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PRESENTATION

Operator

Good morning. My name is Mary Ann, and I will be your conference operator today. At this time, I would like to welcome everyone to the Hudson Highland Group's fourth quarter earnings conference call. [OPERATOR INSTRUCTIONS.]

At this time, I would like to turn the conference over to David Kirby, Director of Investor Relations. Sir, you may begin.

David Kirby - ***Hudson Highland Group, Inc. - Director of Investor Relations***

Thank you, Operator, and good morning, everyone. Welcome to the Hudson Highland Group conference call for the fourth quarter of 2006. Our call this morning will be led by Jon Chait, Chairman and Chief Executive Officer, and Mary Jane Raymond, Executive Vice President and Chief Financial Officer. Before we begin, I will read the Safe Harbor Statement.

Please be advised that except for historical information the statements made during the presentation constitute forward-looking statements under the applicable securities laws. Such forward-looking statements involve certain risks and uncertainties, including statements regarding the Company's strategic direction, prospects, and future results. Certain factors, including factors outside of our control, may cause actual results to differ materially from those contained in the forward-looking statements, including economic and other conditions in the markets in which we operate, risks associated with acquisitions, competition, seasonality, and the other risks discussed in our filings made with the Securities & Exchange Commission.

These forward-looking statements speak only as of today. The Company assumes no obligation and expressly disclaims any obligation to review or confirm analysts' expectations or estimates, or to update any forward-looking statements, whether as a result of new information, future events, or otherwise.

With that, I will now turn the call over to Jon Chait.

Jon Chait - ***Hudson Highland Group, Inc. - Chairman and CEO***

Thank you very much, David. Thank you for joining us today. I want to start off with just a couple of remarks from a strategic perspective, and then I'm going to turn the call over to our Executive Vice President and Chief Financial Officer, Mary Jane Raymond, to go through the numbers in much more detail.

As you look at our reported financial results for the quarter and the year, one of the things is that our goal for some time has been to simplify our reported financial statements. Unfortunately, our statements for this quarter and the year have become somewhat more complex, and that's going to require a little more of an explanation than we would like. But as you parse through our financial statements, I would draw your attention to adjusted EBITDA as the best indicator of operational results for the quarter and the year. Adjusted EBITDA is before restructuring and the impact of the divestiture of Highland Partners, which is reported as a discontinued operation.

If you look at adjusted EBITDA from continuing operations for 2006, we reported $31.8 million, compared to $21.4 million in 2005. Another way to look at that is to look at the $31.8 in 2006 and compare it to the EBITDA for continuing operations in 2006, which included at that point--I'm sorry, for 2005--which included at that point Highland Partners. That would give you an EBITDA in 2005 as reported of $25.1. So if you compare the $31.8 to $25.1 we had an increase of 26%. What that means to me is that we were able to absorb the entire dilution from the Highland Partners divestiture and still report earnings growth in the year.

The second strategic point that I'd like to make is that we continue to narrow our focus of our business. We think that's important to allow us to be successful in the future. Part of my thinking and a fundamental principle of mine is that if our focus is narrower it will cause our operating colleagues to focus their activities and will increase their chances of success.

We've made a number of divestitures during 2006 and another small one in the first quarter of 2007. For example, we've completed, and I think we've reported to you in the past, the sale of our Scottish industrial business. And, of course, you know about the sale of Highland Partners in 2006. In the first quarter of 2007 we completed the sale of a small unit in the UK in office support. So we're continuing to narrow our scope through these divestitures.

A number of you have asked me to comment on the scope of the possible divestitures, so let me start off by commenting on how we define our core business. We see our core business as being focused around high margin, professional recruitment and staffing, including temporary project solutions and permanent services. We will also provide services that enhance our core business and our thought leadership, such as talent management and other activities in specific jurisdictions in which a nonprofessional unit might be highly profitable or might be critical to our value proposition in that market.

For example, and an example of the latter is the service and support business in Australia. It's a nonprofessional business, but it's very important in that market as a support to our professional business. We also don't particularly worry about the core, non-core distinction in smaller or emerging markets where the size of the market does not particularly support segmentation. For example, in New Zealand.

After saying all of that, over a period of time we would expect that businesses to be divested might amount to 10% of our total revenues, with EBITDA ranging from 3 to 5%. We believe there are buyers for these businesses but probably not at the same multiple as which we currently trade.

Turning now to the North American market, which has been a market on which we and many investors have focused over the last year. I think the quarterly results demonstrate another step forward in improved financial performance. It is, of course, way too early to declare victory in that market, but I think we have made a sound step forward. Obviously, we continue to be focused on the revenue line, and the revenue progress has not been where we want it to be and where we aspire for it to be. But, on the other hand, we think the return to profitability is a very good indicator of future performance.

We announced yesterday, as well, a change in the management of our North American operation with the resignation of our president, Tom Moran. And, as a result, I will assume the role of acting president and CEO of Hudson North America for the next period of time.

I've indicated, I think, in the press release that I intend to be in this role somewhere between six months and a year. We have not instituted a search at this point for a replacement for me because I want to spend the time to understand the business and understand the skill set that's required of the next chief executive. I think, also, we have a number of internal candidates that I want to have a chance to evaluate on a real-time basis before I make a decision of whether or not to go to the outside.

The next thing that I would just comment on briefly is restructuring. During the quarter we took the opportunity to accelerate a number of restructuring activities, as we had discussed with you in our previous quarterly conference calls. The financial flexibility that we gained through the Highland divestiture allowed us to accelerate a number of actions that we thought were necessary to improve the financial performance and the efficiency of our business in the future. Mary Jane is going to discuss those in much more detail, so I won't go into that right at the moment.

While I mentioned that we were narrowing our focus, which I think is appropriate to ensure the success of our organization, at the same time we are continuing to expand our business in our fast-growing attractive markets and, also, earlier, I think yesterday we announced an acquisition in China of the Tony Keith organization. This is a very important market in our industry, as it is in many, many industries, and we were able to sign the major IT recruitment company in China, which we think will significantly augment our offering in that very important market.

I would tell you that this transaction is consistent with our philosophy in terms of pricing discipline, which is the price transaction is at sometimes around five times EBITDA with earn outs over three to five years. Obviously, that pricing discipline eliminates us from many other types of acquisitions, and we don't particularly look at large acquisitions as being fundamental to our Company, but we do look for small bolt-on acquisitions that can fill a gap. And in this case the gap was in IT in China, or fill a gap in a particular geographic market. So we think this fits within our acquisition strategy.

One of the things about the financial results that I think is important to understand is that while we are reasonably satisfied with the operating results on a consolidated basis, those results are somewhat affected by the underperformance in our North American market during 2006. I'd like to point out that we had a significantly improved year in our other two major markets, in Europe and Asia-Pacific, and looking particularly at a significant improvement in terms of adjusted EBITDA margins in 2006 versus 2005. In both of those important regions, and in our Asia sub region, which is becoming increasingly important to us, we continue to operate at a very high level of profitability.

So I think on a whole, it's fair to say that we continue to make improvement in important parts of our business, while we have dealt with the challenges that we faced in the North American market. That gives us confidence as we look to 2007 and an improved consolidated result.

With that, I'll turn it over to Mary Jane Raymond to go through the financial results in more detail.

Mary Jane Raymond - ***Hudson Highland Group, Inc. - EVP and CFO***

Thanks, Jon. Good morning.

Regarding the financial results for, first, the fourth quarter of 2006 and then the full year, I'd like us to just begin with two reminders. First, other than net income all of the numbers I'm going to talk about are from continuing operations. They exclude Highland Partners for both 2005 and 2006 because that is the treatment for discontinued operations. I'll talk about the impact of the Highland transaction during the full year results.

The second reminder is that our financial statements reflect the adoption of FAS 123, the accounting pronouncement for expensing stock options,on the modified retrospective method. Our Company elected that method when we began this adoption in the first quarter, and what that means is the stock option compensation costs are recorded in both 2005 and 2006. Just as a reminder, the costs are relatively equivalent per quarter, and in total were $4.5 million for 2006 and $4.2 for 2005.

Turning to the quarter, we'll begin, as we reported, our reported revenue for the fourth quarter was $341.6 million, which is an increase of 1% from prior year and down 2% on a constant currency basis. The specific color on the constant currency is that Europe's revenue declined 7%, while Asia-Pac's rose 5%.

From a gross margin perspective the reported gross margin increased 10% from prior year. On a constant currency basis the gross margin dollars increased 5%, including 5% in Hudson Europe and 10% in Hudson Asia-Pacific. The gross margin as a percent of the revenue was 37.4 in the fourth quarter of '06, compared to 34.5 a year ago.

And adjusted EBITDA, as Jon said, what we consider the best measure of our ongoing operating performance, in the fourth quarter was 15.6, compared to 4.5 a year ago. EBITDA, which is adjusted EBITDA less the restructuring charges, was $12 million or 3.5% of revenue. EBITDA was driven by regional EBITDA margins of 7% in Hudson Asia, 6% in Europe, and 3% in Hudson Americas, as well as reduced corporate costs.

The restructuring charge for the fourth quarter was $3.6 million. This was higher than the guidance that we gave of roughly about $2, because we were able to successfully complete more actions during this quarter, particularly in geographies where restructuring is very difficult to accomplish. We also reviewed the actions taken in our previous programs and recorded revised estimates where they were necessary.

The depreciation and amortization expense in this quarter was higher than normal at $8.3 million because we wrote-off $1.4 million of impaired intangibles on the Alder Novo acquisition and we recognized $2.8 million of accelerated depreciation on the leasehold improvements for our former New York headquarters. We moved from the New York headquarters to a new location in the beginning of January 2007. These items total $4.2 million, and excluding them, the D&A is within the range of our recent trends.

Our provision for income taxes in the quarter was a credit of $1.7 million. This is driven by the recognition of a deferred tax asset in the UK of $3.5 million that is related to tax deductible capital cost allowances. I'll provide more color on the taxes shortly.

The consolidated net income in the fourth quarter was reported at $23.7 million, up from a consolidated net income of $1.8 a year ago. The net income from continuing operations was $5 million, up from a loss of just under $200,000. Basic and diluted EPS were $0.96 and $0.94, respectively, compared with 7% basic and diluted in '05, the same quarter.

Let me turn to the full year to talk about our year for 2006. The reported revenue for the full year was $1.4 billion, essentially flat to 2005. It was up 1% on a constant currency basis. The color here, again, on the constant currency is Europe's revenue declined a little bit less than 2% and Asia-Pac's rose a little bit more than 2%. From a mix perspective, on a constant currency basis the temporary contracting revenue was flat to prior year. Permanent placement increased about 10%, and talent management revenue declined 11%.

The reported gross margin increased 3% from prior year, with a 4% decline in Hudson Americas, 7% and 4%, respectively, for Hudson Europe and Hudson Asia-Pac. On a constant currency basis for the year, the gross margin dollars increased 4%, including gains of 6% in both Hudson Europe and Hudson Asia-Pacific. Gross margin as a percent of revenue advanced 100 basis points to 35.9 for the year 2006, compared to 34.9 a year ago.

Adjusted EBITDA for the year was $31.8 million, compared to $21.4 a year ago. EBITDA, again, which is the adjusted EBITDA less the restructuring charges, was $25.3 million. This result is 1.8% of revenue. EBITDA was driven by regionally but down margins of 7%, and Hudson Asia-Pacific, 5 in Europe, and a negative 1% in Hudson Americas, as well, for the year in reduced corporate costs.

To provide some color on the restructuring program that we initiated in 2006, our charges recorded in this year are $6.4 million, against our range that we set at the end of the second quarter of $4 to $7 million. As I mentioned during the call in the third quarter, I expected that our restructuring charges for moving or reducing space in a number of offices, including two of our most expensive properties, would be incurred in the first quarter of 2007 and are estimated at between $3 and $4 million. The reason that those charges moved into the first quarter and were not completed in 2006 is because, as many of you know, moving from complex regional headquarter properties is actually very complicated. That said, I'm happy with the completion of our move in the New York property, and I'm confident that we'll be on with the rest of this.

So if we think about the total 2006 program, as we conceived it, the restructuring program, the charges are between $9 and $10 million. This total is higher than our overall estimate but, again, it's because we were able to complete more actions. And, as Jon mentioned very well, the completion of the Highland Partners deal provided us the ability to do that and it was our goal to take advantage of that and drop our cost base where we could.

The provision for taxes for the entire year was $4.5 million. During 2006 we released the remaining valuation reserves for New Zealand and the UK of about $4.3 million in total. The net income from continuing operations of negative $100,000--of $100,000 is $3.8 million ahead of last year's equivalent loss of $3.9 million.

To turn our minds then to the discontinued operations, to provide you some color on that. Again, the discontinued operations line includes everything having to do with Highland Partners and in both years. It includes, first, the gain on the sale, which is $20.4 million and the results of operations of $900,000, as well as the tax provision on parts of this sale, leaving a net income for the operation of $200,000. Therefore, the amount that's recorded for total discontinued operations is $20.6.

The consolidated net income which as reported includes both net income from continuing operations and the net income from discontinued operations was $20.5 million, compared with just under $1 million in 2005.

The basic and diluted EPS were $0.84, compared to $0.04 basic and diluted for the year 2005. The EPS from continuing operations was zero, compared to a loss of $0.17 last year, both basic and diluted.

We had $24.5 million diluted shares outstanding at the end of 2006, compared with $22.3 million in 2005.

Let me pause and move to some business mix and other color on how our results were achieved this year. While our mix of business by product and geography remains more or less unchanged in Hudson from prior years, we continue to benefit from the strategy that we have been executing. We continue to advance the gross margin of the business with a year-on-year increase of 100 basis points. Our temporary contracting acquisitions continued to perform well. Permanent recruitment was our largest contributor in gross margin dollars, showing our taking advantage of this. We sold, as Jon said, the Scottish industrial business and the sale of Highland Partners this year, as we continued to shrink the percentage of non-core in the business. And we acquired this recruiting firm, as Jon described it, in China.

From a regional perspective, as we think about the results in those areas, let's start with Europe. Europe's fourth quarter revenue declined 7% on a constant currency basis as they continued to exit low margin business. With that, the gross margin dollars advanced 5% and the EBITDA nearly doubled after absorbing $2 million of restructuring charges. For the year, Europe delivered EBITDA increase of over 50% on revenue that was down 2% and gross margin growth of 5% on a constant currency basis.

With respect to Asia-Pacific, their fourth quarter revenue grew 5% on a constant currency basis as they continued to reposition their value propositions with customers. Gross margin dollars advanced 10% and EBITDA, as well here, advanced over 50% after absorbing about $600,000 of restructuring charges. For the year, Asia-Pacific delivered an EBITDA increase of 11% on revenue increases of 2% and gross margin growth of 6%. New Zealand and Japan did particularly well considering that both of them have weathered economic and business challenges through this year.

As for North America, their fourth quarter revenue declined 4%. As a result, their adjusted EBITDA declined 10% to prior year. At the completion of this difficult year for Hudson Americas, full year revenue increased 2% and gross margin declined 4. The adjusted EBITDA loss of $1 million was helped by the reductions in expenses during the second half of 2006. Hudson Americas reported a restructuring charge of $2.2 million, for a complete EBITDA loss of $3.2 million.

Regarding corporate expense, which last year was $37 million, corporate expense in 2006 was $28.4, including $700,000 of restructuring charges. It occurs to me that some of you may ask about the run rate for corporate expense, given that the fourth quarter was 5.5. That is primarily due to lower compensation costs as we ended this year and evaluated the results. I would say for purposes of evaluating the run rate, going forward into next year, Q2 and Q3 provide a run rate that is what I would expect to see going forward.

Just to give you a few more points of color, on currency, we've talked about that through the comments here. For the fourth quarter the EBITDA results were improved by $500,000 for currency, but the whole year was reduced about 700, basically due to the reversal as we saw through the year of the strength of the dollar, from the beginning of the year, to a less strong dollar by the end of the year.

With respect to PeopleSoft, as we noted in the shareholders letter, the implementation phase began in the fourth quarter pursuant to the program that we put in place, led by Oracle, the parent of PeopleSoft. We expect this work to continue through the middle of 2007. This work remains on schedule and on budget. Related expenses for this in the fourth quarter were about $1.5 million.

To provide some Technicolor on North America, vis-Ã -vis PeopleSoft, I'll give you some things that probably only CFOs love, and that is that North America continued to see good improvements in their management reporting and back office efficiency as a result of being able to begin to implement this remediation program. We're cautiously optimistic about the outcome, since this is an important area for us. We want to be careful about this. We still have five months of work ahead of us, but certainly we feel like the back office, which is the first area to be affected by this, is beginning to see a greater level of efficiency than we saw through the first part of this year, 2006, and certainly in 2005.

Our fourth quarter cash flow, turning to cash flow, for operations was a positive $18 million. This compared to a use of cash in the fourth quarter of 2005 of $5 million. Our cash flow from operations for the year is slightly north of $35 million. Our net cash, which is cash on the balance sheet, less debt, is over $44 million versus $4 million for 2005, and $10 million at the end of the third quarter.

We exited 2006 with no debt outstanding on our credit facility. We used, obviously, as we reported at the time, the proceeds of the Highland Partners sale to Heidrick and the repayment of about half the debt outstanding in October, and our improved cash flows from operations did the rest. This was a year where aggressive focus on cash and strong collaboration between the operating teams and the finance staff allowed us to improve cash collections.

As a final point on cash, in general, we made significant progress in reducing the total outstanding letters of credit, which are a reduction to our availability of credit line, during the 2006 year. We began the year with $15.5 million in letters of credit, and we exited the year with $10.7. Again, this increases our borrowing capacity and our financial flexibility.

As I mentioned earlier, on depreciation and amortization expense of 8.3 in the fourth quarter was higher than normal, due to the two items that I mentioned. Excluding this amount, D&A would have been consistent with the levels we've seen before.

Capital spending for the year was about $11 million, compared to CapEx in the 2005 year of roughly $10. For 2007, my expectation is that the capital will be between $12 and $14 million.

Turning to the balance sheet, as I've mentioned, probably the most significant change in this year compared to last year was the change in the cash and the retirement of the debt that we had outstanding at the end of 2005. Our DSO for our Company is down one day to 55 days from 56 days last year. In North America, their DSO was 55 days, down from 70 days at last year end.

With respect to taxes, we had, as I mentioned, a net tax credit in the fourth quarter of $1.7 million. Excluding this, we had $1.8 million of tax expense, a more normalized level. Going forward, our past tax guidelines remain true. Except for a near 30% rate in the Asia-Pacific area--sorry, let me start that again. Basically, we pay taxes in the Asia-Pacific area of roughly about 30%, as well as taxes on the profits from Balance. We do expect to incur, as we enter '07, taxes on the UK. We had been, as the UK became more profitable, recognizing deferred tax assets against that. We did conclude those in the 2006 year, and we would expect to see P&L taxes for the UK through 2007 and forward. Though, we'll continue to have the cash benefit of deductions going forward.

With respect to guidance, let me first say we will continue to stay with our revised format in the middle of last year, of providing quarterly guidance. We expect the first quarter of 2007 to be revenue of about $330 to $345 at prevailing exchange rates, and we expect adjusted EBITDA, the EBITDA with no restructuring charges in it, at roughly $3 million. We expect to record restructuring charges in addition to that of between $3 and $4 million, for as I mentioned before, the completion of property actions that we anticipated. This compares with a revenue of $327 million, last first quarter, and an adjusted EBITDA loss of 3.6.

So just to reiterate, the adjusted EBITDA number does not include the restructuring charges and, therefore, if you add the two together it's at roughly a breakeven sort of number.

With that, I'd like to open the lines for questions.

David Kirby - ***Hudson Highland Group, Inc. - Director of Investor Relations***

Operator?

QUESTION AND ANSWER

Operator

[OPERATOR INSTRUCTIONS .]

Your first question comes from the line of Matt Litfin of William Blair and Co.

Matt Litfin - ***William Blair and Co. - Analyst***

Hi, good morning. Congratulations on a nice end to the year.

Jon Chait - ***Hudson Highland Group, Inc. - Chairman and CEO***

Thank you.

Matt Litfin - ***William Blair and Co. - Analyst***

My question is around Alder Novo, I wondered what the impetus for the write-off of the intangibles there?

Mary Jane Raymond - ***Hudson Highland Group, Inc. - EVP and CFO***

Hi, Matt. How are you? The--as we--as Jon mentioned, one of the things that we are doing and I think actually accelerated through this year is a focus of the business on our core activities, and the things that best fit with the core of the business.

The Alder Novo acquisition, while a good company, is primarily, as we probably described last year around this time, a business on executive coaching. We took a decision that that probably going forward was not consistent with the focus areas we would have in talent management and some of their own challenges through this year assisted us in that decision. So the bottom line is that we felt the ongoing performance we expected to see from that unit, as well as its fit with our strategy, provided an importation rationale for our decision in writing the goodwill off.

Matt Litfin - ***William Blair and Co. - Analyst***

Okay. The next question is on the collections. Your collections activity improved across the year. I wondered, where can you get that DSO number to and what are your goals there?

Mary Jane Raymond - ***Hudson Highland Group, Inc. - EVP and CFO***

You're asking me the big internal secret. Well, first of all, I think as I said during our call in the third quarter, given that ours is a business that certainly bills every month and in many, many cases bills every week, I do not like a DSO number that starts with a 5. I have been clear with the organization about that. And the good news is that I'm blessed with having a lot of operating colleagues and financial colleagues who believe that, as well.

It's a little bit tough to tell exactly where it can go when we operate so broadly across three main or four main geographies, but my general sense is that we would strive hard to get it into a number that starts with a 4, not necessarily putting any timing on that, and that a continued reduction in that number is very important to us.

Matt Litfin - ***William Blair and Co. - Analyst***

Thanks, Mary Jane. The last question is for Jon. If you want to head up North America on an interim basis in, for the next 6 to 12 months, with the other operations, it seems like a lot to do, so I was asking--I wonder if you could tell us a little bit about what the management structure looks like in North America now underneath you as the interim head?

Jon Chait - ***Hudson Highland Group, Inc. - Chairman and CEO***

Well, thank you, Matt. I think we have a good structure, a good management structure underneath me. We're organized by what we call "practice groups," such as IT, financial solutions, legal, engineering, and so forth. And so each of those practice groups you can think of as a business unit, each of those is headed up by an executive vice president who has the responsibility for that particular unit. And then we have the sort of typical headquarters positions in marketing, legal, finance, et cetera, HR.

So we have an entire management team that on a day-to-day basis has the primary responsibility for running the business. I think, you know, I may make some additions to take care of some of the day-to-day operating decisions. You know, the small issues, but I want to be involved in much more of the strategic level decisions.

One of the things to understand is that throughout the organization at every point in time I have a succession plan for every, certainly all of my direct reports and, basically, every senior executive within the Company. And in this case it has always been the succession plan in North America that I would be the interim successor, and the reason is I'm here, I'm familiar with the market, and so forth and so on.

As I said, one of the opportunities I have in being involved in a six-month period is really understanding more about the business, and in any situation where you're working through someone else, you know, you're always limited on how much you can understand about a business. So I'd like to really focus on the business and really focus on, first, an evaluation of the talent that we have in the business. And my belief is that it is often the case there is someone in the business that is a natural successor, and they may be running a particular part of the business today and, therefore, they don't get the visibility with me or with the other senior management that would allow us to really effectively evaluate them. So that, that's the first order of business.

Matt Litfin - ***William Blair and Co. - Analyst***

Great. Thank you very much.

Jon Chait - ***Hudson Highland Group, Inc. - Chairman and CEO***

Okay, Matt.

Operator

Your next question comes from the line of Mark Marcon of Robert W. Baird.

Mark Marcon - ***Robert W. Baird - Analyst***

Good morning. This is a follow-up to that, Jon. Is it your sense that Europe and Asia-Pac are progressing at a sufficient pace that you feel comfortable with pulling back a little bit in terms of your involvement there?

Jon Chait - ***Hudson Highland Group, Inc. - Chairman and CEO***

Well, let me put it this way, yes, I think that we have a good management team in both places. One of the things I've--I have worked hard at is building teams of managers so that we are not dependent on single personalities in any jurisdiction. I think in both cases we have strong teams of managers. So I feel, you know, like we have a good team in place and, as I said, we're not dependent on a single personality.

But as we had looked at North America, we have a good team in place. You know, we've worked on the team, we've made some changes in the last year. I think I told you last quarter I feel, I've been involved in those changes. You know, certainly, I've approved them and have responsibility for them. And I feel that we have a good team in North America, as well.

But we're running, you know, in every one of our regions, we're running pretty, pretty reasonably sized businesses. They're not gigantic on the scale of, you know, the largest companies in our industry, but these are pretty big businesses, you know, $300, $400 million businesses. And, as a result, they're not, you know, one-person, ma-and-pa type operations. And one of my areas of attention since I've been in the Company is building up the entire teams. And that's what I think, you know, enables a company to be successful, regardless of what happens to one particular person.

Mark Marcon - ***Robert W. Baird - Analyst***

How many people will be reporting to you out of Europe and out of Asia-Pac?

Jon Chait - ***Hudson Highland Group, Inc. - Chairman and CEO***

Right now, I have a total of eight direct reports. So I have one person that reports to me in Asia-Pac; Don Bielinski is my direct report. Don is the Chairman of Asia-Pac. In Europe Christine Raynaud is my direct report, and she's the President of Europe, I think that's her title. So at this point I

have eight direct reports and obviously on a temporary basis I will have quite a few more direct reports through the North American operation. But I think this is a very, you know, this is a very important market for our Company.

When I came to the Company, you know, I laid it on the line and said that for us to be successful as a company, we have to be successful in North America, we have to build the North American business. You know, we've watched profitability this year in North America has dropped from $16 million to a loss of $1 million. And this is a market, you know, revenue growth is flat to down. You know, this is a market where we have to be successful, and I don't know how I can say it any more clearly, as Chief Executive that's my responsibility.

Mark Marcon - ***Robert W. Baird - Analyst***

Completely understood and agree. What--in terms of the, just quickly on Europe, before shifting back to North America, in Europe you obviously had a tremendous quarter in terms of your adjusted EBITDA hitting about 7.4%. Was there anything unusual in this quarter that led to such strong profitability or is--or should we think of that as a sustainable level that we can build upon?

Jon Chait - ***Hudson Highland Group, Inc. - Chairman and CEO***

Well, certainly, there's a seasonal issue in Europe, as there is throughout--

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Mark Marcon - ***Robert W. Baird - Analyst***

Sure.

Jon Chait - ***Hudson Highland Group, Inc. - Chairman and CEO***

Throughout any geography. So fourth quarter is a good quarter, you know, second quarter is a good quarter, first and third quarters are much smaller quarters and, therefore, their results will never look as strong as they do in second and fourth.

But I'll turn it over to Mary Jane to just answer the question in terms of looking at ongoing earnings, and anything that would cause you to think that it's not sustainable and subject to the seasonal fluctuations.

Mary Jane Raymond - ***Hudson Highland Group, Inc. - EVP and CFO***

I would say that the results that were delivered by Europe are very much, particularly at the EBITDA level, very much a function of their ongoing operating performance. The seasonal fluctuations are real, and there's always also a really great push at the end of the year. But, generally speaking, the results of Europe were delivered through their own operations.

Mark Marcon - ***Robert W. Baird - Analyst***

So no onetime projects or anything like that, that had a positive influence that a year from now we're going to say, "Well, it was hard to--that was a tough compare because we had a big project."

Jon Chait - ***Hudson Highland Group, Inc. - Chairman and CEO***

No. Now, I know onetime things, like we had in Australia a couple of years ago, of benefits from moving or anything like that. I would say across the board the European operations--and looking at the individual countries, you know, have been improving their EBITDA; they've been improving the productivity; they've been improving the business model; improving the focus on the core businesses; and we're seeing the positive results of all those improvements. You know, that have been, you know, those are things that obviously take a lot of work over a long period of time And if you look at the revenue line, you know, we're still absorbing some pain as we make the shift from--make the shift towards, you know, high market professionals. We're still migrating ourselves out of lower market and lower margin contracts.

Mark Marcon - ***Robert W. Baird - Analyst***

Uh-huh.

Jon Chait - ***Hudson Highland Group, Inc. - Chairman and CEO***

But I think, you know, as you know, Mark, my focus since I came here has been on improving the profitability of our basic businesses. And, you know, certainly the organizations in Europe and in Asia-Pacific have done a very good job. We have the benefit in Europe, I think, also, although I would not say that we've seen a huge benefit in the quarter, we have the benefit of an improving economy, particularly in continental Europe. So, you know, I think that has been a help, as well.

Mark Marcon - ***Robert W. Baird - Analyst***

Great. And in terms of North America, how--how would you characterize the economy? And what do you think is the underlying issue behind, you know, if we take a look at the F&A practices, if we take a look at the IT practices? So the performance of Hudson relative to some of the peers in the space? And what can you do over the next six months to help change that?

Jon Chait - ***Hudson Highland Group, Inc. - Chairman and CEO***

I think we have not--I think our problem has been that we have not established the perception in the market, so in the minds of clients or candidates as Hudson, in either the accounting space or the IT space, as a unique value proposition. I think we need to work harder at establishing our brand, in particularly those two key areas. We've been much more successful in the legal area. But I think it's a--I think it all starts with basics, and the basic fundamental thing is that we need to establish our perception of our value proposition in the minds of candidates and clients.

Mark Marcon - ***Robert W. Baird - Analyst***

And how do you think you're going to do that?

Jon Chait - ***Hudson Highland Group, Inc. - Chairman and CEO***

I think that we need to simply sharpen our market focus; we need to sharpen our marketing focus, and we need to sharpen our sales focus and strategy. One of the distractions in the last year and not to--I'm not blaming it, but PeopleSoft has been a distraction. And we've talked about one impact, you and I have talked about this, as well--one impact of PeopleSoft was that the organization was confused about what results were and what key performance indicators were, and that sort of thing. And it really took the organization away from what should have been a natural maturation process of really building upon the sales strategy. You know, who are the customers? What are the skill sets that are in demand? You know, where do we find those? How do we attract them? You know, why would candidates with those skill sets come to us rather than Brand X? And those are very basic things in our industry. Every company deals with those, and we need to execute on those, as well.

Mark Marcon - ***Robert W. Baird - Analyst***

Okay. Great. Thank you.

Operator

Your next question comes from the line of Jeff Silber of BMO Capital Markets.

Jeff Silber - ***BMO Capital Markets - Analyst***

Thanks so much. My first question is regarding guidance. In the past you've been kind enough to give us a little bit more color in terms of some of the assumptions leading up to your top line and bottom line guidance, and I was wondering if we could get those, as well?

Mary Jane Raymond - ***Hudson Highland Group, Inc. - EVP and CFO***

Well, with respect to the top line, I think that we generally expect to see the trends that we have sort of coming through this year generally continuing without necessarily a huge up tick. As Jon mentioned, we think that delivering this Company as a more profitable company is really very much predicated on a focus on the core business. As a result of that, we expect to see a continuing balancing of shifting to higher margin business, getting out of lower margin business. Though quite a lot of that has been accomplished already, and, as a result, we have the revenue guidance that we do, which is basically a forward motion on what we saw kind of as we exited 2006.

With respect to the guidance on the first quarter EBITDA, there--you guys know this almost better than I do, there's a million caveats on the first quarter in this industry, mostly that it's a pretty small quarter. And I think what we are expecting is a return to more of a typical seasonal trend, certainly more normalized than we saw last year in the first quarter. While at the same time trying to make sure that we continue to take actions and reap the benefit of actions that move us on the ongoing improved EBITDA trajectory and, also, in first quarter proper, finalizing these last restructuring actions under the 2006 program.

Jeff Silber - ***BMO Capital Markets - Analyst***

All right. Maybe just drilling down a little bit by segment, and I'm specifically talking about the Americas segment, I know you had some tough comps in the fourth quarter with, you know, some Katrina related work, et cetera. Do you think that Hudson Americas will show year-over-year revenue growth in the first quarter, or is that underling your assumption?

Jon Chait - ***Hudson Highland Group, Inc. - Chairman and CEO***

I think we're--we're forecast--I mean I think our assumption about year-over-year revenue growth in North America is basically flat. And probably, Jeff, that's, you know, simply an--I don't know if I'd say it's an excess of caution but as we look at the year, you know, I suppose I'm probably the foremost advocate of this, which is from the 50,000 foot view is that, you know, we're focusing on shifting our mix of business, but now there's less shifting going on in North America. But in North America we have a mix of business and we--we, you know, we have to deal with that. But I would say right at the moment, given all the other factors going on in our business, including the management change in North America, our assumption is flat revenue.

Jeff Silber - ***BMO Capital Markets - Analyst***

Okay, that's fair. And actually that's a good segway to my next question. In terms of the different business lines, can you remind us roughly where you stand right now. In the 8-K you gave a lot of good detail, in terms of legal, energy, financial solutions, if we can just get a segment breakdown roughly where North America is, that would be helpful?

Jon Chait - ***Hudson Highland Group, Inc. - Chairman and CEO***

I don't remember off the top of my head whether we've released to the public of, you know, how big our various segments are, but probably the best thing to do, Jeff, would be to talk offline because we're--I'm handicapped because I just don't remember now how much of this detail we've previously released.

Jeff Silber - ***BMO Capital Markets - Analyst***

Okay, that's fair. I'll do that. Just a couple other modeling questions. Just for, to help us out in 2007, again, I know you're not giving annual guidance, but what should we be expecting for stock based compensation and appreciation and amortization?

Mary Jane Raymond - ***Hudson Highland Group, Inc. - EVP and CFO***

The stock option expense for the year, we expect to be about roughly $5 million. I probably--between the cost of restructured stock going on, stock options, and the ESPP.

Jeff Silber - ***BMO Capital Markets - Analyst***

And I'm sorry, D&A depreciation and amortization?

Mary Jane Raymond - ***Hudson Highland Group, Inc. - EVP and CFO***

Sorry. For D&A, I would expect our D&A to be roughly in the range of what we've seen, you know, in the past, kind of a continuation of that--hang on a second.

Jon Chait - ***Hudson Highland Group, Inc. - Chairman and CEO***

Is that 17 million?

Mary Jane Raymond - ***Hudson Highland Group, Inc. - EVP and CFO***

Yes, so I'd say somewhere between kind of $16, $17 million.

Jeff Silber - ***BMO Capital Markets - Analyst***

Okay. Great. That's helpful. Just a couple of other just small numbers questions. In terms of the China acquisition, I think you've mentioned it's relatively small. Again, if we can just get some kind of order of magnitude of what we're talking about?

Jon Chait - ***Hudson Highland Group, Inc. - Chairman and CEO***

I think we're talking about revenues of $3 million and, you know--

Mary Jane Raymond - ***Hudson Highland Group, Inc. - EVP and CFO***

I'd say EBITDA of roughly about kind of $800,000 or so.

Jeff Silber - ***BMO Capital Markets - Analyst***

Okay. Great. And then the same question for the UK divestiture, that you just did this quarter?

Mary Jane Raymond - ***Hudson Highland Group, Inc. - EVP and CFO***

So, which is the office support business. The revenue on that is roughly about $9.5 million, and the EBITDA for that is roughly about $900,000.

Jon Chait - ***Hudson Highland Group, Inc. - Chairman and CEO***

On an annual basis.

Mary Jane Raymond - ***Hudson Highland Group, Inc. - EVP and CFO***

On an annual basis.

Jeff Silber - ***BMO Capital Markets - Analyst***

On an annual basis, right. And, again, the first quarter guidance assumes that divestiture has occurred?

Mary Jane Raymond - ***Hudson Highland Group, Inc. - EVP and CFO***

Oh, absolutely, because we closed it on January 13th.

Jeff Silber - ***BMO Capital Markets - Analyst***

Great. Just wanted to double-check that. All right. Thanks so much.

Jon Chait - ***Hudson Highland Group, Inc. - Chairman and CEO***

You're welcome.

Operator

Your next question comes from the line of Mike Carney of Aperion.

Mike Carney - ***Aperion - Analyst***

Good morning.

Jon Chait - ***Hudson Highland Group, Inc. - Chairman and CEO***

Hi, Mike.

Mike Carney - ***Aperion - Analyst***

I have a few questions. I'll just try to run through them fast. First of all, Mary Jane, you had--it looks like you've cut a lot of the corporate expenses, maybe $15 or $20 million at this run rate, but I think in the last 18 months, but you said that the run rate would be--I think you had mentioned something, you expected the run rate around previous levels?

Mary Jane Raymond - ***Hudson Highland Group, Inc. - EVP and CFO***

No, sorry, Mike. So the corporate expense last year was about $37 million. The corporate expense that we reported this year is around about $28. What I was saying was Q4 was only $5.5 million, so that's a little--

Jon Chait - ***Hudson Highland Group, Inc. - Chairman and CEO***

Right.

Mary Jane Raymond - ***Hudson Highland Group, Inc. - EVP and CFO***

--abnormally low. What I expect the run rate to be is the rate of Q2 and Q3 of 2006, which is in round numbers $7 million a quarter.

Mike Carney - ***Aperion - Analyst***

Okay. And what was the difference in Q4, what was the adjustment there?

Mary Jane Raymond - ***Hudson Highland Group, Inc. - EVP and CFO***

Well, if you look at the results that we delivered for this year, these results are below the expectation that we had as a company and they're below the targets that we set for the senior management bonuses and the bonuses across the corporate organization in general. While certainly we were adjusting that bonus accrual through the year, we took the final adjustments to that in the fourth quarter.

Mike Carney - ***Aperion - Analyst***

Right. Okay. So that--because the bonuses aren't that big on an annualized basis, but those are adjusted, are accrued in the fourth quarter? I mean the difference, $1.5 million, basically? Because normally the bonuses wouldn't be $6 million.

Mary Jane Raymond - ***Hudson Highland Group, Inc. - EVP and CFO***

So just to make sure I'm following you, normally the bonuses for the corporate team is somewhere around $5 million, and we took the final adjustment of that, again, we adjusted it through some of the quarter so roughly I'd say about $1.5 million in the fourth quarter, down, but they actually were taken down to zero. Is that--

Mike Carney - ***Aperion - Analyst***

Okay.

Mary Jane Raymond - ***Hudson Highland Group, Inc. - EVP and CFO***

Are we straight on that?

Mike Carney - ***Aperion - Analyst***

Yes.

Mary Jane Raymond - ***Hudson Highland Group, Inc. - EVP and CFO***

Okay.

Mike Carney - ***Aperion - Analyst***

And then D&A, wouldn't that be a little bit lower because you, you know, the last--you had all this true up and D&A, or?

Mary Jane Raymond - ***Hudson Highland Group, Inc. - EVP and CFO***

What we wrote off for this year?

Mike Carney - ***Aperion - Analyst***

Yes, the write-off?

Mary Jane Raymond - ***Hudson Highland Group, Inc. - EVP and CFO***

That's, I mean that's a good question, but actually not really, because the 2.3--or sorry, 2.8 that we wrote off for the New York property is a leasehold improvement so that's one of those deals that has a really long life, like eight years, the remaining life of that lease. So the reduction coming out annually of that is not oh, so gigantic. And then, as I mentioned, I'm expecting to see the capital expenditures for the year go up a bit, you know, as much as $5 million against what we invested in 2006. So that's how I get to--on balance I think, frankly, the D&A will be roughly the same run rate.

Mike Carney - ***Aperion - Analyst***

Okay. Got it. And then on Alder Novo, does that assume that you don't have really a talent management business in the U.S. now?

Mary Jane Raymond - ***Hudson Highland Group, Inc. - EVP and CFO***

No, it does not assume that. The talent management business--I might have Jon give a few comments on this, but sort of to do the math with you, you know, typically in the U.S. markets has consisted of in the past several different areas. One is actually the main talent management business which is really assessments in organizational design, a type of professional services activity that is very, very important for us part and parcel to perm. The Alder Novo business was precisely focused in the area of executive coaching, and then previously we also had the Center For High Performance, a small team that would actually go in and help an organization, you know, sort of diagnose its various organizational issues. We closed the Center for High Performance in the third quarter, and we have, as we say, written off the Alder Novo business. But the more important part--or, excuse me, they're all important and all of these people did a very good job, but the part that I think is the closest aligned with the core business is the assessment of people coming in which can be a good addition in a perm offering, continues in the North American market and in the other markets.

And I'll just see if Jon wants to add to that?

Jon Chait - ***Hudson Highland Group, Inc. - Chairman and CEO***

No, I think that's a very complete explanation. Let me just take it on a philosophical level, Mike. You know, we've--I think we've been pretty successful on acquisitions. And having said that, you know, we've made it very clear that we make acquisitions but they're, you know, we don't view it as something fundamental to the growth of our company. But I think if you look back, the Balance acquisition, the JMT acquisition, we had another small financial solutions acquisition in Cleveland, have been very successful.

Just philosophically our view about this is we make acquisitions, we obviously hope we make good acquisitions, but at any given point in time if we have to reevaluate, we reevaluate pretty quickly, and, you know, change tact. So we don't, you know, we don't hang on to things that might be perfectly good things but just don't work within our Company. They don't work because we misjudged the culture or the market changed or, you know, we weren't sharp enough about our strategy even in the beginning.

You know, I was a major initiator of the Center For High Performance, which was a high-end consulting type business with a very experienced team, very energetic, committed people. But, you know, notwithstanding our best efforts after a couple of years it was clear it just didn't fit within our culture and within our organization, so we negotiated with the team and ended up exiting.

So I think, you know, that's just the way we do things. And I think everybody has some things that don't work out, and some of this was that we've changed--one piece of this is, you know, we've changed our strategy in the sense that we've really looked ourselves in the eye and said, "We need to be a lot more focused on our core business and the things that are directly related to the core business." And, as Mary Jane very well put, you know, assessment is fundamental to permanent recruitment, and we have a big assessment business around the world. So we've really redoubled our focus in that area and deemphasized our focus in the coaching area.

Mike Carney - ***Aperion - Analyst***

Okay. Got it. And then, also, on acquisitions, Jon, on Tony Keith, you've mentioned several times serving U.S. multinationals. Is--I know that's the easiest--is there any other reasons or better, are there any businesses to acquire in Asia to serve the Asian companies at this point?

Jon Chait - ***Hudson Highland Group, Inc. - Chairman and CEO***

There are some. If you're specifically talking about China, the--and I've--it's a good question, Mike, and it's a question that I've asked, as well, which shows you it's a really good question. But the information I've gotten back is that the companies that are specializing, kind of Chinese companies specializing in Chinese domestic market, the margins are very, very low. And most of them specialize in bulk recruitment at the nonprofessional level, so we have looked pretty carefully at China.

The reason is, you know, we have a good management team in China, we have a good management team in Asia, we have the infrastructure, you know, we have a large business that is, you know, depending on who wants to count and how you count it, you know, number one or number two in China. China is obviously a very fast-growing market that everybody in the world is thinking about.

So, you know, we are pretty much on the constant lookout for good, sensible acquisitions at good, sensible prices in China. And, you know, it mean it's a good team of people that are going to fit in with an American public company with quarterly reporting and Sarbanes-Oxley and, as well, have a good business. And we just haven't really, you know, we haven't found anything, we haven't seen any.

Mike Carney - ***Aperion - Analyst***

Okay. Understood. What was the purchase price, the initial on Tony Keith?

Jon Chait - ***Hudson Highland Group, Inc. - Chairman and CEO***

Around $1 million.

Mike Carney - ***Aperion - Analyst***

Okay. And, also, further on acquisitions, now that you have some cash, what is the likelihood that you would, you know, make a bigger acquisition so that you actually are going to have to use some leverage?

Jon Chait - ***Hudson Highland Group, Inc. - Chairman and CEO***

You know, we always--it goes back to kind of the same thing. We constantly look at acquisitions and we constantly, you know, look for things that are going to help us build our business faster. And, again, I think acquisitions like JMT and Balance were--have really been great acquisitions for the Company. A great group of people, done very well since the acquisition.

The biggest gating item for us is the cultural fit. And, actually, the second gating item is probably the price because we don't pay big multiples and, you know, right now in today's market everybody thinks they're going to get ten times earnings. So we, you know, I think that's the big gating item. But we continually look. I also have a bias against kind of really big acquisitions, so I would say, you know, I don't know if our limit is balanced but it's more in that realm than a really big one.

Mike Carney - ***Aperion - Analyst***

Okay.

Mary Jane Raymond - ***Hudson Highland Group, Inc. - EVP and CFO***

Mike, let me just correct one bad hand signal I gave Jon here. Just to talk about the financials on the China acquisition, the initial payment is $1 million. There's an additional up front payment of about $4 million that's actually contingent upon getting two licenses to operate in key cities, one of which we already have. One license we already have.

Mike Carney - ***Aperion - Analyst***

Okay.

Mary Jane Raymond - ***Hudson Highland Group, Inc. - EVP and CFO***

So just--that's probably the kind of extent of our disclosure on the terms, but conceptually all end with the receipt of a license; it's $5 million.

Mike Carney - ***Aperion - Analyst***

Okay, plus earn out?

Mary Jane Raymond - ***Hudson Highland Group, Inc. - EVP and CFO***

Plus the earn out, right.

Mike Carney - ***Aperion - Analyst***

Okay. And then, Jon, on the financial, obviously, finance and accounting has been down, and staffing in the industry, but you're down quite a bit there. Is that not related to JMT and then Professional Solutions?

Jon Chait - ***Hudson Highland Group, Inc. - Chairman and CEO***

Correct.

Mike Carney - ***Aperion - Analyst***

Okay, that was the legacy business?

Jon Chait - ***Hudson Highland Group, Inc. - Chairman and CEO***

You know, I--let me say, I have not looked at the detailed numbers, but the last time I did look JMT and Professional Solutions have continued to do extremely well, and our challenge has been in the--as you put it, the legacy side of the business. And I don't know, you know, for the quarter, I just haven't looked at the detail to see exactly where the shortfall was, but I'm pretty sure those two have continued to really plow ahead and do very well for us.

I think the--you know, and the other thing just mathematically is that we have, you know, we have a nice business in Financial Solutions and, again, I think we have a business that's well positioned to do better. But it is a smallish business, so that we're a little bit subject to the tyranny of small numbers, to quote one of my colleagues. And so a small shortfall, you know, might be ten contractors, ends up being a huge percentage in our business. So not to say that, you know, the reverse is true, too. Ten positive would be a big percentage, so we need to do more work there without a doubt, but it's not--I don't think it's, you know, in a sense it's not as bad as the numbers look.

Mike Carney - ***Aperion - Analyst***

Okay. Mary Jane, do you have the recruitment, or perm growth, in Europe and Asia-Pacific in the quarter?

Mary Jane Raymond - ***Hudson Highland Group, Inc. - EVP and CFO***

Do I have that--yes. So--

Mike Carney - ***Aperion - Analyst***

I'm assuming temp--it sounds like temp is down, but perm is up quite a bit? For both those regions?

Mary Jane Raymond - ***Hudson Highland Group, Inc. - EVP and CFO***

So for Europe the temp growth year-on-year for the fourth quarter was down about 5% and the perm growth was up about 20%.

Mike Carney - ***Aperion - Analyst***

Okay.

Mary Jane Raymond - ***Hudson Highland Group, Inc. - EVP and CFO***

Is there a second part to your question?

Mike Carney - ***Aperion - Analyst***

And in Asia-Pacific?

Mary Jane Raymond - ***Hudson Highland Group, Inc. - EVP and CFO***

In Asia, okay. I'm getting good at these rapid fire questions here. In Asia the temporary contracting is actually up, and this is all Asia-Pac, ANZ and Asia, temporary contracting is actually up 3%, and the perm is up 16%.

Mike Carney - ***Aperion - Analyst***

Okay. One more question. On the guidance it seems like, I mean you've been kind of year-over-year kind of doubling and tripling your EBITDA, and then you come out with this first quarter guidance and it's, you know, only a little bit better than you did back in '05. Is the trends declining a little bit, are you just being conservative, or is it, you know, is it somewhat I guess because that corporate expense is going to go up a little bit or, you know, how much level of bonuses are you including? And basically just kind of any other comment you have on that?

Mary Jane Raymond - ***Hudson Highland Group, Inc. - EVP and CFO***

Okay. Well, first of all, I think as a concept the fact that the first quarter guidance for '07 is not all that dramatically different, as you say, from '05, this is the color I would provide and, you know, don't run away with this or I'll have to kidnap the favorite toys of your children. But conceptually this is a small quarter. It's a small quarter in every region of the world. In the Asia-Pacific market it's impacted by the fact that it's the summer, as well. So I would say, particularly as Jon said, with the change in the leadership we are being cautious about the guidance on this quarter. I would not say we have de-risked it by orders of magnitude just to be a bit ridiculous about it, but I would say that we think it is important given the challenges we faced last first quarter in North America to get them back on an even keel, of a more normalized first quarter. And, as a result of that, I'd say and I think you'd sort of expect, it would be--this wouldn't be the quarter for us to be overly aggressive and so we're not being so.

Mike Carney - ***Aperion - Analyst***

Okay. Great.

Jon Chait - ***Hudson Highland Group, Inc. - Chairman and CEO***

Mike, I'm going to have to thank you very much, and just give somebody else a chance to have one more question.

Operator

Your final question comes from the line of Gabriel Loenberg of Falco Capital.

Gabriel Loenberg - ***Falco Capital - Analyst***

Thank you very much. I have four quick questions, and just, some of them are clarification questions. The adjusted EBITDA that you include on the income statement and you include in the supplemental information for the income statement, do you include the stock based comp in that, or not? Or where is the stock based comp included?

Mary Jane Raymond - ***Hudson Highland Group, Inc. - EVP and CFO***

It's--the adjusted EBITDA includes the stock based compensation because that's recorded in the compensation area.

Gabriel Loenberg - ***Falco Capital - Analyst***

So--

Jon Chait - ***Hudson Highland Group, Inc. - Chairman and CEO***

It's the regular--

Mary Jane Raymond - ***Hudson Highland Group, Inc. - EVP and CFO***

It's a regular expense.

Jon Chait - ***Hudson Highland Group, Inc. - Chairman and CEO***

Regular SG&A charge.

Gabriel Loenberg - ***Falco Capital - Analyst***

So the stock based comp is included in SG&A and the adjusted EBITDA is off the--this stock based comp?

Mary Jane Raymond - ***Hudson Highland Group, Inc. - EVP and CFO***

Yes.

Gabriel Loenberg - ***Falco Capital - Analyst***

Okay, so if we wanted to sort of think about the EBITDA on a cash basis we would think about adding back the stock based comp, is that correct?

Mary Jane Raymond - ***Hudson Highland Group, Inc. - EVP and CFO***

If that were the math you wanted to do, that's the math you could do.

Gabriel Loenberg - ***Falco Capital - Analyst***

The math we could do. Okay. Fine. The second question is I think Jon sort of talked about still migrating out of low margin contracts during the comments in the call. And I just wanted to clarify was that sort of the 10% of the business that you had sort of penciled out, that you still wanted to divest, or was it more than that?

Jon Chait - ***Hudson Highland Group, Inc. - Chairman and CEO***

It's more than that. It's--that's really built within many of our core markets, so, for example, our UK business has done a very good job, and our Australian business has, as well, exiting low margin contracts. And both of those are core businesses, but they've exited low margin contracts over the course of the last year and continue to evaluate carefully, you know, whether we want to participate in contracts that have lower margins.

Gabriel Loenberg - ***Falco Capital - Analyst***

So it's significantly greater than the 10% you sort of penciled?

Jon Chait - ***Hudson Highland Group, Inc. - Chairman and CEO***

Yes.

Gabriel Loenberg - ***Falco Capital - Analyst***

The next question is just the $1 million payment for the China acquisition, that's the initial payment, and just to clarify again, the other $4 million comes when they get the two licenses and they've got one of the licenses, and then there's an earn out on top of the $5 million in total?

Jon Chait - ***Hudson Highland Group, Inc. - Chairman and CEO***

Correct. That's correct. So I think the math that we've given you in pieces is about $3 million revenue, about $1 million profit, about $5 million purchase price, which is about five times the $1 million. And to basically get the earn out they have to make more money.

Gabriel Loenberg - ***Falco Capital - Analyst***

I understand. Thank you. And how quickly can that sort of leverage itself, or and sort of grow that platform? Or does it require acquisitions within the China, within the country to grow the platform? Or can it just do it internally?

Jon Chait - ***Hudson Highland Group, Inc. - Chairman and CEO***

You know, I think it can do it internally. This, you know, we don't want to blow this out of proportion because it's still a small part of our business, but there's--there is not much overlap in our respective customer bases. So we have customers that basically are all names that you would recognize, you know, they're European and developed world names that everybody would love to do business with. And we have those customers that we're servicing, and the general management area, they have a whole different range of businesses because their business is much more focused on technology companies in the IT area. So there's a great opportunity for us to leverage the respective customer bases.

Now, having said that, that's how chief executives talk. On the ground my colleagues have to execute and have to make the sales calls and make it--make it work. And that's a--you know, you've heard that before from many companies, that's a challenge. But I think it's a good opportunity for us, so we, you know, I don't think we need to make more acquisitions. As I say, the balance is we're always sniffing around because we think this is a critical market in the world, which no surprise, so does everybody else. But we don't think we have to make acquisitions.

Gabriel Loenberg - ***Falco Capital - Analyst***

Thank you. Two more questions, and then that's it. The--just if you could remind us, this cyclical nature of the industry and when you guys do best, is it when unemployment is sort of at a--at a low and basically it's hard for companies to find job--hard for companies to find the people to fill their positions and so they need you or your industry to help fill those positions, is that correct?

Jon Chait - ***Hudson Highland Group, Inc. - Chairman and CEO***

That's basically it. I mean that's a little bit simplistic but that's--you know, from a 50,000 foot basis that's basically it. The more--slightly more sophisticated slant on that is that it's really about skills, and so you can have high unemployment, even within a--let's say, a medium economy you can have a skill shortage.

So in the last two years there's been a dramatic skill shortage in any kind of accounting personnel in North America. And so that's fueled a big demand for accounting personnel in North America. Even beyond what you would think of looking at the North American economy.

But I would say your basic premise is right, which is in a situation where unemployment is very high it is seldom the case that business is very good. You know, it's seldom the case that there are dramatic skill shortages, and it's amazing what people, you know, high unemployment usually means a weak economy, and then it's amazing what people find they can do without.

Gabriel Loenberg - ***Falco Capital - Analyst***

Yes, exactly, that's--I like to keep things simple, I find that they work. So basically in this kind of employment environment if it holds steady at this level I think the unemployment rate is 4.6 in the U.S., it should really be your sweet spot for the next year?

Jon Chait - ***Hudson Highland Group, Inc. - Chairman and CEO***

Yes. I mean, you know, the Goldilocks economy, if that's what you want to call it, is meaning moderate economic growth, low inflation, I mean inflation actually doesn't have a big impact on us, although that gets us worried about the future. But, you know, moderate economic growth is great for our industry and great for our Company because it creates demand, so to speak. You know, people grow, they need more people, and they come to us. They're making more money, they feel like they can pay fees to find people. You know, high economic growth actually isn't necessarily twice as good, because then the skill shortages become so rampant that you can't fill the orders.

Gabriel Loenberg - ***Falco Capital - Analyst***

Understand, I understand.

Jon Chait - ***Hudson Highland Group, Inc. - Chairman and CEO***

So right now things are pretty good at the moment I think in this industry.

Gabriel Loenberg - ***Falco Capital - Analyst***

Now, my last question, and that's my fifth question which is you guys, I think, talked about--I don't know where it was, but I read it--talked about a long-term goal of 5 or 7 to 10% on the EBITDA line, a press release or someplace else I read it.

Jon Chait - ***Hudson Highland Group, Inc. - Chairman and CEO***

That has been our long-term goal, that is our long-term goal.

Gabriel Loenberg - ***Falco Capital - Analyst***

Now, in 1988, when I--I think '88 or '89, when you guys were part of the Monster and the spin-off document, you guys had those kinds of margins, but what I wanted to ask was how big was the Highland Partners' segment of that business back then versus, obviously now it won't be [inaudible]?

Jon Chait - ***Hudson Highland Group, Inc. - Chairman and CEO***

Well, first of all, I think you meant 1998.

Gabriel Loenberg - ***Falco Capital - Analyst***

Sorry.

Jon Chait - ***Hudson Highland Group, Inc. - Chairman and CEO***

Yes. Highland Partners was pretty big in the old days, you know, and I don't recall the math right off the top of my head, but I would say the other components of our business were very, very profitable, and we're working hard to get back to those levels of profitability. But I think, you know, obviously we're at--we're less than 3% and so 7 to 10% looks like it's a long way off at the moment.

But, you know, I think this business model with a--essentially on a consolidated basis a 55% perm component is a, you know, potentially a very valuable and very profitable business model. And we were, like the entire industry, you know, we--the effects of this--the recession in 2000, you know, and going from a big peak down to a valley is something that's been lingering throughout the industry, not just with us but through many companies. We have our own challenges, and we need to do better than we've been doing.

Gabriel Loenberg - ***Falco Capital - Analyst***

I thought--

Jon Chait - ***Hudson Highland Group, Inc. - Chairman and CEO***

With that, I'm going to have to say thank you very much. You know, please do give us a call offline, because we've run out of our allotted time.

Gabriel Loenberg - ***Falco Capital - Analyst***

Thank you very much.

Jon Chait - ***Hudson Highland Group, Inc. - Chairman and CEO***

Thank you. Then I would just want to close, and I'm going to turn it over to David for our official closing remarks. I want to just make my own closing summary.

Obviously, in this quarter we've made a very significant management change, that we announced yesterday, with Tom Moran's resignation. And one of the things I would just like to remind all of you is that at every point in time I continuously evaluate our management team and I continuously make the decision of building the right team to be successful in the future. I have a philosophy of not being dependent on any one individual, and so building a team around people, and I focus a lot of my attention on the teams and not just--not just the people at the top of the teams but on the teams, themselves.

As we look at our business, I am very conscious of the fact that we've made a lot of progress in our business. We took a business that was losing, I think we'd say $60 million a year on an operating basis, and last year we had EBITDA of $31 million. But I'm also conscious that while we've

made progress, we have quite a ways to go. We're at below--we're at a level of less than 3% EBITDA and our goal is 7 to 10%, and we've been working at this for some time.

One of the things I have to evaluate at all times is whether I have the team to go forward, and to go forward and take this Company to success, to the level of success that I believe it can achieve. That's something that I constantly evaluate every day in my job, and I will assure you that I will continue to make decisions that will drive the Company to the levels of operating performance which I believe it can achieve.

With that, I'll turn it over to David for our closing remarks.

David Kirby - ***Hudson Highland Group, Inc. - Director of Investor Relations***

Thank you, Jon. Excuse me. I'll give you one updated data point. Mike Carney, you asked about revenue growth in the fourth quarter, and I'll just give the constant currency growth rates. Gross margin in Asia-Pac in temp was down 3% in constant currency, and perm was up approximately 15%. In Europe temp gross margin was also down approximately 3%, the perm gross margin there up 10%, all constant currency data.

With that, let me thank you all for joining the Hudson Highland Group fourth quarter conference call. If you do have any further questions, please feel free to contact Mary Jane Raymond or me at any time. You can reach Mary Jane at 212-351-7232. You can reach me at 212-351-7216.

Our call today has been recorded and will be available later today by calling 800-642-1687, followed by the pass code, 6067406. For calls outside the U.S., please dial 1-706-645-9291, followed by the same pass code. The archived call will remain available for the next seven days at those numbers. Our call today has been webcast, as well, and will be available on the Investor Section of our website, hudson.com. Thank you very much.

Operator

Thank you for participating in today's conference. You may now disconnect.