

Accenture

Second Quarter FY 17 Financial Results

Conference Call Transcript

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CORPORATE PARTICIPANTS

Angie Park – *Managing Director and Head of Investor Relations*

Pierre Nanterme – *Chairman and Chief Executive Officer*

David Rowland – *Chief Financial Officer*

PRESENTATION

Operator

Ladies and gentlemen, thank you for standing by. Welcome to Accenture's Second Quarter Fiscal 2017 Earnings Call. During today's conference all participants will be in a listen-only mode. Later we will conduct a question and answer session; instructions will be given at that time. If you should require assistance during today's conference, please press the star followed by the zero and a specialist will assist you offline. As a reminder, today's conference is being recorded.

I would now like to turn the conference over to Managing Director, Head of Investor Relations, Angie Park. Please go ahead.

Angie Park

Thank you, Shannon, and thanks, everyone, for joining us today on our second quarter fiscal 2017 earnings announcement. As Shannon just mentioned, I'm Angie Park, Managing Director, Head of Investor Relations. With me today are Pierre Nanterme, our Chairman and Chief Executive Officer; and David Rowland, our Chief Financial Officer.

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. Pierre will begin with an overview of our results. David will take you through the financial details including the income statement and balance sheet for the second quarter. Pierre will then provide a brief update on our market positioning before David provides our business outlook for the third quarter and full fiscal year 2017. We'll then take your questions before Pierre provides a wrap up at the end of the call.

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'll discuss on the call, including our business outlook, are forward-looking and, as such, are subject to known and unknown risks and uncertainties, including but not limited to those factors set forth in today's news release and discussed in our annual report on Form 10-K and quarterly reports on Form 10-Q and other SEC filings. These risks and uncertainties could cause actual results to differ materially from those expressed on this call.

During our call today we'll reference certain non-GAAP financial measures, which we believe provide useful information for investors. We include reconciliations of non-GAAP financial measures, where appropriate, to GAAP in our news release or in 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 Pierre.

Pierre Nanterme

Thank you, Angie, and thanks everyone for joining us today. We are very pleased with our financial results for the second quarter and first half of fiscal year '17. For the quarter, we again delivered broad-based revenue growth across many dimensions of our business and we continued to gain significant market share.

We see excellent demand for our services, especially in high-growth areas such as digital-, cloud- and security-related services. Our very strong bookings confirm both the relevance and success of our strategy to rotate our business to the New and support our confidence as we look ahead to the rest of the fiscal year.

Here are a few highlights for the second quarter and year to date:

- We delivered very strong new bookings of \$9.2 billion for the quarter and \$17.5 billion for the first half.
- We grew revenue 6% in local currency for the quarter and 7% year to date, with continued strong growth across many areas of our business.
- We delivered earnings per share of \$1.33, which brings EPS for the first half of the year to \$2.91, an 11% increase on an adjusted basis.
- Operating margin was 13.7% for the quarter and 14.7% for the 6 months, an expansion of 20 basis points year to date.
- We generated free cash flow of \$50 million for the quarter and \$1 billion year to date.
- And, we continue to return a substantial amount of cash to shareholders through share repurchases and dividends, including more than \$2 billion year to date. Today, we announced a semi-annual cash dividend of \$1.21 per share, which will bring total dividend payments for the year to \$2.42 per share, a 10% increase over last year.

So, with the first half of the year behind us, I feel very good about our business. We see very strong demand in the marketplace for our differentiated capabilities, and remain confident in our ability to deliver our business outlook for the year.

Now, let me hand over to David, who will review the numbers in greater detail. David, over to you.

David Rowland

Thanks, Pierre, and thanks to all of you for joining us on today's call. Overall, we delivered strong results in the second quarter which were aligned with our expectations and position us very well to achieve our full year financial guidance. We continue to see favorable market conditions in most areas of our business, especially as it relates to strong demand for digital-, cloud-, and security-related services, which plays to our strength as a leader in innovating and leading in the New.

Our second quarter and year-to-date results demonstrate our ability to continue to deliver on the essential elements of our formula for driving superior shareholder value. So, before I get into the details, let me summarize the major headlines.

- Net revenue growth in local currency of 6% in the second quarter and 7% year to date continues to significantly outpace the market driven by double-digit growth in all three components of the New, including digital-, cloud-, and security-related services. Growth continues to be broad-based with positive growth in the vast majority of our industries and geographic markets, more than offsetting cyclical market pressures that continue in a few concentrated areas of our business, specifically Energy, Chemicals & Natural Resources, and Communications & Media. Absent those concentrated areas of pressure, the majority of our business grew 9% on a quarter-to-date basis and 10% on a year-to-date basis.
- Operating margin of 13.7% in the quarter came in as expected and consistent with last year. Operating margin of 14.7% for the first half of the year represents 20 basis points of expansion. These results continue to reflect significant levels of investment in our business and our people

to further enhance our differentiation and competitiveness in the marketplace. And, on a year-to-date basis, we have delivered 11% growth in earnings per share over fiscal '16 adjusted EPS.

- Our free cash flow of \$50 million in the quarter and over \$1 billion year to date puts us on a trajectory to deliver on our annual guidance, which reflects free cash flow in excess of net income. And, importantly, we continue to execute against our strategic capital allocation objectives, first, by investing over \$800 million across 16 transactions in the first half of the year, and second, by returning roughly \$2.2 billion to shareholders via dividends and share repurchases.

So, as Pierre said, we are pleased with our overall results so far this year, and we're encouraged by the trends we see in the market and the potential for even stronger growth and momentum in the second half of the year.

With that said, let's get into the details of the quarter, starting with new bookings. New bookings were \$9.2 billion for the quarter, consulting bookings were \$4.6 billion with a book-to-bill of 1.1, and outsourcing bookings were \$4.6 billion with a book-to-bill of 1.2. We were very pleased with our bookings which landed in the range we expected and represents the third-highest level of new bookings over the past ten quarters.

From a business dimension perspective, we were pleased with our bookings in both Strategy and Consulting Services combined and Application Services. And, as you would expect, digital-, cloud- and security-related services continued to be an important theme in the work we contracted with our clients. Looking forward, we began the third quarter with a healthy pipeline and we believe we're positioned for continued strong bookings in the second half of the year.

Turning now to revenues. Net revenues for the quarter were \$8.32 billion, a 5% increase in USD, 6% in local currency reflecting a foreign-exchange headwind of approximately 2%, consistent with the guidance provided last quarter. Our Consulting revenues for the quarter were \$4.4 billion, up 3% in USD and 5% in local currency. And, our Outsourcing revenues were \$3.9 billion, up 7% in USD and 8% in local currency.

Looking at the trends in estimated revenue growth across our five business dimensions, growth was led by Operations which posted double-digit growth for the fifth consecutive quarter. Application Services delivered mid-single-digit growth and Strategy and Consulting Services combined grew low single-digits. Once again, the dominant driver of our growth was continued strong double-digit growth in the New with all three components growing double-digits as well.

Taking a closer look at our operating groups, Products, our largest operating group, led with 15% growth reflecting continued strong momentum in the business. Growth continued to be broad-based with strong growth across all geographies and industries.

Financial Services grew 8% in the quarter driven by double-digit growth in Banking & Capital Markets globally, and overall in both Europe and the Growth Markets. As expected, Banking & Capital Markets in North America returned to positive growth this quarter.

H&PS came in as expected at 2% growth with positive growth in both Health and Public Service globally and strong overall growth in both Europe and the Growth Markets. Overall growth in North America was flat. We expect H&PS to deliver stronger growth in the second half of the year and to deliver full-year growth in the mid-single-digit range, consistent with the comments I made in September.

Communications, Media & Technology grew 1% reflecting solid positive growth in North America and double-digit growth in the Growth Markets, partially offset by continued contraction in Europe. From an industry perspective, CMT was led by significant double-digit growth in Software & Platforms with positive growth in Electronics & High Tech. However, Communications & Media contracted on an overall basis primarily driven by our business in Europe. We expect that revenue growth in our European Communications & Media business will continue to be challenged for the rest of the year.

Finally, Resources revenues decreased 1% in the quarter, which is in the range we expected, and the storyline remains the same. We continue to see strong growth in Utilities which is more than offset by challenges in both Energy and Chemicals & Natural Resources, especially in North America. We expect our Resources group to continue to navigate a challenging environment, but to deliver positive growth in the second half of the year.

Moving down the income statement. Gross margin for the quarter was 30.1% compared to 29.8% in the same period last year. Sales and marketing expense for the quarter was 10.5% consistent with the same quarter last year. General and administrative expense was 5.9% compared to 5.7% for the same quarter last year. Operating income was \$1.1 billion in the second quarter, reflecting a 13.7% operating margin, consistent with quarter two last year.

As a reminder, in the second quarter of last year, we closed our Navitaire transaction which lowered our quarter two tax rate by 1.7%, and increased net income by \$495 million and diluted earnings per share by \$0.74. The following comparisons exclude this impact and reflect adjusted results.

Our effective tax rate for the quarter was 20.7%, compared with an adjusted tax rate of 15.4% for the same period last year. Net income was \$887 million for the second quarter compared with adjusted net income of \$905 million for the same quarter last year. Our diluted earnings per share were \$1.33 compared with adjusted EPS of \$1.34 in the second quarter last year.

Days services outstanding were 42 days compared to 44 days last quarter and 39 days in the second quarter of last year.

Free cash flow for the quarter was \$50 million, resulting from cash generated by operating activities of \$155 million, net of property and equipment additions of \$104 million. Our cash balance at February 28th was \$3.2 billion compared with \$4.9 billion at August 31st.

With regards to our ongoing objective to return cash to shareholders... in the second quarter, we repurchased or redeemed 7 million shares for \$816 million, at an average price of \$117.27 per share. At February 28th, we had approximately \$4.3 billion of share repurchase authority remaining.

As Pierre just mentioned, our board of directors declared a dividend of \$1.21 per share, representing a 10% increase over the dividend we paid in May last year, and this dividend will be paid on May 15, 2017.

So, at the halfway point in 2017, we feel good about our results and our positioning to deliver on our full-year business outlook. We continue to be laser-focused on driving our business to achieve our core financial objectives, which include growing faster than the market, delivering modest margin expansion and strong EPS growth, investing at scale for market leadership, and generating strong cash flow, which is both invested in the business and returned to shareholders through disciplined and smart capital allocation.

With that, let me turn it back to Pierre.

Pierre Nanterme

Thank you, David. Our strong performance in the second quarter and year to date demonstrates that we are executing our strategy very well to position Accenture as the leading and most innovative professional services company for the new digital world.

With 7% revenue growth in local currency in the first half of the fiscal year, we are clearly growing faster than the market. This is driven by our accelerated rotation to the New – digital-, cloud- and security-related services – which generated revenues of about \$8 billion in the first half, more than 45% of total revenues, and continued to grow at a strong double-digit rate.

And I am particularly pleased that we have achieved these results while continuing to invest for the future in strategic acquisitions, in building assets and solutions, and in the skills of our people, while at the same time, returning substantial cash to shareholders.

For Accenture, acquisitions are an engine to drive organic growth above the market. And we have stepped up our pace of acquisitions, investing more than \$800 million of capital in the first half of the fiscal year. And in the second quarter alone, we completed or announced 11 acquisitions to further strengthen our capabilities.

In digital, we are acquiring SinnerSchrader, one of the largest digital agencies in Germany. In cloud, we acquired solid-serVision, a leading ServiceNow provider. In security, we acquired Endgame's federal services business and announced the acquisitions of iDefense and Arismore. Avanade, our majority-owned joint venture with Microsoft, acquired Infusion, a leading provider of digital transformation services in the Microsoft ecosystem. And, we completed three acquisitions that further enhance our industry-deep expertise – InvestTech in asset management, Seabury Group in aviation, and Davies Consulting in utilities.

Across Accenture, we are leveraging the capabilities we have acquired to bring even more innovation to clients and to drive growth and scale organically:

- With MOBGEN, which is part of Accenture Digital, we teamed with Shell and Jaguar Land Rover to create the first-ever payment system in a car. This new innovation allows drivers to pay at Shell stations using an in-car touchscreen and app, ultimately delivering a better and more convenient customer experience.
- In Banking & Capital Markets, our recent acquisitions of InvestTech and Beacon Consulting are further strengthening our asset management capabilities adding deep skills and industry expertise, which has enabled us to win new business with top-tier asset managers.
- And in Security, with the capabilities of FusionX, which we acquired in 2015, we are helping a large international resort company safeguard millions of daily transactions – providing advanced services such as security audits across 15 properties, digital identity management and rigorous testing to prevent cyber-attacks.

We also continue to make significant investments in our unique Innovation Architecture, which integrates our capabilities across research, ventures, labs and studios to pioneer new ways of collaborating with clients to develop and deliver disruptive innovations.

As part of our innovation-led approach, we are opening new facilities around the world, including several in just the last few months.

In Dublin, we opened The Dock, our new multi-disciplinary innovation, R&D and incubation hub, where all elements of our Innovation Architecture come to life. The Dock is a launch pad for our more than 200 researchers to innovate with clients and ecosystem partners, with a particular focus on artificial intelligence.

In Hong Kong, we launched an Accenture Interactive Studio, where we are bringing together end-to-end digital customer experience services for clients.

In London and Singapore, we opened new Accenture Liquid Studios designed to help clients apply rapid development techniques like Agile methodologies and DevOps to quickly turn concepts into products.

And, finally, in the United States, we are accelerating our innovation investment including ten new innovation hubs. We just opened our first one in Houston, enabling us to collaborate more closely with clients to co-create and scale innovative solutions.

Turning to the geographic dimension of our business, I'm going to comment on our results for both the quarter and the first half of the year.

In North America, we grew revenues in local currency 4% for the quarter and 5% year to date, driven by the United States where we continue to grow ahead of the market. And, given our strong market position and pipeline, we expect to see stronger growth in North America in the second half of the fiscal year.

In Europe, we continue to grow significantly ahead of the market, with 7% revenue growth in local currency for both the quarter and the first half, driven primarily by double-digit growth in the United Kingdom, Germany and Switzerland. We are confident Europe will keep up the strong pace in the second half.

And in Growth Markets, we were very pleased with our 9% growth in local currency for the quarter and 10% year to date, led once again by very strong double-digit growth in Japan as well as strong growth in China and Australia. We expect Growth Markets to accelerate its growth in the second half.

Before I turn it back to David, I want to share a few thoughts on our talent strategy to lead in the New. The large-scale transformation of our business is requiring a very significant investment in our people to ensure they have the most relevant skills to serve our clients both today and in the future. We are proactively training and up-skilling thousands of people in key areas such as cloud, artificial intelligence and robotics. In new IT alone, which is all about new architectures, intelligent platforms and automation, we have already trained more than 70,000 people in just over a year.

Our approach to continuously investing in the skills and capabilities of our people helps us meet the needs of our clients and enhances our ability to attract the very best talent in our industry. And that is why I'm very proud that Accenture was recently named one of *Fortune's* Best Companies to Work For, for the ninth consecutive year.

So, with that, I will turn the call over to David to provide our updated business outlook. David.

David Rowland

Thank you, Pierre. Let me now turn to our business outlook.

For the third quarter of fiscal '17, we expect revenues to be in the range of \$8.65 billion to \$8.90 billion. This assumes the impact of FX will be a negative 2.5% compared to the third quarter of fiscal '16, and reflects an estimated 5% to 8% growth in local currency.

For the full fiscal year '17, based upon how the rates have been trending over the last few weeks, we continue to assume the impact of FX on our results in U.S. dollars will be negative 2% compared to fiscal '16. For the full fiscal '17, we now expect our net revenue to be in the range of 6% to 8% growth in local currency over fiscal '16.

Before I continue with our business outlook, as a reminder, in March 2016 we announced the termination of our U.S. pension plan. We expect to record a non-cash charge of approximately \$425 million upon final settlement in quarter three 2017. We will provide both GAAP and adjusted quarter three and year-to-date results.

For operating margin, on an adjusted basis, we continue to expect fiscal '17 to be 14.7% to 14.9%, a 10 to 30 basis-point expansion over fiscal '16 results.

We continue to expect our annual effective tax rate on an adjusted basis to be in the range of 22% to 24%.

For earnings per share, on an adjusted basis and reflecting our updated revenue range, we now expect full-year diluted EPS for fiscal '17 to be in the range of \$5.70 to \$5.87, or 7% to 10% growth over adjusted fiscal '16 results.

For the full fiscal '17, we continue to expect operating cash flow to be in the range of \$4.6 billion to \$4.9 billion, property and equipment additions to be approximately \$600 million, and free cash flow to be in the range of \$4 billion to \$4.3 billion.

We continue to expect to return at least \$4.2 billion through dividends and share repurchases, and also continue to expect to reduce the weighted average diluted shares outstanding by slightly more than 1% as we remain committed to returning a substantial portion of cash to our shareholders.

And, finally, for the full year, we now expect to invest in the range of \$1.5 billion in acquisitions.

With that, let's open it up so that we can take your questions. Angie.

QUESTIONS AND ANSWERS**Angie Park**

Thanks, David. I would ask that you each keep to one question and one follow up to allow as many participants as possible to ask a question. Shannon, would you provide instructions for those on the call?

Operator

Thank you. Ladies and gentlemen, we will now begin the question and answer session. If you would like to ask a question, please press star then one on your telephone keypad. You will hear a tone indicating that you have been placed in queue. You may remove yourself from queue at any time by

pressing the pound key. Once again, if you would like to ask a question, please press star then one at this time.

And our first question is from the line of Bryan Keane with Deutsche Bank. Please go ahead with your question.

David Rowland

Good morning, Bryan.

Bryan Keane

Hi, good morning, David. I just want to ask on bookings, it came in at \$9.2 billion. I know the Street was at \$10 billion, and \$9.2 billion I think is down 3% year over year, but it sounds like that was within the range of your expectations. So, just trying to gauge was bookings a little bit lighter than you expected or was the Street just too aggressive in their assumptions.

And then just secondly, on the potential for stronger growth in the second half '17, maybe you can just give us an idea of what that looks like between Consulting and Outsourcing, in particular, Consulting slowed a little bit this quarter but, maybe it sounds like it's going to pick up. Thanks so much.

David Rowland

Yes. First of all on the bookings, putting aside the consensus estimate, what I had signaled last quarter is that we felt confident that bookings would be stronger in the second quarter than the first quarter, beginning a pattern of building through the year which is typically what we've seen. So, we ended up with about \$1 billion more in bookings in the second quarter versus the first quarter; that's consistent with the comments that I made and it's in the range that we expected.

As you know, in any particular quarter, there are a few deals that can fall on either side of the line, so we will always have a range that we expect to land in and we're very solidly in the range that we expected. And, for the full year, we're very optimistic about our bookings. As I said, we began the third quarter, second half of the year with a healthy pipeline and we expect to see continued strong bookings in the third and fourth quarter supporting our revenue guidance.

In terms of the growth by type of work, which I think was the other part of your question, is that right? I guess he's dropped off the line. So, for the full year we expect Consulting type of work growth to be in the mid to high single-digits and we expect Outsourcing type of work growth to be in the mid to high single-digits as well.

If you look at it by business dimension, which I also comment on, we think Strategy and Consulting Services combined will be in the mid-single-digit range, so we do see an increase in the growth rate of our Strategy and Consulting Services combined in the second half of the year. We see Application Services in the mid-single-digit range. We see Operations in the double-digit range, and of course, the New will continue to grow very strong double-digit growth throughout this year.

Bryan Keane

Okay. Thanks so much.

David Rowland

Alright. Thank you, Bryan.

Operator

And the next question comes from the line of Jim Schneider with Goldman Sachs. Please go ahead.

Jim Schneider

Good morning, thanks for taking my question. I was wondering, maybe to follow up on the previous question, you delivered pretty good 6% growth this quarter and a little bit of last quarter, so I guess can you maybe talk about—you talked about acceleration in the back half of the year. So can you maybe talk about some of the factors that you're seeing that would lead you to not raise your revenue outlook for the full year given the commentary you just made about the back half?

David Rowland

Yes. So, let me give a few comments and Pierre will perhaps want to make some comments, as well, from his perspective. Let me just start.

When we provided full year guidance of five to eight percent, we really entered the year with one possible scenario where the growth in the first half of the year would be, relatively speaking, lower than the second half of the year, and that scenario, in fact, is continuing to play out. As we always say, we started the year, although we had a range of five to eight, as we say, working hard each and every day to be at the upper end of the range, and that is still our focus.

In terms of what's underneath that, there are a couple of ways I could help you understand the way we look at the first half versus the second half of the year. But, one way is through the lens of what I have called out as these three concentrated areas of pressure which make up 15% to 18% of our revenue overall. When you look at those three areas, Energy, Chemicals & Natural Resources, and Communications & Media, two of those three areas, we see, and we believe we will see positive growth in the second half of the year relative to where they were in the first half of the year, and we have some confidence in that.

Beyond that, when you look at the rest of our business, which is growing 10% on a year-to-date basis, even within that, we see certain areas of our business that did have positive growth in the first half of the year but we expect will have even more positive growth in the second half of the year. An industry that comes to mind is Health, for example, which has been lower in North America, but we expect will be stronger in the second half of the year, more in kind of the typical growth rates that we expect for Health.

So, overall, the year is really playing out as we expected. We continue to work hard to try to land in the upper end of our range as we always do, supporting our confidence level in the second half of the year, we've narrowed the range to six to eight.

Pierre Nanterme

Yes, no, it's hard to build on this, you said it very well. To put it very simply, we feel very good for the second half of the year. That's it, based on facts. We have very good bookings. We have good pipeline. We have great momentum in most parts of our business.

Just to give you a clue, we're covering 13 industries, groupings, if you will, 13 industries. Of these 13 industries, 10 are positive, and of the 10, 6 are high-single or — when I say high-single, one is at 9.5, that's 10 for simplicity — 6 would be double-digit. So, you could only be positive when you see such a momentum.

Indeed, we have three very specific situations, and frankly, these three situations, at least two are linked to some client situation where indeed the business has been slowing down for absolutely good and valid reasons, and we have evidence that these two industries in Resources, CNR and Energy, will be back in the second half of the year. So, I am extremely positive for the second part of the year.

David Rowland

Okay, Jim, thanks.

Operator

The next question is from the line of Tien-tsin Huang with JP Morgan. Please go ahead with your question.

David Rowland

Hi, good morning, Tien-tsin, how are you?

Tien-tsin Huang

I'm good. Thanks for taking the call.

David Rowland

Somebody told me you're in Hawaii this morning, so I guess it's early for you.

Tien-tsin Huang

Yes, 2:30, not too bad, sitting outside.

Pierre Nanterme

I appreciate your commitment.

David Rowland

Pierre said he appreciates the commitment. You may not have heard that.

Tien-tsin Huang

Well, not too bad, sitting outside, the wind feels good. Well, Virginia lost, so it's a good way to take my mind off of things, focus on Accenture. I'll ask about, I guess you just talked about the three areas of pressure. Some of them are linked to some client situations. I'm curious, have you been able to replenish your pipeline, or are you seeing just comps improve? Are you actually selling into those existing clients? I'm just trying to understand how you're able to remix out of the troubled areas and see improvement there if that makes sense.

David Rowland

Yes, I would say it's a combination of the two. I mean just to be blunt, it is a combination of the two. There is a benefit from the comps getting easier and that's just the math, but more importantly, there are really underlying fundamental improvements that we see in the business activity, the dialogue that we're having with our clients, the investment in digitization in addition to the kind of the cost rationalization focus that those industries have had for so many quarters now. And so the comps are part of it, but there is some fundamental improvement in the business, a lot of green shoots that we see that I think have us much more optimistic about the trajectory.

Pierre Nanterme

And, I would add, if you look at Resources, which has been one of the areas we watch carefully, again, that's too tough, because you're not mentioning Utilities. Our Utilities business is continue growing double-digit. So, this one is on reasonably good fire, and we're doing very well because this is an industry rotating rapidly to the New.

And, you have a direct correlation in the business with the rotation to the New from our clients and the performance of these industries. This is as simple as this. Energy is back. And I think when I look at the three, Energy, and then you have CNR, Chemicals & Natural Resources, CNR being the smallest of the three, to be clear, and so Energy is very important moving forward. And we are getting more and more

evidence that Energy will perform much better in the second part of the year.

David Rowland

Yes.

Tien-tsin Huang

I see, okay, I'd just like to follow up just on the M&A contribution in the quarter and for the year. It sounds like you upped the spend target to \$1.5 billion.

David Rowland

Yes, for the full year, we continue to expect to be in the range of 2%, but if you peel it back, H1 is let's say closer to 1.5%, and H2 would be closer to 2.5%, and so in the second half of the year, we will see an additional contribution in inorganic relative to H1, but for the full year, it'll still be in the 2% range. The additional spend up to \$1.5 billion, Tien-tsin, a lot of that will happen in the fourth quarter, and the revenue impact of those transactions is much more relevant to FY '18 than it would be FY '17.

Tien-tsin Huang

Got it, got it, thank you so much.

David Rowland

Okay, thank you.

Operator

And the next question is from the line of David Grossman with Stifel Financial. Please go ahead with your question.

David Rowland

Good morning, David.

David Grossman

Hi, good morning. So, I know there's been already several questions about growth, but if you look back, Consulting growth over the last four years has been pretty lumpy, right; '13, '14 relatively weak; '15 and '16 relatively strong, and this year is falling somewhere in between. I know we've had some fairly significant technology cycles as well as periods that outlined some pretty significant industry cycles impacting growth for the entire industry. But, can you help us think through what the growth in the Consulting business should really look like on a normalized basis, if there really is such a thing, recognizing that you have a portfolio, and there's always going to be pluses and minuses each year?

David Rowland

Yes, I would say on a normalized basis, Consulting and Strategy services combined would be in the mid-single-digit kind of range to let's say high single-digit depending on the cycle that we're in. So, it's going to be a mid- to high single-digit contributor across our portfolio of businesses. I mean, the Consulting growth, to be clear, as well, is connected to this dynamic that we've talked about with our overall growth, meaning that if you look at these three industries that are contracting, primarily because of these cyclical pressures, that has had an impact in recent quarters in particular on our Consulting and Strategy growth rate. And we think that that drag, if you will, that we've seen, let's say, the last few quarters will start to mitigate some in the second half of the year. We're also making investments in our Consulting business, which start to help drive our growth rate in the second half of the year and beyond as well.

Pierre Nanterme

The line, the direction should be mid- to high single-digit. We believe this is where the Consulting business

should be. Sometimes they're going to be higher than this because you have a combination of good factors, and sometimes you're just a bit behind, and here we have this combination of these three situations creating a disproportionate drag on our Consulting. So, as we mentioned before, definitely two of the three will get back, and so the Consulting that's associated, will get back as well.

On the other side of the spectrum, we are not only investing in what we're calling the New – digital, cloud and security – but we, as you know, are putting some investments in building extraordinarily deep skills in areas where we believe there could be higher growth, in a very specific way. You've seen the acquisition of Kurt Salmon, a premium brand in retail North America. We are doing the same in aviation, in very deep skills. In investment management, where we believe it's going to be a great market, and we are making acquisitions there on a very targeted basis. So, I'm extremely confident that the Consulting will be back.

David Grossman

Right, and if I could just ask a quick follow-up to your comment about reskilling. Obviously the pace and breadth of the current cycle has driven the need to reskill at a faster than normal pace. So, that aside, is it fair to expect, after this year, that the pace of acquisitions would continue to contribute this 2% rate of growth, or would you expect that to come back a little bit as the cycle matures?

Pierre Nanterme

Yes, I mean, we're putting very significant attention on the skills of our people. I mean we just broke the 400,000 mark in terms of people, and we want to have 400,000 talented people. And, by talented people, I mean having the right skills, is what we mean by talented people, the right skills for today, and more important, the right skills for tomorrow.

So, what we did, and not starting now, but starting years ago, is to make sure that in training and education, we are investing significantly. I think the number is public. We're roughly investing \$900 million in training and education to make sure that we have the best skilled people and are able as well to attract the best talent.

So, we're combining our organic reskilling, if you will, \$900 million. We have digitalized all our training to make sure that our cost of training is extremely efficient, and I was just impressed frankly to recognize my friend Bhaskar Ghosh on what he has been doing with our Accenture Technology business in reskilling last year, in what we're calling new IT, 70,000 people. He's managing roughly 200,000 people, Bhaskar.

The goal for us is to reskill 100% of these people over 3 years, 70, plus 70, plus 70,000. In addition, we are recruiting in the, through acquisitions, very deep skills, very deep skills. We believe it's going to take too long to grow organic. And so, we have a good, I think, a two-prong strategy, if you will, investing in our people to make them relevant, and I think this is something we owe to our people.

We have a responsibility. I feel that way. I have the responsibility to make them relevant for the future, and then complement with top-notch, iconic talent we're getting from the market. So, we have a kind of perfect blend.

David Grossman

Very good, thank you.

David Rowland

All right, thank you, David.

Operator

The next question is from the line of Edward Caso with Wells Fargo. Please proceed with your question.

David Rowland

Hi, Ed.

Edward Caso

Good morning. I'm only on the East Coast, so not too bad off here.

David Rowland

Well, we appreciate your commitment as well.

Edward Caso

Thank you. My question is really around robotics and artificial intelligence from two dimensions. How much are you applying that to your own business to maybe de-link a little bit revenue from people growth? And, how much are you helping your clients, and at what pace is it coming on? Thanks.

Pierre Nanterme

Yes, thanks for the question, and the answer to your question number one, is extensively and the answer to your question number two is extensively. I mean what we are, especially in Accenture Technology and in Accenture Operations, and of course, in Accenture Digital, we have now infused in Accenture Technology all new capabilities called, for us, intelligent platforms.

The name we're using, the public name is myWizard. myWizard is the first in that category of intelligent platforms, so you can develop code using more and more intelligent virtual agents. So, we're doing that massively, but it's not enough.

We're indeed applying to Accenture Technology in our technology delivery centers, and more important, to Accenture Operations in our BPO centers, RPAs, I mean Robotic Process Automations, that we are executing for Accenture. And it's interesting to see that many clients are visiting us and considering Accenture as now the benchmark, and they're learning from what we do to apply themselves.

So, extensively in Accenture, because the name of the game is not labor, it's productivity. And, that's always been the name of the game in Accenture. So, we want to operate at maximum productivity and efficiency with talented people. That's what we have in mind.

And, as you said, starting to see in some parts of our BPO business the de-correlation between revenue and labor, and we believe strongly that the combination of artificial intelligence, machine learning, robotic process automation in the coming five years will make a significant difference in this correlation between labor to revenue.

From the client standpoint, huge demand. Yes, I've just been pitching RPA, and closing RPA deals, last week, just to give you a view. So it's extremely vibrant. Why? Because you know the clients' agenda is still the same, as we said in one of our IA Days, digitalization and rationalization. Digitalization to create new business models, and all the architecture we have been putting in place in the New is resonating with that, with Accenture Interactive, mobility, analytics, cloud, and security, and rationalization, RPA is at the heart of rationalization, robotics, and automation and the demand is just growing and we are very well positioned.

Edward Caso

My other question is on the benefit side of your pension charge, what kind of, in basis points, contribution

to operating margin will that drive in fiscal '18? Thanks.

David Rowland

It's not material. In the scheme of Accenture, the benefits that we're deriving from doing this are not that material in terms of the bottom line.

Edward Caso

Thank you.

David Rowland

Thank you.

Operator

The next question is from the line of David Ridley-Lane with Bank of America. Please proceed with your question.

David Rowland

Hello, David.

David Ridley-Lane

Sure, thank you. Good morning. I did want to—maybe touching on that last question, I know you do not manage to a gross margin, but the year-to-date gross margin expansion is notable given the longer-term trend. Are you seeing the benefit of automation show up there or is this driven more from the revenue mix shift towards digital? Just trying to get a sense of is this theme of automation and robotic process automation helping on the gross margin today.

David Rowland

Yes, it is. By the way, let me say that even though gross margin has looked good the last two quarters, our message has still stayed the same. For many reasons we've explained, we really focus more on operating margin.

Having said that, to your question, the big driver I think when you look at the first two quarters has been improvement in our contract profitability, so our cost to serve clients is one of the major components in our gross margin. And we have seen improvements in contract profitability which reflects broadly some of the improvements we've seen in pricing.

It reflects—there's some mix shift as we, let's say we have a higher percentage of higher value kind of added services, even higher percentage of those, that type of work, which includes digital but not limited to digital in the mix, etc. And, as well, just the overall efficiency of our payroll structure, which is of course the biggest driver of our cost overall. And so, it's more about contract profitability and managing our payroll efficiency at a high level of efficiency.

Is automation in the mix of our improved contract profitability? It is, but in no way would that be a dominant driver. It's in the mix but with many other things as well.

David Ridley-Lane

And just as a quick one, do you see any drag from regulatory uncertainty among your U.S. health insurance clients? Or, maybe said differently, since you expect an acceleration there, what would be the main drivers to get you there?

David Rowland

We did see an impact in the pace of decision-making. When you look back now in the rearview mirror, we did see an impact in the pace of decision-making in Health in North America during the first half of the year. We believe, and we have fact points and tangible evidence that we would point to that that slower pace of decision-making is behind us, and that as we've now turned into the new calendar year, every month that goes by, we're a month into the new administration, then the decision-making is resumed at normal levels. And that's part of the reason why we are positive on improved growth rates in the second half of the year.

So, we did see an impact in the first half of the year. We believe that that's largely behind us. Okay? Thank you, David.

Operator

And the next question is from the line of Brian Essex with Morgan Stanley. Please go ahead with your question.

Brian Essex

Hi, good morning, and thank you for taking the question. I was wondering if you could maybe dig in a little bit to banking, financial services. You called out North America and capital markets mix improving. Maybe, can you provide a little bit of color behind the improvement in that business and what the primary drivers of that improvement might be?

Pierre Nanterme

Yes, overall Financial Services is doing very well, and we have been posting, I think, 8% growth in the—

David Rowland

Yes, Banking & Capital Markets is double-digit.

Pierre Nanterme

Double-digit, yes, so we're doing very well. In North America, more especially, we're starting to see again more demand in the New, and we are working on having a more diversified portfolio of clients and not only the kind of big category leaders, if you will, due to a most significant regionalization of our business in the United States where we expect great benefits starting in H2.

And, in addition, as I mentioned especially in investment management, which is part of Capital Markets, we've made a few acquisitions, you've seen Beacon, and they are providing as well deep skills. So again, as in everything, it's a combination of two or three factors you're putting together to create growth, and we see some more optimism as well from clients linked to the expected deregulation of some part of their business. So, all of this put together is creating an environment which is getting better.

Brian Essex

Great, that's very helpful. Maybe as a follow up, could I ask about Accenture Interactive? I've seen some kind of interesting news in the press recently there. How big is that business, and is that primarily CMT-focused, or how do you plan to weave that in with your digital aspirations?

Pierre Nanterme

Yes, I'm extremely pleased with Accenture Interactive. You've given me the opportunity to recognize the leader of Accenture Interactive, Brian Whipple, who is just doing a great job in leading that part of the business. In less than seven years or something like this, we created the largest pure player in digital marketing, so the digital agency of Accenture is now one of the largest and a category leader.

We are leading in digital design, especially after the acquisition of a company named Fjord and many other acquisitions, the last one Karmarama in the UK, which is a premium independent, the best independent company in the UK. Digital production, you remember the acquisition of avVenta some years ago. Digital commerce, which of course is very important on the back of the acquisition of Acquity we made in the U.S. some years ago, and all what we're doing in terms of customer analytics. So we were very pleased that last year, *Advertising Age* ranked Accenture Interactive number one, and for us it's a very critical milestone. We see more and more clients indeed turning from the so-called holding companies to Accenture Interactive, and now I'm very pleased to report that we [will be] very close to \$6 billion [this fiscal year] [corrected] in Accenture Interactive, making us a category leader. So we couldn't be more pleased with Accenture Interactive because—sorry to elaborate a bit, I know we're running out of time. Again I'm passionate about this, so I'm sharing my passion with you.

The business in the future will be more and more driven by experience and design of new capabilities, of new products, of new ways of engaging with customer, consumer, patient, and employees. So, for us it was absolutely critical to put on the top of our services the experience, this design-led, experience-led, kind of capability. And just to give you a data point, I think when we acquired Fjord they had 150 people roughly, 150, 180, something like this, less than 200. Now, we're going to crack the 800 people in Fjord, making certainly Fjord one of the largest pure players in digital creative design. So, that's what we do, and we're pleased.

Brian Essex

Okay, so quite a bit larger than we last heard, so it's great to hear, very helpful, thank you.

Pierre Nanterme

In our rotation to the New, sorry to be maybe too long, but in our rotation to the New, in interactive, mobility, analytics, cloud and security, we want not only to be the number one if you add up all these things, which is where we are with our \$8 billion in H1 only, but we want to be number one in each of the five. That's what we mean by scaling to lead, and this is what we are doing relentlessly.

Angie Park

Shannon, we have time for one more question, and then, Pierre will wrap up the call.

Operator

Thank you, and our final question comes from the line of Joe Foresi with Cantor Fitzgerald. Please go ahead with your question.

Joe Foresi

Hello, so I guess what inning do you think digital might be in, and what's the next phase of the digital movement?

David Rowland

I mean I would say the digital wave is still, in your baseball analogy, I would say it's still in the early innings. If you talked about it in terms of the maturity curve, it is low on the maturity curve. There is a ways to go.

Pierre Nanterme

Yes, early days. If you look at this, and of course, some capabilities are more mature than the others, and when we're putting that into our Accenture framework, we said we have three waves. The digital consumer, and this wave is maturing quite a lot, because you see this is probably where we're doing the majority of our Accenture Interactive business of around \$6 billion [this fiscal year] [corrected].

Then, you have the digital enterprise, how you digitalize all the parts of the enterprise, and here the robotics and the automation we're bringing a lot, so I think this is coming.

And then you have what we are calling digital operations and IoT, and this is nascent to be honest. And this might be certainly the biggest wave of the three, and so we are positioning Accenture already in what we're calling industry X dot zero. We are probably 4.0 as we speak, but there are going to be five, six dot zero, and we're positioning a lot Accenture on mobility, connected platform, Internet of Things.

We have already developed many partnerships in the ecosystem with OEM providers to expand our reach to this industrial Internet. We have labs. I'm thinking about what we have in Bangalore, what we have in Beijing, where we are developing very deep industry solutions in the context of the IoT. So, it's early days. It's going to be underway for probably a couple of decades.

Joe Foresi

Okay, and then just as a quick follow up, how is competition in outsourcing, particularly pricing? Thanks.

David Rowland

I would say really no notable change in the competitive landscape in Outsourcing. If you're maybe asking specifically about the application maintenance piece of our Application Services, that continues to be a very, very competitive pricing environment, so that's more of the same. And I would say if you look at BPO as another big piece of Outsourcing, I would say no notable change.

Pierre Nanterme

So, no notable change, but some at Accenture, again, because if there's something we hate in our company, it's commoditization of services. So we're fighting against commoditization, always to move and to rotate to higher-value services.

The business you mentioned is subject to commoditization at great pace. Our answer to fight against commoditization has been to infuse, as I mentioned before, through Bhaskar Ghosh and Debbie Polishook leading Accenture Technology and Accenture Operations, a lot of robotics, a lot of automation, less labor arbitrage, more technology, more intelligence. And so indeed, we want to make these activities more tech automated-led, less labor-intensive like many of our competitors have been doing, and we are following a very different trajectory.

Joe Foresi

Thanks.

CONCLUSION

Pierre Nanterme

Okay, it's time to wrap up. Thanks a lot to have been so patient with us. Thanks again for joining us on the call today.

As you can tell, and have heard from David and I, we are very confident in our ability to deliver another strong year in fiscal year '17, to continue gaining significant market share as we do, to even further accelerate our rotation to new and innovative services, and at the same time as we are investing significantly for the future, continuing delivering value for our clients, our people, and our shareholders at the same time we transform Accenture to be even more successful.

We look forward to talking with you again next quarter. In the meantime, if you have any questions, feel free to call Angie and her team. All the best, and talk to you very soon.

Operator

Ladies and gentlemen, this conference will be available for playback beginning today at 10:30 a.m. Eastern time running through Thursday, June 22, 2017 at midnight Eastern. You may access the AT&T playback service by dialing 1-800-475-6701 and entering the access code of 418844. International participants, please dial 320-365-3844 with the access code of 418844.

That does conclude our conference for today. Thank you for your participation and for using AT&T. You may now disconnect.