09-Nov-2022

Genpact Ltd. (G)

Q3 2022 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good day, ladies and gentlemen, welcome to the 2022 Third Quarter Genpact Limited Earnings Conference Call. My name is Michelle, and I will be your conference moderator today. At this time, all participants are in a listen-only mode. We will conduct a question-and-answer session toward the end of the conference call. As a reminder, this call is being recorded for replay purposes. The replay of the call will be archived and made available on the IR section of Genpact's website.

I would now like to turn the call over to Roger Sachs, Head of Investor Relations at Genpact. Please proceed.

Roger Sachs
Vice President-Investor Relations, Genpact Ltd.

Thank you, Michelle, and good afternoon, everybody, and welcome to our third quarter earnings call to discuss results for the period ended September 30, 2022. We hope you had a chance to review our earnings release, which was posted to the IR section of our website, genpact.com. Speakers on today's call are Tiger Tyagarajan, our President and CEO; and Mike Weiner, our Chief Financial Officer.

Today's agenda will be as follows. Tiger will provide an overview of our results and an update on our strategic initiatives. Mike will then walk you through our financial performance for the quarter as well as provide our current thoughts on our outlook for the full year 2022. Tiger will then come back for some closing remarks, and then we will take your questions. We expect the call to last roughly an hour.

Some of the matters we will discuss in today's call are forward looking and involve a number of risks, uncertainties, and other factors that could cause actual results to differ materially from those in such forward-looking statements. Such risks and uncertainties are set forth in our press release.

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In addition, during today's call, we will refer to certain non-GAAP financial measures that we believe provide additional information to enhance the understanding of the way management views the operating performance of our business. You can find a reconciliation of those measures to GAAP in today's earnings release posted to the IR section of our website.

And with that, let me turn the call over to Tiger.

N. V. Tyagarajan

President, Chief Executive Officer & Director, Genpact Ltd.

Thank you, Roger. Good afternoon, everyone, and thank you for joining us today for our third quarter 2022 earnings call. We delivered another quarter of solid results with revenue, adjusted operating income margin, and adjusted diluted EPS all in line with our expectations. Demand for both our Data-Tech-AI and Digital Operations services remained strong as we continue to help clients address pressing challenges around cost and productivity, growth, mitigating risk, and building long-term resiliency in their operating models. In these times, we believe the essential and nondiscretionary nature of most of our services makes us even more valuable to our clients.

Specifically during the third quarter of 2022, we delivered total revenue of $1.111 billion, up 12% on a constant currency basis. Data-Tech-AI services revenue of $510 million, up 21% on a constant currency basis. Digital Operations services revenue of $601 million, up 6% on a constant currency basis. Adjusted operating income margin of 17.1%, expanding 50 basis points year-over-year, and adjusted diluted earnings per share of $0.75, up 14% year-over-year.

Overall demand remained healthy as reflected in our high quality pipeline. We have a durable and resilient business model, primarily made up of annuity like revenue streams derived from designing, building, transforming and running mission-critical operations for our clients across our chosen set of industry segments.

Given the unprecedented macro environment, many clients are behaving cautiously. We have seen some multi-stage, large scale transformational deals being broken up into medium-sized deals that deliver faster payback and return on investment. At the same time, we have seen a dramatic increase in the importance of driving cost agendas across all industry segments we serve.

What many clients are doing is finding ways to preserve strategic long-term transformational programs and funding them through aggressive cost initiatives in which we are often their partner. As a result, bookings in the quarter were supported by higher levels of medium and small deals, with approximately two-thirds of the total being annuity-based and almost half sole-sourced, all very consistent with the past many quarters.

We have several large engagements progressing through the latter stages of our pipeline across all three of our industry segments, and there's a good line of sight for some of these to close before the year end. I'm also excited that we continue to win new logos and added 34 for this quarter, compared to an average of 29 during the last 12-month period through June 30 of this year. Many of these start as initial Data-Tech-AI relationships, that

then set the stage to expand the engagement beyond the initial scope with the range of services we have that are relevant for a variety of challenges our clients face today.

Total revenue for the quarter was up 12% year-over-year on a constant currency basis, and growth was broad-based across all of our industry segments. In particular, financial services and hi-tech and manufacturing services

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continued to deliver strong double-digit growth. Data-Tech-AI services, where we design, build solutions to transform our clients' businesses, grew 21% year-over-year on a constant currency basis.

Performance was driven by the ongoing momentum in our emerging services, including supply chain management, sales and commercial, and risk. That was once again up more than 25% during the quarter. Digital operation services, where we digitally transform and run our clients' operations globally, delivered another quarter of steady growth, increasing 6% year-over-year on a constant currency basis.

During the quarter, we continue to execute on the strategic initiatives we outlined at our June Investor Day. We are positioning ourselves to achieve our long-term financial goals of driving 10% plus organic top line revenue growth and expanding profitability at a more meaningful pace than historical levels through 2026.

Let me share a few highlights of our progress. First, revenue from our priority accounts grew 14% year-over-year and represents 65% of total revenue. We are disproportionately investing in these accounts that are undertaking significant transformation journeys. We see many opportunities that interlink multiple areas to drive meaningful outcomes for them.

For instance, finance and accounting with supply chain or financial risk and crimes with customer service. In these engagements, we are reimagining processes connected to multiple buying centers that drive holistic change throughout an entire organization.

For example, we helped a large global technology company diversify their semiconductor supplier base to build long-term supply chain resilience. Leveraging digital and analytics, we improved their supply and demand forecasting, enabled global inventory analysis, and spot price forecasting to optimize timing of purchases. We're now expanding our relationship into a long-term digital operations deal, where we will run their demand planning operations for all new growth opportunities.

Second, outcome and consumption-based commercial models now represent 12% of total revenue on our path towards 20% by 2026. These constructs align to outcomes and performance targets to deliver more value for clients and allow us to expand our relationships, particularly with our priority accounts. Interestingly, they also tend to have higher margins, given that they have a risk/reward construct.

And third, we are sharpening our focus and better deploying our resources, capital and leadership bandwidth to areas where we see our best long-term opportunities. As such, we are progressing with our plans to divest a small business we designated as held for sale last quarter.

We participate in a growth market that continues to be underpenetrated and is expected to further expand over time. The current macro environment creates opportunities for us as we help our clients navigate a rapidly changing landscape with cost considerations at the forefront. We are seeing this with new clients who have become more open to partnerships for the first time to change and transform themselves in response to this uncertain environment. Over the past six months, we have added 64 new logos, including nine who are new buyers for our kinds of services, with several of those deals greater than $5 million.

We're also seeing existing relationships that started out with Data-Tech-AI transformation utilizing our emerging services now looking for cost transformation leveraging our foundational services in areas such as procurement, finance and accounting, insurance and banking back office operations. Many of these expanded engagements are sole-sourced deals that we won because of our domain and process depth across our chosen verticals. Let me share a couple of examples that demonstrate these trends.

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We are partnering with a European pharmaceutical client, a first-time outsourcer, to help digitally transform their back office to support future growth, lower costs and drive better outcomes such as cost and cash flows. We are designing and implementing and will be running finance and accounting and IT services leveraging digital technologies such as Genpact Cora, robotic process automation, as well as implementing ServiceNow as a common business workflow platform. This represents a great example of a new relationship that have significant opportunities to become a priority account given their anticipated rapid growth.

Next, for a large industrial and manufacturing client, the success of our recent Data-Tech-AI supply chain transformation, improving demand forecasting and supply planning has positioned us for a sole source long-term digital operations transformation deal of their sourcing and procurement operations to drive savings in their total spend. These dynamics are helping expand the size of many of our relationships.

During the 12-month period ending September 30, 2022, we grew the number of relationships with annual revenue over $5 million from 143 to 158. Clients with more than $25 million in annual revenue increased from 27 to 34. Clients with more than $50 million in revenue increased from 11 to 14. We saw a decrease in our quarterly attrition to 36% versus the 38% percent reported last quarter.

While too early to say that we are on a path to a more normalized level, our attrition rate improved in each successive month during the quarter and has continued to decline throughout October. The majority of our attrition continues to be concentrated at the lower end of our organizational pyramid, where we are able to quickly fill roles to meet demand. As discussed last quarter, our attrition rate includes all employees who leave the company regardless of tenure or reason.

Adjusting for both involuntary attrition as well as employees with less than three months of service, our third quarter attrition would have been 33%. During the quarter, we welcomed more than 14,000 new team members across the globe. As our purpose, the relentless pursuit of a world that works better for people, and our values, combined with a strong opportunity to learn and grow one's career, continues to attract great talent at all levels in a competitive market.

Additionally, leveraging our internal redeployment platform, Talent Match, we've successfully redeployed over 6,000 reskilled employees to support the changing needs of our clients. During the quarter, our employees completed approximately 2.3 million training hours, leveraging our online demand Genome learning platform. This includes our proprietary data and analytics certification program that is available to all our global team members to develop their expertise to generate critical insights from our vast operating data set. This unique program continues to be a differentiator for us, and was recently recognized at the NASSCOM Business Innovation Showcase for the ability to rapidly provide upskill and cross-skill training.

We have found that team members who are active on Genome, and employees who take advantage of opportunities to change roles internally, have at least 50% lower attrition rate than the company average. This is a competitive advantage that we bring to our clients, particularly in today's macro environment, given our clients themselves are struggling to find the right talent.

Throughout the year, we've actively been engaging with clients to help offset the impact of wage pressure and higher than normal attrition, from a combination of off-cycle pricing adjustments and implementing non-FTE commercial models. We've made good progress on this initiative, meeting our initial target set out earlier in the year.

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Our year-to-date performance highlights the resilience of our business model and durable competitive advantage in the market. We believe the investments we made and our strategic choices over the years position us well to help clients navigate the many challenges in the macro environment. The combination of deep domain and process expertise with digital technologies and analytics is even more relevant in these times to create lasting value for clients. At the core of this is our agility and nimbleness, which allows us to take these different services to our clients to partner with them at speed and scale.

With that, let me turn the call over to Mike.

Michael Weiner

Chief Financial Officer, Genpact Ltd.

Thank you, Tiger, and good afternoon, everybody. Today I'll review our third quarter results and update you on our full year 2022 financial outlook.

Total revenue was $1.111 billion, up 9% year-over-year, or 12% on a constant currency basis and in line with our expectations. Data-Tech-AI services revenue, which represents 46% of our total revenue, increased 19% year-over-year, or 21% on a constant currency basis, largely driven by continued growth in our cloud-based data and analytics solutions across our focused areas, including supply chain, sales and commercial, and risk services. Digital Operations services revenue, which represents 54% of total revenue, increased 2% year-over-year, or 6% on a constant currency basis, primarily due to deal ramps from existing and recent wins.

From a vertical perspective, financial services increased 18% year-over-year, largely due to continued strong demand for our risk management services from both traditional banks and fintechs leveraging data and analytics. Consumer and healthcare increased 6% year-over-year, largely driven by Data-Tech-AI, sales and commercial, and supply chain engagements. And our high tech in manufacturing increased 16%, primarily driven by sales and commercial, supply chain, and finance and accounting engagements with both new and existing clients.

As Tiger mentioned earlier, we're progressing with our plan to divest the business that we designated for held for sale in the second quarter of this year. As reflected in the other operating expense line in our third quarter P&L, we recorded a $21 million pre-tax charge reflecting the expected net realizable value of this business.

Adjusted operating income margin expanded 50 basis points year-over-year to 17.1%, largely due to growth related to operating leverage and the impact of our recent cost containment initiatives. Our performance for the quarter includes the impact from classifying the non-strategic business held for sale and excluding the charge that I referred to a moment ago.

Gross margins for the third quarter declined 20 basis points year-over-year to 35.4%; however, increased 100 basis points sequentially from the second quarter. This sequential quarter-on-quarter expansion was largely due to better utilization from ongoing demand of our Data-Tech-AI services and the benefit of off-cycle pricing adjustments. As a reminder, gross margin in the second quarter included a negative 80 basis point impact from restructuring costs related to strategic actions we took in that period.

SG&A as a percentage of revenue was 20.8%, down 50 basis points year-over-year, largely due to G&A leverage. Adjusted EPS was $0.75, up 14% year-over-year, from $0.65 in the third quarter of last year. This $0.10 increase was primarily driven by higher adjusted operating income of $0.08, the impact of lower outstanding shares of $0.02, and $0.01 related to higher FX remeasurement gains recorded in the quarter compared to the same period last year, partially offset by higher net interest expense and taxes of $0.02. Our effective tax rate was

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20.8%, compared to 17.3% last year. The increase was primarily due to the mix of lower benefits recorded in the current year.

Turning to our cash flow and our balance sheet, during the quarter, we generated $226 million of cash from operations. That compared to $210 million from the same period last year. The increase was primarily driven by higher adjusted operating income margin and a sequential improvement in DSOs to 81 days from 84 days in the second quarter. We now believe we will exit this year with DSOs in the low-80 range, instead of our early expectations in the high-70s, given clients' cash management practices as interest rates remain elevated.

Overall credit quality of our portfolio continues to be very strong and unchanged. Cash and cash equivalents totaled $519 million, compared to $460 million at the end of the second quarter of 2022. Our net debt to EBITDA ratio for the last four rolling quarters was 1.5 times. With undrawn debt capacity, existing cash balances, we continue to have ample liquidity to pursue growth opportunities and execute on our capital allocation strategy. We continue to expect our net debt to EBITDA ratio will remain in our preferred range of 1 time to 2 times.

Given the current market environment, we're pleased that almost 80% of our total debt is fixed rate. During the quarter, we continued on our program of a more regular cadence of share repurchases and bought back approximately 627,000 shares for a total cost of $30 million at an average price per share of $47.86. We also paid out dividends totaling $23 million.

Through the end of the third quarter, we repurchased more than $180 million of shares, which is in line with the expectations we set forth for the full year 2022 that we discussed earlier this year.

Capital expenditures, as a percentage of revenue, was approximately 1% in the quarter. And we now expect this percentage to be 1% to 1.5% for full year 2022, due to the more effective use of a hybrid delivery model. Going forward, we anticipate returning to a more normal level of 1% to 2% related to expansion of our facilities in various geographies.

Now, let me turn to the full-year outlook. Given the continued strength of the US dollar, we now expect total revenue to be between $4.320 billion and $4.355 billion, representing reported year-over-year growth of 7.5% to 8.5%. This incorporates an incremental currency headwind of $15 million, more than we provided in our update on full-year outlook last quarter. This also includes $21 million of the expected revenue associated with the business held for sale, down from $28 million. We now expect total revenue to be between 10% and 11% on a constant currency basis, compared to our [prior] full-year outlook of 9.5% to 11%.

We continue to expect our full year 2022 operating income margins to be towards the high end of our range of 16% to 16.5%. We now expect adjusted earnings per share for full-year 2022 to be between $2.69 and $2.74, compared to our [prior] outlook of $2.68 to $2.74. This updated outlook takes into account the incremental currency headwind impact at the top end of our revenue outlook and slightly higher net interest expense, offset by higher year-to-date below the line FX re-measurement gains.

Lastly, given our revised DSO outlook, we now expect to generate full year cash flow from operations closer to $450 million. This lower cash flows expectation is not related to a business slowdown as overall demand remains strong.

With that, let me turn the call back over to Tiger.

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N. V. Tyagarajan

President, Chief Executive Officer & Director, Genpact Ltd.

Thank you, Mike. The capabilities we built organically and through targeted acquisitions continue to resonate in the marketplace, and our own agility enables us to quickly meet the changing needs of our clients. This is reflected in our year-to-date performance.

One of the most interesting things we are seeing is that clients increasingly want to leverage their data across their organizations to build more meaningful insights and predictions that are then used for actions to deliver improved outcomes. More than 50,000 people in our Digital Operations team have completed their data reskilling program and are building prediction models to drive better outcomes for our clients.

A few examples include: in financial services, predicting a consumer's propensity to pay; in consumer and healthcare, predicting demand at various price and promotion points; and in manufacturing and high-tech, predicting customer satisfaction, driving better renewal rates for maintenance and SaaS products.

We continue to be recognized for our commitment to ESG initiatives and are thrilled to have recently been named for the second year in a row to the Forbes List of World's Best Employers. We were also recognized again by Forbes as one of America's Best Employers for Veterans and acknowledged as an exemplar of inclusion in the Most Inclusive Companies Index.

Against the backdrop of the current macroeconomic environment, I want to thank [our] more than 110,000 global team members for their continued commitment to drive value for our clients, communities, and shareholders. Your tenacity, resilience, and ability to meet new challenges head on is the key to our long-term success.

With that, let me turn the call back to Roger.

Roger Sachs

Vice President-Investor Relations, Genpact Ltd.

Thank you, Tiger. We'd now like to open up our call for your questions. Michelle, can you please provide the instructions?

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QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] And our first question comes from the line of David Koning with R.W. Baird. Your line is open. Please go ahead.

David John Koning
Analyst, Robert W. Baird & Co., Inc. Q

Yeah. Hey, guys. Nice job again this quarter.

N. V. Tyagarajan
President, Chief Executive Officer & Director, Genpact Ltd. A

Thank you, David.

Michael Weiner
Chief Financial Officer, Genpact Ltd. A

Thanks.

David John Koning
Analyst, Robert W. Baird & Co., Inc. Q

Yeah. Yeah, good. Thanks. And, yeah, maybe just as my question or my first question, year-to-date revenue has been very good, I think constant currency about 13%. But the full year, now you're saying 11% for the full year. And if we kind of back into Q4, it seems like mid-single digits or so constant currency. And is that – is there anything really driving that? I know you said there's some breaking up into smaller pieces of some of the deals, but maybe talk through a little bit of that, if I'm thinking of that right.

N. V. Tyagarajan
President, Chief Executive Officer & Director, Genpact Ltd. A

Yeah, it's also a great question, David, and let me start off by saying that, overall, the quality of our pipeline remains really good. What we have been seeing, and we talked about this the prior quarter and we continue to see this, is large transformational deals. I think clients are breaking them down into a phased approach, primarily driven by I want faster payback and I want speed, which is actually interestingly good news, which is why the smaller and medium deals are – the cycle times on those continue to be really good.

As it relates to larger deals, particularly from first-time outsourcers, they are taking longer. It requires buying from many more people. People are much more careful about payback and time and when do you pull the trigger, and we are seeing that play through in a very interesting way through our pipeline as we navigate this. But as I said, many of those are getting broken up into medium-sized deals and those are moving forward very nicely.

We also saw a churn in our pipeline on Data-Tech-AI from growth-related agenda to cost-related agenda. And we've seen that, by the way, across all industry segments. Very quickly, customers are refocusing back on costs, and that has generated a new set of pipeline, fresh, while some of the growth agenda has gone a little bit slower. So that churn slows down as we cycle through in our pipeline and then go back into the races.

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David John Koning
Analyst, Robert W. Baird & Co., Inc.

Q

Got you. No, thanks for that. And does the pipeline suggest right now anything different as we kind of look into next year? I mean, does it feel right now like it would support a pretty normalized year in both segments, or is that a little early to tell, and the churn makes it a little tougher than usual to tell?

N. V. Tyagarajan
President, Chief Executive Officer & Director, Genpact Ltd.

A

Yeah. So, David, I think in – under normal conditions out of that, it's too early to tell. Under the conditions of the current world, I would certainly say it's too early to tell. So, I think we've got – by the time we get to the first quarter in February, when we announce the full-year results and we talk about our full-year outlook for 2023, I think we'll have much better visibility. I think we'll have – the world will have much better visibility. We are in the process as usual of building that up grounds up in terms of a total plan, client by client, particularly starting with our priority clients. Mike, do you want to add anything to that?

Michael Weiner
Chief Financial Officer, Genpact Ltd.

A

Yeah. Building on what you said earlier, Tiger, two things. One is that we are seeing a notable pivot in our Data-Tech-AI business as Tiger alluded to, from more of a growth agenda to a cost agenda, which makes complete sense with macroeconomic environment. And keep in mind, at any given time, we have about 70% visibility on a rolling basis into our forecast, right?

So layering that on top, we'll roll up. We're doing our strategic planning for next year on an account by account level basis. We'll have more color on that. And so, we've laid out our blueprint 2026 or our long-term strategy for the organization, which really has us targeting about 10% growth year-on-year. And in any given year could be higher; this year, we're guiding between 10% and 11%, so by definition will be a little bit higher. Potentially next year could be lower or higher. So we'll have a little bit more clarity on that. But nothing marketable to pull from, from what you're seeing in the fourth quarter, building that guidance from year-to-date 3Q to the full year.

N. V. Tyagarajan
President, Chief Executive Officer & Director, Genpact Ltd.

A

Yeah.

David John Koning
Analyst, Robert W. Baird & Co., Inc.

Q

Yeah.

N. V. Tyagarajan
President, Chief Executive Officer & Director, Genpact Ltd.

A

Yeah. And just to round that up, David, because it is probably a very important question in the markets we are in, to round that up, I mean, clearly, what we've shown historically is that as the world goes through what one can call a macro down cycle, whether the global financial crisis or the pandemic, we weather that really well. While overall growth may have come down across the board for everyone including us, the relative difference for us was our strength, because we did not come down the way others did. And that is a reflection of the type of services we provide, as well as the diversity and the kind of clients that we work with. So, we can really feel good about that.

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The overall environment will play itself out over the next few months, and I think a lot better visibility by the time we get to February.

David John Koning
Analyst, Robert W. Baird & Co., Inc.

Q

Got you. Well, thanks, guys. Nice job.

N. V. Tyagarajan
President, Chief Executive Officer & Director, Genpact Ltd.

A

Thank you, David.

Operator: Thank you. And one moment for our next question. Our next question comes from the line of Bradley Clark with BMO. Your line is open. Please go ahead.

Bradley Clark
Analyst, BMO Capital Markets Corp.

Q

All right. Thank you for taking my question, and nice results. I wanted to follow up on the cash flow commentary about the increasing DSO. Clients are preserving cash, et cetera, during a higher interest rate environment. And I just want to understand how this evolves, and what can Genpact do to perhaps minimize some of the impact of longer cash payments? And how much specifically are you working with your customers to get the best outcome for both parties? Just want to understand how this dynamic is playing out more. Thank you.

Michael Weiner
Chief Financial Officer, Genpact Ltd.

A

Yes. Well, let me take it off here, and then [indiscernible] (00:31:05) to add on anybody. So essentially what's going on is that we are reverting to a more normal DSO pattern that we had historically. We had a number of clients essentially prepay us or pay us early, right, which drove that down and exacerbated our cash flow. So when we gave out our original set of guidance, we built upon that model.

We saw a marketable turn in that behavior probably between the first and the second quarter as people became a lot more mindful of cash flow management. So what we're seeing right now is more of a reverting back to historical mean. Well, as far as working with our clients, all of our agreements have collection days, T minus 30, 60, 90, and we'll work with them for payments from that perspective. But fundamentally, the way I kind of think about it from a rolling five-quarter basis, we'll be back to where we are. But more interestingly that I focus on is credit quality of that collection, which has just been phenomenal. It doesn't keep me up at night at all regarding that.

N. V. Tyagarajan
President, Chief Executive Officer & Director, Genpact Ltd.

A

Yeah. I think the key to note there to what Mike said is that this is a reversion back to the mean of our DSOs, which has always been the case pre-pandemic. We got some benefits actually through the pandemic on the DSOs coming down. That benefit has been given back as we have navigated through this year.

Bradley Clark
Analyst, BMO Capital Markets Corp.

Q

Great. Appreciate the clarification. Thank you.

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N. V. Tyagarajan
President, Chief Executive Officer & Director, Genpact Ltd.

A

Thank you, Bradley.

Operator: Thank you. And one moment for our next question. Our next question comes from the line of Maggie Nolan with William Blair. Your line is open. Please go ahead.

Kate Kronstein
Analyst, William Blair

Q

Hi. This is Kate Kronstein on for Maggie. I wanted to quickly ask about the improvement in attrition levels, and if you could – guys could kind of dive into what has driven that improvement, and if you think it's sustainable in the long term.

N. V. Tyagarajan
President, Chief Executive Officer & Director, Genpact Ltd.

A

Yeah. I think I'll start by saying that the macro has a role to play here. We did say that the macro is beginning to change, and we talked about it last quarter. And as whether it is in the US, in Europe, in Philippines, in India, the reality is that as a number of large enterprises, as well as startups in the various technology and data and analytics arenas, have slowed down their own hiring, not to talk about some companies that have announced layoffs, I think we expected attrition levels to come down or start coming down.

As I said in my prepared remarks, I don't think we should declare victory in a hurry. We've seen the attrition level come down across the board, all geographies, all kinds of skills, and all levels. They are still higher than pre-pandemic levels. So if we were to play this forward, one would expect attrition to continue to come down going into the next few quarters, if the world continues to go through the cycle it's going through right now.

So we've been doing all the right things around talent, talent match, reskilling, making sure that our employees get great opportunities to add value to clients and learn. And those practices are things that we've always been proud of. But there's no question that the macro has changed in the last 90 to 120 days.

Kate Kronstein
Analyst, William Blair

Q

Okay, great. Thank you. That's really helpful color. And then, I have one quick follow-up. Has automation been in higher demand given the current macro right now? And if so, is that impacting the number of full-time employees that you're able to deploy on clients?

N. V. Tyagarajan
President, Chief Executive Officer & Director, Genpact Ltd.

A

If I understood the question right, I guess you're saying, is there a higher demand for automation? Did I get that question right? And is that impacting the demand for talent? Did I get that right, the question?

Kate Kronstein
Analyst, William Blair

Q

Yeah. Yes.

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N. V. Tyagarajan
President, Chief Executive Officer & Director, Genpact Ltd.

A

Yeah. So I would say – I mean there's been a secular demand for digital transformation that, not just us, but everyone in our industry has called out, in fact every one of our clients has spoken about, that got further accelerated through the pandemic. And that included robotic process automation, deploying AI and machine learning technologies, workflows on the cloud, migrating technologies and processes to the cloud. And that journey continues with our clients.

In my prepared remarks, I talked about the desire for a number of our clients to preserve some of their strategic transformation journeys. I would call out digital transformation as one of those areas that they want to preserve. And the way they do that is by further driving cost improvement, productivity and efficiency in various other parts of the business, sometimes by actually further accelerating automation in those parts.

So all of this ends up being a tailwind for our business because when clients undertake those journeys, they want scale, they want expertise, and they want speed. As a partner, we bring scale, we bring expertise, we bring speed. And actually, overall, it's great for our talent. And our talent is constantly being reskilled in both digital technologies as well as data and analytics to be able to provide that for our clients.

Kate Kronstein
Analyst, William Blair

Q

Okay, great. Thank you. And congrats on a nice quarter.

N. V. Tyagarajan
President, Chief Executive Officer & Director, Genpact Ltd.

A

Thank you very much.

Operator: Thank you. And one moment for our next question. And our next question comes from the line of Bryan Bergin with Cowen. Your line is open. Please go ahead.

Zack Ajzenman
Analyst, Cowen Inc.

Q

Hi. Thanks. This is Zack Ajzenman on for Bryan. Looking to dig further into the underlying dynamics of the implied 4Q guide, can we peel back the Data-Tech-AI segment a bit more just looking for insight into which specific areas cater to growth initiatives versus the areas that are more cost-focused? And can you give us a sense of the high level mix of the growth bucket versus the cost-focused bucket?

N. V. Tyagarajan
President, Chief Executive Officer & Director, Genpact Ltd.

A

Yeah. I'd start by saying if you look at the Data-Tech-AI world, let's pick three emerging services that we called out both on Investor Day and on subsequent calls that we've done: supply chain, sales and commercial, and risk. And we can look at all three of them and have a conversation of how each of those have services and solutions that are pivoted on driving growth for our customers, as well as other services and solutions in those same arena that are pivoted on cost of the agenda.

Let's take supply chain. I mean, clearly, there still is a significant demand for improving supply chain in a situation where geopolitics, transportation, energy costs and availability of raw materials. Let's just take those four topics,

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create supply chain challenges for all manufacturing companies and consumer goods retail and life sciences companies. And in that environment, two things is what clients are looking for. How do I optimize my supply chain in order to drive lower cost of transportation in a high energy, high transportation cost environment and in a inflationary raw material environment? Now, you flip that to how do I make sure that I have the right product available in the shelf with my customers by optimizing my supply chain in an environment where demand is highly volatile, and therefore my ability to forecast demand and navigate supply in order for products to be available allows me to drive growth in my agenda. So, there's a balance in supply chain on which agenda is more important, and you'll see the importance of cost rise up.

From six months back, most of the conversations were about fulfillment and market share and customer satisfaction in supply chain. And I can articulate a similar story on sales and commercial and on risk where it's a balance or kind of solution, some focused on cost, some focused on growth, and we are seeing a rise of the cost agenda in all three arenas.

Zack Ajzenman
Analyst, Cowen Inc.

Q

Okay. Thanks. And a follow-up on the operating margins here. Can you discuss the progress in getting contracting and pricing where it needs to be? It sounds like there's been some nice improvement here that helps you hold the 16.5% calendar 2022 guide. But curious how this informs the calendar 2023 setup, any considerations to be mindful of that can change the starting point for the adjusted operating margin next year or did the base expectation to build off of 16.5% remain?

Michael Weiner
Chief Financial Officer, Genpact Ltd.

A

Yeah. Let me kind of kick them off. I think the base remains as we alluded to a year or so ago, that we are going to work through this year, right? Work diligently to get what we consider the off cycle pricing adjustments, working in concert with our clients to provide value on both sides of that and get that more in line with what our inflationary cost structure was for the year. I think I can successfully report back if we did that.

We said at that time the natural trajectory of the business would be to linearly move towards 16.5%, and we're in that process. And we'd like you to build all of your models or how everyone thinks about the business in 2023 off of that 16.5% with an expanding margin. What that might be? I don't know. But we'll have the inherent operating leverage of the business of just being a bigger player as well as the benefit of all the actions that we've taken. So what we said nine months ago was really playing out quite well. We've got a lot of fits and starts and deviations in the macroeconomic environment but that's where we are this point.

Zack Ajzenman
Analyst, Cowen Inc.

Q

Great. Thank you.

Operator: Thank you.

N. V. Tyagarajan
President, Chief Executive Officer & Director, Genpact Ltd.

A

Thank you.

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Operator: [Operator Instructions] One moment for our next question. Our next question comes from the line of Bryan Keane with Deutsche Bank. Your line is open. Please go ahead.

Bryan C. Keane
Analyst, Deutsche Bank Securities, Inc.

Q

Hi, guys. Congrats on the quarter. When I look at the quarter, it's incredibly solid 12% constant currency growth, that was well ahead of our estimates and consensus. But I'm still trying to understand the fourth quarter guide that that's quite a bit lower in that kind of that mid-single-digit range. How much of that is macro the fourth quarter guide? How much of that is conservatism on your part? And I heard a little bit about the growth versus cost and some payback cycles, but I'm just trying to figure out the lower guide. What is that resulting from exactly if you can quantify it?

N. V. Tyagarajan
President, Chief Executive Officer & Director, Genpact Ltd.

A

Yeah, I'll start off...

Michael Weiner
Chief Financial Officer, Genpact Ltd.

A

I'll kick this off and – oh, go ahead, Tiger.

N. V. Tyagarajan
President, Chief Executive Officer & Director, Genpact Ltd.

A

Go ahead. Go ahead. No, go ahead. Go head. Go ahead.

Michael Weiner
Chief Financial Officer, Genpact Ltd.

A

No, I was just going to say let's be mindful of the comp on a year-over-year basis to start with, right? So ostensibly we had a very, very strong fourth quarter last year with some Data-Tech-AI license sales, that type of thing, which were wonderful. But it certainly made for a tough year-over-year comp. And again, maybe – Tiger, I don't know, if you want to build upon that with this. But the point of cost versus growth agenda and what we're seeing kind of sitting where we are now in November 9 and our predictability in the next six, seven weeks.

Bryan C. Keane
Analyst, Deutsche Bank Securities, Inc.

Q

Got it. Got it.

N. V. Tyagarajan
President, Chief Executive Officer & Director, Genpact Ltd.

A

Bryan – and Bryan, just to add to what Mike said, and thank you for your compliments. Appreciate that. We – I'll start-off by saying we do feel really good about our year-to-date results through the three quarters where overall across the three quarters we have exceeded our own expectations that we had of the three quarters. Now, in that three-quarter period, we clearly must recognize that the world around us has changed. Our clients have become more cautious. They have, in many instances, grabbed onto topics that they hadn't grappled with until three or four months back, which is I need to resize my own business, I need to announce a little bit of layoffs here, I need to cut back on investment in this particular business or that geography.

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As they go through that, typically, in these cycles, we see a little bit of a pause in big decision-making, particularly as it relates to bigger deals and bigger transmission agendas, and that takes a quarter or so to settle down. We recognize that. We see that. We feel that, particularly in our larger deals decision-making taking longer because more people are being asked to sign off within a client a client environment. And I think we are just being very realistic. I wouldn't say we are being conservative, I just think they are being realistic about our view about the balance of the year. And we feel really good that we will end the year with having met all the expectations. In fact, getting to the higher end of all our expectations that we set out at the beginning of the year. And the world has changed through these last 12 months.

So, yeah, it is a recognition of what our clients are going through. And they are also churning their most important agendas from, A and saying actually A is not that important, let's do B. When that churn happens, it takes a little bit of our extra cycle time to actually make that churn happen. Good news is we have solutions for the original agenda that we had, and we have the solutions for the new agenda we have.

Bryan C. Keane
Analyst, Deutsche Bank Securities, Inc.

Q

Yeah. And I thought it was encouraging that the new logos is jumping a little bit so that – that you're actually getting new business for some of the people looking for more help on the cost side of things.

N. V. Tyagarajan
President, Chief Executive Officer & Director, Genpact Ltd.

A

That's right, Bryan. And one of the good things about that is it actually sets up for a much longer term growth with some of those becoming priority accounts. A couple of years from now, I'm absolutely convinced that many of those will be priority account for us.

Bryan C. Keane
Analyst, Deutsche Bank Securities, Inc.

Q

Okay. Helpful. Thanks for the color.

N. V. Tyagarajan
President, Chief Executive Officer & Director, Genpact Ltd.

A

Thank you, Bryan.

Operator: Thank you. And I'm showing no further questions at this time. And I'd like to hand the conference back over to Roger Sachs for any further remarks.

Roger Sachs
Vice President-Investor Relations, Genpact Ltd.

Thank you everybody for joining us today. And we look forward to speaking to you again next quarter.

Operator: This concludes today's program. You can all disconnect. Everyone, have a great day.

***Editor's note: Texts in square brackets are inserted at the request of the company for added clarity to the speaker's statements.

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