

Tata Consultancy Services Limited
Q2 FY22 Earnings Conference Call.
October 8, 2021, 20:00 hrs IST (10:30 hrs US ET)

Moderator: Ladies and gentlemen, good day and welcome to the TCS Earnings Conference Call. As a reminder, all participant lines will be in the listen-only mode, and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing '*' then '0' on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Kedar Shirali – Global Head, Investor Relations at TCS. Thank you and over to you, sir.

Kedar Shirali: Thank you, Steven. Good evening and welcome everyone. Thank you for joining us today to discuss TCS Financial Results for the Second Quarter of Fiscal Year 2022 that ended September 30, 2021. This call is being webcast through our website and an archive including the transcript will be available on the site for the duration of this quarter.

The financial statements, quarterly fact sheet and press releases are also available on our website.

Our leadership team is present on this call to discuss our results. We have with us today, Mr. Rajesh Gopinathan -- Chief Executive Officer and Managing Director; Mr. N G Subramaniam -- Chief Operating Officer; Mr. Samir Seksaria -- Chief Financial Officer and Mr. Milind Lakkad -- Chief Human Resources Officer.

Rajesh and Samir will give a brief overview of the company's performance followed by a Q&A Session.

As you're aware, we don't provide specific revenue or earnings guidance. And anything said on this call which reflects our outlook for the future or which could be construed as a forward-looking statement must be reviewed in conjunction with the risks that the company faces. We have outlined these risks in the

second slide of the quarterly fact sheet available on our website and which has been e-mailed out to those who have subscribed to our mailing list.

With that, I would like to turn the call over to Rajesh.

Rajesh Gopinathan: Thank you, Kedar and once again, welcome everyone. Thank you for joining us on a Friday evening. We are very pleased with the all-round strong performance this quarter. On the revenue side, all our industry verticals grew in the mid-teens or more. Overall, we grew **15.5%** year-on-year in constant currency terms, and **16.8%** in reported dollar terms as well as in reported rupee terms.

Our operating margin for the quarter showed its inherent resilience, expanding to **25.6%** despite industry-level inflationary headwinds. Net margins in Q2 came in at **20.5%**.

I will now ask Samir to go over the headline numbers, financials and segmental performance, and I will join you again later to talk about the demand trends we are seeing and the emerging opportunities in growth and transformation. Over to you, Samir.

Samir Seksaria: Thank you, Rajesh. Let me first walk you all through the headline numbers. In the second quarter of FY 22, our revenues grew **15.5%** YoY on a constant currency basis.

Reported revenue in INR was **₹468.67 billion** which is a growth of **16.8%**. In USD terms, revenue was **\$6.333 billion**, again a YoY growth of **16.8%**.

Let me now provide our segmental performance details for the quarter. All growth numbers are in year-on-year constant currency terms. We saw strong double-digit growth in all our verticals.

Growth was led by Manufacturing vertical which grew **21.7%**, followed by Life Sciences and Healthcare at **19%**, Retail and CPG at **18.4%** and BFSI at **17%**.

Speaking of BFSI, an important milestone worth highlighting here is that our quarterly run rate from our major markets BFSI services alone crossed the **\$2 billion** mark. Including revenues from our products and platforms, and from regional markets, we would be one of the largest providers of IT consulting services and solutions in the BFSI industry globally.

We also saw good acceleration in Communications and Media which grew **15.6%** and in Technology and Services which grew **14.8%**.

In geography terms, we had good growth across all our markets; growth was led by North America at **17.4%**, UK grew **15.6%** and Continental Europe grew **13.5%**.

Among regional markets, growth was led by India at **20.1%**, followed by Latin America at **15.2%**, Middle East and Africa at **13.8%** and Asia Pacific at **7.6%**.

Our portfolio of products and platforms performed well in Q2.

ignio™, our cognitive automation software signed up **22** new customers and **8** go-lives. Digital has continued to build out a strong ecosystem in terms of technology partners as well as channel partners. Its adaptor factory now provides 50 out-of-box integrations between ignio and third-party commercial products and platforms.

Digital Academy has trained 9,761 professionals till date and certified 3,106 professionals on ignio.

ignio success stories continue to pour in. Here is one example: One of the largest midwestern consumer banks of US went live this quarter with ignio AIOps and has experienced a reduction in MTTR or Mean Time To Resolve of 90%, which significantly improves their operational resilience, reduces downtime of critical applications and avoids critical business SLA misses.

TCS BaNCS™, our flagship product suite for financial services domain had five new wins and three go lives in Q2. One of India's leading private insurance players has successfully rolled out TCS BaNCS for Insurance across India for servicing, renewal and claims processing of its health insurance policies. 1.9 million policies spanning more than 30 products in health and personal accident were migrated in this program.

Quartz Blockchain platform has two new wins and one go live in Q2. We also won our first customer in pharma industry.

A large custodian in UK has selected Quartz for handling announcements for its centralized corporate actions event capture utility, that services multiple business clients including local custody and fund accounting. TCS BaNCS Corporate-Actions-as-a-Service solution will provide the security, compliance

and high availability that financial services companies require, combined with the flexibility and agility of the cloud.

TCS HOBS™ suite of products for communications service providers had four new wins and six go lives in Q2. The HOBS product cloud was leveraged by one of the largest telecom service providers in India to launch a first of its kind converged solution to deliver mass personalization by bundling two or more services.

TwinX™, our AI-based digital twin solution has had four wins and six go lives.

TCS iON continues to be the largest assessment provider in the country and we have now expanded our work in education transformation through our engagements in the states of Odisha, Kerala and Telangana.

Lastly, TCS MasterCraft™, suite of intelligent automation products for enterprise application development, modernization and delivery had 22 new wins in Q2. Jile™, our enterprise agile planning and delivery platform saw three new wins.

Moving on to client metrics, we track these closely because they are proof points and customer-centric strategy of continually expanding and deepening our engagement is working.

In Q2, we had robust additions in every revenue bucket compared to the year ago period. We added five more clients in the \$100 million+ band, bringing the total to 54. We added 17 more clients in the \$50 million+ band, bringing the total to 114; 19 clients in the \$20 million+ band, bringing the total to 247; 31 clients in the \$10 million+ band, taking the total to 417; 44 in the \$5 million+ band with a total of 609; and lastly, 62 more clients in the \$1 million+ band, taking the total to 1,138.

Let me now go over the financials. Supply side shortages and increased employee churn have led to higher back-filling expenses and greater use of subcontractors across the industry. Additionally, currency was not favorable this quarter. While the US dollar appreciated, all other currencies depreciated against the Rupee, creating a margin headwind. Despite these headwinds, through disciplined execution, we were able to expand our operating margin by 10 basis points to **25.6%**.

Net income margin was at **20.5%** and our EPS grew **15.8%** year-over-year. ETR or effective tax rate for the quarter was **25.6%**.

Our accounts receivable was at **67** DSO or days' sales outstanding in dollar terms, up two days compared to Q1.

Net cash from operations was at **₹99.45 billion** which is **103%** of net income. Free cash flow was **₹92.29 billion**. Invested funds as on September 30 stood at **₹605.48 billion**.

Board has recommended an interim dividend of **₹7** per share.

On the people front, we had net additions of **19,690** in Q2, bringing the total headcount to **528,748**. It continues to be a very diverse workforce with **157** nationalities represented and with women making up **36.2%** of the base.

We continue to invest in the employees to help them gain the skill and capabilities needed to realize their potential.

Our Digital Learning platform saw TCS log in over **14.3 million** learning hours in Q2. Over **417,000** employees were now trained on multiple new technologies and we now have over **26,000** contextual masters in the company.

LTM attrition in IT services was at **11.9%**. While this is still the lowest in the industry, it is a big increase from the unusually low attrition we had over the last year due to pandemic, and reflects the industry-wide churn.

We had the foresight to continue hiring in large numbers throughout the second half of the last year and the first half of this year. In this fiscal, we have already onboarded **43,000** fresh engineers, all trained on the latest technologies, while also ramping up our organic talent development initiatives and our employee engagement outreach. This helped us create solid pipeline of talent while containing attrition. This has helped us overcome the supply side challenges seen across the industry and continue to meet all our delivery commitments.

Over 95% of our associates have received at least one dose of the vaccine and over 70% have been fully vaccinated. We plan to bring back our workforce to the workplace gradually by the end of the year.

Over to Rajesh now for Demand Drivers and Trends.

Rajesh Gopinathan: Thank you, Samir. If you look at our growth over the last few quarters, it has been driven by three broad trends: increased outsourcing, investments in building a digital core and the growth and transformation agendas of our clients. Our strong growth in Q2 was once again driven by all three drivers. Let me now talk a little about each of these.

Operations optimization has been an ongoing theme with many of our customers and I have mentioned earlier customers are looking to free up resources, both human and financial, to support their transformation programs. This is resulting in higher levels of outsourcing activity in IT operations as well as in business operations, and is gaining further urgency because of the scarcity of talent and the speed at which the demand is being driven.

We continue to dominate this space by taking a differentiated approach that leverages our innovative Machine First Delivery Model or MFDM™. By embedding intelligent automation deep within the enterprise, we are able to help customers unlock tremendous value that traditional models based on labor arbitrage alone find very difficult to match.

At the heart of our Machine First™ approach is TCS Cognix™, an AI-driven human-machine collaboration suite, that consists of a large library of pre-built solutions, addressing the entire breadth of IT and business operations, across multiple industries.

Using this, we are able to very quickly transform operations embedding AI and machine learning and machine vision and conversational systems across the enterprise, and take the customer to an end-state operating model that is leaner, more agile and reduces turnaround time for key processes to deliver superior customer experience. In the last 12 months since we launched Cognix, we have won multiple engagements using this suite. In Q2, we had six large deals that use Cognix to transform customers' operating models.

In addition to this, we continue to gain market share, benefiting from the flight to quality that we have seen over the last 18 months, as well as in structured vendor consolidation exercises.

Coming to cloud transformation, cloud adoption and the possibilities for business transformation that the hyperscaler stack opens up, continue to be very big drivers of growth. These multi-horizon cloud transformation journeys typically begin with cloud migration, including application modernization and

data estate modernization. Once again, in this quarter, we have had a large number of deal wins around such Horizon 1 initiatives, some of which we have listed in our press release.

As part of the modernization, we also saw instances of customer shifting their ERP and other enterprise applications from on-premise models to SaaS and hosted versions. Areas of focus include eCommerce and customer experience, supply chain and human capital and leveraging SAP S4/HANA or Salesforce Cloud or Oracle Cloud suite along with other leading SaaS applications.

As an example, for a US-based medical technologies multinational, we are implementing an SAP S4/HANA solution to help them realize their vision of consolidating onto a one global ERP platform to harmonize the business processes and support new business model opportunities.

Some of them are also progressing to Horizon 2 using native capabilities of the cloud to transform their core activities, driving superior business outcomes and also paving the way for innovative business models.

For example, a large reinsurer in Europe has engaged us to design and develop their next-generation credit and surety insurance underwriting platform on the cloud. The new platform will leverage cloud-native capabilities to help our client transform their underwriting process, using larger and richer datasets, deep analytics and automation to significantly enhance underwriting quality, speed and throughput.

This will enable them to take on more business, offer a broader range of products and provide a superior customer experience. But more importantly, the platform is also being architected so that it can be monetized in the future by opening it up to other smaller insurers or reinsurers, and giving them access to new attractive risk pools through the large ecosystem of banks and other lenders anchored by our client.

This is the kind of Horizon 3 opportunities that we are most excited about, where individual anchor clients will start energizing ecosystems to come together around these cloud-based solutions to seamlessly reach multiple customers.

Coming to the second broad theme of industry transformation, we have been highlighting how TCS has been playing an impactful role in helping individual enterprises realizing their growth aspirations through technology-enabled business transformations and business model innovations. The impact is

manifold higher when the client happens to be an ecosystem owner or a market infrastructure whose transformation can reshape an entire market altogether.

Let me share a couple of examples:

In Australia, the Australian Energy Market Operator or AEMO is an independent organization and manages all electricity and gas systems and markets across Australia. It is responsible for the settlement of the national electricity market which connects the grids of eastern and southern Australian states to create a wholesale energy market.

Until now, AEMO had only been able to settle the market in 30-minute blocks, limited by its ability to segment the data. This time block was thought to favor incumbent technologies and handicap innovation. To address this inequity, the five-minute settlement rule was introduced, in what might be the biggest ever market reform in the Australian energy market till date, and possibly one of the leading reforms globally in this market.

The five-minute settlement rule will shift the current 30-minute wholesale electricity spot market settlement period to five minutes or less, providing a better price signal for investment in faster response technologies, such as battery and gas peaking generators. It will also enable more efficient bidding, operational decisions and investments, aligned to dispatch and financial settlement periods. TCS was chosen as a technology partner for the change on the basis of the solution we proposed, and the cloud-based settlement platform we designed and developed, successfully went live on October 1st.

Similarly, in the financial services industry, as you know, we are the largest independent software provider to market infrastructure institutions with our proven suite of TCS BaNCS for Market Infrastructure and custody solutions, powering the operations of over 50 market critical institutions across 66 countries.

With its unique ability to support multiple markets, currencies and asset classes on the same platform, and support for a wide range of messaging standards that enable real time interfaces with market participants and external ecosystems, it has been a key catalyst in driving transformation in many markets worldwide.

Closer home in India, some of you would have followed our recent announcement about the work that we're doing with the Multi Commodity

Exchange of India (MCX) which has selected TCS as its technology partner for its growth and transformation. As part of Project *Udaan*, TCS will help MCX build a new technology core, transforming its trading as well as post-trade functions to support its future growth and further strengthen its leadership position in the commodity derivatives market in India.

The interesting aspect of this is how we have partnered with another customer of ours, Deutsche Boerse, and are using trade solution components from them, tightly integrated with the settlement components from TCS BaNCS to create a world-class solution for MCX in India. This kind of ecosystem-based opportunities where multiple technology solutions come together from different players in the industry will be the path of the future, and we see our role as a system integrator with significant domain capability and a strong suite of our own products and platforms, serving as the unique glue that will hold this ecosystem together.

Another example is our newly launched Quartz for Markets which helps market infrastructure institutions such as exchanges, depositories and central banks, payment infrastructures, etc., evolve with the times and launch next generation services around tokenized securities to drive their future growth.

Four market infrastructure institutions have already signed up for this, including three in India, and deployment is currently under way.

Another area that we have spoken about in the past, and are very excited about, is the field of engineering services. Product innovation is central to our customers' growth and transformation strategies. Building newer products or newer features or capabilities in existing products allows them to sell more to existing market segments or address new segments altogether.

We have traditionally been strong players in this space, helping product companies expand their innovation velocity and capability by using our engineering design, R&D and industrialization services.

The emergence of digital technologies, particularly IoT, big data, analytics and cloud, has significantly expanded the addressable market for us, as more and more product manufacturers seek to make their products intelligent with sensors, and embrace as-a-Service models, building service layers around the product to enable lifelong engagement with the customer and to drive new revenue streams.

Our engineering services practice has seen steady growth over the last five years, straddling the product innovation opportunity end-to-end, helping customers develop an idea into a prototype and a product, and then take the concept product all the way to production. With connected technologies like IoT, TCS also helps track product usage performance at the customer-end, closing the loop as it were.

Very importantly, we are a major player in the ongoing CASE ecosystem that is the connected, autonomous, shared, electric transformation of the automotive sector, working with almost all the major auto OEMs, start-ups, and Tier-1 suppliers in their product innovation lifecycles.

TCS teams are working with leading Tier-1s and OEMs in building new age solutions such as autonomous AI-based algorithms, electric vehicle battery management software, some of which we have spoken about last time, and cloud-based connected car applications.

One particular engagement, which I think best exemplifies the breadth and depth of TCS' automotive design capability, is with a European-headquartered global auto OEM. TCS has been the strategic partner for developing a new range of car models catering to emerging markets. These markets, as you can appreciate, are characterized by price-sensitive consumers. So, the product design and engineering has to adapt accordingly.

We are doing the complete product strategy, product design and engineering, homologation and helping build a high level of localization of the parts in each market, all designed to very stringent cost targets.

This is another example of how TCS is going beyond its traditional remit, where we're actually working with the customer to build out that supply ecosystem, and working with their suppliers to actually go into an iterative design mode to get to the price targets of the end-product that this customer seeks to launch in a market two to three years ahead. So, that kind of ability to see that, and to link that back into a tight value-engineering loop, and to leverage technology, and the ability to engage with domain knowledge with the entire ecosystem is something that we believe is quite unique to TCS, in terms of the spread of services that we have systematically been investing and building out on.

The customer appreciated our ability to bring together these end-to-end capabilities that are needed to help it and the product design and innovation

expertise, value engineering, etc., The work that started for Asian markets has now been expanded to cover Latin American markets also and has been deeply appreciated by the customer who has awarded us their best supplier award, among other areas of appreciation that they have given to us.

Moving on to another space which is gaining a lot of traction in recent times, let me talk about the emergence of the B2B commerce opportunity and also the direct-to-consumer commerce opportunity.

CPG companies in particular, have been investing in direct-to-consumer initiatives to gain direct access to end consumers and to deepen insight-driven consumer engagement without encumbering the intermediary channels.

We are enabling the rapid shift to online eCommerce as the preferred channel from brick-and-mortar stores, on aggregator retailers, helping our clients establish direct customer connect, gain better margins and enhance the scale of their business volumes.

A leading Swiss-based pharmaceutical company specializing in dermatological treatments and skincare products has selected TCS to implement a human centric hyper-personalized and experience-driven B2C customer journey to enable healthcare professionals with next generation eCommerce capabilities. The project includes an initial implementation in three countries, followed by a global rollout across over 30 countries over the next three years and support, leveraging a leading commerce cloud platform.

Another example is a leading global dental and medical products distributor who has partnered with TCS to accelerate the transformation of their digital channel. Facing intense competition from online players, our client wanted to move to a more touchless sales and service paradigm. The program covers B2B eCommerce transformation across Europe, UK, and Americas, covering customer-facing interactions and channels.

The counter-trend to this is that channel intermediaries are investing in technology to make themselves more relevant to the customer and in certain cases even seeking to achieve eclipse the OEMs. We are participating in that opportunity as well.

For example, for a global distributor of electrical and electronic components, TCS has helped to build a cloud-based industrial IoT platform that connects and collects data from high-value industrial assets and provides a

comprehensive analytical dashboard and insights for driving improvements in predictive maintenance, reliability management and operational efficiency. Using this, our client has been able to offer a range of new services and deliver a range of benefits to the end-customers, beyond just being the preferred supplier of multiple individual vendor items that they were originally positioned as. The predictive maintenance capacity has resulted in availabilities reaching 99%, and acts as a new SKU which is their own SKU being delivered into their end-customer systems.

Partnering with TCS helped our client accelerate their transformation from being a component distributor to an industrial digital solutions provider. The new platform created new revenue streams with component servitization, boosted profitability and reinforce its position as an innovation pioneer in the industrial component ecosystems.

So, the broad theme here is, as we have been talking in the past, of growth and transformation being the common agenda.

Coming back to some of the other themes that we have spoken about in the past, M&A divestitures continues to be a great area of growth for us and we are once again participating in several new deal wins in Q2.

An example of that is the sale of Cordis, the world-leading cardiovascular and endovascular medical devices company that was spun off from Cardinal Health to Hellman & Friedman in August. TCS was engaged to enable Cordis to function as an independent company. TCS will lead the development of their end-state technology strategy. This includes portfolio rationalization, day one readiness planning, as well as business case support and cost model option. TCS will also create a post day one operational support organization to provide an optimized opex model.

Similarly, we have been selected by a leading consumer goods company in Europe to enable the divestiture of its domestic appliances business and drive their business transformation into a state-of-the-art digital-first CPG company. TCS will design, build and implement brand new greenfield processes and applications to set up the new entity as an agile B2C company leveraging one of the most respected brands in this industry and manage its technology landscape.

We have spoken about how we have invested early in a dedicated M&A strategy offering, that brings together multiple service offerings, acceleration frameworks and sophisticated change management capabilities. Leveraging this and our contextual knowledge of our customers' complex IT landscapes, we are able to provide practical and pragmatic M&A solutions to our clients from strategy through execution.

Over the last three years, built a solid reputation in this domain as someone who can be relied upon to enable smooth day one operations, helping us more and more with such deals.

Coming to the area of sustainability that we spoke about at length last time, I wanted to showcase a few recent engagements. A port authority in Middle East and Africa region has selected TCS for implementation of TCS Clever Energy™ for its terminals to build a monitoring and visualization system by integrating various utility meters and the building management systems into a single platform.

Similarly, a Middle Eastern warehousing corporation has engaged TCS to help analyze and report their carbon footprint across the value chain to effectively manage their overall carbon emission.

A leading European bank has partnered with TCS to incorporate climate risk factors in credit risk scoring across climate risk scenarios to quantify the bank's exposure to climate risk.

Finally, TCS was engaged by a leading UK-based bank in the strategic climate risk assessment program. TCS will provide services for data sourcing, climate methodology analysis and dashboard reporting in compliance with the regulation.

Coming now to the Q2 order book, some of the representative trends that have been driving our strong growth and revenue as well as in our order book. On the back of a very strong order book in Q1, we have once again had strong set of deal wins in Q2 across all industry verticals and geographies. Our TCV in Q2 was **\$7.6 billion**. Once again, it's a very heterogeneous mix of large, mid-sized and small deals.

When you compare this against the last year's number, after removing one very large mega deal that we reported in Q2 of last year, this represents a 25% expansion on like-to-like TCV. By vertical, BFSI had a TCV of **\$2.1 billion** while

retail once again had a very strong order book of **\$1.2 billion**. TCV of deals signed in North America stood at **\$3.9 billion**.

Lastly, while the strength of the demand environment is now no longer in doubt and we are very confident of sustainability in the medium term, we also believe that the growth tailwind offers us an opportunity to position ourselves as the preferred growth and transformation partner of our customers. While pursuing the opportunities at hand, we will continue to invest in organic talent development to build the workforce of the future, in research and innovation, intellectual property and in building out a comprehensive set of offerings that caters to the needs of every key stakeholders in the enterprise across every point in the business cycle. We believe this is very important to build a sustainable business that will continue to create value for all our stakeholders in the long-term.

With that, thank you for listening in and we will open the line for questions.

Moderator: We will now begin the question-and-answer session. The first question is from the line of Yogesh Aggarwal from HSBC. Please go ahead.

Yogesh Aggarwal: I just have a couple of questions, if I may. Rajesh, just trying to reconcile the TCV of \$7.6 billion in the overall demand environment, I think you mentioned 25% growth ex of one large deal, but one of the trends we have seen at the sector level in the recent ones is limited mega deals but high velocity of smaller deals. So, in your 7.6 billion, how is the mix looking like, has the duration come down and if the ACV or the annual contract value is better than TCV 25% growth? And secondly, in the past, we have seen deflation in legacy business which you have talked about as well and there is a renewal. More importantly, are you expecting this rate of deflation in legacy to come down with all the supply crunch and overall strong demand?

Rajesh Gopinathan: Yogesh, I wouldn't call out any significant change to the overall TCV or the pipeline. For mega deals, by definition, the frequency is different. And when you look at the pipeline or the TCV without the mega deal, they are pretty much similar. It's a good mix of both, low duration, as well as medium to large duration deals. So, there's no significant movement to either expanded durations or reduced durations.

On your second question on deflation, I think this is a topic that we have discussed multiple times in the past individually also. The trend that we are

seeing is in line with the overall technology agenda. Deals that come up for renewal five years later will benefit from all the technological progress that has happened in that period. So, when you compare it against the deal value of the last period versus the current period, that might seem optically to be a reduction. But remember that it also reflects the kind of efficiency gains that have been achieved in the space.

If you take something as traditional as, let's say, infrastructure support, nowadays deals come packaged a lot with cloud-based businesses or even in the past, the same infrastructure estate would be significantly more compressed on a like-to-like basis, over a five-year duration. The point is not that. The point is that, is the technology spending at a client level, and the technological intensity of the overall value chain, reducing or increasing? And as long as it is increasing, the total value is what we are trying to address.

This is in line with other trends that have happened in this industry – cost of compute goes down, total compute consumption increases; cost of network goes down, total network consumption increases. Not just the volume of network consumption increases, the total value spent on network consumption increases. So, this is not very different, and I don't see any change to this scenario. Unit cost will go down, total consumption will increase. If you invest, and stay ahead of the curve to be the most efficient producer, you will participate in the cycle or the cycle will kill you.

Moderator: The next question is from the line of Sandip Agarwal from Edelweiss. Please go ahead.

Sandip Agarwal: I have one question on the margin and one question on the growth. So, the way the deal momentum is building up and you made a statement it is one of the best times in a decade, so what is your sense, where are we seeing the growth trajectory to be moving? In particular, will there be any impact of seasonality which generally happens because the kind of demand we are seeing and the supply constraint clients would have seen, they might have pushed some of the deals to the next quarter.. so do you think that there was some kind of challenge in execution also because of the high attrition and manpower issue, that is number one? And number two will be on the margin front. Will it be fair to call that the peak of the pain in terms of financial intervention to retain employees is behind us and we can see substantial improvement going forward on the margin front?

Rajesh Gopinathan: The demand environment is very strong and it's likely to continue to be strong in the medium term. However, the seasonality of demand and seasonality of operations will be an overlay on top of it. How much will that impact be? That we will get to know only closer to the end of the year. But I don't think the seasonality will go away but the underlying demand trend will provide a significant positive support to it. The important thing is that when we spoke about the nature of this demand environment, the period of time for which we think that the demand environment is likely to remain strong is quite high. And that that is where this has changed in terms of the visibility of the demand environment which we've called out in the past also.

So, we are investing into that kind of a spectrum which is why our significant focus over the last many quarters also, on very high campus hiring because we want to make sure that we have the right talent, while we continue to invest into our existing talent, we want to enhance that with fresh campus hiring and we are doing that at unprecedented scale which is betting on the sustainability of the demand environment.

Short term volatility to cost basis coming from the attrition levels that you see, should be expected to play out. But these are not structural elements, but more transitional elements as the industry supply chain settles down. It is triggered by the fact that many players in the industry did not invest early on into creating that supply chain. That will rationalize over the next few quarters. Our agenda is slightly longer, and we continue to invest into that demand visibility.

Moderator: The next question is from the line of Gaurav Rateria from Morgan Stanley. Please go ahead.

Gaurav Rateria: Two questions. Firstly, has fulfillment related challenges limited your ability to grow revenue in the current quarter or the trends have broadly been in line with the expectations?

Milind Lakkad: Actually, like I said earlier, we have planned for growth two quarters ahead this time. That's why we brought in 43,000 campus hires in the first half of the year and then we continue to hire for the market with high velocity and have volumes in the last two quarters also. So, the impact of supply basically on the growth is definitely not there till now. We will continue to basically get in more and more and better and better invest more and more, so that we don't face lack of growth because of supply.

Gaurav Rateria: Secondly, typically, 2Q we see an operating leverage playing out on the margins and probably there were supply related issues and margins have been resilient on a sequential basis, but I'm just trying to understand split between the investments made and potential headwinds from the supply side challenges and how long these investments will continue after which the large operating leverage will be visible in the margins?

Rajesh Gopinathan: I think the operating leverage is visible in the expansion in margin that you've seen. The extent of it might not be as much given our increased dependence on subcontractors, partially caused by restrictions on travel and mobility of talent. So, as some of those restrictions ease, we should be able to rationalize the employee pool further. But again, as I said, it's not structurally any different than what we have seen in the past.

Coming to the investment side, our investment agenda will continue at pace. We have always spoken about the fact that it is our investment agenda that gives us the industry-leading margins and it is our intent to continue with that agenda across even a wider cross-section of spaces that we're interested in. You see that playing out in all aspects of our business, whether it be products and platforms or new services or new markets that we're investing into.

Moderator: The next question is from the line of Apurva Prasad from Elara Capital. Please go ahead.

Apurva Prasad: Couple of ones. While I understand that mega deals have got long cycles, do you think there's any change in the frequency of mega deals, and more so, can you highlight whether your pipeline composition looks similar to recent wins or do you think that can change? I'm getting to this with the assumption that there are more G&T deals in the mix, and more deals with ecosystem partners. Is that increasing the complexity and reducing the frequency of mega deals?

Rajesh Gopinathan: I don't think these two are linked. Frequency of mega deals if anything, as you can see, when you take a slightly longer term perspective like let's say 10 years, there are a lot more like mega-deals today than there used to be in the past, at an industry level. So, that's one aspect of it.

The pipeline that we have, that has a mix of deals of all sizes. Growth and transformation deals, typically will be of smaller value but due to shorter duration. So, the ACV level will not be very different. Ecosystem partner leverage does not significantly change the nature. We rarely have scenarios

where we pass partner revenues through our book. So, what you're seeing is our own value of the deal. So, it does not significantly change that mix. So, short answer, I don't see any difference in the overall mix.

Apurva Prasad: Just a related piece on that, Rajesh. On the cloud transformation deals that you referred to, so in your assessment as customers transition from Horizon 1 to Horizon 2, do you think that can have a bearing on deal sizes with increase in scope?

Rajesh Gopinathan: Yes and no. Typically, Horizon 1 deals are multi-year deals, more consumption driven. They're simpler deals whereas Horizon 2 deals are more complex, project-based deals. So, typically, Horizon 1 deals start small and then the consumption is driven by new programs that come onboard which will, one way or the other, have Horizon 2 and Horizon 3 features. So, it is very difficult to break out the value difference, but Horizon 2 deals are more project-centric and then lead to ongoing consumption.

Apurva Prasad: So, Europe appears to be slowing on sequential basis versus prior quarters trend, so any color or any vertical flavor from Continental Europe, that'll be helpful?

Rajesh Gopinathan: Europe has had a soft quarter, but we don't think it's structurally a very different one. It has been across multiple verticals and multiple themes are driving it. In some areas, a very large program that we had, that has come to an end and that has had some impact. We're also seeing much more offshoring out of Europe, I'd say, to tackle the whole talent scarcity by significantly increasing leverage closer to global standards. That provides volume, but has a deflationary impact on the reported revenue. There is also slowdown in some industry sectors, which we are keeping a close watch on.

When you look at the deals per se, new customer addition and new deal signings in Europe are actually higher and that gives us the confidence that this is a transitional phase, and we should see continuing momentum there when we look one or two quarters forward.

Moderator: The next question is from the line of Ruchi Burde from Bank of Baroda. Please go ahead.

Ruchi Burde: I have two questions; first for Milind. With energized hiring engine and talent pipeline, do you expect the intensity of supply pressure to ease possibly maybe three, four quarters down the line?

Milind Lakkad: Basically, we are estimating that this will continue for about two to three quarters, and then it will ease. So, from Q2 onwards is what we say it will start easing is our estimate based on what we're seeing. But we will continue to monitor as we go along.

Ruchi Burde: Secondly, last year December quarter was anything but seasonally weak. Do you see Rajesh, or what is your initial sense on furloughs and seasonality impact this year?

Rajesh Gopinathan: Ruchi, last year Q3 was when we actually got back to revenue parity. So, on a sequential basis, it had a very benign comparative. We are currently coming off of four quarters of straight growth. The seasonality, we will have to wait and see how it plays out.

Moderator: The next question is from the line of Sudheer Guntupalli from ICICI Securities. Please go ahead.

Sudheer Guntupalli: While we do understand that year-on-year growth rate still look strong, there is still a base discussion given that September 20 itself is below what a normal trend line would have been in the absence of COVID. But if I look at it on a QoQ basis, overall constant currency growth of around 3.6% and growth ex of India at 3.1% looks tepid especially in the context that September is seasonally a strong quarter. So, Rajesh, are we seeing a situation where as the correction is happening, growth rates are reverting to pre-COVID trend lines?

Rajesh Gopinathan: The constant currency growth rate this quarter sequential will be 4%, which is fairly strong even on a sequential basis. So, the growth trends and the growth visibility that we're talking about, or the sustainability of the growth visibility that we're talking about, is fairly extended given the nature of work that is driving it. I spoke earlier about the cloud transformation kind of programs, the various platform driven programs. So, the nature of demand is such that we think that the growth visibility into the medium term continues to be very strong.

Sudheer Guntupalli: Milind, given the buoyancy in the job market, we are actually seeing companies hiring at exotic and salary hikes, of course TCS still seems to be disciplined on that front, but when we look at the industry trend, the higher salaries kind of distort the internal employee parity and may remain structurally elevated for several years to come, however, demand can be more cyclical. So, how do you read the situation and what are your thoughts on the structural impact of this on the long-term margin perspective of the industry?

Milind Lakkad: Couple of points here; one is yes, when we backfill attrition, yes, there is a marginal increase in the cost we see which is not for this quarter, it has been like this for a reasonably good period of time. The point is internally the way we manage talent is we do have strategic talent development programs where people go through that and can significantly accelerate their career paths, and their compensation. There are ways to increase and accelerate compensation internally also. So, those two things kind of balance each other in a reasonably good way for us.

Moderator: The next question is from the line of Sandeep Shah from Equirus Capital. Please go ahead.

Sandeep Shah: Rajesh, in one of your interviews earlier, you indicated that the adoption of the Horizon 1 deal is faster by the clients versus the adoption of the Horizon 2. So, just wanted to understand where are we in terms of the adoption journey by the client on the Horizon 1? And do you believe once it achieves a desired level of adoption, the growth can be slightly slower versus what we have seen in Horizon 1? And in television interview, you also said that the growth is getting consolidated versus earlier quarters. So, is it that comment for specific segment or is it at the overall level as a whole?

Rajesh Gopinathan: I will answer the first part, I didn't fully understand second, but first one, workload migration to the cloud just on a pure migration perspective, estimates vary, but it's somewhere in the range of 20% to 30%, while it might vary by industry-to-industry. So, we are still at the early stages of this kind of adoption of infrastructure-as-a-service, which is the primary driver of Horizon 1 demand and that still has quite a few legs to play out. The second question I didn't understand.

Sandeep Shah: Yes, just the follow up to that, once this Horizon 1 phase is over and we enter the Horizon 2, do you believe the growth rate sustainability maybe similar or slightly lower? And in your television interview today, you also made a comment that growth is getting consolidated versus high growth in the last few quarters. Is it specific to some segments or the markets or is it the overall?

Rajesh Gopinathan: The Horizon 1 as it plays out, we had spoken about this in the past if you think as an architectural shift that we're seeing and that is the major point. In the past we have seen that happen when we went from client server to web technologies and later on as we went from web to mobile technologies. These architectural shifts that have significant benefits. So, Horizon 1 is the enabler

towards that architectural shift. Once that migration takes place, it unlocks a lot more possibilities and triggers new investment. So, while the Horizon 1 base case volume might go down but it will unlock significantly higher volumes on the Horizon 2, Horizon 3 spectrum. That's the promise and the hope that this industry is always built on. On the consolidation of demand, I would have said it in certain contexts or in terms of sequential trend per se. I think what I said is that we are consolidating the growth and looking forward into the future but I don't exactly remember what the context was.

Sandeep Shah: Second question to Samir, I think in your television interview you also said generally seasonally second half margin picks up versus the first half. But this time could be slightly different because attrition may have a short-term challenges in terms of margin management even in second half of this year?

Samir Seksaria: Yes, the mention is about short term volatility. And whenever there is short-term volatility, there would be tightness and pressure on margins. So, in spite of those supply side challenges, we were able to sustain our margins in Q2 but we will have to watch this for the next couple of quarters till such challenges continue.

Sandeep Shah: Rajesh, whether clients are receptive about this in terms of compensating through pricing increase or is it too early to call out? Looking at legacy portfolio being also higher for the industry, the overall pricing increase may not be a tailwind at a consol level for the industry as a whole?

Rajesh Gopinathan: We are seeing a full spectrum of responses there. I mean, a lot of the consolidation-led engagements are predicated on a win-win which includes overall efficiency gains for the client, while we use technology levers to transform the operating estate that we spoke about in the early part of my commentary today.

Newer areas command a pricing premium – areas like what we spoke about design thinking, developing new platforms, Horizon 2, Horizon 3 kind of engagements. These are all coming at a premium. So, there is both efficiency-led business and innovation- and transformation-led business which comes in at different price points. Net-net, it's a balancing kind of an environment. There is no significant move in either direction. At a portfolio level, it stays fairly stable.

Moderator: The next question is from the line of Manik Taneja from JM Financial. Please go ahead.

Manik Taneja: Rajesh, wanted to get your thoughts around the fact that if you see any new engagement models emerge beyond the typical onsite, offshore model as the clients as well as the industry at large, tries to address the talent deficit as well as the significant need to accelerate or fulfill the demand?

Rajesh Gopinathan: I think the one that we're most excited about is the leverage of automation in a deeply embedded manner, which we call the Machine First Delivery Model (MFDM). This is a space that we think still has quite a lot of upside left in it and we are systematically investing in how to embed it deeper into our service provision. So, that's the biggest delivery model change.

Otherwise, agile which significantly changes the efficiency of consumption, is of course, another transformative model. Add third model that has a lot of resonance is what we call as the product-centric operating model which combines agile at its core, and integrates technology a lot more closely with business transformation. So, all of these trends that are gaining momentum systematically.

Moderator: Ladies and gentleman, that was the last question for today. I now hand the conference over to the management for the closing comments.

Rajesh Gopinathan: Thank you. To repeat, we had a strong broad-based growth across all our industry verticals and very strong deal wins yet again in Q2. Our client additions were very strong across all revenue buckets this quarter, an important measure of the depth of our customer relationships.

Our margins continue to be industry-leading and have shown immense resilience despite supply side challenges this quarter and currency headwinds. On the people front, by investing ahead of time in hiring the right talent across the world and onboarding a record number of fresh engineers, we have been able to overcome supply side challenges and stay on track with all our execution timelines. Our attrition went up this quarter but continues to be lowest in the industry. We are still watching this closely for the next few quarters.

We have vaccinated 70% of our employees fully and over 95% have received at least one dose. This sets us up well to start bringing them back to the workplace towards the end of the year.

Thank you all for joining us on this call today. Enjoy the rest of your evening and do stay safe. Thank you.

Moderator: Thank you members of the management. On behalf of TCS that concludes this Conference Call. Thank you all for joining us and you may now disconnect your lines.

Note: This transcript has been edited for readability and does not purport to be a verbatim record of the proceedings.