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Cognizant Technology Solutions Corp.

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MANAGEMENT DISCUSSION SECTION

Operator: Ladies and gentlemen, welcome to the Cognizant Technology Solutions' Fourth Quarter 2021 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] I would now like to turn this conference over to Mr. Tyler Scott, Vice President, Investor Relations. Please go ahead, sir. You may begin.

Tyler Scott

Vice President, Investor Relations, Cognizant Technology Solutions Corp.

Thank you, operator, and good afternoon, everyone. By now you should have received the copy of the earnings release and investor supplement for the Company's fourth quarter and full year 2021 results. If you have not, copies are available on our website, cognizant.com. The speakers we have on today's call are Brian Humphries, Chief Executive Officer; and Jan Siegmund, 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 risk and uncertainties as described in the company's earnings release and other filings with the SEC.

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

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

Brian J. Humphries

Chief Executive Officer & Director, Cognizant Technology Solutions Corp.

Thank you, Tyler. Good afternoon, everybody. Throughout 2021, clients have meaningfully accelerated spend on digital transformation initiatives, accelerating the demand for IT services. Elevated attrition in key digital scales is, however, a direct consequence of this, creating revenue fulfillment challenges and cost pressure that need to be carefully navigated. I'm therefore pleased that we had another quarter of solid execution, delivering against our commitment to clients and to you, our shareholders.

Fourth quarter revenue was $4.8 billion, up 14.5% year-over-year in constant currency, above the high end of our guidance. Growth was led by digital, which grew 20% year-over-year. Fourth quarter adjusted operating margin was 15.3%, and full year adjusted operating margin was 15.4%, in line with our guidance.

During the quarter, we also progressed against our key strategic initiatives, including scaling our digital capability, globalizing the company, helping our clients be successful by leading with greater industry insights and solutions and repositioning the Cognizant brand.

Turning now to industry segments, our recovery in Financial Services continued with fourth quarter growth of 19% year-over-year in constant currency. This includes an approximate 9 percentage point benefit from the impact of the prior year charge related to Samlink. As you know, we've been rebuilding our strength in Financial Services by refreshing our leadership in client-facing teams, strengthening our partner engagement, shifting our portfolio of services to more attractive market segments and sharpening our focus on priority industry solutions and clients. We expect to build further on this progress in 2022.

As we reposition Cognizant as a digital transformation provider in larger banking clients, we've complemented this with sustained momentum in regional banks. KeyBank, where we've just renewed our engagement as their primary digital partner, is a great example of this. We will further enable their digital transformation by digitizing their products to increase their digitally-active customers to approximately 85%, by driving remote self-service growth by more than 40%, by automating front-to-back processes and by migrating more than half of their application portfolio to the cloud.

In insurance, we see continued demand for core modernization and digital transformation, including cloud and analytics. Unum, a global leader in disability insurance and group benefits, is partnering with us to pursue their digital transformation focus on agent and customer experiences and associated analytics. These digital solutions enhance our existing application development and maintenance services relationship with Unum.

And for a long-time client, Royal London, the UK's largest mutual life, pensions and investment firm, we're now extending our partnership to reimagine their customer engagement through personalized, seamless, connected customer journeys enabled by cloud, data and customer-centric principles.

In Healthcare, revenue grew 8.2% year-over-year in constant currency. We've substantially increased our competitiveness in Healthcare by investing in digital solutions, domain expertise and partnerships, and by modernizing our core platforms. We've seen continuing momentum in our TriZetto product business, which grew 13% in 2021. We continue to add new footprints and in 2021 increased a number of overall members supported by our platforms to approximately 210 million.

We see solid commercial momentum across our Healthcare payer and provider business. For instance, Humana, a large national payer, is modernizing and moving their legacy ecosystem to the cloud and has chosen Cognizant as a partner for agency, marketing and clinical transformation. These initiatives will help improve Humana's customer and employee satisfaction, reduce costs and enhance the delivery of integrated personalized experiences to their members.

We also have momentum with next-generation healthcare companies like Reliq Health Technologies, a rapidly growing global telemedicine firm, which turned to us to expand their care management capabilities. Reliq will leverage Cognizant care management services to support the deployment of their care platform across managed care organizations, hospital networks and health insurance providers.

In life sciences, we partnered with AbbVie, a leading global biopharma company, to help advance their digital transformation in safety and risk management, which will improve patient care and outcomes. Through our digital health consulting services, augmented by capabilities in human-centered design and digital product engineering, AbbVie can understand the needs of patients and care providers, design fit-for-purpose solutions that support the patient journey and incorporate feedback for ongoing innovation. These improvements will help AbbVie better support patients and care providers across a broad range of therapeutic areas and products.

Within Products and Resources, we continue to deliver our excellent growth in client success across travel and hospitality and in manufacturing, logistics, energy and utilities. Drawing on our extensive experience helping automakers streamline their operational tasks, Volvo Cars chose us to help harmonize their finance and accounting and procurement processes and implement intelligent process automation to support their digital transformation. This is a great example of our growing momentum in digital business operations, which significantly outpaced the BPO industry in 2021 and is set to continue to gain share. Top line growth has been fueled by momentum in intelligent process automation and strength in our digital-native client portfolio.

Our work at Grundfos, a global leader in water technology and the world's largest pump manufacturer, perfectly illustrates our growing digital credentials. Grundfos initially selected Cognizant to establish an IoT-based intelligent platform to gather real-time pump data from the sensors and perform analytics to prevent, predict and respond to issues caused by leakages. Based on this success, we've since been selected to build a modern enterprise system based on SAP S/4HANA.

Finally in Communications, Media and Technology, we saw continued strength in technology, in particular, where we've sustained strong double-digit growth over the past three quarters.

Turning now to bookings, which grew 22% year-over-year in the fourth quarter, our second consecutive quarter of 20%-plus growth. Full year 2021 bookings growth was in the mid-teens. We entered 2022 with a healthy book-to-bill ratio of 1.2. Throughout the year, our bookings strength, which has been fueled by digital, has been broad-based across industries and geographies.

Moving to the macro demand environment, industry demand remains robust and I expect it to continue throughout 2022. Clients are embracing digital operating models to become more efficient, agile, automated, scalable, innovative and indeed, secure whilst also responding to the expectations of their customers and employees for hyper-personalized experiences.

Continuing to scale our digital capabilities is at the heart of our company strategy. Digital represented 45% of our revenue mix in Q4. As we noted during our recent investor briefing, we believe digital can become 55% to 60% of revenue in the coming years. Reflecting our strength in digital credentials, during the fourth quarter, we were named an industry leader in 17 new industry analyst reports. They highlighted the company's client partnerships, scalability, digital capabilities and expertise as factors in recognizing our leadership.

Accelerating digital is not only a driver of double-digit revenue growth and improved margin, it also fosters greater client intimacy and higher levels of employee engagement as we partner on strategic transformation projects that leverage advanced skills.

Moving on now to an industry phenomenon, you are accustomed to hearing about the unprecedented competition for talent, reflective of the industry-wide demand supply and balance in key digital skills. Fourth quarter voluntary attrition moderated a little to 31% on an annualized basis or 28% on a trailing 12-month basis. As a reminder, when we measure attrition, we count the entire company, including trainees and corporate across IT services and BPO. We've been working aggressively to mitigate attrition levels whilst intensifying our efforts and focus on employee training, promotion cycles, professional development and total rewards.

During 2021, we also facilitated more than 14,000 job moves across 40 countries, continued to revitalize our campus recruitment program in India, established new compensation measures and a revised promotion cycle to retain employees and invested heavily in upskilling. In fact, our associates completed 23 million hours of learning and consumed 130,000 courses in 2021. Given that we compete on our knowledge and skills, we're proud to have won 42 awards for excellence in learning and development from the Brandon Hall Group, often considered the leading independent HCM research analyst firm.

We more than offset elevated attrition levels in 2021 by accelerating our hiring, allowing us to increase company head count by 14%. I'm pleased to say that in recent years we've made meaningful progress in correcting our delivery pyramid by significantly increasing the number of college graduate hires onboarded in India. In 2021, we added a record 33,000 college graduate hires in India, up from 17,000 in 2020. In 2022, we plan to add approximately 50,000 in India.

Digital acquisitions have also brought incredible talent to Cognizant. During 2021, we completed seven acquisitions that extend our digital leadership, most recent being our fourth quarter acquisition of Devbridge. This software consultancy and product development firm expands our software product engineering capabilities and global delivery footprint by adding more than 600 engineers, designers and product managers in Lithuania, Poland, the UK and North America. This extension of our global delivery network complements recent announcements in the United Kingdom, Australia and indeed Canada.

In closing, I'm proud of our execution against our strategy in 2021. We've re-established commercial momentum and have a healthy book-to-bill ratio. Our delivery teams executed against our commitments despite challenging labor market conditions. Our performance in our two largest industries, Financial Services and Healthcare, has strengthened. Growth in key international markets such as the UK has meaningfully accelerated. Our digital portfolio has been extended and has never been stronger. And we've made significant progress in our people strategy, our internal digitization agenda and indeed our brand repositioning.

For several quarters now, I've been holding hour-long open-ended virtual sessions with small groups of employees. What I've learned from these intimate sessions as well as from our large virtual town hall meetings is that employee pride in the company is building. Employees see not only how far we've come but also clear path to an exciting future.

Employees also recognize the consistent execution of our strategy, our commercial momentum and a commitment to our purpose, vision and values. This purpose has kept us focused on executing our ESG agenda despite the stress for prolonged COVID-19 pandemic. Our ESG focus commitment is evident in our Cognizant Combats COVID-19 initiative in India, in our intensified efforts to drive a culture of belonging throughout Cognizant, in our $250-million philanthropic initiative to advance diversity, equity and inclusion, along with health and well-being in communities around the world and many other areas covered in our 2021 ESG Report.

In summary, our broad-based progress allows us to approach the new fiscal year with confidence in our ability to execute against the multi-year financial outlook we presented at our November investor briefing.

So with that, I'll turn the call over to Jan who will cover the details of the quarter and our financial outlook before we take your questions.

Jan Siegmund

Chief Financial Officer, Cognizant Technology Solutions Corp.

Thank you, Brian, and good afternoon, everyone. We finished the year with solid momentum driven by digital projects and enter 2022 with bookings momentum and strong customer demand. For the full year, revenue was $18.5 billion, representing an increase of 11% or 10% at constant currency. This includes 320 basis points contribution from our acquisitions. The charge in Q4 2020 related to the proposed exit from the customer engagement of our Samlink subsidiary contributed 70 basis points of growth. I will refer to this as the Samlink Impact for the remainder of my remarks.

For the full year, digital revenue grew over 19% and represented approximately 44% of total revenue. Q4 revenue was $4.8 billion, representing an increase of 14% year-over-year or 14.5% in constant currency. Year-over-year growth includes 280 basis points of the Samlink Impact and also 280 basis points of growth from our recent acquisitions. In Q4, digital revenue grew over 20% year-over-year and represented approximately 45% of total revenue.

As Brian mentioned, we were pleased with our bookings performance in the quarter and for the full year. In Q4, we have begun providing trailing 12-month bookings, which can be found in the supplemental presentation posted on our Investor Relations website. We took the opportunity to enhance our bookings definition, modifying it to exclude overlap from early renewals and to include bookings from unintegrated acquired entities. As of Q4 2021, trailing 12-month bookings based on our revised definition were $23.1 billion, representing a book-to-bill of approximately 1.2.

Moving on to segment results for the fourth quarter where all growth rates provided will be year-over-year in constant currency. Financial Services revenue increased approximately 19%, which includes a positive 900 basis points of Samlink Impact. During the quarter, we saw positive trends in our North American banking business, where revenue grew high-single digits, and internationally within insurance. Across banking and insurance, we are continuing to invest into our talent and digital capabilities while focusing on broadening our client base and driving improved profitable growth. In 2022, we expect our recovery to continue.

Healthcare revenue increased approximately 8%, driven by double-digit organic growth in life sciences. Our Healthcare payer and provider business grew in the mid- single-digits, driven by our integrated software solutions. As we discussed during our investor briefing in November, we see a large and growing market opportunity in the Healthcare space, and our capabilities across Healthcare payer, provider and life sciences provide us a unique industry perspective and client intimacy that we believe provide ample opportunity to support sustainable growth in the years ahead.

Products and Resources revenue momentum continued with revenue increasing 18%, the third consecutive quarter of strong double-digit growth. Revenue was again driven by strong performance in manufacturing, logistics, energy and utilities, which grew double-digits for the seventh consecutive quarter and surpassed $2 billion in annual revenue in 2021.

Retail and consumer goods and travel and hospitality also grew double-digits year-over-year with quarterly revenue now back above pre-pandemic levels. Revenue growth also included 550 basis points from our recent acquisitions. Communications, media and technology revenue grew 13%, of which approximately 300 basis points of growth was attributable to recent acquisitions. Organic growth was again led by our Technology business, where our work with digital-native clients has continued to drive growth in our core portfolio.

From a geographic perspective, in Q4, North American revenue grew 9% year-over-year, driven by banking, life sciences, manufacturing, logistics, energy and utilities and technology. Growth in North America also included the benefit of recently completed acquisitions across segments. Revenue outside of North America grew approximately 33% year-over-year in constant currency, including 13 points of Samlink impact. Growth was led by the UK where we saw strong double-digit growth within Financial Services, Products and Resources and Communications, Media & Technology segments. We also continued to experience strong growth in Australia and Germany, driven in part by our acquisitions of Servian and ESG Mobility, respectively.

Now moving onto margins, in Q4, our GAAP and adjusted operating margins were 15.3% as there were no non-GAAP charges in the quarter. On a year-over-year basis, adjusted operating margin improved by approximately 300 basis points driven primarily by the Samlink charge in the prior-year period. As we discussed last quarter, merit increases for the majority of employees were effected October 1 which negatively impacted margin in the quarter. Supply chain constraints and our elevated attrition has kept subcontractor recruiting and other delivery costs elevated, while our recently completed acquisitions have also negatively impacted our margin.

While we continue to invest in SG&A to drive and support organic revenue growth, we have also moderated non-strategic spend, which has helped partially offset the labor cost pressure. Our GAAP and adjusted tax rate in the quarter was 22%, below the low end of full-year guidance range, benefiting from discrete items, which we do not expect to repeat in the future. Q4 diluted GAAP and adjusted EPS were both $1.10.

Now turning to the balance sheet, we ended the quarter with cash and short-term investments of $2.7 billion or net cash of $2.1 billion. Free cash flow in Q4 was $760 million, representing approximately 130% of net income. This resulted in a full year free cash flow of $2.2 billion and represented a cash flow conversion of over 100% of net income, which was in line with our prior guidance. DSO of 69 days declined by 3 days sequentially and by one day year-over-year. DSO will remain a key lever to support strong free cash flow conversion over the medium term.

During the quarter, we repurchased 800,000 shares for $66 million under our share repurchase program and returned $127 million to shareholders through our regular dividend and spent cash of $255 million on acquisitions. In 2021, we've returned $1.3 billion to shareholders through share repurchases and dividends and spent approximately $1 billion in acquisitions. This was consistent with our capital deployment framework introduced in Q4 2020 and reiterated at our November investor briefing.

In support of our capital deployment framework, today, we have also announced a 12% increase in our quarterly cash dividend, our third consecutive annual increase and fourth since we initiated the dividend in 2017. We also expect to return at least $500 million through share repurchases in 2022, subject to market conditions and other factors.

Turning to guidance, for Q1, we expect revenue in the range of $4.8 billion to $4.84 billion, representing year-over-year growth of 9% to 10% or 10.2% to 11.2% in constant currency. Our guidance assumes currency will have a negative 120 basis points impact and an inorganic contribution of approximately 200 basis points. For the full year, we expect revenue growth to be towards the high end of our medium-term financial framework, which is consistent with our expectations at the November 2021 investor briefing.

We expect full-year revenue of $20 billion to $20.5 billion, representing 7.8% to 10.8% growth, or 8.5% to 11.5% in constant currency. Our outlook assumes currency will have a negative 70 basis points impact and includes 200 basis points contribution from inorganic revenue. This inorganic assumption includes approximately 100 basis points from future acquisitions. Full-year guidance also includes the negative impact from the sale of our Samlink subsidiary, which was completed on February 1.

Moving on to adjusted operating margin, consistent with our outlook at the November 2021 investor briefing, we expect 2022 to be towards the lower end of our medium-term financial framework. For 2022, our full-year adjusted operating margin guidance of 15.6% to 15.7% assumes approximately 25 basis points of expansion at the midpoint from 2021. While we are not providing quarterly margin guidance, we expect typical seasonality in 2022, which includes stronger margin performance in Q2 and Q3, while Q1 and Q4 are expected to be below our full-year guidance. In Q1, we expect some modest sequential pressure driven by compensation costs and seasonal factors.

Our outlook for margin assumes the industry supply side constraints continue and that attrition remains elevated in 2022. In response, we will continue to invest into our talent, including through merit increases, promotions, career development opportunities and training. This will include hiring of approximately 50,000 recent college graduates, targeted lateral hires and the continued use of subcontractors. Similar to 2021, we will continue to moderate non-strategic SG&A spend to help offset some of this pressure in the near term.

This leads to our full year adjusted EPS guidance, which is $4.46 to $4.60. Our full-year outlook assumes interest income of $25 million. Our outlook also assumes average share outstanding of approximately 522 million and a tax rate of 25% to 26%. Finally, we expect free cash flow will represent approximately 100% of net income for the full year.

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] In the interest of time, we ask that you please limit yourself to one question and one follow-up. Our first question comes from the line of Brian Essex with Goldman Sachs. You may proceed with your question.

Brian Essex
Analyst, Goldman Sachs & Co. LLC

Q

Hi. Good afternoon and thank you for taking the question. Maybe we can start with Brian. No question, you seem well exposed to demand in this environment. But on the supply side, as we sit here, I guess, over a month into the first quarter, could you share a few thoughts on attrition and level of confidence you have that we may be on the right side of the peak in attrition trends at this point? And maybe share what initiatives seem to be resonating the most with employees?

Brian J. Humphries
Chief Executive Officer & Director, Cognizant Technology Solutions Corp.

A

Yeah. Hi, Brian. Yeah. What I'd add there is we're in a robust demand environment. That's not a concern for me. I'm expecting that to continue in the coming year. And there's lots of [ph] mega (00:28:19) trends that will support that statement undoubtedly. But we're certainly in, from my perspective, an unprecedented competition for talent. We've seen a slight moderation sequentially on an annualized basis. January has been in line with that. But to be very honest, it's too early to call this a trend for the year. There's natural seasonality one expects to see in the course of the year coming up to bonus periods, et cetera. As Jan pointed out, we're expecting elevated attrition through the course of the year. And obviously, we're going to work very hard to try to mitigate that and try to minimize it, the impact on the business.

The implications of attrition, of course, are across financial, commercial implications as well as employee implications. And the levers we're using against that is naturally to try and recruit as many people as we can. I'm delighted we've been able to recruit – to add a net 41,000 head count year-over-year. And compliments to our team, because I think it is core competency of Cognizant in this regard. But, what we're doing in terms of employees, as Jan pointed out, as I did too in my script, a lot of efforts around hearts and minds. There's a lot of effort around compensation measures, which, of course, is pretty critical. I think it's essential for us to continue to show up and post strong double-digit growth, which is helping get a degree of confidence and swagger and optimism back into the company. And just continue to support our employees by celebrating success and giving them career path potential, which of course, growth does. And on top of that, we've revised the way we think about promotion cycles and other such things in the course of the year.

So, it's been a very hands-on engagement for me down through the entire leadership team. In the last six, nine months, we spotted this early. We've added more recruiters and we've really put a lot of efforts in place around a retention task force. But, be that as it may, as you've seen with many of our peers, attrition is elevated and we assume will stay elevated through the course of the year.

Brian Essex
Analyst, Goldman Sachs & Co. LLC

Q

Great. That's super helpful. Thank you for that. And maybe to follow up with Jan, could you maybe frame out the scenarios where we might see upside to margins for the year? And is there any rule of thumb for appreciation of the dollar versus the rupee and how that might impact margins going forward as we track FX?

Jan Siegmund
Chief Financial Officer, Cognizant Technology Solutions Corp.

A

Yeah. I don't want to up my guidance in my first question for the call, I'd imagine so. We have our work cut out to achieve the margin guidance that we did. We feel confident about it, but as you know, we talked about compensation measures, but other factors that are impacting our portfolio in a negative as there are positive factors. So, I want to point out some of the drivers that, obviously, are helping us.

The accelerated revenue itself is a helper on margin. So that helps. Our digital business continues to be slightly more profitable than our traditional business. So, accelerated digital is built into our – solid digital growth is built into our plan. And we continue to make progress on our cost of delivery structure with bringing in college graduates, which will improve the overall cost structure over time. So, we rely on a number of offsetting factors in order to achieve our guidance. And, obviously, any over or underperformance could yield positive or negative outcome. So, I stay balanced. We feel good about our 20 to 30 point outlook.

Brian Essex
Analyst, Goldman Sachs & Co. LLC

Q

Got it. Thank you very much.

Operator: Our next question comes from the line of Lisa Ellis with MoffettNathanson. You may proceed with your question.

Lisa Ellis
Analyst, MoffettNathanson LLC

Q

Terrific. Thanks, guys, and good stuff here. I had a follow-up question on attrition, but this time more related to the senior levels of Cognizant. Can you give a sense for how your attrition levels are running in the top tier levels of the organization and what steps you've been taking to retain some of the key leaders that have been driving the transformation? Thanks.

Brian J. Humphries
Chief Executive Officer & Director, Cognizant Technology Solutions Corp.

A

Hey, Lisa. It's Brian. So, let me address that. To be very honest, I'm not at all concerned about that. The majority of our attrition is at the junior levels in certain odd skills, and I would say at the senior levels of the organization at this moment in time, we're very much, what I would term, business as usual. Promotions, some refreshing of talents, if deemed necessary, based on financial results and other leadership attributes, and what is essentially normal in a company of our size, some retirements, et cetera. So, sometimes we intervene based on performance, but this is more classic business as usual operations at this stage. I feel very good about the motivation of the team collectively. We're all in this together, it's certainly a team sport as we say internally, and I feel as though we're all in the same page. The leaders I've brought in have certainly refreshed their teams, strengthened their teams. I will tell you, right now, I feel I have better instrumentation in terms of how to run the company than at any time since I've been here in terms of the analytical rigor that Jan and his team has put in place. The HR team have done some tremendous work in terms of where we stand there, et cetera. So, we just feel – or I certainly feel a lot more comfortable that we're on top of our game, and we know how things are going. So, not a concern.

Lisa Ellis
Analyst, MoffettNathanson LLC

Q

Okay. Good. And then a follow-up for you as well, Brian, just on the demand environment. Can you just talk a little bit as you're engaging with clients going into 2022, what do you anticipate or you feel is sort of different about the demand environment looking forward as your clients are emerging from the pandemic and maybe trying to get a little bit back to business as usual?

Brian J. Humphries
Chief Executive Officer & Director, Cognizant Technology Solutions Corp.

A

Yeah. Look, I mean, I think to be very honest, clients are well past by now the initial spend hesitancy of COVID for a CEO or for anybody in the sales organization. Certainly, the enemy is indecision, and we don't have indecision, far from it these days. People have really moved well beyond where we were approximately two years ago at this stage. And people are extremely focused, of course, driving digital transformation agendas, evolving their business models which is good for us because our portfolio is stronger now than it's ever been before, and it allows us to work on high impact work for clients. So, really driving some of the big innovation journeys that they have. Now, of course, that leads to discussions around AI and analytics, consumer-centric, if you will, user experiences built-on enterprise class applications, obviously, cybersecurity, digital engineering, cloud migrations. And throughout the world as I deal with clients, it's always surprising to see how different clients are in terms of where they are in client migrations.

I think the one thing that continues to go from strength to strength is, of course, the growing scale of hyperscaler cloud providers. They are, from my perspective, certainly shortening innovation cycles, throwing a lot of commercial muscle and financial muscle to accommodate or ensure accelerated cloud migrations.

And, of course, in more recent times, they've really evolved towards industry clouds, not just the hyperscalers, but also the major SaaS vendors which allow more integrated vertical workflows. And Cognizant's strength therefore in areas like Healthcare and Financial Services is of interest to them. But it's very consistent with what we've seen before, Lisa, to be very honest, a huge push towards classic modernization initiatives toward data, analytics, cloud, digital engineering. And really what I find clients are certainly willing to spend for skills and innovation, but certainly expect more efficiencies and a more traditional non-digital work. And we see that on our pricing dynamics, and I certainly see that in terms of client strategic intentions in the years ahead.

Lisa Ellis
Analyst, MoffettNathanson LLC

Q

Terrific. Thank you.

Operator: Our next question comes from the line of Darrin Peller with Wolfe Research. You may proceed with your question.

Darrin Peller
Analyst, Wolfe Research LLC

Q

Thanks, guys. When looking at your outlook, your confidence level around your revenue growth, but obviously coupled with margins in the right direction, a little more than we had initially modeled for the year ahead. I mean, it really does give us more conviction that the pricing power you have is able to offset wage inflation. So, I'd love to hear more color on that, if you don't mind, in terms of the environment you're in and whether or not you're able to really pass through whatever you need to on the price point side.

And then maybe just as a follow-up to that, are there other – have there been any like advances in decoupling the linearity on the business model at all in a greater way over the past quarter into this next couple of quarters?

Brian J. Humphries
Chief Executive Officer & Director, Cognizant Technology Solutions Corp.

A

Yeah, I'll start. Jan, by all means, jump in at any stage. So, Darrin, first of all, pricing remained somewhat stable. And as I've just mentioned to Lisa, based on her question, we see differences between the digital work and the non-digital side. Clients will pay out for skills and innovation and frankly, availability for resources in digital. Of course, that happens to be in an industry where people tend to have MSAs and rate cards that have been agreed in advance, so it requires us to interrupt those rate cards, but certainly clients see in their own workforce, as well as other vendors a desire for companies like Cognizant to ultimately drive some pricing power given the labor trends that we see.

But, of course, price increases can and have lagged talent related to cost increases. We've put a lot of effort around pricing, both rate card, intelligence, big deal pricing and it is certainly one of the factors that's inherent in our guidance for the coming year. And as I said earlier as well, the fact that we have scaled our digital portfolio to approximately 45% of the business pits us into more strategic client projects, pits us against different competitors and inarguably provides us with a pricing opportunity as long as we get the gross margin right on digital skills versus the classic non-digital skills. But the last thing I'll say just around pricing, of course, because it's inherent in your question, it's a margin question. And our margins can also naturally be helped by the type of work we sell solution and deliver. So, we continue to focus on evolving the company towards selling and delivering client outcomes. That allows us to own more of our pyramid, to industrialize delivery, to better leverage automation and optimized our mix as well as our pyramid.

Specific to your other question around decoupling of – I guess, the Holy Grail on the services company to decouple revenue growth from head count growth, look, there are many factors at play there as well, including the shift to more offshore delivery in the course of the last year. Offshore delivery has increased for us about 2 points, year-over-year about 1 point sequentially and that can help margin.

But, of course, it can hurt you in terms of head count growth versus revenue growth or the so-called average rate per employee. And it can also change dollar margins, as well as dollar revenue per employee. So, there are multiple things at play here. We are a services company. We're committed to being a services company. We'll certainly try to optimize and industrialize delivery where we can, leveraging automation, templatization, AI, et cetera. But at the end of the day, we are in a head count business and as we scale our head count, we'll scale our revenue. And you guys are more than familiar with that model.

Jan Siegmund
Chief Financial Officer, Cognizant Technology Solutions Corp.
A

Yeah. Maybe, Brian, you covered it, I think, on the pricing thing, but a little bit of color on the margin expansion, because we really have taken a balanced view about the sources of the margin expansion her, and pricing is a factor, but it's not the dominating factor. We have other elements like the natural shift of the business towards higher margin business. We have a scaling of – you saw this in the fourth quarter. We slowed the growth of SG&A in a meaningful way and it's now contributing to margin actually at slower than revenue growth rate. We expect that to contribute next year as well.

And we have – we hope to see impact from our initiative to refresh our delivery permit and Brian talked out about the success that we had of bringing college graduates on. We mentioned this that we're planning to onboard 50,000 college graduates this year. That will help to streamline our cost of delivery pyramid. And it's also – so, there's a variety of factors that drive it. And so, pricing is a factor, but only one among many.

Darrin Peller
Analyst, Wolfe Research LLC
Q

Okay. All right. I mean, I have other questions, but just in the interest of time, I'll let you guys turn it back to the queue, and thank you.

Jan Siegmund
Chief Financial Officer, Cognizant Technology Solutions Corp.
A

Thank you.

Operator: Our next question comes from the line of Keith Bachman with BMO. You may proceed with your question.

Keith Bachman
Analyst, BMO Capital Markets Corp.
Q

Hi. Thank you. I had two if I could. Brian, if you could talk a little bit about Healthcare and the potential for growth during 2022 and beyond. You mentioned TriZetto was 13%, but just what are some of the factors that would lead to Healthcare continuing, if not, getting – improving its growth rate to contributing presumably to Cognizant being able to break on a consolidated basis the 10% kind of organic growth? I would think Healthcare would be one of the key drivers. If you could just talk a little bit about that and then I have a margin question to ask, Jan, after.

Brian J. Humphries
Chief Executive Officer & Director, Cognizant Technology Solutions Corp.
A

Yeah. Yeah. Look, it's certainly our ambition to accelerate Healthcare growth. In the November analyst meeting, we talked about market growth. But, of course, within our Healthcare business, we have the US Healthcare vertical, which is payer, provider, the payer being the vast majority. And then a product business, of course, coupled within that and then the less than 50% of our Healthcare business is our life sciences business, which continues to grow double-digits.

I feel really great about that, both the nature of our capabilities, the nature of our client intimacy, the global nature of those clients and our bookings momentum in life sciences through the course of the year has been frankly outstanding and was very strong in Q4 as well.

So, candidly, as we're getting after the life sciences opportunity, it's all about continuing to scale bio pharma. And then, in this year, we've accelerated a little bit on medical device momentum there as well. You've also seen us, Keith, do some targeted acquisitions in the life sciences vertical in the last few years including Zenith, as well as TQS more recently.

In the US Healthcare business, a lot of it is about getting the TriZetto business back on track. I think I mentioned in the November briefing, our growth rate in 2020 was twice that of – of 2020 was twice that of 2019, and we've approximately doubled growth rate again in 2021 over 2020. And that's good in terms of client intimacy and relevance, in terms of margins and the pull-through opportunity or the stickiness of Cognizant in those accounts. So, getting the payer and provider back into a higher growth trajectory, but making sure that the product-driven side of that scales as well is pretty essential to us.

And I've got to be honest, I'm very motivated about where we are with TriZetto. I think it's a fantastic gem within the company. Now that we've got growth back, we continue to explore possibilities in terms of where we can scale our Healthcare franchise, both in terms of the market within the US, in terms of different applications within the ecosystem or different control points as well as exploring how we can scale our Healthcare business into Canada, and indeed, into select international markets. I think if we do all of that right, we will drive market growth, if not more than market growth. And that's what the team is focused on.

Keith Bachman
Analyst, BMO Capital Markets Corp.

Q

Okay. Perfect. Jan, for you. Thank you, Brian. On the free cash flow margins, I think you said for 2022, you want to do 1x net income. If I just do some back-of-the-envelope, that would suggest that the free cash flow margin, which is free cash flow divided by the revenue, will be down again this year, I think, perhaps not meaningfully. But are there other forces at work you think in free cash flow in 2022 that we should be aware of that might either positively or negatively impact, whether working capital, taxes, CapEx? Anything else you want to call out for our free cash flow models?

Jan Siegmund
Chief Financial Officer, Cognizant Technology Solutions Corp.

A

No. I can give you a little bit the background of our thinking around the free cash flow conversion, which I think I mentioned in my script to be around 100%. We did a little bit better this year, had a very good quarter in free. I think with all these ins and outs, there is basically maybe a slight increase in capital expenditures in the next year that we could see that is related to some more strategic investments internally, but nothing major. We continue to be laser focused on our sources of cash from our clients. So we made good progress on DSO this year and that focus will remain.

And to be quite honest, I'm drawing a blank on cash. I think cash is going to be – on taxes. I think tax is going to be fairly similar to this year, so no major variation on the tax side. So, that's kind of how I expect the cash flow situation to evolve for us. So nothing specific comes to mind. Maybe a slight increase on capital expenditures that could drive it.

Keith Bachman
Analyst, BMO Capital Markets Corp.

Q

Okay. All right. Thanks very much.

Operator: Our next question comes from the line of Tien-Tsin Huang with JPMorgan. You may proceed with your question.

Tien-Tsin Huang
Analyst, JPMorgan Securities LLC

Q

Hi. Great. Thanks. Hope you can hear me, guys? I think I wanted to ask on Financial Services. Safe to say that some of the money center bank headwinds that we've been seeing – you've been seeing are behind the company. I know there's a lot of pressure to spend in general amongst the banking side, but just curious how you're feeling there, both from a competitive standpoint and from a cyclical standpoint.

Brian J. Humphries
Chief Executive Officer & Director, Cognizant Technology Solutions Corp.

A

Look, from my perspective, we've been working on recovering in Financial Services for quite a time. There's been a pace of recovery candidly through the course of the year, but the 10% constant currency growth, if I exclude the 9 points benefit we got from the year-over-year compare from the accounting charge in Q4 last year's results, is probably the highest level of constant currency growth we've had in quite a few years. And this has ultimately been on the back of a series of things we've been doing, sharpening our focus on our top clients, refreshing some of the commercial team as well as, by the way, some of the leadership team, both in delivery as well as in the business.

And back to a question I had earlier, that's part and parcel of running a world class company. Sometimes, you have to refresh leaders if you're not getting the results you want. We've added a lot of talent with a focus on executive engagement at a client-facing level, a lot of collaboration with the hyperscalers committed to their industry cloud or financial cloud, and of course, a partner ecosystem. And all of that has now started to bear fruit.

I'm cautiously optimistic around our growing competitiveness there. We are leading more with digital. We're leading more with, what I would call, less interviews or staff augmentation-type work. We're getting better margins for that, and I think our competitiveness will continue to increase in the course of the year.

Of course, with the decision that we took last year, which was closed ultimately yesterday, I believe, around the Samlink sale, we have a compare sequentially and year-over-year in the first quarter and beyond, which will have an anomaly that we can talk to in subsequent calls. But generally, I feel that the team have done great work. We expect continued improvements in 2022 will be a paced recovery. I'm not suggesting we're back to our full strength yet, but we're working both well across the regional banks, but I'm also optimistic around the progress that the refreshed leadership team are making with some of the larger global banks. And if we're able to crack some of those, of course, that will show up in the numbers as well.

So, generally, I feel as though we're on the right track and the team have worked hard and deserve growing momentum in the business.

Tien-Tsin Huang
Analyst, JPMorgan Securities LLC

Q

Understood. Thank you for that.

Operator: Our next question comes from the line of Rayna Kumar with UBS. You may proceed with your question.

Rayna Kumar
Analyst, UBS Securities LLC

Q

Good evening, Brian and Jan. Thanks for taking my question. So, you've now had two consecutive quarters of 20%-plus bookings growth. Could you talk about the sustainability of that as well as book-to-bill above 1?

Jan Siegmund
Chief Financial Officer, Cognizant Technology Solutions Corp.

A

Yeah. We had 22% bookings growth, mid-teens for the full year, and it's driven obviously by the strong demand that we see in the market. It's supported by the investments that we made into our market organization with incremental sales capabilities and solution capabilities. And it's aided by a broadening solution set that we're developing ourselves as well as our M&A that is contributing to this.

So, we are optimistic about maintaining a book-to-bill ratio that is similar to where we are. That is at least our mindset and we have seen really a very consistent execution, very consistent pipeline development and the bookings momentum itself has been broad based, has been good geographically split, and it has been, in general. Of course, there are ups and downs by smaller business units, but it has been when you lean back, fairly broad based, which is all good news basically to assume that we're going to continue on that path.

Rayna Kumar
Analyst, UBS Securities LLC

Q

Great. Thank you.

Operator: Our next question comes from the line of Jason Kupferberg with Bank of America. You may proceed with your question.

Jason Kupferberg
Analyst, BofA Securities, Inc.

Q

Yeah. Thanks, guys. Nice results here. Just wanted to ask a follow-up on bookings to start, anything you can tell us about the mix of new work versus renewals in that $23 billion of trailing 12-month bookings?

Jan Siegmund
Chief Financial Officer, Cognizant Technology Solutions Corp.

A

Yeah. We don't really disclose details of the bookings number. It is a mix but the mix has been stable. And it is really not contributing one way or the other to the overall composition of the bookings number stayed basically stable but we're not disclosing components of it.

Jason Kupferberg
Analyst, BofA Securities, Inc.

Q

Okay. Just as a follow-up, I know you're including 100 basis points of inorganic revenue contribution in the 2022 guide for deals that you haven't yet announced. Can you just talk about the line of sight to executing on enough deals to drive that, I guess, $185 million or so of internal revenue that you'd need?

Jan Siegmund
Chief Financial Officer, Cognizant Technology Solutions Corp.

A

Yeah. We have a very capable development team and M&A team, of course, proven over the last two years to execute steady stream of these strategic acquisitions, mid – small and medium size in nature. And we continue to see great opportunities for us to align our strategic goals with that. So, we're bringing already approximately as you can see from our guidance in the first quarter, we're bringing already some momentum with acquisition of Devbridge into the momentum. So, yeah, we feel confident about the 100 basis points, which we'll be executing within this year.

Jason Kupferberg
Analyst, BofA Securities, Inc.

Q

Okay. Thanks, Jan.

Operator: Our next question comes from the line of David Togut with Evercore ISI. You may proceed with your question.

David Mark Togut
Analyst, Evercore Group LLC

Q

Thank you very much. Looking at the slide 13, on-site employee utilization fell to the lowest level in three years, which is really the history of this chart and looks like offshore employee utilization fell to about a six quarter low. Can you just talk through the utilization dynamics? Clearly, they're tied to the attrition numbers and what are your expectations for both offshore and on-site utilization in your 2022 guidance? Thank you.

Jan Siegmund
Chief Financial Officer, Cognizant Technology Solutions Corp.

A

Yeah. You're right in the observation. There is some impact in the chart by our switch to nine-hour bill week that has lowered our utilization. So that is in the last few quarters in there. But the overall dynamic is largely driven by the acceleration of onboarding new associates that have some utilization lack in the beginning of their tenure. So that was really the biggest driver of a downtick in utilization that we're seeing basically. And so we are kind of happy to have a little bit bigger bench to fulfill client needs. So, for us, utilization levels are really at the desired level of where we want to see it.

David Mark Togut
Analyst, Evercore Group LLC

Q

Understood. Just as a quick follow-up, Brian, could you expand upon your comment that you're seeing more clients ask for price efficiency in the legacy work? What – how much price efficiency, if you will, are they looking for? And are you able to offset that through lower costs?

Brian J. Humphries
Chief Executive Officer & Director, Cognizant Technology Solutions Corp.

A

Yeah. Look, we have obviously embraced automation. We've taken out double-digit thousands of people from our fixed price contracts in the last few years, so we continue to automate our agenda. I will say the other thing you've seen is our digital mix hasn't scaled as much as we assumed previously because we've been quite successful in the non-digital part of our portfolio, arguably more successful than others scaling that and mitigating the downside. So it's a street combat every single time you're coming up for renewal.

You want to be clever as well in some of the classic areas to make sure you try and upsell to help modernization or beyond and try to get a renewal plus an expansion. But I feel as though we've handled ourselves well in that regard and we have a lot of effort underway, as I said earlier, to try to continue to evolve the company to an area where we are better able to industrialize delivery, which will help ultimately our margins and indeed the quality of our delivery. So, I feel pretty good about where we are in that regard.

David Mark Togut
Analyst, Evercore Group LLC

Q

Thank you.

Brian J. Humphries
Chief Executive Officer & Director, Cognizant Technology Solutions Corp.

A

Our biggest focus naturally is to scale digital while we protect the non-digital business and mitigate the downside. And for the guidance we gave in November, we assume that will grow low to mid-single digits, our real focus as a company and that's core to our strategy is our momentum in digital, which is growing 20% plus or minus.

David Mark Togut
Analyst, Evercore Group LLC

Q

Thank you very much.

Brian J. Humphries
Chief Executive Officer & Director, Cognizant Technology Solutions Corp.

A

Yeah.

Operator: Our next question comes from the line of Bryan Bergin with Cowen. You may proceed with your question.

Bryan C. Bergin
Analyst, Cowen & Co. LLC

Q

Hi. Good afternoon. Thank you. Within the 2022 growth outlook, can you talk about some of your expectations across the industry segments this year? And anything to be mindful about around the cadence of growth as you built the plan?

Jan Siegmund
Chief Financial Officer, Cognizant Technology Solutions Corp.

A

Can you repeat that? You broke up in the beginning of your question.

Bryan C. Bergin
Analyst, Cowen & Co. LLC

Q

Yeah. Sure. So the expectations across the industry segments for growth this year within the context of the consolidated plan. And then just anything around cadence we should be aware of.

Jan Siegmund
Chief Financial Officer, Cognizant Technology Solutions Corp.

A

On the cadence of the growth, I think we have a typical revenue number we gave you, basically our outlook for the first quarter. It's nothing really that I have to specify more, I think, on the revenue quarterly cadence.

Relative to the industry growth, I would just point out that we had a one-time impact from Samlink in the Financial Services sector. But we – despite that grow over a one-time impact, we expect continued moderate growth in the Financial Services group and all other groups should continue with the momentum. So, I think it's a fairest thing if you just build a momentum case for our four big industry groups to get a good forecast.

Bryan C. Bergin
Analyst, Cowen & Co. LLC

Q

Okay. And then just the international opportunity, I know this has been a big focus for you, putting investments to drive more traction there. Can you talk about your expectations for growth in markets outside of the US in 2022, which ones you most excited about and some of the initiatives that you continue to drive?

Brian J. Humphries
Chief Executive Officer & Director, Cognizant Technology Solutions Corp.

A

Yeah. So, look, this is something I'm particularly passionate about. Cognizant's brand internationally certainly wasn't known as much as in key industries in North America and naturally in our offshore areas. So we put a coordinated effort in place to reposition the brand. We've refreshed a lot of our country leaders across Europe and the Middle East, and I think we're seeing the fruits of that labor right now. You saw a 28% growth in the UK this quarter. Our UK momentum has been building through the course of the year. It's nicely profitable for us as well in terms of relative profitability vis-à-vis other European countries. And we also have a lot of momentum in areas like Australia, New Zealand.

So the seniority and the capability of the team we've built allows us to have confidence to deploy M&A, support their growth ambitions as well. That's what we did in Australia and that's what we're doing in Germany. You've seen the ESG acquisition we did in the last year. So, generally, I feel very optimistic about our potential there. It is a year where we had strong bookings. We have to just continue to build on that in the years ahead, but I am – ultimately, if we're here three, four years from now looking back, I'd like to think this will have been a really big success story for us.

Now it's not only about capturing the revenue opportunity, that revenue opportunity which will be fueled more with digital-type work more than historical levels also requires more local and a global delivery network. And that's also an area where I'm pleased to see the momentum we've had. We announced most recently the buildout in Canada in Nova Scotia. But in the last few months, we announced thousands of extra roles across Adelaide in Australia as well as the UK in Northern England and Northern Ireland. So, we're doing what is needed in terms of partnership, talent, delivery capabilities to get after the market opportunity internationally. And the fruit is very visible in our second largest country in the UK, which grew 28% this quarter.

Bryan C. Bergin
Analyst, Cowen & Co. LLC

Q

Okay. Very good. Thank you.

Tyler Scott
Vice President, Investor Relations, Cognizant Technology Solutions Corp.

A

Hi, Laura, I think we have time for one more question.

Operator: Our last question comes from the line of James Faucette with Morgan Stanley. You may proceed with your question.

James E. Faucette
Analyst, Morgan Stanley & Co. LLC

Q

Thank you very much and appreciate all the detail and color that you've provided. Back on the hiring side, how should we think about what you are feeling as the appropriate level of pace of hiring in the current environment? And I guess as part of that, I'm looking for kind of number of net head count additions, et cetera, going forward. And I guess maybe more importantly, how are you feeling about your capacity or infrastructure that you have in place to be able to address that, or is that an area of potential investment?

Brian J. Humphries
Chief Executive Officer & Director, Cognizant Technology Solutions Corp.

A

We've been investing behind our recruitment engine in the course of the last six, nine months, as we spotted attrition to be a likely industry problem, we got out in front of perhaps others and we moved fast. And you've seen a net head count expansion of 41,000 year-over-year since Q4 prior-year period and another 12,000 sequentially. Of course, within a given year, subject to when we bring in our college graduates and onboard them, you'll see different peaks country by country. But I'm more than confident that we have an engine that is a core competency. The team has done an outstanding job for us. We have processes, tools, capabilities in place.

Our brand standing is stronger increasingly, not just in India, but overseas. And some of the brand work we've done, both externally as well as our internal branding, has given us more and more confidence that we have brand ambassadors in the company to make that happen. So, we are absolutely in the mode of accelerating head count as best we can. The lower we can keep attrition, of course, is the most predictive way to do that. And in the meantime, as Jan pointed out, we've done the heavy lifting. We've made significant progress around the delivery pyramid this year, 33,000, up from 17,000 in the prior-year period, and next year we're assuming 50,000. And if needed, we'll try and scale beyond that.

So for me, it's about retention and it's about recruitment and getting the balance right between those. But I'm certainly bullish on the industry, bullish on our position within the industry. And I'd like to have more head count in Cognizant. So if you know people, send them our way.

Jan Siegmund
Chief Financial Officer, Cognizant Technology Solutions Corp.

A

Regarding capacity, as you know, we are still operating in a largely virtual environment. And depending on the development of the pandemic, we'll make obviously decisions in the future. But I think the working model is that we're going to settle in a hybrid model. So relative to capacity in the sense of bricks and mortar, I think we feel very well equipped to handle the growth and that shouldn't be anything unusual. The re-igniting of the non-virtual component will bring some cost pressures in it, but that is reflected in our margin guidance.

James E. Faucette
Analyst, Morgan Stanley & Co. LLC

Q

That's great. Thanks, Brian. Thanks, Jan.

Tyler Scott
Vice President, Investor Relations, Cognizant Technology Solutions Corp.

Great. Thanks, James, and thank you, everyone, for joining. We appreciate your interest in Cognizant and look forward to catching up next quarter. Thank you.

Operator: This concludes today's Cognizant Technology Solutions' Q4 2021 earnings conference call. You may now disconnect your lines at this time. Thank you for your participation. Enjoy the rest of your day.