David Straube, Head of Investor Relations

Thank you, operator and good morning, everyone. By now, you should have received your copy of the earnings release for the Company's third quarter 2022 results. If you have not, a copy is available on EPAM.com in the investor's section.

With me on today's call are Arkadiy Dobkin, CEO and President, and Jason Peterson, Chief Financial Officer.

I would like to remind those listening that some of the comments made on today's call may contain forward-looking statements. These statements are subject to risk and uncertainties as described in the Company's earnings release and SEC filings. Additionally, all references to reported results that are non-GAAP measures have been reconciled to the comparable GAAP measures and are available in our quarterly earnings materials located in the investors section of our website.
And now, I would like to turn the call over to Ark.

Arkadiy Dobkin, CEO and President

Thank you, David. Good morning, everyone. Thank you for joining us this morning.

Let me begin today with a simple statement that we are very proud of everything EPAM achieved over our nearly three decades and that we are very thankful to the people of EPAM for their tremendous contributions over those years. And I would also like to add one more thought, which feels very important to bring to the top of our conversation.

While we all know that the war in Ukraine is still dominating global headlines, and we are seeing its ripple effects across many sectors and geographies. For us, at EPAM, and many people around us, this war continues to be a very central part of our lives, deeply personal and a constant priority.

With that, I would like to start with an update on our progress across our four phased approach, which we shared with you six months ago, back in May as well as an update on some adjustments we are making as a result of newly available information.

Our First Phase – The safety of our employees and stabilization of our operations in Ukraine.

The war has been ongoing for eight months already. Last time we met, we indicated that we thought that it was going to be longer than anybody was thinking when it began. And we all understand that the situation continuous to be very serious and, also, that 'safety' is a very relative term for people within Ukraine's borders today. With all of that, we are constantly and proactively helping our employees, their families, and the people of Ukraine as much as we can, by providing a wide range of support including regional relocations and all forms of local assistance, making it possible for our people, their families and, often, industry colleagues to continue to live and work in Ukraine.

We are also continually developing ways to address new and unpredictable 'just yesterday' challenges, and we are trying to also think proactively about what we can do today to make it easier and safer for tomorrow. And with all of that, we are working together across our all locations to maintain the highest levels of service possible for our customers across all of our delivery locations within Ukraine.

Even with the recent level of infrastructure instability, the productivity of our teams in country remains high, which makes us believe that we can count on this level of resilience in our delivery operations, when we are sharing our guidance with the market today.

Thank you to our Ukrainian team and all EPAMers for making this possible. It is simply just incredible. Thank you!

Moving to our Second Phase – The acceleration of our global diversification efforts and continued growth of our diverse capabilities.

Over the last eight months we have accelerated key parts of our global strategy, in many ways accomplishing what we had planned to do over several years.

Our delivery location geographies become more and more balanced. Last quarter we reported that impacted regions accounted for 40% of our talent, while today, with practically a full exit from Russia, approximately 30% of our talent remains in the immediate regions. Something we planned to achieve closer to the end of the year. So, our presence in Europe outside of those regions, in Central and Western Asia, India, and Latin America are growing proportionally.

In short, the adaptation of our business and the reposition of our delivery organizations is moving forward at unprecedented pace. We are very thankful to the many thousands of EPAMers and their immediate families for their loyalty, trust and their decisions to move to new country locations, while staying with and continuing to work at EPAM. While it has been a complex undertaking, we are encouraged by the overall levels of engagement and productivity we are seeing in our many new hubs and satellite locations. Many of these employees bring years of experience, skills, and knowledge with them and are key to our global expansion efforts, as we further seed, integrate and scale a globally resilient workforce, now operating in more than 50 countries.

Please note, that during that time, we practically doubled the number of locations, which should enable us to establish an additional large (large means over 5 thousand people) talent hubs during the next few years, and some of these hubs did not even exist at EPAM in February of 2022. As you can see, we are passionate about creating technology hubs and expanding our investments in many of those geographies. As a result, our global delivery platform, and new ways of working, should position us to become one of the most geographically balanced and value-added services companies in the market.

Moving to Phase 3 of continuing to serve and expand demand for our services for our growing, global customer portfolio. And Phase 4 of focusing on profitability. Those two are very connected.

We are working closely with our customers to reposition sizeable portions of our program portfolio without disruption and impact on quality. And while our business continuity programs have been necessary to plan for contingencies and enable uninterrupted service quality, our customer portfolio is now better diversified and more resilient, giving them a new level of engagement and new talent options that should establish a broader, more valuable partnership framework for us, post war. Today, we are staying close to our customers and working through different proactive plans and contingencies in what has become for us “New Normal.” That also includes our efforts around coming back to the profit levels that are in line with our historic numbers. As you can see – we have some intermediate success in that direction already, while it is still too early to say that we have overcome the challenge to make it sustainable.

On that topic of navigating the unpredictable. I would like also to share here that during the recent Gartner Symposium in October, EPAM was a featured case study on Labor and Global Talent Resilience exactly based on our efforts over the last eight months to adapt, to provide safety for our people and assistance with relocations, and for continually investing in our capabilities and future growth, while navigating the unpredictable.

We believe that most of the efforts highlighted by Gartner, have put us onto a new trajectory or established a foundation, if you will, that will position EPAM for continued future growth and market differentiation. Here I would like to mention three more on top of what we have already shared:

- Progressing EPAM Continuum, our integrated consulting offering, which opens new market entry points, and extends the depth and breadth of our existing relationships with customers to cover an even more strategic set of buyers in our portfolio. Also reflected by our increased onsite production headcount ratio, which is now 13.6% - the highest in our history.

- Furthering our ecosystem partnerships, enabled by our product and platform engineering heritage and new scale in-market to bring domain-relevant solutions to customers facing increasingly complex business and technology environments.

- Lastly, significantly investing in our education platforms, which keeps our employees on the cutting edge and allows us to attract, onboard, develop and deploy global talent for EPAM; as well as offer composable education services to our customers.

In more simple way, with all the above efforts we are very focused on maintaining our Engineering and technology advantage and reputation across all our new and already established locations. Yes – we do understand that it is exactly one of the key questions you, as investors, and all our clients, are asking today. And, also, probably, about our ability to continue moving higher in the value chain; something we started ten years ago and what we are very eager to continue doing now and, in the future, proving to the market that we would be able to navigate the next transformation at EPAM to be able to offer to our clients something, which is rare on the market, strategy and implementation simultaneously and at scale. And doing that better than most of our competitors can.

With that let’s talk a bit about our Q3 results, while Jason will share, as always, the full level of details right after.

In the third quarter EPAM delivered $1 billion 230 million in revenues, a 24% year-over-year growth, and non-GAAP earnings per share of $3.10, a 30% increase over Q3 2021. I think it is important to mention that in constant currency terms and with proper adjustment on discontinued revenue in Russia that growth would be about 35%.

Also, during the quarter, the Company generated $234 million of free cash flow and now has approximately $1.5 billion of cash on hand.

We are proud and grateful to all our teams for continuing to manage the business at this level while responding to constant pressures to plan and execute a large number of tactical adjustments in an increasingly complex global geopolitical and economic environment. And especially thankful to our teams in Ukraine.

As you have likely heard during the last months, some of our partners and customers have been messaging their expectations for a global slowdown in demand, and their resulting actions to better align their businesses to this new environment. So, for us, while the demand environment continues to be active across a number of our end markets, including clients seeking help with transformational programs, products, platform development and modernization efforts in addition to the opportunities, triggered from the recent acquisitions, we can confirm that there has been an increasing focus for programs that are tied to driving short-term cost savings, other Opex efficiencies and a broad range of ‘Optimization’ programs for which EPAM is also properly positioned today. Still, even with all confidence that our services remain highly relevant and in demand, we are beginning to see signs of a growth level slowdown.

So, while we are taking steps to moderate our hiring and spending in response, we are also reminded of previous downturns, out of which we grew at an unprecedented rate. As such, we are working to carefully calibrate our supply and demand outlooks to capture the demand upswing when it returns, as we did it in the past.

As we wrap up 2022, we believe that we will have contained the initial impact of the war within the fiscal year, including the discontinuation of our operations in Russia.
But, in overall, we know that we are still in the middle of the ongoing crisis in Ukraine. And unfortunately, it does not seem that right now it will be possible to contain the full impact of the war just within 2022 as we had previously hoped.

What has changed over the past three quarters is that when we say we can and will adjust our operations, we are confident that under circumstances, we can do so reliably and quickly.

And, exactly that for us is a very important confirmation, that after almost 30 years of our existence, after ten years of being a publicly traded company, and after becoming S&P 500 member, we still can demonstrate our strong entrepreneurial DNA and we still can benefit from it by acting as ‘start-up’, and that ensures our ability to adapt and to grow further again, while, for the current time, we are still planning for different types of mitigating scenarios in response to ongoing war events to protect EPAM and our employees who remain in the region.

Nonetheless, we are confident that the steps we have taken to reposition and diversify the Company have created an even stronger foundation for future growth as we focus on EPAM as a $10 billion company. Very much in line with what we shared with you in early 2022, before the war began.

Now let me turn the call over to Jason who will talk about our Q3 results and additional perspective as we look at Q4 and beyond.

Jason Peterson, CFO

Thank you, Ark, and good morning, everyone.

Before covering our Q3 results, I wanted to remind everyone that in addition to our customary non-GAAP adjustments, expenditures related to EPAM’s humanitarian commitment to Ukraine, the exit of our Russian operations, and costs associated with accelerated employee relocations have been excluded from non-GAAP financial results.

We have included additional disclosures specific to these and other related items in our Q3 earnings release.

In the third quarter, EPAM delivered another set of strong results across both top and bottom line, in addition to strong cash flow generation.

During Q3, EPAM generated revenues of $1.23 billion, a year-over-year increase of 24.1% on a reported basis and 29.8% in constant currency terms, reflecting a negative foreign-exchange impact of 570 basis points. Additionally, the reduction in Russian Customer revenues resulting from our decision to exit the market had a 470 basis point negative impact on revenue growth. Adjusting for the exit of our Russia operations, reported revenue growth would have been approximately 29.0%.

Looking at the performance of our industry verticals and geographic regions in the quarter, growth was negatively impacted by the ongoing exit of our Russia operations, and the effect of foreign exchange on our U.S. dollar reported results. Where helpful, I will provide an adjusted year-over-year comparison.

Beginning with our industry verticals:

- Travel & Consumer grew 41.9%, driven by strong organic growth primarily from our Retail customers as well as revenue contributions from recent acquisitions.

- Life Sciences & Healthcare grew 35.0% with strong growth coming from the Healthcare industry in addition to growth in Life Sciences.

- Financial Services grew 10.4%, with growth coming from Asset Management, Banking and, to a lesser extent, Insurance. Excluding our Russia customers, growth would have been 25.4% and, 29.9% in constant currency.

- Business Information & Media delivered 20.8% growth in the quarter, driven primarily by customers in the Business Information industry.

- Software & Hi-Tech grew 17.8% in the quarter, and finally,

- Our Emerging Verticals delivered 26.6% growth, driven by clients in Energy, Manufacturing and Automotive. Excluding our Russia customers, growth was 29.5% or 39.4% in constant currency.

From a geographic perspective:

- Americas, our largest region representing 61% of our Q3 revenues, grew 26.3% year-over-year or 27.7% in constant currency.

- EMEA, representing 36% of our Q3 revenues, grew 35.3% year-over-year or 50.3% in constant currency. EMEA performance was driven by strong organic growth combined with an incremental contribution from recent acquisitions.

- CEE, representing 1% of our Q3 revenues, contracted 77.2% year-over-year or 80.2% in constant currency. Revenue in the quarter was impacted by our decision to exit Russia and the resulting ramp down of services to Russia customers.

- And finally, APAC grew 10.5% year-over-year or 15.4% in constant currency terms and now represents 2% of our revenues.

In Q3, revenues from our top 20 clients grew 22% year-over-year while revenues from clients outside our top 20 grew 25%.

Moving down the income statement:

Our GAAP Gross Margin for the quarter was 32.6%, compared to 33.9% in Q3 of last year. Non-GAAP Gross Margin for the quarter was 34.4%, compared to 35.1% for the same quarter last year.

Compared to Q3 2021, Gross Margin in Q3 2022 reflects the negative impact of lower utilization as well as a benefit from foreign exchange and the positive impact of a more normalized expense related to variable compensation. In Q3 2021, expense related to variable compensation was unusually high based on the strong bottom line and extremely strong top-line performance during the year. Q3 2022 was also negatively impacted by the timing difference associated with EPAM's ongoing efforts to align bill rates based on employee relocations. However, we have made better progress adjusting rates than originally anticipated. As a result, the negative impact on profitability was more limited than originally expected.

GAAP SG&A was 16.1% of revenue compared to 17.1% in Q3 of last year, and non-GAAP SG&A came in at 14.1% of revenue compared to 15.3% in the same period last year. SG&A performance in the quarter reflected a lower level of costs related to both variable compensation and facilities, and also includes a positive benefit of foreign exchange.

GAAP income from operations was $180 million or 14.7% of revenue in the quarter compared to $144 million or 14.6% of revenue in Q3 of last year. Non-GAAP income from operations was $232 million or 18.9% of revenue in the quarter compared to $180 million or 18.2% of revenue in Q3 of last year. Q3 Non-GAAP income from operations reflects a lower level of variable compensation and a positive impact from foreign exchange, offset by a lower level of utilization.

Our GAAP effective tax rate for the quarter was 18.4% primarily driven by excess tax benefits related to stock-based compensation. Our Non-GAAP effective tax rate, which excludes excess tax benefits was 23.1%.

Diluted earnings per share on a GAAP basis was $2.63 reflecting a $0.68 or 34.9% increase year-over-year. GAAP EPS includes the impact of Ukraine humanitarian expenditures, expenses related to accelerated staff relocation, and costs related

to the planned exit of our Russian operations. Our Non-GAAP Diluted EPS was $3.10 reflecting a $0.68 increase or 28.1% growth over the same quarter in 2021.
In Q3, there were approximately 59.4 million diluted shares outstanding.

Turning to our cash flow and balance sheet:

Cash flow from operations for Q3 was $252 million, compared to $206 million in the same quarter of 2021.

Free cash flow was $234 million, compared to free cash flow of $185 million in the same quarter last year.

We ended the quarter with approximately $1.5 billion in cash and cash equivalents.

At the end of Q3, DSO was 69 days and compares to 71 days for Q2 2022 and 70 days for the same quarter last year. In Q4, we traditionally experience a further improvement in DSO and expect a similar result this year.

Moving on to a few operational metrics:

We ended the quarter with more than 53,900 Consultants, Designers and Engineers, a year-over-year increase of 14.5%. Our total headcount for Q3 was more than 60,250 employees. Compared to Q2, we saw a net decrease of approximately 1,000 headcount. The net decrease in headcount is a result of the reduction in Russia-based headcount, combined with a lower level of hiring across the organization due to better-than-expected productivity in Ukraine and with a focus on moving utilization towards higher levels.

Utilization was 73.5% compared to 77.1% in Q3 of last year and 78.0% in Q2 2022. Utilization continues to be impacted by the war in Ukraine.

Now let's turn to our business outlook:

As we have done in previous quarters, let me provide some context that is informing our guidance for the fourth quarter.

We expect a solid demand environment including demand for programs helping clients drive additional revenue, modernization, and optimization. In a few cases in the Retail and Consumer space, we are seeing signs of moderation in demand due to delays in decision making, or additional scrutiny on program budgets, as certain customers become more cautious regarding shifting demand in their end markets.

As a reminder, the exit of our Russian operations and the reduction in Russia customer revenues produces a tougher year-over-year revenue comparison, particularly in Q4 which has generally been a seasonally strong quarter in Russia.

To date, our operations in Ukraine have not been materially impacted by the recent escalation of attacks, and our teams remain highly focused on maintaining uninterrupted production. Our guidance assumes that we will continue to be able to deliver from our Ukraine delivery centers at productivity levels at or somewhat lower than those achieved in Q3 and consistent with our experience in the month of October.

Through September 30th EPAM has spent more than $39 million as part of the Company's $100 million humanitarian commitment to our Ukrainian employees and their families. We expect further humanitarian expenditures will be made in Q4 and during 2023.

Now, moving to our Q4 2022 outlook we expect:

- Revenues to be in the range of $1 billion 220 million to $1 billion 230 million producing a year-over-year growth rate of approximately 11.0% on a reported basis and 15.0% in constant currency terms, both at the mid-point of the range.

Included in these growth rates is approximately 100 basis points of revenue contributed from acquisitions closed over the last 12 months. Additionally, the ramp down of Russian customer revenues due to our decision to exit this market has a negative impact reducing our expected revenue growth rate by approximately 500 basis points.

- For the fourth quarter, we expect GAAP Income from Operations to be in the range of 12.0% to 13.0% and Non-GAAP Income from Operations to be in the range of 16.0% to 17.0%.

- We expect our GAAP Effective Tax Rate to be approximately 21.0% and our Non-GAAP Effective Tax Rate, which excludes excess tax benefits related to stock-based compensation to be approximately 23.0%.

- For Earnings per Share, we expect GAAP diluted EPS to be in the range of $2.02 to $2.10 for the quarter, and Non-GAAP Diluted EPS to be in the range of $2.62 to $2.70 for the quarter.

- We expect a weighted average share count of 59.6 million diluted shares outstanding.

Finally, a few key assumptions that support our GAAP to Non-GAAP measurements in the fourth quarter:

- Stock-based compensation expense is expected to be approximately 33 million.

- Amortization of intangibles is expected to be approximately 5.7 million.

- The impact of foreign exchange is expected to be negligible.

- Tax effect of non-GAAP adjustments is expected to be around 9.6 million.

- And finally, we expect excess tax benefits to be around 4.3 million in the quarter.

In addition to these customary GAAP to Non-GAAP adjustments, and consistent with the prior quarters in 2022, we expect to have ongoing non-GAAP adjustments in Q4 resulting from Russia's invasion of Ukraine. Please see our Q3 earnings release for a detailed reconciliation of our GAAP to Non-GAAP guidance.

Our fourth quarter outlook reflects a solid demand environment, combined with improved operating performance allowing EPAM to return to its traditional 16 - 17% AIFO range sooner than anticipated. Although we still face ongoing challenges, this is a significant achievement given the amount of disruption that the Company is managing through as the result of the war in Ukraine. We will continue to closely manage the operations of EPAM while remaining attentive to any changes in the demand environment.

Lastly, I'd like to thank our employees for their continued dedication and focus on our customers.