11-Feb-2020

Cognizant Technology Solutions Corp.

(CTSH)

Goldman Sachs Technology & Internet Conference

Copyright © 2001-2020 FactSet CallStreet, LLC

CORPORATE PARTICIPANTS

Karen Anne McLoughlin
Chief Financial Officer, Cognizant Technology Solutions Corp.

OTHER PARTICIPANTS

Brian Essex
Analyst, Goldman Sachs & Co. LLC

MANAGEMENT DISCUSSION SECTION

Brian Essex
Analyst, Goldman Sachs & Co. LLC

Okay. All right. Great. Well, thank you everyone for joining us. My name is Brian Essex. I cover security software with Goldman Sachs but I have an IT services' CFO here with me this afternoon. So, very pleased to have Karen McLoughlin, the CFO of Cognizant. Karen, thank you for joining us.

Karen Anne McLoughlin
Chief Financial Officer, Cognizant Technology Solutions Corp.

Thank you, Brian.

Copyright © 2001-2020 FactSet CallStreet, LLC

QUESTION AND ANSWER SECTION

Brian Essex
Analyst, Goldman Sachs & Co. LLC

Q

So, I wanted to maybe start off real quick. I saw that you reported earnings last week and that was very exciting, great stock reaction. You've been very busy. Perhaps it would be a good idea just to recap the release, the first time you've given your initial 2020 guide. And I was a little bit surprised of the stock reaction. So, maybe you can kind of put that in context and frame out guidance and your expectations for 2020.

Karen Anne McLoughlin
Chief Financial Officer, Cognizant Technology Solutions Corp.

A

Sure. So, as you said, we did release earnings last week and I think wrapped up the year on a slightly positive note. Certainly 2019 overall performance wasn't where we would have liked it to be at the beginning of last year. But we did end the year at 5.2% year-over-year on a full year basis constant currency revenue growth and in the fourth quarter it was 4.2% constant currency growth year-over-year. But we did exceed our fourth quarter revenue guidance and I think certainly as we went through the fourth quarter saw some continued strengthening in our North America business versus where it had been earlier in the year. So, I think we were very pleased to see that trajectory and the activity and the energy that's coming back into our North America business. So, that was good.

We did of course give our full year 2020 guidance in our call last week. And as we look forward into 2020, we have guided to revenue growth of between 2% and 4% on a year-over-year basis, constant currency and reported growth for 2020 at this point are the same, so, there's no differences there. But that does adjust for the fact that we are exiting our content moderation business. That will be about 110 basis point impact – negative impact to growth this year. So, I think that will continue to filter in as we go through this year.

From a margin perspective as we look forward to 2020 we have guided, as we talked about last fall, to an adjusted operating margin range of 16% to 17%. We did say that in the first quarter, we'll be slightly below that. We have, as many people know, started ramping up our investments in sales hiring over the last few months and we are in the middle of our large transformation program, but a lot of the head count reductions don't take place until later in the first quarter and into the second quarter and into the middle of the year. So, we won't get all of the cost saving benefits till later in the year while we're ramping up investments in sales as we move forward.

But I think versus where we were a few months ago and what I see happening in the business, I think folks have really gotten refocused on selling and being in front of clients. And I think certainly we are starting to see what I would call a little bit more stability amongst the team. Obviously, we went through a CEO transition last year and that was the first time we had an outside CEO. And so that brought with it its own sense of transition for the company, but you can really start to see people settling into their roles. Targets are out. We've got new sales comp plans in place. Our transformation program is well underway. So lots of things happening, a lot of activity, but we're very excited to see how the year plays out.

Brian Essex
Analyst, Goldman Sachs & Co. LLC

Q

Right. So, you mentioned the CEO transition. So, when Brian came in, I did see a lot of different personnel changes occur within the company. But maybe if you could frame out what would his management style has

Copyright © 2001-2020 FactSet CallStreet, LLC

been? How maybe his perception has changed within the company? And then how do you see his role with the transformation plan and the objectives that he's trying to achieve going forward?

Karen Anne McLoughlin
Chief Financial Officer, Cognizant Technology Solutions Corp.

A

Sure. I think first and foremost, Brian focuses on accelerating growth and returning to more of a growth story. And so, everything we are doing is really anchored around that and the notion that we are in a market that has tremendous potential. We are in a market where all of our peer groups have very low market penetration rates. So, there's lots of opportunity for us. And what do we do to position ourselves to take best advantage of those opportunities. So, first and foremost is getting the top line back.

He himself is personally on the road every week meeting clients as well as employees and other folks but really setting the tone for the whole company and you can see that energy permeating. At the same time, he is also very focused on the notion of accountability and doing what we say we're going to do. And so that's both on the top line execution, but as importantly on how we run the company instilling operating discipline, getting cost out where we can and should and really making ourselves fit for growth.

And so, when he came onboard last spring, we launched a number of initiatives around really looking sort of across the organization of where were the opportunities, what were the market opportunities for us from a selling side, what are the cost opportunities, how we manage that more effectively. That led to the Fit for Growth initiative that we announced at the end of October and now we're sort of in the execution mode of all of those various work streams. I'm leading that with Brian and the rest of the executive committee. We have a number of things underway but first and foremost is the growth story and then making sure that at the same time we're taking care of the operational infrastructure and discipline that we need to support that.

Brian Essex
Analyst, Goldman Sachs & Co. LLC

Q

Right. And maybe we'll get back to Fit for Growth in just a second. But maybe while you're on it, the outlook 2020, how would you frame the spending environment as you're going into 2020 and you're talking to clients about how their budgeting and where they're focused on spending, particularly relative to last year?

Karen Anne McLoughlin
Chief Financial Officer, Cognizant Technology Solutions Corp.

A

Obviously, we've seen a tremendous change this year. I mean client budgets tend to get locked down right about now. And so, we're not really seeing any change in timing of that nor have we seen any significant pullback or acceleration. I think it's fairly consistent with what we saw last year. We do think there's a little bit of concern maybe in the UK and a little bit of concern with some of our European banking clients. And so, we're certainly not expecting any significant recovery in banking as we look forward to this year. And we also talked on our call about not expecting a significant turnaround in our healthcare business.

But I think generally speaking it's steady. Obviously, we've seen some companies in the last few days talk about negative impacts potentially from the coronavirus. We haven't seen an impact yet on our clients and our business specifically, but that is something obviously that we will watch over the next couple of weeks but that's the only thing I think that I've seen a little bit of news about in the last few days post when we released our earnings.

Brian Essex
Analyst, Goldman Sachs & Co. LLC

Q

Copyright © 2001-2020 FactSet CallStreet, LLC

Right. And then how would you think about the gross margin and shareholder returns set up for Cognizant in 2020? And do you think about your guidance as a relatively conservative bar? Or are there meaningful levers that could push that higher or lower as you run through the year?

Karen Anne McLoughlin
Chief Financial Officer, Cognizant Technology Solutions Corp.

A

So, when we gave guidance and certainly as we think about revenue for the year, we try to give guidance that we think is prudent, but achievable, we certainly don't want to miss guidance. What happened in the beginning part of last year is something we don't want to repeat. So, we've certainly been thoughtful about the guidance and what we see in the marketplace, and we will continue to be prudent both as we give quarterly revenue guidance as well as the full year. And it would be great if there's upside, but that's certainly not assumed in the guidance at this point.

From a margin perspective, at the 16% to 17% rate that we've given, there are a number of puts and takes. We talked about, last call, about the fact that in 2019 or in 2020 for 2019 performance we're paying out lower than target bonus, and this year we expect to pay out [ph] least (00:08:46) target bonuses. So, we baked that into our assumption that has an impact on margins for making all these investments in the sales team. That obviously has an impact on margin and then offsetting that are the benefits that we'll get from the transformation programs and reducing our cost of delivery.

So, all of that gets us back into 16% to 17% range. But I think as I think about margin guidance for the year, first and foremost as I said, it's getting back to growth. And so, for any margin dollars we do have available to us, we will continue to reinvest those for growth and really trying to position ourselves well for the next few years.

Brian Essex
Analyst, Goldman Sachs & Co. LLC

Q

Okay. And then maybe on the Fit for Growth Plan, if you can maybe frame out some of the primary objectives. I mean you have a big company. It's hard to change things overnight. And sometimes some of the changes, you'll ask a company and they'll be perpetual in nature, we're always trying to make things more efficient. How much of this is short-term versus long-term? Is there a time horizon associated with Fit for Growth and what are the primary, I guess, objectives that you're trying to achieve?

Karen Anne McLoughlin
Chief Financial Officer, Cognizant Technology Solutions Corp.

A

Sure. So, as we've thought about the program, we think about it is a two-year initiative. But to your point, there'll always be a need for continuous improvement beyond that. But as I think about what we're doing right now and the next two years, first and foremost is getting the sales structure right and so making sure we have enough feet on the street making sure that our sales teams have enough support in the way of sales operations folks, solution architects, service line specialists, contract attorneys, pricing people, right, and surrounding them with that whole ecosystem of people that you need to actually go out and sell services to clients and that we are thoughtful about how we go to market, where we're going to market and that we're really putting the right resources against the right opportunities where we think we have the biggest opportunities.

So, we've been much more thoughtful I think as we went into this year and as we were planning as to how we align those teams against those client opportunities. So, that's a big piece for us. We've changed our comp plans for this year. So, our comp plans for the sales folks have a higher variable component to them. So, a little bit more risk, but a lot more upside for folks who perform well and we're also modifying those comp plans to ensure that

Copyright © 2001-2020 FactSet CallStreet, LLC

people are selling the right services. So, historically, in our comp plan a dollar of revenue with a dollar of revenue. As we look into 2020 and beyond, we really are targeting folks and incenting folks to go out and sell the services that we want them to sell. So, it's a big change, but I think certainly one that will set us on the right path.

At the same time, you have to make sure that you have an appropriate cost of delivery to deliver services. And I would almost bifurcate the business into two pieces. One is what we call sort of the heritage IT services business; and then you've got the new, the digital business. But certainly in the heritage business you have seen price compression over the last couple of years. And so, with that you have to make that you are bringing down your cost of delivery to clients, so that you can compete effectively in the marketplace.

And so, that is a big part of the Fit for Growth program. We talked back in October about a head count impact of about 10,000 to 12,000 people, about half of those we assume will leave the company in some form or another and the other half we will rescale into new digital skills. But that is really intended to bring down our cost of delivery and as well as our overhead costs as well. But to make sure that we can compete effectively in that marketplace. At the same time then you're investing in the digital skills.

So, not just new sales teams or additional sales teams, but really making sure you have the right resources that can deliver services to clients with [ph] new (00:12:42) mandate. So that is another big piece. And then, as I look at our overhead and the infrastructure to support the company, we're looking at our real estate footprint, all of our own internal systems and teams and so forth and really making sure that we've optimized those for the future.

Brian Essex
Analyst, Goldman Sachs & Co. LLC

Q

And then maybe, how did this transformation plan evolved? I mean, it seems as though that you're focused on some of these elements before Brian was announced. How involved was Brian in kind of taking that over the goal line and how long was the gestation period for developing this transformation plan?

Karen Anne McLoughlin
Chief Financial Officer, Cognizant Technology Solutions Corp.

A

So, we moved very quickly. I mean, some of this is work that we had started a while ago, but I think with the announcement of the CEO transition and so forth had maybe lost a little bit of the focus on that. So, when Brian joined last April and very quickly realized what was happening in the business, we moved very quickly in the few weeks after him joining to really stand up a bunch of new work streams and teams to go after all of this and we really tried to leave almost no stone unturned as we looked across the company over last summer.

So, we had several hundred people in the company looking at this and we did a lot of benchmarking work and really looking at ourselves as to where we thought the biggest opportunities lay for us. That culminated in what we announced on October 30th with the Fit for Growth program. So, we tried to move very quickly from benchmarking to planning and now into execution and each of the work streams was led by an executive committee member. And today, as we have the transformation office that is helping with execution again there are still executive committee members driving each piece of this.

Brian Essex
Analyst, Goldman Sachs & Co. LLC

Q

Right. Okay. And I believe I saw $500 million to $550 million of gross cost savings over a two-year period. How do we think about the net savings and what factors may offset that number in terms of what you might decide to plough back into the business?

Copyright © 2001-2020 FactSet CallStreet, LLC

Karen Anne McLoughlin
Chief Financial Officer, Cognizant Technology Solutions Corp.

A

Sure. So, I think about for this year, for 2020, we talked about a number of about $450 million that will actually grow to $550 million in 2021. And so if you think about the $450 million today and the fact that we've guided margins to 16% to 17%, so if you assume we're in the middle of that range from a guidance perspective, we landed at about 16.6% last year. So, when you factor in the fact that we are replenishing our variable comp plan so back to a 100% target and the investment in the sales people as well as other investments we're making in the business this year such as increasing our academy training programs for all the rescaling and so forth, that sort of offsets – those things all essentially offset the $450 million of benefits that we'll get this year. So, it's essentially neutral. And then, obviously, as we look into 2021 we will determine what investments we need to continue to enhance.

Brian Essex
Analyst, Goldman Sachs & Co. LLC

Q

Okay. And then is the idea to establish a cadence of gradual improvement over time and are you committing to a certain level of margin and revenue growth performance? And then how do you anticipate performing to those expectations over time?

Karen Anne McLoughlin
Chief Financial Officer, Cognizant Technology Solutions Corp.

A

So, we certainly have not given long-term margin guidance yet, and we'll do so when we feel like it's appropriate and have a better sense of what we think that is. Right now it really is about what do we need to do to get the growth back and what are the investments we need to make. Obviously, we'll see as we get later into this year how the productivity of the new sales hires is starting. We haven't assumed that they get to full productivity until about seven quarters after they start. So, we have given ourselves a reasonably long ramp period. But for the folks that we brought on in Q4 of last year, we should start to see some benefits as we get into the back part of this year. So, that will give us a bit of a sense of how that investment is trending and then we'll decide obviously accordingly how to take that.

Brian Essex
Analyst, Goldman Sachs & Co. LLC

Q

Okay. And then it's interesting that it seems as though your business is evolving towards more – one of more exposure to digital and cloud growth from traditional outsourcing services. I think I've seen it framed out by management in a couple of different ways. But if we think about the legacy business, where your entry point into a new business may evolve from the consulting side, how might that be changing with the way that you're trying to take the business going forward?

Karen Anne McLoughlin
Chief Financial Officer, Cognizant Technology Solutions Corp.

A

I think it's still important to have a really strong consulting practice and it's interesting our long-term relationships with our clients, we have very strong client relationships and always have. We've been known for client centricity and that's really been one of our strong points. To make the shift to digital, it's certainly helpful to have those strong client relationships. The key is can you expand those relationships beyond just the CIO organizations?

So, while the CIOs team plays a very critical role in a lot of the digital transformation work, a lot of the idea generation and the decisions of who to partner with and what work to do are being done beyond just the CIO organization and oftentimes with the CEO, COO, CMO, CFO, et cetera, and other business unit leaders. And so

Copyright © 2001-2020 FactSet CallStreet, LLC

to make that transition in the relationship you really do have to have very strong client partners who are fundamentally business people as well as potentially technology people and you have to have a strong consulting frontend who can help with those introductions and those relationships.

So, I don't think that's changed necessarily, but clearly clients are looking for really strong business partners who can come with a point of view and with a perspective and really have a seat at the table both with a client and client meetings potentially with their board as they're thinking about some of these very important strategic decisions. And so, you really do have to make sure you have the right people who can have those conversations.

Brian Essex
Analyst, Goldman Sachs & Co. LLC

Q

Got it. Maybe how much of your business is shifting away from your own internal sales versus partnerships with maybe outside consulting firms that build practices around certain ISVs and go-to-market that way. I noticed that several of your competitors have been very acquisitive like buying up some of those areas of digital expertise around those ISV platforms. What's your perspective on that? And I notice that you've done a little bit of M&A yourself relative to historical how you think about growing the business and maybe focusing a little bit more on that aspect of your kind of go-to-market strategy?

Karen Anne McLoughlin
Chief Financial Officer, Cognizant Technology Solutions Corp.

A

Yeah. No. I think partnerships in general have become a much more important part of the go-to-market story. Historically, if you go back 6, 10 years ago we tended to not have a lot of strong partnerships and we would certainly help a client with decisions around solutions and so forth, but we tended to be much more product agnostic. And in today's world you must have strong partnerships with a number of different types of firms including the hyperscale firms and then specialized firms like a Temenos or a Guidewire or so forth. And it's okay to go-to-market like that and that is a bit of a change for us and it is certainly something that Brian has accelerated our thinking about and the investments that we make in those partnerships.

So, we've talked to on our call last week about investing particularly in our relationships with the hyperscale firms and those partnerships, some of that will come through acquisitions that we do like the two transactions we announced last week with Code Zero, which is already closed, and then EI-Technologies, which are both Salesforce partners. We will continue to ramp up those types of investments to support us. And we think those are great opportunities to really go-to-market together and drive a lot of growth going forward.

Brian Essex
Analyst, Goldman Sachs & Co. LLC

Q

Maybe digging in a little bit on digital transformation. I mean, there's a number of different headwinds to like some legacy outsourcing business particularly kind of that in India and one is the impact that DevOps may have in the test and development space as well. How are you thinking about kind of with that framework of – it also seems as though Brian is really focused on bringing in and accelerating the quality of employee at the company. How are you, one, transforming some of the head count that you may have offshore? And then two, how are you kind of migrating to the higher quality across the company to kind of address some of the better growth opportunities ahead of you?

Karen Anne McLoughlin
Chief Financial Officer, Cognizant Technology Solutions Corp.

A

Copyright © 2001-2020 FactSet CallStreet, LLC

I think about [ph] less as quality of (00:21:29) – we have a lot of really talented people in the company and very strong technical skills. I do think and what you're saying is us trying to enhance some of the client relationships, okay, that's really critical. I do think as you get more into digital work in today's world anyhow that work does tend to be more on site and so there is a shift in how and where you hire people. And obviously that's a big change in the model that we're working on.

And you do have to have people who can come with a perspective, right. And so, you do need folks who have a little bit more of that consulting background, again are comfortable having a business conversation and providing an opinion to a client versus just saying we'll take your request and we'll go execute that for you, right. If you're truly going to be a digital partner today, you must bring perspective and you must bring solutions to the table. And so, really making sure that we have enough of those people is a lot of what we're doing.

Brian Essex
Analyst, Goldman Sachs & Co. LLC

Q

Right. One of the comments that you made earlier on is external CEO hire. And I just wanted to ask questions I think that's really important with all the IT services vendors on culture. How do you see the culture changing at Cognizant? And do you think you're at a point now where culturally you're at a steady state? Or do you think it's an ever-changing environment. And just overall sentiment within the company of around the way that employees view the workplace and the opportunities that are ahead of them.

Karen Anne McLoughlin
Chief Financial Officer, Cognizant Technology Solutions Corp.

A

Yeah. I think in terms of the culture, the Cognizant culture has always been one that was designed for growth and always focused on being extremely client-centric. And those are key parts of our DNA that we need to make sure we retain and I'm very confident we will. That is Brian, right, very focused on that and that is what he wakes up every day and thinks about it.

I think there is a part of our culture that we're working on very quickly, which is to ensure that we get back to having a culture of meritocracy. I think we lost that a little bit over the last couple of years. And so, that notion of we do what we say we're going to do, if you do that you do it well you will be rewarded and if you don't there will, unfortunately, be consequences for that. That was a little bit of a change last year as it became apparent to folks that we were doing that and I'm sure we will go through a little bit more of that change as we get into this year. But the reality is that people are motivated by success and successful people want to be rewarded. And so, your top performers will rise to the top in a culture like that and we're looking forward to that.

Brian Essex
Analyst, Goldman Sachs & Co. LLC

Q

Great. I want to give an opportunity for anyone in the audience that might have a question. I have more to go, if you want me to come back I can do that. But I just wanted to open it up to see if there is anyone that might have a question. I think, maybe if you can wait for a mic, we have one in the back.

Q

Thanks. Yeah. So, my question was you've talked a lot over the last several months about being under-represented on the international side. And so, maybe just walk through what you're doing to kind of fill that gap and how M&A might be involved going forward in filling that gap?

Copyright © 2001-2020 FactSet CallStreet, LLC

Karen Anne McLoughlin
Chief Financial Officer, Cognizant Technology Solutions Corp.

A

Yeah, sure. So, growth markets needs to be that [ph] for us (00:25:20) as you said, right, our North America business is still over 75% of the business. And while that's terrific and we're excited to see that business continue to get better, it really is important that we drive significant expansion outside of North America as well. There are very significant markets in Europe and Asia and elsewhere and we are under-represented there.

A lot of the investments that we're making in these new sales hires are in the growth markets. So, from a percentage perspective of where the head count is going, it is weighted towards those marketplaces and we will continue to add more talent to those teams to accelerate the growth there.

From an acquisition perspective, for last several years now, if we can find good acquisitions particularly in Europe that we like – we've done a number of them, we've done acquisitions in Australia, small one in Japan, we will continue to look for those acquisitions. First and foremost, we think of acquisitions as an enabler of our strategy, we don't view them as growth in and of themselves. So, we really want to make sure that they do align with our strategy, that they are acquisitions that we can integrate effectively because at the end of the day, this is a people business.

And so, when we buy companies we really look at the talent and culturally do they align with us. Are there things that they are bringing to Cognizant that we don't have already ourselves or that we can't build faster or cheaper? But certainly we try to put a focus on where those acquisitions are, and if we can find them outside of North America that's clearly a homerun for us. So, we will continue to use that as a vehicle as well.

Brian Essex
Analyst, Goldman Sachs & Co. LLC

Q

Great. Any others from the audience? I think we have one in the middle here. Please [indiscernible] (00:27:08) the mic.

Q

I think in the healthcare and financial services verticals, you guys have seen an impact from some consolidation and then in-sourcing trends as well. Can you just talk about both of those trends and maybe where we are or early/late innings and how you see that impacting the business?

Karen Anne McLoughlin
Chief Financial Officer, Cognizant Technology Solutions Corp.

A

Yeah. So, I'll talk about healthcare first. So our healthcare business last year was impacted by a couple of things. As we talked about we had four clients who merged into two companies and we went through a large contract renegotiation with those clients that did negatively impact revenue last year by about $100 million. And then, we had one other client that was in-sourcing, launching a captive, which also impacted us negatively.

With the acquisitions, we will begin to lap the impact of that as we get into the second quarter and we do expect to see some recovery in those clients, although not to where we were in 2018. So, I think healthcare growth overall will continue to be lower than company average, but certainly not as bad as it was in 2019. So, I think that's a positive.

Copyright © 2001-2020 FactSet CallStreet, LLC

On the financial services side, in banking, we continue to have challenges with few of our large European headquartered banks. Now, some of those banks are clients that we do work for around the globe. So, it can impact different regions of our revenue, but they're headquartered in Europe. And then one of them is a large client in Europe, it's really all the work is done in Europe for that client. So, I think we will continue to see pressure in those clients.

I feel better about our North America banking relationships. I do think we've seen some good progress there, still again growth that is slower than company average but we have a new banking leader. He's been very focused in his first couple of months, looking at the team, thinking about how they go-to-market, what are the solutions they're taking to market and really being focused on how they're going to do that. So, obviously, we'll have to see how the productivity pays off there. But I feel better about that market, I think Europe we still have a little bit of work to do with our banking clients.

Brian Essex
Analyst, Goldman Sachs & Co. LLC

Q

On that point, some of the different headwinds you're seeing in banking and financial services and healthcare, how do you anticipate that might affect your linearity through the year, and the confidence in ability to kind of reaccelerate growth as you kind of progress through the year?

Karen Anne McLoughlin
Chief Financial Officer, Cognizant Technology Solutions Corp.

A

So, put the content work aside for a second because excluding that what we would have expected to see this year is a bit more of a normal seasonal pattern with a little bit of a increase in the back half of the year over what you might normally expect. So, typically, Q1 tends to be a little slow for us and then client budgets get released and we see growth in Q2 and Q3 and then Q4 tends to be a little slow.

This year, I would have expected that to be a little different only in the sense of as we get into the fourth quarter, we would expect to see a little bit of this acceleration from the new sales hires. So, that would have been the ramp for this year. The problem is when you offset that with the content services business going away. That's about a 110 basis point negative impact to the year. First quarter is about $20 million to $25 million and then that will build as we get into the back part of the year. And essentially then, by the time we get to the end of this year, there'll be a little spillover into 2021, but we'll get through most of that exit this year.

So, when you factor that in, I think what you're actually going to see is probably much more stable growth rates year-over-year throughout the year. And so, you may not see that typical seasonality quite as much as we might have.

Brian Essex
Analyst, Goldman Sachs & Co. LLC

Q

Maybe I want to hit too on an update to your view on shareholder return. With the changes that you have occurring and I saw that you increased your dividend as well. How are you thinking about shareholder return priorities for uses of cash? And then really how you kind of set your goals going forward and what shareholders should expect on that front?

Karen Anne McLoughlin
Chief Financial Officer, Cognizant Technology Solutions Corp.

A

Copyright © 2001-2020 FactSet CallStreet, LLC

Sure. So, if you think about November 18 (sic) [November 16] when we held our first Investor Day, we had outlined a framework there that was roughly 50% for buybacks and dividends, 25% of our annual free cash flow goes to India and the remaining would be used for M&A. And then what we had said was we knew we had some excess cash on the balance sheet at the time and if we wanted to or needed to, we could obviously add some levers to the balance sheet for funding acquisitions.

The framework – we haven't really changed that framework per se. This year the guidance that we've given we did take the dividend up and obviously that's something that over time we want to be able to continue to do. Buybacks, we've assumed share neutrality. So, it's a little bit less than the 25%, if you've done 25%, 25% to make the 50%, it's slightly less, but fairly close.

And then we'll preserve obviously the remainder for what doesn't go to India for M&A and other investments in the company and continue to try and ramp the volume of acquisitions, we've announced two already this year. We hope to continue to do more. Not that we really hit pause on acquisitions last year, we didn't per se, but certainly when Brian came in he wanted to make sure he understood what his strategy was going to be, where he wanted his focus to be and making sure that we align our acquisitions against the strategic imperatives for the company. So, I think we've got that outlined now and we've got the corp dev team really focused on how they can go execute.

Brian Essex
Analyst, Goldman Sachs & Co. LLC

Q

Great. And then I noted that there were a few tax changes kind of on the horizon. How might that – it's kind of interesting what's going on particularly in India with the tax situation. So, maybe frame that out, where do we stand now, what could change going forward and how might that impact where you generate and where you I guess utilize some of that cash?

Karen Anne McLoughlin
Chief Financial Officer, Cognizant Technology Solutions Corp.

A

Sure. So, two things that have happened in India in recent weeks. So, in the fourth quarter, the government announced a change to the corporate tax rates. They lowered the rates effectively from about 35% to 25% and that's effective this year. Companies can elect when to – if and when to adopt the lower tax rate. Now, if you adopt the lower tax rate, so, in our case, today, we would have to forego any of our remaining SEC tax holidays, as well as we wouldn't be able to utilize that carry forward asset we have on the balance sheet. And for us that's a big impact.

So, our effective tax rate today in India is – we don't break it up but close to the 25%. So, we would really get no benefit today. The benefit for us comes down the road because if they had not lowered the tax rate, what would have happened over the next few year is our effective tax rate in India would have gone up as the holidays expired and as we utilized our carry forward. So, that's the big benefit for us is really avoidance in the future versus true savings. But that's a good thing, we're very happy to do that.

The second thing that they announced last week as part of the preliminary budget was a change to the dividend distribution tax. So, as most people know, it's been very expensive for us to get our cash out of India . If we had wanted to in recent years, the dividend distribution tax was about 20%. Depending on the structure of your company, that tax rate has dropped and it can be in the range of 5%, 10%. There's different factors that contribute to that.

Copyright © 2001-2020 FactSet CallStreet, LLC

Some of the things that we're looking at, one is this is not yet law. So, obviously, we have to wait for it to become law. But there are some implications to us if we bring the cash out in terms of interest income and some questions around do you pay the tax just on cash? Do you pay it on accumulated earnings? So, there's a lot of questions and things that we're looking at now. And obviously, if it becomes law, we'll come back with some thinking around that.

Brian Essex

Analyst, Goldman Sachs & Co. LLC

All right good stuff. I think, with that, we're out of time. So, thank you very much for joining us and thank you for all for attending. Appreciate it.

Karen Anne McLoughlin

Chief Financial Officer, Cognizant Technology Solutions Corp.

Okay. Thank you.

Disclaimer
The information herein is based on sources we believe to be reliable but is not guaranteed by us and does not purport to be a complete or error-free statement or summary of the available data. As such, we do not warrant, endorse or guarantee the completeness, accuracy, integrity, or timeliness of the information. You must evaluate, and bear all risks associated with, the use of any information provided hereunder, including any reliance on the accuracy, completeness, safety or usefulness of such information. This information is not intended to be used as the primary basis of investment decisions. It should not be construed as advice designed to meet the particular investment needs of any investor. This report is published solely for information purposes, and is not to be construed as financial or other advice or as an offer to sell or the solicitation of an offer to buy any security in any state where such an offer or solicitation would be illegal. Any information expressed herein on this date is subject to change without notice. Any opinions or assertions contained in this information do not represent the opinions or beliefs of FactSet CallStreet, LLC. FactSet CallStreet, LLC, or one or more of its employees, including the writer of this report, may have a position in any of the securities discussed herein.

THE INFORMATION PROVIDED TO YOU HEREUNDER IS PROVIDED "AS IS," AND TO THE MAXIMUM EXTENT PERMITTED BY APPLICABLE LAW, FactSet CallStreet, LLC AND ITS LICENSORS, BUSINESS ASSOCIATES AND SUPPLIERS DISCLAIM ALL WARRANTIES WITH RESPECT TO THE SAME, EXPRESS, IMPLIED AND STATUTORY, INCLUDING WITHOUT LIMITATION ANY IMPLIED WARRANTIES OF MERCHANTABILITY, FITNESS FOR A PARTICULAR PURPOSE, ACCURACY, COMPLETENESS, AND NON-INFRINGEMENT. TO THE MAXIMUM EXTENT PERMITTED BY APPLICABLE LAW, NEITHER FACTSET CALLSTREET, LLC NOR ITS OFFICERS, MEMBERS, DIRECTORS, PARTNERS, AFFILIATES, BUSINESS ASSOCIATES, LICENSORS OR SUPPLIERS WILL BE LIABLE FOR ANY INDIRECT, INCIDENTAL, SPECIAL, CONSEQUENTIAL OR PUNITIVE DAMAGES, INCLUDING WITHOUT LIMITATION DAMAGES FOR LOST PROFITS OR REVENUES, GOODWILL, WORK STOPPAGE, SECURITY BREACHES, VIRUSES, COMPUTER FAILURE OR MALFUNCTION, USE, DATA OR OTHER INTANGIBLE LOSSES OR COMMERCIAL DAMAGES, EVEN IF ANY OF SUCH PARTIES IS ADVISED OF THE POSSIBILITY OF SUCH LOSSES, ARISING UNDER OR IN CONNECTION WITH THE INFORMATION PROVIDED HEREIN OR ANY OTHER SUBJECT MATTER HEREOF.

The contents and appearance of this report are Copyrighted FactSet CallStreet, LLC 2020 CallStreet and FactSet CallStreet, LLC are trademarks and service marks of FactSet CallStreet, LLC. All other trademarks mentioned are trademarks of their respective companies. All rights reserved.