Syntel Participants

Bharat Desai	**Co-Chairman and Co-Founder**
Rakesh Khanna	**CEO and President**
Anil Agrawal	**CFO**
Zaineb Bokhari	**VP, Finance**

Operator

Ladies and gentlemen, thank you for standing by, and welcome to the Syntel First Quarter 2018 Earnings Call. At this time all participants are in a listen-only mode. Later we will conduct a question and answer session.

At that time if you have any questions, you need to press star then the number 1 on your telephone keypad to place your line into the question queue. If you would like to withdraw your question, press the pound key.

As a reminder, this call is being recorded, today, Thursday, April 19, 2018. I will now turn the call over to **Zaineb Bokhari**, Syntel's Vice President of Finance.

Zaineb Bokhari

Thank you, and good morning, everyone. Syntel's first quarter earnings release crossed GlobeNewswire at 8:30 a.m. today. It's also available on our website at www.syntelinc.com.

On the call with us today, we have Bharat Desai and Prashant Ranade, Syntel's Co-Chairmen; Rakesh Khanna, Syntel's CEO and President; and Anil Agrawal, Syntel's Chief Financial Officer.

Before we begin, I'd like to remind you that some of the comments made on today's call and responses to questions may contain forward-looking statements. These statements are subject to the risks and uncertainties described in the company's earnings release and other filings with the SEC.

I'll now turn the call over to Syntel's Co-Chairman, **Bharat Desai**. Bharat?

Bharat Desai

Thank you, Zaineb. Good morning, everybody, and thank you for joining us today. I'm pleased with the first quarter results and the strong execution by our teams. The broader environment improved modestly during the first quarter and the headwinds we experienced last year have started to show signs of abating.

While some challenges remain, Syntel is investing for growth, enhancing our service offerings, tools and platforms and developing our talent on a global scale. Our client-focused strategy to expand coverage and strengthen Syntel's relationships across our top 50 customers had meaningfully improved our ability to identify new opportunities across these important relationships.

This focus has helped improve close rates. We'll continue to invest in these efforts over the balance of the year and look to build on the positive momentum we have seen thus far.

Through these efforts, we also continue to gain perspective on our clients' business needs and the challenges they face. Many established companies and brands are experiencing considerable disruption as consumer tastes and preferences evolve. Companies are focused on connecting with their customers to gain deeper insights and provide personalized products or services and seamless delivery at an attractive value.

These capabilities are rapidly becoming table stakes as nimble, digital native challengers leverage technology to lower traditional barriers to entry. Many companies have recognized that we successfully compete and grow in this environment. They need to modernize core systems, applications and data to alleviate the cost and functional limitations of their legacy systems.

Syntel is well-positioned to help our customers sustain and grow their competitive advantage. Our holistic approach to digital transformation allows us to support our clients with high-impact digital capabilities and core services powered by intelligent automation that enable efficient IT operations and de-risk legacy modernization.

Our technology and services portfolio is complemented by considerable industry experience and a deep commitment to the success of our customers. I'm encouraged by our progress and confident that our teams has put together a strong strategy for Syntel's growth going forward.

I would now like to turn the call over to **Rakesh Khanna**, Syntel's Chief Executive Officer and President, to provide further details. Rakesh?

Rakesh Khanna

Thank you Bharat and welcome everyone. We are pleased with our Q1 results. We continue to benefit from our improved positioning across our top 50 customers, particularly the 4 to 50 segment. Our ability to identify opportunities has improved and the enhancements we have made to our responsiveness and agility helped us capture and close deals at a healthy pace in Q1. We also saw broader contribution across our industry segments during Q1 as the demand environment improved slightly. Due to the combination of these factors, we did not see the typical Q4 to Q1 revenue softness as in some recent years.

Client budgets have finalized largely in-line with our expectations. By segment, we continue to anticipate healthy trends across the Insurance and Retail Logistics and Telecom segments. There are still many cross currents impacting the healthcare industry in the U.S. However, based on our current visibility, we expect our Healthcare and Life Sciences segment to contribute to overall company growth during 2018.

Banking and Financial Services segment remains challenged, in our view. Some of this is clearly specific to our footprint and business mix. After considerable headwinds during 2017, we saw some stabilization on a quarter over quarter basis during Q1. Based on what we know at this time, we still expect the BNFS segment to trail company growth in 2018. But, some of the headwinds we saw last year have decelerated.

In addition to industry trends and our internal efforts at improving execution across the 4 to 50 customer segment, we continue to expect demand for digital services to remain strong in 2018. By geographic region, we also expect favorable trends from Europe.

To support our growth plans, we plan to continue to invest in workforce transformation and skill development. We are also investing in our partner channel. Syntel recently achieved certification as a Google Cloud Services partner and signed a strategic partnership with Esko, a leading provider of software for labeling and packaging. These partnerships strengthen and align our service offerings with the technology and business needs of our customers.

Our business is changing as digital adoption continues to rise. This has clearly been a focus for us as we invest in our service offerings, create new IP and transform our global talent. We feel good about the progress we have made and have great confidence in our positioning, our solutions and our capabilities. However, we continue to see shorter durations for some of our engagements as compared to what has been traditional. We incorporate this dynamic into our full year outlook and because of the variability we’ve observed, we have continued to keep our guidance ranges wide and our visibility thresholds high. Anil will expand on our Quarter 1 metrics and 2018 outlook in his prepared remarks.

Now, let’s review our results. Syntel’s Quarter 1 quarter revenue was $245.3 million, up 8.6% year-over-year and 2.3% on a sequential basis.

By industry segment, the Banking and Financial Services segment revenue increased 0.4% year-over-year in Quarter 1. The Retail, Logistics and Telecom segment grew by 11.9%, Healthcare and Life Sciences increased 18.8%, Insurance increased 16%, and Manufacturing grew 20.4% from a year ago.

Europe revenue increased 34.2% year-over-year. Revenue from digital projects accounted for approximately 20.5% of revenue in Quarter 1, as compared to 18.3% in the year ago quarter. On a year over year basis, Quarter 1 digital revenue increased by 21.6 percent.

Quarter 1 gross margin narrowed to 37.2% from 41.4% in the fourth quarter 2017. Offshore utilization for IT fell to 74% in Quarter 1 from 76.6% in Quarter 4 on a period-end basis. It fell to 75.3% in Quarter 1 from 76.5% in the previous quarter, on average. We continue to expect utilization above long-term historical trends. The mix between onsite versus offshore delivery was 25% and 75% in Quarter 1; as compared to 23.7% and 76.3% in Quarter 4.

Net headcount increased by 2.1% on a sequential basis to 22,571 in Quarter 1. Hiring continues across geographic regions tied to anticipated needs and requirements of our customers. Attrition, calculated on a current quarter annualized basis, was 21.9% in Quarter 1, as compared to 22.4% in Quarter 4 2017.

I will now turn the call over to **Anil Agrawal**, Syntel's Chief Financial Officer, who will discuss Syntel's financial performance in greater detail. Anil?

Anil Agrawal

Thanks, Rakesh and good morning everyone. After I conclude my comments, we will open the call for questions.

Syntel's first quarter revenue came in at $245.3 million, up 8.6% from the prior-year period and 2.3% from the prior quarter. For the first quarter, Banking and Financial Services contributed 43.4%%, with Retail, Logistics and Telecom at 18.4%, Healthcare and Life sciences at 18.2% Insurance 15.3%, and Manufacturing 4.7 percent. On a year-over-year basis, segment growth was led by our Manufacturing segment, which grew 20.4%, Healthcare and Life Sciences at 18.8%, Insurance at 16%, and Retail, Logistics and Telecom at 11.9%.

Syntel's customer concentration levels were as follows: our top 3 clients represented 43.4% in the first quarter of 2018, as compared to 47% in the year ago quarter and 43.2% in the fourth quarter of 2017. Accounts 4 to 50 represented 52.5% of revenue in the first quarter of 2018, as compared to 48.7% in the year ago quarter and 52.2% in the fourth quarter of 2017. The fixed-price component of our business was at 43.8% of revenue for the first quarter of 2018.

With respect to Syntel's margin performance, our first quarter gross margin was 37.2%, as compared to 36.6% reported in the year-ago period and 41.4% in the fourth quarter of 2017. By segment, gross margin for Banking and Financial Services was 39.6%, with Retail, Logistics and Telecom at 38.8%, Healthcare and Life Sciences at 37%, Insurance 33.9%, and Manufacturing 23.2 percent. During the first quarter of 2018, the Indian Rupee depreciated by 16 basis points on average relative to the U.S. Dollar from the prior quarter resulting in a 2 basis point favorable impact on the gross margin.

Moving down the income statement, our selling, general and administrative expenses were 11% in the first quarter of 2018, compared to 13.4% in the prior-year period and 12.1% in the fourth quarter of 2017. On a dollar basis, SG&A was lower by $2.1 million sequentially. The impact on the first quarter SG&A from currency-related balance sheet translations, based on quarter end exchange rates, was a $168 thousand gain, as compared to a $180 thousand loss recorded in the fourth quarter 2017.

Other expense was $2.2 million during the first quarter of 2018 as compared to $2.4 million in the fourth quarter of 2017, including a gain of approximately $0.4 million from mutual fund sales in the first quarter of 2018 as compared to a gain of $0.7 million in the fourth quarter 2017.

Our tax rate for the first quarter came in at 26.5% as compared to 37.4% posted in the fourth quarter of 2017. As a reminder, during the fourth quarter, following the enactment of the Tax Cuts and Jobs Act, there was a one-time impact of approximately $9 million in the tax provisions.

Net income for the first quarter was $45.6 million or 55 cents per diluted share as compared to a $38.4 million or 46 cents per diluted share in the prior-year period and net income of $42.4 million or 51 cents per diluted share in the previous quarter.

The Company's Balance Sheet at the end of the first quarter of 2018 remained healthy. Our total cash and short term investments balance on March 31 was $72.5 million and the portion held in U.S. dollars stood at 35 percent. DSO levels were at 56 days. Capital spending for the quarter was approximately $2.2 million.

Syntel ended the first quarter with total headcount of 22,571 of which 8,338 were assigned to KPO. Our global headcount was higher by 2.1% from the fourth quarter 2017. Our billable headcount was 4,587 on-site and 16,550 offshore for a total of 21,137. Utilization levels at the end of the quarter were 94.9% on-site, 79% offshore and 82.4% globally. Our delivery mix at quarter end was 25% onsite and 75% offshore. Voluntary attrition during the quarter was 21.9% as compared to 22.4% reported last quarter. Syntel added 3 new customers in the first quarter.

Looking forward, based on our current visibility levels, Syntel expects 2018 revenue to be in the range of $920 million to $960 million and earnings per share to be in the range of $1.76 to $1.96 for the full year of 2018. The Company currently has 82% visibility to the low end of the revenue range, and our guidance is based on an assumption for an average exchange rate of 65 rupees to the dollar. We anticipate that operating margins will be in the 23 to 25% range. Our effective tax rate will be in the mid to upper 20% range for 2018 and CAPEX is expected to be in the range of $10 to $15 million.

We will now open the call for our question-and-answer session. Operator?

Operator

At this time I would like to remind everyone that if you would like to ask a question please press star then the number 1 on your telephone keypad. To ensure that all of our participants have an opportunity to ask a questions, please limit yourself to one question and one follow up. We'll pause for just a moment to compile the Q&A roster.

Our first question comes from the line of Joseph Vafi of Loop Capital.

Joseph Vafi

I was wondering if we could dig down a little bit, I think, in one of Rakesh's comments that you did not see the normal seasonal fall-off in Q1.

And I know that you said that perhaps some of the project durations are shorter right now, but I would think that, that would be a relatively bullish setup for Q2 because you have already kind of — some of the budgets have already rebounded and should be more in full swing in Q2. And then I'll have a follow-up.

Zaineb Bokhari

Joe, we called this out this last quarter also, and we are not expecting the traditional seasonality that we see in the year. And you're absolutely right, this ties into what Rakesh was calling out where some of the engagements can be a smaller in size, especially on the digital side, maybe shorter on duration, and this still can change. So this is having an impact on our line of sight. The annual outlook that we're providing encompasses everything that we know at this time, again, including this dynamic.

Joseph Vafi

Okay. And then, I guess we still — I guess we have to wait for the 10-Q on the breakout of customers, I would imagine at this point, on the top 3?

Zaineb Bokhari

Correct. But I think that we obviously have very strong relationships, and we were very pleased with the trends, certainly, across 4 to 50, where they continued from strong gains in terms of our overall percentage revenue contribution. And we certainly expect that there are growth opportunities within our top relationships as well. So we feel pretty good about them. But yes, we will wait for the Q for some of the nitty-gritty details about revenue.

Joseph Vafi

Okay. And if I could just sneak one more, I might as well then, on the Financial Services practice, maybe a little color on which functional areas or technologies where you are seeing a little bit of a strength to rebound and perhaps what's not rebounding, or what's in the decline or steady-state.

Rakesh Khanna

Yes, Joe, in the Banking and Financial Services segment, we are seeing weakness. But clearly, what we've seen — definitely in the year 2017, we had seen a lot of headwinds, a lot of spending type discretionary decisions being pushed out. This time of the year as compared to same time last year, we see a difference.

The rate of decline has decelerated and the weakness that we are seeing is really in the — our view of Banking and Financial Services, which is limited to the payments, capital markets buy side and a little bit of corporate banking. Those are the 3 areas in which we operate.

So we see overall weakness in the discretionary spend. The traditional app development kind of projects are on hold, but we see a good uptick in the digital side of the business, which is also reflected in the overall Syntel digital revenues, which grew at 21% for the quarter Y-over-Y. So that's really the summary view along the Banking and Financial Services segment, Joe.

Operator

Our next question comes from the line of Maggie Nolan of William Blair.

Maggie Nolan

I was looking at your cash flows, and it seems like you've paid down a little more debt than usual this quarter. Can you talk us through your priorities in terms of your usage of cash? And then any update on your M&A strategy in that regard?

Anil Agrawal

So let's start with debt repayment. So we obviously paid down $85.6 million in this quarter. And our priority would continue to be managing our working capital in the best possible manner, and that would include the debt repayments.

Rakesh Khanna

On M&A, Maggie, we continue to look for a tuck-in kind of opportunity, which could either extend or add capability or enhance our geographic footprint. But our strength has been to primarily grow through organic means, and we do continue to evaluate options as we evolve and as we proceed.

Maggie Nolan

Okay. And then on your gross margin, that it came in kind of at the high end of your range for 2018 this quarter. Do your expectations for the full year still hold? And then over the course of the year, should we expect a similar pattern to pass through, where you have a little bit stronger gross margin in the second half of the year? Or what do you expect for 2018?

Anil Agrawal

So Maggie, we have guided to gross margin in the range — you could expect it within the range of 35% to 37%. And compared to the Q1, the rest of quarters would have an impact of the increments which we'll give starting 2Q.

And also as we have stated, all our investments which we have in our account coverage and the development of IP and digital and industry solutions and this also includes — and part of our strategy to invest in technology transformation and IP development. So second half will be more likely to be — as we move into the second half and we move during the year, we would let you know at that point of time.

Operator

Our next question comes from the line of Bryan Bergin of Cowen.

Bryan Bergin

I wanted to start on — Did the 1Q performance exceed your own internal expectations, and — call that seasonality — but is there anything else, any individual project that stood up for you as a driver? I'm just trying to reconcile your commentary around driving increased visibility in your guides, but then the outsized performance.

Rakesh Khanna

For the most part, Bryan, no outsized performance or — nothing got pulled in as a one-timer out there. We made great progress in Q1 on our 4 to 50 strategy. We improved the deal closures. We did a good job in terms of really executing very well. We saw the demand environment incrementally improve as the quarter progressed. And like I said in my earlier remarks, the combination also, because of this, we did not see the typical Q4 to Q1 decline, what we've seen in the past few years.

So by industry, we saw sequential growth and Y-o-Y growth across almost each industry, and we saw early signs of stabilization in the banking and finance vertical. Finally, digital was great. We have delivered a very strong 21.6% Y-o-Y growth. Europe also delivered, and our investment in that geography is also paying off very well. So we're really pleased about the overall execution and the opportunity, with the strong service offerings and our very good presence in our top 50 customers.

Zaineb Bokhari

If I could, just add one thing, Bryan. One other delta from when we introduced the outlook in February to now. That point in time, we were also not able to say specifically how we felt about the healthcare segment. And we did see some decent contributions. So that was the other — that was incremental as demand also improved, as Rakesh mentioned.

Bryan Bergin

Okay, that makes sense. And then just on operating margin. Can you comment on the margin profile of your digital work versus your non-digital work?

Zaineb Bokhari

On the service lines, including digital, we haven't provided a lot in terms of margin commentary. Clearly, the digital work that we do is high-value, high-bill services, and we feel very pleased with how that's growing, but we haven't made any statements about what the margin profile is.

Operator

Our next question comes from the line of James Friedman of Susquehanna.

James Friedman

It's Jamie. I was just wondering, do you anticipate any customers 4 through 50 piercing the 10% level this year?

Zaineb Bokhari

Well, Jamie, I don't know if that's an expectation that we would actually share on a call like this, but we certainly look at those names and they are Global 2000, high-caliber names. The spend is significant, and we've called that out before, and that's why we view it as a great opportunity. But the potential is definitely there. And that's why we see a great runway ahead and we're investing in expanding our footprint there.

James Friedman

Okay. And then I noticed you took up the margin guidance to 23 to 25 from 22 to 24, I think, is the math. What's contemplated there? Why — because some others in the industry are going the other way. Why do you have the margins moving higher?

Anil Agrawal

So Jamie, Q1 came in at 26%, and that is one thing, which has — to say that. And second, we continue to find ways to optimize our operations to see how we can continue to deliver strong profitability.

Operator

Our next question comes from the line of Joseph Foresi of Cantor Fitzgerald.

Joseph Foresi

I was wondering, just on the outperformance, was there 1 or 2 customers in the 4 to 50 batch that you saw an increase in demand? Was it around digital projects? Were there any kind of specific projects you were doing that caused the uptick? I'm just trying to get a little bit more color on what caused the beat.

Rakesh Khanna

Joe, digital, like I said, grew overall across multiple business segments, okay. So we saw a pretty solid uptick out there. In terms of specific verticals, we saw, again, B&FS, Banking and Financial Services, stabilizing. We looked at — we have a 0.4% growth Y-over-Y for banking; Retail, we saw about a 12% growth; Healthcare, 19; Insurance, 15%; and Manufacturing, 20%.

So if you see, it's fairly uniform, very good, barring Banking and Financial Services. Each of the verticals actually grew very well for us. And I will tie it back, Joe, to what we've been talking about the last few calls, our investments in strengthening our outreach in the top 50 accounts, specifically 4 to 50, then our investments in the service offerings in services led by SyntBots — powered by automation, the investments we do around IP and digital.

And this is a continuous process. All of those are resonating very well in the market, helping us to deliver a very strong quarter. And that's really also, if you see, we updated upgraded the guidance this time. So we really feel good about the business overall, Joe.

Joseph Foresi

Got it. And then secondly, would you expect the cost to be static throughout the year, excluding the wage increases? It sounded like the change in the margin profile is driven solely on what you see through 1Q, but I want to get a sense of your thoughts throughout the year.

Anil Agrawal

So Joe, usual things that comes into our financials after the Q1 is the visa cost that comes in Q2, and then the wage increases. And, of course, there are several other mix of the cost that comes into — in terms of our investments and those all our — what we do in terms of transformation and IP development. So I would say right now, as we speak, the gross margin to 35%, 37% and operating within 23% and 25% is where I would like it to be there, Joe.

Operator

Our next question comes from the line of Frank Atkins of SunTrust.

Frank Atkins

You did a very good job on SG&A. Can you talk a little bit about SG&A trajectory for the back half of the year? And maybe give us a quick update in terms of where the sales force sits in terms of skill sets and capacity and relative to the pipeline?

Anil Agrawal

So SG&A, I would say that we do expect that SG&A, we also could do well at 13% for the year. And as I said, we continue to invest in our business in terms of expanding our top 50 customer reach, and also into our sales and marketing efforts. So I would say the 12% to 13% range of SG&A, with operating margin of 23% to 25% is what I would say is the right way to look at it.

Frank Atkins

Okay, great. And then very strong performance in healthcare. Can you talk about some of the areas that are driving that demand?

Rakesh Khanna

Yes, Frank. In Healthcare, what we see is really a focus. First of all, there's a great demand in digital initiatives in Healthcare, okay. As the peers move over to more analytics, more consumerization, so improving the patient experience, overall. That definitely is a key priority.

The other area where we've seen more interest in the entire wellness preventive care, keeping patients out of the ER, driving low claims, improving the ratios in that area. But overall, also, what we see, there has been still some crosscurrents in Healthcare and Life Sciences. There's definitely less uncertainty related to the policy changes. And M&A seems to be taking a slightly different shape and form this year.

But despite all of that, we really see a good traction. And we do expect to see growth from definitely this vertical segment, Frank.

Operator

Our next question comes from the line of Dave Koning of Baird.

David Koning

Thanks for taking my question. And I guess, first of all, I know you mentioned the pace of growth this year seasonally is going to be a little different than normal. But I know typically, Q1 is not the highest revenue quarter. The way you're guiding this year is for Q1 to be a bigger number than kind of the average of the rest of the year. And can you just refresh us on that and why that might be?

Zaineb Bokhari

Yes, Dave, I would point you back to the comments that Rakesh made in his section about the other dynamics that we are seeing with — that is impacting our overall line of sight. The changes in our business with respect to some of the duration of engagements and deal sizes, and that's impacting our view on seasonality.

We've called this out before, because if you see other things that have been happening with Agile, the move to Agile, it's somewhat less dependent on big budget releases. So I think there are these factors that are causing us to say that we don't expect that traditional seasonality.

David Koning

Does that also mean then that you're guiding probably a little more conservatively than usual? I mean, the beat was pretty impressive. Just because you don't have quite the line of sight. So if things do come in kind of as planned, you might actually have more upside than normal just because you don't want to guide too aggressively?

Zaineb Bokhari

I don't think I would characterize it quite that way. I think that, certainly, this is something that plays a role in terms of what we see. But we've made some tweaks to our methodology. We're setting the ranges a bit wider and the visibility threshold is a bit higher. And this is really an effort to kind of try to capture some of this dynamic. We're not trying to be any different in terms of our methodology but adjusting some of these things to capture the new dynamics that we're seeing.

David Koning

Got you. And maybe just one quick follow-up on margins. Frank kind of asked about SG&A little bit. But you raised your overall margin by about 100 bps, operating margins. Is that more from the SG&A or more from gross margin?

Anil Agrawal

It's more from SG&A is what I would say. And there is also a factor of revenue coming in, as we increase our low end and higher end from $905 million to $920 million and $960 million.

Operator

Our next question comes from the line of Jason Rodgers of Great Lakes Review.

Jason Rodgers

Could you comment on overall pricing in the quarter as well as pricing for digital transformation and if you're seeing any material change in the competitive environment?

Rakesh Khanna

Jason, pricing at a company level, we are experiencing it to remain stable. There is some pressure on the run the business, which we are offsetting through more managed services and automation. On digital, we don't again break it down margins by service line, but definitely, the pricing that we charge and the price realizations we get for digital projects are on the higher side, compared to the traditional businesses.

In terms of competitiveness, I believe we have a very differentiated solution where we are focusing on the end-to-end digitization, which comprises of not only building the front end, but also Digitizing the process — helping our customers navigate their digital journey by also improving and modernizing their core platforms to be able to drive digital faster.

So again, our investments in IP, SyntBots, the digital stuff that we are doing with customers is definitely giving us a leg up. For example, what we've done is we have teams where we've implemented machine vision, free text search, deep learning, a lot of that stuff is resonating extremely well. And we believe we do have with SyntBots a first-mover advantage. So all of these, Jason, has positioned us fairly strongly. And I don't see a material shift in the competitive trends.

Jason Rodgers

Okay, that's helpful. And if I could squeeze one more in. Strong growth there in Retail, Logistics and Telecom, but the gross margin, on a year-over-year basis, was down fairly significantly. I think it's at the lowest level that it's been in a few years. I wonder if you could talk about the reason for that and what can be done to improve the gross margin there.

Anil Agrawal

So Jason, normal factors, usually, that generally impacts our gross margin is a combination of several, including the proportion of development and maintenance, the mix of on-site versus offshore and the underlying project cycles, the way it is. So, several combination of factors, and then as I would say, we continue to look at ways to optimize and deliver strong profitability. So this is where I would...

Operator

Our next question comes from the line of Puneet Jain of JPMorgan.

Puneet Jain

Hi. Good quarter. So you have reported such high upside to consensus revenue estimates over the last 4 or 5 quarters. And I understand your comments around lower visibility. But, given the magnitude of recent beats, could you share some qualitative comment, thoughts on second quarter revenue?

Rakesh Khanna

Puneet, first of all, the guidance, okay just to also clarify and explain. The lower end of the guidance is a function of visibility. And that's a fairly scientific method, and what we have talked about is that it is at 82% visibility of the committed revenues to be the lower end of the guidance.

Upper end of the guidance is a function of the deal closure of the probability of the pipeline closing when we have a very healthy pipeline. So that's how the guidance methodology stayed consistent. And like Zaineb said, we tweaked it to take care of some of the volatility by increasing the visibility percentages and also by widening the range. Okay, so that's how we've adopted the model.

Now the qualitative part, like I said, if you see the last call when we talked about budget in Healthcare and Life Sciences, we have talked about uncertainty. At that point in time, we were really not aware about which way is going to go. Now we have full visibility. We know that the budgets are finalized. We see them flattish Y-on-Y for the year. And the current visibility qualitatively, like I said, on Healthcare and Life Sciences, we see good demand despite the crosscurrents that we saw.

Funding is coming back. Projects which had been kept on hold due to the policy uncertainty is getting funded. And hence, we are definitely expecting good growth for the rest of the year. Similarly, in digital, in 4 to 50, in Europe, these are our areas as part of our strategy, what we already talked about. We do expect these to grow above company average.

Other verticals also, we see good strength except Banking and Finance segment, where we are again calling our weakness. We are talking about a recovery, which will take time. Although the decline has decelerated, okay. We did see a stabilization, actually, you see from Q4 to Q1, we did seem to stabilize, but it's at a lower level. So these would might be qualitative comments Puneet, and I hope that helps.

Puneet Jain

It does, it does. So it seems like you expect some growth in second quarter, given like demand being strong and all — and the comments that you made. And then second...

Zaineb Bokhari

Puneet, if I could interject— Rakesh's comment on our guidance commentary is all on an annual level. Given some of what we've described as far as what we're seeing out there, we are not going to provide quarter-to-quarter types of commentary. So these are annual comments.

Puneet Jain

Got it, got it. And some of your larger peers have talked about sacrificing margins in pursuit of growth. And given your margin levels overall are also above most peers, could you share your views on Syntel's longer-term margin profile? Can they stay in this mid-20s level, excluding any potential currency moves?

Anil Agrawal

So Puneet, usually, we don't provide long-term margin targets. I already gave margin expectation for the current year in which we are reporting. Having said that, I would assure you that we are focused to provide profitable growth over long term and running our business smartly. Very well, we see a need to invest or drive support for growth, we do make those investments.

Operator

Our next question comes from the line of Edward Caso of Wells Fargo —

Edward Caso

My question is around hiring in the United States and meeting those needs. What efforts are you doing on the localization of talent? Some of your competitors are fairly aggressive in that area. Could you also talk about maybe your level of H-1B interest, submittals this year relative to prior years, and also talk about wage increases.

Zaineb Bokhari

Sure, Ed. Some of what I'm going to say is going to be more far more qualitative than quantitative. I think with respect to visas and filings and things of that nature, we apply for what we think is an adequate number to meet our business needs. And this kind of ties into our local hiring and some of those efforts — we have a long-term plan to invest in local hiring invest in the infrastructure, develop some of the campus hiring programs here.

This is a long-term and multiyear plan, again, with the focus on making sure that our customers do not experience any interruption in their service delivery, regardless of policy headwinds. The last question around wage inflation, that's an update we'll provide next quarter, that's our normal pattern, as they go into effect, April 1. So we'll share that with you on our next call.

Operator

Our next question comes from the line of Mayank Tandon of Needham & Company.

Mayank Tandon

Rakesh, in the context of the growth in digital, what are some of the challenges you're seeing in terms of hiring talent on the digital side? And in the context of that, could you also talk about your expectations for wage inflation on that specific hiring pool and attrition expectations, given that there might be increased poaching from some of your larger competitors?

Rakesh Khanna

Right. In terms of the skill sets for digital talent, clearly, the demands are higher in terms of the roles that they perform, which is slightly more consultative, combined with architecture and domain technical skills and full stack programming background, okay? So what we do is we have — we dug deep into 2 options. Of course, we hire locally the talent from what's available in the market. But more important, we have — I had talked last year about — we've invested in a significant program around state-of-the-art learning management system with labs on of the cloud, which enables our current workforce, gives them an opportunity to re-skill themselves using computer-based learning, using digital labs on the cloud.

And we have these partnerships with Pivotal, Google and a lot of other players. So using our existing talent, redeploying them, enabling them, giving them an opportunity to re-skill because they have very deep knowledge of the client's current business, by virtue of the fact that they have been supporting either the middle office, front office or back office. So that helps us in building the supply chain for the digital projects.

Now definitely, there is a wage pressure just like we get higher rates for the digital projects. Clearly, there's an expectation to pay higher for those kind of skills. And then again, depending on the technical expertise or the depth, there are different compensation and promotion plans linked to the evolution in that journey for the associates.

From attrition, overall, what we've seen is, clearly, some folks would like to continue to stay on legacy skills, right? Not everybody would be interested to transition into the digital skills. And this is not just a Syntel issue. I believe this is more at an industry-level, what we are experiencing. Not everybody will be interested to move into a different paradigm. So that's definitely one of the triggers causing attrition. But having said that, we have maintained stable levels of attrition. And then we continue to sort of expect them to remain at slightly elevated levels until we reach a point where the skills have become much more mass available, versus a specialist kind of a role. So that's really the view.

Mayank Tandon

Right. That's a helpful color. If I could just follow up with one more question around the hiring pool. Do you anticipate over time that you might have to target other regions from a delivery perspective, whether it's Eastern Europe where you have some competitors on the digital side, maybe even Latin America? Do you expand your delivery hubs over time to be able to source talent?

Rakesh Khanna

That's a great question. And actually, we've already factored this. In fact, we run a global delivery. So in addition to delivery centers in India, which constitutes a large part of our delivery, but we, over the last few years, we have actually got development centers in Poland, Manila, Glasgow, and we have local centers, near-shore centers in the U.S. for the last many, many years, actually.

So it's a very resilient delivery structure, which is really a combination of on-site plus nearshore, onshore, and then offshore delivery, which enables us to provide uninterrupted service delivery, which enables us to get into a lot of local catchment areas to harness talent from the local regions, which strengthens our delivery, overall. So that's been our approach over the years.

Operator

Our next question comes from the line of Vincent Colicchio of Barrington Research.

Vincent Colicchio

Yes, question on the BFS side of things. So to what extent is the relative weakness client-specific versus the broader sub-verticals?

Rakesh Khanna

It is more broad across the sub-verticals. It's not client specific.

Vincent Colicchio

Okay. Question on the KPO business. You have a sequential decline in the workforce. Is that indicative of things perhaps slowing? I know last quarter, there was a big turn in labor, and you sounded a bit more optimistic on that business.

Zaineb Bokhari

So Vince, I'll provide some qualitative comments in terms of what we're seeing there, since we don't report that segment out for some time now. I would say that qualitatively, year-over-year and Q-over-Q, we saw a healthy trend for KPO.

Operator

Our next question comes from the line of Joseph Vafi of Loop Capital.

Joseph Vafi

Just a quick one, I know we've been talking about some of the shorter-duration projects and maybe in the digital area. Is there an impact to potential utilization rates and keeping them high, especially on-site if project durations compress?

Zaineb Bokhari

I mean, on-site, some of the digital work certainly is coming through, and you saw a pickup in on-site utilization. Rakesh, do you want to comment on the deal size?

Rakesh Khanna

Yes, the deal sizes, as digital percentage of our revenue increases, what we see is there are — there is variability in terms of the team size, structure and duration. The tendency is to fund an MVP, which is really a minimum viable product, launch it quickly in maybe 3 or 4 sprints, which could be maybe a 4, 5-month duration, go live quickly, test the waters and then fund the next release.

So that's been the nature of funding for digital projects leading to also what we are experiencing — a slightly shorter line of sight into the revenue visibility. That's one impact. In terms of the utilization, I would not correlate that directly. We have a strong bench on-site and offshore and nearshore, I talked about, which really is part of the overall supply chain. And with a good amount of planning, and then we have a good velocity in this area, I would not really link it to overall utilization.

Operator

Thank you. That concludes our question-and-answer portion for today's call. I'd like to turn the call back over to Rakesh Khanna for closing remarks.

Rakesh Khanna

Thank you, operator. I want to close today's call by thanking Syntel's employees for their contributions. I look forward to updating you on our progress on our next quarterly call. Thank you.

Operator

This concludes Syntel's first quarter earnings call. A replay of today's call will be available until April 26, 2018, by dialing (855) 859-2056 and entering the passcode, which is 4089007. Thank you, and have a great day.