

HEIDRICK & STRUGGLES INTERNATIONAL INC
Form 10-Q
October 26, 2016

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT
OF 1934

FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 2016

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT
OF 1934

For the transition period from _____ to _____

Commission File Number 0-25837

HEIDRICK & STRUGGLES INTERNATIONAL, INC.
(Exact Name of Registrant as Specified in its Charter)

Delaware 36-2681268
(State or Other Jurisdiction of (I.R.S. Employer
Incorporation or Organization) Identification Number)
233 South Wacker Drive-Suite 4900
Chicago, Illinois
60606-6303
(Address of Principal Executive Offices)

(312) 496-1200
(Registrant's Telephone Number, Including Area Code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period of time that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a small reporting company. See definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer
Non-Accelerated filer (Do not check if a smaller reporting company) Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

As of October 21, 2016, there were 18,582,574 shares of the Company's common stock outstanding.

HEIDRICK & STRUGGLES INTERNATIONAL, INC. AND SUBSIDIARIES
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PART I. FINANCIAL INFORMATION

ITEM 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
HEIDRICK & STRUGGLES INTERNATIONAL, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS

(In thousands, except share amounts)

| | September 30, 2016 (Unaudited) | December 31, 2015 |
|---|---|-------------------------|
| Current assets: | | |
| Cash and cash equivalents | \$99,975 | \$190,452 |
| Accounts receivable, net | 114,726 | 76,058 |
| Prepaid expenses | 23,936 | 19,197 |
| Other current assets | 14,867 | 18,447 |
| Income taxes recoverable | 5,451 | 4,809 |
| Total current assets | 258,955 | 308,963 |
| Non-current assets: | | |
| Property and equipment, net | 36,137 | 36,498 |
| Assets designated for retirement and pension plans | 17,438 | 16,857 |
| Investments | 17,268 | 14,145 |
| Other non-current assets | 11,233 | 11,115 |
| Goodwill | 155,313 | 131,122 |
| Other intangible assets, net | 20,154 | 18,687 |
| Deferred income taxes | 37,277 | 35,331 |
| Total non-current assets | 294,820 | 263,755 |
| Total assets | \$553,775 | \$572,718 |
| Current liabilities: | | |
| Accounts payable | \$9,644 | \$6,150 |
| Accrued salaries and employee benefits | 120,102 | 158,875 |
| Deferred revenue, net | 31,713 | 29,724 |
| Other current liabilities | 25,103 | 31,239 |
| Income taxes payable | 3,897 | 3,442 |
| Total current liabilities | 190,459 | 229,430 |
| Non-current liabilities: | | |
| Accrued salaries and employee benefits | 30,363 | 32,690 |
| Retirement and pension plans | 39,921 | 35,949 |
| Other non-current liabilities | 27,267 | 19,847 |
| Total non-current liabilities | 97,551 | 88,486 |
| Total liabilities | 288,010 | 317,916 |
| Commitments and contingencies (Note 16) | | |
| Stockholders' equity: | | |
| Preferred stock, \$0.01 par value, 10,000,000 shares authorized, no shares issued at September 30, 2016 and December 31, 2015 | — | — |
| Common stock, \$0.01 par value, 100,000,000 shares authorized, 19,585,777 shares issued, 18,578,176 and 18,379,398 shares outstanding at September 30, 2016 and December 31, 2015, respectively | 196 | 196 |
| Treasury stock at cost, 1,007,601 and 1,206,379 shares at September 30, 2016 and December 31, 2015, respectively | (32,915) | (39,583) |

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| | | |
|--|-----------|-----------|
| Additional paid in capital | 229,318 | 232,358 |
| Retained earnings | 60,050 | 52,572 |
| Accumulated other comprehensive income | 9,116 | 9,259 |
| Total stockholders' equity | 265,765 | 254,802 |
| Total liabilities and stockholders' equity | \$553,775 | \$572,718 |

The accompanying Notes to Condensed Consolidated Financial Statements are an integral part of these statements.

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HEIDRICK & STRUGGLES INTERNATIONAL, INC. AND SUBSIDIARIES
 CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(In thousands, except per share amounts)

(Unaudited)

| | Three Months Ended | | Nine Months Ended | |
|--|--------------------|-----------|-------------------|-----------|
| | September 30, | | September 30, | |
| | 2016 | 2015 | 2016 | 2015 |
| Revenue: | | | | |
| Revenue before reimbursements (net revenue) | \$143,519 | \$138,421 | \$422,569 | \$386,619 |
| Reimbursements | 4,720 | 4,429 | 13,773 | 12,396 |
| Total revenue | 148,239 | 142,850 | 436,342 | 399,015 |
| Operating expenses: | | | | |
| Salaries and employee benefits | 95,355 | 95,724 | 288,015 | 264,914 |
| General and administrative expenses | 36,158 | 29,764 | 106,986 | 92,928 |
| Reimbursed expenses | 4,720 | 4,429 | 13,773 | 12,396 |
| Total operating expenses | 136,233 | 129,917 | 408,774 | 370,238 |
| Operating income | 12,006 | 12,933 | 27,568 | 28,777 |
| Non-operating income (expense): | | | | |
| Interest, net | 42 | (54) | 172 | (300) |
| Other, net | 340 | (1,742) | 418 | (1,696) |
| Net non-operating income (expense) | 382 | (1,796) | 590 | (1,996) |
| Income before income taxes | 12,388 | 11,137 | 28,158 | 26,781 |
| Provision for income taxes | 5,448 | 3,647 | 13,238 | 10,909 |
| Net income | 6,940 | 7,490 | 14,920 | 15,872 |
| Other comprehensive (loss) income, net of tax: | | | | |
| Foreign currency translation adjustment | (717) | (347) | (1,173) | (1,645) |
| Net unrealized gain (loss) on available-for-sale investments | 519 | (941) | 1,030 | (802) |
| Unrealized loss on cash flow hedge | — | — | — | (78) |
| Other comprehensive loss, net of tax | (198) | (1,288) | (143) | (2,525) |
| Comprehensive income | \$6,742 | \$6,202 | \$14,777 | \$13,347 |
| Basic weighted average common shares outstanding | 18,577 | 18,372 | 18,528 | 18,318 |
| Dilutive common shares | 273 | 277 | 273 | 277 |
| Diluted weighted average common shares outstanding | 18,850 | 18,649 | 18,801 | 18,595 |
| Basic net income per common share | \$0.37 | \$0.41 | \$0.81 | \$0.87 |
| Diluted net income per common share | \$0.37 | \$0.40 | \$0.79 | \$0.85 |
| Cash dividends paid per share | \$0.13 | \$0.13 | \$0.39 | \$0.39 |

The accompanying Notes to Condensed Consolidated Financial Statements are an integral part of these statements.

HEIDRICK & STRUGGLES INTERNATIONAL, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY
(In thousands)
(Unaudited)

| | Common Stock | | Treasury Stock | | Additional Paid in Capital | Retained Earnings | Accumulated | Total |
|---|--------------|--------|----------------|------------|----------------------------------|----------------------|---------------------------------------|-----------|
| | Shares | Amount | Shares | Amount | | | Other Compre- hensive Income | |
| Balance at December 31, 2015 | 19,586 | \$ 196 | 1,206 | \$(39,583) | \$232,358 | \$52,572 | \$ 9,259 | \$254,802 |
| Net income | — | — | — | — | — | 14,920 | — | 14,920 |
| Other comprehensive loss, net of tax | — | — | — | — | — | — | (143) | (143) |
| Treasury and common stock transactions: | | | | | | | | |
| Stock-based compensation | — | — | — | — | 5,055 | — | — | 5,055 |
| Vesting of equity, net of tax withholdings | — | — | (167) | 5,636 | (8,324) | — | — | (2,688) |
| Re-issuance of treasury stock | — | — | (31) | 1,032 | (470) | — | — | 562 |
| Cash dividends declared (\$0.39 per share) | — | — | — | — | — | (7,252) | — | (7,252) |
| Dividend equivalents on restricted stock units | — | — | — | — | — | (190) | — | (190) |
| Tax surplus related to stock-based compensation | — | — | — | — | 699 | — | — | 699 |
| Balance at September 30, 2016 | 19,586 | \$ 196 | 1,008 | \$(32,915) | \$229,318 | \$60,050 | \$ 9,116 | \$265,765 |

The accompanying Notes to Condensed Consolidated Financial Statements are an integral part of these statements.

HEIDRICK & STRUGGLES INTERNATIONAL, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

(Unaudited)

| | Nine Months Ended September 30, | |
|---|------------------------------------|-------------|
| | 2016 | 2015 |
| Cash flows—operating activities: | | |
| Net income | \$ 14,920 | \$ 15,872 |
| Adjustments to reconcile net income to net cash used in operating activities: | | |
| Depreciation and amortization | 11,676 | 9,983 |
| Deferred income taxes | (1,731) | (153) |
| Stock-based compensation expense | 5,055 | 3,684 |
| Accretion expense related to earnout payments | 198 | 861 |
| Changes in assets and liabilities, net of effects of acquisitions: | | |
| Accounts receivable | (33,267) | (40,582) |
| Accounts payable | 2,270 | (1,311) |
| Accrued expenses | (47,130) | (5,361) |
| Deferred revenue | 1,298 | 3,921 |
| Income taxes payable, net | (76) | (3,101) |
| Retirement and pension plan assets and liabilities | 3,009 | 69 |
| Prepaid expenses | (4,228) | (1,054) |
| Other assets and liabilities, net | (1,008) | (2,868) |
| Net cash used in operating activities | (49,014) | (20,040) |
| Cash flows—investing activities: | | |
| Restricted cash | 7,228 | — |
| Acquisition of businesses | (27,722) | — |
| Capital expenditures | (2,179) | (13,897) |
| Purchases of available for sale investments | (2,361) | (1,402) |
| Proceeds from sales of available for sale investments | 510 | 630 |
| Net cash used in investing activities | (24,524) | (14,669) |
| Cash flows—financing activities: | | |
| Debt repayment | — | (29,500) |
| Debt issuance costs | — | (422) |
| Cash dividends paid | (7,442) | (7,496) |
| Payment of employee tax withholdings on equity transactions | (2,676) | (878) |
| Acquisition earnout payments | (7,461) | (5,496) |
| Net cash used in financing activities | (17,579) | (43,792) |
| Effect of exchange rates fluctuations on cash and cash equivalents | 640 | (3,891) |
| Net decrease in cash and cash equivalents | (90,477) | (82,392) |
| Cash and cash equivalents at beginning of period | 190,452 | 211,352 |
| Cash and cash equivalents at end of period | \$ 99,975 | \$ 128,960 |
| Supplemental Schedule of Non-Cash Activities: | | |
| Term loan facility retirement | \$— | \$(26,500) |
| Subsequent drawing on line of credit | — | 26,500 |

The accompanying Notes to Condensed Consolidated Financial Statements are an integral part of these statements.

HEIDRICK & STRUGGLES INTERNATIONAL, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(All tables in thousands, except share and per share figures)
(Unaudited)

1. Basis of Presentation of Interim Financial Information

The accompanying unaudited Condensed Consolidated Financial Statements of Heidrick & Struggles International, Inc. and subsidiaries (the "Company") have been prepared pursuant to the rules and regulations of the U.S. Securities and Exchange Commission ("SEC"). The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue and expenses. Significant items subject to estimates and assumptions include revenue recognition, income taxes, interim effective tax rate and assessment of goodwill and other intangible assets for impairment. Estimates are subject to a degree of uncertainty and actual results could differ from these estimates. These financial statements and notes are to be read in conjunction with the Company's Consolidated Financial Statements and Notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2015, as filed with the SEC on March 10, 2016.

2. Summary of Significant Accounting Policies

A complete listing of the Company's significant accounting policies is discussed in Note 2, Summary of Significant Accounting Policies, in the Notes to Consolidated Financial Statements included in the Company's Annual Report on Form 10-K for the year ended December 31, 2015.

Recently Issued Financial Accounting Standards

In August 2016, the Financial Accounting Standards Board ("FASB") issued accounting Standards Update ("ASU") No. 2016-15, Statement of Cash Flows: Classification of Certain Cash Receipts and Cash Payments, which is intended to reduce diversity in practice as to how certain cash receipts and cash payments should be presented and classified. The standard is effective for interim and annual reporting periods beginning after December 15, 2017 with early adoption permitted. The Company has evaluated the standard and noted the guidance for contingent consideration payments made after a business combination are applicable to the Condensed Consolidated Statements of Cash Flows. The Company currently classifies all contingent consideration payments as financing activities. The impact of this change is not expected to be significant to the classification of these activities on the Consolidated Statements of Cash Flows.

In March 2016, the FASB issued ASU No. 2016-09, Stock Compensation: Improvements to Employee Share-Based Payment Accounting, which is intended to simplify several aspects of the accounting for share-based payment transactions including the income tax accounting, classification of awards as either equity or liabilities, the accounting for forfeitures and classification on the statement of cash flows. The standard is effective for annual reporting periods beginning after December 15, 2016 with early adoption permitted. The Company is planning to early adopt this standard during the fourth quarter of 2016. The impact of this change is not expected to be significant to Condensed Consolidated Financial Statements.

In February 2016, the FASB issued ASU No. 2016-02, Leases, intended to improve financial reporting about leasing transactions. The new guidance will require entities that lease assets to recognize on their balance sheets the assets and liabilities for the rights and obligations created by those leases and to disclose key information about the leasing arrangements. ASU 2016-02 is effective for interim and annual periods beginning after December 15, 2018 with early adoption permitted. The guidance requires lessees and lessors to recognize and measure leases at the beginning of the

earliest period presented using a modified retrospective approach. The Company is currently evaluating the impact of this accounting guidance. The effect is not known or reasonably estimable at this time.

In January 2016, the FASB issued ASU 2016-01, Financial Instruments: Recognition and Measurement of Financial Assets and Financial Liabilities, which addresses certain aspects of recognition, measurement, presentation and disclosure of financial instruments including the recognition of unrealized changes in fair value within net income. The standard is effective for annual reporting periods beginning after December 15, 2017. The Company is currently evaluating the impact of this accounting guidance. The effect is not known or reasonably estimable at this time.

In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers. The ASU requires that an entity recognizes revenue to depict the transfer of promised goods or services to customer in an amount that reflects the consideration to which the Company expects to be entitled in exchange for these goods or services. The effective date has been deferred for one year to the interim and annual reporting periods beginning after December 15, 2017. Early adoption is permitted as of the original effective date, which was interim and annual reporting periods beginning after December 15, 2016.

The guidance permits the use of either of the following transition methods: (i) a full retrospective approach reflecting the application of the standard in each prior reporting period with the option to elect certain practical expedients or (ii) a retrospective approach with the cumulative effect upon initial adoption recognized at the date of adoption. The Company is currently evaluating the impact of this accounting guidance. The effect is not known or reasonably estimable at this time.

3. Allowance for Doubtful Accounts

The activity of the allowance for doubtful accounts for the nine months ended September 30, 2016 is as follows:

| | |
|-------------------------------|----------|
| Balance at December 31, 2015 | \$5,376 |
| Provision charged to income | 1,475 |
| Write-offs | (3,944) |
| Foreign currency translation | (19) |
| Balance at September 30, 2016 | \$2,888 |

4. Property and Equipment, net

The components of the Company's property and equipment are as follows:

| | September 30, 2016 | December 31, 2015 |
|--|--------------------------|-------------------------|
| Leasehold improvements | \$42,187 | \$40,583 |
| Office furniture, fixtures and equipment | 17,079 | 16,234 |
| Computer equipment and software | 30,884 | 28,648 |
| Property and equipment, gross | 90,150 | 85,465 |
| Accumulated depreciation | (54,013) | (48,967) |
| Property and equipment, net | \$36,137 | \$36,498 |

Depreciation expense for the three months ended September 30, 2016 and 2015 was \$2.4 million and \$2.2 million, respectively. Depreciation expense for the nine months ended September 30, 2016 and 2015 was \$7.0 million and \$6.5 million, respectively.

5. Investments

The Company has a U.S. non-qualified deferred compensation plan that consists primarily of U.S. marketable securities and mutual funds, all of which are valued using Level 1 inputs (See Note 6, Fair Value Measurements). The fair value for these investments was \$17.3 million and \$14.1 million as of September 30, 2016 and December 31, 2015, respectively. The aggregate cost basis for these investments was \$13.2 million and \$11.1 million as of September 30, 2016 and December 31, 2015, respectively.

6. Fair Value Measurements

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. A three-level fair value hierarchy prioritizes the inputs used to measure fair value. The hierarchy requires entities to maximize the use of observable inputs and minimize the use of unobservable inputs. The three levels of inputs used to measure fair value are as follows:

Level 1 – Quoted prices in active markets for identical assets and liabilities.

•

Level 2 – Quoted prices in active markets for similar assets and liabilities, or other inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument.

Level 3 – Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets and liabilities. This includes certain pricing models, discounted cash flow methodologies and similar techniques that use significant unobservable inputs.

The following tables provide a summary of the fair value measurements at September 30, 2016 and December 31, 2015 for each major category of assets and liabilities measured at fair value on a recurring basis:

| | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) | Total |
|--|---|---|--|-----------|
| At September 30, 2016 | | | | |
| U.S. non-qualified deferred compensation plan | \$ 17,268 | \$ — | \$ — | \$ 17,268 |
| Assets designated for retirement and pension plans | — | 18,790 | — | 18,790 |
| Acquisition earnout accruals | — | — | (9,790) | (9,790) |
| | \$ 17,268 | \$ 18,790 | \$ (9,790) | \$ 26,268 |

| | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) | Total |
|--|---|---|--|-----------|
| At December 31, 2015 | | | | |
| U.S. non-qualified deferred compensation plan | \$ 14,145 | \$ — | \$ — | \$ 14,145 |
| Assets designated for retirement and pension plans | — | 18,164 | — | 18,164 |
| Acquisition earnout accruals | — | — | (12,033) | (12,033) |
| | \$ 14,145 | \$ 18,164 | \$ (12,033) | \$ 20,276 |

The Level 2 assets above are fair valued using a market approach. The Level 3 liabilities include accruals for future earnout payments related to prior acquisitions, the values of which are determined based on discounted cash flow models. The Company considers the recorded value of its financial assets and liabilities, which consist primarily of cash and cash equivalents, accounts receivable, and accounts payable, to approximate the fair value of the respective assets and liabilities at September 30, 2016 and December 31, 2015 based upon the short-term nature of the assets and liabilities.

The following table provides a reconciliation of the beginning and ending balance of Level 3 assets and liabilities for the nine months ended September 30, 2016.

| | |
|---------------------------------------|------------------------------------|
| | Acquisition Earnout Accruals |
| Balance at December 31, 2015 | \$ (12,033) |
| Acquisition earnouts (Note 7) | (5,039) |
| Co Company earnout amendment (Note 7) | (577) |
| Earnout accretion | (198) |
| Earnout payments | 7,461 |
| Foreign currency translation | 596 |
| Balance at September 30, 2016 | \$ (9,790) |

7. Acquisitions

Philosophy IB, LLP

On September 1, 2016, the Company acquired substantially all of the assets of Philosophy IB, LLP ("Philosophy IB"), a New Jersey-based leadership, organization development and management consulting firm for \$6.0 million, which was funded from existing cash. The former owners of Philosophy IB are eligible to receive an additional cash consideration based on two components: achieving revenue milestones generated from its software products from September 2016 through August 2019 and percentage of consulting revenue achieved over the period September 2016 to August 2019, subject to a profitability test. The Company estimates the value of future cash consideration to be between \$0.8 million and \$1.5 million. Due to the timing of the acquisition, the Company is currently performing the fair value valuation for the acquired assets and liabilities, including identifying other intangible assets from goodwill.

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JCA Group Limited

On August 4, 2016, the Company acquired JCA Group Limited ("JCA Group"), a UK-based provider of executive search, succession planning and coaching services, and, from the partners thereof, the entire partnership interest in JCA Partners LLP for £11.2 million (equivalent to \$14.5 million at September 30, 2016) of initial consideration, which was funded from existing cash. The former owners of JCA Group are eligible to receive additional cash consideration upon the realization of specific revenue milestones achieved over the period August 2016 through August 2018. When estimating the value of future cash consideration, the Company has accrued £2.7 million (equivalent to \$3.5 million) as of September 30, 2016. The Company recorded \$3.5 million of intangible assets related to customer relationships and \$15.5 million of goodwill. The goodwill is primarily related to the acquired workforce and strategic fit. Due to the timing of the acquisition, the Company has not completed the fair value valuation for the acquired assets and liabilities, including identifying other intangible assets from goodwill.

Decision Strategies International, Inc.

On February 29, 2016, the Company acquired substantially all of the assets of Decision Strategies International, Inc. ("DSI"), a Pennsylvania-based business consulting firm and its wholly owned subsidiary, Decision Strategies International (UK) Limited. DSI specializes in advising organizations and institutions on strategic planning and decision making in uncertain operating environments, leadership development and talent strategy. Total consideration for the acquisition of DSI's assets was approximately \$9.0 million and was funded from existing cash. The former owners of DSI are eligible to receive an additional cash consideration payment in 2019 based on revenue targets to be achieved in 2017 and 2018. When estimating the value of future cash consideration, the Company has accrued \$1.7 million as of September 30, 2016. The Company recognized \$0.1 million and \$0.2 million of accretion expense included in General and administrative expenses during the three and nine months ended September 30, 2016, respectively. The Company recorded \$3.2 million of intangible assets related to customer relationships and \$5.7 million of goodwill. The goodwill is primarily related to the acquired workforce and strategic fit.

Co Company Limited

On October 1, 2015, the Company acquired Co Company, a UK-based management consulting firm that specializes in organizational development for £7.1 million (equivalent to \$9.2 million and \$10.4 million at September 30, 2016 and December 31, 2015, respectively) of initial consideration, pursuant to a stock purchase, which was funded from existing cash. The former owners of Co Company are eligible to receive additional cash consideration upon the realization of specific revenue and EBITDA Margin milestones achieved over the period October 2015 through December 2018. On August 25, 2016, the Company and the former owners of Co Company entered into a Deed of Amendment (the "Amendment") to the Share Purchase Agreement dated October 1, 2015. The Amendment adjusts the target fee revenue and targeted EBITDA margin for each remaining earn out period taking into consideration the unanticipated acquisitions completed subsequent to the Share Purchase Agreement. The new targets shall include subsequent acquisitions and take effect retrospectively from January 1, 2016. When estimating the fair value of future cash consideration, the Company has accrued £2.9 million (equivalent to \$3.8 million and \$4.3 million) as of September 30, 2016 and December 31, 2015, of which \$0.2 million was paid during the second quarter of 2016. As a result of the Amendment and related adjustment of the earnout liability, the Company recognized \$0.5 million and \$0.2 million of income in General and administrative expenses during the three and nine months ended September 30, 2016, respectively. The Company recorded \$2.9 million of intangible assets and \$10.7 million of goodwill. The goodwill is primarily related to the acquired workforce and strategic fit.

Scambler MacGregor Executive Search Pty Limited

In November 2013, the Company acquired Scambler MacGregor, an Australian-based retained Executive Search boutique in the financial services industry for 1.1 million Australian dollars (equivalent to \$0.8 million at both September 30, 2016 and December 31, 2015) of initial consideration, pursuant to a stock purchase, which was funded from existing cash. In December 2013, the Company paid an additional \$0.1 million related to the final working capital settlement. The former owners of Scambler MacGregor are eligible to receive earnout payments of up to 2.8 million Australian dollars (equivalent to \$2.1 million and \$2.0 million as of September 30, 2016 and December 31, 2015, respectively) based on the achievement of certain revenue metrics over the period November 2013 through December 2018, of which \$0.4 million and \$0.7 million was paid during the nine months ended September 30, 2016 and 2015, respectively. When estimating the fair value of future earnout payments, the Company had accrued 1.1 million Australian dollars and 1.6 million Australian dollars (equivalent to \$0.9 million and \$1.2 million) as of September 30, 2016 and December 31, 2015, respectively. The Company also recorded \$0.4 million of intangible assets and \$2.7 million of goodwill. The goodwill is primarily related to the acquired workforce and strategic fit.

Senn-Delaney Leadership Consulting Group, LLC

In December 2012, the Company acquired Senn-Delaney Leadership Consulting Group, LLC, a global leader of corporate culture shaping. Under the terms of the purchase agreement, the Company paid \$53.5 million at closing for 100 percent of the equity of Senn Delaney. The agreement also included additional cash consideration up to \$15.0 million based on the realization of specific earnings milestones achieved over the period December 2012 through December 2015, of which \$6.8 million, \$4.8 million and \$3.4 million was paid during the second quarter of 2016, 2015 and 2014, respectively. The Company had accrued \$6.6 million at December 31, 2015 for the remaining cash consideration, which was paid during the nine months ended September 30, 2016. The Company recognized zero and \$0.3 million of accretion expense during the three months ended September 30, 2016 and 2015, respectively, and \$0.2 million and \$0.8 million of accretion expense during the nine months ended September 30, 2016 and 2015, respectively. Accretion expense is included in General and administrative expenses in the Condensed Consolidated Statements of Comprehensive Income. At December 31, 2015, the Company held \$6.5 million in a retention escrow that was paid to certain key executives of Senn Delaney in January 2016 for remaining with the Company for three years subsequent to the acquisition. The Company recognized zero and \$0.5 million of compensation expense during the three months ended June 30, 2016 and 2015, respectively, and zero and \$1.6 million of compensation expense during the nine months ended September 30, 2016 and 2015, respectively. Compensation expense is included in Salaries and employee benefits in the Condensed Consolidated Statements of Comprehensive Income.

8. Goodwill and Other Intangible Assets

Goodwill

Changes in the carrying amount of goodwill by segment for the nine months ended September 30, 2016 are as follows:

| | Executive Search and Leadership Consulting | | | Culture Shaping | Total |
|-------------------------------|---|----------|-----------------|--------------------|-----------|
| | Americas | Europe | Asia Pacific | | |
| Balance at December 31, 2015 | \$81,626 | \$10,745 | \$9,211 | \$29,540 | \$131,122 |
| DSI acquisition | 5,673 | — | — | — | 5,673 |
| JCA Group acquisition | — | 15,535 | — | — | 15,535 |
| Philosophy IB acquisition | 4,253 | — | — | — | 4,253 |
| Foreign currency translation | 196 | (1,719) | 488 | (235) | (1,270) |
| Balance at September 30, 2016 | \$91,748 | \$24,561 | \$9,699 | \$29,305 | \$155,313 |

On September 1, 2016, the Company acquired Philosophy IB and included the fair value of the acquired assets and liabilities as of the acquisition date in the Consolidated Balance Sheets. The Company also included \$4.3 million of goodwill related to the acquisition in the Americas segment. On August 4, 2016, the Company acquired JCA Group and included the fair value of the acquired assets and liabilities as of the acquisition date in the Consolidated Balance Sheets. The Company also included \$15.5 million of goodwill related to the acquisition in the Europe segment. On February 29, 2016, the Company acquired DSI and included the fair value of the acquired assets and liabilities as of the acquisition date in the Condensed Consolidated Balance Sheets. The Company also included \$5.7 million of goodwill related to the acquisition in the Americas segment.

Due to the timing of the acquisitions, the Company has not completed the fair value valuation for the acquired assets and liabilities, including identifying other intangible assets from goodwill for JCA Group and Philosophy IB.

Other Intangible Assets, net

The Company's other intangible assets, net by segment, are as follows:

| | September 30, 2016 | December 31, 2015 |
|--|--------------------------|-------------------------|
| Executive Search and Leadership Consulting | | |
| Americas | \$ 3,221 | \$ 764 |
| Europe | 4,828 | 2,548 |
| Asia Pacific | 149 | 209 |
| Total Executive Search and Leadership Consulting | 8,198 | 3,521 |
| Culture Shaping | 11,956 | 15,166 |
| Total other intangible assets, net | \$ 20,154 | \$ 18,687 |

The Company identified client relationships of \$3.5 million as a part of the JCA Group acquisition and included the fair value in the Europe segment. Due to the timing of the acquisitions, the Company has not completed its evaluation of identifying other intangible assets from goodwill for JCA Group and Philosophy IB.

The Company identified client relationships of \$3.2 million and as part of the DSI acquisitions and included the fair value in the Americas segment.

The carrying amount of amortizable intangible assets and the related accumulated amortization are as follows:

| | Weighted | September 30, 2016 | | | December 31, 2015 | | |
|-------------------------|----------|--------------------|--------------|-----------|-------------------|--------------|-----------|
| | Average | Gross | Accumulated | Net | Gross | Accumulated | Net |
| | Life (in | Carrying | Amortization | Carrying | Carrying | Amortization | Carrying |
| | years) | Amount | | Amount | Amount | | Amount |
| Client relationships | 7.8 | \$31,503 | \$ (20,214) | \$ 11,289 | \$25,414 | \$ (17,550) | \$ 7,864 |
| Trade name | 15.0 | 9,077 | (4,077) | 5,000 | 9,251 | (3,416) | 5,835 |
| Software | 7.0 | 7,200 | (3,857) | 3,343 | 7,200 | (3,086) | 4,114 |
| Non-compete | 5.0 | 570 | (307) | 263 | 586 | (117) | 469 |
| Technology | 3.0 | 389 | (130) | 259 | 442 | (37) | 405 |
| Total intangible assets | 9.4 | \$48,739 | \$ (28,585) | \$ 20,154 | \$42,893 | \$ (24,206) | \$ 18,687 |

Intangible asset amortization expense for the three months ended September 30, 2016 and 2015 was \$1.6 million and \$1.2 million, respectively. Intangible asset amortization expense for the nine months ended September 30, 2016 and 2015 was \$4.7 million and \$3.5 million, respectively

The Company's estimated future amortization expense related to intangible assets as of September 30, 2016 for the years ended December 31st is as follows:

| | |
|-------------------|----------|
| Remainder of 2016 | \$1,709 |
| 2017 | 5,434 |
| 2018 | 4,204 |
| 2019 | 3,242 |
| 2020 | 1,853 |
| Thereafter | 3,712 |
| Total | \$20,154 |

9. Other Non-Current Liabilities

The components of other non-current liabilities are as follows:

| | September 30, 2016 | December 31, 2015 |
|-------------------------------------|--------------------------|-------------------------|
| Premise related costs | \$ 18,066 | \$ 17,790 |
| Accrued earnout payments | 7,831 | 788 |
| Other | 1,370 | 1,269 |
| Total other non-current liabilities | \$ 27,267 | \$ 19,847 |

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10. Line of Credit

On June 30, 2015, the Company entered into a Second Amended and Restated Credit Agreement (the “Restated Credit Agreement”). The Restated Credit Agreement amended and restated the Credit Agreement executed on June 22, 2011 (the “Credit Agreement”). Pursuant to the Restated Credit Agreement, the Company replaced its Revolving Facility and Term Facility (“Existing Facility”) with a single senior unsecured revolving line of credit with an aggregate commitment of up to \$100 million, which includes a sublimit of \$25 million for letters of credit, and a \$50 million expansion feature (the “Replacement Facility”). The Replacement Facility will mature on June 30, 2020. Borrowings under the Restated Credit Agreement bear interest at the Company’s election at the existing Alternate Base Rate (as defined in the Credit Agreement) or Adjusted LIBOR Rate (as defined in the Credit Agreement) plus a spread as determined by the Company’s leverage ratio.

Borrowings under the Replacement Facility may be used for working capital, capital expenditures, Permitted Acquisitions (as defined in the Credit Agreement) and for other general corporate purposes of the Company and its subsidiaries. The obligations under the Replacement Facility are guaranteed by certain of the Company’s subsidiaries.

As of September 30, 2016 and December 31, 2015, the Company had no outstanding borrowings under the Restated Credit Agreement and the Company was in compliance with the financial and other covenants under the Restated Credit Agreement and no event of default existed.

11. Stock-Based Compensation

The Company’s 2012 Heidrick & Struggles GlobalShare Program (the “2012 Program”) provides for grants of stock options, stock appreciation rights, and other stock-based awards that are valued based upon the grant date fair value of shares. These awards may be granted to directors, selected employees and independent contractors. The 2012 Program originally authorized 1,300,000 shares of Common Stock for issuance pursuant to awards under the plan.

On May 22, 2014, the stockholders of the Company approved an amendment to the 2012 Program to increase the number of shares of Common Stock reserved for issuance under the 2012 Program by 700,000 shares. As of September 30, 2016, 1,397,410 awards have been issued under the 2012 Program and 1,003,228 shares remain available for future awards, which includes 400,638 forfeited awards. The 2012 Program provides that no awards can be granted after May 24, 2022.

The Company measures its stock-based compensation costs based on the grant date fair value of the awards and recognizes these costs in the financial statements over the requisite service period.

A summary of information with respect to stock-based compensation is as follows:

| | Three Months Ended | | Nine Months Ended | |
|--|-----------------------|----------|-----------------------|----------|
| | September 30, 2016 | 2015 | September 30, 2016 | 2015 |
| Salaries and employee benefits | \$ 1,155 | \$ 1,094 | \$ 4,492 | \$ 3,234 |
| General and administrative expenses | — | — | 563 | 450 |
| Income tax benefit 437 related to stock-based compensation | | 259 | 2,005 | 1,301 |

included in net
income

Restricted Stock Units

Restricted stock unit activity for the nine months ended September 30, 2016:

| | Number of Restricted Stock Units | Weighted- Average Grant-date Fair Value |
|--------------------------------------|--|--|
| Outstanding on December 31, 2015 | 473,935 | \$ 19.98 |
| Granted | 207,405 | 22.92 |
| Vested and converted to common stock | (119,455) | 20.02 |
| Forfeited | (24,612) | 22.81 |
| Outstanding on September 30, 2016 | 537,273 | 20.97 |

As of September 30, 2016, there was \$4.4 million of pre-tax unrecognized compensation expense related to unvested restricted stock units, which is expected to be recognized over a weighted average of 2.0 years.

Performance Stock Units

The Company grants performance stock units to certain of its senior executives. The performance stock units are generally subject to a cliff vesting at the end of a three year period. The vesting will vary between 0%—200% based on the attainment of operating income goals over the three year vesting period. The performance stock units are expensed on a straight-line basis over the three year vesting period.

In 2014, the Company granted market-based performance stock units to the Chief Executive Officer. The market-based awards vest after a two year service period and if the price of the Company's common stock exceeds specified targets. The fair value of the market-based awards was determined using the Monte-Carlo simulation model. A Monte Carlo simulation model uses stock price volatility and other variables to estimate the probability of satisfying the market conditions and the resulting fair value of the award. Compensation costs related to the market-based awards are recognized regardless of whether the market condition is satisfied, as long as the requisite service has been provided. All of the market-based performance conditions were satisfied such that all 125,000 performance stock units granted to the Chief Executive Officer vested upon the completion of the two year service period in February 2016.

Performance stock unit activity for the nine months ended September 30, 2016:

| | Number of Performance Stock Units | Weighted- Average Grant-date Fair Value |
|--------------------------------------|---|--|
| Outstanding on December 31, 2015 | 272,024 | \$ 18.28 |
| Granted | 125,388 | 22.98 |
| Vested and converted to common stock | (160,600) | 15.51 |
| Outstanding on September 30, 2016 | 236,812 | 22.64 |

As of September 30, 2016, there was \$2.6 million of pre-tax unrecognized compensation expense related to unvested performance stock units, which is expected to be recognized over a weighted average of 2.1 years.

12. Income Taxes

The Company reported income before taxes of \$12.4 million and \$11.1 million and an income tax provision of \$5.4 million and \$3.6 million for the three months ended September 30, 2016 and 2015, respectively. The increase in the income tax provision was due to higher consolidated income before taxes of \$1.3 million and the mix of income.

The Company reported income before taxes of \$28.2 million and \$26.8 million and an income tax provision of \$13.2 million and \$10.9 million for the nine months ended September 30, 2016 and 2015, respectively. The increase in the income tax provision was due to higher consolidated income before taxes of \$1.4 million and the mix of income.

13. Changes in Accumulated Other Comprehensive Income

The changes in Accumulated other comprehensive income (“AOCI”) by component for the nine months ended September 30, 2016 is summarized below:

| | Available- for- Sale Securities | Foreign Currency Translation | Pension | AOCI |
|---|--|------------------------------------|-----------|---------|
| Balance at December 31, 2015 | \$ 2,394 | \$ 8,561 | \$(1,696) | \$9,259 |
| Other comprehensive income / (loss) before classification, net of tax | 709 | (1,173) | — | (464) |
| Amount reclassified from AOCI (1) | 321 | — | — | 321 |
| Net current period other comprehensive income / (loss) | 1,030 | (1,173) | — | (143) |
| Balance at September 30, 2016 | \$ 3,424 | \$ 7,388 | \$(1,696) | \$9,116 |

(1) Available-for-Sale Securities reclassifications from AOCI are included in Other, net in the Condensed Consolidated Statement of Comprehensive Income.

14. Segment Information

The Company operates its executive search and leadership consulting services in the Americas; Europe (which includes Africa); and Asia Pacific (which includes the Middle East) and operates its culture shaping business as a separate segment.

For segment purposes, reimbursements of out-of-pocket expenses classified as revenue and other operating income are reported separately and, therefore, are not included in the results of each segment. The Company believes that analyzing trends in revenue before reimbursements (net revenue), analyzing operating expenses as a percentage of net revenue, and analyzing operating income more appropriately reflects its core operations.

The revenue and operating income (loss) by segment are as follows:

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|--|--|-----------|---------------------------------------|-----------|
| | 2016 | 2015 | 2016 | 2015 |
| Revenue: | | | | |
| Executive Search and Leadership Consulting | | | | |
| Americas | \$78,198 | \$78,265 | \$237,557 | \$218,560 |
| Europe | 32,895 | 25,946 | 91,017 | 69,679 |
| Asia Pacific | 23,801 | 25,031 | 67,325 | 72,712 |
| Total Executive Search and Leadership Consulting | 134,894 | 129,242 | 395,899 | 360,951 |
| Culture Shaping | 8,625 | 9,179 | 26,670 | 25,668 |
| Revenue before reimbursements (net revenue) | 143,519 | 138,421 | 422,569 | 386,619 |
| Reimbursements | 4,720 | 4,429 | 13,773 | 12,396 |
| Total | \$148,239 | \$142,850 | \$436,342 | \$399,015 |
| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
| | 2016 | 2015 | 2016 | 2015 |
| Operating income (loss): | | | | |
| Executive Search and Leadership Consulting | | | | |
| Americas | \$18,552 | \$18,193 | \$56,817 | \$50,563 |
| Europe | 2,371 | 1,470 | 2,429 | 1,018 |
| Asia Pacific | 2,029 | 2,630 | 5,179 | 8,088 |
| Total Executive Search and Leadership Consulting | 22,952 | 22,293 | 64,425 | 59,669 |
| Culture Shaping | 41 | 1,539 | (1,928) | 2,948 |
| Total Segments | 22,993 | 23,832 | 62,497 | 62,617 |
| Global Operations Support | (10,987) | (10,899) | (34,929) | (33,840) |
| Total | \$12,006 | \$12,933 | \$27,568 | \$28,777 |

15. Guarantees

The Company has issued cash collateralized bank guarantees and letter of credit backed bank guarantees supporting certain obligations, primarily the payment of office lease obligations and business license requirements for certain of its subsidiaries in Europe and Asia Pacific. The bank guarantees were made to secure the respective agreements and are for the terms of the agreements, which extend through 2018. For each bank guarantee issued, the Company would have to perform under the guarantee if the subsidiary defaults on a lease payment. The maximum amount of

undiscounted payments the Company would be required to make in the event of default on all outstanding guarantees is approximately \$2.5 million as of September 30, 2016. The Company has not accrued for these arrangements as no event of default exists or is expected to exist.

16. Commitments and Contingencies

Litigation

The Company has contingent liabilities from various pending claims and litigation matters arising in the ordinary course of the Company's business, some of which involve claims for damages that are substantial in amount. Some of these matters are covered by insurance. Based upon information currently available, the Company believes the ultimate resolution of such claims and litigation, including the "UK Employee Benefits Trust" matter discussed below, will not have a material adverse effect on its financial condition, results of operations or liquidity.

UK Employee Benefits Trust

On January 27, 2010, HM Revenue & Customs (“HMRC”) in the United Kingdom notified the Company that it was challenging the tax treatment of certain of the Company’s contributions in the United Kingdom to an Employee Benefits Trust between 2002 and 2008. HMRC alleges that these contributions should have been subject to Pay As You Earn tax and Class 1 National Insurance Contributions in the United Kingdom. HMRC is proposing an adjustment to the Company’s payroll tax liability for the affected years. The aggregate amount of HMRC’s proposed adjustment is approximately £3.9 million (equivalent to \$5.1 million) at September 30, 2016. The Company has appealed the proposed adjustment. At this time, the Company believes that the likelihood of an unfavorable outcome with respect to the proposed adjustment is not probable and the potential amount of any loss cannot be reasonably estimated. The Company also believes that the amount of any final adjustment would not be material to the Company’s financial condition.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Management's Discussion and Analysis of Financial Condition and Results of Operations as well as other sections of this report on Form 10-Q contain forward-looking statements. The Private Securities Litigation Reform Act of 1995 provides a safe harbor for forward-looking statements. Forward-looking statements are not historical facts, but instead represent only our beliefs, assumptions, expectations, estimates, forecasts and projections regarding future events, many of which, by their nature, are inherently uncertain and outside our control. These statements include statements other than historical information or statements of current condition and may relate to our future plans and objectives and results. By identifying these statements for you in this manner, we are alerting you to the possibility that our actual results and financial condition may differ, possibly materially, from the anticipated results and financial condition indicated in these forward-looking statements.

Factors that may affect the outcome of the forward-looking statements include, among other things, leadership changes; our ability to attract, integrate, manage and retain qualified consultants and senior leaders; our ability to develop and maintain strong, long-term relationships with our clients; fluctuations in the global and local economies and our ability to execute successfully our strategies; social or political instability in markets where we operate, the impact of the U.K. referendum to leave the European Union (Brexit); the impact of foreign currency exchange rate fluctuations; unfavorable tax law changes and tax authority rulings; price competition; the ability to forecast, on a quarterly basis, variable compensation accruals that ultimately are determined based on the achievement of annual results; our ability to realize our tax losses; the timing of the establishment or reversal of valuation allowance on deferred tax assets; the mix of profit and loss by country; our ability to integrate future acquisitions; our reliance on information management systems; any impairment of our goodwill and other intangible assets; and the ability to align our cost structure and headcount with net revenue. For more information on the factors that could affect the outcome of forward-looking statements, refer to our Annual Report on Form 10-K for the year ended December 31, 2015, under Risk Factors in Item 1A. We caution the reader that the list of factors may not be exhaustive. We undertake no obligation to update publicly any forward-looking statements, whether as a result of new information, future events or otherwise.

Executive Overview

Our Business. We are a leadership advisory firm providing executive search, culture shaping services and leadership consulting. We help our clients build leadership teams by facilitating the recruitment, management and development of senior executives. We provide our services to a broad range of clients through the expertise of over 350 consultants located in major cities around the world.

Executive Search. We partner with respected organizations globally to build and sustain the best leadership teams in the world, with a specialized focus on the placement of top-level senior executives. We believe focusing on top-level senior executives provides the opportunity for several advantages including access to and influence with key decision makers, increased potential for recurring search and consulting engagements, higher fees per executive search, enhanced brand visibility, and a leveraged global footprint. Working at the top of client organizations also facilitates the attraction and retention of high-caliber consultants who desire to serve top industry executives and their leadership needs.

Our executive search services are provided on a retained basis. Revenue before reimbursements of out-of-pocket expenses ("net revenue") consists of retainers and indirect expenses billed to clients. For each assignment, we enter into a contract with our client that outlines the general terms and conditions of the assignment. Typically, we are paid a retainer for our executive search services equal to approximately one-third of the estimated first year compensation for the position to be filled. In addition, generally, if the actual compensation of a placed candidate exceeds the estimated

compensation, we often are authorized to bill the client for one-third of the excess. Indirect expenses are calculated as a percentage of the retainer with certain dollar limits per search. We generally bill our clients for our retainer and indirect expenses in one-third increments over a three-month period commencing in the month of a client's acceptance of the contract.

On August 4, 2016, we acquired JCA Group Limited ("JCA Group") a UK-based provider of executive search, succession planning and coaching services.

Culture Shaping. Our culture shaping business uses its proprietary technology to analyze and interpret organizational cultures and drivers and partner with clients to administer methods that develop alignment on leadership teams and desired organizational outcomes. Culture Shaping is currently less than 10% of our net revenue. Our culture shaping services generate revenue through a combination of professional service and license fees related to the engagement. Net revenue associated with culture shaping consulting is recognized proportionally as services are performed. Net revenue associated with licenses to use culture shaping proprietary materials is typically recognized over the term of the arrangement.

Leadership Consulting. Leadership consulting works with clients to accelerate performance at the strategic, organization, team and individual leader levels. Leadership Consulting is currently less than 10% of our net revenue. Our leadership consulting services generate revenue primarily through the professional fees generated for each engagement which are generally based on the size of the project and scope of services. Depending on the terms of the agreement, net revenue from leadership consulting is either recognized proportionally as services are performed or in accordance with the completion of the engagement deliverables. On September 1, 2016, we acquired Philosophy IB, LLP, a leadership, organizational development and management consulting firm. On February 29, 2016, we acquired Decision Strategies International, Inc., which specializes in advising organizations and institutions on strategic planning and decision making in certain operating environments, leadership development and talent strategy. On October 1, 2015, we acquired Co Company Limited, an organizational development consulting firm.

Key Performance Indicators

We manage and assess Heidrick & Struggles' performance through various means, with the primary financial and operational measures including net revenue, operating income, operating margin, Adjusted EBITDA (non-GAAP), and Adjusted EBITDA margin (non-GAAP). Executive Search and Leadership Consulting performance is also measured using consultant headcount and consultant productivity. Specific to Executive Search, confirmation trends and average revenue per search or project are used to measure performance.

Revenue is driven by market conditions and a combination of the number of executive search engagements and leadership consulting and culture shaping projects and the average revenue per search or project. With the exception of compensation expense, incremental increases in revenue do not necessarily result in proportionate increases in costs, particularly operating and administrative expenses, thus potentially improving operating margins.

The number of consultants, confirmation trends, number of searches or projects completed, productivity levels and the average revenue per search or project will vary from quarter to quarter, affecting net revenue and operating margin.

Our Compensation Model

At the Executive Search consultant level there are fixed and variable components of compensation. Individuals are rewarded for their performance based on a system that directly ties a portion of their compensation to the amount of net revenue for which they are responsible. A portion of the reward is based upon individual performance against a series of non-financial measures. Credit towards the variable portion of an Executive Search consultant's compensation is earned by generating net revenue for winning and executing work. Each quarter, we review and update the expected annual performance of all Executive Search consultants and accrue variable compensation accordingly. The amount of variable compensation that is accrued for each Executive Search consultant is based on a tiered payout model. Overall Company performance determines the amount available for total variable compensation. The more net revenue that is generated by the consultant, the higher the percentage credited towards the consultant's variable compensation and thus accrued by our Company as expense. The mix of individual consultants who generate the revenue can significantly affect the total amount of compensation expense recorded, which directly impacts operating margin. As a result, the variable portion of the compensation expense may fluctuate significantly from quarter to quarter. The total variable compensation is discretionary and is based on Company-wide financial targets approved by the Human Resources and Compensation Committee of the Board of Directors.

A portion of our Executive Search consultants' and management cash bonuses is deferred and paid over a three-year vesting period. The compensation expense related to the amounts being deferred is recognized on a graded vesting attribution method over the requisite service period. This service period begins on January 1 of the respective fiscal year and continues through the deferral date, which coincides with our bonus payments in the first quarter of the following year, and for an additional three year vesting period. The deferrals are recorded in Accrued salaries and

employee benefits and Other non-current liabilities in the Condensed Consolidated Balance Sheets.

Fourth Quarter 2016 Outlook

We are currently forecasting 2016 fourth quarter net revenue of between \$142 million and \$152 million. Our 2016 fourth quarter guidance is based upon, among other things, management's assumptions for the anticipated volume of new executive search confirmations and leadership consulting and culture shaping projects, the current backlog, consultant productivity, consultant retention, the seasonality of our business and average currency rates in September 2016.

Our 2016 guidance is subject to a number of risks and uncertainties, including those discussed under Item 1A - Risk Factors in our 2015 Annual Report on Form 10-K. As such, actual results could vary from these projections.

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Results of Operations

The following table summarizes, for the periods indicated, our results of operations as a percentage of revenue before reimbursements (net revenue):

| | Three Months Ended | | Nine Months Ended | |
|---|--------------------|---------|--------------------|---------|
| | September 30, 2016 | 2015 | September 30, 2016 | 2015 |
| Revenue: | | | | |
| Revenue before reimbursements (net revenue) | 100.0% | 100.0 % | 100.0% | 100.0 % |
| Reimbursements | 3.3 | 3.2 | 3.3 | 3.2 |
| Total revenue | 103.3 | 103.2 | 103.3 | 103.2 |
| Operating expenses: | — | — | — | — |
| Salaries and employee benefits | 66.4 | 69.2 | 68.2 | 68.5 |
| General and administrative expenses | 25.2 | 21.5 | 25.3 | 24.0 |
| Reimbursed expenses | 3.3 | 3.2 | 3.3 | 3.2 |
| Total operating expenses | 94.9 | 93.9 | 96.7 | 95.8 |
| Operating income | 8.4 | 9.3 | 6.5 | 7.4 |
| Non-operating income (expense): | | | | |
| Interest, net | — | — | — | (0.1) |
| Other, net | 0.2 | (1.3) | 0.1 | (0.4) |
| Net non-operating income (expense) | 0.3 | (1.3) | 0.1 | (0.5) |
| Income before income taxes | 8.6 | 8.0 | 6.7 | 6.9 |
| Provision for income taxes | 3.8 | 2.6 | 3.1 | 2.8 |
| Net income | 4.8 % | 5.4 % | 3.5 % | 4.1 % |

Note: Totals and sub-totals may not equal the sum of individual line items due to rounding.

We operate our executive search and leadership consulting services in the Americas; Europe (which includes Africa); and Asia Pacific (which includes the Middle East) and operate our culture shaping business as a separate segment (See Note 14, Segment Information).

The following tables set forth, for the periods indicated, our revenue and operating income by segment (in thousands):

| | Three Months Ended | | Nine Months Ended | |
|--|--------------------|-----------|--------------------|-----------|
| | September 30, 2016 | 2015 | September 30, 2016 | 2015 |
| Revenue: | | | | |
| Executive Search and Leadership Consulting | | | | |
| Americas | \$78,198 | \$78,265 | \$237,557 | \$218,560 |
| Europe | 32,895 | 25,946 | 91,017 | 69,679 |
| Asia Pacific | 23,801 | 25,031 | 67,325 | 72,712 |
| Total Executive Search and Leadership Consulting | 134,894 | 129,242 | 395,899 | 360,951 |
| Culture Shaping | 8,625 | 9,179 | 26,670 | 25,668 |
| Revenue before reimbursements (net revenue) | 143,519 | 138,421 | 422,569 | 386,619 |
| Reimbursements | 4,720 | 4,429 | 13,773 | 12,396 |
| Total | \$148,239 | \$142,850 | \$436,342 | \$399,015 |

| | Three Months Ended September 30, 2016 | | Nine Months Ended September 30, 2015 | |
|--|--|-----------|---|-----------|
| Operating income (loss): | | | | |
| Executive Search and Leadership Consulting | | | | |
| Americas | \$ 18,552 | \$ 18,193 | \$ 56,817 | \$ 50,563 |
| Europe | 2,371 | 1,470 | 2,429 | 1,018 |
| Asia Pacific | 2,029 | 2,630 | 5,179 | 8,088 |
| Total Executive Search and Leadership Consulting | 22,952 | 22,293 | 64,425 | 59,669 |
| Culture Shaping | 41 | 1,539 | (1,928) | 2,948 |
| Total Segments | 22,993 | 23,832 | 62,497 | 62,617 |
| Global Operations Support | (10,987) | (10,899) | (34,929) | (33,840) |
| Total | \$ 12,006 | \$ 12,933 | \$ 27,568 | \$ 28,777 |

Three Months Ended September 30, 2016 Compared to the Three Months Ended September 30, 2015

Total revenue. Consolidated total revenue increased \$5.4 million, or 3.8%, to \$148.2 million in 2016 from \$142.9 million in 2015. The increase in total revenue was due primarily to the increase in revenue before reimbursements (net revenue).

Revenue before reimbursements (net revenue). Consolidated net revenue increased \$5.1 million, or 3.7%, to \$143.5 million for the three months ended September 30, 2016 from \$138.4 million for the three months ended September 30, 2015. Foreign exchange rate fluctuations decreased revenue by \$0.6 million, or less than one percentage point. Executive Search and Leadership Consulting net revenue was \$134.9 million, an increase of \$5.7 million compared to the three months ended September 30, 2015. The increase in Executive Search and Leadership Consulting net revenue is primarily due to our recent acquisitions, as well as growth in all practice groups, with the exception of the Financial Services and Global Technology & Services practice groups. Culture Shaping net revenue was \$8.6 million for the three months ended September 30, 2016, a decrease of \$0.6 million compared to the three months ended September 30, 2015.

The number of Executive Search and Leadership Consulting consultants was 356 as of September 30, 2016 compared to 334 as of September 30, 2015, with our recent acquisitions contributing 23 consultants to 2016. Productivity, as measured by annualized net Executive Search and Leadership Consulting revenue per consultant was \$1.5 million for the three months ended September 30, 2016 compared to \$1.6 million for the three months ended September 30, 2015. Specific to Executive Search, our primary business, the number of confirmed searches increased 5.7% compared to the third quarter of 2015. The average revenue per executive search decreased to \$113,700 in the third quarter of 2016 compared to \$121,200 in the third quarter of 2015.

Salaries and employee benefits. Consolidated salaries and employee benefits expense decreased \$0.4 million, or 0.4%, to \$95.4 million for the three months ended September 30, 2016 from \$95.7 million for the three months ended September 30, 2015. The decrease was primarily due to lower variable compensation partially offset by increased fixed compensation of \$7.3 million. Fixed compensation increased due to higher compensation related to our four recent acquisitions, higher base salaries and benefit costs, new hires over the last year with incentives and minimum guarantees that are part of the consultant hiring process, and \$1.3 million of investments in new and existing partners in our Culture Shaping business. As a result of higher fixed compensation expense and an increase in the use of third-party consultants, whose costs are included in General and administrative expenses, variable compensation declined \$7.7 million in the quarter reflecting the overall profitability of the business.

In the 2016 third quarter we had an average of 1,770 employees compared to an average of 1,548 employees in the 2015 third quarter. Foreign exchange rate fluctuations increased salaries and employee benefits expense by \$0.1 million, or less than one percent, in the third quarter of 2016.

As a percentage of net revenue, salaries and employee benefits expense was 66.4% in in the third quarter of 2016 as compared to 69.2% for the same period in the prior year.

General and administrative expenses. Consolidated general and administrative expenses increased \$6.4 million, or 21.5%, to \$36.2 million for the three months ended September 30, 2016. The increase was due to ongoing general and administrative expenses related to our four recent acquisitions including the use of third-party consultants in these businesses to execute work, higher professional service fees supporting technology implementation, training and development, marketing and audit fees,

higher unbilled travel and business development expense, higher temporary help and hiring fees, and an increase in technology subscription costs reflecting additional headcount throughout the business for cloud-based services.

Foreign exchange rate fluctuations did not impact general and administrative expense in the third quarter of 2016.

As a percentage of net revenue, general and administrative expenses were 25.2% in the third quarter of 2016 compared to 21.5% in the third quarter of 2015.

Operating income. Consolidated operating income was \$12.0 million for the three months ended September 30, 2016, compared to \$12.9 million for the three months ended September 30, 2015. The net impact of foreign exchange rate fluctuations decreased operating income by \$0.7 million.

Net non-operating income (expense). Net non-operating income was \$0.4 million for the three months ended September 30, 2016 an increase of \$2.2 million from net non-operating expense of \$1.8 million for the three months ended September 30, 2015.

Interest, net was zero in the third quarter of 2016 compared to \$0.1 million of expense in 2015. Interest expense decreased \$0.1 million due the repayment of outstanding debt in the third quarter of 2015.

Other, net was \$0.3 million of income and \$1.7 million of expense for the three months ended September 30, 2016 and 2015, respectively. Other, net increased due to lower net losses on available for sale securities compared to the prior year and decreased losses on the disposal of fixed assets.

Income taxes. See Note 12, Income Taxes.

Executive Search and Leadership Consulting

Americas

The Americas segment reported net revenue of \$78.2 million for the three months ended September 30, 2016, a decrease of less than one percent, from \$78.3 million for the three months ended September 30, 2015. The decrease in net revenue was driven by decreases in the Financial Services and Global Technology & Services practice groups, partially offset by growth in the Consumer Markets and Industrial practice groups. The revenue from DSI also partially offset the revenue decline. Foreign exchange rate fluctuations increased net revenue by less than one percentage point. The number of consultants within the Americas segment was 164 as of September 30, 2016 compared to 152 at September 30, 2015, with DSI and Philosophy IB each contributing three consultants to 2016.

Salaries and employee benefits expense decreased \$3.0 million from the third quarter of 2015. Fixed compensation increased \$2.7 million due to higher base salaries and payroll taxes of \$1.4 million due to an increase in headcount. Variable compensation decreased \$5.7 million due to lower bonus accruals.

General and administrative expense increased \$2.6 million primarily due to the acquisition of DSI in February 2016 and higher unbilled travel and business development costs.

The Americas region reported operating income of \$18.6 million for the three months ended September 30, 2016, an increase of \$0.4 million compared to \$18.2 million for the three months ended September 30, 2015.

Europe

The Europe segment reported net revenue of \$32.9 million for the three months ended September 30, 2016, an increase of 26.8%, from \$25.9 million for the three months ended September 30, 2015. All industry practice groups contributed to net revenue growth except for the Education, Nonprofit & Social Enterprise practice group. Also contributing to this growth was the Company's acquisition of Co Company in October 2015 and JCA Group in August of 2016. Foreign exchange rate fluctuations reduced net revenue by approximately four percentage points. The number of consultants within the Europe segment was 103 as of September 30, 2016 compared to 91 at September 30, 2015, with Co Company and JCA Group contributing six and 11 consultants to 2016, respectively.

Salaries and employee benefits expense increased \$3.0 million from the third quarter of 2015. Fixed compensation increased \$3.0 million due to increased minimum guarantees and higher base salaries and payroll taxes, primarily from merit increases and additional headcount related to the Co Company and JCA Group acquisitions. Variable compensation remained unchanged compared to the third quarter of 2015.

General and administrative expense increased \$3.0 million from the third quarter of 2015 primarily as a result of ongoing general and administrative expenses related to our recent acquisitions and the use of third-party consultants in Co Company's business to execute work along with increased professional services.

The Europe segment reported operating income of \$2.4 million for the three months ended September 30, 2016, an increase of \$0.9 million compared to the three months ended September 30, 2015.

Asia Pacific

The Asia Pacific segment reported net revenue of \$23.8 million for the three months ended September 30, 2016, a decrease of 4.9% from \$25.0 million for the three months ended September 30, 2015. The decrease in net revenue was across all industry practice groups except for the Consumer Markets and Healthcare and Life Sciences practice groups. Foreign exchange rate fluctuations increased net revenue by approximately three percentage points. The number of consultants within the Asia Pacific segment was 89 as of September 30, 2016 compared to 91 at September 30, 2015.

Salaries and employee benefits expense decreased \$1.4 million from the third quarter of 2015. The decrease in salaries and employee benefits expense is due to lower variable compensation of \$2.2 million from lower bonus accruals for consultant performance. Fixed compensation increased \$0.8 million compared to the prior year related to an increase in average headcount.

General and administrative expense increased \$0.8 million from the third quarter of 2015 due to higher professional services, higher unbilled travel and business development cost and higher office occupancy expenses.

The Asia Pacific segment had operating income of \$2.0 million for the three months ended September 30, 2016, a decrease of \$0.6 million from the third quarter of 2015.

Culture Shaping

The Culture Shaping segment reported net revenue of \$8.6 million for the three months ended September 30, 2016, a decrease of 6.0% from \$9.2 million for the three months ended September 30, 2015. The decrease is the result of a lower volume of client work.

Salaries and employee benefits expense increased \$0.5 million from the third quarter of 2015 due to investments in new and existing consultants.

General and administrative expenses increased \$0.4 million from the third quarter of 2015 primarily due to higher professional services and internal travel expenses, partially offset by lower hiring fees and temporary labor costs.

The Culture Shaping segment reported operating income of zero for the three months ended September 30, 2016, a decrease of \$1.5 million compared to the three months ended September 30, 2015.

Global Operations Support

Global Operations Support expenses for the three months ended September 30, 2016 increased \$0.1 million, or 1.0%, to \$11.0 million from \$10.9 million for the three months ended September 30, 2015.

Salaries and employee benefits expense increased \$0.5 million due to higher base salaries and payroll taxes and bonus accruals for management and support personnel.

General and administrative expense decreased \$0.4 million due to lower internal travel costs.

Nine Months Ended September 30, 2016 Compared to the Nine Months Ended September 30, 2015

Total revenue. Consolidated total revenue increased \$37.3 million, or 9.4%, to \$436.3 million in 2016 from \$399.0 million in 2015. The increase in total revenue was due primarily to the increase in revenue before reimbursements (net revenue).

Revenue before reimbursements (net revenue). Consolidated net revenue increased \$36.0 million, or 9.3%, to \$422.6 million for the nine months ended September 30, 2016 from \$386.6 million for the nine months ended September 30, 2015. Foreign exchange rate fluctuations decreased revenue by \$4.3 million, or 1.1%. Executive Search and Leadership Consulting net revenue was \$395.9 million, an increase of \$34.9 million compared to the nine months ended September 30, 2015. The

increase in Executive Search and Leadership Consulting net revenue is primarily due to our recent acquisitions, as well as growth in all practice groups except for the Education, Nonprofit & Social Enterprise practice group. Culture Shaping net revenue was \$26.7 million for the nine months ended September 30, 2016, an increase of \$1.0 million compared to the nine months ended September 30, 2015.

The number of Executive Search and Leadership Consulting consultants was 356 as of September 30, 2016 compared to 334 as of September 30, 2015, with our recent acquisitions contributing 23 consultants to 2016. Productivity, as measured by annualized net Executive Search and Leadership Consulting revenue per consultant was \$1.5 million for each of the nine months ended September 30, 2016 and 2015, respectively. Specific to Executive Search, our primary business, the number of confirmed searches increased 6% compared to the nine months ended September 30, 2015. The average revenue per executive search decreased to \$110,800 for the nine months ended September 30, 2016 compared to \$111,200 for the nine months ended September 30, 2015.

Salaries and employee benefits. Consolidated salaries and employee benefits expense increased \$23.1 million, or 8.7%, to \$288.0 million for the nine months ended September 30, 2016 from \$264.9 million for the nine months ended September 30, 2015. The decrease was primarily due to lower variable compensation partially offset by increased fixed compensation of \$24.7 million. Fixed compensation increased due to higher compensation related to our four recent acquisitions, new hires over the last year with incentives and minimum guarantees that are part of the consultant hiring process, \$5.2 million of investments in new and existing partners in our Culture Shaping business and severance related to the repositioning of the Leadership Consulting business. As a result of higher fixed compensation expense and an increase in the use of third-party consultants, whose costs are included in General and administrative expenses, variable compensation decreased \$1.6 million in the quarter reflecting the overall profitability of the business.

For the nine months ended September 30, 2016 we had an average of 1,721 employees compared to an average of 1,520 employees for the nine months ended September 30, 2015. Foreign exchange rate fluctuations decreased salaries and employee benefits expense by \$2.5 million, or approximately one percentage point.

As a percentage of net revenue, salaries and employee benefits expense was 68.2% for the nine months ended September 30, 2016 compared to 68.5% for the same period in the prior year.

General and administrative expenses. Consolidated general and administrative expenses increased \$14.1 million, or 15.1%, to \$107.0 million for the nine months ended September 30, 2016. The increase was due to ongoing general and administrative expenses related to our recent four acquisitions primarily from the use of third-party consultants in these businesses to execute work, the repositioning of our Leadership Consulting business of \$1.5 million, higher professional service fees supporting technology implementation and training and development fees, higher unbilled travel and business development expense, and an increase in technology subscription costs reflecting additional headcount throughout the business for cloud-based services.

Foreign exchange rate fluctuations decreased general and administrative expense by \$0.9 million, or approximately one percentage point.

As a percentage of net revenue, general and administrative expenses were 25.3% for the nine months ended September 30, 2016 compared to 24.0% for the nine months ended September 30, 2015.

Operating income. Consolidated operating income was \$27.6 million for the nine months ended September 30, 2016, compared to \$28.8 million for the nine months ended September 30, 2015. The net impacts of foreign exchange rate fluctuations reduced operating income by \$0.9 million.

Net non-operating income (expense). Net non-operating income was \$0.6 million for the nine months ended September 30, 2016, an increase of \$2.6 million from net non-operating expense of \$2.0 million for the nine months ended September 30, 2015.

Interest, net was \$0.2 million of income for the nine months ended September 30, 2016 compared to \$0.3 million of expense in 2015. Interest expense decreased \$0.5 million due the repayment of outstanding debt in the third quarter of 2015, which had been outstanding during the nine months ended September 30, 2015.

Other, net was income of \$0.4 million for the nine months ended September 30, 2016 and expense of \$1.7 million for the nine months ended September 30, 2015. Other, net increased due to lower net losses on available for sale securities compared to the prior year and decreased losses on the disposal of fixed assets.

Income taxes. See Note 12, Income Taxes.

Executive Search and Leadership Consulting

Americas

The Americas segment reported net revenue of \$237.6 million for the nine months ended September 30, 2016, an increase of 8.7%, from \$218.6 million for the nine months ended September 30, 2015. The increase in net revenue was driven by our DSI acquisition and growth in all practice groups except the Industrial practice group. Foreign exchange rate fluctuations reduced net revenue by less than one percentage point. The number of consultants within the Americas segment increased to 164 as of September 30, 2016 compared to 152 at September 30, 2015, with DSI and Philosophy IB each contributing three consultants to 2016.

Salaries and employee benefits expense increased \$8.9 million compared to the prior year. Fixed compensation increased \$10.8 million primarily due to higher base salaries and payroll taxes of \$3.7 million, higher minimum guarantees and sign-on bonuses of \$2.3 million and increased deferred compensation due to market fluctuations. Variable compensation decreased \$1.9 million due to lower bonus accruals.

General and administrative expense increased \$3.9 million primarily as a result of ongoing general and administrative expenses related to our recent acquisition of DSI and its use of third-party consultants to execute work, higher office occupancy costs and higher unbilled travel and business development cost.

The Americas region reported operating income of \$56.8 million for the nine months ended September 30, 2016, an increase of \$6.2 million compared to \$50.6 million for the nine months ended September 30, 2015.

Europe

The Europe segment reported net revenue of \$91.0 million for the nine months ended September 30, 2016, an increase of 30.6%, from \$69.7 million for the nine months ended September 30, 2015. All industry practice groups contributed to net revenue growth except for the Education, Nonprofit & Social Enterprise practice group. Contributing to this growth were the Company's acquisitions of Co Company in October 2015 and JCA Group in August 2016. Foreign exchange rate fluctuations reduced net revenue by approximately four percentage points. The number of consultants within the Europe segment increased to 103 as of September 30, 2016 compared to 91 at September 30, 2015, with Co Company and JCA Group contributing six and 11 consultants to 2016, respectively.

Salaries and employee benefits expense increased \$10.9 million from the nine months ended September 30, 2015. Fixed compensation increased \$8.0 million due to higher base salaries and payroll taxes of \$5.6 million primarily from merit increases, additional headcount related to the Co Company and JCA Group acquisitions, higher minimum guarantees of \$1.7 million and costs related to the repositioning of our Leadership Consulting business of \$0.6 million. Variable compensation increased \$3.0 million due to higher bonus accruals for consultant performance.

General and administrative expense increased \$9.0 million compared to the nine months ended September 30, 2015 primarily as a result of ongoing general and administrative expenses related to our recent acquisitions, including the use of third-party external consultants to execute work, \$1.5 million of costs associated with repositioning of our Leadership Consulting business and higher unbilled travel and business development cost.

The Europe segment reported operating income of \$2.4 million for the nine months ended September 30, 2016, an increase of \$1.4 million compared to the nine months ended September 30, 2015.

Asia Pacific

The Asia Pacific segment reported net revenue of \$67.3 million for the nine months ended September 30, 2016, a decrease of 7.4% from \$72.7 million for the nine months ended September 30, 2015. The decrease in net revenue was across all industry practice groups. Foreign exchange rate fluctuations reduced net revenue by less than one percentage point. The number of consultants within the Asia Pacific segment decreased to 89 as of September 30, 2016 as compared to 91 at September 30, 2015.

Salaries and employee benefits expense decreased \$2.9 million compared to the nine months ended September 30, 2015. The decrease in salaries and employee benefits expense is due to lower variable compensation of \$4.7 million from lower bonus accruals for consultant performance partially offset by an increase in fixed compensation \$1.8 million as a result of headcount increases and the timing of merit increases.

General and administrative expense increased \$0.5 million compared to the nine months ended September 30, 2015 primarily due to higher office occupancy expenses and higher unbilled travel and business development cost, partially offset by lower litigation expenses.

The Asia Pacific segment had operating income of \$5.2 million for the nine months ended September 30, 2016, a decrease of \$2.9 million from the prior year.

Culture Shaping

The Culture Shaping segment reported net revenue of \$26.7 million for the nine months ended September 30, 2016, an increase of 3.9% from \$25.7 million for the nine months ended September 30, 2015. The increase is the result of a higher volume of client work.

Salaries and employee benefits expense increased \$4.7 million compared to the nine months ended September 30, 2015 due to investments in new and existing consultants.

General and administrative expenses increased \$1.2 million compared to the nine months ended September 30, 2015 primarily due to third-party external consultant costs.

The Culture Shaping segment reported an operating loss of \$1.9 million for the nine months ended September 30, 2016, a decrease of \$4.9 million compared to \$2.9 million of operating income for the nine months ended September 30, 2015.

Global Operations Support

Global Operations Support expenses for the nine months ended September 30, 2016 increased \$1.1 million, or 3.2%, to \$34.9 million.

Salaries and employee benefits expense increased \$1.5 million due to additional stock-based compensation expense related to meeting the vesting requirements of the performance share awards for the chief executive officer.

General and administrative expense decreased \$0.4 million due to decreases in internal travel costs and office occupancy expenses that were partially offset by increased professional services.

Liquidity and Capital Resources

General. We continually evaluate our liquidity requirements, capital needs and availability of capital resources based on our operating needs. We believe that our available cash balances together with the funds expected to be generated from operations and funds available under our committed revolving credit facility will be sufficient to finance our operations for the foreseeable future, as well as to finance the cash payments associated with our cash dividends and stock repurchase program.

We pay the non-deferred portion of annual bonuses in the first quarter following the year in which they are earned. Employee bonuses are accrued throughout the year and are based on our performance and the performance of the individual employee.

Lines of credit. On June 30, 2015, we entered into a Second Amended and Restated Credit Agreement (the "Restated Credit Agreement"). The Restated Credit Agreement amended and restated the Credit Agreement executed on June 22, 2011 (the "Credit Agreement"). Pursuant to the Restated Credit Agreement, we replaced our Revolving Facility and

Term Facility (“Existing Facility”) with a single senior unsecured revolving line of credit with an aggregate commitment of up to \$100 million, which includes a sublimit of \$25 million for letters of credit, and a \$50 million expansion feature (the “Replacement Facility”). The Replacement Facility will mature on June 30, 2020. Borrowings under the Restated Credit Agreement bear interest at our election at the existing Alternate Base Rate (as defined in the Credit Agreement) or Adjusted LIBOR Rate (as defined in the Credit Agreement) plus a spread as determined by our leverage ratio. As of September 30, 2016, we did not have any borrowings outstanding under the Restated Credit Agreement.

We were in compliance with the financial and other covenants under the Restated Credit Agreement and no event of default existed.

Cash and cash equivalents. Cash and cash equivalents at September 30, 2016, December 31, 2015 and September 30, 2015 were \$100.0 million, \$190.5 million and \$129.0 million, respectively. The \$100.0 million of cash and cash equivalents at September 30, 2016 includes \$51.0 million held by our foreign subsidiaries. A portion of the \$51.0 million is considered permanently reinvested in these foreign subsidiaries. If these funds were required to satisfy obligations in the U.S., the

repatriation of these funds could cause us to incur additional U.S. income taxes or foreign withholding taxes. Any additional taxes could be offset, in part or in whole, by foreign tax credits. The amount of such taxes and application of tax credits would be dependent on the income tax laws and other circumstances at the time these amounts are repatriated. Based on these variables, it is not practicable to determine the income tax liability that might be incurred if these earnings were to be repatriated.

Cash flows used in operating activities. For the nine months ended September 30, 2016, cash used in operating activities was \$49.0 million. This use of cash was primarily the result of a reduction in accrued expenses due to cash bonus payments of \$145.0 million related to 2015 and prior year cash bonus deferrals with 2016 variable compensation accruals of \$101.0 million partially offsetting these payments, an increase in accounts receivable of \$33.3 million, the payment of \$6.5 million for the retention bonus paid to certain key executives related to the Senn Delaney acquisition and an increase in prepaid expenses of \$4.2 million. These uses of cash were partially offset by a net income of \$14.9 million, depreciation and amortization expense of \$11.7 million, stock compensation expense of \$5.1 million an increase in accounts payable of \$2.3 million and an increase in deferred revenue of \$1.3 million.

For the nine months ended September 30, 2015, cash used in operating activities was \$20.0 million, principally reflecting an increase in accounts receivable of \$40.6 million and a decrease in accrued expenses of \$5.4 million, partially offset by net income of \$15.9 million. The accrued expense decrease reflects approximately \$113 million of bonus payments for 2014 and prior year cash deferrals partially offset by 2015 bonus accruals of \$93.6 million.

Cash flows used in investing activities. Cash used in investing activities was \$24.5 million for the nine months ended September 30, 2016 primarily due to our recent acquisitions of JCA Group, DSI and Philosophy IB for \$14.9 million, \$9.0 million and \$6.0 million, respectively. This use of cash was partially offset by a reduction in restricted cash of \$7.2 million primarily due to a release of funds for the retention bonuses paid to certain key executives related to the Senn Delaney acquisition.

Cash used in investing activities was \$14.7 million for the nine months ended September 30, 2015 primarily due to capital expenditures of \$13.9 million and net purchases of available for sale securities of \$1.4 million. Capital expenditures primarily related to the office build out for our new Chicago office space.

Cash flows used in financing activities. Cash used in financing activities for the nine months ended September 30, 2016 was \$17.6 million primarily due to earnout payments for Senn Delaney, Scambler MacGregor and Co Company acquisitions of \$6.8 million, \$0.4 million and \$0.2 million, respectively, cash dividend payments of \$7.4 million and the payment of employee tax withholdings on equity transactions of \$2.7 million.

Cash used in financing activities for the nine months ended September 30, 2015 was \$43.8 million primarily due to debt repayments of \$29.5 million, cash dividend payments of \$7.5 million and earnout payments of \$5.5 million related to the Senn Delaney and Scambler MacGregor acquisitions.

Off-Balance Sheet Arrangements. We do not have material off-balance sheet arrangements, special purpose entities, trading activities of non-exchange traded contracts or transactions with related parties.

Application of Critical Accounting Policies and Estimates

Management's Discussion and Analysis of Financial Condition and Results of Operations is based upon our Condensed Consolidated Financial Statements, which have been prepared using accounting principles generally accepted in the United States of America. Our significant accounting policies are discussed in Note 2, Summary of Significant Accounting Policies, in the Notes to Consolidated Financial Statements included in our Annual Report on Form 10-K for the year ended December 31, 2015 as filed with the U.S. Securities and Exchange Commission ("SEC")

on March 10, 2016, and in Note 2, Summary of Significant Accounting Policies, in the Notes to Condensed Consolidated Financial Statements included in Item 1. The preparation of these financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue and expenses, and related disclosure of contingent assets and liabilities. Management bases its estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions. If actual amounts are ultimately different from previous estimates, the revisions are included in our results of operations for the period in which the actual amounts become known.

An accounting policy is deemed to be critical if it requires an accounting estimate to be made based on assumptions about matters that are highly uncertain at the time the estimate is made, and if different estimates that reasonably could have been used, or if changes in the accounting estimates that are reasonably likely to occur periodically, could materially impact the

financial statements. Management believes its critical accounting policies that reflect its more significant estimates and assumptions relate to revenue recognition, income taxes, interim effective tax rate and assessment of goodwill and other intangible assets for impairment. See Application of Critical Accounting Policies and Estimates in Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations included in our Annual Report on Form 10-K for the year ended December 31, 2015, as filed with the SEC on March 10, 2016.

Recently Issued Financial Accounting Standards

In August 2016, the Financial Accounting Standards Board ("FASB") issued accounting Standards Update ("ASU") No. 2016-15, Statement of Cash Flows: Classification of Certain Cash Receipts and Cash Payments, which is intended to reduce diversity in practice as to how certain cash receipts and cash payments should be presented and classified. The standard is effective for interim and annual reporting periods beginning after December 15, 2017 with early adoption permitted. The Company has evaluated the standard and noted the guidance for contingent consideration payments made after a business combination are applicable to the Condensed Consolidated Statements of Cash Flows. The Company currently classifies all contingent consideration payments as financing activities. The impact of this change is not expected to be significant to the classification of these activities on the Consolidated Statements of Cash Flows.

In March 2016, the FASB issued ASU No. 2016-09, Stock Compensation: Improvements to Employee Share-Based Payment Accounting, which is intended to simplify several aspects of the accounting for share-based payment transactions including the income tax accounting, classification of awards as either equity or liabilities, the accounting for forfeitures and classification on the statement of cash flows. The standard is effective for annual reporting periods beginning after December 15, 2016 with early adoption permitted. The Company is planning to early adopt this standard during the fourth quarter of 2016. The impact of this change is not expected to be significant to Condensed Consolidated Financial Statements.

In February 2016, the FASB issued ASU No. 2016-02, Leases, intended to improve financial reporting about leasing transactions. The new guidance will require entities that lease assets to recognize on their balance sheets the assets and liabilities for the rights and obligations created by those leases and to disclose key information about the leasing arrangements. ASU 2016-02 is effective for interim and annual periods beginning after December 15, 2018 with early adoption permitted. The guidance requires lessees and lessors to recognize and measure leases at the beginning of the earliest period presented using a modified retrospective approach. The Company is currently evaluating the impact of this accounting guidance. The effect is not known or reasonably estimable at this time.

In January 2016, the FASB issued ASU 2016-01, Financial Instruments: Recognition and Measurement of Financial Assets and Financial Liabilities, which addresses certain aspects of recognition, measurement, presentation and disclosure of financial instruments including the recognition of unrealized changes in fair value within net income. The standard is effective for annual reporting periods beginning after December 15, 2017. The Company is currently evaluating the impact of this accounting guidance. The effect is not known or reasonably estimable at this time.

In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers. The ASU requires that an entity recognizes revenue to depict the transfer of promised goods or services to customer in an amount that reflects the consideration to which the Company expects to be entitled in exchange for these goods or services. The effective date has been deferred for one year to the interim and annual reporting periods beginning after December 15, 2017. Early adoption is permitted as of the original effective date, which was interim and annual reporting periods beginning after December 15, 2016. The guidance permits the use of either of the following transition methods: (i) a full retrospective approach reflecting the application of the standard in each prior reporting period with the option to elect certain practical expedients or (ii) a retrospective approach with the cumulative effect upon initial adoption recognized at the date of adoption. The Company is currently evaluating the impact of this accounting guidance. The effect is not

known or reasonably estimable at this time.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Currency market risk. With our operations in the Americas, Europe and Asia Pacific, we conduct business using various currencies. Revenue earned in each country is generally matched with the associated expenses incurred, thereby reducing currency risk to earnings. However, because certain assets and liabilities are denominated in currencies other than the U.S. dollar, changes in currency rates may cause fluctuations in the valuation of such assets and liabilities. As the local currency of our subsidiaries has generally been designated as the functional currency, we are affected by the translation of foreign currency financial statements into U.S. dollars. A 10% change in the average exchange rate for currencies of all foreign countries in which we operate would have increased or decreased our net income for the nine months ended September 30, 2016 by \$0.4 million. For financial information by geographic segment, see Note 14, Segment Information, in the Notes to Condensed Consolidated Financial Statements.

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ITEM 4. CONTROLS AND PROCEDURES

(a) Evaluation of Disclosure Controls and Procedures

The Company maintains disclosure controls and procedures as defined in the Securities Exchange Act of 1934, as amended, (the "Exchange Act") Rule 13a-15(e) and 15d-15(e), that are designed to ensure that information required to be disclosed in the Company's reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission rules and forms, and that such information is accumulated and communicated to the Company's management, including its principal executive officer and principal financial officer, as appropriate, to allow timely decisions regarding required disclosure. Any system of controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives.

Management of the Company, with the participation of the principal executive officer and the principal financial officer, evaluated the effectiveness of the design and operation of the Company's disclosure controls and procedures as of September 30, 2016. Based on the evaluation, the Company's principal executive officer and principal financial officer concluded that the Company's disclosure controls and procedures were effective as of September 30, 2016.

(b) Changes in Internal Control Over Financial Reporting

There have been no changes in our internal control over financial reporting that occurred during the period covered by this Quarterly Report on Form 10-Q that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

The information presented in Note 16, Commitments and Contingencies, to our Condensed Consolidated Financial Statements within this Quarterly Report on Form 10-Q is incorporated herein by reference.

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Item 6. Exhibits

| Exhibit No. | Description |
|-------------|--|
| *31.1 | Certification of the Company's Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 |
| *31.2 | Certification of the Company's Executive Vice President and Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 |
| *32.1 | Certification of the Company's Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 |
| *32.2 | Certification of the Company's Executive Vice President and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 |
| *101.INS | XBRL Instance Document |
| *101.SCH | XBRL Taxonomy Extension Schema Document |
| *101.CAL | XBRL Taxonomy Calculation Linkbase Document |
| *101.DEF | XBRL Taxonomy Extension Definition Linkbase Document |
| *101.LAB | XBRL Taxonomy Extension Label Linkbase Document |
| *101.PRE | XBRL Taxonomy Extension Presentation Linkbase Document |

* Filed herewith.

SIGNATURE

Pursuant to the requirements of the Securities Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Date: October 26, 2016

Heidrick & Struggles International, Inc.
(Registrant)

/s/ Stephen A. Bondi
Stephen A. Bondi
Vice President, Controller