28-Oct-2019

TrueBlue, Inc. (TBI)

Q3 2019 Earnings Call

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A. Patrick Beharelle
Director & Chief Executive Officer, TrueBlue, Inc.

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Henry Sou Chien
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Mark S. Marcon
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MANAGEMENT DISCUSSION SECTION

Operator: Thank you for calling and welcome to the TrueBlue Third Quarter 2019 Earning call. I will now turn the call over to Derrek Gafford, Executive Vice President and Chief Financial Officer. Please go ahead.

Derrek L. Gafford
Executive Vice President & Chief Financial Officer, TrueBlue, Inc.

Good afternoon, everyone and thank you for joining today's call. I'm here with our Chief Executive Officer, Patrick Beharelle.

Before we begin, I want to remind everyone that today's call and slide presentation contain several forward-looking statements, all of which are subject to risks and uncertainties, and we assume no obligation to update or revise any forward-looking statements. These risks and uncertainties, some of which are described in today's press release and in our SEC filings, could cause actual results to differ materially from those in our forward-looking statements.

We use non-GAAP measures when presenting our financial results. We encourage you to review the non-GAAP reconciliations in today's earnings release, or at trueblue.com under the Investor Relations section, for a complete understanding of these terms and their purpose.

Any comparisons made today are based on a comparison to the same period in the prior year, unless otherwise stated. Lastly, we will be providing a copy of our prepared remarks on our website at the conclusion of today's call, and a full transcript and audio replay will also be available soon after the call.

With that, I'll turn the call over to Patrick.

A. Patrick Beharelle
Director & Chief Executive Officer, TrueBlue, Inc.

Thank you, Derrek, and welcome everyone to today's call. We appreciate you joining us. Strong execution drove better than expected top line and bottom-line results this quarter. While revenue growth has yet to return, we were pleased to see monthly revenue trends were consistent during the quarter and we delivered another quarter of earnings growth. TrueBlue has been driving digital disruption within the staffing industry with our JobStack and Affinix offerings, and we continue to experience favorable employee and customer adoption.

We remain squarely focused on client expansion and retention, disciplined cost management, and investing in our digital strategies to differentiate our service offerings. We also announced today that our board of directors approved an additional $100 million of share repurchase. Our board remains highly supportive of our focus on opportunistically repurchasing shares and returning capital to shareholders.

Now, I'd like to update you on the financial results and strategic initiatives within each of our segments starting with our largest segment PeopleReady. PeopleReady is the leading provider of on-demand labor and skilled trades in the North American industrial staffing market and represents 62% of trailing 12-month total company revenue and 59% of segment profit. PeopleReady's revenue was down 4% during the quarter due to lower business activity across our client base. Growth at PeopleReady was favorably impacted in Q3 by project work at one of our clients, creating a 2% year-over-year growth benefit.

Excluding the project work I just mentioned, underlying monthly revenue trends at PeopleReady were consistent throughout the quarter. Consistent with our focus on managing costs across the business, we've been taking a hard look at PeopleReady's cost structure. Since our last earnings call, we've taken cost actions that are expected to result in approximately $10 million of net annualized savings. It's important to note that these reductions were focused on mid-level management and support positions and did not impact branch staff or sales resources.

Derrek will provide additional information including the expected impact to Q4 in conjunction with our outlook. As always, our objective is to balance smart cost management with strategic investments to build our client base and drive growth.

One example, we touched on last quarter is PeopleReady's new client experience team. This is a team of seasoned operational and sales leaders, who are dedicated to enhancing client satisfaction by proactively reaching out in the critical early days and helping clients move up the curve in terms of JobStack usage. While the program is still in its infancy, the feedback from our branch-based colleagues and our customers has been overwhelmingly positive. The team is also helping us proactively drive more activity through our strategic cross-selling program, which continues to drive revenue growth year-over-year for TrueBlue. We have several customers, where overall, we've uncovered millions of dollars in additional revenue.

Our digital transformation via our JobStack mobile app remains one of the most important strategic initiatives within PeopleReady. Our JobStack mobile app is transforming the way we do business. Over the past several quarters, we've seen disproportionately high-revenue growth from clients that are heavy users of JobStack. We've been working hard to build the critical mass we need within the app and we're very pleased with the progress we've made on that front. We've deployed more than 1 million shifts via JobStack during the quarter, representing a digital fill rate in excess of 40%, up from approximately 30% as recently as the fourth quarter of 2018.

Associate adoption is now 87% and we have approximately 19,000 clients using the app, up from 13,000 in December. We also recently announced a new strategic relationship with Uber Works. Uber Works is separate and distinct from JobStack, and this new venture represents another step forward in our digital strategy for temporary staffing.

Uber Works is a platform that connects workers with businesses that need to fill available shifts. Now, while Uber Works has a great platform, one area they don't have experience is paying and managing W2 employees. So, Uber Works turned to TrueBlue for help, and we've created a new business venture called PeopleWorks, to serve as an employer and payroll service provider for workers booking jobs on the Uber Works app.

It's early days for the PeopleWorks venture and we don't know yet if there will be a longer-term material impact. But it's clear that Uber Works' choice to work with TrueBlue is a testament to the strength of our payroll offering, world-class service and decades of expertise in on-demand staffing.

Turning to our next segment, PeopleManagement provides onsite workforce solutions in the North American industrial staffing market that offers compelling value and are a perfect fit for larger clients with longer duration strategic needs for contingent workers. This business represents 27% of trailing 12-month total company revenue and 10% of segment profit.

Revenue was down 12%. Roughly half of this decline is due to previously disclosed headwinds namely, the loss of Amazon's Canadian business, and volume and price reductions at another retail client. The remainder is due to less same customer demand due to lower activity levels within their own businesses. We are pleased with the strength of our year-to-date new business wins, which are up 20% over the same period last year.

Turning to our last segment, PeopleScout is the global leader in filling permanent positions through our recruitment process outsourcing and managed service provider offerings, and represents 11% of trailing 12 months total company revenue and 30% of segment profit. Revenue was down 9% overall primarily due to previously disclosed headwinds, namely one client that was lost after being acquired, and less volume and lower margins at another large account that was repriced to reflect a multiyear arrangement.

In spite of these recent headwinds, we like the strength of our service offerings and are getting good traction.

During Q3, PeopleScout was recognized as an enterprise RPO leader in HRO Today's 2019 Baker's Dozen Customer Satisfaction rankings. PeopleScout was also ranked as a healthcare RPO leader on this year's survey. Additionally, PeopleScout was identified by NelsonHall as a leader in every category in their 2019 evaluation of the RPO marketplace.

Our strategy for PeopleScout is unchanged, and is aimed at capitalizing on our leadership position in the North American RPO market to expand our global capabilities and differentiate our service offerings through technology. Affinix is our proprietary next-generation HR tool that is improving our ability to compete in the marketplace.

For example, in several recent winning, sales pursuits RPO buyers shared with us that Affinix was a clear differentiator and a key reason for PeopleScout being selected. Moreover, clients fully implemented on Affinix are experiencing improved time to fill, candidate flow and candidate satisfaction. Summarizing our performance, we're executing on our three primary initiatives of putting our segments on a path towards sustainable growth, managing our cost to enhance profitability and leveraging excess free cash flow to return capital to shareholders.

These areas of focus along with our strategic use of technology, which is something that our clients are embracing regardless of the ebbs and flows of their own businesses will help us capture the many opportunities ahead in the changing world of work.

I'll now pass the call over to Derrek, who will share greater detail around our financial results.

Derrek L. Gafford

Executive Vice President & Chief Financial Officer, TrueBlue, Inc.

Thank you, Patrick. Total revenue was $637 million was at the high end of our $613 million to $638 million outlook. The better performance was driven by $11 million of benefit from project work with one client that was not anticipated in our Q3 outlook. Total revenue was down 6% which was larger than the decline in Q2 of 4% due to the anniversary of the TMP acquisition in Q2. Organic revenue was down 6% which was consistent with the decline in Q2 of this year. Excluding the project previously mentioned, monthly revenue trends were consistent during the quarter.

Turning to the bottom line, net income per diluted share of $0.68 exceeded the high end of our $0.50 to $0.60 outlook and adjusted net income per diluted share of $0.76 also exceeded the high end of our $0.61 to $0.71 outlook. EPS was up 11% and adjusted EPS was down 4% on top of strong EPS and adjusted EPS growth in Q3 last year up 20% and 32%, respectively. The better than expected EPS and adjusted EPS results were primarily due to the revenue beat and a variety of cost management actions.

In addition, the effective income tax rate for the quarter of 10% was below our 14% expected rate due to additional Work Opportunity Tax Credits. Gross margin of 26.6% was down 50 basis points primarily due to higher workers' compensation expense and the previously disclosed headwinds at PeopleScout. Workers' compensation expense as a percentage of revenue this quarter was consistent with Q2 this year but higher than Q3 last year.

SG&A expense was down $14 million, $3 million of which is due to lower adjusted EBITDA exclusions and the remainder due to a variety of cost management actions. SG&A was down 10%. And SG&A as a percentage of revenue was down 80 basis points. Excluding adjusted EBITDA exclusions, SG&A was down 8% or 30 basis points. We've also taken a number of actions to reduce operating costs in the future. This will produce $2 million of benefit in Q4, offset by a charge of $2 million which will be excluded from adjusted net income and adjusted EBITDA. These actions are also expected to provide $11 million of benefit in 2020, $3 million of which we plan to reinvest into customer acquisition and retention activities, resulting in $8 million of net benefit in 2020.

Throughout 2019, we’ve consistently discussed some revenue and segment profit headwinds within our PeopleScout business associated with the repricing of an account and the loss of a client that had been acquired by a strategic buyer. Similarly, in our PeopleMnagement business we discussed the transition of a customer from our SIMOS business to our Staff Management business and the diminishing impact of the lost Amazon account. This quarter, these items suppressed total company revenue by $16 million and adjusted EBITDA by $6 million. Adjusted EBITDA of $39.3 million was down 10% due to lower revenue, and related margin was down 20 basis points as a result of lower gross margin.

During the quarter, we repurchased $22 million of common stock, bringing our year-to-date repurchases to $31 million, which represents about 90% of year-to-date free cash flow. This activity took the amount remaining under our 2017 authorization down to $27 million and we're pleased to announce today that our board of directors authorized an additional $100 million share buyback. This authorization reflects our confidence in the long-term outlook for our business and our desire to continue to return capital to shareholders.

Turning to our segments, PeopleReady revenue was down 4%, which was better than expected but a step down from the 2% decline in Q2. As discussed earlier, revenue was favorably impacted by project work at one of our clients creating $11 million of benefit in comparison with our Q3 outlook. Excluding the project work, underlying monthly revenue trends were consistent throughout the quarter. Segment profit was down 1%.

PeopleManagement revenue was down 12% which was consistent with our expectation. Of the 12% decline, 5 percentage points came from the previously disclosed customer headwinds, and the remainder from lower same-customer demand. Segment profit was down 45% which includes $2 million or approximately 27 percentage points of decline from the headwinds previously discussed.

PeopleScout revenue was down 9% which was also consistent with our expectation. Segment profit was down 14% which is primarily associated with the previously discussed headwinds.

Turning to cash flow for the company, year-to-date cash flow from operations totaled $53 million and capital expenditures were $18 million netting to free cash flow of $35 million. The overall strength of our balance sheet continues to improve. Total debt of $44 million is down from $80 million at the end of 2018 and our debt to capital ratio is 7%. On a trailing 12-month basis, our total debt to adjusted EBITDA multiple stands at 0.4.

Turning to our outlook for the fourth quarter of 2019, we expect a revenue range of minus 10% to minus 6%. The midpoint of the range is 2 percentage points lower than the 6% decline posted in Q3. 1 percentage point of the step down is due to the roll-off of some of the project work that favorably impacted Q3 results. The remaining step down is due to softening trends experienced in early October. The step down occurred across most geographies and industries, with notable softening within the construction vertical of our PeopleReady business and in the same customer demand trends within our PeopleManagement business.

We expect net income per share of $0.18 to $0.28 or $0.35 to $0.45 on an adjusted basis, which assumes a share count of 38.4 million, and an effective income tax rate of 14%, The midpoint of our EPS guidance is a decline of about 40% versus growth of 11% in Q3 this year. The drop in the trend is primarily due to a deceleration in the revenue trend. I mentioned a few moments ago, and to a lesser extent, lower gross margin and a lower decline in SG&A expense.

The lower gross margin is primarily due to the timing of payroll tax benefits which were recognized throughout 2019 versus an annual true-up in Q4 last year. We're expecting a lower decline in SG&A expense in Q4 versus Q3, due in part to the anticipated charge in Q4 discussed earlier, related to the additional cost reduction actions.

Lastly, I'd like to remind everyone that the Work Opportunity Tax Credit expires at the end of this year. While this program has been in existence for decades and we expect this program to be renewed due to its appeal to both political parties, the timing can be lumpy. Since this program contributes about 10 to 12 percentage points of benefit to our effective income tax rate, if it is not renewed, we would expect an effective income tax rate of about 26% to 28%. Additional information on our outlook for the fourth quarter and certain annual assumptions can be found in today's earnings release deck.

While some economic uncertainty exists, our focus is clear. We're staying committed to our digital strategies. We believe we are leading the industry in moving to a more digitally-oriented business model to differentiate our services and acquire market share. We plan to invest in customer acquisition and retention initiatives, to not only acquire more business, but to ensure we come out strong when the economic climate improves. We also plan to stay diligent in managing our operating costs. And lastly, we're committed to returning capital to shareholders through stock repurchases.

This concludes our prepared remarks. We'll now open the call for questions.

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] Your first question comes from the line of Josh Vogel with Sidoti and Company. Please go ahead.

Josh Vogel
Analyst, Sidoti & Co. LLC

Q

Thank you. Good afternoon, guys. My first question, Derrek, you mentioned there was some roll-off in Q4 from that large project that PeopleReady that contributed $11 million of additional revenue. What is your expectation for the contribution from this project in Q4 that's built into your guidance?

Derrek L. Gafford
Executive Vice President & Chief Financial Officer, TrueBlue, Inc.

A

Yeah. Hi, Josh. We expected to be about half that rate. So, that roll-off is contributing to about, 1 point of revenue headwind, additional revenue headwind in Q4 because of the roll-off, call it, $5 million to $6 million less in revenue.

Josh Vogel
Analyst, Sidoti & Co. LLC

Q

Okay. Great. So, I know you continue to invest in digital strategies and for good reason. And now that we're nearing the end of the year, I was just curious how you feel on this front entering 2020? How much more are you planning to invest in these offerings, if at all, or do you feel the capabilities are fully there now it's just about scaling them up further?

A. Patrick Beharelle
Director & Chief Executive Officer, TrueBlue, Inc.

A

Hey, Josh. This is Patrick. A big part of our focus in the fourth quarter and in 2020 is to leverage the phenomenon that we've seen of clients that are heavy users of JobStack. We've seen disproportionate growth for those clients that are using JobStack in heavy way versus those that are using it in a moderate way or not using it and also a big part of our investments in Q4 in 2020 is around sales and marketing campaigns to target our existing client base to use the tool more because as I mentioned earlier, we've seen disproportionate growth north of 20% year-over-year growth and those clients that are using it heavily.

We're also making some investments around the acquisition of talent with the tool. So, we're going to be rolling out some new features in the first quarter that we think are going to help drive more candidate flow. So, we're looking at this from two ways both from a supply perspective and from a demand perspective. So, those will be the areas of focus.

Yes, just to put in perspective some numbers for you, as we think about 2020, we finished the year – we'll finish the year somewhere around 45% or so of our fills coming in a digital way. We think we can get that number closer to 55% by the end of 2020. We'll finish the year around 21,000 clients on the tool. We think we'll get closer to 30,000 by the end of 2020. Shifts will do around 4 million or so this year. We think we can get that number north of 5 million. So, these are some goals that we've set for ourselves in terms of 2020 and continuing progress on our digital strategy.

Josh Vogel
Analyst, Sidoti & Co. LLC

Q

That's helpful. Thank you. Just looking at some of the – you had a repricing of an account at PeopleScout and I was just curious, are there any other notable or sizeable clients whether within PeopleScout or maybe PeopleManagement where you're currently engaging or exploring similar type of repricing arrangments?

A. Patrick Beharelle
Director & Chief Executive Officer, TrueBlue, Inc.

A

Well, any time a client comes up for renewal, there's conversations around repricing. I wouldn't say there's any outside the normal course of business, Josh, so I wouldn't expect us to be making any announcements about significant price concessions or price increases. It'll be more normal course of business.

Josh Vogel
Analyst, Sidoti & Co. LLC

Q

Okay, great. And if I could just sneak in one more, nice to see the cost reduction efforts that'll result in I guess about $8 million in net annualized cost savings next year. Is that something that you think will be spread out evenly over the course of the year or will be more back-end heavy?

Derrek L. Gafford
Executive Vice President & Chief Financial Officer, TrueBlue, Inc.

A

Hi, Josh. It's Derrek here. Yeah, that will be relatively consistent through 2020.

Josh Vogel
Analyst, Sidoti & Co. LLC

Q

Okay, great. Thank you for taking my questions.

Operator: And your next question comes from the line of Kevin McVeigh with Credit Suisse. Please go ahead.

Kevin McVeigh
Analyst, Credit Suisse Securities (USA) LLC

Q

Great. Thank you. Patrick, how are you?

A. Patrick Beharelle
Director & Chief Executive Officer, TrueBlue, Inc.

A

Great. Thanks, Kevin.

Kevin McVeigh
Analyst, Credit Suisse Securities (USA) LLC

Q

[ph] Just two question (00:20:57), fantastic. Hey, Derrek. Derrek, just one point of clarification. Was the $11 million kind of the onetime revenue, was that contemplated in the guidance at the time you issued it or was it – does that kind of come in after the guidance has gotten issued?

Derrek L. Gafford
Executive Vice President & Chief Financial Officer, TrueBlue, Inc.

A

That came in after the guidance was issued, Kevin. We're – our job is just to run the business we can based on any set of circumstances that are coming along economically. [ph] And we set the guidance (00:21:25), that's what we know of at that point in time, and we've been doing, of course, some analysis and had some ideas about some things that we wanted to do, but really that were picked up after the guidance was issued.

Kevin McVeigh
Analyst, Credit Suisse Securities (USA) LLC

Q

Got it. And is there any way to frame, is it the type of thing where the incremental margin on that would be high or was it kind of consistent with what the corporate average is overall?

Derrek L. Gafford
Executive Vice President & Chief Financial Officer, TrueBlue, Inc.

A

Well, give that to me one more time on the cost because I'm not following you on the margins. [ph] We got the dollars (00:22:02).

Kevin McVeigh
Analyst, Credit Suisse Securities (USA) LLC

Q

I guess, I guess on the revenue side of it, would the margins associated with that $11 million of revenue consistent with the corporate average in the quarter or was it kind of maybe a little bit higher given – just trying to get a sense of what the margin profile of that revenue stream was.

Derrek L. Gafford
Executive Vice President & Chief Financial Officer, TrueBlue, Inc.

A

Well, you should think about it this way. Those cost savings it didn't come from variable cost reductions associated with revenue declines or anything like that. That $11 million that we're talking about for 2020, by the way, we're going to be reinvesting three of that, so we will deliver $8 million of net is – are just cost reductions that we've made broadly across the business. Now maybe you're referring to the margin on the extra project work?

Kevin McVeigh
Analyst, Credit Suisse Securities (USA) LLC

Q

Yeah, that's right, Derrek.

Derrek L. Gafford
Executive Vice President & Chief Financial Officer, TrueBlue, Inc.

A

Okay. Now that's – well it's a little bit above the average but right at the PeopleReady blended average incremental, standard incremental for PeopleReady mid-teens.

Kevin McVeigh
Analyst, Credit Suisse Securities (USA) LLC

Q

Got it. And then, you said this and I apologize it's just – I was muddled on the call, my line. The 150 basis points of margin erosion in the next quarter was that a function of the revenue or was that worker's comp or is there worker's comp dynamic that maybe – I just – I didn't hear that if you could just refresh me on that?

Derrek L. Gafford
Executive Vice President & Chief Financial Officer, TrueBlue, Inc.

A

Well, we are expecting the gross margin – gross margin in Q3 this year versus Q3 last year was down 50 basis points, partly because of workers' compensation and then partly because of the mix on some of these client headwinds that we've talked about.

But we go to Q4 we're expecting the year-over-year gross margin to be down about 80 basis points or call that 30 basis points of more incremental decline. And that's largely tied with payroll taxes. We had some payroll tax benefits that we trued up at the end of 2018 and we have some more in 2019. We've been realizing that benefit every quarter. So that's mostly timing on the gross margin.

Then you got the extra 2 points of revenue decline and the deleveraging that comes along with that. And then on the SG&A side, we still have a nice SG&A decline built-in but it's not quite as large as what we had in Q3, somewhat because of the extra charge we're taking on these cost savings that's in our guidance of $2 million.

Kevin McVeigh
Analyst, Credit Suisse Securities (USA) LLC

Q

Helpful. And then just it sounds like there was kind of a little bit of a step down in terms of couple – 100 to 200 basis points. [ph] What are you seeing that? (00:25:01) And I guess just within the context of there's been so much debate on the macro, is it – Derrek, does that [indiscernible] (00:25:11) – does that feel more like kind of a traditional pause or something that's kind of the initial stages is something maybe a little bit more – that your monitor?

Derrek L. Gafford
Executive Vice President & Chief Financial Officer, TrueBlue, Inc.

A

Well, I'll talk about this last step-down that we saw and then we incorporated in the guidance towards the end of my answer, Kevin, but to just to kind of reframe the answer, is kind of addressing your bigger-picture question. This has been an interesting year because we've seen really three step-downs this year.

We saw one at the end of March and first week of April. We saw one during the first couple of weeks of July and also on the first couple of weeks of October. And what's been interesting about it is it's been both at our PeopleReady business and in our PeopleManagement business. And [ph] we've really (00:25:58) shows up in our same customer trends in our PeopleManagement business.

So, we don't think that we've – well, we've always got room for improvement here. We don't think that there's anything that we're doing different in the business model. So, we really do think this is macro-driven. When it comes around to how we run the business and look at that, we're just going to continue to make the right adjustments as we see those step-downs. Our take with customers is that everybody remembers the last recession. It snuck up on everybody and everybody is watching these economic signals very closely and trying to make real timely adjustments to the workforces. And we believe that's what we're experiencing in our trends as we look at the business.

In regard to your specific question about the most recent step-down, it was at -- both at PeopleReady and at PeopleManagement. Again at PeopleManagement, same customer demand trends, no lost clients. On the PeopleReady side, it was fairly broad-based across a variety of geographies and customer types and sizes. If you had to pick one though that stood out the most, it would be in the construction area for PeopleReady. So, I hope that gives some more color to our thoughts.

Kevin McVeigh
Analyst, Credit Suisse Securities (USA) LLC
Q

Yeah. Super helpful, Derrek. Can I just -- if I could, and I'll get back in an interest of time, on the construction side, was that kind of residential or the commercial? And then just – is any of it may be an impact from GM and/or Boeing that maybe comes back or do you think this is again is kind of the initial [ph] page (00:27:40) maybe something that's and tariff-related or is it because I'm sure there's a lot of uncertainty out there. Is it the [indiscernible] (00:27:49) I guess the conversations? Is it more something you think it's a little longer in duration or something that again, it's right to get Boeing ahead General Motors. You obviously at the tariff crosscurrents and is it any state-specific or just pretty broad?

Derrek L. Gafford
Executive Vice President & Chief Financial Officer, TrueBlue, Inc.
A

It's pretty broad, and in answer to construction, it was both in residential and in non-residential but non-residential has the biggest impact to us of our – it makes up two-thirds of our construction business. In thinking about, how long is this and how does this carry itself on? It's a really hard question to answer Kevin. I don't know really the answer to that one.

There are a lot of things going on out there from trade policies to manufacturing [ph] data and a variety of other (00:28:40) things, so we're just continuing to -- keep our eyes really closely on it and stay really and very in touch with our customers, serve them well and make adjustments as best we can to both preserve the profitability level of the company but at the same time fund investments for 2020 when it comes to customer and candidate acquisition or retention.

Kevin McVeigh
Analyst, Credit Suisse Securities (USA) LLC
Q

Understood. Nice job and obviously a tough environment.

Operator: And your next question comes from the line of John Healy with Northcoast Research. Please go ahead.

John Healy
Analyst, Northcoast Research Partners LLC
Q

Thank you. I wanted to ask you guys to dive in a little bit more about the Uber relationship. I apologize, but did you guys call that a joint venture? Is that a partnership? Is that a business relationship, just agreement? Just trying to understand the structure of how you're working with them? And then, additionally, if the payrolling opportunity that you're working with them on, if that's exclusive, that it has an update on a ceiling to it, or an upward range of, how fast that can roll out as well?

A. Patrick Beharelle
Director & Chief Executive Officer, TrueBlue, Inc.
A

Thanks, John. It's Patrick. In terms of our relationship with Uber, think of it as a business relationship where Uber is a client of ours and in terms of the impact to TrueBlue, we expect the near term impact to be relatively small. As you might imagine the degree of impact on TrueBlue, it's directly related to the pace of scaling and the degree of success that Uber Works, ultimately has in the marketplace. We started in Chicago; we'll be expanding to other cities soon.

Our vision for the partnership is really straightforward. We believe the light industrial staffing market along with some adjoining staffing verticals are ripe for digital transformation. As you know, we've been investing heavily in our capabilities and are seeing firsthand in the early stages of that transformation. So, we're pretty confident in the digital capabilities that we've rolled out in our business via JobStack and is a best-in-class solution and ultimately, we think will drive above-market growth.

One important point to note about this relationship with Uber is that, when you study other industries that have been disrupted, oftentimes the pie has gotten bigger. A good example is Uber in the cab dispatch business, end-user behavior changed and created a bigger pie, and we think that there's elements of that phenomenon here as well.

And so what's in it for TrueBlue with the partnership? First, if Uber Works proves to be successful this would be lucrative for TrueBlue. And will profit from the partnership's success. There's the obvious revenue and EBITDA lift that would come from the services that we're providing.

Secondly, by partnering with the nimble and innovative company like Uber, we think there's some practical learnings that will accrue to both companies. We've already seen some of that happen already.

And then thirdly, we view Uber Works as an anchor client and should we decide we want to launch employer of record services to other companies with similar needs, we have that additional optionality in terms of a referenceable anchor client to jumpstart that effort.

Related to your question on is this an exclusive relationship? We're one of two. We're the much larger partner among the two. And so, it's not completely exclusive but it's limited to two firms that are providing support with us being the larger of the two.

John Healy
Analyst, Northcoast Research Partners LLC

Q

Great. And along those same lines and I don't want to get too much into the world of science fiction, but if you thought about kind of [ph] Uber and Wix (00:32:41) in kind of the ride-hailing or the digital category in itself, is there any interest or is there any talk about potentially working to become the employer of record for those potential drivers that are on those platforms? I know in some states there are some legislative battles that that might be starting up. I was just curious as you studied that kind of – if you guys have studied that part of the market and if that is something that potentially could be on the horizon for the company?

A. Patrick Beharelle
Director & Chief Executive Officer, TrueBlue, Inc.

A

Well, I just say this I wouldn't rule it out. We've certainly taken a look at it. We want to be prepared should that eventuality come but I don't think we're ready to make any pronouncements on that yet. Certainly, there could be a pretty significant business opportunity there down the road.

John Healy
Analyst, Northcoast Research Partners LLC

Q

Understood. Understood. And then just final question for me. As you guys look in the calendar for the fourth quarter, is there anything worth noting in terms of the days or the way the holidays fall, and just how you think about weather and the pluses and minuses, how those things add up for the fourth quarter? Thanks.

Derrek L. Gafford
Executive Vice President & Chief Financial Officer, TrueBlue, Inc.

A

Well the one thing that I'll mention is that there be a slight benefit this time around with – slight less benefit because Christmas falls on Monday versus a Sunday last year. So there could be a slight negative impact, or – excuse me, got my dates wrong. It falls on a Wednesday versus a Tuesday. So there is a little bit more during the middle of the week versus the earlier part of the week, so there could be a slight amount of that headwind from that but nothing worth – significant worth calling out, John.

John Healy
Analyst, Northcoast Research Partners LLC

Q

Thank you, guys.

Operator: And your next question comes from the line of Henry Chien with BMO. Please go ahead.

Henry Sou Chien
Analyst, BMO Capital Markets (United States)

Q

Hey, guys, good afternoon. I wanted to ask about the planned cost cuts and investments. Just wondering if you could talk a little bit more about sort of where you're finding the efficiencies and [indiscernible] (00:34:52).

A. Patrick Beharelle
Director & Chief Executive Officer, TrueBlue, Inc.

A

Thanks, Henry. Yeah. The cost cuts that we made were in the PeopleReady organization. And specifically, I'll start by saying where we did not cut. We did not make any cuts in our branch organization. In fact, we're adding some resources in that area. So folks that are working with workers and working with clients on a day-to-day basis, there were no cuts in those areas.

We made a number of cuts more at the senior levels in terms of the leadership team and one and two layers down from that organization. So, we're flattening the organization, bringing the leadership team closer to the field organization. We also received some concession from some of the vendors that support us as well. So, it wasn't all in the area of head count reduction. It was a pretty broad-based look where we could, we could make some cuts that wouldn't necessarily impact our clients or our workers. So, those were the areas of focus Henry, in terms of areas that we cut.

In terms of investments, one of the challenges that we've had over the last couple of years has been around our client count. We've done a pretty good job from a pricing perspective of keeping up with wage increases and pricing that in. We've done a pretty good job of retaining our clients but one of the things we haven't done as good a job in is going out and acquiring new clients and then hanging onto them in the early days.

Those that have been with us for a long time we've done a good job with but the early days is where we've had some challenges. And so, what we've done is we've made a multimillion-dollar investment in a team that's focused on onboarding our clients and making sure that they get off to a really good start. And then once they're on-boarded, we've also made some pretty significant investments in the area of expanding wallet share within those clients and making sure that they get signed up on job stack and are using it in a heavy way.

And so, we rolled that team out in the third quarter and early days, it's been really successful. In fact, we're probably going to be expanding the size of that team based on the early results that we've had. And so, we've carved out about $3 million of the cost savings that we had and we're looking to reinvest in our sales and marketing capabilities in both at new clients, as well as within our existing installed base. And so, those are the areas of focus.

Henry Sou Chien
Analyst, BMO Capital Markets (United States)

Q

Got it. Okay. Great. That's helpful. And just on PeopleManagement, just looking at the business, I mean it appears to be facing some pretty significant headwinds both on pricing and volume. Just kind of curious like what – where are you seeing the new business and why is it, I guess, sort of worth continuing to sort of expand that business unit?

A. Patrick Beharelle
Director & Chief Executive Officer, TrueBlue, Inc.

A

Well, we're actually – we're pretty bullish on PeopleManagement right now. We've had a number of wins in that business. In fact, our wins are up more than 20% on a year-over-year basis. And it's – these are multi-year contracts with very large companies. And so, we're feeling pretty bullish on that business after you rightly point out a couple of years of pretty unimpressive revenue growth and margin profile. So, we feel like the pricing we put in place is solid on these new deals. And these are large companies that are signing up the multiyear engagements. And so, as we look into 2020 and beyond, we see that business returning to growth.

Henry Sou Chien
Analyst, BMO Capital Markets (United States)

Q

Got it. Okay. Makes sense. Thank you.

Operator: And our final question comes from the line of Mark Marcon with Baird. Please go ahead.

Mark S. Marcon
Analyst, Robert W. Baird & Co., Inc.

Q

Hey, Patrick. Hey, Derrek. I'm just wondering with regards to the workers' comp, what's the underlying reason why the workers' comp went up?

Derrek L. Gafford
Executive Vice President & Chief Financial Officer, TrueBlue, Inc.

A

Hi, Mark, it's Derrek here. The – our run rate this year has been quite consistent. Matter of fact, workers' compensation as a percentage of revenue here in the third quarter was the same as it was in the second quarter. [ph] This just sat (00:39:26) in the third quarter of last year, we have the benefit from reductions to prior period reserves was larger than normal and took that down to its – our lowest point that we've, I believe we've ever had [ph] unless we've (00:39:40) done an EBITDA exclusion. Certainly, the lowest point during the 2018 fiscal year.

Mark S. Marcon
Analyst, Robert W. Baird & Co., Inc.

Q

Got it. Okay, great. And then with regards to PeopleReady just in terms of the trends that you're seeing in the business, could you describe outside of the construction areas what you're seeing, is there any light at the end of the tunnel? And also, could you talk a little bit about what you're seeing in terms of with minimum wage increases having gone through, how is that impacting demand and just how hard is it to fill some of the positions?

Derrek L. Gafford
Executive Vice President & Chief Financial Officer, TrueBlue, Inc.

A

Sure. So, if we're talking about PeopleReady from a trend perspective, certainly, manufacturing has been very heady headwind. So, put into perspective in Q1 of 2019, we were down about 2% in manufacturing. During the third quarter, we were down about 15%. In my earlier comments, there's a little bit of additional pressure coming from construction in the early parts of the fourth quarter but overall, construction, for the most part, held up pretty well in the first two quarters. We're also seeing pressure in the transportation industry. That business is down low-double-digits, call it minus 12%, minus 13%.

And then, we've got some other businesses. If you take out some of the retail noise that we've had in the business particularly this last project that we just did in Q3. Retail in the PeopleReady business is actually been holding up quite well. I mean we were mid-single-digit as far as growth there. So, there's some resiliency for us in that business.

When it comes to minimum wage increases, the last set of minimum increase, wage increases this year was in California. Those have been the toughest because those have been sizable increases that have been happening year-after-year. So, those are tough costs for businesses to take on year-after-year. We typically see a little bit of pressure on that in their early parts when it first comes through and then that moderates three to four months afterwards and we recover on the volume. And I would say that that's the way this has been running its course.

As far as minimum wages for increases for next year, we're still in the process of assessing that. But I wouldn't be surprised if it was relatively close to the minimum wage increases that we had this year, which was roughly $10 million with minimum wage increase that we pushed through.

Filling open requisitions with people, it's still quite tough. We'll – we're in an environment here where businesses are really looking at the workforces and where they oftentimes go first as the [ph] contingent space (00:42:41). That's only 2% of total unemployment and that's why you're seeing, of course, more about headwind in the staffing businesses than you are at the overall employment numbers. So, if you take that with still an economic workforce that's pretty much fully put to work, it is a challenging environment to fill those positions given what's going on.

Mark S. Marcon
Analyst, Robert W. Baird & Co., Inc.

Q

I mean when you think about kind of the overall macro environment, it has been soft and softening throughout the year. Obviously, as you start looking towards next year, what are the factors that you would say would make you feel more optimistic or less optimistic about the trajectory and potentially hitting an inflection? Because it sounds like you're doing well in JobStack. It sounds like you've got some contracts lined up on the PeopleReady side. So how are you thinking about that and also just deploying the capital on the buyback?

Derrek L. Gafford
Executive Vice President & Chief Financial Officer, TrueBlue, Inc.

A

Well, we're focused on is that how can we best operate under these conditions and one place where we've got an opportunity is to increase the percentage of candidates that make it through our hiring process. So a big focus of ours in 2020, while we have JobStack in place, it's the matching engine for that brings people who are not candidates but actual employees and matches them with jobs so that's really about utilizing the workforce.

We're investing a lot of time and resources in changing the experience that our candidates have and how they comes through the system to become an employee and become unboarded, and we think we've got some opportunities to make that much more seamless and then make a sizable improvement in the conversion ratio of those candidates. So in 2020, we'll also be expanding our JobStack application for that to also be the process in which employees come to work for us, which we think was it will cut down the time significantly that it takes and make it much it more seamless for the candidate and improve our conversion ratios of applicants.

Mark S. Marcon
Analyst, Robert W. Baird & Co., Inc.

Q

How will you expand that Derrek?

Derrek L. Gafford
Executive Vice President & Chief Financial Officer, TrueBlue, Inc.

A

And your question. Pardon.

Mark S. Marcon
Analyst, Robert W. Baird & Co., Inc.

Q

How will you expand that Derrek?

Derrek L. Gafford
Executive Vice President & Chief Financial Officer, TrueBlue, Inc.

A

Well...

Mark S. Marcon
Analyst, Robert W. Baird & Co., Inc.

Q

You said you're going to expand JobStack next year and...

Derrek L. Gafford
Executive Vice President & Chief Financial Officer, TrueBlue, Inc.

A

Yeah. And so instead of going through our legacy applicant tracking system, now candidates will be applying really through the JobStack application. So it will become a more candidate-facing application, and they will move through the process with some of the things that we've learned about a digital business model to make that a much more easy and seamless experience. And then they'll also, once they come to work for us, of course, get dispatched that way. So that's the – those are plans that we have for 2020.

Mark S. Marcon
Analyst, Robert W. Baird & Co., Inc.

Q

Great.

Derrek L. Gafford
Executive Vice President & Chief Financial Officer, TrueBlue, Inc.

When it comes to capital allocation, we don't think it's the right time to be seriously looking at acquisitions given the uncertainty that exists out there. If the horizon were to clear and there's be less uncertainty, we'll change our minds on that a bit.

On the other side of the coin, hopefully, it doesn't go this way, but if we were to get into more of a traditional recession and feel like we're more at the bottom and there were some deals that came along with some very opportunistic prices. We would consider that if we could see that some uncertainty would be clearing in the near future.

But outside of that, we're going to – our number one place of putting our time and resources is in this digital business model. I think really true to that, we're going to continue investing in that whether times are good or whether times are bad. And then with excess capital that we have, we plan to put that into share repurchase.

We want – we think doing some consistently makes sense but also repurchasing opportunistically makes sense. So with less acquisitions, as part of the strategy, there's more capital to put back to stock repurchased and we authorized – or announced today that the board authorized an additional $100 million.

So I think that speaks somewhat to our intentions.

Mark S. Marcon
Analyst, Robert W. Baird & Co., Inc.

Q

It does. I was thinking more about the timing of that being deployed particularly in light of the strong balance sheet. So...

Derrek L. Gafford
Executive Vice President & Chief Financial Officer, TrueBlue, Inc.

A

Well, you're right. The balance sheet's in really good shape. And so, we could – we probably wouldn't want to get over a turn of debt to EBITDA in this type of environment. But given the right circumstances, you could see us flex up on that some to be opportunistic.

Mark S. Marcon
Analyst, Robert W. Baird & Co., Inc.

Q

Great. And then with regards to PeopleReady, can you just talk about the pacing of when you would expect the inflection to occur given the contract signings? And then one other question would be like how should we think about the margin profile that occurred this past quarter on a sequential basis relative to the sequential increase in revenue? Was there any more repricing or is there anything else to talk about there?

A. Patrick Beharelle
Director & Chief Executive Officer, TrueBlue, Inc.

A

Yeah. Mark, this is Patrick. In terms of the contract signed, I was referring to PeopleManagement and those earlier was...

Mark S. Marcon
Analyst, Robert W. Baird & Co., Inc.

Q

I meant PeopleManagement.

A. Patrick Beharelle
Director & Chief Executive Officer, TrueBlue, Inc.
A

Okay. Great. Well, we're not necessarily giving guidance by quarter for 2020 right now, but when you look at the size and magnitude of the signings, I think there's a pretty good chance that that in Q1 we'll see a significant step-up from where – what we've guided to in Q4. So, I think it will be fairly early in the year that we'll see a pretty significant step-up from where we've been, again assuming kind of current business conditions. [ph] I'd have (00:48:57) been asked I think on an earlier call about when we thought the inflection point would happen. And I'd said a couple of quarters ago, I thought Q4. And we did see some improvement in Q – we've guided to improvement in Q4 versus Q3, but the deal has taken a little longer to ramp-up and implement than what we had originally thought. So I think we'll really see that inflection in Q1 versus what we originally thought in Q4 of this year.

Mark S. Marcon
Analyst, Robert W. Baird & Co., Inc.
Q

Great. And just because as it relates to the PeopleManagement margin this past quarter, was part of that due to the efforts to sign some of these larger deals or any sort of setup fees or anything along those lines or what led to the sequential decline in the EBITDA margin, in PeopleManagement?

Derrek L. Gafford
Executive Vice President & Chief Financial Officer, TrueBlue, Inc.
A

Yeah, it was mostly timing involved with less than a handful of customer accounts, some which were positive, some which were negative. But it's really just a one quarter impact so, I think what you'll see, while we don't – we've given guidance for the fourth quarter already, you'll see when the results come out assuming we're within our guidance overall and with PeopleManagement. You'll see a more normal year-over-year margin profile for PeopleManagement. And consider the third quarter just a few timing issues, but nothing that's sustainable as far as we can see.

Mark S. Marcon
Analyst, Robert W. Baird & Co., Inc.
Q

And just on the guidance, two things. One would be that the project work which is continuing into Q4, would you expect that to continue into next year as well?

A. Patrick Beharelle
Director & Chief Executive Officer, TrueBlue, Inc.
A

Yeah, Mark. This is Patrick. With that particular client, we're in conversations now as we speak about doing additional project work next year as well. This is a client that's been with us for multiple years now and so, the nature of the projects is lumpy but it's a very strong relationship. It's one of our top 10 clients in terms of size right now. So, I would expect that we'll continue to see some lumpiness in terms of new projects in 2020.

Mark S. Marcon
Analyst, Robert W. Baird & Co., Inc.
Q

Okay. So, people shouldn't necessarily assume that that $5 million to $6 million that you're expecting to experience in Q4 should go away in Q1?

A. Patrick Beharelle
Director & Chief Executive Officer, TrueBlue, Inc.
A

No, I wouldn't – I would not just draw that conclusion, this is a very large client that has a lot of projects.

Mark S. Marcon
Analyst, Robert W. Baird & Co., Inc.
Q

Great. And then the second question would be with regards to guidance, you are excluding the cost for the restructuring, correct?

Derrek L. Gafford
Executive Vice President & Chief Financial Officer, TrueBlue, Inc.
A

Yeah, that's right, Mark. We've – the actions that we've taken provide $2 million of savings in the fourth quarter but it also – we've got $2 million of costs of reserve related to some of the workforce reductions that take that part away. So, that $2 million charge that I just mentioned that will be excluded from adjusted EBITDA and adjusted net income.

Mark S. Marcon
Analyst, Robert W. Baird & Co., Inc.
Q

Okay. And then, how should we think about the tax rate for next year just broadly speaking? Assuming that WOTC goes through?

Derrek L. Gafford
Executive Vice President & Chief Financial Officer, TrueBlue, Inc.
A

Yeah, the 14% that we've been talking about this year should be about the right amount, the right rate for next year. I mean, we're still putting together our estimates for that but we've stayed within a 14% expected rate throughout this year and stuck with that for the fourth quarter. I don't see any reason to change that at this point in time but will – sometimes there's some new tax things that come up and we do wrap that into that but it looks pretty good for now.

Mark S. Marcon
Analyst, Robert W. Baird & Co., Inc.
Q

Great. Thank you.

Operator: Thank you. And I will now turn the call to Patrick Beharelle for closing remarks.

A. Patrick Beharelle
Director & Chief Executive Officer, TrueBlue, Inc.

Thank you and I appreciate, everyone, listening to our third quarter earnings call. We look forward to talking to you again in 2020. Have a great week everyone.

Operator: Ladies and gentlemen, this concludes today's conference. Thank you for participating. You may now disconnect.