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ADP - Q2 2018 Automatic Data Processing Inc Earnings Call

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OVERVIEW:

Co. reported 2Q18 revenue of $3.2b and adjusted diluted EPS of $0.99. Expects FY18 revenue growth to be 7-8% and adjusted diluted EPS growth to be 12-13%.

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PRESENTATION

Operator

Good morning. My name is Christine, and I will be your conference operator. At this time, I would like to welcome everyone to ADP's Second Quarter Fiscal 2018 Earnings Call. I would like to inform you that this conference is being recorded. (Operator Instructions) Thank you. I would now like to turn the conference over to Mr. Christian Greyenbuhl, Vice President, Investor Relations. Please go ahead.

Christian Greyenbuhl - *Automatic Data Processing, Inc. - VP of IR*

Thank you, Christy, and good morning, everyone. This is Christian Greyenbuhl, ADP's Vice President, Investor Relations, and I'm here today with Carlos Rodriguez, ADP's President and Chief Executive Officer; and Jan Siegmund, ADP's Chief Financial Officer. Thank you for joining us for our second quarter fiscal 2018 earnings call and webcast. During our call today, we will reference certain non-GAAP financial measures, which we believe to be useful to investors. A reconciliation of these non-GAAP financial measures to their comparable GAAP measures is included in our earnings release and in the supplemental slides on our Investor Relations website. Before Carlos begins, I'd like to remind everyone that today's call will contain forward-looking statements that refer to future events, and as such, involve some risks. We encourage you to review our findings with the SEC for additional information on risk factors that could cause actual results to differ materially from our current expectations. Now let me turn the call over to Carlos.

Carlos A. Rodriguez - *Automatic Data Processing, Inc. - CEO, President & Director*

Thank you, Christian, and thank you all for joining our call this morning. We appreciate your interest in ADP. This morning, we reported our second quarter fiscal 2018 results with reported revenue up 8% to $3.2 billion, 7% organic. This revenue growth was slightly above our expectations, and we are pleased with the progress that we've made so far in the first half of fiscal 2018. Our adjusted diluted earnings per share grew 14% to $0.99 per share and benefited from a lower effective tax rate and fewer shares outstanding. We continue to work diligently this quarter to overcome the difficult grow-over from our strong fiscal 2017 second quarter performance. And we are pleased with our overall results, which Jan will take you through in more detail shortly, including some additional information on the recently enacted Tax Cuts and Jobs Act. Before I continue further with our operational highlights, I'd like to focus on the execution of our strategy and our innovation efforts. Innovating to help our clients meet the dynamic needs of a rapidly evolving workforce has always been in our DNA and continues to be at the very core of our strategy. More and more, we see workers demanding a greater, ease of access to and functionality of the digital world. Whether it is the convenience offered by our ADP mobile solutions app, the insights delivered by our data cloud offerings or, increasingly, the optionality of flexible payment solutions, it is clear that the worker is at the center of the HCM strategy of tomorrow. While we continue to innovate around our core strengths, such as with our recently announced next-gen payroll and tax platforms, you will also recall that in October, we announced our acquisition of Global Cash Card, which further strengthened our payroll offering with the expansion of digital accounts and flexible payment offerings. This was an exciting acquisition that allows us to further support the evolving needs of our clients, and we are very pleased with the level of client interest in their digital payment services. With this acquisition, ADP became the only HCM provider with a proprietary digital payments processing platform, thus, enabling the opportunity for greater operational efficiency and a seamless client experience. Furthermore, we expect Global Cash Card will allow us to broaden our engagement with our clients' workforce through compelling options to service their flexible pay needs and improve their financial lives, be they traditional or freelance. With the world of work changing, so are our clients' needs. We are proud to be the leading global provider of innovative technology-based HCM solutions across the entire workforce. And with the composition of work increasingly moving toward the freelance worker or gig worker, we have actively pursued going beyond the status quo in order to maintain and expand our industry-leading position. The gig economy is large and continues to grow, with some third-party studies suggesting that between 20% and 30% of today's labor force is on demand.

With over 90% of our mid and upmarket clients already using gig workers and the majority expected to increase their use for the next 2 years, we believe we are uniquely positioned to service this growing market, and it is specifically with this evolution in mind that we believe in having the worker at the center of our strategy and our next-gen solutions. Along these lines, we have continued to differentiate our offerings with the recently announced acquisition of WorkMarket, a leading cloud-based freelance management solution serving both multinationals and small- to medium-sized businesses, allowing them to build and manage their integrative workforce, while aiding them with their important compliance obligations.

WorkMarket solutions include comprehensive talent management and compliance solutions to help source and vet freelance workers, manage their engagements and evaluate their performance. In addition, WorkMarket solutions already permit freelance workers on the platform to receive their payments using a Global Cash Card pay card. Our acquisition of WorkMarket establishes ADP as the first HCM provider with robust freelance worker management and payment functionality, with reporting insight and compliance monitoring across the entire labor pool. Acquisitions with strategic fit like Global Cash Card, WorkMarket and last year's acquisition of TMBC in the talent management space are just one way ADP is helping clients keep pace with change and manage the increasing demand for flexibility in the way people work and how organizations manage their talent.

I am proud of our progress to date in our innovation-focused investment strategy to develop open and flexible solutions that can be adopted to meet the needs of any client. We believe that pursuing a healthy mix of acquisitions that align with our strategic priorities, in combination with investments and organically-driven innovation, is the right approach for us to deliver market-leading capabilities to clients that will foster sustainable growth.

Now I'd like to cover some operational highlights, starting with new business bookings and retention, both of which continue to show progress and stability against our expectations. As a reminder, we view new business bookings as a metric that demonstrates our ability to drive organic growth, and which represents annualized recurring revenues anticipated from sales to new and existing clients. New business bookings grew 6% for the quarter. We are pleased with the progress from our investments in headcount and product, which are helping reaccelerate our growth, in line with our expectations. And as a consequence, we are maintaining our new business bookings forecast of 5% to 7% growth for fiscal 2018. We are pleased with the progress we are making on our service investments and with the continued improvements in our net promoter scores. We are now substantially complete with our mid-market upgrades and have less than 1% of our mid-market clients left to migrate. We continue to see an improving trend in our Employer Services client loss metrics. And while this quarter's retention declined slightly by 20 basis points, given the quarterly volatility in this metric, we remain pleased with our year-to-date retention improvement of 70 basis points.

We remain on course with our plans to consolidate our real estate footprint and with our associate onboarding across our new strategic locations. As we streamline our service infrastructure and scale our new service centers, we are continuing to see the benefits to both our clients and our associates. Cross-functional teams we have formed in these new sites are leveraging best-in-class service tools and processes to deliver exceptional service to clients across the HCM spectrum in a cost-efficient manner. At the same time, this allows us to better transfer knowledge among these service teams and offer robust career opportunities within the service organization. I'm proud of these efforts and of the speed of execution despite the pressure that comes from our client calendar year-end service deliverables.

Now I'd like to take a moment to recognize the PEO business, which as of December 31 surpassed the 500,000 worksite employee mark. In fact, if ADP TotalSource were an independent employer, it would currently rank second among private sector employers in the United States. We are pleased with this business' continued success and with its healthy pace of growth, which demonstrates the value in the market of our broad-based, compliance-oriented HR outsourcing solutions.

We have made a lot of progress in executing against our strategy in the first half of 2018, and we remain focused on continuing to accelerate our pace of change through the remainder of the year and beyond. Before I turn the call over to Jan for a detailed financial review, I want to note how proud I am of the unwavering commitment of our associates, and how especially proud I was to see Fortune magazine name us to their Most Admired Companies list for the 12th time. I am particularly proud of this because it is a testament to the confidence our stakeholders place in us and to the continued dedication of our associates who work tirelessly to provide our clients the best solutions for today and tomorrow. And with that, I'll now turn the call over to Jan for further review of our second quarter results.

Jan Siegmund - *Automatic Data Processing, Inc. - Corporate VP & CFO*

Thank you very much, Carlos, and good morning, everyone. In my commentary to follow, I will be referencing non-GAAP measures that excludes the impact of certain items in the second quarter of fiscal year 2018 as well as the second quarter of fiscal year 2017. A description of these items and the reconciliation of these non-GAAP measures can be found in this morning's press release and in the supplemental slides on our Investor Relations website.

As Carlos mentioned, ADP revenues grew 8% in the quarter to $3.2 billion, and includes approximately 1 percentage points of benefit from foreign currency. On a reported basis, net earnings declined 8% or 9% on a constant-dollar basis, largely due to the prior year second quarter pretax gain of $205 million related to the sale of our CHSA and COBRA businesses, offset by a onetime fiscal year 2018 second quarter net tax benefit related to the U.S. corporate tax reform of approximately $46 million.

Adjusted earnings before interest and taxes, or adjusted EBIT, increased 2% on a reported basis. And it included approximately 1 point of pressure from the impact of acquisitions, the second quarter fiscal year 2017 disposition of our CHSA and COBRA businesses as well as FX.

Adjusted EBIT margin decreased about 120 basis points compared to 19.8% in last year's second quarter. This decrease was slightly better than our expectations, though we continue to see increased pressure from stronger-than-anticipated growth in pass-throughs and from acquisitions.

During the quarter, we have maintained our investments into innovation, service and distribution, and we continue to believe in the benefits of these investments helping us deliver against our long-term financial -- long-term strategic financial objective. Adjusted diluted earnings per share grew 14% to $0.99. 13% on a constant-dollar basis, and benefited from a lower effective tax rate and fewer shares outstanding compared with a year ago. The enactment in December 2017 of the Tax Cuts and Jobs Act includes significant changes to the U.S. corporate tax system, including a federal corporate tax rate reduction from 35% to 21% and, among other provisions, a repeal of the Section 199 domestic production activities deduction as well as new limitations on the deductibility of executive compensation. Our adjusted effective tax rate for the quarter of 25.6% was positively impacted by a lower blended statutory rate of 28.1%, which became effective at the beginning of our fiscal year. This benefit was partially offset by adjustments to access tax benefits on stock-based compensation and foreign tax credits. As a reminder, our adjusted results exclude a net tax benefit of approximately $46 million for onetime items, which encompass the benefit of the reevaluation of deferred tax assets and liabilities and transition tax on accumulated overseas earnings and a valuation allowance on foreign tax credits.

Overall, we have continued to make good progress this quarter. Let me now take you through our segment results before moving on to our updated fiscal year 2018 outlook.

In our Employer Services segment, revenues grew 6% for the quarter, 4% organic. Our same-store pays per control metric in the U.S. grew 2.6% in the second quarter. Average client fund balances grew 7% compared to a year ago. This growth was driven by higher payroll volumes in December, resulting from higher bonus activity. Outside the U.S., we continue to see solid performance from our international operations with double-digit revenue growth in our multinational businesses. Employer Services margin decreased about 50 basis points in the quarter and included approximately 70 basis points of pressure from the impact of acquisitions and FX. PEO revenues grew 15% in the quarter, with average worksite employees growing 10% to 498,000. This revenue growth was driven by growth in worksite average -- growth in average worksite employees and from a continued acceleration in the growth of pass-through revenues from the higher health care premiums and higher-than-expected payrolls in the second quarter. This acceleration in pass-throughs was the primary driver for the 30 basis points of decline in the PEO's reported margins this quarter. I'm pleased with the performance of both of our segments this quarter, while, as Carlos mentioned, we continued to work to accelerate our pace of change for the remainder of the year.

Before I disclose our -- discuss our fiscal year 2018 outlook, I wanted to highlight some additional detail regarding the acquisition of WorkMarket. The results of operations of this business will be included in the Employer Services segment and are not expected to materially impact our updated revenue guidance. While we anticipate future synergies from this acquisition and our second quarter acquisition of Global Cash Card, we also anticipate some slight pressure to margins this year, largely driven by acquisition-related costs. Accordingly, we have factored these operational impacts into our updated fiscal year 2018 outlook. With these items in mind, I will now take a moment to walk through our revised outlook with you. First, as Carlos mentioned earlier, we are reaffirming our full year new business bookings guidance of 5% to 7% growth on the $1.65 billion sold in fiscal year 2017. With the higher-than-anticipated growth in our pass-through revenues during the first half of fiscal year '18, we have updated both our consolidated revenue forecast growth to 7% to 8% compared to our prior forecast of 6% to 8%, and our PEO revenue forecast to 12% to 13% from 11% to 13%. Our Employer Services revenue guidance of 4% to 5% remains unchanged. We are also now expecting growth in client fund interest revenues to increase $55 million to $65 million compared with our prior forecasted increase of $45 million to $55 million. The total impact from the client fund extended investment strategy is now expected to be up $45 million to $55 million compared to the prior forecast increase of $35 million to $45 million. The details of this forecast can be found in the supplemental slides on our Investor Relations website.

As a result of the growth in pass-through revenues, we have also updated our margin forecast, and now anticipate our consolidated adjusted EBIT margin to contract approximately 50 basis points compared to our previously forecasted contraction of 25 to 50 basis points from 19.8% in fiscal year 2017.

Overall, as our investments begin to make an impact, and we lap the easier compares from fiscal year 2017, we continue to anticipate a stronger finish as the year progresses. At a segment level, due to the pass-through pressure, we now anticipate PEO margins to be flat to down 25 basis points compared to our previous forecast of up 25 to 50 basis points. And we continue to anticipate margin contraction in Employer Services of 50 to 75 basis points, which includes approximately 60 basis points of pressure from acquisitions, costs and FX.

Adjusting to the anticipated benefits of U.S. corporate tax reform, we now expect our forecasted adjusted effective tax rate of fiscal year 2018 to be 26.9% compared to the 31.7%. This benefit is primarily attributable to the lower blended federal corporate statutory rate of 28.1% for fiscal year 2018.

Accordingly, we now expect growth in adjusted diluted earnings per share of 12% to 13% compared to our prior forecast of 5% to 7%. This forecast does not contemplate any further share buybacks beyond anticipated dilution related to equity compensation plans. However, it remains our intent to continue to return excess cash to shareholders, subject to market conditions.

Before moving to Q&A, I would like to touch briefly on our long-standing cash allocation strategy, which involves reinvesting in the business, pursuing acquisitions and returning capital to shareholders through dividends and share buybacks in that order. As I said earlier, we currently participate -- anticipate an adjusted effective tax rate of 26.9% for fiscal year 2018. And while new IRS guidance or interpretations may change things, we currently anticipate a future effective tax rate excluding any possible onetime items of 25% to 26% beyond fiscal year '18. Clearly, we are one of the beneficiaries of U.S. corporate tax reform. And while this offers us additional financial flexibility going forward, our priorities, which have delivered total strong shareholder return performance to our shareholders, remain unchanged. So with that, I will turn it over to the operator to take your questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) We will take our first question from the line of Jason Kupferberg of Bank of America Merrill Lynch.

Jason Alan Kupferberg - *BofA Merrill Lynch, Research Division - MD in US Equity Research & Senior Analyst*

I just wanted to start with a question on the margin outlook, obviously, understandable with the pass-throughs on the PEO side growing faster than expected. But you are still -- it looks like you're going to move from year-over-year declines in the first half of '18 to some modest year-over-year increases in margins in the second half. I wanted to see if you can also comment on the trend in underlying margins. I mean, if we exclude the PEO pass-throughs and the floating comment, you've talked a little bit about this in the past as far as this being perhaps a more accurate measure of underlying profitability, what are the trends you're seeing there?

Carlos A. Rodriguez - *Automatic Data Processing, Inc. - CEO, President & Director*

I'll make a couple of comments, then maybe Jan can add some -- maybe more specifics. But I think in general, I think the answer is positive trends. Because the other factor that I think you didn't mention, which you do have to kind of factor in to understand what's really happening underneath the covers. So besides the PEO pass-throughs, we do have a couple of acquisitions now that are putting a little bit of pressure. And as you can see, the underlying trend must be pretty positive if we are holding to our full-year forecast for EPS and margins and so forth. So I think the fact that we're able to absorb the pressure, and I think it was mentioned previously that I think it was somewhere along the order of 70 basis points between acquisitions and FX, most of which was acquisitions in the Employer Services segment, I think gives you some sense that I think the underlying trends are positive. And I think it is important to note that as we've said before that some of this is related to comparisons and grow-overs. Just as a reminder, last year's second quarter, we had, I believe, it was somewhere around 20% growth in EBIT and EPS. And I think that gives you some sense of a company our size, and because of the recurring revenue nature of our business that those results last year were the result of the issues around ACA, which gave us tailwind on the revenues before we have lapped the expenses. So we've been talking about this now for 8 quarters. And I think the -- it starts to get a little bit easier going forward for it to be a little bit more clear what is happening. So maybe I'll let Jan add a couple of comments.

Jan Siegmund - *Automatic Data Processing, Inc. - Corporate VP & CFO*

Yes. So if you -- Jason, if you think about our full-year guidance of 50% pressure, ADP-wide, like 30 to 40 bps comes from pressure from acquisitions that we haven't anticipated, were clearly at the beginning of the year. And the pass-through pressure, if you calculate it out like we did historically, amounts to kind of a very strong 100, 130 bps pressure. So the rest is operational scale. And some of our initiatives that we launched in a year-plus ago are now leaped. And we're going to see the benefit, increased benefit of that result. So there's operational scale that we anticipate last year. And that goes really across the entire business system. There's really not a specific function I can point out because I think the trend is, across the operations, fairly consistent.

Carlos A. Rodriguez - *Automatic Data Processing, Inc. - CEO, President & Director*

And I think one last thing that I would add is I think what's easier probably for, which we all should do going forward, is to really focus on ES and focus on PEO separately. There's really -- there's only 2. It's fairly straightforward to understand. So if you take the information we're giving about ES, which we are very transparent about, and we're also giving you additional color here around the pressure from acquisitions and FX and so forth, you can really figure out that ES is performing well and ahead of our expectations and probably ahead of your expectations. And if you look at the PEO separately, the only issue in the PEO, which is not a negative issue, is that the pass-throughs grew faster than everyone anticipated. And that creates a margin issue. But to be clear, excluding pass-throughs, the PEO, what we call processing revenues, grew at a very healthy pace. And the profitability grew faster than the revenues of the PEO, excluding pass-throughs. And so both segments, I think, are performing well. And the mix that you get is mathematical and shouldn't necessarily get in the way of us understanding the underlying strength of the business.

Jason Alan Kupferberg - *BofA Merrill Lynch, Research Division - MD in US Equity Research & Senior Analyst*

Okay, that's all helpful. Just a quick follow-up on bookings. Obviously, good to see some recovery there in the fiscal second quarter. So you need to deliver, I guess, somewhere in the high single-digit range in the second half to achieve the full-year forecast. Obviously, the comps get easier. We're now more or less past the key selling season. So I wanted to see if you can just characterize the visibility on the affirmed 5% to 7% target compared to what that visibility looked like a quarter ago, including any sense that you might be able to provide on how January bookings might have trended at least directionally?

Carlos A. Rodriguez - *Automatic Data Processing, Inc. - CEO, President & Director*

As you know, we wouldn't really comment on our bookings going forward, where -- the call is really to talk about what happened last quarter. And you have our, I guess, maintaining of our 5% to 7%. So I think that would give you some sense that we have confidence that we'll be able to deliver. But obviously, there's a lot of -- as always, there's an unknown. And bookings numbers are always the most unknown number, and this -- and the rest of the business is recurring revenue. Bookings are 1 week at a time, 1 day at a time, 1 month at a time. So you just have to wait and see for the results. But we're -- as we mentioned in our comments, the headcount growth that we've had, the additions to product, like those things will give us some confidence. And I think 6% growth was ahead of our expectations. It was strong. So it feels -- that feels good. And I'll also just point out that it just so happens that the second quarter new business bookings number is the highest we've ever had. So it's -- I think that's, I think, a testament to our ability of our sales force to really turn things around. But there's still a lot of work to do. It's still a very competitive market. So I think we have a lot of sales still in front of us. We had really good results in our downmarket, as we've had for the last several quarters. We had really good results also in our multinational business. And our PEO, I think, also did quite well, just to give you a little bit of additional color. But there's still a lot of wood to chop, for sure.

Operator

And our next question is from Tien-tsin Huang of JPMorgan.

Tien-tsin Huang - *JP Morgan Chase & Co, Research Division - Senior Analyst*

Just, I guess, you guys mentioned pace of change a couple of times. I'm curious if you can maybe elaborate on what you mean there and what you might do differently in terms of like giving your strategy, et cetera.

Carlos A. Rodriguez - *Automatic Data Processing, Inc. - CEO, President & Director*

Yes. Well, it's a good question. It's, unfortunately, probably beyond the scope of a brief answer because we have a lot of things going on. But we've always had a lot of things going on. So we have quite a number of initiatives that I think some have been -- we've been discussing with all of you, some of which we're not probably ready to start talking about yet. You heard in our comments about our strategic alignment initiatives. You've heard about our next-gen platforms, which we hadn't really discussed up until the fall of last year. So I think that gives you some sense of how much we had going on. And we have other things going as well, including a couple of acquisitions that we've mentioned, I think, on the call are pretty significant in the sense that they, despite slight pressure on our margins in the short-term, we're very, very excited about in terms of what they do, in terms of opening up our -- the possibility of a wider market for us to go after with our existing distribution and sales force. And so we just have a number of initiatives. I wish I could kind of go down the list, but I think it might take longer than we have for the call. But we're trying to move and to complete our upgrades, which we're almost done with in the mid-market. We are accelerating -- trying to accelerate the pace of our go-to-market of our next-gen platforms. We want to do that at the right pace, but we're also trying to do it as quickly as possible because we recognize and we anticipate that it's going to create a competitive advantage for us. And this is our next-gen payroll platform as well as some of the back-office stuff, tax, including also our local platform, which we discussed as we went on the road to talk to investors back in the fall. So just a lot of great things happening, and we're excited about trying to accelerate on a number of fronts.

Tien-tsin Huang - *JP Morgan Chase & Co, Research Division - Senior Analyst*

All right. Great. Just maybe just my quick follow-up for Jan, just the impact on the -- on sort of balance growth from the tax reform. I was a little surprised to see plus 7% for the year if you have 3% prior. Can you -- just a big picture question on that.

Jan Siegmund - *Automatic Data Processing, Inc. - Corporate VP & CFO*

Yes. We haven't gotten a balance question for a long time, Tien-tsin, so I appreciate that. The balance growth accelerated for the quarter to about a little bit more than 7%, and there was a percent of FX in it. So excluding FX, the balance growth was 6.6% actually. And the guidance that we give is 4% to 5%. So you see, for the remainder of the year, we anticipate a little bit slower balance growth. And you point out that taxes, which represent about 3/4 of our total client fund balances, are impacted by a lower effective tax rate. And so the estimates -- before I talk about the outlook, in December, we did see higher bonus payment activity, which we attribute maybe to corporate behavior that is related to the corporate tax reform. So was also the growth maybe slightly inflated for the quarter relative to the run rate, but we also had good payroll performance basically in the balances. So for the year, we anticipate 2 to -- 1% to 2% kind of potential impact on growth that the corporate tax -- that tax reform in general and the retail rates could have. There's a little bit of uncertainty. I don't think nobody really knows exactly how big the impact is going to be on the personal rates, but that's anticipated. So hence, the 4% to 5% is still better than we had, but it is -- includes this 1% to 2% rough estimate on the lower tax balances basically.

Operator

And our next question is from Jim Schneider of Goldman Sachs.

James Edward Schneider - *Goldman Sachs Group Inc., Research Division - VP*

I was wondering if you could maybe comment on the broader business environment in the different segments and what you're seeing in terms of client feedback, either on the overall economy, generally speaking, and/or in terms of the impact of tax reform on their business. How does that translate into bookings, if at all? And generally speaking, is the client tone kind of optimistic? And is it different across the different sizes of the clients?

Carlos A. Rodriguez - *Automatic Data Processing, Inc. - CEO, President & Director*

So again, we have -- I guess, we can give you some anecdotal information. But I think we like -- because of the size of our company and also the size of our sales force and the geographic disbursement of our folks and our clients, I think it's best to focus kind of on macro trends. And so we do look at a lot of the macro trends. And we have a lot of information, obviously, around our national employment report and wage inflation. And so far, that gives us some insight. But rather than getting into kind of anecdotal stories, because the anecdotal stories are pretty very positive. Everyone seems to be very positive and very happy. But the -- I think all the numbers that we're looking at that everyone else looks at, which are important for us to understand in terms of the potential drivers to our business, when you look at Small Business optimism, consumer confidence, like all of these indicators, I think, are all very -- pointing in very positive directions. We look at things also, particularly in our downmarket, around bankruptcies and new business formations. So just a number of economic indicators that are pointing to strong underlying growth. One of the things that's been a positive surprise to us, I think we had our National Employment Report issued today. And I think this is the second quarter where I think Jan and I would both say that we are pleased, but slightly surprised, by the strength, the underlying strength of growth in employment still. So we're still kind of bullish and positive that our sales force will be able to take advantage of what's a very, very strong underlying economy. Our downmarket business and our PEO should hopefully especially be beneficiaries -- other things notwithstanding, should be beneficiaries of this kind of strong ongoing tailwind around Small Business optimism and new business formation. So I think it's all positive. I think the other factor that obviously will help us as well, and to the extent that it doesn't then turn into a negative down the road, is to the extent that wage inflation picks up and maybe interest rates begin to tick up, which they are, that obviously helps us in our fluid income business, which we happen to believe is part of our core business. The SEC also agrees with us. As you know, it's just part of our operating results. And we spent many years having to fight the headwinds. And again -- and if you looked at our margins over the last 6 or 7 years, we absorbed several hundred million dollars in headwind and still managed to either maintain or improve margin slightly in the face of -- if you look at the business that way in terms of the overall ADP margin. So now, we're looking forward to hopefully getting a little bit of help. And just to put it in perspective, in Q2 of '08, the average yield on our balances was around 4.5%, and the balances were around $14 billion. Today, our balances are around $22 billion, and our average yield is 1.9. So it just gives you a sense of -- and our margins are higher, obviously, today than they were back then. And we had $160 million or so in float income then and about $100 million or so -- it was $107 million this quarter. So that's another kind of economic factor that we are looking forward to benefiting from here on a go-forward basis. We have -- I would caution you that we've spent the last 2 or 3 years expecting that to happen, and it didn't quite happen. But it does look like, finally, we're in an environment where not only our balances will hopefully growth at a healthier rate because of wage inflation, but that will bring with it some improvements in interest rates -- at least improvement from our perspective, which is higher interest rates.

James Edward Schneider - *Goldman Sachs Group Inc., Research Division - VP*

And maybe as a follow-up, can you maybe be a little bit more explicit about how you intend to use the benefits of the corporate tax reform? I know you reiterated the overall capital allocation policy, but some of your competitors have called for reinvesting a substantial portion of that savings in one way or another. So can you maybe clarify what you would intend to do more reinvestment? Or would you CT most of that back to shareholders?

Carlos A. Rodriguez - *Automatic Data Processing, Inc. - CEO, President & Director*

At the risk of contradicting Jan, who's our CFO, I would say that I think what Jan stated is actually quite accurate. We are not a capital-constrained business. We never -- we haven't been for a long time for several decades. So I guess, other companies are in maybe different situations. But we've been investing in our business, and we've communicated that. And it's created a little bit of pressure in fiscal year '18, and it created some pressure 5 or 6 years ago. So we've -- ADP has always been in growing markets that have a lot of opportunity. And hence, we've been in investment mode for a long time. And tax rates and tax policy in our specific situation, if you are perhaps a manufacturer with multinational operations, differences in tax rates might lead to different capital allocation strategies. But we welcome tax reform because we think it's good for the economy, it's good for U.S. competitiveness, and that's good for ADP as well. But our company specifically is not capital-constrained. And so we would anticipate that the majority of the benefits of tax reform will flow to the bottom line. And subject to the board's approval, things like share buybacks and dividends should flow from that. Having said that, we are looking at some modest increases in our charitable contributions, and perhaps increasing some of the wages of some of our folks who are at 15 -- below $15 an hour. And also, we anticipate having a higher merit-based pool for our merit increases in the next fiscal year. So we are doing some things to, I think, make some investments in our business. But I think the message you should hear is the one that Jan delivered, which is the majority of the benefits of tax reform to ADP's bottom line should flow through, I think, to shareholders.

Operator

And our next question is from David Grossman with Stifel.

David Michael Grossman - *Stifel, Nicolaus & Company, Incorporated, Research Division - MD*

Carlos, if you just go back to that last question about the macro or in the relatively strong labor markets. And maybe this isn't kind of the right metric to look at, but your pays per control has stayed relatively stable over the last 3 years. Could you perhaps at least make the connection between what we're seeing in the underlying labor markets in that particular metric?

Carlos A. Rodriguez - *Automatic Data Processing, Inc. - CEO, President & Director*

Yes. I think it's -- honestly, I think it's consistent because what happens is the unemployment rate doesn't always reflect everything that's happening because, as you know, the underemployment rate has also been coming down. So as people get pulled back into the labor market, that can create underlying growth in labor that might not be reflected in the government's reported unemployment rate. Our NER number, obviously, doesn't take into account -- it's just a number of how many people are getting hired each month. And I think the trends there have been strong and consistent, as you said, for several quarters. So I think our pays per control metric, or NER, in my opinion, are better proxies for measuring underlying labor growth, unless you're willing to go one level deeper in the government's data and not focus just on the unemployment rate. So I don't know, Jan probably has a couple of comments.

Jan Siegmund - *Automatic Data Processing, Inc. - Corporate VP & CFO*

David, I think the delta between the national growth employment, which hovers around 2%, I believe, and our 2.5% pays per control is fairly consistent. So our client base historically has outgrown the economy a tiny bit, and that has to do with company mix and the type of clients we attract. So the trends are strong. And I think what Carlos was indicating in his earlier comments is really a question of how long is the U.S. labor market providing that type of pool for those types of growth rates. And I think you see this in the beginnings of the wage levels increasing and the tighter labor market. So at some point, that could happen. But so far, our trends are very consistent and consistent with the reports of the overall economy.

David Michael Grossman - *Stifel, Nicolaus & Company, Incorporated, Research Division - MD*

Right. And just -- one point of clarification. I'm sorry, I've just forgotten how this was accounted for. But when you divested the consumer-directed benefits business last year, are those numbers still in the historical base? And if so, is that about 100 basis points of headwind to your growth rate this year? Or is that eliminated from the base?

Carlos A. Rodriguez - *Automatic Data Processing, Inc. - CEO, President & Director*

That is correct. It is -- there's no more -- not no more, but discontinued ops treatment changed a while back. And so that is one of the things that we have to help you with, both from an acquisition and disposition standpoint of making sure that you guys understand all the ins and outs. And so we just finished lapping that disposition. And it will not be in our numbers on a go-forward basis, but it has put about 1 point of pressure for the last 4 quarters on our growth rates.

Jan Siegmund - *Automatic Data Processing, Inc. - Corporate VP & CFO*

That's right. And part of the acceleration that you'll see is driven by that thing growing out, but we also then have acceleration of our organic revenue growth driven by the 2 incremental acquisitions that we did. So both the impact in the quarter from M&A activity was slightly below 1%. And so all netted out in the quarter.

Operator

Our next question is from Rick Eskelsen of Wells Fargo.

Richard Mottishaw Eskelsen - *Wells Fargo Securities, LLC, Research Division - Associate Analyst*

Carlos, I just wanted to circle back on your comments earlier about acquisitions. I know for a while you'd really stressed simplifying the business. And now that you've made these acquisitions, I'm just wondering if you could sort of tie it into your prior comments about simplification. Did you get the business to a point where it made sense to bolt these things on? Did you see things in the internal environment? Just sort of if you can help us tie it together to your prior strategy.

Carlos A. Rodriguez - *Automatic Data Processing, Inc. - CEO, President & Director*

It's a great question because, again, people can convince themselves of anything. So I think we believe that this is not a departure from our strategy around simplification because, frankly, we still have a lot of work to do on that front. So these acquisitions are -- in the case of the Global Cash Card, we did have a card business, but we have a very clear plan that is fairly quick around migrating onto the Global Cash Card platform. So we bought that acquisition, not to keep it as a separate business, to just have another thing hanging off on the side that we go out and sell and have no integration, which is what got us maybe into some challenges over the years. There's a very clear plan here with a very clear time line and with a very clear benefit. So we feel like we gained a lot in terms of efficiency, innovation and distribution with Global Cash Card. And our plan is to use that platform on a go-forward basis. And I think we mentioned that shortly after the acquisition. So that would be very different from maybe historically some things that we acquired that just basically added another product into the lineup and, in many cases, added another product in a business that we were already in. So as an example, we accumulated several benefits, administration platforms and several payroll platforms over the years, and these acquisitions are really entering new markets that are fast-growing with big upside rather than just accumulating, I guess, additional assets in existing businesses. The WorkMarket acquisition is opening up a whole new category for us, which is independent contractors or freelance workers. So again, like anything in life, we acknowledge that we could look back 2 or 3 years from now and say that was all a rationalization, and it just added more complexity. But we think that the risk/reward here was definitely on the right -- came out on the right side to make these investments. And we're incredibly excited about what they could do to our top line growth and our new business bookings going forward.

Richard Mottishaw Eskelsen - *Wells Fargo Securities, LLC, Research Division - Associate Analyst*

Very helpful. Just my follow-up is on the balance sheet, Jan, you saw -- put to a net debt position. Unusual for you guys. I know some of that's probably due to timing and some acquisition payments. But just sort of talk about your comfort with the balance sheet and staying potentially in a net debt position.

Jan Siegmund - *Automatic Data Processing, Inc. - Corporate VP & CFO*

Yes. I think there's just really, on the balance sheet, nothing fundamental happen. We had a few short-term movements on the accounts receivable that resolved themselves. We had the acquisition payment. The balance sheet movement is nothing that would concern us. The business generates free cash flow in line with our operating earnings growth. And so I'm not seeing anything. What you see and what you will observe is, due to the rising rate environment, the gains in our client fund portfolio have shifted to a loss, which means, basically, the embedded rate in our client fund portfolio are now lower than the market rates. But since we hold all these securities to maturity, there will be no impact on our operations. So this is to be expected for the portion of the client fund assets that we have on our balance sheet. That should be just mathematical basically.

Carlos A. Rodriguez - *Automatic Data Processing, Inc. - CEO, President & Director*

And I think -- I would just comment that I think we still have one of the most conservative balance sheets around. And I think that the debt offering that we did, which is now that we've returned several billion dollars back in the form of share buybacks over the last few years, as you see our cash balance going down, that's exactly what we wanted to do. We're trying to optimize our capital structure. So I would argue we still have a little bit of debt capacity. And I think we're very happy with our balance sheet, as are the credit rating agencies. And we have all the financial flexibility in the world that we need. So I see it, frankly, as a positive that we've worked down our balances through both acquisitions, share buybacks and dividends or cash balances.

Operator

Our next question is from James Berkley of Barclays.

James Robert Berkley - *Barclays PLC, Research Division - Research Analyst*

Just on the recent WorkMarket and Global Cash deals, could you speak to the opportunity on the cost and revenue synergy side, particularly as it pertains to helping ADP continue its push towards cloud-based solutions and expand into new markets? Just what percent of your business in terms of revenue is this deal touching -- the deal's touching? And what size TAM do you see that opening up for you? I know you spoke to new opportunities there as well.

Carlos A. Rodriguez - *Automatic Data Processing, Inc. - CEO, President & Director*

Listen, it's a great question. Again, it's probably beyond the scope of the call, but I'll try to give you a little bit of color. As with a lot of things that ADP does, I hate to keep saying it, but because of our size, the short-term impact on revenues in the bottom line are not going to be immediately obvious. So then a little bit of pressure on our margin as a result of some dilution. But that's only really short-term. On the Global Cash Card side, I think we've given a ballpark, it's probably around a $100 million business in terms of revenues. That gives you some sense. We expect that, when it's combined with our pay card business, to grow faster than the line average of the business. We've, I think, mentioned previously in our comments about impact of acquisitions that our acquisition had about a 1% impact on our revenue growth. So I think it gives you a little bit of sizing, if you will. WorkMarket was small, but the technology in the platform -- first of all, it is a cloud-based platform modern technology stack. We anticipate that, that could touch and is an opportunity for our entire client base in the United States in the domestic market. Almost every company from small to large companies use independent contractors or freelance workers. And so, obviously, it's going to take us some time to make sure that we have the right value proposition of the combination of Global Cash Card with WorkMarket, with our traditional compliance and HCM solutions. But as we work through that, we think that, that opens up an enormous market before us in the kind of the rest of the way people work, which are around freelance work. So I think having the ability to cover both W2, traditional W2 employees as well as freelance workers, I think this opens up a huge opportunity for ADP. The freelance market is growing faster than the W2 way of employing people. And so I think that also allows us to capture that segment of the market, which is clearly growing faster than the traditional part of the economy, which is the traditional W2 employer -- employee.

Jan Siegmund - *Automatic Data Processing, Inc. - Corporate VP & CFO*

Yes. Just with the market sizing, we have approximately, I think, 170 million W2 workers and about 50 million to 60 million 1099 workers in U.S. according to our market research. So -- and about 90% of our major accounts, the national account clients have meaningful contingent worker employments. So that makes the acquisition that is clearly very early stage, very small today kind of strategically so interesting to us. And so it will do 2 things. I think it will enhance the competitiveness of our core offerings because, over time, this will take a little bit of a while to integrate, but it will become part of our -- deeply integrated into our core HCM platforms. And then we'll offer, obviously, incremental revenue opportunities to service those gig workers. So for the immediate impact during -- given the small size this business is today, next 18 months, probably not as much, but over time I think a meaningful differentiation going forward.

James Robert Berkley - *Barclays PLC, Research Division - Research Analyst*

Yes. I would think, over time, there'd be some ample opportunity there on the margin side, just given the shift to the cloud, and the fact they can touch your entire U.S. ES segment, it looks like. But just as a quick follow-up, just on the -- in terms of you guys are nearing the end of your mid-market migrations, should we see a meaningful benefit to margins from shutting down the old platform at all? Or any color you can give on the progress and timing or expectations for the upmarket as well would be helpful.

Carlos A. Rodriguez - *Automatic Data Processing, Inc. - CEO, President & Director*

I think the best way to look at it is to see the experience we had in Small Business in our downmarket, which is the shutdown of the platform, of legacy platforms when they occur are -- they have an impact on our margins and our cost. But typically, the largest cost, the largest improvement comes as a result of simplification and focus and ability to really focus on process improvement in a single platform. And that usually evolves over time. So what you've seen in the downmarket, I think as we've given you color every quarter and every year for the last 3 or 4 years, the day that we shut down the legacy Small Business platform, the next day, we didn't have this massive margin improvement and an incredible reduction in cost. But over the ensuing 2 or 3 years, we did. And so that business has increased its volume in a significant way in the last 3 or 4 years, and the headcount has remained relatively flat. And we attribute a lot of that to, first, developing the right technology; second, migrating all the clients onto one platform; and third, driving process improvement to take out non-value-added activities and really create value for the clients. And so we anticipate the same thing happening in the mid-markets. So the good news is, if you look at that historical experience in Small Business is that we're close to the end on phase one. We have the technology. We have the upgrades almost complete. And now, over the next several quarters and years, we anticipate real benefits to accrue to us from the simplification and the focus.

Jan Siegmund - *Automatic Data Processing, Inc. - Corporate VP & CFO*

And as a reminder, improvement in retention is probably economically the most important factor in this, but we still have a few clients to migrate as we saw in the mid-market in the third quarter. And as we have indicated in the past, we take a very, very careful approach, so that we don't lose clients in the process unnecessarily. But you never know when you come to the end. But -- so the stabilization of retention rates that we have seen and the improvement, quite frankly, in the mid-market, hopefully, will continue. And that will drive really then incremental profit opportunity by just keeping more clients longer.

Carlos A. Rodriguez - *Automatic Data Processing, Inc. - CEO, President & Director*

That's a fair point. It's great that Jan brought that up because if we go back to Small Business, a main reason why we've seen these margin improvements, efficiency improvements and client experience improvements is because of all things I mentioned about one platform simplification. But clearly, we have much higher retention rates in the downmarket than we did 4 or 5 years ago. And that obviously leads to incredible improvement in the economics of these businesses.

Operator

Our next question is from David Togut of Evercore ISI.

David Mark Togut - *Evercore ISI, Research Division - Senior MD, Head of Payments, Processors & IT Services Research and Fundamental Research Analyst*

Historically, Carlos, ADP's seen a nice pickup in demand whenever there's major changes in the tax code. And I think, historically, those changes have created more complexity, which drives the increased demand. Could you talk about U.S. corporate tax reform in terms of whether you think it creates more complexity or more simplicity and how the impacted tax reform longer term might impact demand for ADP services, both in ES and in PEO.

Jan Siegmund - *Automatic Data Processing, Inc. - Corporate VP & CFO*

Yes. David, if I jump ahead of Carlos here, I would rate the impact on our tax filing business as relatively neutral at this point in time. So the changes were relatively easy to implement, and I don't think that has fundamentally changed the complexity of the payroll business. Going forward, I think there's a high degree of uncertainty as states evaluate their reactions and their consequent steps to the overall changes of the compact of the overall tax bundle that was created. And in theory, it could make it complex. If states is going to change their attitude of how they want to tax their constituencies, it could. But I think that's very speculative today. So my answer would be fairly neutral at this point. We're implementing and implemented those tax rate changes fairly quickly. And that itself was not a big trigger point. I think the increased liquidity and the increased cash inflow from overseas and all that stuff should be a stimulus in the U.S. economy. And I think we're seeing certainly immediate results from that from all the reactions that you also read in the newspaper. So that should help the overall economy, and that will be positive for us. That's kind of my overall assessment.

David Mark Togut - *Evercore ISI, Research Division - Senior MD, Head of Payments, Processors & IT Services Research and Fundamental Research Analyst*

Got it. And just as a quick follow-up. You called out strength in bookings in the quarter, both in downmarket and multinational accounts. Could you give us an update on demand trends in the mid-market and also in U.S. national accounts?

Carlos A. Rodriguez - *Automatic Data Processing, Inc. - CEO, President & Director*

Yes. I mean, I'd say that, again, this quarter, because, again, it's -- the bookings number, like the retention number, can fluctuate from quarter-to-quarter. But I'd say we held our own. I mean, obviously, if I didn't mention them when I talked about our strength. And they weren't on a relative basis as strong, but I can tell you that compared -- it's all about relativity. So the relative performance of our mid-market and upmarket are much better this quarter than last year's second quarter. But the growth itself was strongest and driven by the businesses that I mentioned previously. But it is important to note that from a -- trend-wise that we are very happy with the direction that our mid-market and upmarket businesses have taken. We had a nice increase in the quarter, for example, in new business bookings on our Workforce Now platform in the upmarket, above 1,000, which I think we've kind of reinvigorated that offering in that product to really compete in a segment of the upmarket where it competes very, very well for particular types of clients. So we had a nice growth versus the prior year in terms of the total number of units in the upmarket on our Workforce Now platform. And then on Vantage, we -- I would say we held our own versus the previous year in terms of new client count sales. So I'd say we're pleased and still working through a grow-over issue that the second quarter of last year was the last quarter where we saw meaningful ACA sales in our business. And so that gives you some sense of why I can't be as positive because it's just mathematically difficult. It was mathematically difficult.

Operator

Our next question is from Ashwin Shirvaikar of Citi.

Ashwin Vassant Shirvaikar - *Citigroup Inc, Research Division - Director and U.S. Computer and Business Services Analyst*

Carlos, a question on PEO services. You've commented, obviously, in the past about the continued strength in worksite employee growth. It was a pretty solid 10% this quarter. Given what's happening with both ACA funding and the low unemployment rate, do you think PEO growth might taper off in the next couple of years as we get into late cycle? And any thoughts on sort of the multiyear view on that?

Carlos A. Rodriguez - *Automatic Data Processing, Inc. - CEO, President & Director*

I think it's a great question, and I wish I had a crystal ball. We're not planning on it. So our headcount plans and our investments, I think, are not planning for a deceleration. We're going to try to continue the growth because the opportunity is still there. The value proposition is very strong. But I think you're absolutely asking a fair question, which is we have to be -- and this is a place for us to be cautious in terms of we happen to have very strong pass-through growth, which gives us healthy top line growth. But that obviously has a margin impact, and it makes things hard to read. But the worksite employee count growth is really the right place to focus on, and I think that double-digit growth is still quite strong and, I think, quite satisfying to us. But I think it's something that we have to keep an eye on. We have a lot of tailwinds in our business as a result of ACA. I have said during it, not just afterwards, that it felt like we were getting some tailwinds. And obviously, those tailwinds have abated. So I think it's just become harder in the PEO business.

Jan Siegmund - *Automatic Data Processing, Inc. - Corporate VP & CFO*

I think my one thought that might be also helpful is if you see health care inflation, that means our clients' experience, higher benefit renewals, basically, and that causes, obviously, more thinking in the clients. And so you have to be very thoughtful that you remain committed in your benefit offerings. But overall, faster inflation, I think, will create just focus on the value proposition, which is exactly why we have to pay attention to it and be thoughtful.

Ashwin Vassant Shirvaikar - *Citigroup Inc, Research Division - Director and U.S. Computer and Business Services Analyst*

Understood. And then the follow-up question's on the WorkMarket activation. It seems like a good one, the gig economy in general. Will gig economy workers be included in your pays per control metric as they flow in and out? I mean, how should one treat them vis-à-vis a permanent employee? And I think you addressed this, but this is more of a technology play. So I assume you don't have to go make many similar acquisitions to build scale.

Carlos A. Rodriguez - *Automatic Data Processing, Inc. - CEO, President & Director*

That is correct. It's a technology acquisition. And I think that as we've always talked about pays per control, our pays per control is a subsegment of our total pays in ADP because we want to use one platform in order to be able to isolate same-store sales growth. And so, for example, our pays per control metric that we report doesn't include every platform that ADP has to begin with. And hence we would not anticipate including WorkMarket in that. And as WorkMarket becomes bigger, this is probably a few years down the road, we'll find a way to give you that metric separately, right, because I think it's important. Because my sense is that's going to grow very rapidly, and it might be of interest to the external market. But I think, for now, it's business as usual.

Operator

Our next question is from Jeff Silber of BMO.

Sou Chien - *BMO Capital Markets Equity Research - Associate*

It's Henry Chien for Jeff. I just wanted to follow up on the pass-through revenues just to make sure I'm understanding this correctly. Is the uptick there, is that more a function of product mix and, say, just increases in premiums? I'm just trying to understand if there's any change in the underlying growth rate for either PEO or Employer Services and any changes there, I think.

Carlos A. Rodriguez - *Automatic Data Processing, Inc. - CEO, President & Director*

I think it's probably -- I think Jan has some details, but I would say that -- it's safe to say that the Affordable Care Act, as a result of either the law itself, because I don't want to make a political statement here, but I think health care inflation is higher, let's just say, in general, than it was 2 or 3 years ago. And we serve 500,000 worksite employees, most of which have health care, and it's part of the value proposition that our clients come to us for. And hence, we would not be immune from that, and our clients would not be immune from that, especially given that we treat this as, "a pass-through." And so I think it's that simple. There's really not -- there's not a big mix issue here, and it's higher health care inflation. And by the way, we've had that -- we've owned this PEO for a long time, and we've been through other periods of accelerating health care inflations. So this is not unusual in the historical context.

Jan Siegmund - *Automatic Data Processing, Inc. - Corporate VP & CFO*

Yes. The pass-throughs are growing faster than our worksite employee count. For that reason, the pass-throughs are harder to forecast because there's a number of factors that drive this. It starts with the actual renewal that we get on our policies. And then, obviously, with the lineup that our clients, the employers choose and the plan mix that they offer to their employees, and then what plans employees are actually choosing in enrollment period. And we have seen higher renewals, which is the health care inflation that Carlos mentioned, and that's a large chunk of the faster growth above our worksite employee growth. But we have also seen -- now comes the 201 inside that employee is choosing slightly richer plans, and then they have a slight mixed shift away from the lowest offering to a little bit of richer plan and mix. So that's -- what we have seen throughout enrollment season. And so the vast majority is health care inflation, but there's some little mixed shift in the pass-through growth as well.

Operator

And we have time for one more question, which comes from the line of Mark Marcon of R. W. Baird.

Mark Steven Marcon - *Robert W. Baird & Co. Incorporated, Research Division - Senior Research Analyst*

Carlos, you've got a long history on the PEO side, and I was wondering if you could share your perspective on 2 fronts. One would be like where do you think we are in terms of the maturation of the PEO concept? And specifically across the country, when we take a look, obviously, Florida, Texas, well penetrated, more mature. But when we think about the country broadly speaking outside of those markets or maybe a couple of other states, where do you think we are in terms of the evolution? And then secondly, could you comment a little bit about the balkanization that we're seeing with regards to regulations? When we take a look at states like California, New York, et cetera, we're starting to see all sorts of different regs that are popping up. That must make it difficult to be in compliance.

Carlos A. Rodriguez - *Automatic Data Processing, Inc. - CEO, President & Director*

Yes. I think on the first point, I just -- I think my reaction about the question about the PEO, first and foremost, is to say, my immediate reaction is pride, right? So what's happened to that business in the last 18 or 19 years as ADP has owned it, if we could do a few of those, would certainly make a difference for the company. And I think that what drove the success, besides a lot of hard work from a lot of people, and a lot of good execution was the fundamental strength, the value proposition and the underlying trends. And I think those still are intact. So despite the comments you made about penetration in some states improving over the years, it's still really a relatively small part of the market that's served by PEOs. So -- and it's tied to the second part of your question, which is, unless you believe that all of a sudden it's going to get easier to be an employer -- and I think Jan touched on this a little bit around tax and the fact that states might have different views on how to deal with tax reform from their perspective. And then tying that to the second part of your question, one of the good things for ADP is that since ADP has existed and since this country has existed, there's been a non-ending trend towards more complexity around being an employer or even being a corporation. And we clearly now have a focus on deregulation from the current administration. But you have to take that in context. A lot of that is around energy and other sectors of the economy, in some cases, appropriately so probably. But again, without making political statements, it's safe to say that the task of being an employer at either the federal level or the state and local level because it matters. It's not just about headlines around what the federal government is doing, it's also around what you're talking about, is if you're an employer in multiple states, you have a very difficult task keeping up with all of the various regulations that are intended to push forward public policy at the state level, if not at the federal level. And so that is all kind of a dream situation, if you will, for ADP because companies should be focused on their core business and on executing on their companies not on trying to deal with all of these changes in the regulation. And the majority of companies want to be in compliance with these regulations. So I think it affects not just the PEO, but it affects the overall ADP business. And I think we remain as optimistic today as we ever have. That's probably why the industry in general, the HCMs in general is growing faster than GDP. And ADP, with its strong compliance orientation, probably has an even greater benefit because of the DNA that we have around helping clients deal with the complexity that you're describing. So I think answer number one is, I think the PEO's not done in terms of the opportunity that's out there just because of simple mathematics. That doesn't mean or guarantee that the execution will be there because we have to still execute, and the rest of the industry has to execute. But I think the opportunity is still definitely there. And then secondly, you touched on a very important point that I think Jan kind of also touched on, which is we don't see any abatement in the complexity and the difficulty of being an employer in the United States.

Mark Steven Marcon - *Robert W. Baird & Co. Incorporated, Research Division - Senior Research Analyst*

Great. That's precisely where I was getting at. And then, I mean, just to boil it down on the long runway. I mean, if you were putting it in baseball terms, would you say PEO is maybe in the third or fourth inning in terms of penetration? Or how would you characterize it?

Carlos A. Rodriguez - *Automatic Data Processing, Inc. - CEO, President & Director*

I'm going to let Jan answer that question because he's an expert in baseball. Jan, do you know how many innings there are in baseball? I can answer that question. I don't think that's -- it probably shouldn't be in the business we're trying to forecast. I think the -- I would focus really, like I always do, on the math, right? The number of -- the total -- I think the industry says that there are about 2 million -- you probably know better than I do, Mark, but I think the PEO industry says that there's about 2 million people under PEO arrangements, maybe 2.5 million. And Jan said there's 170 million private sector employees. We know that, obviously, this is a downmarket and mid-market type of value proposition. There's 26 million people on our own payroll systems, as we report every -- to you on a regular basis. And we have 500,000. So I think anyway you look at it, it looks like there's plenty of opportunity. But I think it's dangerous for me to use a baseball analogy because you'll probably remind me of it for the next 5 or 10 years.

Operator

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

Carlos A. Rodriguez - *Automatic Data Processing, Inc. - CEO, President & Director*

Thanks. I think as you can see, we're very pleased with the progress that we've made on our strategic initiatives during the first half of the year. And we also want to just reiterate our welcome to our colleagues from WorkMarket to ADP, and we look forward to the success we're going to have together. It's acquisitions like these, along with the investments we've made in the next-gen solutions that I think demonstrate our commitment to progress and our commitment to our transformative strategy. As you can probably tell from the call, we also are anything but status quo here at ADP. We intend to move forward with pace and with conviction. We've talked to our leadership about moving with urgency, but also with care because our client experience and our retention rates are also incredibly important. And lastly, I'll say that we carefully listened and learned from all of our shareholder engagements during the proxy contest. And I think they decided the things we learned. It also strengthened our resolve to accelerate the execution of the strategy that I think was -- I think on the right path to begin with. But there's nothing wrong with a little bit of acceleration. Our markets are changing. The nature of work is changing. I think that creates opportunity. And it creates, as we said, in some cases, complexity for employers. And I think that's good for ADP. So I thank you for joining the call today. We look forward to continuing to share the details of our journey with you down the road, and we appreciate your interest in ADP.

Operator

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