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ACN – ACCENTURE'S Q4 FISCAL 2014 EARNINGS
CONFERENCE CALL

SEPTEMBER 24, 2014 / 8:00 A.M. EDT



Accenture's Q4 FY '14 Earnings Conference Call

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CONFERENCE CALL PARTICIPANTS

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David Grossman *Stifel Nicolaus - Analyst*

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PRESENTATION

Operator

Ladies and gentlemen, we'd like to thank you for standing by and welcome to the Accenture fourth quarter FY14 earnings call.

(Operator Instructions)

And as a reminder, today's conference call will be recorded. I would now like to turn the conference over to your host and senior facilitator, Managing Director, Head of Investor Relations, KC McClure. Please go ahead.

KC McClure - Accenture - Managing Director, Head of IR

Thank you, Steve, and thanks, everyone, for joining us today on our fourth quarter and full year FY14 earnings announcement. As Steve just mentioned, I'm KC McClure, 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, along with some key operational metrics for both the fourth quarter and the full fiscal year.

Pierre will then provide a brief update on our market positioning, before David provides our business outlook for the first quarter and full FY15. We will 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 in this 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 in this call.

During our call today, we will reference certain non-GAAP financial measures which we believe provide useful information for investors. As a reminder, our results last year included benefits from final determinations of prior-year US federal tax liabilities and a reduction in reorganization liabilities.

We include reconciliations of non-GAAP financial measures, where appropriate, to GAAP in our news release or in the Investor Relations sections of our website, at Accenture.com. As always, Accenture assumes no obligation to update the information presented on this conference call.



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Now, let me turn the call over to Pierre.

Pierre Nanterme - Accenture - Chairman & CEO

Thank you, KC, and thanks, everyone, for joining us today. We are very pleased with our results for both the fourth quarter and the full fiscal year.

Starting with the quarter, our strong revenue growth of 8% was broad-based across the different dimensions of our business and, coming on top of our strong growth in Q3, enabled us to deliver an excellent second half of the year. For the full year, we increased market share, generated record revenues and new bookings, grew EPS faster than revenues, and generated strong cash flow, all while continuing to invest to further differentiate our business and delivering significant value for our clients and shareholders.

David will provide more detail in a moment, but here are a few highlights for the year:

- We delivered record new bookings of \$35.9 billion.
- We grew revenues 5% for the year.
- We delivered earnings per share of \$4.52, a 7% increase.
- We expanded operating margin 10 basis points, to 14.3%.
- We generated free cash flow of \$3.2 billion, and we continue to have a very strong balance sheet, ending the year with a cash balance of \$4.9 billion.
- We returned \$3.8 billion in cash to shareholders through share repurchases and dividends.
- And we just announced our semi-annual cash dividend of \$1.02 per share, which is a 10% increase over our prior dividend.

Our performance in FY14 clearly demonstrates that we are executing very well against our strategy, and given our strong growth in the second half of the year, I am pleased with the momentum in our business as we enter the new fiscal year. Now let me hand over to David. David, over to you.

David Rowland - Accenture - CFO

Thank you, Pierre, and thanks to all of you for joining us on today's call. Let me start by saying that we were very pleased with our overall results in quarter four, as they continue to reflect positive momentum in many areas of our business and clearly illustrate the relevance of our growth strategy and the yield we're getting from important investments we've made over the past two years.

Before I get into the details, I'd like to highlight three aspects of our quarter four results which are particularly noteworthy.

- First, the most distinguishing aspect of our results was clearly the strong top-line growth of 8%, exceeding our expectations and landing above the top end of our guided range for the quarter. Our revenue growth is underpinned by continued improved growth rates in many areas of our business, building further on the improvements we delivered in quarter three. And overall net revenue growth was at the highest levels we've seen since quarter four of FY12.
- Second, our profitability in quarter four came in as expected, yielding 10 basis points of expansion for the full year. It's noteworthy that we achieved this result while taking actions to continue to align our headcount and labor cost in certain parts of our business. We're pleased with the progress we're making to better position our profitability going forward.
- Third, we generated strong cash flow of \$1.5 billion in the quarter, putting us at the upper end of our previously guided annual range. And of course, we continued to return significant cash to shareholders while at the same time investing in our business. So we were very pleased with the quarter and, in fact, more broadly, with our strong performance in the second half of the year.



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With that said, let's now turn to some of the details, starting with new bookings. New bookings for the quarter were \$8.3 billion, resulting in \$35.9 billion in new bookings for the full fiscal year, which was at the very top of the business outlook range provided in June and represents an all-time high in annual new bookings. Consulting bookings were \$3.9 billion, with a book-to-bill of 1.0. Outsourcing bookings were \$4.4 billion, with a book-to-bill of 1.2.

Taking a closer look at our new bookings, there are several additional points worth noting. For the fourth consecutive quarter, Consulting bookings landed within our target book-to-bill range and reflected good demand for Systems Integration and Management Consulting. For the year, Consulting bookings of \$17.1 billion were the highest ever, with Management Consulting and Systems Integration both achieving a strong 1.1 book-to-bill, and Technology Consulting also delivering a solid year at 1.0.

We continue to be pleased with another quarter of solid Outsourcing bookings. Results in Technology Outsourcing reflected an uptick compared to quarter three and BPO bookings continued to reflect healthy demand.

Also, there were a number of record highs with our new bookings results in FY14 in both Consulting and Outsourcing, particularly in BPO, which had a 1.7 book-to-bill. CMT, Financial Services and H&PS set record highs, as well. And finally, we continued our track record of winning large, transformational projects with 9 clients with bookings in excess of \$100 million, bringing the total for the year to 39.

Turning now to revenues. Net revenues for the quarter were \$7.8 billion, an increase of 10% in US dollars and 8% in local currency, reflecting a positive 1.5% FX impact, consistent with the assumption provided in June. Consulting revenues for the quarter were \$4 billion, up 6% in USD and 4% in local currency. Outsourcing revenues were \$3.8 billion, up 15% in USD and 13% in local currency.

Looking broadly at the major drivers of growth in the quarter, Outsourcing was a highlight, coming in even stronger than we expected, driven by strength in both BPO and Technology Outsourcing. In addition, we continue to be pleased with the strong contribution of our digital-related services to our overall growth.

Turning to the operating groups. The momentum in Communications, Media & Technology continued with 12% growth, the highest in 10 quarters. Broad-based growth was driven by three notable areas, E&HT, Outsourcing and the Americas.

In Products, the 12% growth was broad-based across all industries and in both Consulting and Outsourcing. H&PS grew 9% in the quarter, coming from both Public Service and more notably, Health, where we continued to deliver double-digit growth in Consulting and Outsourcing.

Financial Services grew 8%, up from last quarter, led by very strong growth in Outsourcing and within our Banking and Capital Markets industries. Resources was flat in quarter four; and while we still have some work to do, we were encouraged by progress in several areas. We had growth in three of the four industries, while Natural Resources continues to be challenged globally.

Moving down the income statement. Gross margin for the quarter was 31.7%, compared with 33.2% for the same period last year, down 150 basis points. Sales and Marketing expense for the quarter was 11.8% of net revenue, compared with 12.6% of net revenues for the fourth quarter last year, down 80 basis points.

G&A expense was 6.1% of net revenues, compared with 6.7% of net revenues for the fourth quarter last year, down 60 basis points. Operating income was \$1.1 billion in the fourth quarter, reflecting a 13.9% operating margin, equal to the operating margin for the same period last year.

Our effective tax rate for the quarter was 30.1%, compared with 24.6% for the fourth quarter last year. The higher rate in the fourth quarter was primarily due to lower benefits related to final determinations of prior-year liabilities and a higher level of reserve additions.

Net income was \$760 million for the fourth quarter, compared with \$727 million for the same quarter last year. Diluted earnings per share were \$1.08, compared with EPS of \$1.01 in the fourth quarter last year. This reflects a 7% year-over-year increase and includes a negative impact of \$0.09 from a higher tax rate this quarter.

Turning to DSOs, our days services outstanding continue to be industry-leading. They were 36 days, up from 35 days last quarter. Free cash flow for the quarter was \$1.5 billion, resulting from cash generated by operating activities of \$1.6 billion, net of property and equipment additions of \$101 million.

Moving to our level of cash, our cash balance at August 31 was \$4.9 billion, compared with \$5.6 billion at August 31 last year. The current level reflects the cash returned to shareholders through repurchases and dividends, as well as the acquisitions we made in FY14.

Moving to some other key operational metrics, we hired approximately 80,000 people in FY14, ending the year with a global headcount of more than 305,000; and we now have over 205,000 people in our Global Delivery Network. In quarter four, our utilization was 88%, consistent with last quarter. Attrition, which excludes involuntary terminations, was 15%, up from both quarter three and the same period last year.



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Now, turning to our ongoing objective to return cash to shareholders. In the fourth quarter, we repurchased or redeemed approximately 8.2 million shares for \$658 million, at an average price of \$80.36 per share. For the full year, we repurchased or redeemed 32.6 million shares for \$2.6 billion, at an average price of \$78.52 per share.

Finally, as Pierre mentioned, our Board of Directors declared a semi-annual cash dividend of \$1.02 per share. This dividend will be paid on November 17 and represents a \$0.09 per share, or 10%, increase over the previous semi-annual dividend we declared in March.

So, before I turn things back over to Pierre, let me just briefly reflect on where we landed for the full year across the key elements of our business outlook. Again, new bookings were \$35.9 billion, at the top end of our guided range. Net revenues grew 5% in local currency for the full year, at the top end of our most recent guided range and in the upper end of the range provided at the beginning of the year.

As a reminder, in FY13 we had two unusual items that impacted certain metrics. The following year-over-year comparisons exclude those impacts and use FY13 adjusted results.

Operating margin was 14.3%, within the guided range we provided at the beginning of the year and spot on the guidance we provided most recently. EPS was \$4.52, at the mid-point of our most recent guided range and at the upper end of the range provided at the beginning of the year, and reflects 7% growth over FY13, consistent with our objective of growing EPS faster than revenue.

Free cash flow was a rounded \$3.2 billion, at the upper end of our previously guided range and at the low end of the range provided at the beginning of the year. And then finally, we returned approximately \$3.8 billion of cash to shareholders, more than \$100 million above our initial objective, through \$2.6 billion in repurchases and \$1.3 billion in dividend payments. In addition, we reduced our weighted average diluted shares outstanding by about 3%.

So, reflecting on the business outlook we provided at the beginning of the year, we successfully managed our business and delivered on each metric, with several of the metrics landing in the upper end of the range. We're pleased with the overall improvement we saw in our results in the second half of the year, especially the acceleration in growth we signaled one year ago.

Now let me turn it back over to Pierre.

Pierre Nanterme - Accenture - Chairman & CEO

Thank you, David. Our performance for the fiscal year, especially our strong revenue growth in the fourth quarter and the second half of the year, demonstrates that we are executing the right growth strategy. We are providing relevant and highly differentiated services that are clearly resonating with the needs of our clients. And we are gaining market share in an environment that continues to be very demanding and highly competitive.

In FY14, we made significant investments in our business, including \$740 million in acquisitions, and we aligned our organization to be even more relevant, differentiated and competitive in the marketplace.

- We created Accenture Strategy, a unique capability and the first in the market to bring together business strategy and technology strategy, equally and at scale.
- We created Accenture Digital by combining our market-leading capabilities in Accenture Interactive, Accenture Analytics and Accenture Mobility. We now have more than 28,000 professionals working in Accenture Digital, making it the world's largest end-to-end digital capability.
- We formed Accenture Operations by bringing together our market-leading business process capabilities with our infrastructure and cloud services to offer our clients an even more compelling value proposition, running key operations "as a service" and at scale.
- In Accenture Technology, we further enhanced our Global Delivery Network, recruiting significant talent and investing to build intelligent tools to increase efficiency and productivity. We continue to harness innovation through our Technology Labs and to play a leading role in the technology ecosystem.
- And we infused even more talent into our five operating groups, which together serve clients in more than 40 industries, further strengthening our management and technology consulting capabilities. Our people in the operating groups orchestrate and bring together the very best of Accenture across the entire organization to serve our clients, helping us to continue to build long and enduring relationships with the world's leading companies.



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These investments have positioned us very well to capture new growth opportunities, as our clients and the industries in which they operate continue to be transformed and reinvented every day.

In this fast-changing environment, we see the market becoming more and more polarized around two major themes—digitization, to create competitive advantage and drive new sources of value, and rationalization, to create productivity and efficiency gains. At the same time, we continue to see demand for large-scale transformation programs, which has always been Accenture's sweet spot. Let me bring this to life with a few examples that demonstrate our unique position in the marketplace and the value we deliver to our clients.

Today, all of our clients are facing the imperative to transform their businesses to compete in the digital world, and we are partnering with them on this journey.

A great example is our work with a global media and entertaining company, where we are leveraging the full range of Accenture's capabilities, especially mobility, supply chain and analytics, to fundamentally transform the customer experience by implementing a broad set of digital tools. The centerpiece of this technology is a wearable device that allows customers to access their hotel room and pay for goods and services wirelessly. Through our work, we are helping our clients engage millions of customers each year with a truly integrated and personalized experience.

At the same time, our clients are looking to drive more efficiency and to increase productivity in their operations. At a leading commodity trading and mining company, we are providing finance & accounting and procurement services to help improve business operations. We are leveraging our end-to-end sourcing, procurement and analytics capabilities, together with the full power of the Global Delivery Network, to deliver over \$500 million in bottom-line savings, while also providing flexibility for future growth. The acquisition we made last year of Procurian, combined with our own sourcing and procurement capabilities, makes Accenture the clear market leader in procurement BPO and has been instrumental in positioning us for many recent wins in the market.

Finally, our clients continue to focus on large-scale transformation programs. With our extensive industry expertise and broad global footprint, as well as our skills in strategy, digital, technology, and operations, we have built an end-to-end capability that is second to none. And as demonstrated by our strong new bookings for the year, including 39 quarterly bookings over \$100 million, Accenture remains the partner of choice for our clients.

A key example is our work in Texas, where we are leading the state's effort to build a more efficient and effective Medicaid program. We are leveraging our healthcare expertise, as well as our long track record of delivering claims processing systems, to support 3.6 million Texas Medicaid participants and 45,000 healthcare providers, while processing more than 12.5 million claims each month.

Turning to the geographic dimension of our business, we are very pleased with the strong revenue growth we are seeing in many of the largest countries in which we operate. Taken together, these countries represent a very significant part of Accenture business.

Let me start with the United States, our largest single market, where I'm particularly pleased with our 10% revenue growth for the fourth quarter and 8% revenue growth for the full year. I am even more pleased with our sustained performance in the US over the past four years, where we have consistently delivered high single-digit or double-digit revenue growth, clearly gaining market share in the largest economy in the world.

In Europe, despite an economic environment that continues to be difficult, we are performing very well in many of our largest countries, including France, Italy, Germany and the United Kingdom. And in Asia-Pacific, our growth in Japan has just been outstanding. Japan delivered very strong double-digit growth for both the fourth quarter and the full year.

So we ended FY14 strong, and we are clearly benefiting from the investments we have made to build and launch highly differentiated capabilities, both organically and through acquisitions, to recruit and develop new talent with highly specialized skills, including hiring approximately 80,000 people, and to further strengthen Accenture's marketplace positioning and our brand, which is among the top 50 brands in the world.

At the end of the day, the real measure of our success and relevance comes from our clients. And for me, increasing the number of Diamond clients, our largest client relationships, is key. I'm delighted that we added 28 new Diamond clients during the fiscal year, which brings us to a net total of 141 Diamond clients, an all-time high.

And of course, we continue to apply rigor and discipline in everything we do at Accenture, to increase our efficiency and enhance our competitiveness, so that we can continue to achieve our ultimate goal of delivering sustainable, profitable growth over the long term.

With that, I will turn the call over to David to provide our business outlook for FY15. David, over to you.



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David Rowland - Accenture - CFO

Thank you, Pierre. Let me now turn to our business outlook. For the first quarter of FY15, we expect revenues to be in the range of \$7.55 billion to \$7.8 billion. This assumes the impact of FX will be negative 2% compared to the first quarter of FY14.

For the full FY15, based upon how the rates have been trending over the last few weeks, we currently assume the impact of FX on our results in US dollars will be negative 2% compared to FY14. For the full FY15, we expect our net revenue to be in the range of 4% to 7% growth in local currency.

For the full FY15, we are targeting new bookings to be in the range of \$34 billion to \$36 billion. We expect bookings to be a little lighter in the first quarter and build throughout the year.

For operating margin, we expect FY15 to be 14.4% to 14.6%, a 10- to 30-basis-point expansion over FY14 results. We expect our annual effective tax rate to be in the range of 26% to 27%. For earnings per share, we expect full-year diluted EPS for FY15 to be in the range of \$4.74 to \$4.88, or 5% to 8% growth over FY14 results.

Now turning to cash flow. For the full FY15, we expect operating cash flow to be in the range of \$3.95 billion to \$4.25 billion, property and equipment additions to be approximately \$450 million, and free cash flow to be in the range of \$3.5 billion to \$3.8 billion. Finally, we expect to return at least \$3.8 billion through dividends and share repurchases, and also expect to reduce the weighted average diluted shares outstanding by approximately 2%, as we remain committed to returning a substantial portion of our cash to shareholders.

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

KC McClure - Accenture - Managing Director, Head of IR

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

QUESTION AND ANSWER

Operator

(Operator Instructions)

Question one will come from Bryan Keane, Deutsche Bank. Please go ahead.

Bryan Keane - Deutsche Bank - Analyst

Hello, guys. Good morning. Just want to ask about the acceleration in revenue growth. I think last quarter it was 7% in constant currency. This quarter, 8% constant currency in revenue growth. But you're guiding to 4% to 7%, which is a little bit of a modest down-tick from the 8%. Just want to get your thoughts on the outlook compared to where we've been here in the last two quarters.

David Rowland - Accenture - CFO

I think it's important to look at -- maybe just to step back -- by the way, hello, Bryan. Thanks for the question, by the way. I think it's important to maybe look at that in a broader context and reflect on where we've been and where we're going, let's say over a three-year period. So two years ago, in FY13, we had growth at about 4%. This year, the year we just completed, we had growth at 5%. And while the 4% to 7% reflects what we think is a full range of reasonable outcomes, as I've always said, clearly we're working hard to be as high in that range as we possibly can.

So if you take the upper half of the range, and assuming that the market conditions and our own efforts allow us to land in that space, then you start to see the progression of our building business momentum from 2013 to 2014 to 2015, if we can deliver in the upper end of that range, which is 5.5% to 7%. And while 4% to 7%



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is our range, it reflects what we think are possible outcomes, depending on what happens with market growth. Everything that we do every day is to drive profitable growth and to work to be as high in the range as we can. So you're right. But if we deliver, if we execute at the upper half of the range, then that is indicative of the momentum that I think you got from Pierre's comments and from my comments.

Bryan Keane - Deutsche Bank - Analyst

Okay. And just maybe a breakout between Consulting and Outsourcing in that outlook. And then just wanted to ask on the bookings. They're essentially kind of flattish. Just wanted -- flattish to slightly down, I think, on the guidance. Just want to get a sense of how you guys see the market going forward. Thanks so much and congrats.

David Rowland - Accenture - CFO

Thank you, Bryan. On the bookings, Bryan, we follow, this is the approach we've taken since we've been a public company, where we peg our bookings range to our revenue range at our book-to-bill target. And it's very simply that math.

And we're much more focused on year in and year out delivering against our book-to-bill objective in the year than we are on the year-over-year growth in new bookings. Because bookings can be lumpy, not only quarter to quarter, but they can be lumpy year to year. And as we pointed out, we just had an exceptional year in FY14, with roughly \$36 billion in bookings. And if we land in the \$34 billion to \$36 billion range, as we're guiding to, that would imply that we'll be within our book-to-bill targets. That supports our revenue ambition for the year. And that's a result which we would feel good about, based on the book-to-bill objective. So that's the logic there.

On the revenue growth by type of work, Outsourcing, we're thinking in our guidance in the high single-digit to low double-digit range. And in Consulting, probably relatively consistent with this year, could be a click lower but could also be a click higher. So in that kind of general range.

Operator

David Grossman, Stifel Financial.

David Grossman - Stifel Nicolaus - Analyst

Thank you. I wonder if we could just go back, David, to some of the commentary earlier in the year, or I guess even on the call, about the margin pressure resulting from the need to remix some of the labor content. And while we recognize that's clearly an ongoing process, can you help us better understand when you would expect to reach a more favorable balance, at least based on where you are right now?

David Rowland - Accenture - CFO

Yes. We, as you would expect, we took -- we began taking actions on that as we transitioned into the second half of the year, in both quarter three and quarter four. David, as you mentioned, it is an ongoing process, so we're always focused on tuning the supply side of the equation, but within the supply side, tuning the payroll efficiency in our P&L. As I referenced in my comments, we did have actions that were noteworthy, which is why I called them out in the fourth quarter, reflecting what we're doing on the supply side and payroll efficiency side in the fourth quarter. And that was accounted for, if you will, in the results that we delivered.

What I would say is that while this is an ongoing process, we have seen a number of important areas of improvement in our profitability as we progressed into the second half of the year. We have seen good progression in payroll efficiency, but yet have more work to do. We have seen very good progression in contract profitability, which has been sequentially better in quarter three as compared to quarter two, and then again in quarter four as compared to quarter three. We have seen improvements in our business operations cost. And so when you peel back the P&L and you look at the underpinning, if you will, of our operating expense structure against our revenues, we have had some good improvement in the second half of the year, which we will build from further as we move into FY15.



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David Grossman - Stifel Nicolaus - Analyst

Thank you for that. And then just on the cash flow, if my math is right, it looks like your FY15 guidance for free cash flow may actually exceed net income. And again, recognizing there are going to be several moving pieces in any given year, can you help us understand the various puts and takes this year, other than the lower bonus accrual last year?

David Rowland - Accenture - CFO

Yes. David, the free cash flow to net income metric is 1.1, within the range. It's 1.1, which puts us back in the same territory as where we have been in many years in the past. At a high level, when you really step back and look at our cash flow, there's a number of things that drive it. One is the efficiency of our cash operating expenses in the year. So our cash operating expense efficiency in relation to the revenue.

The second thing that would be a driver would be the year-over-year change in DSO. And I'll point out that while we're very pleased with our DSO, even with the day increase that we had in the fourth quarter, we have allowed, in our free cash flow guidance, the possibility of a continued uptick of a day to day-and-a-half, in that range. Certainly we'll work hard to try to make sure that doesn't happen, but we've allowed for that. So that's a factor. The other factor would be large cash outflows. You mentioned what we pay out in variable comp as one. But another big swing factor is tax cash payments. Tax cash payments are a significant cash outflow for a company of our size. And they can vary significantly year to year, and they will be higher next year than they were this year.

David Grossman - Stifel Nicolaus - Analyst

Thank you.

David Rowland - Accenture - CFO

Hopefully that helps.

David Grossman - Stifel Nicolaus - Analyst

No, it does. Thank you very much.

David Rowland - Accenture - CFO

All right. Thank you.

Operator

Darrin Peller, Barclays.

Darrin Peller - Barclays Capital - Analyst

Thanks. I just want to talk a little bit about the cash strategy and the capital structure strategy for a moment. Because you're in a year now where clearly you're showing some pretty good trends on the key revenue segments you have. Financials are going, as you guys said, very well. The healthcare segment's growing well again. And you've had some very good growth, constant currency in the quarter relative to the beginning of the year. When we look at that and we look at your underlying EPS growth, it's still less than 10%, just given really the dynamic of margin expansion being 10 to 30 basis points.

And what I'm trying to figure out here is your cash use. You said 2% is going to -- the share counts will come down by about 2%. Can you just give us your thoughts, maybe Pierre, on how the company thinks about EPS growth in the framework of the long-term strategy? What kind of target are you really looking at over the long haul? Because you definitely have more cash flow that could be put to work, especially if you think about using your balance sheet.



Pierre Nanterme - Accenture - Chairman & CEO

Let me start, and David will give more comments on this. Our capital allocation strategy and cash allocation strategy has always been very clear and very straightforward, as you know. The different buckets where we're using our cash would be internally to fund our capital expenditure. The second bucket will be around acquisitions. And what we've seen, these last three years, is we've been ramping up the acquisitions and we will continue to do so, as long as we could find the right opportunities. But this is our expectation, that we will continue to deploy capital to acquisitions.

We set, in our mental model, something around 15% of the operating free cash flow, if I'm right. And it might be anything between 15% to 20%. Because we believe, based on our results, that we have demonstrated we can make the right acquisitions in order to create new capabilities and boost organic growth on top of that. And then the rest, our strategy has always been to return a very significant portion of our cash to our shareholders through share repurchases and dividends. What you've seen from a dividend standpoint, very consistent to what we said, is a kind of, I would say, evolution in the way we are delivering our dividend, with some, what I would qualify, solid, even robust increase year-over-year. And then we continue on our share repurchase strategy to make sure -- and this is what we communicated in an IA Day a couple of years ago -- that we will continue to make sure there's not going to be any dilution between the shares we are issuing as well as the share repurchase. So we own that strategy very clearly and it's still the strategy we're planning to execute moving forward. But maybe, David, you can give more color.

David Rowland - Accenture - CFO

No. In fact, you summarized it very well. When you look at --

Pierre Nanterme - Accenture - Chairman & CEO

I'm applying to be the next CFO. (Laughter)

David Rowland - Accenture - CFO

I think that was a good interview, Pierre. In terms of the 2% which you referenced, that's in the range of really what we've done on average since we've been a public company. I think that -- I haven't looked at the calculated number lately, but I think it's probably like 3% -- and probably the average, that reflects what we did in the earlier years of being a public company. But 2% to 3% is the range that we've been in.

When you look at our EPS range this year, which is 5% to 8% growth in USD terms, this is a year where we do have two headwinds that you don't necessarily have in every year. One is the 2% FX drag and then the other is we do have a higher expected tax rate. And so you look at the 5% to 8% in the context of covering an FX drag and, in this particular year, a higher tax rate, and then you can start to extrapolate what you think is possible in years where we don't have those. And so that gives you maybe a way to think about our EPS.

Darrin Peller - Barclays Capital - Analyst

All right. That's very helpful. Just one quick follow-up. Through the year, margins were a little below what you expected. You're now calling, once again, for 10 to 30 basis points of margin expansion, in line with how you guys like to deliver. Can we say -- is it fair to say that the pricing pressure, the off-shoring questions that we had seen that may have affected that, has been steady or potentially abating now, it's getting better?

David Rowland - Accenture - CFO

I would say that the inflection point that we saw in the first half of the year is more stable, but yet the trend continues. I think what we saw in the first half of the year was an inflection point where there was a period of acceleration which, I pointed out at the time, is not unusual. We've had to manage through inflection points previously, and so that's what we're doing now.

On the pricing overall, and if I talk about pricing in the context of the margin quality on our bookings, our pricing, I will say now, has improved in the second half of the year. I was hesitant to say that in the third quarter, because we don't want to kind of jerk back and forth on pricing. We want to see a trend. But now that I've seen the two quarters strung together, our pricing, as defined as the margin quality of the work we put on the books, was better in the second half of the year than it was in the first half of the year. So in that sense, we have seen improved pricing in the second half of the year.



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Darrin Peller - Barclays Capital - Analyst

Good. That's great to hear. Thanks, guys.

David Rowland - Accenture - CFO

All right. Thank you.

Operator

Tien-tsin Huang, JPMorgan. Please go ahead.

Tien-tsin Huang - JPMorgan - Analyst

Great. Thanks. Good morning. Just wanted to ask -- hello, David. Hello, Pierre. I just wanted to ask about the visibility into the 10 to 30, as well, on the operating margin front, especially curious about gross margin. Because I heard the comments on taking action on improving profitability. Is that action -- it sounded like also work to do. So is that subject to market conditions in terms of what you're going to do, or is there something that's in flight today? Just trying to get a better appreciation, again, of the visibility into that 10 to 30.

David Rowland - Accenture - CFO

If you think about it, Tien-tsin, maybe I'd call out four things that we're focused on to deliver the 10 to 30. And some of these are things that you'll understand very well. The first thing, at the core of what we're focused on, is overall payroll efficiency. And we referenced that in certain parts of our business, as we had this inflection point, there were some payroll inefficiencies that had resulted from that which we would address beginning in the second half of the year, and we've done just that. That is ongoing, but yet what we've done so far has some benefit into next year. But job number one, with margin expansion for us, is payroll efficiency. And I think we've proven that if you look at it over a period of time, we're very good at doing that. But we're certainly not immune to having a quarter or two where business conditions change where you can't just turn the dial at the moment.

The second thing we're focused on is our overall contract profitability. And that means for each dimension of work we do, we're working to optimize the profitability in the context of that market. So if you take what we do in digital or application services or Accenture Strategy, as an example. But then the other part of that is that we have a diverse set of businesses within Accenture now, and so the other dial is making sure that we have the right mix across the different offerings, businesses that we have, so that at the portfolio level, we're optimizing the overall contract profitability.

The third thing that we're focused on is business operations efficiency, which is the cost of us just running and managing our business, which is an ongoing objective. And so maybe I'll just stop there. But those are the three big things, and we have our sights set on actions around each of those areas. Now, it's on us to deliver. But there isn't anything that happened this year -- even reflecting on our second-quarter call -- there's not anything that's happened this year that has taken our eyes off of our focus on modest margin expansion, which we've defined as 10 to 30 basis points.

Tien-tsin Huang - JPMorgan - Analyst

Okay. No, that's helpful. So can you just quickly elaborate on -- I don't know if you gave it -- on headcount growth targets this year. And as my real follow-up, just the acquisition contribution in FY15. I'm curious how overall acquisitions are performing. And we've seen some larger acquisitions in the space, and I'm curious if your appetite to do deals has changed in any way. That's all I had. Thanks.

David Rowland - Accenture - CFO

Let me comment first on the inorganic 2014 to 2015, and then maybe Pierre would want to comment just on our acquisition philosophy and strategy. So Tien-tsin, you'll remember that on the last call I said that the inorganic contribution would be in the 1.5 to 2 range in 2014, to be clear. I'll just remind everyone that we measure



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inorganic on a rolling four-quarter basis. So from the time an acquisition comes on the books, for four quarters, we include it in our inorganic number. After that, it becomes part of our organic engine, if you will.

So where we landed the year is that the inorganic contribution, which we felt very good about, was closer to 2% than 1.5%. And we do expect next year that, part of this is just the timing, we had our most significant acquisition activity in the first half of this year, so the timing is such that the inorganic contribution next year will be closer to the 1% range. So when you think about organic growth in 2015, that's all in the mix of the 4% to 7%, as well. We feel very good about what we see in our organic business and hence, we've got the range of 4% to 7%, even with the lower contribution of inorganic.

Pierre Nanterme - Accenture - Chairman & CEO

Yes. On acquisitions, what you've seen these last couple of years is all the effort we've made, and yielding results now, to position our portfolio of businesses for growth in this new environment of a mainly digital computing world. And so we've been working hard on this. And we've been using acquisitions to accelerate this repositioning, especially in two areas of our business. One is what we are calling now Accenture Digital and the other one being Accenture Operations. We are really channeling significantly our investments in these two areas to provide the right response to the market, which is quite keen to buy on digitalization, and on the other end, on rationalization.

We deployed, if I remember well, around \$800 million in FY13, \$740 million in FY14. So it's giving you a sense about the kind of level of cash we might deploy in the context of the strategy, which doesn't mean that if we have the opportunity, we can't do more. If we believe there is an opportunity we need to capture that would significantly enhance our capabilities, both in the digital world or in the operations world, or in some of our markets around the world, we will be prepared to step in.

Again, we're not changing the over-arching philosophy. We're making acquisitions to grow on top of these acquisitions and to acquire unique and differentiated capabilities we can grow then organically. And this is exactly what we did with Procurian. And this is exactly what we did in the past with the acquisitions of Fjord, avVenta and Acquity. So this is the mental model. Capabilities, deploying in the range of \$800 million, plus the opportunity to deploy more, if this is necessary, with always the perspective to scale and to scale rapidly to take a market-leading position.

Operator

James Friedman, Susquehanna, please go ahead.

James Friedman - Susquehanna Financial Group - Analyst

Hello. Thank you. Pierre, in the fiscal Q2 conference call, you had suggested that Accenture Digital -- I think the language you used was growing solid double-digit. I was wondering if you'd be comfortable giving us an update as to the growth rate as of the end of the year.

Pierre Nanterme - Accenture - Chairman & CEO

Regarding Digital?

David Rowland - Accenture - CFO

Digital, yes.

Pierre Nanterme - Accenture - Chairman & CEO

And I'm taking this opportunity to -- I was very pleased to read and very impressed with the note you communicated on us. And I liked especially the call to action, a good offense is a good defense. And I think this is exactly what we do at Accenture. We're always playing offense. And indeed, for us playing offense is to take some very significant steps in the digital, because this is the segment of the market which is growing. We anticipated that a few years ago and we definitely accelerated our growth strategy regarding digital.



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If you will, today, and probably for the first time, we're going to communicate this number outside. But we feel very confident now we can communicate that number of our digital business, because it's extremely analytical-based and the scope is very precise. Today, what we're doing with Accenture Digital is around 17% of our business, growing in the double-digits. So around \$5 billion revenue in FY14 at Accenture.

And I'm indeed very pleased with that, because this is a business which is growing fast, double-digit, which is extremely relevant for our clients and which is now meaningful in the business of Accenture. When you're starting to hit the 17%, trending certainly to the 20% of the business, it is a meaningful business and I'm extraordinarily pleased with the repositioning we've been undertaking.

James Friedman - Susquehanna Financial Group - Analyst

I'll need to pay more attention to my titles, now that I know you're reading them. I wanted to ask, in that same regard, do you have any observations, Pierre, about which operating groups it's more prevalent in or which geographies it's more prevalent in? Those would be my follow-ups. Thank you.

Pierre Nanterme - Accenture - Chairman & CEO

Yes, sure. What's good, if you will, or impressive in digital, it's pervasive across the patch. So it's clearly a set of technologies -- and I'm talking about, of course, the digital consumer, the digital enterprise, the digital operations, all related to analytics, of course, cloud-enabling technologies, usually known as SMAC, in the past -- Social, Mobile, Analytics, Cloud. It's absolutely pervasive across the board.

So we're starting to see good traction, of course, with more the B2C kind of industries, if you will. I'm thinking about retail, I'm thinking about consumer goods, financial services, telecom, good appetite for that. But rapidly, we see the second wave of digital impacting now the B2C businesses. I could have mentioned healthcare. So healthcare is probably a hybrid, because it's B2C, as well as B2B. And then you're moving to more the manufacturing kind of organizations, with what now we're calling the famous IOT, the Internet of Things. And we are taking steps, as well, to move from the B2C to the B2B2C, and from the B2B, and from the digital consumer to the Internet of Things. So the early adopters, we're very pleased with them. They are the usual suspects. But now we see good traction in other parts of the business.

And I'm thinking even about Resources, where we're starting to put digital in what we're calling digital plant and digital operations, and things we are doing with some of our partners. And we have recently created joint ventures, as you might have seen, with General Electric around aircraft maintenance, as well as intelligent pipeline, which is the new launch we made with General Electric. And on the other side of the spectrum, with Siemens around the smart grid.

So, extremely pleased to answer that question. I guess you see my excitement playing the offense.

Operator

Lisa Ellis, Sanford Bernstein.

Lisa Ellis - Sanford C. Bernstein & Co. - Analyst

Good morning, guys. Happy to be joining these calls. I wanted to ask a couple questions about the labor market and get your take on how you're seeing trends in the labor market. If I just look at -- your attrition ticked up again this quarter. Gross profit has ticked down. It looks like your accrued payroll is down year-on-year. So you could read into that that you're seeing some labor pressure in service delivery, especially given your GDN mix has been constant now for six or seven quarters. So just want to see if that's consistent with what you're seeing, and in that context how you see that trending going into next year.

David Rowland - Accenture - CFO

Maybe let me just pick up on the last thing you said. If your read-through is that we're seeing it in service delivery -- by the way, Lisa, welcome to the call. I'll just go back and point out again that our contract profitability, which is our service delivery, is actually improved sequentially the last two quarters. So that is on an upward trend.

Lisa, you also referenced gross margin. And there's a lot of things that go into gross margin, beyond just the contract delivery cost. You have, for example, things like training and recruiting. And we typically bring a lot of people on board in the fourth quarter; and this year that was especially true, as our revenue is growing, as an



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example. You have other things that would impact. For example, I referenced supply-side actions that we've taken in those parts of our business where we're dealing aggressively with fine-tuning the overall payroll efficiency. And when we do that, those costs can go through gross margin.

And then there can be the normal ebb and flow, whereas in one quarter, we can have a lot of business development activity. In another quarter, just even beyond new hires, you might have a heavy training quarter and the overall payroll efficiency isn't changing, just where people charge their time is. That's why we repeatedly say that to understand our business, you really have to focus on operating margin. And that's really the bottom line.

Lisa, you also referenced the attrition number going up, which I called out. It did go up. But at the 15% level, that's well within our range, and really frankly, well within the norm of services companies like ours.

We focus every day on our people, on market-relevant compensation, on employee engagement, which we measure regularly, on pulse surveys, et cetera. And that is a core part of our culture and that will always be. Taking care of our people and our clients first is really what we focus on.

Lisa Ellis - Sanford C. Bernstein & Co. - Analyst

Terrific. And then my follow-up is actually on the BPO side. You highlighted that, or called that out, as one area of particular strength. Can you just elaborate a little bit on what service lines in particular, and is the service mix in there evolving as you're seeing increased demand on BPO?

Pierre Nanterme - Accenture - Chairman & CEO

Yes, absolutely. So BPO, which is now part of what we're calling Accenture Operations, where we put together our infrastructure services and business process services, if you will, to create what we believe is going to be a unique value proposition in the marketplace, in the context of moving more and more BPO, provide more and more BPO as a service on platforms, and all of this -- this is the essence of the creation of Accenture Operations. And again, I think we are making in the market very significant steps, because as far as I know, we are the only one who today are proposing this opportunity.

So BPO is an excellent answer to what I called before the rationalization agenda of our clients to get more efficiency and more productivity. Again, BPO is pretty hot across the board, when you're looking at our results, and especially around what we're calling the horizontals, finance & accounting, HR administration, and of course, procurement, where we are clearly now the market leader. We are selling these three capabilities, from a BPO standpoint, across all the industries.

I'm thinking about a recent win in financial services with a European bank where we are now driving all their finance & accounting operations. Of course, in F&A, we communicated around this big win with this oil and gas company in Europe, a giant, as well. We're doing all the HR administration of one of the largest consumer goods companies in the world. And extremely recently, in electronic equipment, we've been selected to be clearly their backbone in running their finance and accounting, their HR, their IT, and part of their sourcing operation to support them in one of the largest-scale transformation programs today in the industry.

So it is pretty hot. And again, I'm coming back at the heart of our -- at what I call repositioning or rotating our businesses, if you will, from what we were and we are still famous for, the more classic ERP and technology business. We continue, of course, to be competitive in that space. But we added two big engines for growth at scale, double-digit, extremely meaningful for Accenture. Accenture Digital on one hand, I mentioned this \$5 billion business, and Accenture Operations on the other hand, which is another formidable machine for growth.

KC McClure - Accenture - Managing Director, Head of IR

Steve, we have time for one more question, then Pierre's going to wrap up the call.

Operator

Due to time constraints, our last question will come from the line of David Togut of Evercore. Please go ahead.

David Togut - Evercore Partners - Analyst

Thank you. Good morning, Pierre and David.



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David Rowland - Accenture - CFO

Good morning, David.

Pierre Nanterme - Accenture - Chairman & CEO

Good morning.

David Togut - Evercore Partners - Analyst

Good morning. Could you quantify for us the 2015 average wage increase and also the average price increase for 2015?

David Rowland - Accenture - CFO

David, the answer -- I guess the short answer is no. (Laughter) The reason is that when we quote a number like that on the wage side, it potentially creates a lot of confusion within our employee base, where it varies so much country to country, and to have an overall average number sometimes just creates confusion. And maybe I'll just stop there. We really can't comment on either one of those. Sorry about that, but --

David Togut - Evercore Partners - Analyst

But for context, David, we see attrition going up for the last two quarters and that would suggest we're in an environment of rising wages. Can you just bracket for us possible ranges, so we can understand the gross margin question a little better?

David Rowland - Accenture - CFO

What I can say is there is nothing unusual with respect to our wage increases in 2015, I guess I could say there's nothing unusual. There's nothing unusual in response to what you perceive to be perhaps a building issue. I think that certainly there are markets and skills where -- that are in higher demand. And when we see those, we respond very proactively with what we do with our comp. But there are also a lot of markets around the world where there's deflation and deflationary trends for compensation. And so what we always do is we're market-relevant. And so if you're trying to understand, is there anything unusual that we anticipate in 2015 with respect to wage increases, the answer to that is no.

David Togut - Evercore Partners - Analyst

Thank you. That's very helpful.

David Rowland - Accenture - CFO

Okay. Thank you.

Pierre Nanterme - Accenture - Chairman & CEO

Thank you, everybody, and thanks a lot for all your good questions this morning. Just in closing the call and reflecting on what might happen moving forward and as we enter FY15, I am confident in our ability to drive profitable growth and to deliver our business outlook for the year.

We have momentum in our business. We are investing in new capabilities to be even more relevant, differentiated and competitive. And with our highly diverse portfolio of business, combined with the disciplined management of our operations, we are well-positioned to deliver sustainable, long-term, profitable growth.



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I want to take this opportunity to thank the men and women of Accenture who, every day and everywhere around the world, work side-by-side with our clients to bring their unique skills, their true passion and their amazing commitment to deliver value. Thanks to all of them.

And I would like to thank you, our investors, for your continued support and your confidence in Accenture. We look forward to talking with you again next quarter, and also to seeing many of you in person at our Investor & Analyst Conference in New York on October 7.

In the meantime, if you have any questions, please feel free to call KC. All the best.

Operator

Ladies and gentlemen, that does conclude our conference call for today. Thank you for your participation. Thank you for using AT&T. Have a wonderful day. You may now disconnect.

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