

GDYN Q4 2023 Earnings Call Recording Transcript

Company Participants

- Leonard Livschitz, Chief Executive Officer and Director
- Anil Doradla, Chief Financial Officer
- Bin Jiang, Head of Investor Relations

Other Participants

- Maggie Nolan, Analyst, William Blair
- Ryan Potter, Analyst, Citi
- Bryan Bergin, Analyst, TD Cowen
- Puneet Jain, Analyst, JP Morgan
- Mayank Tandon, Analyst, Needham
- Joshua Siegler, Analyst, Cantor Fitzgerald

Bin Jiang, Head of Investor Relations

Good afternoon, and welcome to Grid Dynamics fourth quarter and full year 2023 earnings conference call. I'm Bin Jiang, Head of Investor Relations. At this time, all participants are in listen-only mode.

Joining us on the call today are CEO, Leonard Livschitz; and CFO, Anil Doradla. Following their prepared remarks, we will open the call to your questions. Please note, today's conference is being recorded.

Before we begin, I would like to remind everyone that today's discussion will contain forward-looking statements. This includes our business and financial outlook and the answers to some of your questions. Such statements are subject to the risks and uncertainties as described in the company's earnings release and other filings with the SEC.

During this call, we will discuss certain non-GAAP measures of our performance. GAAP to non-GAAP financial reconciliations and supplemental financial information are provided in the earnings press release and the 8-K filed with the SEC. You can find all the information I have just described in the Investor Relations section of our website.

With that, I'll now turn the call over to Leonard, our CEO.

Leonard Livschitz, Chief Executive Officer

Thank you, Bin. Good afternoon everyone and thank you for joining us today.

As you have seen from our published results, Grid Dynamics' fourth-quarter revenues were above our guidance range and exceeded Wall Street expectations. It was another quarter of solid execution and continued focus on our stated goals. The quarter witnessed a lot of activities both in the sales and CTO organizations, the two key areas within the company where we have invested significantly in 2023. On the sales side, our industry-centric efforts are paying off across all verticals. In 2023, we added 33 new logos, which is a strong testament to our differentiation in a year, where customers were more selective to award business to digital providers. With respect to the CTO office, our scientists and architects are heavily engaged with clients across the spectrum of innovative solutions, including AI, to drive meaningful business outcomes. To that end, we released several new functional accelerators across industry verticals, which have resulted in greater engagements across both new and existing



customers. In supply-chain, manufacturing, pharmaceutical, and financial services, areas of focus with our GigaCube initiative, the ability to offer unique and differentiated offerings has resulted in accelerated acceptance across a wide range of customers.

To support the strong demand for AI skill sets, we established comprehensive AI training programs. I am happy to report that over 25% of our engineers are trained in Generative AI. Our AI curriculum is rigorous and is segmented across three tracks and ranges from introductory AI to more advanced topics. It may take up to several quarters to complete the entire curriculum.

On the macro front, I am happy to report that the demand environment is improving. The demand trends are directionally consistent with my commentary over the last couple of quarters. While we are yet to get back to normalized levels of growth, we are moving in the right direction. In many ways, the sequential growth with our first quarter revenue guidance reflects our sentiment.

We are seeing positive trends with four company-specific factors.

First, we see customers either choosing to maintain their current levels of spending or moderately improve with increases in investments. While we witnessed a similar trend last quarter, the fact that customers demonstrate more stability is an important step in getting back to historically normalized levels of growth. This is reflected in the steady rise in billable headcount trends from our existing logos.

Second, drops in revenue across some of our large existing customers are moderating. To put it in perspective, in 2023, the considerable revenue headwinds we faced, were limited to a handful of existing customers. We anticipate this trend will diminish in 2024. This bodes well for the company's growth in 2024.

Third, our partnership-driven revenues are growing steadily. In 2023, roughly 13% of our revenues came from partnerships. We accelerated the investment into partnership programs a couple of years ago. I am bullish on expanding and monetizing more partnership opportunities in 2024 and beyond.

And finally, fourth, our new logo momentum. In 2023, we accelerated investment into a broader, industry-specific created a dedicated sales team to pursue new logos and opportunities. We expect this to continue to be an important component of our growth in 2024.

Our Follow-The-Sun strategy has been successful with our clients. Today we serve our customers from 18 countries and our global footprint fully aligns with our customers' needs.

Now coming to the first quarter of 2024. We are almost two months into the quarter and the commentary that I have shared with you today extends to the first quarter too. Our billable headcount continues to grow, our AI activity is robust, and the headwinds from a handful of clients continue to diminish. We believe underlying trends are moving in the right direction.

As we enter 2024, our CTO organization is highly focused on expanding our capabilities highlighted in our GigaCube strategy. This includes building new R&D innovations, accelerators, and AI solutions. During the fourth quarter, we made good progress with POCs and customer projects related to AI. Our internal R&D innovation lab, which we call Grid Labs, has generated several functional accelerators and AI-related artifacts. Today AI is infused across practices and industries. Customers representing over 80% of our revenues are engaged with Grid Dynamics on AI initiatives and more than 50% of our new engagements have an AI component. These include industry verticals beyond where we have historically been strong, such as supply chain & manufacturing, financial services, and pharmaceuticals. Some of our new AI innovations include pricing applications, IoT Analytics, visual quality control, and industrial vision LLMs. As a reminder, Grid Dynamics AI engagements are based on



more than seven years of internal research and successful implementations. With our generative AI offering, we partner with customers to employ large language models in a variety of applications. These include prompt-guided image generation, product design & visualization, knowledge retrieval, wealth management, and customer support.

In the fourth quarter, there were several trends and I want to share with you some of them:

Logo Momentum: In the 4th quarter we signed 5 new enterprise customers. This brings the number of new enterprise logos in 2023 to 33. This is a record number of new logos for us and is a testament to our reputation with large global enterprises. Of the new enterprise customers we signed in the quarter, one is the largest omnichannel specialty retailer, one is a large insurance company, and one is a software company focused on revenue management for the healthcare industry.

Delivery Location support: Our “Follow-the-Sun” strategy continues to be the guiding principle in enabling our clients to be served in an uninterrupted fashion around the clock. I am proud of our ability to serve our customers across 18 countries spanning across North America, Europe, and India. In India, I am happy to report that we are opening an office in Bengaluru. This brings the total number of India office locations to three, which includes Hyderabad and Chennai. Our clients have successfully engaged with Grid Dynamics in leveraging our presence in India. In Europe, we continue to expand our footprint in Poland and Romania. In Poland, our growth is increasingly driven by partnerships with the clients’ local centers. With respect to our recent acquisitions, we will complete all the engineering integrations by the end of Q1.

Europe Business: Europe continues to be strategic to our growth. In 2023, our revenue from Europe was roughly 20% of our total revenue with customers across industry verticals. During the quarter, we made good progress in expanding our footprint across industry verticals with our existing and new European clients. To highlight some notable achievements during the quarter. Let me point out that, with a leader in legal and tax services, we are partnering to use GenAI technology and build a global data platform to accelerate the ability to serve their customers with reviews and publishing of contracts. At a large UK-based retailer, we signed a multi-year contract to modernize their e-commerce platform. At a global auto parts company, we expect to roll out their composable commerce modernization platform across other brands within Europe. For a large medical device company, we are launching initiatives in data engineering and Generative AI. The goal is to enhance the efficiency of sales reporting processes. And finally, at a large clean energy company, we are enhancing their sustainable ESG initiative.

Partnership: As I have highlighted before, partnerships are increasingly playing an important role in our growth and our long-term plan towards becoming a billion-dollar company. Let me remind you, in 2023, partnerships contributed to 13% of our overall revenue. Again, this is impressive given that we embarked on this strategy in 2021 and within a short period of two years we have achieved these impressive results. Notably, with our partners, AI is becoming a core element of our joint go-to-market strategy. Looking forward to 2024, we have strong momentum with Hyperscalers and leading digital commerce SaaS companies as well as other specialized software providers. Our focus is to capture greater wallet share.

GigaCube initiative: with GigaCube, we continue to make good progress. As you know, GigaCube is our strategic blueprint that lays out a framework for our company towards a billion dollar in revenue. We operationalize the GigaCube via four key areas. Knowledge Management, Partnerships, New Vertical Focus, and winning larger deals. On each of these fronts we made progress, both in the fourth quarter and full year 2023. With our Knowledge Management efforts, we have cataloged over 100 important delivery case studies that are being used across pre-sales, sales, and delivery organizations. This is important. We accelerate the proliferation of our learnings from each project and program to ensure that the whole company benefits from it.



During the quarter, Grid Dynamics delivered some notable projects.

For a leading global technology company, Grid Dynamic enhanced the recommendation engine of one of the largest online streaming services. We successfully implemented cutting-edge Machine Learning heuristic techniques to enhance the quality of data used by the recommendation engine. Our engagement covered end-to-end Machine Learning processes, including model engineering, evaluation, deployment, and post-production efficacy monitoring. This resulted in significant improvement in the relevancy of recommendations and the system's capability to self-adjust in real time.

For one of the largest auto part distribution & retail companies, Grid Dynamics has been actively engaged in the modernization of the product catalog, which enables search and browse functionality. Our solution uses Generative AI to correct product images, generate descriptions, correct categorization, enhance attributes, and highlight discrepancies in product details. As a result, this client expects to improve customer conversion and user experiences, leading to increases in sales across both B2B and B2C channels.

For a multinational financial service provider, Grid Dynamics leads a cyber-security program to onboard 400+ custom-built applications to Sailpoint IdentityIQ platform. This solution enables our client with a full lifecycle of Identity and Access Management, ensuring proper duties separation to meet the latest security and compliance standards. We expect to expand this project during the next phase and onboard another 1000+ applications to the platform.

For a global automotive manufacturer, Grid Dynamics developed a cloud-native e-commerce platform based on a robust Microservices architecture. This platform enables an intuitive end-to-end user experience and promotes in-house financing to car shoppers, which anticipates to increase the vehicle sales through the digital channel.

With that, let me turn the call over to Anil, who will discuss Q4 results in more detail.

Anil?

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Anil Doradla, Chief Financial Officer

Thanks, Leonard. Good afternoon everyone.

Revenue commentary

Our fourth quarter revenue of \$78.1 million was slightly ahead of our guidance range of \$76.0 million to \$78.0 million and exceeded Wall Street expectations. On a sequential basis our revenue grew 0.8% and was down (3.1)% on a year-over-year basis. Relative to the last quarter, we saw greater stabilization across the majority of our accounts.

During the fourth quarter, retail, our largest vertical representing 31.5% of our revenues, decreased by (7.4)% on a sequential basis and by (4.2)% on a year over year basis. On a sequential basis the decline was largely from specialty retail offset by strength in home improvement. TMT, our second largest



vertical represented 31.0% of our fourth quarter revenues, grew 1.9% on a sequential basis and decreased by (10.9)% on a year over year basis. On a sequential basis, the growth was largely driven by some of the large technology customers.

Here are the details of the revenue mix of other verticals. Our CPG & Manufacturing represented 12.4% of our revenue in the fourth quarter, flat on a sequential basis and a decrease of (31.3)% on a year-over-year basis. During the quarter we witnessed stabilization at our largest CPG customer and growth at other customers. The Finance vertical represented 10.6% of revenue, an increase of 13.4% on a sequential basis and 32.6% on a year over year basis. The growth in the quarter came from a combination of financial technology customers and new logos. And finally, the Other segment represented 14.5% of our fourth quarter revenue and was up 11.5% on a sequential basis. The sequential growth was driven by strength across multiple customers, some of them in the healthcare, restaurant industries.

Headcount Commentary

We exited the fourth quarter with a total headcount of 3,920 versus 3,823 employees in the third quarter of 2023 and up from 3,798 in the fourth quarter of 2022.

At the end of the fourth quarter of 2023, our total US headcount was 331, or 8.4% of the company's total headcount. This remained on the same level compared to the third quarter of 2023 and slightly decreased from 8.9% in the year ago quarter. Our non-US headcount, located in Europe, Americas, and India was 3,589, or 91.6%.

Customers

In the fourth quarter, Revenues from our top 5 and top 10 customers were 39.7% and 55.3%, respectively, versus 43.2% and 60.4% in the same period a year ago, respectively. We witness continuous diversification and greater contributions from our recently acquired logo.

During the fourth quarter, we had a total of 218 customers down from 224 in the third quarter of 2023 and flat in the year ago quarter. The declines were largely from our commercial customers offset by growth in our enterprise customers.

P&L Commentary – GM, EBITDA, and EPS

Moving to the income statement, Our GAAP Gross Profit during the quarter was \$28.1 million, or 36.0%, and remained flat compared to \$28.2 million, or 36.4% in the third quarter of 2023 and down from \$32.3 million or 40.1% in the year ago quarter. On a non-GAAP basis, our gross profit was \$28.6 million, or 36.6%, versus \$28.7 million, or 37.0% in the third quarter of 2023 and down from \$32.7 million, or 40.6% in the year ago quarter. The decrease in GM% on a year-over-year basis, both on a GAAP and non-GAAP basis was largely due to a combination of FX headwinds, costs associated with expansion into new geographies, and other investments.

Non-GAAP EBITDA during the fourth quarter that excluded stock-based compensation, depreciation and amortization, restructuring and expenses related to the geographic reorganizations, transaction and other related costs was \$10.7 million, or 13.7% of sales versus \$10.7 million, or 13.9% of sales in the third quarter of 2023 and down from \$16.5 million, or 20.4% of sales, in the year ago quarter. The year



over year decline in non-GAAP EBITDA as a %age was largely due to a combination of decline in gross margins, increase in operating expenses related to acquisitions, and investments into our sales organization.

Our GAAP net income in the fourth quarter totaled a \$2.9 million or a \$0.04, based on a basic share count of 75.7 million shares, compared to the third quarter income of \$0.7 million, or \$0.01 based on a basic share count of 75.5 million and a loss of \$(6.7) million or \$(0.09) per share based on 74.0 million basic shares in the year ago quarter. The year-over-year increase in GAAP net income was largely due to lower levels of stock based compensation and significant decrease in geographic reorganization costs. On a non-GAAP basis, in the fourth quarter our non-GAAP-NI was \$5.7 million, or \$0.07 per share based on 78.0 million diluted shares, compared to the third quarter non-GAAP NI of \$5.9 million, or \$0.08 per share based on 77.3 million diluted shares and \$10.5 million or \$0.14 per diluted share based on 76.5 million diluted shares in the year ago quarter.

Balance Sheet

On December 31, 2023, our Cash and cash equivalents totaled \$257.2 million, up from \$253.7 million in the third quarter of 2023

Q1 Guidance

Coming to the first quarter guidance, we expect revenues to be in the range of \$77 million to \$79 million. We expect our Non-GAAP EBITDA in the first quarter to be in the range of \$9.5 million to \$10.5 million.

For Q1 2024, we expect our basic share count to be in the 76.5 to 77.5 million range and our diluted share count to be in the 78.5 to 79.5 million range.

That concludes my prepared comments. Bin, we are ready to take questions.

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Questions and Answers

Bin Jiang: Thank you, Anil. As we go through the Q&A session of this call, I will first announce your name. At that point, please unmute yourself and turn on the camera. Our first question comes from the line of Maggie Nolan from William Blair. Maggie, your line is open.

Maggie Nolan @ William Blair: Hi. Thank you. Appreciate the update. The business sounds really solid, so congrats. I know you only guide one quarter at a time, but at this point in the year, I'm wondering if there's any visibility, anything you can share with us, either quantitatively or qualitatively, about how the second quarter is coming together and beyond if there's anything to comment there?

Leonard Livschitz: Thank you. Thank you for your question. Well, it's interesting to start with the ramp-up of 2023, as we talk about six months going forward. But you probably sense the tone of conversation that we are a bit on a rebound and we do sound optimistic. I would say that without



going into all the details, because the environment is still a bit of a complex. I would say that the -- I expect Q2 to be our new high watermark in terms of our revenue position at all time. Now, it doesn't sound a lot today, but if you look at the last 12 months, I think we are kind of getting ourselves back to shape to the normalized growth.

Maggie Nolan @ William Blair: Okay. Great. And then, great to see that new logo commentary, the -- the additions that you've had. I'm curious what we can expect from those in terms of the revenue ramp and the margin contribution as we see those accounts ramping?

Leonard Livschitz: So, the -- as you know, our model, probably it's a -- it's a little bit beat out by now. It's 85, 10, 5, right? But this 5% is turning to be a little bit more predictable and to some extent, the 10 as well. So, the -- the larger logos, which we grabbed upon in now -- in last quarter, the quarter after, they ultimately are a bit more defined in terms of the project-based rather than broad-based. So there's a little bit better anticipation of the ramp-up of their logos.

Saying that, again, that gives me the -- the confidence for some of the upswing for the company. But also I see them return back to the positive momentum on our existing logos. I think the question on the new enterprise logo, the winnings in late 2023 and what we already have actually in 2024 combined with some of the brands with the larger existing customers, gives that level of optimism.

Maggie Nolan @ William Blair: Thank you.

Leonard Livschitz: Thank you, Maggie.

Bin Jiang: Okay. Thanks, Maggie, for your question. Next question -- question comes from Ryan Potter from Citi. Ryan, please go ahead.

Ryan Potter @ Citi: Hey. Thanks for taking my question and good quarter here. Want to start on head count. It's good to see head count growing sequentially on an organic basis in the quarter, but can you help reconcile the flattish sequential growth in the 1Q outlook versus headcount growth? Is it attributed as more of a sign of you seeing a demand recovery coming later in the year? And then, also, any color you can give in terms of where you're growing headcounts, whether be it in India or any other geos?

Leonard Livschitz: Well, a lot of questions from Ryan, you're getting demanding, right? So, let me start with the last, because it kind of rolls back, right? So you noticed from even our press release, we indicated a bit of a shift in terms of the diversification. We see more on the rate of growth in, what I say, non-retail verticals or non-retail customer verticals. It doesn't mean we're moving away from B2C. It's all B2B business. But the skills and capabilities and the more traditional skill sets in data management, cloud migrations, the -- the bespoke tooling partnerships mentioned that combined with a new developed applications related to the AI technologies, and that's a separate point of discussion. Everybody is asking that, right? This gives us a bit more upswing on the fintech, on the pharma, we see more in the TMT, the tech segment. So that gives us a bit more of a, I would say, continuation of the growth. So that -- that -- and again, those sectors are a little bit less volatile, given the economy has not been stable again.

And the first part of the question I believe you wanted to know specifically... can you just give me a little bit more...

Ryan Potter @ Citi: Yeah. So the headcount growth versus the flattish outlook sequentially is a -- is it a sign of demand in headcount later in the year?

Leonard Livschitz: Right, right, right. So -- so this is about reading on tea leaves, right? So, the growth of the headcount happens in India. That's one area, as we mentioned, again, is picking up. I think that our customer base has grown with an understanding of our versatility of the follow-the-sun strategy. What it means? It means that, Grid Dynamics provides the same quality level of services, whether we're in Europe, in Latin America or in India. And access to talent in India is a quite larger from the market, but everybody is there. So as you see the little bit of uptick. Part of it -- it's a little bit longer time to bring the talent in India. And so, we need to start building the pipeline there.

Not saying we're -- we're going to reshuffle some of the people in Europe. There's -- there are many activities there, but that's where the -- the growth comes in. And it just requires a bit more the -- the capable people and also if you notice, we talked about in our presentation about rigorous training program, right? So I mentioned that it takes that up quarter to bring the talent up to speed with the new tools and capabilities, specifically in the AI/ML sector. So it's an investment of the, I would say, rounding the people and building the pipeline of capable technical execution folks. And India is at the forefront.

Ryan Potter @ Citi: Got it. And I agree that was good to see the sales momentum continue in the quarter. But as the demand environment stabilizes and your existing client base, we -- should we foresee any changes to your sales strategy in 2024? We have to shift more to sales or more to kind of expansion with clients versus hunting new logos or are you able to continue to balance both our efforts?

Leonard Livschitz: Well, that's one of the area which you again noticed from our conversations was the point of investment in 2023. It's a -- it's a bit -- it's a bit, I would say, so let me be ambiguous. When the company invested into R&D and sales during the year have been flat, right? But at one point of time it's -- it's been beneficial to reach for the resources when they're available in the market, right? So when the market is a bit stagnant, you have a broader selection of the talent.

On the R&D side, it takes more time for people to come to speed, both on the architecture side, SME side, read the materials, industry-specific artifacts, accelerators. So, when we talk about sales, it's a combination of sales and technical pre-sales and personal level of engagement. When it comes to the hunting per se, we actually have a hunting capability for the first time. Typically, as a company -- we're still relatively small to compare with many, many others. So we -- we're focused on a diversity of the responsibilities for the same individuals. Right now, we have dedicated sales force, people in the United States with the hunting excellence, but we also doubled down on farming new business lines within existing large accounts. So that's pretty much based now.

The proof is in the pudding. But I think even though we a little bit sweated the margins last year, I think that gives us a bit more runway, not just kicking the can to the second half of the year, talk about 2025, but more immediate targets as early as now.

Ryan Potter @ Citi: Great. Thanks again.

Leonard Livschitz: Great. Thank you.

Bin Jiang: Thank you, Ryan. Next question comes from the line of Zack Ajzenman from TD Cowen. Zack, please go ahead.

Zack Ajzenman @ TD Cowen: Hey, thanks. Zack Ajzenma on for Bryan Bergin. First question we had was just on the -- the overall demand backdrop. So good to hear more of the stabilization commentary evident in the Q1 guide. I was hoping to further dig into the dynamics that have actually changed from three months ago. Is it just the higher prevalence of more optimistic client conversations? Or have you seen a change in -- in actual signings or willingness to go ahead with new programs? Just trying to get a

better sense of recent client behavior and how that's informing your view into 2Q, which sounds like it's going to be even -- even better than what we're seeing into 1Q.

Leonard Livschitz: Really, Zack, well, you have -- you have to fill big shoes, because Bryan is one of the most talented analysts, so welcome. The -- the question is about what is really happening in the forefront of our business. And as you know, traditionally, at least from Grid Dynamics perspective, from our client perspective, there is always a, what they call, the -- the -- the bit of a turnover from the projects and -- and business directions between the late Q4 and early Q1. That's kind of I wouldn't call it a pitstop, but it's really more than just budgets, the reassessment of their own performance tuning the business, and a lot of disruption that happened with AI tools. So we had to go last year and start making a lot of proposals, on how to get viable conversion of their top line with a more economic budget leveraging various AI technologies. And again, it's not just you plug in, and check button, it gives you more money, right? So it's a very complex process of using private data and public in various clouds. Our Grid Dynamics know-how and understanding of their business are based on previous expertise, even in machinery -- traditional machine learning to AI. So, we see the conversion on a contractual basis. I think that's very important. So not just the awards.

Again, we're still in February and we are not completely out of the spirit of retooling of our clients, but the -- the new logos and existing logos on the demand side are contractually driven. So we're not talking just about the proof of concept that's run another one, two or three months of the test what are the initiatives to trend out. On -- the is -- this is on the B2C business. On the B2B business, it's a bit different, right? Because the -- there is no more like people understand that new technology, first and foremost need to bring them better results and their models is not as trivial, because it's a complex of supply chain logistics, the demand on the various products. So that business is probably going to kick in a little bit more in the later part of this year because there's still more in the steady state of learning and adoption. But because we have both markets, we see an immediate remuneration as well as potential upside with existing clients.

Zack Ajzenman @ TD Cowen: That's helpful. Maybe we are at the margins. We were hoping to dig into the factors that have been weighing more recently. How long are these items expected to be headwinds? And what are the controllable levers that Grid can pull to partly insulate, including maybe any color around pricing or utilization?

Anil Doradla: Sure. So, Zack, again, that's a loaded question. There are many moving parts of it, right, from COGS's point of view and OpEx's point of view. I'll let Leonard talk about the pricing, but let me talk about a couple of moving parts as we move in the course of the year.

Now, year-over-year, you've seen the difference rate on our gross margins. Half of it came from FX, the other half of it came from the fact that we've expanded into some of these new geographies and there's a certain cost structure in there. If you look at our OpEx, 2023, as Leonard pointed out, was a year of investment, because we are investing into our future.

As we move into 2024 and beyond, let me talk about OpEx and we'll talk about cost. On the OpEx front, the focus for me internally is to keep the growth rate lower than the revenue growth rate. So you're going to see leverage on that front. Now, there will be times when you'll have to invest, but that is my focus right now.

On the COGS side, as you can see, we're in all these different geographies. We're scaling in each of these geographies. And as we scale into some of these geographies, some of them identified in all of the sub-strategies, you're going to get some benefits there. But as far as the -- the focus again is obviously go back to customers, but operationally also reorganize ourselves. We have T&M, we have pods, we have fixed prices, and we have the pyramid. There are so many operational aspects which we can work on.

And Leonard, do you want to talk about pricing?

Leonard Livschitz: You just covered it. I don't want to double down. Actually, I want to walk you a little bit, Zack, on a visualization on pricing to cost and back, because there are two things actually very well connected with each other. In order for us to get to the higher profitability, it's not directly margin-related, but it's contract-related, right? So, pods, fixed bids, the delivery performance associated with a certain major milestone, expanding budget signing now longer-term budgets, we see that happening. It doesn't mean that individual rates, for example, are going to be aggressively moving up. I mean, the market is still, I would say, demand-driven and -- and supplied. And the value we're bringing while we're increasing some of the basic rates, we're offering more and more systems, which I just described with, which Anil pointed out, which ultimately brings a better architecture of the team structure. In other words, within the team, our cost-benefit is evident to us, but for the customer, it's result-driven. So they're getting better efficiency with understanding their pocketbook spending without constantly going back and forth and looking at each individual rate. In many cases also, we gained the trust of the customers sufficiently that they allowed us to pick a proper team formation and it's getting more and more in the scale. That also helps to all the -- all the efficiencies right, moving from Eastern Europe to Central Europe, scaling the number of offices. Opening the offices in India. That's well understood.

But our model of 40/20, no matter how difficult it sounds today with where we are, it's a relentless pursuit. And I see the trend is coming. The numbers, can't say there yet, but judging by the contracts we're signing, I'm quite bullish.

Zack Ajzenman @ TD Cowen: Thanks for all the color.

Leonard Livschitz: Thank you.

Anil Doradla: Thank you.

Bin Jiang: Thank you, Zack. The next question comes from Puneet Jain from JP Morgan. Puneet, your line is open.

Puneet Jain @ JP Morgan: Thanks for taking my question. I wanted to ask about GigaCube. It looks like great progress in financial services. The vertical was up nicely. Can you also share the contribution from other verticals such as healthcare? And do you plan to share progress like you make in India and Europe, as well as smaller verticals on a quarterly or annual basis there?

Leonard Livschitz: Anil, why don't you talk about it...

Anil Doradla: Deeper. So as you see, the other segment was about 14.5%, right? And that had a nice growth. So what you're going to see starting from next quarter, we're going to break down the other segment, because we're going to have the healthcare part. So, healthcare, life sciences, that's becoming an increasingly bigger part. That has actually been one of the contributors to our growth.

And as we evolved in the course of the year, some of the sectors that you talked about, financial services, I mean, there's a lot of activity going on there. And we're bullish on that.

Leonard Livschitz: So Puneet, that's a formal way -- informal way. I like to have statistical significance before I acclaim the flag at the top of the hill. I can tell you confidently, that in the fintech world, our investment is turning to factual material improvement.

When we talk about pharma and health care, the number of accounts is growing. But I can't say that we are a dominant player yet. We understand the capability. We're learning new ways of adding business value. You will see that trend. The wealth management and insurance part of BFSI, right, you know for a long time, we had one very large partner in wealth management. That those things will grow too.

And why we grow is because you guys to some extent helped us to assess four years ago that what does it mean to be a public company, right? And you need constantly to challenge yourself not just on the growth, but on the hedge, right? How you build the business? So we were very heavily depending on the bricks-and-mortar. So that's a long history we were having depending on certain brands. And again, it's a history.

The tech is also diversifying. But I would give the more specific material that comes in when I see at least two-quarters or three-quarters of the consistent signing of new clients. And I think the biggest right now division for me is B2C application, B2B application. We will continue to break it down. As I said, we feel that they are statistically significant.

Puneet Jain @ JP Morgan: Got it, got it. That's very helpful. And let me ask like second question like, so now that macro headwind appears to be behind you and you're seeing stabilization in some of the large customers. So some of those like the largest of your large customers, like I think they peaked at somewhere around like \$30 million, \$35 million, maybe \$40 million. Like how high is the addressable market at those clients? Like, how large those customers can get, given your current service mix?

Leonard Livschitz: Yeah. Actually, you're getting into trouble. All right. There is quite a bit of a ceiling on those clients. Why? Because we're changing our Tier 2, right? Maybe the market cap is still not there, but we're a much more mature company, not just from a performance perspective, but the stable capability perspective and resilience perspective, right?

Every client, every large client... They look not just into the internal supplier capability, but as you know, again, hedging against certain unforeseen events, right? So I think they're getting more comfortable with our reach and with our touch, right? So I would say that the ceiling is less driven by our capabilities, which are proven and more are opening up when people are starting to become comfortable. Coming back to the GigaCube stage that one day we are a billion-dollar company. So yeah, if you -- just from that perspective, I'm not going to throw a number of \$100 million account today. Again, it would be a bit premature, but there is nothing that stands between us and having a number of accounts which are in that \$30 million to \$50 million range right now. And then, they'll tell us how much we can go further.

Having just one account, being so much bigger than everything else, that's another bit of a challenge. So we're seeing others struggling. So we want to do not only diversification on the verticals and the skill set but heading large driven partners to be somewhat diversified as well.

Puneet Jain @ JP Morgan: Yeah. I totally agree. Multiple clients that are comparable in size I think we totally get like that's unique. Appreciate the comments. Thank you.

Leonard Livschitz: Thank you.

Anil Doradla: Thank you, Puneet.

Bin Jiang: Thank you, Puneet. The next question comes from Josh Siegler from Cantor Fitzgerald. Please go ahead.

Josh Siegler @ Cantor Fitzgerald: Hi, guys. Thanks for taking my question today. Nice to see the strong KPIs in the quarter and business stabilization throughout this more difficult macro period. I wanted to

touch on the partnerships specifically because they seem to be a big contributor over the past year. How are you thinking about how partnerships will contribute as we progress through 2024 with a more positive macro potentially at our tailwind? Thank you.

Leonard Livschitz: Well, I'm glad you pointed out that. I mean, we tried to repeat the favorite number 13. Enough, long enough for people to memorize it. It would be not as exciting with 12 or 14. But anyway, the factor that Anil mentioned of having just a few years behind the belt is not truly about the partnerships per se. I mean, we always have partners. I think there are a couple of fundamental changes that happened a couple of years ago. The number one is we realized that sitting only on open source is not enough to increase the breadth of the customer relationships. We need to become a bit of an advisory on a buy and build as a combination. So, it's a step. It's basically a stage of maturity, right? You -- everything requires investment. So, it's not only about hyperscale, it's also about the ability to stitch multiple sort-through products. So we started with areas where we have done most of the work, which is commerce. We've done major progress both in Europe and in the US and we're expanding the number of the products we own. So that point is very clear. So, it's not just open source to the companies.

The other one is going back to hyperscaler, right? The hyperscalers represent a very complex system, right? And you come in and knock on the door and ask them, give me the clients, typically it goes backward and you bring the client will see, right? I'm not going to report that. It goes two ways. When you turn two ways on top of building the capabilities and contributing to the hyperscalers themselves, then you start getting the tractions, because it's a joint client effort. So not only understanding the systems, but understanding the customer's ability to have us as a partner of choice, not just the integration partner. Let's just address this number now.

How big is the number going to be? Honestly, I can't tell, because we're going into new verticals. And again, it's an investment, because you can just come up with the open source and drop all these ideas on the laps of the big decision maker in other verticals. But it is certainly the model which we are extending at this point.

Josh Siegler @ Cantor Fitzgerald: Understood. Appreciate that color there. And then, Anil, real quickly, can you give us an update on how you're thinking about capital allocation as we progress through the year? Thanks.

Anil Doradla: Well, look, I mean, the focus obviously is M&A internally. And I know this is a question that comes up very often. The -- at any given point, we're evaluating. Obviously, we will tell you when we actually get something done. But the priority, obviously, is our cash usage is going there. Beyond that, it's all about cash generation. It's all about ensuring that we get back to our 40/20 and we convert it, right? I mean, as you know, we don't have any debts on our balance sheet. But it's these are the two elements in terms of how we're looking at our balance sheet.

Leonard Livschitz: And just to get a little bit of color on M&As. I know you've been patiently waiting for us. I mean, it's been a long time since we collected enough funds, right? And our cash generation exists, but it's not super large. But we sit on a nice pile of cash. So we completed all the conversions again if you look at our press release and the reported once, so we have no lingering issues or necessary investments into any of those four acquisitions we've done. It's all integrated, not converted by now. And we're, I mean, integrating and integrating both sales and engineering. Engineering sometimes takes a little bit longer on the skill set.

So we are exploring deals across all these verticals and geographies. Again, there is a range. Obviously, we're not going to burn all the money in one swoop, but it has to be more focused on skill development. So we're big enough to train people in what we know. Some customer acquisition obviously is good, but we really want to add the skills in the AI revolution part, right? So there are new



areas which open up by building those skills. So it's not about just the marketing, because we understand what we're good at there, what it makes sense for us to complement with acquisition. So that's kind of a shift you may see from like six months ago.

Josh Siegler @ Cantor Fitzgerald: Great. Thank you. I really appreciate the color. And thanks for taking my questions today.

Leonard Livschitz: Thanks, Josh.

Anil Doradla: Thanks, Josh.

Bin Jiang: Thank you, Josh. The next question comes from Sam Salvas from Needham. Please go ahead.

Sam Salvas @ Needham: Thanks, Bin. And thanks for taking the questions, guys. Most of my questions have been asked, but are there any related metrics or anything you can share in terms of the number of projects or engagements, or logos? Just any color you can give us to get some kind of sense of the demand you guys are seeing from AI?

Anil Doradla: So the question, Sam, was what are the AI-related metrics, right? And so, Leonard is the AI expert, but I'll tell you that from my point of view, when I look at the activity, right? We talked about it in the Analyst Day, and in the press release, also we talked about there's a lot of activity going around with both existing and some of our new.

What I am very impressed with is that many of our new engagements have some level of AI component to it. So there is a lot of interest where AI is infused across our practices. But if you're talking about what are we going to reveal the standalone revenues and everything when the time is right, we'll do that. But AI is pretty active across the company.

Leonard Livschitz: Well, I'm glad that Anil stepped in because I wasn't sure exactly what you were asking. Sorry about that. Now, that I know, I can tell much a little bit more color, right? So, first of all, the areas where we have progressed a lot, it's conversational AI, it's recommendation AI, catalogs, and compliance. We do quite a few of the forum solutions. What happened is leading expertise in the verticals, especially things that relate to e-commerce, but now it's growing helps us to tune the proper models, help get the visual parts, help us to guide the internal client marketing and business teams to understand the ability to reach certain business results.

The number of cases is growing for a very simple reason. They are factual. The models change. The conversion rates are changed. We can't promise results unless the client understands the reasonable targets. So the catalog and the understanding of their existing environment, leaning out of their codes, sometimes switching from their old models to the model. First, we need to get the code capable of accepting the new things. So we do that conversion to augmentation and of course, very close work with all the offerings related to the AI models on the cloud as well as the you know common standalone solution. So I'm sure we'll do more, more presentation webinars. You guys can look at our website. We have a ton of demos, but those demos typically are something open to people to look at.

I had a question about why one of the press releases we did with a certain client and certain project mainly because a lot of the work is so cutting edge of the front of the customer DNA that we're grateful to the ones who are willing to open to share, but many more are preferring to maintain the total proprietary approach to their goal.

Sam Salvas @ Needham: Yeah. Well, that's helpful. And then, just one quick follow-up from me. The weakness in the retail vertical this quarter. Was that one larger specialty retail client or was that kind of broad-based?

Anil Doradla: So the question Sam, because the volume is not clear, your question was we talked about...

Anil Doradla: How many retail clients do it? Was that the question?

Sam Salvas @ Needham: Yeah. The weakness in the retail...like was that one big client...

Anil Doradla: So we talk about the...

Leonard Livschitz: Well, that's not a weakness of retail. It's just others grow fast. It's not an absolute dollar situation in general. I mean, you see the trends, but there's more investment to their modernization where we are participating in the way. I mean, again, I mentioned the people who work with us know that the brick-and-mortar business was a dominant part of our business and then it became brands and CPGs. We are not dismissing this business, but we put eggs in different baskets, right? So many years ago when we had a market dependency in retail, like three-quarters of the business, people are saying, can you grow and bring the market to 20%? So we're not there in 20%, but we're certainly in a much more comfortable position. So we want to grow it numerically as the company grows, but we want to focus on the proper brands that have the growth capabilities and also on various platforms to retail because platforms also come and go. You're probably aware there's a big reshuffling in the industry going on right now. So we're actively pursuing value-add businesses like home improvement businesses, and various products and services that are growing in our industry, both in the United States and in Europe. But we are a little bit less excited to go into something we developed 6, 8, 10 years ago because that market is a bit diminishing. So I think that's a better scope for what's happening.

Sam Salvas @ Needham: Okay. Thanks, guys.

Anil Doradla: Thanks, Sam.

Leonard Livschitz: Thank you, Sam.

Bin Jiang: Great. Thank you, Sam. Ladies and gentlemen, that would be all for the Q&A session for today. I will now pass the call back to Leonard for the closing comments.

CLOSING COMMENTS

Leonard Livschitz, Chief Executive Officer

Thank you everybody for joining us on the call today. We enter 2024 with a marked improvement in sentiment from a year ago. We are focused on our goals of getting back to our long-term model, both from growth and profitability. The last twelve months have proven that Grid Dynamics is adept at navigating uncertainties. Our existing customers appreciate our value, and in 2023 we established a record number of new customers. I am getting more and more bullish.

Looking forward to seeing you all in the next quarter.

Thank you.