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Conference Call Transcript

ACN - Q1 Fiscal 2011 Accenture Earnings Conference Call

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PRESENTATION

Operator

Ladies and gentlemen, thank you for standing by and welcome to Accenture's first-quarter fiscal 2011 earnings call. At this time, all lines are in a listen-only mode. Later, there will be an opportunity for your questions. (Operator Instructions).

I'll now turn the conference over to KC McClure, Managing Director of Investor Relations. Please go ahead.

KC McClure - Accenture - Managing Director, Investor Relations

Thank you, Kathy, and thanks everyone for joining us today on our first-quarter fiscal 2011 earnings announcement. As Kathy just mentioned, I'm KC McClure, Managing Director of Investor Relations. With me this afternoon are Bill Green, our Chairman and Chief Executive Officer; Pamela Craig, our Chief Financial Officer; and Pierre Nanterme, who will become our Chief Executive Officer on January 1st. We hope you've had an opportunity to review the news release we issued a short time ago.



Let me quickly outline the agenda for today's call. Bill will begin with an overview of our results. Pam will take you through the financial details, including the income statement and balance sheet, along with some key operational metrics for the first quarter. Bill will then provide a brief update on our growth strategy and market positioning. Pam will then provide our business outlook for the second quarter and full fiscal year 2011. And then we will take your questions.

As a reminder, when we discuss revenues during today's call, we're talking about revenues before reimbursements, or net revenues. Some of the matters we will discuss on this call are forward-looking, and you should keep in mind that these forward-looking statements are subject to known and unknown risks and uncertainties that could cause actual results to differ materially from those expressed or implied by such statements. Such risks and uncertainties include, but are not limited to, general economic conditions and those factors set forth in today's news release and discussed under the Risk Factors section of our Annual Report on Form 10-K and other SEC filings.

During our call today, we will reference certain non-GAAP financial measures, which we believe provide useful information for investors. We include reconciliations of those measures, where appropriate, to GAAP in our news release, or on the Investor Relations section of our website at accenture.com. As always, Accenture assumes no obligation to update the information presented on this conference call. Now let me turn the call over to Bill.

William Green - Accenture - Chairman & CEO

Thank you, KC, and thanks everyone, for joining us today. Well, the momentum continues, and it's building. I am incredibly pleased with our performance in the first quarter. We achieved very strong growth at both the top and bottom line, building even further on our performance from the second half of fiscal 2010. Here are some highlights from the quarter:

- Revenues were more than \$6 billion. This is our second-highest quarterly revenues ever, and exceeded the upper end of our guided range. Of particular significance, four out of our five operating groups achieved double-digit revenue growth in both US dollars and local currency.
- We delivered earnings per share of \$0.81, an increase of \$0.14, or 20% over Q1 of last year.
- Operating income was \$827 million, also our second-highest ever, with strong operating margin of 13.7%.
- We generated solid new bookings of \$6.3 billion, including outstanding consulting bookings of more than \$3.7 billion.
- And we continue to have a very strong balance sheet, with a cash balance of \$4.2 billion, and of course, no debt.

Our exceptionally strong results in the first quarter position us very well for the remainder of fiscal 2011, and frankly, the future. Now I'll turn the call over to Pam, who will provide some more detail on the numbers.

Pamela Craig - Accenture - Chief Financial Officer

Thank you Bill. Best wishes for this season, and thank you all for joining us today. I am pleased to tell you more about Accenture's fiscal year 2011 first-quarter financial results. We recorded overall outstanding revenue growth across the dimensions of our business in both consulting and outsourcing around the world and in the broad base of clients and industries we serve. In addition, we continue to drive the business, delivering net revenue growth well into the double digits in four of our five operating groups. We have posted up a strong first quarter toward the full-year financial outlook we provided last quarter.

Unless I state otherwise, all figures are GAAP except the items that are not part of the financial statements or that are calculations.

New bookings for the quarter were \$6.31 billion and reflected a negative 1% foreign exchange impact compared with new bookings in the first quarter of last year. Consulting bookings were \$3.72 billion; outsourcing bookings were \$2.59 billion.

Consulting bookings were the highest in 10 quarters and reflected broad-based year-over-year growth. In management consulting, clients are hiring us to help them drive both operational excellence and growth in their businesses. Bookings were very strong in Europe and Asia-Pacific. We continue to see robust demand from clients for our offerings in supply chain optimization, customer service effectiveness, and sales and marketing transformation. This quarter's bookings also reflected healthy demand for our strategy offerings in post-merger integration and global operating model design and also our talent and organizational performance offerings. Finally, activity is building in the areas of risk management and new-market entry.



In technology consulting, bookings were strong, as our clients continued to seek sound unbiased strategies they can implement to improve their technology infrastructures. Their interest in innovation and flexibility continues to grow, in order to drive down IT cost through increased use of virtualization and the cloud. At the same time, they continue to rationalize legacy operations through data center consolidation, application modernization and renewal, and address security and IT governance.

In Systems Integration, bookings were the highest in nine quarters. The SI business has rebounded nicely, and is showing increasing strength. Post-merger integration and rationalization of technology platforms are major drivers. Client demand also reflects the critical need for modernization of legacy applications as well as the implementation and upgrades to ERP applications. We are particularly pleased with this level of bookings, given that we are also proactively and successfully managing the shift of SI work to lower-cost locations.

Turning to outsourcing bookings, we're right in line with what we expected in September, when I stated we thought they would be relatively lighter this quarter. In technology outsourcing, cost optimization remains paramount, and we are benefiting from the vendor consolidation that has occurred. We recorded a significant number of wins and saw clients launching more projects. We also have a healthy expansion in our pipeline. Finally, our solid BPO bookings reflected demand for cost-effective solutions in finance and accounting, procurement and industry-specific processes, particularly in North America and Europe.

Now, turning to revenue. Net revenues for the first quarter were \$6.05 billion, an increase of 12% in US dollars and 14% in local currency from the same period last year. These revenues reflected a rounded foreign-exchange impact of negative 1% compared with Q1 last year. Consulting revenues were \$3.57 billion, an increase of 14% in US dollars and 16% in local currency. Outsourcing revenues were \$2.48 billion, an increase of 10% in US dollars and 11% in local currency. Let me give you a little color on each operating group.

In Financial Services, revenues grew 21% in local currency. Consulting revenues were a record in both dollars and year-over-year growth. We saw demand in all three industry groups. The demand for our services related to post-merger integration, core banking and insurance replatforming, risk and regulatory compliance and business model transformation drove the momentum this corner.

Resources revenue growth at 18% in local currency this quarter reflected double-digit gains in both consulting and outsourcing. Consulting growth continued to be driven by demand for global operating model design, ERP, operational excellence, and smart grid-related products. Similar to last quarter, outsourcing revenues reflected demand for client programs around cost take-out in IT and financial business processes.

The Products operating group had local currency growth of 17%, driven by very strong growth in consulting. Demand is across virtually all of the industry groups in Products, with both new and existing clients starting to expand beyond cost-cutting projects to more customer-focused offerings to drive their growth. In addition, we saw good revenue growth in Asia-Pacific, where we are working with clients on global expansion strategies.

Communications & High Tech revenues increased 12% in local currency, up from 7% last quarter. Consulting demand continues to be driven by strategic sourcing, globalization, cost take-out, and customer acquisition and retention, as well as deploying new technologies to support growing wireless product demand. In addition, we saw more interest from clients developing differentiated capabilities, such as improved broadband content delivery and the management of investments in cloud computing. Outsourcing revenues in C&HT grew as well in Q1, as clients continued to focus on cost take-out and improving operational efficiency.

Health & Public Service revenues were down 1% in local currency, as uncertainty and challenges in the public sector continue, particularly in Europe. Consulting revenues declined modestly in Public Service and were partially offset by growth in Health, particularly in the Americas. We're leading some of the most-defining health engagements around the globe and investing to take Health to the next level. Outsourcing revenues grew again this quarter, primarily driven by US federal.

In summary, the outstanding revenue results are evidence of healthy demand for our offerings across the majority of our industry groups and geographies.

Moving down the income statement, gross margin was 32.2%, down from 33.1%, a 90-basis-point decrease from Q1 last year. The return of strong growth and demand in the business resulted in higher subcontractor needs and higher recruiting and training activities from the onboarding of many more employees. This year's gross margin also reflects our take-up of significantly higher compensation increases effective this September versus last September.

Sales and marketing costs were \$731 million, or 12.1% of net revenues, compared with \$622 million, or 11.6% of net revenues, for the first quarter last year. The 50-basis-point increase reflected higher business-development costs, as we continue to grow our sales pipeline and new



bookings. General and administrative costs were \$386 million, or 6.4% of net revenues, compared with \$412 million, or 7.7% of net revenues, for the first quarter last year. The 130-basis-point decrease reflects an 80-basis-point impact from our continued efforts to actively manage our cost structure, with the remaining 50-basis-point decrease coming from a reduction of part of our bad-debt reserve, due to better-than-expected bad-debt experience.

Operating income for the quarter increased 11%, to \$827 million, resulting in a 13.7% operating margin, a 20-basis-point decrease compared with Q1 of last year. As Bill mentioned, this level of operating income was our second-highest ever.

Three of our operating groups delivered strong results in operating income and margin in the first quarter. The operating income in Health & Public Service was negatively impacted by continued lower contract profitability in parts of the public service portfolio, and higher selling costs.

Our effective tax rate for the quarter was 28.3%, compared with 30.5% in the first quarter last year. The lower rate this year was due to a number of factors that impacted geographic distribution of income.

Net income for the quarter was \$606 million, compared with \$525 million for the first quarter last year, an increase of 15%.

Diluted earnings per share were \$0.81, compared with \$0.67 in the first quarter last year. This \$0.14 rise reflects an \$0.08 increase from higher revenue and operating income in local currency, a \$0.04 increase from the lower share count, a \$0.02 increase from the lower effective income tax rate, and a \$0.01 increase from higher non-operating income, offset by a \$0.01 decrease from foreign exchange rates.

Now let's turn to some key parts of our cash flow and balance sheet. Free cash flow for the quarter was \$31 million, resulting from cash generated by operating activities of \$106 million, net of property and equipment additions of \$75 million. For the same period last year, free cash flow was \$184 million. Our property and equipment additions more than doubled, and the level of free cash flow this quarter also reflected a rise in working capital as our revenue ramped during the quarter.

Turning to DSOs, our days services outstanding were 33 days, up from 30 days last quarter and 32 days in the same quarter last year. We continue to focus on strong working capital management.

Our total cash balance at November 30 was \$4.2 billion, versus \$4.8 billion at the end of August. As you can see on our cash flow statement, the free cash flow in the quarter was more than offset by the cash we returned to shareholders and a slight uptick in M&A.

Turning to some key operational metrics. We ended the quarter with global headcount of 211,000 people, and we now have 120,000 people in our Global Delivery Network. In Q1, our utilization rounded to 87%, up less than half a point from Q4. Attrition, which excludes involuntary terminations, was 15%, down from 17% in Q4. And lastly, we continue to plan to hire at least 64,000 people around the world this year.

Before I turn things back to Bill, I will comment on our ongoing objective to return cash to shareholders through share repurchases and dividends. In the first quarter, we repurchased or redeemed approximately 14.6 million shares for \$620 million, an average price of \$42.37 per share, including 3.2 million shares repurchased in the open market. Repurchases included \$170 million worth of shares employees sold back to us in order to fund their tax-withholding obligations for shares delivered to them in Q1. At November 30, we had \$2.5 billion of share repurchase authority remaining.

Also in November, we paid a semi-annual cash dividend of \$0.45 per share, which was a \$0.075, or 20%, increase over the dividend we paid in May, for a total of \$321 million. We expect that our Board of Directors will declare the second part of our semi-annual dividend at the time of our Q2 earnings call.

In summary, we're off to a great start in fiscal 2011, beginning the year with a strong Q1 and good momentum going into Q2. We are focused on executing our strategy and driving our business with discipline. Now, here's Bill to give you his look ahead.

William Green - Accenture - Chairman & CEO

Thank you, Pam. Over the past year, we have talked to you about our two major areas of focus. First, navigating the challenging and changing environment in a focused and disciplined way, and delivering a great result. Second, all we're doing to position Accenture for the future by launching and driving a series of strategic actions. What you're seeing is the impact of both: Accelerating new business on top of a solid and profitable operational platform. And we continue to execute our growth initiatives exceptionally well across three dimensions.



Dec 16, 2010 / 09:30PM GMT, ACN - Q1 2011 Accenture Earnings Conference Call

First, our core business. This is the backbone and includes our traditional services of consulting, technology and outsourcing, refreshed and relevant for today's market, not yesterday's. Our unique ability to serve clients across the entire stack is what clients want now.

Second, our new initiatives and businesses, including things like analytics, mobility, smart grid and digital marketing, and the many other new products and services, especially in the technology area. We're building these within and on top of our core, and all of them are getting traction and kicking in.

And third, our geographic expansion agenda, focusing our leadership position in emerging and fast-growing markets as well as increasing growth, market share and profit in our most-developed and mature markets. We are doing more work in more places for more people than ever to help our clients achieve high performance.

I think you'll agree that our excellent results in Q1, coupled with the fact that we are gaining market share in virtually every part of our business, clearly show that we are executing this growth agenda extremely well. We are very close to our clients, helping them with their critical new initiatives, while at the same time staying focused on running Accenture as a high-performance business. As a result, we have great momentum, and are on a solid trajectory for continued growth, and more importantly, are expanding our market leadership.

As you know, Pierre Nanterme, who is here with us in Boston this week, will become the CEO on January 1st. So I thought it would be good for you to hear from Pierre. Pierre?

Pierre Nanterme - Accenture - Chief Executive Officer Designate

Thanks, Bill. I'm delighted to be here today, and I can tell you that the transition with Bill is going exceptionally well.

Let me start by saying that my first and highest priority will be to work with Pam and the rest of our leadership team to deliver on our priorities and commitments for fiscal year 2011, building on the last few quarters. We are on a strong trajectory, with the right actions for capturing growth underway. So, you should not expect any big changes in our strategy moving forward. My focus will be on accelerating the execution of our growth agenda to make sure we are capturing the growth opportunities we see in the marketplace.

Now, let me share with you a few principles that I hold deeply. The first is profitable growth. Growth without profits doesn't mean much. This is the discipline we demonstrated in the Financial Services operating group, as reflected in our Q1 results. We will pursue robust growth while making smart investments and improving profits.

Second, bringing the best of Accenture. Our clients, who are so important to us, are the envy of the industry, especially our Diamond client relationships. Over time, we expect to significantly increase the number of Diamond clients we have, for even greater durability in our business.

Third, shareholders as partners. From my experience in the financial services industry, I understand what the market expects: Openness, transparency and responsiveness. You can be assured that I and the rest of our leadership team are totally committed to this.

Fourth, sustained leadership. We will never cede our market position. Our goal is to remain the leader in our industry. We will always stay relevant to our clients and the industries we serve, and we will continue to be the company that competition wants to be like.

And finally, our highly skilled people. The incredibly talented group of Accenture people around the world, who are so committed to the success of our clients, make me even more confident in our ability to achieve our goals.

So, we are on a good trajectory for growth, and I am very excited about taking on the CEO role. I believe there are great opportunities ahead for Accenture. Now, let me turn the call back to Pam, who will provide our business outlook.

Pamela Craig - Accenture - Chief Financial Officer

Thank you, Pierre. As a reminder, each quarter we provide an outlook for the next quarter's revenue and an update on our annual outlook for the full fiscal year. As we stated throughout this call, we are very pleased with the momentum in the first quarter, as our strategy of strong business propositions for our clients is working. We also recognize that the global economy continues to have a mix of positive and negative news around the world, and we remain vigilant about that.



Dec 16, 2010 / 09:30PM GMT, ACN - Q1 2011 Accenture Earnings Conference Call

We know we need to continue to drive a focused strategy of what generates value for money for our clients and to manage our business with discipline. So, for the second quarter, we expect revenues to be in the range of \$5.6 billion to \$5.8 billion. This range assumes a foreign-exchange impact of negative 2% for the quarter and reflects the foreign-exchange rates over the past few weeks.

Now turning to the full fiscal year, we are now assuming a foreign exchange impact of 0%. Based on our qualified pipeline, strong demand for our services continues. We are raising our fiscal year 2011 revenue outlook to be 8% to 11% growth in local currency. And based on our Q1 results and what we see for Q2, we believe we are tilting toward the high end of that range.

We continue to expect new bookings for the fiscal year to land in the range of \$25 billion to \$28 billion. We continue to expect operating margin to be in the range of 13.6% to 13.7%. You should expect some fluctuations quarter to quarter, as we've seen in the past.

We continue to expect our annual effective tax rate to be in the range of 28% to 29%.

We now expect our earnings per share for the full fiscal year to be in the range of \$3.08 to \$3.16, an increase of \$0.08. About \$0.05 of the increase is due to higher revenue at the same operating margin, and about \$0.03 is due to the updated assumption from the impact of foreign exchange on our results.

Finally, we continue to expect operating cash flow to be in the range of \$2.7 billion to \$2.9 billion, property and equipment additions to be \$340 million, and free cash flow to be in the range of \$2.4 billion to \$2.6 billion. Our free cash flow this year compared to last year assumes slightly higher DSOs, higher tax cash payments due to their timing, higher property and equipment additions, and higher bonus payments related to fiscal year 2010 performance. The impact of these items will continue into Q2 and have the biggest impact on our free cash flow during the first half of the year. As you know, most of our free cash flow is generated in the second half of our fiscal year.

As our fiscal Q2 takes shape and we turn now into calendar year 2011, we are positioned well to drive revenue growth and market share for our broad and durable base of services. And at the same time, we will continue to responsibly invest in developing talent and new business while maintaining a strong balance sheet and cash-flow generation.

So with that, let's open it up so that we can take your questions. KC?

KC McClure - Accenture - Managing Director - Investor Relations

Thanks, Pam. I would ask that you each keep your questions limited to one question and follow-up to allow as many participants as possible to ask questions. Kathy, would you provide instructions for those on the call?

QUESTION AND ANSWER

Operator

(Operator Instructions). Our first question comes from Rod Bourgeois with Bernstein.

Rod Bourgeois - Sanford C. Bernstein & Co. - Analyst

Hi, guys, I just want to talk about the revenue acceleration, or at least the apparent acceleration in demand here. So you beat consensus by 5% on revenues, and I guess I'm wondering if you've been at all supply-constrained in recent months. In other words, are you seeing above-normal cases where you actually don't have enough staff to meet the demand that you're seeing in the market, given that you far exceeded the upper end of your revenue range, or have you been nimble enough to hire fast enough to meet the demand that you are seeing?

William Green - Accenture - Chairman & CEO

Well, Rod, this is Bill. One of the things I am just incredibly proud of is our ability to on-board people, have them trained, have them deployed and deliver 87% utilization while we're doing that. You know how the economics of our business works, and the management of supply and demand is just critical. We were able to mobilize and get people in the door and get them productive. And we continued on that journey, actually,

7



continue with that momentum. And so, I think we were able to respond to the increasing demand in a first-class way. And we believe, and Pam mentioned, our target for this year. We believe we will be able to continue to do that. We also had a 2-point improvement in our attrition, which means a lot to us as well. But I think it's interesting, because what we've seen is the intersection of an improving economy. And I think if you put an improving economy with a series of tech waves, and the fact that I think as a company we are executing in an exceptional way on just about every dimension, we've been able to take advantage of the growth opportunities we see in the market and not only on-board more work, but to be doing, really frankly, higher-quality work as well.

Rod Bourgeois - Sanford C. Bernstein & Co. - Analyst

So Bill, can you elaborate on the tech waves that you're seeing that are kind of across the board as the economy improves, and specifically in the area of cloud. Are you having enough activity in the cloud arena to declare that cloud will definitely be a net opportunity for Accenture's demand rather than a net threat? Thanks a lot.

William Green - Accenture - Chairman & CEO

Let me sort of back into it. I think, first of all there's a series of technology waves. One of them is quite simply just a delayed refresh; people that had slowed spending and the technology space are starting to accelerate. Then you add virtualization and the cloud — and mobility is also another important wave — so there's a series of things going on there. And right now we just see ourselves at the front end of everybody figuring out how do I ride these waves in as practical and pragmatic and economically responsible way? So we're doing a lot of work on what people's strategy should be. Some of that is the rationalization of current environments to be prepared for the cloud, and others, how are people going to get from where they are to the cloud over the next three to five years and take advantage of the innovations that have come out in the marketplace in the last 12 to 18 months? So we see this thing is a huge business booster to Accenture. We see ourselves at the intersection of trade and commerce as it relates to the on-boarding and the on-ramping to the cloud, which we've talked about. And I think importantly, a lot of our clients have a lot more confidence in their business and they're positioning themselves now to make more investments in 2011 as we get into the calendar year.

Rod Bourgeois - Sanford C. Bernstein & Co. - Analyst

Well said, thanks guys.

Operator

We'll go next to Adam Frisch with Morgan Stanley.

Nathan Rozof - Morgan Stanley - Analyst

Hi, this is Nathan Rozof on for Adam Frisch. Pierre, let me be the first to welcome you to the earnings call circuit. I had a question for you. One of the things that we posed during the analyst day was a question about Accenture's financial identity. Really what that is, the relative prioritization between revenue growth and margin expansion. With your new role that you're going to be taking on here in a month or so, we wanted to get your thoughts on how you see the interplay between revenue growth and margins for Accenture going forward.

Pierre Nanterme - Accenture - Chief Executive Officer Designate

Thanks for the question, and I'm pleased to be with you today here in Boston. Our financial identity, as you said, has always been around profitable growth, and we'll probably never trade one against the other. This is exactly my intent, to continue with that discipline. We've been able over time, and especially this last quarter, to post excellent growth together with, as well, excellent profit, and this is what we will continue to do moving forward.

Nathan Rozof - Morgan Stanley - Analyst

Thank you. For our follow-up question, I wanted to turn over to bookings. Obviously, bookings started off strong — I think as of the fourth-quarter call, bookings were up 14%, versus where they were at that time last year, and they continued through the quarter. Can you give us any insight as to how bookings have been progressing into the fiscal second quarter, in terms of where you are year-to-date versus last year?



Dec 16, 2010 / 09:30PM GMT, ACN - Q1 2011 Accenture Earnings Conference Call

Pamela Craig - Accenture - Chief Financial Officer

Yes, I'll take that one, Nathan. As you can see, the consulting bookings continue to be very strong. We have \$3.5 billion in Q4, we're up over \$3.7 billion in this quarter, the highest in ten quarters. And so that continues. The outsourcing bookings this quarter, as I had signaled, we did expect them to be relatively light. Interestingly, they weren't as light as most of the last several first quarters. And I can't tell you why the first quarter is lighter, to be honest. We did feel that way and we did expect them to trend up next quarter for sure.

Nathan Rozof - Morgan Stanley - Analyst

Thanks, I appreciate it. And Bill, I know you're not going far, but we just wanted to wish you all the best in your new role.

William Green - Accenture - Chairman & CEO

Thank you very much.

Pamela Craig - Accenture - Chief Financial Officer

Thanks, Nathan.

Operator

We'll go next to Julio Quinteros with Goldman Sachs.

Julio Quinteros - Goldman Sachs - Analyst

Hey guys, how are you? I was about to ask you how Interchange impacted you guys, but I realize that was a different call altogether.

Pamela Craig - Accenture - Chief Financial Officer

You cover too much.

Julio Quinteros - Goldman Sachs - Analyst

Busy night, for all of us. On the -- we were just in India and came back, and had a chance to meet with you guys and a bunch of other companies that were down there. And the pace of activity, the sentiment was so positive for offshore, I just wanted you guys to maybe dig in a little bit deeper in terms of this continued transition that you guys have talked about. How much further does it go? Because as it is already, it's a major part of your headcount, I think it was half of your headcount, and by our own estimates, we think that you guys are approaching somewhere in the neighborhood of \$5 billion to \$6 billion of revenue. My question I guess very specifically is, when does all of this offshore stuff actually begin to benefit you guys from a margin perspective, because if I look at the margin profile of all of these other companies that do offshoring, it's much higher. Why should we not expect it to also help you guys benefit your margin profile as well?

William Green - Accenture - Chairman & CEO

I think over time you probably should. You probably should be demanding on that dimension.

Julio Quinteros - Goldman Sachs - Analyst

I'm demanding.



William Green - Accenture - Chairman & CEO

Yes, I know that. And so are we. We continue to work on our cost to serve. Unlike others, we have this journey, right, of some work that was onshore traditionally, to offshore. We talk about India a lot, but I was in Manila two or three weeks ago. We have 20,000 employees [there], we'll have 25,000 by the end of the year. We've been in the country 25 years. We opened three new buildings. I mean, this thing is just going to continue, and we keep getting scale and we keep getting better at it, and we keep industrializing and some of the things that you've seen down there, and I think all of that is going to serve us well.

It's notable though, that we have been able to continue to deliver and execute in the superb way while we manage this onshore to offshore transition, in really frankly a very seamless way as it relates to our clients, which is the first thing. And then secondly, as it relates to our economic result, and we continue to focus on mining more profits out of the opportunities that we have because of the Global Delivery Network. We'll let Pam follow up.

Pamela Craig - Accenture - Chief Financial Officer

I'll just give you a little bit, right, because that was it. We're very pleased with the cost to serve and the progress that we have made there, and we're going to continue to tackle the rest of the cost structure, Julio; we don't ever see that as an ending thing, right, so we have stuff underway this year to sort of tackle the whole selling side of things, and as you know, we hold the line on G&A.

Julio Quinteros - Goldman Sachs - Analyst

Understood. One last thing, the other point that was really clear too, was just this mentality, right, that the way the models are changing, for the offshore guys moving up as well, right, is switching to more of a demand-generation mentality, and every time I hear that, I almost feel like, that's what you guys do, right? So do you have to change the way that you guys approach the marketplace today, or is the model with offshore what you have to continue to take in the marketplace, just to stay effective?

William Green - Accenture - Chairman & CEO

I think the offshore dimension added a whole new life to Accenture over the past five to eight years. This going up the stack stuff is not for the faint of heart. It is incredibly hard to do, and I would just tell you that I've seen people taking bigger things horizontally but very few really moving up the stack. The interesting thing about the recovery, the economic recovery — and we always talked about this — it wasn't a recession, it was a reset, and that buyer values were going to be different when they came back. And the thing that is incredibly different as buyer values come back and as people start investing again, is they expect companies to be able to provide the full stack of services from envision and architect, design and build, and operate on behalf of their business. I think the business that's coming back is coming towards our model.

Julio Quinteros - Goldman Sachs - Analyst

That's helpful. Thank you, guys.

Pamela Craig - Accenture - Chief Financial Officer

Thanks, Julio.

Operator

You have a question from Jason Kupferberg with UBS.

Jason Kupferberg - UBS - Analyst

Hey thanks guys. Bill, I just wanted to pick up on one of the drivers you talked about. I think you mentioned the delayed refresh. I just wanted to get a read from you whether or not we should interpret that as release of pent-up demand if you will. It clearly seems like you see some of that persisting into calendar 2011. But, do you feel like the industry, including yourselves, are still riding a wave of pent-up demand that at some point peters out. I guess where I'm ultimately going with this is, how do you see the structural growth rate of Accenture going forward? You



guy's are going to do 8-11[%] this year, maybe near the upper end of the range, albeit off a pretty easy year-over-year comparison, but where does that leave us in terms of thinking longer term if we try to separate what might be the refresh in the pent-up demand from the underlying trends that you see out there?

William Green - Accenture - Chairman & CEO

I think you're going down a rat hole with this pent-up demand thing, to be perfectly honest. We look at our business, we can grow 7% to 10% consistently over a business cycle. Let's hope we have a business cycle that's many, many years and let's hope that we can outperform that, and we're delighted with where we're starting. What you've really seen this year is, people were cautious about spending in calendar 2010, and now we're getting to the end of calendar 2010, and they're feeling more confident about their business, so they're spending a little more money. I'm not sure it's pent-up demand, per se, it's just more confidence in investing in the business. I think that's just going to fall right over into 2011. I don't think it's anything about the release of pent-up demand. I think it's just going to be a higher level of people investing in their business in order to get better economic results. And there's no question that people had held off a lot of investments that people are going to now start to do. And I think what we're just seeing is the confidence that's returned in management, in companies across the board, has had people get ahead of some of those investments. But I think it's something that's consistent, and I think it's going to continue into the medium term at least.

Pamela Craig - Accenture - Chief Financial Officer

Let me just give you a few more facts here, Jason. Our qualified pipeline, if we look at just how it's been building over the year, it's up just in consulting alone 25% year-over-year. So we don't see sort of pent-up demand stuff in there. This is stuff that we expect to continue. I told you last quarter that we saw 14% more revenue in our backlog for this year than we had seen in the prior year. As I look at this quarter ahead, the nine months versus last year's nine months ahead, 13% more. This is not about things popping and coming down. This is a very steady increase that we see in terms of our pipeline and future look for our business.

Jason Kupferberg - UBS - Analyst

That's really helpful. If we can just pick up on some of the offshore discussion, but switch it over to China. More attention being paid there to some Chinese IP services firms; they're obviously still pretty small. But can you guys talk a little bit about what you're doing in China, what's customer demand like? And I'm thinking about this both in terms of servicing local Chinese clients as well as using China as part of your GDN, and any numbers you might be able to share around revenue or headcount out of China?

William Green - Accenture - Chairman & CEO

We have a lot of moving parts there, but there's sort of three dimensions. First is Dalian and our related offshore capabilities, which continue to grow. The second is, way back the business was very much a global multi-national business, with a lot less work for the national companies, and now I would say it's sort of like a third, a third, a third in terms of headcount if you look across it, and we actually even have a Diamond client in China, which is a phenomenal thing, that's a local company. The ambitions of the Chinese company are incredibly high to compete on the global stage. Pierre knows that from his work in banking over there. An insurance company in China is about 25 times the size of a big insurance company here in the United States in terms of customers, and all those companies have their sights set on operating on the global stage, which means global business practices that were consistent, which means making sure they deliver real value for money, and making sure that they have sort of the transparency, if you will, to be compared against other great companies around the globe. We see China as a good and growing market. It grows at many times the normal rate of Accenture. And we're pleased with our growth there, but we think the opportunities are just incredible, and the key thing is to capture the market space with the leading companies, and that's what we're very much focused on.

Jason Kupferberg - UBS - Analyst

Can you share the headcount number in China?

William Green - Accenture - Chairman & CEO

I'm going to have to wing it, but right now, I'd say it's between 5,000 and 6,000.



Dec 16, 2010 / 09:30PM GMT, ACN - Q1 2011 Accenture Earnings Conference Call

Jason Kupferberg - UBS - Analyst

Terrific. All right. Thanks, guys.

William Green - Accenture - Chairman & CEO

Thanks.

Pamela Craig - Accenture - Chief Financial Officer

Thanks, Jason.

Operator

We have Darrin Peller with Barclays Capital.

Darrin Peller - Barclays Capital - Analyst

Nice job on bookings again. Any more color on operating group or industry verticals, and also, can you talk a bit about the competitive landscape? Specifically, are you seeing more market share gains, especially in light of some of your larger competitors having recently shown only mild growth or decreases, and then just a quick follow-up?

William Green - Accenture - Chairman & CEO

I guess there's two things that when we went through the season getting ready, we always use this "all cylinders thing," if we can ever get the firm on all cylinders, and with four of our five operating groups showing double-digit growth, there's a lot of momentum, and as Pam mentioned, Health & Public Service continues to be challenged, mostly because of the public-service dimension. But that will work its way out as well, and so I think that's important. And then interesting, our win rates on the new work have been higher than they were historically, and a lot of the new work — and you see that in the consulting bookings — has a heavy consulting component, which is a place where there aren't that many competitors that can go. So if you just look at those dimensions, we feel pretty good about the broad-based momentum that's across the firm. And even in some of the countries in Europe, or people ask the question "what about Europe," you really have to look at it three dimensions. One is the economy, second is the sovereign debt, and the third is who are our clients. And if you look at who our clients are, they're the big global European companies. Their businesses have a totally different dynamic than the economic condition of Spain, and if you look at the economy, sovereign debt aside, there's growth in many of the economies over there and some good momentum, so we're not down on Europe at all. I know it draws a little fire in the newspaper, but frankly, we feel good about our business there and the prospects.

Darrin Peller - Barclays Capital - Analyst

But even Public Service is, I mean, Health & Public [Service] was sequentially a nice pickup. Does that seem to be getting a little better?

William Green - Accenture - Chairman & CEO

Health, we're doing some really profound stuff. If you look at the health business broadly, it's sort of all the things we do for the payors and the people that have to deal with the health administration, we're doing some of the most-defining things around medical records that anybody's doing anywhere in the world, and in fact we will be working on the first project where an entire country's medical records are totally digitized. But also important to that is initiatives around the world in new markets, where they sort of have a clean sheet of paper to build a healthcare service industry, if you will, and we're on the front end of that, so we feel particularly good about what's happening in health.

Public service continues to be a rocky ride; the UK and the US, they're not big in terms of the whole of Accenture, but they're a big component of our public service business, and those have been, as you read in the paper, particularly challenged. But frankly, there's still a lot of money being spent and a lot of services that need to be deployed, and we're just trying to make sure we're lining up with the right opportunities that are going to continue to go forward.



Darrin Peller - Barclays Capital - Analyst

All right. Just a quick follow-up for Pam. Pam, your prior guidance is to return \$2.6 billion in capital. This quarter you saw \$620 million of buybacks, and with a dividend of \$320 million, you're obviously at a run rate that's a fair amount higher, I think over \$3 billion for the year. I didn't hear you mention guidance on or an update to that number, the \$2.6 billion return. Can you just comment on that number, real quick?

Pamela Craig - Accenture - Chief Financial Officer

Sure. I don't have an update to it at this point, and of course the dividend is twice a year, so this quarter was skewed by that. And at this point we are on track for that \$2.6 billion.

Darrin Peller - Barclays Capital - Analyst

Okay. Thanks, guys.

William Green - Accenture - Chairman & CEO

Thank you.

Operator

We'll go next to Tien-Tsin Huang with JPMorgan.

William Green - Accenture - Chairman & CEO

Hi, Tien-Tsin.

Pamela Craig - Accenture - Chief Financial Officer

Hi, Tien-Tsin.

Tien-Tsin Huang - JPMorgan - Analyst

Good afternoon, good quarter here. I wanted to ask about the margins. The G&A cost came in quite low here, a little bit – there's definitely some upside there in terms of what the lower dollar run rate looks like. So I'm curious if that was designed to offset some of the gross margin headwinds, and whether or not this level is permanent, Pam, on the G&A side.

Pamela Craig - Accenture - Chief Financial Officer

I think what was -- As you know, we've had this strategy of really holding the line on G&A cost. We certainly did that, so in terms of, as a percentage of net revenue, we saw that fall. We also, every quarter, take a look at our bad debt reserve. It's not a big number in the scheme of things — a very small number on a \$20 billion cost base — but because we've had good experience in the last two years with that, we did take that down a click, that reserve, and that was reflected in the G&A costs as well.

Tien-Tsin Huang - JPMorgan - Analyst

I see. So on the gross margin side, you mentioned the use of sub[contractor]s and training and bonuses. Did you frame how much of the pressure was coming from each, in particular the subcontractors, I'm guessing because that would be temporary.



Dec 16, 2010 / 09:30PM GMT, ACN - Q1 2011 Accenture Earnings Conference Call

Pamela Craig - Accenture - Chief Financial Officer

Yes. In the gross margin this quarter, we're in the process and doing very well with absorbing the salary increases, and obviously we had some this year, and they were negligible last year. So that's one, and that was job one. But with the demand, the revenue did come in higher than expected. The demand was even higher, 87% utilization, as Bill said, in answer to the first question. So we did fill in with marginally more subs this year, and that did have a slight impact on the gross margin, but clearly, we needed to do that and we did do that. Also, with on-boarding so many people, right, as the revenue started to ramp, we do have higher recruiting and training costs when we're doing that. So is it temporary, yes, in the sense of it's a little ahead of the future revenue.

Tien-Tsin Huang - JPMorgan - Analyst

Got it. Thanks so much.

William Green - Accenture - Chairman & CEO

Thank you.

Operator

We have Ed Caso with Wells Fargo Securities.

Ed Caso - Wells Fargo Securities - Analyst

Hi. Let me add my congratulations. The acquisitions, there's been a bunch of small ones lately. Did that factor at all into the guidance for the next quarter, or the rest of the year?

Pamela Craig - Accenture - Chief Financial Officer

No, not really, Ed. As you said, there were three small ones that closed in the first quarter; we've announced another one in Germany. They're all consistent with our tactical tuck-in strategy and did not have a big impact on the guidance.

Ed Caso - Wells Fargo Securities - Analyst

Can you talk a little bit about the transformational business that you've got. Are the milestones still fairly short or is the business picking up, but with shorter milestones? Is there a day when we're going to again see the \$100 million, \$200 million ERP implementation?

William Green - Accenture - Chairman & CEO

We actually do have some of those. You just think everyone's got it, and then you realize they don't. I was on the phone with a CEO, one that we were just going to get started this morning, actually. But I guess what we have found, and we have looked across our Diamond clients for the nature of the work we're doing and across our portfolios, and the work that has come on in the last three to five months has more of a transformational bent to it. In other words, people are solving for an outcome, as opposed to buying labor. We're making fundamental changes in how business gets done. It has operating model ramifications in its core. It's not only technology, but it's process and people-related as well. But true to the form over the last several years, people are taking smaller bites. We talked about that. There's interim gating points, and people are taking it as a pay-as-you-go kind of go kind of basis. So the work content has become more transformational, which really plays to our consulting power, but at the same time, people aren't signing those \$500 million or \$1 billion deals. They are more bite-size steps, and things that go over three to six years, but they'll do so one step at a time.

Ed Caso - Wells Fargo Securities - Analyst

Congratulations on finishing on a high note and enjoy your semi retirement.



Dec 16, 2010 / 09:30PM GMT, ACN - Q1 2011 Accenture Earnings Conference Call

William Green - Accenture - Chairman & CEO

Thank you very much.

Pamela Craig - Accenture - Chief Financial Officer

We're not going to let him semi. Thank you, Ed.

Operator

Next we have Bryan Keane with Credit Suisse.

Bryan Keane - Credit Suisse - Analyst

Hi, guys. Solid results. One question I had was the SI business, it sounds like it's showing increasing strength, but I guess you guys are still seeing deflationary revenue pressure as you shift to more lower-cost locations. So my question is, how much longer do you have on that, and is there any way to quantify how much that might be impacting revenues — two to three points, I'm guessing — but anything along those lines?

Pamela Craig - Accenture - Chief Financial Officer

The hours are up significantly more than the revenue as the shift occurs. And interestingly, there's also, as Bill said, with this uptick in this more transformation work, there's also more demand onshore, interestingly, too. So this is all in the mix, as we expected.

When we first talked about this in April, we said medium term. We'll still be -- we're probably a little ahead of where we expected to be at this point, but we're going to still be doing this this year and next year. And again, managing it very carefully, and at least to date, very successfully.

Bryan Keane - Credit Suisse - Analyst

But on a longer-term basis when we get to apple to apples, if it's a couple years from now, that should automatically help the growth rate?

Pamela Craig - Accenture - Chief Financial Officer

Absolutely.

Bryan Keane - Credit Suisse - Analyst

And then just last question for me. I might have missed this, I'm jumping around a few calls here, but on the Health & Public [Service] margins, I heard there were some investments in there, and the margins were a little lower than we expected. Should we continue to see those margins at these lower levels, or should it start to spring back, next quarter?

Pamela Craig - Accenture - Chief Financial Officer

This year I think is going to be a repositioning year for that business. That's what we've said, and we are supporting more investments in terms of selling costs, investment in the health business, and we do have some contracts in the public service portfolio that are just a little challenged in terms of profitability right now.

Bryan Keane - Credit Suisse - Analyst

Okay, that's helpful. Great work, thanks.



Dec 16, 2010 / 09:30PM GMT, ACN - Q1 2011 Accenture Earnings Conference Call

Pamela Craig - Accenture - Chief Financial Officer

Thank you.

William Green - Accenture - Chairman & CEO

Thanks.

KC McClure - Accenture - Managing Director - Investor Relations

Kathy, we have time for one more question.

Operator

That will come from Moshe Katri with Cowen.

Moshe Katri - Cowen and Company - Analyst

Thanks. Pam, can we get some metrics on the revenue growth side, looking at some of the large European economies, including the UK?

Pamela Craig - Accenture - Chief Financial Officer

Interestingly, I think we had our best growth in the quarter from France. I think that was particularly appropriate, given our new CEO. So we had good positive growth in France and Italy and the UK. Some of the smaller countries also had very good growth, like Sweden, and we just have a couple of the smaller ones with negative growth in the quarter.

Moshe Katri - Cowen and Company - Analyst

And then in the UK market, is there a specific vertical that's strong? And I'm focusing on the UK just because it is still your largest revenue contributor out of Europe, right?

Pamela Craig - Accenture - Chief Financial Officer

Yes, it is still our largest country in Europe.

William Green - Accenture - Chairman & CEO

I feel good about the UK. I was just there... some number of days ago, I can't remember. And both had big new opportunities, and there were things on the Capital Committee this last week that were big UK opportunities. We're managing the business we have there very well, but we see a lot more stability in the country, the economic condition, the banks — Pierre would know well — the financial services industry has come roaring back, leaving some of the other industries in their wake, but many of those are kicking in as well. And so we're very optimistic about the UK. They are the homes to some big global companies. Those are the companies that are our clients, and I think for the most part, their economic performance has improved dramatically, and maybe most importantly, and I always talk about this with us, the confidence of management of these companies has improved dramatically, so people are starting to invest in the future, more now than they have been in the past number of years. One thing I would just mention just broadly is The Business Roundtable, I think on Tuesday, the results came out, and for the first time in nine quarters companies saw increasing sales, increasing headcount, and increasing capital expenditure, and we haven't had that in nine quarters. And if you look at some of the other major measures like that that we look at around the world, it's pretty much consistent with that. Nobody wants to declare that things are getting better, and certainly the media doesn't, but frankly, when you sit with a group of business leaders, people are looking forward and are starting to become dramatically more optimistic, and certainly willing and have an imperative to invest in their business.



Moshe Katri - Cowen and Company - Analyst

And just a brief follow-up, I haven't heard too much about pricing on the call. Maybe you can talk a bit about what you're seeing in terms of pricing trends. The tier-one offshore companies out of India are talking about some pricing increases, and about the fact that clients are willing to let these go through. What's your feedback on that?

William Green - Accenture - Chairman & CEO

Our consensus view is pricing is stable. If you take the puts and takes across all the industries and across all of the services we have, pricing is stable, which we're fine with. There's the places where we always have, and continue to historically get, very favorable pricing, because we have dramatic power. There's still pieces of the business where the pricing is incredibly challenged and the work is very competitive. So our public view is that pricing is stable at this point.

Moshe Katri - Cowen and Company - Analyst

Great. Thank you.

William Green - Accenture - Chairman & CEO

Let me just say a couple things in closing. First, I couldn't be more pleased with the very strong results in Q1 and the momentum we're seeing in the business. Momentum is a big deal to us. As we get this machine moving, it generally keeps moving, and I just couldn't be more pleased that momentum continues here.

Importantly, I want to thank the now 211,000 men and women of Accenture, whose tremendous efforts and dedication are what enable us to deliver values to our clients and to our shareholders alike.

Pierre is stepping into the CEO role in just a few weeks; I will continue as Chairman, where I plan to devote my time to our clients, our growth, and our leadership. We've been joking this week as people do about the shape an organization is in when you "turn it over to the new guy." While I am very proud, not only of our position, but maybe more importantly, how well positioned we are for the future. The best is ahead for Accenture. Our team sees nothing but opportunity, and we're raising our game yet again. This has always been and always will be a team effort, and I am excited to contribute to this next chapter.

I really enjoyed these calls over the past six years, it's been a great experience for me, and I'm sure I'll continue to see many of you along the way. Thank you very much for joining us today on the call. As always, we appreciate your continued support. If you have any questions, please feel free to call KC to make arrangements for follow-up.

Best wishes for a safe, relaxing happy holiday and new year. All the best.

Operator

Ladies and gentlemen, this conference will be available for replay after 7 PM today through midnight, Thursday March 24, 2011. You may access the AT&T Executive Playback Center at any time by dialing 1-800-475-6701 and entering the access code 178235. International callers, dial 320-365-3844, using the same access code, 178235. That does conclude our conference for today. Thank you for your participation and for using AT&T Executive Teleconference. You may now disconnect.



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