

31-Jul-2024

Cognizant Technology Solutions Corp.

(CTSH) Q2 2024 Earnings Call



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MANAGEMENT DISCUSSION SECTION

Operator: Ladies and gentlemen, welcome to the Cognizant Technology Solutions Second Quarter 2024 Earnings Conference Call. All lines have been placed on mute to prevent any background noise. After the speakers' remarks, there will be a question-and-answer session. [Operator Instructions] Thank you.

I would now like to turn the conference over to Mr. Tyler Scott, Vice President, Investor Relations. Please go ahead, sir.

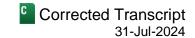
Tyler J. Scott

Vice President-Investor Relations, Cognizant Technology Solutions Corp.

Thank you, operator, and good afternoon, everyone. By now, you should have received a copy of the earnings release and the investor supplement for the company's second quarter 2024 results. If you have not, copies are available on our website, cognizant.com. The speakers we have on today's call are Ravi Kumar, Chief Executive Officer; and Jatin Dalal, Chief Financial Officer.

Before we begin, I would like to remind you that some of the comments made on today's call and some of the responses to your questions may contain forward-looking statements. These statements are subject to the risks and uncertainties as described in the company's earnings release and other filings with the SEC.

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Additionally, during our call today, we will provide certain non-GAAP financial measures that we believe provide useful information to our investors. Reconciliations of non-GAAP financial measures, where appropriate, to the corresponding GAAP measures can be found in the company's earnings release and other filings with the SEC.

With that, I'd now like to turn the call over to Ravi. Please go ahead.

Ravi Kumar Singisetti

Chief Executive Officer & Director, Cognizant Technology Solutions Corp.

Thank you, Tyler, and good afternoon, everyone. Thank you for joining our second quarter 2024 earnings call. I'm pleased with our strong execution and results in what remains a challenging market. We delivered revenue above the high end of our guidance range, expanded our adjusted operating margin, both quarter-over-quarter and year-over-year, sustained our large deal momentum by signing five deals each with a total contract value of \$100 million or more, and announced an agreement to acquire Belcan, which is expected to expand our ER&D capabilities while diversifying into the high-growth aerospace and defense sectors.

Although the demand environment remains challenging and clients' discretionary spending behavior is unchanged from recent quarters, we believe these results demonstrate our rigorous execution against the strategic priorities we set forth last year.

Q2 revenue was \$4.85 billion, which was \$30 million above the high end of our guidance range and grew 2.1% sequentially in constant currency. This was the highest quarter-over-quarter growth since 2022. With strong execution of our NextGen program and overall cost discipline, we achieved adjusted operating margin of 15.2%, an increase of 10 basis points sequentially and 100 basis points year-over-year. Our trailing 12-months voluntary attrition for tech services was 13.6% compared to nearly 20% in the prior-year period.

Second quarter bookings grew 5% year-over-year. And on a trailing 12-months basis, bookings were \$26.2 billion, representing a 1.4x book-to-bill. In addition to the five deals, each with TCV of over \$100 million, we signed two deals that were above \$90 million each. In the first half of this year, we have now signed 13 deals each with TCV of over \$100 million, well ahead of our 2023 pace, which included 17 deals of this size for the entire year.

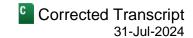
From a segment perspective, we are especially pleased with Financial Services, which grew 5% sequentially in constant currency, driven by growth in the Americas. Within Financial Services, our banking business posted a second consecutive quarter of sequential growth and returned to modest year-over-year growth in constant currency for the first time since Q2 of 2022. We are seeing demand being driven by client investments in hyper personalization, infrastructure and platform modernization.

Our insurance subsegment also grew sequentially in Q2. And one of the five \$100 million-plus TCV deals we signed this quarter was with a large American insurance provider. I believe these results reflect our actions to stabilize the BFSI business since last year.

Over that period, we put new leadership in place and drove greater industry focus on these customer segments. We also aligned our go-to-market approach and launched industry-led service offerings in areas like real-time payment fraud detection, payments hub modernization and digital banking.

Health Sciences grew by 3% sequentially in constant currency, and we see a number of positive secular trends. For example, payers and providers remain focused on reducing the cost of care. We believe this is benefiting our TriZetto platform, where we are helping clients manage more than \$500 billion in complex claims and improve patient outcomes.

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TriZetto's end-to-end capabilities are gaining traction as clients see the value of – in our ability to provide both revenue cycle management and clearing house services. On the payer side, we are seeing demand being driven by data and cloud modernization as our clients seek to deliver a modern, best-in-class consumer experience for their members.

And in Life Sciences, clients have begun moving beyond cost optimization projects to ones that accelerates their GenAl and digital transformation in R&D and continue to drive enterprise modernization with SAP S/4HANA. By region, we are very pleased with the performance in Americas, where revenue grew 2.8% sequentially and returned to growth year-over-year. I am extremely proud of the progress the team has made, and I'm confident in our opportunities ahead.

Looking back over the last 18 months, we believe our strategic investments and focus on improving our operational rigor has further strengthened a foundation on which we can drive sustainable revenue and earnings growth. We invested in our leadership team and attracted new talent to the organization. We drove internal process improvements, particularly around large deals and our talent. And we focus sharply on strengthening our relevance with clients through investments in our innovation strategy and platform offerings.

We believe these changes are starting to pay off and are reflected in our recent revenue performance and year-over-year operating margin expansion in the first half of this year. We have maintained our focus on becoming an employer of choice in our industry, and we're recognized by the Newsweek as one of America's Greatest Places to Work and Greatest Places for Job Starters.

We also continue to expand our footprint in smaller cities in India with the opening of our newest office in Indore, as we remain committed to bringing offices closest to where our employees are.

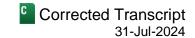
And I'm pleased with Bluebolt, our grassroots innovation program, which has generated 210,000 ideas by our associates since its inception last year. We're also hearing positive feedback from our customers through our project level Net Promoter Score, which I'm pleased to say has improved consistently since 2021 through the first half of 2024. This quarter marks our highest NPS to date.

We have taken a number of actions to date to accelerate growth and drive operational improvements, and we look forward to continuing to update shareholders on our progress.

To that end, we plan to provide an investor update in the first half of 2025 to discuss, among other things, our strategy, our differentiation of the market, our efforts to create long-term value for our shareholders and other stakeholders. A prime example of our investments in higher growth industries and expanding capabilities is our agreements to acquire Belcan, a leading global supplier of engineering, research and development or ER&D services.

We have seen growing demand in ER&D services, an estimated \$190 billion market, whose high growth has been fueled by the convergence of digital technology and the physical world. Over the last three years, we have strengthened our ER&D capabilities, starting with our 2021 acquisition of ESG Mobility, a digital automotive ER&D provider for connected autonomous and electric vehicles. And at the start of my term last year, we acquired Mobica, which focuses on IoT embedded software engineering capabilities from the chip to the cloud.

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We expect the Belcan acquisition to provide an opportunity for us to expand our service offerings into growth vectors that help move the physical world of manufacturing aerospace and automotive into the age of digital data and AI.

Earlier this week, we introduced the next evolution of our experience practice area called Cognizant Moment, which is a new integrated business within Cognizant that builds on our over 20 years of expertise in digital experience.

Cognizant Moment will focus on next-generation experience services that are dynamic, data-led and AI powered, harnessing the content generation and personalization power that Generative AI brings, combined with human ingenuity to help clients innovate, differentiate and grow. The creative and programmatic services life cycle is expected to go through significant transformation in the years ahead. And we see an opportunity to disrupt the status quo agency model as creative content becomes increasingly generated and orchestrated by GenAI-led models.

Moving on to additional highlights from the quarter. We extended our relationship with Victory Capital to provide IT infrastructure and data analytics support. Over the next five years, we aim to provide this client with new service management capabilities, improved service productivity, opportunities for cost savings and the ability for Victory Capital to cost effectively scale in support of business growth.

Additionally, we signed an agreement to provide engineering services to Gentherm, the global market leader of innovative thermal management and pneumatic comfort technologies for the automotive industry. Under this agreement, we'll expand our existing services to help develop a next generation of products aimed at elevating customer vehicle experiences.

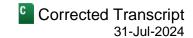
Our expertise in firmware development and verification and validation from the Mobica acquisition played a critical role in differentiating our value proposition. We have also seen increased demand for infrastructure-led transformation to cloud, boosted in part by our Thirdera business, which we acquired in the first quarter. And our platform investments have helped drive increased Gen-Al adoption. As of this quarter, we have over 200 clients on our Al-led platforms, including Neuro IT operations, Skygrade and Flowsource.

Now where are we with GenAl? We see one of the biggest opportunities for GenAl as tech for tech, which applies GenAl to our software development cycles. With higher cost of capital in recent times, we believe that the need to do more with less combined with the leveraging of Generative Al with lead companies into an era of hyper productivity. We believe this will fuel the next wave of digital transformation as clients seek to modernize the tech stack and reimagine business workflows with partners like Cognizant.

In fact, in recently released follow-on analysis to our 2023 study with Oxford Economics, 70% of the respondents globally indicated, they're not moving fast with GenAl. And 82% indicated a delay in execution could put them at a disadvantage. We are seeing a desire from our own clients to move more quickly.

Over the past few quarters, we have become more deeply involved in our clients' GenAl journeys. As of the end of second quarter, we have over 750 early client engagements, up from 450 in Q1, and we have over 600 opportunities in the pipeline compared to 500 last quarter. These early engagements have been across verticals with healthy activity in products and resources along with Financial Services and Health Sciences.

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We're seeing demand across four key areas: first, customer and employee experience; second, content summarization; third, content generation; and finally, tech for tech to accelerate innovation and technology development cycles.

As an example of our recent work, Cognizant designed and recommended a business and technology architecture for AI development for a multinational accounting and audit services firm. This work included identifying the relevant technologies, infrastructure, skill sets, processes and data required to support AI development across the organization. And we are building a strong partnership ecosystem to support our GenAI strategy.

This quarter, we have selected as an AWS GenAI competency partner, driven by our capabilities in addressing complex industry problems and our expertise in AWS-specific GenAI solutions. And we have signed a strategic collaboration agreement with AWS to bring smart manufacturing solutions powered by GenAI to market and transform manufacturing operations across various industries.

As another example, we helped set up the world's largest pharmaceutical company's AWS infrastructure as a part of their GenAl journey. We also automated the client's channeling of desperate data sources into a single vector data store to build a foundation for their GenAl programs.

In Health Sciences, we launched a first set of healthcare large language model solutions on Google Cloud's GenAl technology, including Google's Vertex Al platform and Gemini models. The suite of solutions addressing four workflows, marketing operations, call center operations, provider management and contracting. Our aim is to improve healthcare administrative processes and experiences for our clients and their clients.

We believe GenAl has become a catalyst for clients who are behind in their data modernization or cloud journey, and we're pursuing these projects to help them lay the foundation for enterprise-grade GenAl implementations.

In closing, I want to thank our employees around the world for their dedication to our clients and Cognizant. We have been executing well in a challenging macro environment. In the back half of 2024, we'll remain focused on our strategic priorities to drive revenue growth, become the employer of choice in our industry and to simplify our operations.

With that, I'll hand it over to Jatin.

Jatin Pravinchandra Dalal

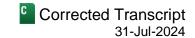
Chief Financial Officer, Cognizant Technology Solutions Corp.

Thank you, Ravi, and thank you all for joining us. Second quarter revenue and operating margin came in above our expectations. Despite customer behavior and discretionary spending trends remaining largely unchanged, strong execution and the ramp-up of large deals supported sequential revenue growth of 2.1% in constant currency. This provides us with revenue exit velocity going into Q3 and has allowed us to increase the midpoint of our organic revenue growth guidance for the full year.

Our cost optimization efforts, including structural actions under the NextGen program helped us deliver adjusted operating margins of 15.2%. This was a modest increase sequentially and 100 basis point increase from the prior year period. We are pleased with the cost savings we have achieved under the program, which allowed us to expand adjusted operating margin while funding growth investments.



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Now, let's turn to the details. Second quarter revenue was approximately \$4.9 billion, which Ravi mentioned, exceeded the higher end of our guidance range. This represented a decline of 0.7% year-over-year or a decline of 0.5% in constant currency. In constant currency, growth was approximately 50 basis points better than the high end of our guidance range. Year-over-year performance includes approximately 60 basis points of growth from the recent acquisitions.

Q2 bookings grew 5% year-over-year and were driven by midsized deals. Our trailing 12-month book-to-bill ticked up slightly to 1.4x from 1.3x in Q1. We continue to see a lengthening of contract durations driven by a shift to larger longer-term contracts. This has extended the revenue conversion timing, but also provided improved forward visibility.

As Ravi mentioned, we were pleased with the improved performance in Financial Services, which grew 5% sequentially. Our Health Sciences business grew over 3% sequentially with solid growth across payer, provider and life sciences customers. Products and Resources revenue was down modestly quarter-over-quarter, and down approximately 4% year-over-year in constant currency. The decline was due to ongoing discretionary spending pressure among our customers.

We have seen demand in areas like grid modernization and cloud modernization investments among our utility customers. We have also seen pockets of strength in the travel and hospitality sector, led by improved travel demand as well as interest in GenAl powered personalization to deliver differentiated guest experiences.

Our pipeline in products and resources remains healthy and we are excited to close the Belcan acquisition, which we expect will provide new growth opportunities in this segment. Communications, Media & Technology grew year-over-year, again, supported by recently completed acquisitions. We have also continued to benefit from the ramp of new business within comms and media, which has helped offset lower level of discretionary spending among the technology customers.

By geography, we were pleased with the growth in North America, driven in part by large deals ramping up over the last few quarters. However, other parts of the world, particularly Europe, remained challenged by soft discretionary spending.

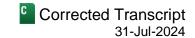
Despite this, we were also pleased with our return to sequential growth in our Rest of the World region, where we are seeing early progress from recently won large deals and new logos and a healthy pipeline of new opportunities.

Now, moving to margins. NextGen cost savings continued to progress and have helped us offset the margin impact of recent large deal wins. During the quarter, we incurred approximately \$29 million in costs related to NextGen, which negatively impacted our GAAP operating margin by approximately 60 basis points.

Excluding this impact, adjusted operating margin was 15.2%, an increase of 10 basis points sequentially and 100 basis points year-over-year. As a reminder, the prior year period included a 60 basis points benefit from an insurance recovery.

Our GAAP tax rate for the quarter was 22.7% and adjusted tax rate in the quarter was 23%, reflecting a benefit from the timing of discrete items. Q2 diluted GAAP EPS was \$1.14 and Q2 adjusted EPS was \$1.17.

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Turning to the balance sheet. We ended the quarter with cash and short-term investments of \$2.2 billion or net cash of \$1.6 billion. DSO of 80 days was up two days sequentially and increased five days year-over-year driven by our business mix. Free cash flow in Q2 was \$183 million, primarily reflecting the seasonality.

During the quarter, we returned \$226 million to the shareholders, including \$76 million through share repurchases and \$150 million through our regular dividend. At the end of Q2, we had \$1.6 billion remaining under our share repurchase authorization.

As of today, other than the expected closing of Belcan, we do not anticipate any material inorganic activity for the remainder of the year as our immediate focus is on closing the Belcan acquisition and its initial integration work.

We expect to return approximately \$600 million to shareholders in form of share repurchases and dividends in the second half of this year. This is expected to bring total capital return to the shareholders to approximately \$1.1 billion for the full year. These amounts exclude the expected additional share repurchase activity to offset the new shares we plan to issue as part of Belcan acquisition.

Turning to our forward outlook now. Our updated guidance does not include contribution from Belcan. We plan to update our outlook after the acquisition has closed, which we still expect to occur in the third quarter. There are no changes to the estimated financial impact that we provided at the time of the announcement.

For the third quarter, we expect revenue to be flat to up 1.5% year-over-year in constant currency. Sequentially, this implies a growth of 0.7% to 2.2% in constant currency. For the full year, our organic revenue growth outlook has modestly improved. We now expect revenue to be in the range of \$19.3 million to \$19.5 billion, which is a decline of 0.5% to growth of 1% year-over-year, both as reported and in constant currency.

Our updated guidance includes approximately 70 basis points of inorganic contribution versus our prior guidance of up to 100 basis points. This reflects the contribution from only our completed transactions. Therefore, at the midpoint, our organic growth outlook has improved by approximately 55 basis points.

Moving on to adjusted operating margin. We are pleased with our first half performance, and we continue to expect the full year to be in the range of 15.3% to 15.5%. Our guidance includes the expected impact of our merit cycle, which will take effect on August 1st. We expect this will be partially offset by the savings from our NextGen program and operational discipline.

For the full year, we anticipate net interest income of approximately \$80 million, which compares to \$60 million previously. Our adjusted tax rate guidance of 24% to 25% remains unchanged. Our full year free cash flow guidance is also unchanged, and we continue to expect it will represent 80% of net income. This includes the negative impact from \$360 million payment made to Indian tax authorities in the first quarter in relation to our ongoing appeal of our 2016 tax matter.

Our guidance for shares outstanding is unchanged at approximately \$497 million. This leads to our full year adjusted earnings per share guidance of \$4.62 to \$4.70, which reflects a \$0.07 increase in the midpoint versus our prior range of \$4.50 and \$4.68.

With that, we will open the call for your questions.

QUESTION AND ANSWER SECTION

Operator: Thank you. We will now be conducting a question-and-answer session. [Operator Instructions] Our first question comes from the line of Jim Schneider with Goldman Sachs. Please proceed with your question.

James Edward Schneider

Analyst, Goldman Sachs & Co. LLC Good afternoon and thanks for taking my questions. First of all, on Generative AI, helpful commentary, and Ravi,

you mentioned the 750 early client engagements. Could you indicate whether any of your clients are moving beyond the proof-of-concept stage? And what are those larger engagements - what form are they taking? And can you maybe quantify the amount of bookings you currently have tied to Generative AI at this stage?

Ravi Kumar Singisetti

Chief Executive Officer & Director, Cognizant Technology Solutions Corp.

Yeah. Thank you for that question. I think the one thing you want to know is Generative AI is diffusing into all our technology-led projects in a very, very fast way. So the ability to ring fence it and start to think about what it does to a technology, what it doesn't do to a technology or how do you place it back is always hard. So the best metric for us was to find out the number of projects we are doing around Generative AI.

So the number we gave this quarter was 750, which is up from 450 last quarter. So we're very, very pleased with the number of early engagements. We have 600 more in the pipeline. And if you remember, quarter two of last year, we spoke about 100 active engagement. So we've gone all the way from 100 to 750.

Now how much of this is going into real production work? I would say very small number of projects are going into production work. And that number is small because of multiple reasons. One is, as you get to production grade work, you need to start to think about your data architecture, you need to start to think about your cloud infrastructure. And you also need to start to think about the cost of compute, the availability of talent and everything else. So only a small minor portion of it is going into live production work.

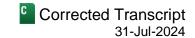
But what we are pleased is as we get past these inhibitors, if I may, we're going to see a sharpest curve. I actually believe the season going to be a sharpest curve. A lot of them are related to productivity and task automation. So the benefits are very tangible. And hence, it will go through the sharpest curve.

But progressively, we will start to see more projects related to innovation, more projects related to change in operating model. And in fact, one of the surveys we did just a few weeks ago, with 2,200 business executives from 15 countries, has also started to tell us that productivity doesn't mean just cost reduction. Productivity also means new revenue streams and new products and new services.

So we are, again, excited about the fact that if it is revenue generating, the acceleration to the sharpest curve is going to be much quicker. So that's one metric to know how well we are doing.

The second metric I would say, which I spoke about is, we have 200-plus clients on all our platforms, Al platforms. The AI platforms we have at Cognizant, are all related to how do you take foundation models and make them production-grade, be it accuracy of the models, be it governance, be it management, be it responsible Al. So these 200 clients are experimenting with us to make sure that they're getting ready for production because they're a part of our platform. So that gives me indication that there is a good momentum in the future.

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We also dissect this into four different categories. A lot of it is content aggregation and customer experience and employee experience. Again, the benefits in the business case are very tangible here. So we will see faster acceleration.

Then, of course, the biggest use case is tech for tech, which is applying into development cycles. The challenges in that particular case you have to share the productivity benefits with your clients. So the good news is it increases our win rates. And if we are ahead of the curve, we get to save some of that.

And the last one, I would say, is content generation, which is more creative. It will take a little longer time. So overall, we're very pleased with where we are. We are very pleased with the fact that some of this is leading to more structural work related to data and cloud, which by itself is a heavy lift for us, which will then get monetized into services dollars.

So that's broadly where the Generative AI story is. And I think the excitement about how much productivity we can generate for our clients and create a flywheel of this, makes it the biggest opportunity for us to tap into the future.

James Edward Schneider

Analyst, Goldman Sachs & Co. LLC

Thanks for that. And second one, if I may, on gross margins. In the quarter, revenue was up sequentially. Headcount was down, I believe, and utilization was up. So what were some of the factors that are pressuring the gross margins such as project pricing and the higher startup costs on large deals? And can you maybe comment on the prospects for expanding those gross margins over the next couple quarters?

Jatin Pravinchandra Dalal

Chief Financial Officer, Cognizant Technology Solutions Corp.

Sure. So, quarter two was a good execution quarter where we improved our utilization. We continue to deliver sequential growth while actually reducing the trajectory of employees in terms of the head count.

So overall, good execution, why you are not seeing it get reflected in the gross margin is really what you mentioned, the growth or the ramp-up of the large deals that we have won in past and they are ramping up and there is an initial investment of slightly lower margin as those deals ramp up.

And that's the reason that gross margin number has remained flattish between quarter one and quarter two. We are optimistic that as we move into quarter three, quarter four, you should start seeing a slightly better performance on gross margin as we get through quarter four.

Ravi Kumar Singisetti

Chief Executive Officer & Director, Cognizant Technology Solutions Corp.

Just to link back to your Al question on this, if you look at the math, we sequentially dropped by 8,000 odd people. And year-on-year, we dropped by 9,000 people. But we sequentially grew by 2%. And what that really means is, a part of it is running with tight utilization. A part of it is related to Al, doing work with lesser number of people, and therefore, creating a productivity benefit for us. So, just to add to the Al – the reason why some of that is explainable is also because Al and automation is starting to be applied to our projects.

James Edward Schneider

Analyst, Goldman Sachs & Co. LLC

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Thank you very much.

Operator: Thank you. Our next question comes from the line of Bryan Bergin with Cowen. Please proceed with your question.

Bryan C. Bergin

Analyst, TD Cowen

Hey. Good afternoon. Thank you. I wanted to ask on bookings. So, nice to see a return to growth here. And it does seem like you've had a recent uptick in deal activity just based on your announcements. Can you comment on the level of bookings that you would say are kind net-new work versus renewals? And just any common threads to highlight across the latest deals that were announced?

Ravi Kumar Singisetti

Chief Executive Officer & Director, Cognizant Technology Solutions Corp.

So let me take a shot at it, and I'll ask Jatin to add. We don't give the renewal and split of renewable and new business. But I can tell you one thing, that our new business is significantly higher than the renewals in 2024 versus 2023. So we're very, very happy about it.

The second is there is also new logos and expansion in the bookings. So we are, again, very pleased. One of the reasons why Financial Services grew well, I mean Financial Services grew sequentially after 2022, and it grew well, because we also opened new logos. We started to look for expansion in existing customers. So that's all contributing to our bookings.

We had five large deals with more than \$100 million, and we had two of them in the range of \$90-plus-million. In fact, all five of them actually had expansion in new business in the mix. So we are, again, very pleased about how the amount of work we're getting, which is new and expansion is increasing. Of course, the duration of deals is also increasing. On the higher end, I mean, the larger deals, above \$50 million, the duration is increasing. While it creates stickiness, but it also creates a little bit of a tail on when the revenue is going to be realized as we go forward.

Bryan C. Bergin

Analyst, TD Cowen

Okay. I appreciate that detail. And then my follow up on Belcan. So understanding you're still waiting to close the deal. I believe you mentioned it was estimated to be about 40 bps of a margin headwind and then, some revenue synergies over three years. Can you detail kind of the transitory costs, the deal cost in that 40 bps versus the structural margin of Belcan? And then just any further detail on kind of how you thought about the phasing the \$100 million plus revenue synergies over three years?

Jatin Pravinchandra Dalal

Chief Financial Officer, Cognizant Technology Solutions Corp.

Yes. So we – I mean, the numbers that you mentioned are accurate, 40 basis point of margin dilution and the synergy numbers. We will share a more detailed update on Belcan on closing, including making sure that our guidance then reflects the Belcan acquisition for the rest of the year. There is no new data point or update to the numbers that we had shared before at this juncture.

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Bryan C. Bergin

Analyst, TD Cowen

Thank you.

Operator: Thank you. Our next question comes from the line of Jonathan Lee with Guggenheim Partners. Please proceed with your question.

Jonathan Lee

Analyst, Guggenheim Securities LLC

Great. Thanks for taking my question and appreciate the insight here. I understand some of the efficiency gains you're seeing, but how much room do you have in utilization before perhaps runs too hot? And how are you thinking about pace of hiring for the remainder the year, particularly as you look to support on the deal-wins and pipeline? Additionally, any call-outs here around competition for talent given the higher attrition you saw?

Jatin Pravinchandra Dalal

Chief Financial Officer, Cognizant Technology Solutions Corp.

So, this is Jatin and I'll go first, and I'll request Ravi to add. I think so far, we are seeing stability in the talent marketplace. It is reflected in our attrition. We are seeing sufficient availability of the talent that we need to hire for the specific skill set that we need to hire from the marketplace. There will always be couple of skill sets, which are more hot or difficult to find than others. But on an aggregate basis, I think we still have a reasonably good market for talent as we look at the second half of the year.

Ravi Kumar Singisetti

Chief Executive Officer & Director, Cognizant Technology Solutions Corp.

Was there a first part of the question as well, Jonathan?

Jonathan Lee

Analyst, Guggenheim Securities LLC

Yeah, it was more about room you have in utilization before it perhaps runs too hot?

Ravi Kumar Singisetti

Chief Executive Officer & Director, Cognizant Technology Solutions Corp.

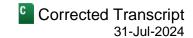
I think we still have some head space for sure as we exit quarter two. Certainly, not as - I mean, it's the headspace we have continued to sort of utilize and this is the third quarter of improvement in utilization. So we are continuing to improve it. We have some space. I wouldn't say it's a significant space, and we are managing the supply chain with that visibility of headspace and the demand which is coming into the door. And we are confident that we'll be able to manage the demand and supply chain equation well as we execute through the second half of the year.

Jatin Pravinchandra Dalal

Chief Financial Officer, Cognizant Technology Solutions Corp.

Yeah. So just to add some more color Jonathan on this. We are now at a spot where we have significant attractiveness in the market for employees to join us. I mean, our momentum in the market also is – also allows us – it gives us the ability to hire. We also have returners. In fact, we have a historic return of returners, as I call it. I mean, it is people coming back who worked at Cognizant before.

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And our fulfillment engine is a combination of four things: freshers, rotating talent inside the company, reskilling from the adjacencies and hiring lateral talent. All four, I think, we are getting better and better and better since the last 18 months. So we are gearing up for a high demand situation whenever, but we're going to be prepared for it.

Our two big industries, Financial Services and Healthcare, together is 60% of our business. They're both in great and in a good spot. So that gives us confidence. I mean these were two verticals where Cognizant's legacy and heritage was so strong. So we are back on those two verticals with a good positive momentum.

Jonathan Lee

Analyst, Guggenheim Securities LLC

Thanks for all the details there. How should we think about potential for stabilization around large-deal project margin, especially given some of the elongation of the duration in these large deals? And how are you thinking about pyramid structure around staffing these large deals?

Ravi Kumar Singisetti

Chief Executive Officer & Director, Cognizant Technology Solutions Corp.

Yeah. So large deals, and Jatin chip in as I complete. Large deals always have a upfront cost and downstream revenue kind of a thing, because you do transition and a lot of these are vendor consolidation, cost optimization kind of deal. So you will have to invest on transition and everything else. So there is lumpiness on how that works.

But we have now muscle to execute them pretty well. We have done this for 18 months now. We've been on the cycle of winning and delivering to large deals. So we're very confident of continuing on that process. We are not only doing this on application services now, which was the heritage of the historic muscle of Cognizant.

We are doing it in BPO and infrastructure services. And now we are starting to see good traction in the R&D. And as Belcan comes in, subsequently, we will – hopefully, as it get closed, we'll hopefully have more of it as well. So it's a much more comprehensive breadth of capability and the breadth of large deals, which we are executing on.

We are competing in the market and the levers to compete are not just arbitrage on labor, the levers to compete are also productivity levers powered by automation and AI and I think we are ahead of the curve. That's one of the reasons why we're winning more. It is a wallet share, which we are picking up from our peers. Jatin, do you want to add anything?

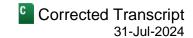
Jatin Pravinchandra Dalal

Chief Financial Officer, Cognizant Technology Solutions Corp.

Yeah. I think the only additional color is there are two ways of looking at a large deal sort of dynamics or financials. One way is that they initially do come with lower margins. But if you see the construct of a large deal, there are typically fixed price projects over a long-term period, which means your ability to improve overall pyramid into the company, deploy Gen Z, as we call them internally, our fresh talent, at the bottom of the pyramid is much better, your ability to execute on your automation goal is far superior in a larger program.

So overall, the second way of looking at a large deal is that you can really push the envelope of efficiency and productivity much better than what you would be able to do in a time and material construct. So it has also a positive angle to it as the deal matures.

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Jonathan Lee

Analyst, Guggenheim Securities LLC

Always appreciate the color. Thank you, guys.

Operator: Thank you. Our next question comes from the line of Rod Bourgeois with DeepDive Equity Research. Please proceed with your question.

Rod Bourgeois

Analyst, DeepDive Equity Research LLC

Okay. Great. Hey, Ravi, a couple of big picture questions. Over the last 1.5 years, you've been in a turnaround situation while also wrestling with a cyclical downturn in demand. You've definitely made progress on shoring up talent and the culture and you're now winning these large deals. I just wanted to see if you can now speak to like your main goals for the next phase of Cognizant's improvement process?

Ravi Kumar Singisetti

Chief Executive Officer & Director, Cognizant Technology Solutions Corp.

Rod, thank you for that question. I've always been a believer of layering performance and change. So for the first 18 months have been constantly making changes and generating performance and using the performance to make more change.

At the end of first year, we bought a company called Thirdera. And that was the time I started to believe that performance and change as you layer it. You also start to get the license to do some big bets, big – some big bets. So we made that big bet of buying Thirdera, which is the single largest ServiceNow stand-alone company. And right now, we're probably one of the top two players of ServiceNow in the market, and I'm very confident that journey will continue.

In the first half of this year, we started to think that we – our business has four vectors, as I said, tech services, BPO, infrastructure-led services, which is security, cloud, everything put together and ER&D. We always wanted to take another big bet and look for a different buyer group and look for a different industry muscle, if I may. And we took a bet on Belcan, which gives us the opportunity to be in aerospace and automotive, embedded software and engineering research and development, which is a different buyer group in any of our clients.

And we took a bet because we think that's going to increase the breadth of services, and it's going to give us a new vector for growth. So I think I'm going to pair – I'm going to layer the performance and change on a constant basis and keep looking for big bets so that we make this a resilient platform.

Remember, Healthcare and Financial Services, we are heavy on it. Now we're going to create muscle on manufacturing, industrial, automotive, aerospace, which is going to be a very different industry vector. We are – we will constantly keep looking for bridging those gaps in new industries and a breadth of capabilities and also expanding internationally as we go forward because we are over indexed on the US. So that will be my goal to create sustained momentum and create a resilient platform for our employees and our clients.

Rod Bourgeois

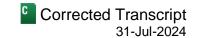
Analyst, DeepDive Equity Research LLC

Great. That's very helpful. Thanks for sharing that. And maybe I'll change my follow-up, given your answer related to Belcan. One of the questions that we're seeing right now, Capgemini recently cited weakened demand in



And therefore, I think the next 10 years are going to be much better.

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aerospace and automotive. Those are verticals that had been very strong over the last year at most players. Are you seeing similar trends in aerospace and automotive weakening? Or is that not really a concern, especially as you onboard the Belcan business?

Ravi Kumar Singisetti

Chief Executive Officer & Director, Cognizant Technology Solutions Corp.

Rod, that's a great question. Organically, we are seeing strength in automotive. Our pivot on Belcan is very simple. We think the next decade is going to be about digitizing everything physical. So we believe the industry is like manufacturing, industrial, automotive, aero. If you pivot into services, which are embedded software, pivot into services, which are digital in nature, there's significant headroom and there is very little spend in the last 10 years.

So therefore, I actually believe there is more space and more room for us. Our concentration is very high in Healthcare and Financial Services. So this actually gives us much – a very different industry vertical but it also gives us an opportunity to bring technology closer to the physical manifestation of these industries.

So that thesis of mine still holds. And I think with AI in the mix now, I actually believe the offerings we will now present to that industry segment are going to be as contemporary and therefore, we'll continue to flourish. So that's my thesis when I looked at Belcan, and that would be the thesis it would remain with me even now.

Rod Bourgeois

Analyst, DeepDive Equity Research LLC

Great. Thank you.

Operator: Thank you. Our next question comes from the line of James Faucette with Morgan Stanley. Please proceed with your question.

James E. Faucette

Analyst, Morgan Stanley & Co. LLC

Great. Thank you so much. Appreciate all the color. Encouraging to see the turn in the Financial Services, end market, et cetera. And it seems like we've heard some of the things from others. Kind of wondering what your visibility is on that part of your end market base? And what the nature of the work is that you're doing now, say, versus before it kind of turned down and if that's changed at all?

Ravi Kumar Singisetti

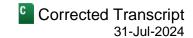
Chief Executive Officer & Director, Cognizant Technology Solutions Corp.

Financial Services, we've been working on it since 2023. 2023, we stabilized the teams. We ensured that the leaks we had – we were on the other side, I mean when consolidation happened, we lost business in 2022. We now are gaining market share when there is consolidation. And we did a very good job of leading that vertical with Industry Solutions. So that helped us to pivot into some of the small discretionary spend, which is coming back to – we rallied behind it.

So, the Industry Solution approach is stable team, walking the corridors, proactively pitching for value-led work, breadth of capability now. I mean, we are no longer a tech services firm. We have a breadth of capability. All of that has helped us to stabilize Financial Services. Of course, there's going to be variability quarter-on-quarter. But we feel confident about the fact that each one of those subsegments underneath it are in good shape. Our business in Americas and banking has sequentially done pretty well for two quarters in a row. So now we are



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starting to progressively take the same template to the international market so that we could replicate that success.

James E. Faucette

Analyst, Morgan Stanley & Co. LLC

Got it. Appreciate that. And then back on GenAI, I'm just wondering if you're seeing those projects crowd-out, other consulting priorities? And if so, which ones? Or are we still, as you suggest, it's still so early before moving to full production, implementation of GenAI projects that is not really having much of an impact?

Ravi Kumar Singisetti

Chief Executive Officer & Director, Cognizant Technology Solutions Corp.

That's a very good question. In fact, I agree with you that a lot of the consulting dollars are getting diverted to Generative AI. I mean, all the way from business case creation to governance to – some companies are reorganizing their – I know companies which are now saying, we need to reestablish an enterprise 2.0. So that process and technology can be together and it could be a distributed network organization versus a hierarchal setup.

So lots of organizational change and experimentation is actually led by Generative AI. So some of the discretionary is getting diverted there. But these are small prototypes. And as you finish the prototypes, you start to see the bottlenecks to take it to production. The good news is at least you start to know what the bottlenecks are, and then you start to work on it and then you take them to production grade. I have at least some projects which have started to go production grade.

I've mentioned it in my earnings, which is a pharmaceutical company taking Generative AI for drug development. An insurer using Generative AI to support claims which come in, which need to be corrected because there are fields which have not been filled up or there are clarifications. So I think at a task level, we are starting to see this go forward. The productivity studies we did in 2023, that's helped us also to put the business case up.

So we've seen in Healthcare in one of my clients, we have done auto adjudication of claims better using Generative AI. So the ability to make this a very outcome-centric business case will allow us to take this to more production-grade work and the ability to continue to look for new use cases will help us to build the pipeline as the old ones mature.

James E. Faucette

Analyst, Morgan Stanley & Co. LLC

Great. Appreciate all that color.

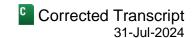
Operator: Thank you. Our next question comes from the line of Tien-Tsin Huang with JPMorgan. Please proceed with your question.

Tien-Tsin Huang

Analyst, JPMorgan Securities LLC

Hi. Thanks so much. Just wanted to follow up on your answer to Bryan, I think, question on bookings. Ravi, you mentioned duration. I always ask you, but I'd love to hear your updated thoughts on just the ACV versus TCV dynamic? Has that changed, improved, worsened? And then also on incremental bookings, where is the work coming from? Is it new work or takeaway from other vendors? Has that changed at all in terms of sourcing deals? Thanks.

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Jatin Pravinchandra Dalal

Chief Financial Officer, Cognizant Technology Solutions Corp.

Yes, sure. So I think fundamentally, not much change in ACV, as you can imagine, with the deal duration going up from 1 point – I mean, over longer term, it has to reflect in a slightly slower growth in ACV and that dynamics continue. However, we are clearly winning market share as we execute every quarter. So the deals that are ramping up or the deal announcement that we have done are really a reflection of new work that Cognizant is getting, sometimes in new accounts, but also in many accounts where we were present, but we were not addressing that segment of the work with our customer.

Tien-Tsin Huang

Analyst, JPMorgan Securities LLC

Great.

Ravi Kumar Singisetti

Chief Executive Officer & Director, Cognizant Technology Solutions Corp.

And there's also a focus on new logos. So it's a combination of new logos expansion and new work. And I can certainly tell you that the new work is outpacing the renewals, at least in 2024.

Tien-Tsin Huang

Analyst, JPMorgan Securities LLC

All right. Heard that, loud and clear. Thank you for that. Just my quick follow-up on the fourth quarter implied from the guide for the full year, it implies some sequential deceleration. Any callouts there beyond seasonality?

Jatin Pravinchandra Dalal

Chief Financial Officer, Cognizant Technology Solutions Corp.

Yes. So you're right, it does – at the midpoint of quarter three performance, it would imply a deceleration in quarter four, but that is really seasonality right now as we see it.

Tien-Tsin Huang

Analyst, JPMorgan Securities LLC

Terrific. Thank you for the time.

Operator: Thank you. Our next question comes from the line of Dan Dolev with Mizuho. Please proceed with your question.

Dan Dolev

Analyst, Mizuho Securities USA LLC

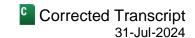
Hi, guys. Very strong results. Nice to see that. Can you maybe – I mean, the number one question we get from investors right now is like, have we seen the bottom in IT services spend? I mean, this is pretty much what everyone is trying to figure out. Can you maybe make a more general comment from your seat on where we are in the cycle? Thank you.

Jatin Pravinchandra Dalal

Chief Financial Officer, Cognizant Technology Solutions Corp.

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So it's a broad question. Let me address it from the context of Cognizant. Clearly, for us, we see growth as a guidance range that we have given for quarter three after a decline sort of a performance for – in [ph] past (00:58:03). So certainly, we are seeing an uptick and an improvement from where we were. So certainly, there is an uptick in the numbers in a positive growth trajectory as we progress through the year.

It's difficult to make a comment on a larger market as we covered in our prepared remarks, market still remains uncertain. But clearly, there are pockets where there are opportunities, and we are capitalizing on those opportunities as it's been reflected in our BFSI performance, as has been reflected in our health performance with both of which our largest sector, we have delivered very strong sequential numbers.

Ravi Kumar Singisetti

Chief Executive Officer & Director, Cognizant Technology Solutions Corp.

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Just to add to that. I said this before, we don't see deterioration or improvement. We see the market unchanged, as I call it. However, our execution, our fulfillment rates and our win ratios continue to be very strong. So therefore, we are winning wallet share in a market which has remained unchanged.

Dan Dolev

Analyst, Mizuho Securities USA LLC

Understood. And then maybe a follow-up on GenAl. I know everyone is talking about this, but would you feel comfortable, I guess, at some point, providing dollar value of the scope of the Al projects?

Ravi Kumar Singisetti

Chief Executive Officer & Director, Cognizant Technology Solutions Corp.



We have to keep thinking about what are the right ways to tell the market about Generative AI. It's a pervasive technology, and therefore, it diffuses into everything we do. And because it is diffusing so fast, you almost want to say – you almost don't know what to categorize as GenAI and what not to categorize as GenAI.

The only thing I can say is this – in this market, you could win using Generative AI, you could increase your win rates, you could create new deals, you could generate more momentum with your clients. Equally, you could flip it around and use it on your own-self to disrupt your own development cycles of our teams and create productivity, which you can share with your clients and then create a flywheel of winnability through it.

So I mean, right now, we are talking about projects which we are doing. We are talking about platforms and how many clients have onboarded on platforms. The traceability to revenues is – I mean anybody's guess, what you call Generative AI as Generative AI and what you can't? I mean today, data modernization project or a cloud modernization project, which we do because Generative AI is going to be the future, I actually can call it as Generative AI or I can say this is not Generative AI. However, it is creating more momentum because that foundation is needed for Generative AI.

So I mean, we have to evolve this to an extent where we could communicate to all of you in a much traceable way but nobody has found – I mean, nobody seems to have found the right way to do it. We are trying our best to tell you the traction we have.

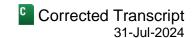
Dan Dolev

Analyst, Mizuho Securities USA LLC



Fair enough. Great results again. Thank you.

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Ravi Kumar Singisetti

Chief Executive Officer & Director, Cognizant Technology Solutions Corp.

Thank you very much.

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Operator: Thank you. There are no further questions. I would like to turn the floor back over to management for closing comments.

Ravi Kumar Singisetti

Chief Executive Officer & Director, Cognizant Technology Solutions Corp.

Thank you so much. Thank you for joining in today and looking forward to the next quarter, and thank you for all your support.

Operator: This concludes today's Cognizant Technology Solutions second quarter 2024 earnings conference call. You may now disconnect.

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