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EDITED TRANSCRIPT

G.N - Q1 2021 Genpact Ltd Earnings Call

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OVERVIEW:

Co. reported 1Q21 total revenue of $946m and adjusted diluted EPS of $0.59. Expects 2021 total revenue to be $3.93-3.99b and adjusted diluted EPS to be $2.27-2.30.

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PRESENTATION

Operator

Good day, ladies and gentlemen. Welcome to the 2021 First Quarter Genpact Limited Earnings Conference Call. My name is RJ, and I will be your conference moderator for today. (Operator Instructions)

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 - *Genpact Limited - Head of IR*

Thank you, R.J., and good afternoon, everybody, and welcome to Genpact's call to discuss our results for the first quarter ended March 31, 2021. We hope you've 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 Ed Fitzpatrick, 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. Ed will then walk you through our financial performance for the quarter as well as provide some thoughts on our outlook for 2021. Tiger will then come back for some closing comments, and then we will take your questions. We expect our call to last about 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.

In addition, during our call today, 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 these 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.

Nallicheri Vaidyanathan Tyagarajan - *Genpact Limited - President, CEO & Director*

Thank you, Roger. Good afternoon, everyone, and thank you for joining us today for our first quarter 2021 earnings call. We had a strong start to the year with first quarter revenue, adjusted operating income margin, adjusted diluted EPS and cash flow, all exceeding our expectations.

I'm pleased with the continued momentum we are seeing across our business. The growing need of enterprises to leverage digital technologies and cloud-based analytics is creating a high demand for our solutions. We are increasingly engaging with clients on large-scale holistic transformations to reimagine their business models and redesign their operations. These operations straddle multiple functions and buying centers opening new parts of our expanding addressable market.

Quickly covering our first quarter 2021 results. We delivered total revenue of $946 million, up 1% on a constant currency basis; global client revenue of $853 million, up 5% on a constant currency basis; adjusted operating income margin of 17.2%, expanding 250 basis points year-over-year; and adjusted diluted earnings per share of $0.59, up 11% year-over-year.

Before I get into the details, I want to provide an update on the COVID-19 situation in India, where we have significant operations. As we've said from the start of the pandemic, all our decisions are centered on 2 key pillars: first, the health, safety and well-being of our global employees; and second, maintaining continuity of services for our clients. While we had a very small in-office presence across [the region] (corrected by company after the call), the majority of those employees are now back to working from home.

I'm extremely proud of the passion and dedication of our teams to support their colleagues in the face of this crisis. They continue to work tirelessly to deliver to our clients while simultaneously doing everything they can to support our impacted colleagues and their families. We also appreciate the outpouring of support we have received from our clients as we partner together to overcome this difficult time. We have set up drive-through testing for employees and their families as well as an employee hotline to help with questions and provide access to medical attention and resources. We have increased insurance coverage and financial aid for our most impacted associate population. We have made provisions to enable employees to get vaccines when they become available at our cost.

Across the globe, we have 24/7 counseling hotlines offering mental health support for our teams, access to education and wellness app and an online community with resources for parents.

Now turning back to our performance. During the first quarter, client demand remained very healthy, carrying forward the momentum we saw in Q4 of last year. Our pipeline reached another all-time high driven by new inflows, including several large complex transformational deals that integrate multiple services such as finance and accounting to supply chain or sales and commercial operations.

We are happy with our overall win rates that highlights our differentiation and competitive deals. Sole-source deals continued to account for more than half our inflows, pipeline and bookings during the quarter. Our strong Global Client performance was broad-based across almost all of our chosen verticals, including double-digit growth in consumer goods and retail, life sciences and health care and high tech.

The exception was banking and capital markets, which was impacted by the restructuring of the relationship with one of our banking capital markets clients that we discussed last quarter. I'm particularly pleased with our Global Client top line performance given our strong first quarter results of 2020, the last period prior to the challenges related to COVID-19. Given the strong start to the year, we believe we are well positioned to deliver on our full year outlook.

As expected, GE declined 24% as a result of productivity delivered and a reduction in IT project spend in this uncertain macro environment. The reduction also includes the impact of GE divestitures that are now part of our Global Client portfolio.

Transformation Services, which includes consulting, analytics and digital, grew by approximately 20%, including the contribution from our recent acquisition of Enquero, and now represents more than 30% of total Global Client revenue. Transformation Services continues to drive new deal wins with consulting, digital and analytics being systematically embedded into more than 70% of our pipeline.

We are seeing a growing opportunity to serve the fast-changing needs of our clients with innovative solutions that leverage cloud architecture and data and analytics. Here are a couple of examples. For a food company, we are using our AI and machine learning solution to generate more accurate and real-time demand forecast, leveraging traditional and nontraditional data sources stored in the cloud after reimagining the entire planning process. For A global banking client, we are designing, building and deploying a digital cloud-native commercial loan solution on AWS, leveraging our deep understanding of the commercial lending and syndication business and processes. The bank's objective is to disrupt this market with dramatically faster decision and funding times, along with a superior customer experience that ultimately should drive market share gains for them.

Many of our Transformation Services engagements lead to much larger intelligent operations deals as clients drive change to gain a competitive advantage in their changing markets. Over the last 4 years, approximately 25% of our Global Client accounts that started initially with small Transformation Services engagement with a relationship of less than $1 million, have now expanded to larger relationships of more than $5 million with some, of course, becoming even larger.

Many of our engagements have alternate commercial models that are not just input or people cost-based. We exited the quarter with more than 40% of our total revenue coming from newer constructs such as outcome-based pricing and fixed price models, up from 30% in 2017. The highlight of the quarter was the growth of analytics in our Transformation Services portfolio. First quarter Global Client Analytics revenue grew more than 30%, and we expect that momentum to continue through the year. Given its significant growth over the past several years, analytics has become the biggest component of our Transformation Services business. For the last couple of years, we've increased our focus and solutions with the use of data and analytics to drive insights and actions in many services like supply chain, sales and commercial and financial crimes and risks. The growing appetite of clients across industries to leverage data and predictive insights on a 10 digital layer in the cloud to solve problems and drive outcomes is fueling demand.

Bolstered by our recent acquisition of Enquero, Something Digital and Rightpoint, we are now designing and implementing new cloud-based data and analytics solutions to accelerate clients' transformation journeys. Some examples are: For a global media and entertainment business, we are creating a cloud enterprise platform that combines siloed in-house data with third-party consumer data to run analytics at scale in order to gain insights about consumer preferences, generate behavior recommendations and improve the buying experience, all to drive new revenue streams and growth across all of its channels.

For a major insurance carrier, we are using AI and machine learning to process claims and litigation expense data to predict exposure to large new claims in order to significantly reduce payouts and mitigate future underwriting risks. As I said in our earnings call last quarter, we are in a growing market that remains highly underpenetrated with digital transformation, driving companies across all industries to redefine themselves, unlocking new opportunities. Our strategic investments over the years enable us to lead clients through their journeys, thus expanding our pipeline and leading to new bookings.

This expansion of total addressable market is led largely by 2 types of clients. First, existing clients looking to accelerate transformation journeys, leading to larger engagements with us that incorporates services and buying centers beyond the CFO and the CIO, such as the COO, the Chief Risk Officer and the Chief Supply Chain Officer; and second, new clients that are now open to partnerships for the first time to change and transform themselves in response to this new global environment.

Two interesting metrics that demonstrate this trend are Global Clients with annual revenue of $50 million or greater increased to 11, up from 10 during the same period last year. And our revenue from this client group grew at more than double Global Client growth. Secondly, clients with annual revenues of $5 million and more increased to 132, up from 128. This included many first-time buyers to the type of services we provide.

We are seeing permanent changes to the way businesses adapt to the new normal operating environment. They no longer exclusively rely on traditional KPIs and frameworks to drive performance such as sales levels, process optimization and efficiency from automation or work in rigid industry-aligned business models. Boards and C-suites have shifted priorities and are investing to design industry-disrupting operating models based on our metrics like customer empathy and delight. We believe these factors provide a longer runway of sustainable low double-digit to low-teen growth for Global Clients.

Our strong first quarter results reflect our resilient business model, focused strategies and top-tier execution, all playing out in the market. We continue to build on our strengths and become even more relevant to clients by solving problems caused by disruption to industry value chains. We believe our agility enables us to quickly bring new innovative transformation solutions, leveraging digital and analytics to the market. This has strengthened our position as a trusted adviser separating us from our competition and fueling our continued growth even in challenging environments.

With that, let me turn the call over to Ed for a detailed review of our [first] (corrected by company after the call) quarter results.

Edward J. Fitzpatrick - *Genpact Limited - Senior VP & CFO*

Thank you, Tiger, and good afternoon, everyone. Today, I'll review our first quarter results and provide our current thinking regarding our full year 2021 financial outlook.

Total revenue was $946 million, up 2.5% year-over-year or 1% on a constant currency basis. This growth was higher than we anticipated, driven by better-than-expected performance in our Global Client businesses. Global Client revenue, which represents 90% of total revenue, increased 6% year-over-year or 5% on a constant currency basis, including an approximate 1 point contribution from revenue related to certain divested GE businesses that is now included in Global Client revenue as of January 1, 2021.

Excluding this revenue, Global Client revenue would have increased 5% year-over-year or 4% on a constant currency basis, ahead of our expectations, largely driven by better Transformation Services performance led by strong analytics growth. GE revenue declined 24% year-over-year due to productivity commitments, the macroeconomic impact on GE's businesses and the impact from certain divested businesses now included in Global Client revenue. Excluding the effect of the revenues related to divested businesses, GE revenue declined 16% during the quarter. I will cover the full year outlook later on. But on an apples-to-apples basis, there is no change to our prior full year outlook for GE revenue.

Adjusted operating income margin was 17.2%, up 250 basis points from the first quarter last year. The year-over-year improvement was largely due to higher gross margin, lower-than-expected travel expenses reflecting the impact from COVID-19 and greater operating leverage. As a reminder, during the first quarter of 2020, our adjusted operating income margin was impacted by lower utilization from limits placed on our ability to work from home that were subsequently resolved as well as charges associated with reduced valuation of our India retirement fund.

Gross margin in the quarter was 36.5% compared to 34.5% during the same period last year. The 200 basis point expansion was largely due to better overall utilization, led by Transformation Services and improved productivity gains. Additionally, the prior year figure was lower than normal due to the impact from the COVID-19-related charges I mentioned earlier. We continue to expect full year gross margin level to improve by at least 50 basis points year-over-year.

As a percentage of revenue, SG&A expenses declined by 20 basis points year-over-year, largely driven by lower-than-expected travel costs related to COVID-19 and partly offset by investments in sales and marketing. Adjusted EPS was $0.59, up 11% year-over-year compared to $0.53 in 2020. The $0.06 increase was primarily driven by higher operating income of $0.10, up approximately 20% year-over-year, and the impact of a lower share count of $0.01, partially offset by a lower year-over-year FX remeasurement gain of $0.04. As a reminder, in the first quarter last year, we recorded a $15 million FX remeasurement gain in comparison to a $3 million gain this quarter. Higher taxes also had a $0.01 negative impact.

Our effective tax rate was 24.1% compared to 22.5% last year. The increase was primarily due to the expiration of certain tax benefits and higher discrete benefits last year.

Turning to our cash flows and balance sheet. During the first quarter, we generated $77 million of cash from operations compared to utilizing $19 million during the same period last year due to higher adjusted operating income as well as improved DSOs and overall lower working capital levels. As a reminder, cash flow from operations during the first quarter of 2020 included a nonrecurring tax payment related to a prior period India tax matter.

Our days sales outstanding improved year-over-year to 84 days compared to 89 days last year, largely driven by a reduction in billing cycle time and improved collection timing. Cash and cash equivalents totaled $644 million compared to $680 million on December 31, 2020, as free cash flow of $63 million was augmented by proceeds from the recent bond issuance, offset by a $259 million bond repayment, share repurchases of $134 million and $20 million related to the dividend payment in the quarter.

During the quarter, we tapped into the low interest rate environment and issued a new $350 million bond with an attractive 1.75% coupon rate. We currently plan to retire our existing $350 million bond with a coupon rate of 3.7% that is scheduled to mature in April 2022 and are closely monitoring market conditions to optimize the timing of the paydown. Once the 2022 bonds are retired, we expect to recognize annual interest savings of approximately $7 million due to the interest rate differential of the 2 bonds.

Our net debt-to-EBITDA ratio for the last 4 rolling quarters was 1.67x including the impact from the new $350 million bond offering. During the quarter, we also took advantage of the attractive valuation of our shares and repurchased approximately 3.3 million shares or almost 2% of the outstanding amount for a total cost of $134 million at an average price per share of $40.68. Our intrinsic value calculations highlighted a meaningful disconnect in our share price. And given we had sufficient capital available during the quarter, we stepped up our share repurchases accordingly and we're able to do so while keeping our net debt-to-EBITDA level below 1.7x.

Since we initiated our share buyback program in 2015, we have repurchased 44 million shares at an average price of approximately $28.28 per share for a total of $1.2 billion. The annual return on these purchases to date is approximately 16%. We have approximately $503 million of authorized capacity remaining under our share repurchase program.

There is no change to our capital allocation priorities. We will continue to invest first in driving organic growth, but we also have a solid M&A pipeline and we'll be vigilant in continuing to search for companies that can strengthen our capabilities in our chosen service lines. And to the extent capital is available, we continue to believe repurchasing shares, particularly when our valuation is very attractive in comparison to our view of the intrinsic value of the firm, represents an incredibly value-accretive investment.

When assessing the prospects of the firm, it is certainly prudent to consider past performance as an indicator of future growth. Particularly noteworthy, over the past 5 and 10 calendar year periods, we generated free cash flow growth at a compound annual rate in the mid-teens. We expect to continue to generate strong double-digit plus cash flows moving forward, which aligns with our overall medium- to long-term growth outlook. As we mentioned, we will continue to assess our share price and compare that price with our own valuation assessment and take advantage of valuation dislocations.

Let me now turn to our current thinking on our full year outlook. We continue to expect total revenues to be between $3.93 billion and $3.99 billion, representing year-over-year constant currency growth of 5% to 6.5%. We are pleased with the strong start and believe we are in better position to achieve our full year top line outlook. Of course, we are closely monitoring the COVID-19 situation in India, and so far, have been able to continue to serve our clients through the extraordinary efforts from our global teams and the partnerships with our clients who have been usually supportive.

For Global Clients, we now expect revenue growth to be in the range of 9% to 11% or 8% to 10% on a constant currency basis, which includes an approximate 1 point contribution from revenue related to certain GE divested businesses that is now included in Global Client revenue. Excluding this revenue, Global Client revenue for the year will be expected to grow 8% to 10% or 7% to 9% on a constant currency basis, in line with the outlook we provided last quarter.

During the second quarter, we expect to see a meaningful step-up in year-over-year growth for Global Client revenue to high single digits, given the momentum we are seeing in our business, coupled with top line impact caused by COVID-19 in the second quarter of last year. With expected low single-digit sequential growth during the third and fourth quarters, we continue to believe we are well positioned to return to double-digit Global Client year-over-year growth by the fourth quarter, if not sooner.

GE revenues are expected to decline approximately 20% year-over-year. Excluding the effect of the approximately $40 million in revenue related to GE divested businesses, GE full year revenues are expected to decline 10% to 12%, in line with our prior outlook we gave earlier this year. Given the strong adjusted operating margin we generated in the first quarter, we believe we are even better positioned to expand our adjusted operating margin for the full year to 16%.

We continue to expect to ramp our R&D and sales and marketing efforts, including travel as we navigate through the balance of 2021, along with the expected sequential revenue growth we are anticipating. Given this outlook, we estimate adjusted diluted earnings per share for the full year 2021 to be between $2.27 and $2.30, a $0.01 increase from our prior range of $2.26 to $2.29 due to an FX remeasurement gain of $3 million we recorded during the first quarter.

Before I turn it over to Tiger, I want to mention that we are very pleased that we were recently added to the S&P 400 MidCap Index, which is a nice testament to the fundamental performance of the firm.

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

Nallicheri Vaidyanathan Tyagarajan - *Genpact Limited - President, CEO & Director*

Thank you, Ed. We've had a great start to the year. Our culture of embracing change, strengthen process and relentless focus on client outcomes differentiates us in the market. As we go into the future, we will drive value for our clients, leveraging digital and analytics for predictive insights. Given the combination of our analytics capabilities and our deep domain expertise, we are well positioned to deliver on our long-term growth trajectory.

One of our pillars of success has been the sustained investment in our employees' learning and development on rapidly evolving skills. Coupled with our online learning platform, Genome, we leveraged our talent redeployment platform, Talent Match, to identify, reskill and redeploy another 2,000 team members for new roles during the quarter, resulting in better utilization and talent retention.

For example, we recently launched a proprietary data and analytics certification program available to all our team members to develop the expertise needed to generate critical insights from our vast operating data sets. The response to this program has been overwhelming with nearly 1/3 of our global workforce currently enrolled, demonstrating the desire and dedication of our people to continuously learn, which we believe contributes to our competitive advantage.

Our robust hiring, onboarding and reskilling programs have allowed us to continue to recruit top talent to join our workforce and capture the many long-term opportunities ahead of us. In the last 12 months, we have added more than 20,000 colleagues to our global team and recently crossed the threshold of 100,000 employees globally.

We are deeply committed to investing in ESG initiatives and will provide regular updates on our efforts and progress. We've always had an unwavering commitment to drive sustainability with initiatives around diversity and inclusion, climate impact, supporting our communities and transparent governance, all of which enable us to achieve our long-term financial goals and benefit our communities.

In addition to all our efforts in India, we're also at the forefront of helping to safely and effectively reopen the U.S. economy faster. We recently announced a new collaboration with the COVID Collaborative and the Creative Destruction Lab rapid Screening consortium to launch the U.S. Rapid Action Consortium. The goal of this group is to work together with a diverse ecosystem of leading private sector businesses, experts and organizations to accelerate the use of safe, cost-effective rapid COVID-19 testing to better enable businesses to return to the office safely.

I've been extremely proud of the tenacity and resilience of our teams and partnership with our clients as we have all navigated the COVID-19 crisis, and I'm confident that we will together get through the most recent development in India.

Before I close, I'd like to welcome the newest member of Genpact's Board of Directors, Tammy Franklin, who has an impressive track record of leading digital transformation across numerous companies. We're all excited to bring our deep expertise into our strategic conversations, and I'm very pleased with the diverse talent of our Board.

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

Roger Sachs - *Genpact Limited - Head of IR*

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

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Your first question comes from the line of Bryan Bergin from Cowen.

Bryan C. Bergin - *Cowen and Company, LLC, Research Division - MD & Analyst*

I wanted to just I wanted to just start on the outlook factors. So just how do we translate the strong 1Q results here that came in above plan, but the holding of the outlook? Is it just the fact that it's early stage of the year? Are you building in pandemic-related items within India for operations? Any pull forwards we need to be aware of? Can you just help us marry those 2?

Nallicheri Vaidyanathan Tyagarajan - *Genpact Limited - President, CEO & Director*

I'm just going to say, Bryan, you nailed it in your first comment. It's just the first quarter, really pleased with the strength of the first quarter. And therefore, all the narrative around feel good about the full year.

But it's only 1 quarter. We haven't built in anything on the impact of COVID-19 in India. Our operations, our delivery to clients, the partnership with clients in spite of, obviously, increased absenteeism driven by both COVID-19 in our population as well as the impact on families obviously means that we work very closely with our clients to continue to deliver our services. So we haven't had to build in anything on that impact into our outlook. It's just that it's just one quarter.

Bryan C. Bergin - *Cowen and Company, LLC, Research Division - MD & Analyst*

Okay. And then you heard the pipeline commentary at record levels here. Can you talk about decision-making and also deal ramp timing? Have you seen that change versus 3 months ago?

Nallicheri Vaidyanathan Tyagarajan - *Genpact Limited - President, CEO & Director*

No, Bryan. It seems to be on track, both in terms of the speed at which decision-making is happening and the expected ramp and the time for ramp run. Have to take into account the fact that these are often -- particularly the larger deals are complex deals, clearly multi-geography, but also multi-buy center with connected services. I talked about finance and accounting connected to supply chain and sometimes connected to sales operations. And then you do that kind of a connected large deal, that takes time to ramp up. It's got nothing to do with the pandemic.

Operator

Your next question comes from the line of Mayank Tandon from Needham.

Mayank Tandon - *Needham & Company, LLC, Research Division - Senior Analyst*

Tiger, Ed and Roger, congrats on the quarter. I wanted to start with just a little bit more color on the revenue momentum that you're seeing. I don't have your data sheet in front of me. So just would love to get some perspective on which verticals outperformed your expectations. Are you seeing any soft spots within that vertical portfolio? So any more color on the revenue breakdown that you're seeing across your verticals and regions.

Nallicheri Vaidyanathan Tyagarajan - *Genpact Limited - President, CEO & Director*

So I'll kick it off and then Ed can add to it. I'd like to -- on our prepared remarks, Mayank, we're seeing pretty pervasive good growth performance across all our verticals other than banking capital markets, which I'll talk about separately, but all our verticals other than banking capital markets. In fact, consumables, retail, life sciences and health care and high tech, all double digit. And then when it comes to banking capital markets, we saw a decline versus last year first quarter. But that was as we had expected. Because if you remember last quarter, we had said that one of our banking capital markets clients in the asset management business was restructuring, resizing their entire business as well as therefore our contract. And we have planned for this. As we entered the quarter, we knew that's exactly what is going to happen, and it got executed exactly the way we had planned.

What we are seeing in the banking capital markets business is an increased inflow into a new pipeline. Pipeline is growing very nicely. So as we finish the year, we expect banking capital markets to be actually very strong. Ed, do you want to add to that?

Edward J. Fitzpatrick - *Genpact Limited - Senior VP & CFO*

I think you hit it, Tiger. I think consumer goods, life science is growing, continuing to grow at a fast clip, which is great, high tech as well within HMS growing a nice clip. Just in general, pleased with all the verticals, barring just the one that Tiger mentioned. So we feel really good about the comprehensive nature of the growth across the board.

Mayank Tandon - *Needham & Company, LLC, Research Division - Senior Analyst*

Got it. And then just as a quick follow-up. Ed, maybe on margins, just given the strong outperformance in the first quarter, what are some of the puts and takes that are going to weigh in margins over the next 3 quarters to drive that 16% level that you mentioned? One would think given the strong start to the year, you might be able to actually outperform that. So just if you could call out some of the various factors that might weigh in the margins, that would be helpful.

Edward J. Fitzpatrick - *Genpact Limited - Senior VP & CFO*

And I'll touch on the full year expectation or thoughts. I think Tiger said it. We're really happy that we got out of the gate the way we did. That's great. We feel better about the full year. So that's a nice place to start. In terms of the first year, better than expected. We mentioned transformation services, which is better. And analytics within Transformation Services, really higher-level services at a nice margin clip. So mix was a piece of it, and that's good. Can that continue? Sure, but do we expect it to continue for the rest of the balance of the year? We thought not appropriate at this point. So want to see how that plays itself out.

And then other things are going to come back in. We're going to continue to invest. We're going to invest -- travel will come back. It looks like at a slower clip than everybody is thinking, particularly with what's happening in the world. But I do think we will be ramping up R&D. We'll be ramping up selling and marketing and investments for the balance of the year. So mix, a piece of it -- early on in the year is another piece of it. And then some of the investments we're going to ramp up for the balance of the year explains the rest. Tiger, anything else to add?

Nallicheri Vaidyanathan Tyagarajan - *Genpact Limited - President, CEO & Director*

No. No, I think you hit it. That was good, yes.

Operator

Your next question comes from the line of Tien-Tsin Huang from JPMorgan.

Tien-Tsin Huang - *JPMorgan Chase & Co, Research Division - Senior Analyst*

I hope everyone is safe at the firm out of India. I wanted to ask on that with -- I think, Tiger, you mentioned there's some absenteeism, but you're not seeing any impact on operations yet. Is that impacting deal flow as well as folks are trying to maybe see how things play out from a delivery perspective? Or do you have contingency in place to deliver from other locations in case things get worse, God forbid, of course?

Nallicheri Vaidyanathan Tyagarajan - *Genpact Limited - President, CEO & Director*

No, Tien-Tsin, thank you very much for your sentiments. Really appreciate it. I'll start off by saying that absenteeism is obviously higher than typical absenteeism driven by regular leave and vacation and all of that. There are a few things that we need to keep in mind. One, our delivery footprint in India is very nicely distributed between the Delhi, Gurgaon National Capital Region, Bangalore, Hyderabad, Calcutta, Jaipur, Bombay, Pune. And what that distribution does in the context of the current pandemic situation in India is that it's not at the same time all cities ramping up in absenteeism in the COVID-19 situation on the ground. And as it rolls through city by city, we have been able to deal with the ability to move volume around a little bit across those cities to bring our European centers and our U.S. centers into play because our global delivery footprint compared to about 7, 8 years back is nicely balanced, really well balanced.

And of course, I think it will be fair to say that our clients have been unbelievably supportive in the way they have worked with our teams, reprioritize one of the important SLAs because our objective here, as I said, to balance and make sure that the safety and health of our employees and their families are fully taken care of while continuing services that we have to deliver. So, so far, really feel good.

On new business and transitions, we have actually transition going on as we speak. I haven't seen any impact, and we don't expect to see any impact as long as we continue our services, which at the moment, we are confident that we will be able to.

Operator

Your next question comes from the line of Dave Koning from Baird.

David John Koning - *Robert W. Baird & Co. Incorporated, Research Division - Associate Director of Research & Senior Research Analyst*

Yes. Nice job. And I guess just a couple. First of all, gross margins were really strong, up 200 bps this quarter. Last quarter was really good, too. The way you guided, you could basically have flat year-over-year gross margins for the rest of the year and hit your guidance. Is there any cadence you're thinking of? Like will Q2 still be up year-over-year and Q3 and Q4 down year-over-year? Just think of all 3 of the last quarters being pretty flattish year-over-year. And maybe I think you kind of reviewed why, but maybe review through that a little bit again.

Edward J. Fitzpatrick - *Genpact Limited - Senior VP & CFO*

Yes. If we hit 36 points of gross margin for the balance of the year, which is kind of what we guided for the full year, gross margins will be just above 36%, which Tiger and I both think that we ought to be able to drive 36% and hopefully better. But again, we're early on, so we're not going to get ahead of ourselves. So we're just assuming that the mix isn't quite as favorable, that we do have some expenses that do start to ramp up a little bit, including travel, some of that including cost of revenue.

So we'll see how it plays out. But the first quarter the favorable mix, a bit lower spending and then just kind of being earlier on in the year, not wanting to get ahead of ourselves is the way we're thinking about it.

Nallicheri Vaidyanathan Tyagarajan - *Genpact Limited - President, CEO & Director*

And Dave, the one other thing I would add is Transformation Services was one of the components of our business in the first quarter that came in very strong. And within that, analytics came in very strong. And therefore, utilization in Transformation Services and Analytics was very strong. All of that helped both gross margin as well as adjusted operating income margin.

And we think that, that is something that we are very focused on because, clearly, our clients are very focused on leveraging data, leveraging the cloud and leveraging data on the cloud in order to drive insights and be much more nimble and agile in the way they take decisions to run their business and operations, which is very different from the way it was just 2 or 3 years back. And all of that actually augurs very well for long-term gross margin and adjusted operating income margin in our business.

David John Koning - *Robert W. Baird & Co. Incorporated, Research Division - Associate Director of Research & Senior Research Analyst*

Yes. Got you. Thanks for that. And then maybe secondly, just as a reminder, I know you did the acquisition in Q1, I think, Enquero. Was that in the original guidance? And maybe give or take how big -- I mean, it looked like a pretty big acquisition, you paid $200 million, something for it. How much revenue give or take this year?

Edward J. Fitzpatrick - *Genpact Limited - Senior VP & CFO*

We said it adds about 200 basis points of growth in the year, a little bit less than Rightpoint was adding last year.

Nallicheri Vaidyanathan Tyagarajan - *Genpact Limited - President, CEO & Director*

Yes, it was -- yes, sorry.

Edward J. Fitzpatrick - *Genpact Limited - Senior VP & CFO*

It was included. Yes.

Nallicheri Vaidyanathan Tyagarajan - *Genpact Limited - President, CEO & Director*

It was included in our guidance because we closed the acquisition on the 31st of December of 2020, the last day of the year.

Edward J. Fitzpatrick - *Genpact Limited - Senior VP & CFO*

And no change, no change in the outlook related to that acquisition?

Operator

Your next question comes from the line of Maggie Nolan from William Blair.

Margaret Marie Niesen Nolan - *William Blair & Company L.L.C., Research Division - Analyst*

Nice quarter. I wanted to follow up on some of the business continuity question. When you do have to shift work to other geographies, are you able to share any incremental costs with clients just given that this is such a unique environment that is happening in right now?

Nallicheri Vaidyanathan Tyagarajan - *Genpact Limited - President, CEO & Director*

So actually, Maggie, when we shift work to, let's take Bucharest, which is one of our larger European centers, what we are doing is leveraging our existing teams. We have a pretty significant presence in our European operations in Bucharest, in Krakow, in Cataloochee and in a number of other locations. And the kind of work that they do is the kind of work that -- with some cross-training, they're able to absorb. One of the things that our teams did, which I'm really proud of, is systematically in the last 2 quarters of 2020, they went down the path of cross-training people. Because they said, if something like the current situation in India were to happen, how do you have backups for individuals are very different from the situation we were in last year where all we wanted to do, which is a mammoth exercise, is move from work in office to work from home everyone. Here it is, who is the backup for John? Who's the backup for Mary? Who's the backup for this critical resource?

And no, so it's actually not necessarily incremental costs. It's just that people have to work longer. People are, therefore, have to be paid extra incentives over time. And we do all of that. But remember, clients are going above and beyond in their partnership with us. So it's actually not about -- in this situation, it's not about who pays for what. It's making sure that the services get delivered. And I think our partnerships are really shining through at this time.

Margaret Marie Niesen Nolan - *William Blair & Company L.L.C., Research Division - Analyst*

Got it. And then great to see the strength in TS and analytics continuing the trend of strength that we've seen. What is your ability to turn any kind of project-based analytics work into longer-term relationships and recurring revenue streams?

Nallicheri Vaidyanathan Tyagarajan - *Genpact Limited - President, CEO & Director*

So Maggie, let's start with the Transformation Services at the higher level. We're finding the ability for us to enter a new client relationship with Transmission Services to be one of the real opportunities that we are able to take to clients to quickly start adding value, and that applies to analytics as well. And we are finding in many, many, many of those situations, given a certain amount of time, let's say, at the end of 1 year, at the end of 2 years, they tend to start converting into larger annual [TDs]. I would say analytics often starts with annual TDs themselves, not just project work. So when we talk about our analytics growth, that is easily half of that, if not more, is actually annual analytics work.

Operator

Your next question comes from the line of Ashwin Shirvaikar from Citi.

Ashwin Vassant Shirvaikar - *Citigroup Inc., Research Division - MD & Lead Analyst*

I wanted to kind of start with -- this is sort of heading into the second year of kind of work from home. What are you broadly seeing from your clients in terms of feedback with regards to the need to continue working from home? I know you mentioned supportive, but what are sort of the intermediate and longer-term implications of this continuing, the tragedy that it did?

Nallicheri Vaidyanathan Tyagarajan - *Genpact Limited - President, CEO & Director*

So Ashwin, I don't think it's a one size fits all would be the start of my answer. What we are doing, and we are leading the effort here with and for our clients is actually taking to them the archetype of design of the way a particular service in an industry should run. So how should the closing of the books for a large enterprise run in a typical month, in a typical quarter? What kind of work should be done from an office environment and when? And what kind of work should be and can be done from a remote environment? So we think about that as a design construct of nearshore, onshore, offshore in an office, offshore in work from home environment, and it's really a design discussion.

And like everything else, different customers are going to land at different spots in that design and then will migrate over time to different other spots. So that's one, which is the hybrid design.

And the second one is the flexibility of talent. Some people are going to say that they would like to always work from an office. And some other people are going to say that they think about working a predominant amount of time from a home environment. Our view again is that we must construct a design where particularly for the people who are going to be working from a remote environment, there is a cadence with which they come back into an office. They have an opportunity to come together as a team, build a culture, learn new skills, innovate. And that's, again, a discussion that is very, very relevant with different clients. It will end up in different constructs and different archetypes. Our job is to design those, come up with those archetypes, discuss with different clients, pros and cons. And that's exactly what we are doing as we speak.

Ashwin Vassant Shirvaikar - *Citigroup Inc., Research Division - MD & Lead Analyst*

Understood. Very detailed. The other question -- I mean you're kind of at this point halfway through the second quarter. Is there anything you're seeing in the environment in terms of how your project flow is in terms of costs and such that would cause you to say that the 1Q strength was kind of one-off in nature?

Edward J. Fitzpatrick - *Genpact Limited - Senior VP & CFO*

I won't speak to anything mid-quarter, Ashwin. I think just the commentary we've already provided on kind of why Q1 was stronger and how we're looking at the balance of the year, we think, is appropriate given where we are right now. And as we get through the second quarter, we'll come back to you. But still too early to kind of give any more -- any level of color on the detail for Q2 and the balance of the year.

Nallicheri Vaidyanathan Tyagarajan - *Genpact Limited - President, CEO & Director*

And I think, Ashwin, what Ed has already described in terms of our strength on margins, for example, in the first quarter, and therefore, what does that mean for the year. We are going to be continuing to invest in sales and marketing and R&D as our revenue ramps through the year.

And of course, we do -- we are already seeing travel come back in domestic U.S., certain parts of domestic Europe. Of course, international travel between India and the global markets is right now nothing, and we can't predict as to when that is going to come back. But some of that other travel is coming back. And that is all going to be factored into the overall margin of the company as we go forward into Q2 and beyond.

Operator

(Operator Instructions) Your next question comes from the line of Keith Bachman from Bank of Montreal.

Keith Frances Bachman - *BMO Capital Markets Equity Research - MD & Senior Research Analyst*

I want to ask 2 questions. The first one, Tiger, I'll direct towards you, and it's really about growth. And I wanted to get your views as you think about net new bookings and you called out some interesting areas, but how do you think about the net new bookings contribution to growth associated with existing clients versus new clients? And you seem to highlight -- to use your words, kind of new partnerships with new clients. Just wondering how you're thinking about that.

And really part B to the question is I understand there's probably some conservatism to guidance. How long do you think it takes to really generate into that durable double-digit constant currency Global Client growth. You reached some the -- some of it you reached to kind of Q4 this year, you said. Compares are a little bit easy. But I want to talk about kind of building the pipeline and how you think about the durable double-digit global client growth because you're getting some contribution this year also from M&A. So that's question one, really around demand. And then I had a follow-up.

Nallicheri Vaidyanathan Tyagarajan - *Genpact Limited - President, CEO & Director*

Yes. I'll start from your second question, Keith. As Ed had said, and I think we've said this more than the last couple of quarters, we've said this, which is by the time we get to the fourth quarter, we expect our Global Client growth rate to get back to double digit constant currency. And we had indicated, and again, we indicated this time that it could be a bit sooner, but fourth quarter is when we expect it. And when we say that, we mean that we -- our expectation going forward from there is to come back with a long-term trajectory that we've been calling out for quite some time of Global Client double-digit growth. And our view is that the last 18 months has increased our total addressable market, increased the runway of our opportunity to undertake that double-digit Global Client top line growth.

And we feel very good about that because the number of new clients who are wanting to have partnerships and the number of existing clients who are opening up many more services and connected buying centers in order to drive enterprise-level transformation is just improved the total addressable market, which kind of then relates back to the first question, which is our ratio of a typical year where revenue growth is still materially contributed by existing clients. Because the definition of an existing client is you start a relationship. And sometimes a relationship, barring a few exceptions, starts with Transformation Services relationship, where you're advising our clients, you're implementing a quick payback engagement, you're doing an analytics engagement that drives immediate value.

And as you start doing that, you're already in discussions about a larger relationship. Those take long to orchestrate and undertake. And that's the journey that we've been on since, for example, the fourth quarter when we had very strong bookings, and it takes time to ramp that up. So which is why by the time we get to the fourth quarter, we'll get to double-digit growth.

Edward J. Fitzpatrick - *Genpact Limited - Senior VP & CFO*

The only thing I'd add is the year-over-year comparisons may be a bit easier. But remember, we did grow, I think, 5% or 6% last year, right? We weren't flat to down like many of our peers. So our comparison is a little bit -- it's coming off of growth. I just want to make sure you're aware of the durable nature.

Nallicheri Vaidyanathan Tyagarajan - *Genpact Limited - President, CEO & Director*

It's a very important point, Keith, because we had pretty material growth in the context of what the world is going through and what our industry are going through in 2020, and therefore, our 2021 is in the backdrop of that growth. We didn't have that significant V in our growth trajectory between '19, '20 and '21.

Keith Frances Bachman - *BMO Capital Markets Equity Research - MD & Senior Research Analyst*

Fair enough. My second question is just a clarification, Tiger. Your competitors -- or not true competitors, but Cognizant, Infosys, and TCS had pretty meaningful increase in attrition, not only from September to December, but even more so this December to the March quarter. In a previous question, you had talked about absenteeism. I think everybody is experiencing that and perfectly understandable. But just to be clear, it doesn't sound like you've actually had an increase in attrition. And I just wanted to clarify that, a. And then b, BPO traditionally has higher levels of attrition than some of the other areas of IT services. I just wanted to see if you have any comments or thoughts why it doesn't sound like you're having the same issues surrounding attrition that some of the traditional IT service providers are experiencing.

Nallicheri Vaidyanathan Tyagarajan - *Genpact Limited - President, CEO & Director*

So Keith, our attrition has gone back up between the fourth quarter and the first quarter, but that we had expected. And it's gone back up to tad below what it used to be pre-pandemic. But why would one have any other expectation? So the reason we haven't called it out is because that is exactly what we expected. We planned for it. We know exactly where those attrition seem to be higher versus lower. It seems to be following a pattern that we've seen for 10-plus years.

So -- and our way of addressing that is to manage the business with that attrition to make sure that our high-performing talent get opportunities to do new work, get certifications, gets new skilling, get compensation, promotions. And that's exactly what we've been doing. That attrition is still lower than what it used to be pre-pandemic. It is higher than it was -- what it was in fourth quarter, I'm a little intrigued as to how would one expect Q1 attrition to be not higher than Q4.

Operator

And there are no further questions over the phone line at this time. I would now like to turn back the call over to Roger Sachs. Sir?

Roger Sachs - *Genpact Limited - Head of IR*

Great. Thank you, everybody, for joining us today, and we look forward to speaking with you again next quarter

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Operator

This concludes today's conference call. Thank you for participating. You may now disconnect.
