so two parts of that. So the short answer is, no, but let me explain why because it's important to understand. So, when some questions started to rise – started to get calls relative to what are you seeing with respect to worksite employee growth within existing clients, I did a deeper dive to understand what was going on and we are seeing solid worksite employee growth within existing clients. So, that was an issue that came up and was commented on. So we are not seeing any of that. That's one. Second, if I look at worksite employee growth, worksite employee growth again has been solid in the quarter. So we are not seeing anything there. On the Oasis side, in order for us to get fully optimized on the sales side for Oasis, we are in the process of ramping our sales efforts there and I think that process is ongoing. So, it's – there – I agree that it's somewhat idiosyncratic the reasons for the slight modification in the guidance, but it has no – it really is not indicative of any changes both in demand patterns and in or the underlying market. If I called out the growth rate on sales in PEO I will just say this, it's multiples of revenue growth. So that's one reason why we feel pretty comfortable about where we are at.

**Jim Schneider**

Yes. And the trends in Oasis you are seeing?

**Efrain Rivera**

Yes. I was just talking primarily on the sales side, the integration is going well and we are in the process of pulling it into the Paychex family growth.

**Martin Mucci**

Yes, we are at the point of just finalizing all the combination of the sales teams and the service teams, but we feel like the integration has gone well and we are feeling very good about it. We are also, of course, with Paychex and with that integration, we have the insurance agency, the 21st largest in the country. So when underwriting, if it doesn't fit the PEO, we have that option to take them through the insurance agency that some of the changes that Efrain mentioned as well, we are getting more through that insurance agency and that's going as well. So you don't want to turn down a client, that many times Oasis had to turn down in the past possibly over underwriting, we can now move them to the agency and offer them insurance through the agency itself. So, we feel good about the start here and the integration is certainly on track.

**Jim Schneider**

Good to hear. Thank you very much.

**Operator**

Our next question comes from James Berkley of Wolfe Research.

**James Berkley**

Thanks for the time. Appreciate it. Not to beat the dead horse on the PEO side, but I guess just trying to be like more direct. Are you guys still trending a couple of quarters ago you said bookings in PEO space for like low-double digits, are you guys still in that range? And then on the worksite employee growth, I think it was double-digits last quarter, can you confirm, it's still double-digits this quarter?

**Efrain Rivera**

I think I said that, James. It was strong.

**James Berkley**

Yes, okay. And then I guess Efrain, just we talked a few days ago, I guess just about that new HRA rule, it could be helpful just for investors to hear your thoughts on the impact there it's coming into play in January 2020?

**Efrain Rivera**

Yes. So this is new legislation that makes it easier for employers to use HRAs as an alternative for funding of healthcare plans and the questions that have come up from investors around the impact on the PEO side of the ledger will this impact annual growth and we have looked at it and of course until it's in place and people are actually having the opportunity to take advantage of HRAs in a different way, it's – you can't say 100%, but we feel pretty comfortable that should not have a significant impact on PEO growth.

**Martin Mucci**

Yes, we have had – we have offered HRAs through – for some time, I don't think even with the legislation that gives some support and credit, so I think it doesn't seem like employers are going to run from traditional insurance plans to do the funding. We have offered those as I said for some time and seen – not have seen a great uptake. I think there are some businesses that do that, but I don't think there will be any major shift that we would expect that, that's going to happen from traditional insurance plans over to the HRAs.

**James Berkley**

Okay. Thank you very much. I appreciate that.

**Operator**

Our next question comes from the line of Lisa Ellis from MoffettNathanson.

**Lisa Ellis**

Hi. Good morning, guys. I guess I will ask the inevitable macroeconomic question. Marty, can you give some color on what you are seeing on sort of the second order dynamics around the macro environment? I know you have a very unique look into things like obviously employment growth, but also like small business survival rates, the attach rates, the value-added services like benefits, etcetera. Can you give us a little color there? Thank you.

**Martin Mucci**

Yes, I think we reported our small business index yesterday and it actually we had an uptick from September to August. One month doesn't make a year or trend, but job growth actually ticked up a bit and these were businesses under 50 employees and we saw some growth not only or improvement in the job growth, it's still down about 1% less job growth from last year, but this was the first time we have seen an uptick in a couple of years where it moved up month to month. We also saw wages in hours worked up. So, wages looking pushed up from about 2.6% wage increase, the 2.8% and hours worked went up. So, I think small businesses are still feeling overall a little shaky on the economy and what's going to happen, but generally they are getting good product demand for their services and there is still their biggest challenges hiring enough people to fulfill the demand. So we also did a business sentiment report and everything was positive, everything had gone up from the previous report probably 6 to 9 months ago that felt that it would be easier for them to – a little bit easier for them to hire, a little easier for them to get capital. So I think while the economy itself makes them a little cautious, I think that they are feeling like right now they are getting good product demand and their biggest challenge is hiring. So you saw the hours go up, because they are working with they have more to fulfill the demand and the wages are going up as they are trying to raise wages to get to pickup the employees. So, overall pretty positive actually with our latest report that just came out yesterday.

**Efrain Rivera**

The other thing we said and Marty mentioned this yesterday is SMEs are typically a little less impacted by slowdowns in global trade. So that segment of the economy obviously larger multinationals and enterprise level companies are starting to feel the pinch. You are not feeling as much of that lower down the employee count. So, it's not impossible to have results like this in one segment of the economy where you see more concerned and pessimism in another part of the economy.

**Martin Mucci**

Yes. We have talked about tariffs and trade issues and we found in serving clients that about three quarters of that small businesses, are not impacted. Generally, they are regional businesses. They are the lawyer's office, the doctor's office, the restaurants, etcetera, the contractors, they are not impacted. The 25%, a quarter than our, have a little bit tougher time changing their supply chain and so forth, they don't have the leverage of larger companies, but three quarters of them really don't feel like they would be impacted by trade issues or tariff issues.

**Lisa Ellis**

Alright. And then maybe as my follow-up, can you and this is – Efrain, give your perspective or your best perspective on how you anticipate the PEO business performing if and when we see a macro slowdown. I mean, I know there is an argument that PEO should actually tick up because the cost and economic value proposition is so strong for small businesses, but then on the other hand, it's also got a perks component to it. Just what's your view on that? Thank you.

**Efrain Rivera**

Yes. So I think the first thing to understand that question is, what's the average size, at least in our base, for PEOs and typically a PEO in our world is in the 25 to 30 employee range. So you're comfortably out of the 20 and under-zone where you would tend to see more of an impact from a macro slowdown and what I mean by that specifically is 20 and above, you start to see a lot less impact from business failures in the event of a downturn. You see that Increasing as you go down the employee count. So now you're in an area of the economy where – the employers where you tend to see less of an impact from macroeconomic slowdown. And then the question is, in that kind of environment, do you have a greater demand for HR services or do you have a lower demand for HR services, and when you think about it, the balance really kind of lies on a greater demand for managing your workforce in the event of a downturn. So I wouldn't go so far as to say it would not be impacted. I think there'll be some impact, but it will certainly be less impacted than a typical small business would be.

**Martin Mucci**

And less impacted we are than we used to be. If you went back to the last recession and we were primarily a payroll company, I think, we feel that really half of our revenue coming from non-payroll services and moving to more than half and from non-payroll that also changes kind of the impact to us as a company in a recession area.

**Efrain Rivera**

And one final point on that, Marty raises, which is important, when we went into the recession last time, which was in the ‘08 time frame, we were heavily dependent on float income; almost 30%, somewhere between 25% and 30% of our net income was generated by float. We’re completely different company now. And I’ve heard people make the argument and – hey, look I like a good argument like anyone else’s, but I do think the data suggests that were different.

**Lisa Ellis**

Terrific. Thanks guys.

**Martin Mucci**

Okay.

**Operator**

Our next question comes from Bryan Keane of Deutsche Bank.

**Bryan Keane**

Hi, guys. I was just looking to get a couple of clarifications. What was the revenue growth contribution of Oasis in the quarter trying to get to an organic growth number in the PEO and Insurance in the first quarter?

**Efrain Rivera**

So, Brian, I called it out as a little less than 10%. Organic growth was between 5% and 6%.

**Bryan Keane**

Inside of PEO and Insurance?

**Efrain Rivera**

No, no, total revenue. We didn’t split it out like that. I just caution that that if you want to know what the growth rate for PEO was in the quarter, PEO – not PEO and Insurance, it was solid double-digit.

**Bryan Keane**

Yes. I just was trying to get there was about a $15 million gap I think in Street numbers in PEO and Insurance versus the actuals. It sounds like…

**Efrain Rivera**

Yes. Yes, so part of that, Bryan, I called out; part of it is that at the end of the fourth quarter, we made a small classification change in staffing revenue, which some people picked up and some people did not. I would just caution that you could come back to me offline and I’ll walk you through the numbers, but the starting point was a little bit different. We made that change, not everyone picked it up. So I think that’s part of it. I think that’s generating part of the change there. And so part of that moved into Management Solutions. That probably accounts for a good chunk of the difference.

**Bryan Keane**

Okay, helpful. And then just on that guidance in PEO and Insurance to be toward the lower end of 11% to 14%. Is that that the workers comp will drag a little longer than you expected? Just trying to make sure I understand the change.

**Efrain Rivera**

Yes. Workers’ comp started a bit more slowly than we had anticipated in Q1. And I called out at-risk healthcare and insurance attachment rates based on what we saw in the first quarter. We are walking through all of that with now three pieces of the PEO and we think that that number is going to be a little bit lower, but I would just caution one thing about that that really doesn't have that much of an impact on margins. And then the second thing is I could come back next quarter and say, hey, the attachment rate actually ended up being a little bit higher. It's a little bit tough to nail it with precision, but we'll keep updating it.

**Bryan Keane**

Okay, super. Got it. Thanks guys.

**Efrain Rivera**

You're welcome.

**Operator**

Our next question comes from the line of Andrew Nicholas of William Blair.

**Andrew Nicholas**

Hi guys. Good morning. Thanks for taking my questions. So just to stick with Oasis, briefly, I think based on my math Oasis did maybe $85 million or so in the quarter, which I think was maybe $5 million or $6 million below last quarter. Just wondering if there's anything to highlight on the step down, if there is any seasonal factors to consider, and if that was in line with your expectations as of last earnings call?

**Efrain Rivera**

Yes. I don't do on the spot math. I would say that our – it always was pretty much in line with our expectations. So I'd have to go through that with you to make sure that you are using the right set of numbers.

**Andrew Nicholas**

Okay, fair enough. And then with respect to the PEO market, I'm just curious you've seen any changes in the competitive landscape recently. I think more specifically I'm curious about when you're going head to head with another PEO, which I recognize isn't as frequent, but when you are, what are the determining factors for winning or losing business? And relatedly, how important is pricing in those conversations and if you've seen any changes in the pricing dynamics as well? Thank you.

**Martin Mucci**

Yes, I really haven't seen any changes in the competitive market for PEO, and in fact, I think with Oasis and giving us some new markets, we're in some new markets, it really comes down a lot of times from a competitive standpoint. So you're not seeing something – you really I think more competitors I think it's the same competitors and we're a little bit larger obviously now at this point being the second largest, and I think it's really the insurance plans, which we feel very good about having the insurance plans and of course the service that you provide with the HR specialist. And I think we've been able to demonstrate that we've been in this business for a long time both PEO and ASO, and by the way, we can offer either one of them that's part of the new branding of Paychex One is the brand of our HR outsourcing. So you can go PEO, you can go ASO with us. We've been in this business for 20 years. We have 600 HR specialists out there and we have great insurance plans and we continue to expect to have those. And that's really what it comes down to is, what's the service model, what the insurance plans that you offer, what's your history in the ability to offer that service. The competitive nature hasn't changed much. I think we're very well positioned to win in this market.

**Efrain Rivera**

Hey, one other point to your earlier question and you can call me back offline. I would caution with saying that that revenue is sequential in PEO; certain quarters there's cyclicity in quarters. And typically in the back half of the year, you have higher revenue than the first half of the year. So it's not, preferred compare to look at it quarter-over-quarter because it bounces around now.

**Andrew Nicholas**

No, that's helpful. That's kind of what I assume, that's why I asked. So I appreciate it. Thanks, guys.

**Operator**

Our next question comes from the line of Tien-tsin Huang of JPMorgan.

**Tien-tsin Huang**

Hi, thanks. Good morning. Just a couple questions on the HR and the Management Solutions side that was clearly better you laid out a lot of reasons but versus your 3% to 4%. What was the difference there, another reclass maybe contribute a little bit, but can you comment on payroll HCM pricing maybe raking for.

**Efrain Rivera**

Yes. We still would have had 5% in the absence of the re-class. So I just want to make sure that that's clear. And the other thing I want to make clear is that I did call down in Q1 due to a composition of days issue in the quarter that did hit us. So we had just stronger performance through a combination of both. As we discussed earlier, pricing, client growth, stronger mid-market performance on the sales side; the combination of all of those just ended up being stronger than we had anticipated which was a good turn for us.

**Tien-tsin Huang**

It is. That's great. And then just on the quarterly EPS, Efrain, I think last quarter you mentioned in the first half, net income would run low single-digit growth. This came in ahead. Can you maybe help us recast second quarter versus second half, if you don't mind?

**Efrain Rivera**

Yes. Well, I guess what I'd say, Tien-tsin, as I gave a fairly good guidance on what we expected revenue was going to be in the quarter and what we thought margins were going to be. So I would say, it's implicit in what we were saying was that I give you a decent number for Q2 that we expect to Q3 and Q4 we called out operating margins being at approximately 38% for the back half of the year. So it's going to be better, and at this point, there is an element of conservatism to what we're guiding. We're still in an uncertain interest rate environment. So we want to preserve a little bit of flexibility if the Fed decides that it wants to continue to cut without altering the guidance. So back half from an EPS standpoint is going to be stronger than the first half, even though we got off to a pretty good start in the first half of the year, I should say.

**Tien-tsin Huang**

Yes. No, for sure, I know that tax and interest played some smaller roles to there. So the last one, I think, you mentioned there, Efrain, so 38% second half margins, is there any change or and that's using that as a baseline for fiscal '21?

**Efrain Rivera**

Yes. There is a big danger Tien-tsin, let me explain why. So when we did – when we adopted revenue recognition, what it had the effect that was moving a revenue stream into Q3 that had previously been spread across a number of quarters. When you do that what ends up happening is that you cyclically – cyclically, wrong word, you create a situation where Q3 is always going to be your highest margin quarter, and the reason is very simple. You simply have more revenue with no greater associated costs. All of that drops to the bottom line and you are typically seeing, although I called out 38% for the quarter, it's not going to be uniform –- I'm sorry, 38% for the back half, it's not going to be 38% in Q3 and Q4. Q3 will be higher than Q4. And so that's the danger. If you just take that as the run rate for margins going forward, you're kind of not taking into account the Q4 – I'm sorry, Q3 is going to be a higher margin quarter now going forward. Having said all of that, we do think that that all things being equal, we think that expenses will trend down in the back half of the year and we'll have some opportunity to improve margins from where we are as we go into 2021; hard to believe, but hopefully that's helpful.

**Tien-tsin Huang**

It is. No, I was just looking for clues as you guys are obviously going to get a little bit of benefit from some of your investments. Thank you, guys. I appreciate it.

**Efrain Rivera**

Yes.

**Operator**

Our next question comes from the line of Steven Wald of Morgan Stanley.

**Steven Wald**

Hey, good morning. Maybe just following up on the margin question, if there were a couple of things or one thing that you could call out to hold you back, whether it's perpetual reinvestment or just faster than expected mix shift, like what would keep you from something like notable margin improvement starting in 2021 and how should we think about that conceptually? As you talked about like moving toward less of a payroll model more of a tech model, how should we think about the margin conceptually in that lane?

**Efrain Rivera**

Yes. I guess, I'd like to defer a better or more complete answer to the second half of the year because trends will become more evident, but if I were to point to one thing, we've had relatively high spending and what's been kind of unusual about our performance is that we haven't taken any charges. We have made changes on the fly, we've delivered double-digit EPS growth and we have done that all within the context of the kind of programs that we run. So we understand that as we exit the year some of that spending will decrease, we know that, we're working on that actively, and the question is how much we'll have better sense of that as we go through the second half of the year.

The investments have paid off. I think that the results we're seeing reflect that and I think that all of the technology advances and improvements that Marty was mentioning are really the fruit of that accelerated investment, but you don't continue to invest at that accelerated pace. You pull some of it back down. So we anticipate as we go into '21, that's what you would see.

**Steven Wald**

Got it. And then maybe just one quick follow-up, I think earlier in your comments you talked about this shift away from being sort of thought of as a traditional just payroll-driven model toward the tech offerings and all the products you guys have been rolling out, and all that makes sense. I guess, just as we think about it from a macro perspective and what we sort of seeing in your data ADPs broader macro data, are you guys prepared or of the mind that we shouldn't think of Paychex as being heavily levered to shift and implement?

**Martin Mucci**

Well, I think certainly not as levered. It's going to have some impact, but I think as Efrain mentioned earlier in a question probably more specifically on the PEO, payroll was, especially the small business payroll was very much tied obviously to new business start-ups and losses in businesses going out of business because of a tough economy. When you're 50% or more and more of an HR time and attendance retirement etcetera, services non-payroll and not so focused on just the smallest clients. It's going to have a different impact because in a recessionary period or a down turn of employment, you're going to have a bigger need for HR, how do I retain who I have, how do I maybe lay off people, how do I make changes in cost structures. These are all from our clients perspective, there is a huge need for HR support, and other products and technology like self-service. When you think about 10 years ago, we didn't have a mobile app that had much of it on a self-service from an employee basis and we can save – we're now saving clients a lot of money and better – and giving them better productivity by saying, hey, if you want to change – if your employees want to change their address or change their deductions, etcetera, they can do it all on their phone by themselves now. They don't need to call and go through, you call us etcetera. So the dynamics of the company and the clients and what they need us for has changed pretty dramatically and I think that – and certainly that was our positioning that we started moving toward many years ago to say, hey, you can't just be a small business payroll company, you got to be an HR and a complete outsourcer to small and mid-sized businesses and that certainly is going to have much less of an impact if there is a recessionary time.

**Efrain Rivera**

One of the other thing I would add to Marty, this is just sort of concretely in terms of what we've seen over the last three years certainly since the end of fiscal '16. If you look at our financials, at the end of fiscal '16, about 60% of our revenue came from payroll, 40% of it was what we would have called HRS. If you look at where we're of this forecast, obviously, it depends on what model you are using, but payroll now is in the mid-40%s with everything else being 55%. That trend is something that's deliberate, not something that is happening to us. As Marty said, that is the positioning that he and the management team have adopted and the numbers bear it out and I do think that we have evolved very clearly to a tech-enabled services company that is much more HR focus than it was three years ago.

**Steven Wald**

Alright. Thanks.

**Operator**

Our next question comes from the line of Bryan Bergin of Cowen.

**Bryan Bergin**

Hi, good morning. Thank you. I wanted to follow up on the real-time and on-demand pay the offering rollouts that you've. Can you comment on who may be partnering with those? I'm curious if the strictly for account deposit or card offering there as well. I'm just trying to the mechanics of that offering and how it rolls in your model. Thank you.

**Martin Mucci**

Yes. Bryan, I think we'll announce that probably a little bit later as we get into the last quarter – calendar quarter of this year for the pay-on-demand and because I guess I just want to be sure we're all together on before I announce it publicly who the partner is; there certainly is a partner there that we're doing it with. And then real-time payments, it's the same thing; one of the major banks, and I would wait until we get closer into the first part of the year just to make sure that everything is from a competitive standpoint, I don't want to give out too much too early, but we have partners in both, fairly solid relationships, everything we feel is in place. I just would like to announce those more as we roll it out; one will be in the next really now we're in October next couple of months and then one will be early 2020 for real-time payments.

**Bryan Bergin**

Okay, fair. And then just a follow-up on the Insurance Services business. The pressure from the workers' comp rate there, just your outlook on went out abates. Is it still just the moderation as you go through the second half comps?

**Efrain Rivera**

Yes. So it's a little bit lighter in the quarter than we had planned. And so I was a little bit more cautious as we went through the year. Our expectation is that in the back half of the year, it starts to abate and then by fiscal '21, I keep saying that, but fiscal '21 we should be past.

**Martin Mucci**

So the attachment rate is pretty solid. It's a continuation of the rates that this is – it cycles in and out, and we're just in that cycle where there is lower workers' comp rates and sales are OK. In fact, the attachment is up from last year on clients, but the rates are just lower and that driving in the revenue down and you got to kind of wait for the cycle back around.

**Bryan Bergin**

Okay. Thank you very much.

Okay, Bryan.

**Operator**

Our next question comes from the line of Samad Samana of Jefferies.

**Samad Samana**

Hi, good morning and thanks for taking my question. I just wanted to ask question about the new Paychex Solo offering and I'm curious how we should think about in terms of the size of the opportunity and what maybe go-to-market model is. Is it still got of direct sales organization or is it going to be similar to maybe some of your competitors to have more of an inbound type of model for their small customers? I'm just curious.

**Martin Mucci**

Yes. I think it's going to be a little bit of both. They certainly can be referred and sold by the field sales force. We're also going after it through the web and for leads and then the direct sales – telephonic sales force will be out selling it. We think it's a big market from a sole proprietor standpoint. When you – we found is there is that need for the retirement product and of course the incorporation services, and then if you find that sole proprietor that needs payroll and we can incorporate payroll, a simple retirement product and incorporation, we think we've got a nice market there. It's pretty new. It seems to be off to a good start, but I think we want to see it for a couple of quarters. But it has got a nice opportunity from that micro, this whole proprietor really marketplace as an offering, but it can be sold from a web lead, from telephonic sales or from the field as well. So we think we've got it covered across the field sales forces and we think we've got a nice tight clean product that will have some opportunity there for us.

**Samad Samana**

Great. And then maybe a question similarly on the other end of the spectrum, I mean, the company has invested significantly in its technology and a lot of the commentary today has been focused on that. I'm curious how you guys think about potentially starting to move upstream or targeting larger customers based on the technology investments that you've made and maybe what the company's view on that is.

**Martin Mucci**

Yes. I think our view is really that still that under 1,000 – I mean, we'll have some clients over 1,000 employees. But we focus – there is a big market and when you think about those mid-market, this 20 or 30 employees to 1,000 is a very big market that we think we're very well positioned for. Certainly, we have been from a service perspective, personal service perspective, but also from now from the technology perspective in the breadth of services in the need for those HR services have come down in size so much over the last three to four years and I think we've been very well positioned for that. So really not looking to get into that 1,000 plus generally unless there's a specific need that we can fill there, but we think that the best value, best margin and best approach for us is to stay very focused on a kind of 1 to 1,000 and specifically how we handle under 20 and how we handle 20, 30 to 1,000 is what's really taking off from a technology API in breadth of offerings that we provide. That's where the best margin is, that's what I think we're very well positioned from our experience and product set to be successful at.

**Samad Samana**

Great. Thanks for taking my questions and look forward to visiting the company at HR Tech today.

**Martin Mucci**

Okay .

**Efrain Rivera**

Thanks. We are looking forward to it.

**Operator**

Our next question comes from the line of Mark Marcon of Baird.

**Mark Marcon**

Good morning, Efrain and Marty. I was wondering, with regards to Oasis, just how much of that end up contributing to the expenses for this quarter and how should we think about that furthering and being rationalized is as this year unfolds and going into next year.

**Efrain Rivera**

Yes, Mark, I mean, I mean a lot of it as we call out in the in the press release is driven by Oasis, in particular, the amortization expense and operating expense associated with Oasis. You know, our – there is a lot of combination going on there, but combination of expenses, the expense growth ex Oasis would be somewhere in the 4% to 5% range.

**Mark Marcon**

That's very helpful. And then with regards to what you're seeing from a competitive perspective and then viewing that vis-à-vis all of the technology improvements that you've put together, what are you seeing in the 5 to 20-employee market, how should we think about that? And I'm particularly interested in terms of the new initiatives that you have in terms of being online sales, online implementation that was something that you talked about during the last quarter, what are some of the early results there?

**Martin Mucci**

Yes. They look pretty solid, Mark, particularly I'd say 5 to 10, we focus very much on virtual sales or telephonic sales and in driving those leads. We were doing the 1 to 4 leads internally with telephonic sales because of the speed from lead to close and we had a lot of success as we built the teams out for that last year. We moved the 5 to 9 leads, the majority of those inside the web leads to the inside sales teams for the same reason, we're off to a good start, both on lead demand generation, the way we nurture those leads and get them to inside sales and then our handling those leads that also frees up the field sales forces to get more of the larger customers in that, let's say, under 20 in that frees that small business rep team up to do that. So we're seeing a good start to the year on that. Competitively, not seeing any big changes there we're seeing kind of the same players. I know there is one that's talking about that they've been going down market. I haven't really – we haven't really seen an impact of that much at all. I think again the investments that we made in the technology, the reputation we have for service to that under 20 really bodes very well for us. So I think it's, we haven't seen a big change in the competitive environment and actually, we're off to a pretty good start we feel.

**Mark Marcon**

Great. And then with regards to interest rates, obviously, the Fed has done some things, but rates are actually going is different than what they were basically targeting. When we take a look at like your incremental effective yield in terms of what you're placing now relative to what the effective you have us on the overall portfolio, how does that compare percent right now?

**Efrain Rivera**

I think you're probably, Mark, somewhere in – boy, you asked a great question, which requires layers of layers of explanation. So I will try to summarize it. Unlike other people 45% to 50% of our portfolio is invested short term. So you get an immediate decline on the short-term part of the portfolio by whatever the Fed does. So if you're in the 1.5% range, that's what you're getting on the short-term portfolio, and then if you drop, you lose the 25 bps that – if you have a decline of 25 bps then you're going to lose immediately 25 bps, I mean, immediately, but 30 days or so. So, on the short-term portion of the portfolio, that's what happens. On the long term, it's a little bit trickier because there you're really kind of turning that portfolio over about 20% of that portfolio turns over and I think that we called out in the script. It's a little bit above our effective yield notes, a little bit above 2%. Current investment rates will depend on that frankly on the shape of the yield curve, which in some ways is anyone's guess, but I would say, now you're your 25 bps to 50 bps below where you were when you started the year. Now, I just read an article yesterday. I'm sure you read the same articles I do about kind of what the Fed is anticipating doing or not doing so and I caution taking it to the bank, but that's depend indicator of where we are. And then the final thing which is the third part is we do have opportunities if we see where the yield curve – the shape of the yield curve to extend duration, right now, we said duration was about 3.1 we had flexibility to go longer if we want to, so all of those are the puts and takes.

**Mark Marcon**

I was specifically thinking about that 20% that's rolling over. That would be incrementally invested relative to –

**Efrain Rivera**

Yes, Yes, that's what I said. So you're probably in the 25 bps to 50 bps below.

**Mark Marcon**

But relative to the effective yield that we're currently getting.

**Efrain Rivera**

Yes. Right. I'm sorry, yes, yes.

**Mark Marcon**

Okay, great. And then with regards to some of these new initiatives that you're rolling out that I'll be demoing today at HR Tech, what sort of contribution do you think they're going to end up having as you start making the plans for '21 and how does that impact the size of the sales force?

**Martin Mucci**

Yes. I think from – I'm glad you're out there. The group is excited to demo everything at HR Tech. I think it's always with us with a number of clients we have, it's a small impact to start as we ramp up penetration rates and attachment rates. But I think it does bode well for '21 to get these things and see how we're growing. From a sales force perspective, I think there could be continued growth there, but I think we're also looking for continued productivity with the sales force. We have a very talented sales leadership team and sales force that is always looking to sell more products in the way we're approaching as I mentioned earlier is the power of those 3,000 plus reps selling kind of all of our products, not just the yield traditional way where we would sell payroll first and come back and we're finding much more success, whether it's the small market or the mid-market kind of coming in looking for the value, the client is looking for overall, the needs that they have and selling that completely. So we may have some continued increase in reps, as we see opportunity and there'll be also some increase inside and outside probably from a telephonic sales and field sales perspective.

**Mark Marcon**

Great. Thanks..

**Martin Mucci**

Okay, Mark. Take care.

**Operator**

Our next question comes from the line of Jason Kupferberg of Bank of America/Merrill Lynch.

**Jason Kupferberg**

Hey, guys. Just wanted to follow up on the commentary around the mid-market sales, you certainly sounded bullish there. It sounds like you think that trend is sustainable. So I just wanted to get your perspective from kind of share gain standpoint if you think that this is something that's going to be continuing for a while. So it feels like historically market is maybe where you would highlight some more competitive intensity and now it sounds like you're clearly making some strides to overcome that.

**Martin Mucci**

Yes, I think a couple of things; one, I think from a share perspective, the market has continued to grow. So the good news is while I think we certainly are doing well from a competitive close rate when we're in there, the market itself is growing. So the need for HR has continued to come down in size, so clients that were looking for different solutions at 100, 200 to 300 employees are now looking for those at 50 employees or 40 or 30 employees. So meaning full time and attendance, you just see the over-time rule just came out and changed and put more focus on over-time. Clients will be looking for more time and attendance solutions. And when you can now have the technology of wearables and geo-fencing to say, hey, if they're working remotely they're working from home or another location, you can track all that and they can do it on their watch, all those things make you very viable to even a smaller client than used to think they could afford that kind of thing. And the smaller client needs it. So the market itself is growing from an HR and full service perspective, and then I think the competitive environment really hasn't changed much. I don't – there hasn't been new competitors; different competitors have their strengths and weaknesses. And I think right now between the technology and the service model we have, I think it's a very strong, and we do feel very good about the first quarter and I think what we feel like the momentum is there for certainly the rest of the year and beyond.

**Jason Kupferberg**

Okay. And Efrain, I think it may have been two quarters ago, you had suggested Oasis could do $335 million to $375 million in revenue in fiscal '20, if I've got that right. Is that still the right range? And any thoughts on where within that range might be most likely now that you're about a third of the way through the year?

**Efrain Rivera**

Yes, I don't recall that specific one, but I think we're in that range, Jason. The one thing I would caution is that's total, there's a few revenue streams in there that are reported not just on the PEO side; part of the classification change we made at the end of the year was one of those revenue streams and we had been reporting part of the ASO revenue that Oasis provided. It's not a huge amount, but it's part of that total.

**Jason Kupferberg**

Okay. And then just real quick last one, buybacks uptick pretty materially this quarter. Just an update on what's left on the authorization there and any implications or ways we should interpret that in the context of what might be in your M&A pipeline?

**Efrain Rivera**

Well. That's a good one, Jason. That's a good – that was good, I was tracking there. So, Yes, no, look, shares had crept up – that was a good one, I would say; that's a question of the day. Shares had crept up a bit and – just because it was clever, the shares it crept up a bit and we're committed to keeping our share count flat. So we thought it made sense to be a little bit more aggressive. It really has no implication whatsoever on M&A. We've got still a lot of dry powder and we got a lot of opportunities that we're looking at. And then finally, I think we've got about $250 million or so left on the authorization. But, look to the extent that we needed to get more, we could of course have that conversation with the Board.

**Jason Kupferberg**

Yes. Got it. Thank you, guys

**Efrain Rivera**

You're welcome.

**Operator**

Our last question comes from the line of Kevin McVeigh of Credit Suisse.

**Kevin McVeigh**

Great, thanks for letting me back in. Hey, not to belabor the attrition, but Marty, you go to kind of more of the tech-enabled HCM kind of the incremental disruption from switching full suite versus payroll. Does that reset the opportunity on the attrition side longer term, and is there any way to think about what a longer-term target would be with the kind of new revenue contributions?

**Martin Mucci**

Yes. Good question. I think it does to some degree, although you still got to think about the mix of the clients. So with our mix still definitely toward the low end and with the growth of that under 20 market, that won’t change too dramatically, but it certainly gives us a much better retention tool when you think about also the mobile app in the tied to employees. The services that we’re selling more and more to the direct employees and how they’re using that mobile app really gives us kind of a fresh start on retention. But to the degree that a large majority of our clients are still under 20 and that base is still susceptible to start-ups and turnover and that kind of thing. So can we get retention better overall, I certainly we’re always looking to break records on it. I don’t think it will be huge though, given the makeup of the client base.

**Efrain Rivera**

Hey, Kevin, one build on what Marty said, so while we report client retention, your question really goes to revenue retention and revenue retention has been running in the mid-80s and so I think that as more of these products stick, you do have an opportunity even if a client retention is not materially different to have a bit better revenue retention and so certainly we would hope to see more of that.

**Kevin McVeigh**

And that probably gets wider tend that revenue retention versus client, is that a fair way to think about, Efrain, versus history?

**Martin Mucci**

That's correct. Yes.

**Kevin McVeigh**

Thank you.

**Efrain Rivera**

Okay.

**Operator**

And that was our final question.

**Martin Mucci**

Operator, I think that's it, right. Alright. At this point, we will close the call. If you're interested in replaying the webcast of this conference call, it'll be archived for approximately 30 days. Thank you for taking the time to participate in our first quarter press release conference call and for your interest in Paychex. Have a great day.

**Operator**

Thank you. Ladies and gentlemen, this does conclude today's conference call. You may now disconnect.