Q3 2023 earnings conference call transcript

November 7, 2023

Corporate Participants

- **Guo Xiao** — President and Chief Executive Officer
- **Erin Cummins** — Chief Financial Officer
- **Rob Muller** — Global Head of Investor Relations

Presentation

Rob Muller
Hello, everyone. And welcome to Thoughtworks' Earnings Call for the Third Quarter of 2023. We will be recording today's call and during the presentations all lines will be on listen only.

Joining us today will be Thoughtworks President and CEO, Guo Xiao; and CFO, Erin Cummins.

The earnings press release was issued earlier today and is also available on our Investor Relations page at thoughtworks.com. Some of the matters we'll discuss on this call, including our expected business outlook and anticipated costs and benefits of our restructuring actions are forward-looking and as such, are subject to known and unknown risks and uncertainties.

These include but are not limited to those factors described in today's press release and discussed in the risk factors section of our annual report on Form 10-K, our quarterly reports on Form 10-Q and other reports we may file with the SEC from time to time. These risks and uncertainties could cause actual results to differ materially from those expressed on this call. These forward-looking statements are made only as of the date when made.

During our call today, we will reference certain non-GAAP financial measures. We will also provide growth rates in constant currency as a framework for assessing how our underlying business performed, excluding the effect of foreign currency rate fluctuations. We include non-GAAP to GAAP reconciliations in our press release furnished as an exhibit to our Form 8-K. The non-GAAP financial measures provided

should not be considered as a substitute for or superior to the measures of financial performance prepared in accordance with GAAP. Thoughtworks assumes no obligation to update or revise the information presented on this conference call.

I will now hand over to Xiao.

Guo Xiao
Thank you, Rob. Hello, everyone, and welcome to our third quarter earnings call. I'd like to start with an overall update on our business before Erin takes you through our results in more detail. Erin will then share our guidance before we move to Q&A. The quarter progressed in line with expectations that we discussed during our last earnings call.

We delivered revenue of $280 million, in line with our guidance and adjusted EBITDA margin of 12%, which exceeded our guidance. The restructuring program we shared with you in August is being executed to plan. The results are $17 million in quarterly cost takeout by the end of the quarter or $68 million on an annualized basis. Our global Digital Engineering Center is operational and is driving innovation with our clients and improving our ability to innovate and respond to client demand.

Now let me share an update on the demand environment. We're seeing stability in our sales pipeline compared with Q2 2023 with fewer client pauses. Our new logo acquisition continues to be a strength with 34 new clients in the quarter, increased from 29 in Q2 2023. We are prioritizing our investments in sales and marketing. We're seeing our efforts in outbound demand generation paying off, contributing 51% of the net new bookings in Q3.

Though we're still seeing longer average sales cycles and programs of work being broken up into smaller deals, we're hearing from some of our clients that budget pressure is starting to ease. I personally met with over 70 clients in the third quarter based on my conversations, digital transformation remains a top priority for our clients despite the macro environment. We are focusing on creating value for our clients through service expansion. For example, DAMO innovation around Gen AI and core services, data platforms, data mesh, enterprise modernization, cloud and FinOps. We continue to see a lot of client interest in GenAI, and we're well positioned to meet this demand.

We're focusing on 4 main areas: AI-assisted software delivery, AI-powered digital products, AI and data platforms at scale and AI-assisted enterprise modernization. Alongside some vertical opportunities, for example, drug discovery.

We have a GenAI reskilling program underway at scale. We have trained over 2,300 Thoughtworkers across 51 courses. We were excited by Thoughtworker engagement in our AI for software festival. The festival is a huge success. We're supported by Microsoft and GitHub who are helping with execution, contributing co-pilot licenses and are now working with us on joint opportunity development.

We're pleased with the innovation pipeline that is shaping up as our teams explore and experiment with new tools and technologies.

LegacyBridge is a good example of our innovation around GenAI. LegacyBridge is a Thoughtworks AI-assisted software delivery technology, which brings a differentiated approach to legacy code modernization. According to IDC's August 2023 Worldwide CIO survey, Legacy modernization is a top priority for CIOs. In Q3, we're working with a new client, a North America top 5 insurance company using LegacyBridge to accelerate the modernization of their legacy applications.

At the end of Q3, we're working with around 30 clients on GenAI projects. For example, we're working with a new client, MEGT, an Australian employment and training not-for-profit business. MEGT has been supporting employers, apprentices, trainees, job seekers, and students since 1982. MEGT has an ambitious strategy, underpinned by digital growth and innovation agenda. We partnered to deliver AI capability assessment to service high-value AI use cases across MEGT value chains.

Our scope included baselining organizational, digital maturity and readiness. We provided an actionable road map to help MEGT plan and execute on its high-value digital and AI-enabled strategic initiatives.

Thoughtworks is also working with new client Rightmove. Rightmove is the U.K.'s number 1 property website. We're working with Rightmove to explore how AI and GenAI capabilities could support their strategic goals, using GenAI tools and helping build AI skills in-house, we're looking into ways to increase operational efficiency as well as bring deeper user value across a suite of Rightmove products from B2C property search to features for estate agents.

Additional new GenAI wins in the quarter include a Fortune 500 pharmaceutical, a top 10 semiconductor company and a $10 billion turnover European e-commerce company.

At the core, our growth strategy is to deepen relationships with existing clients and win new logos. We then supplement this with focused strategies around M&A, geographic expansion and partners. First, starting with partners. In October, we announced that Thoughtworks has joined Stripe's partner ecosystem to provide solutions that enable modern digital commerce and financial operations.

At our clients' hipages group, Australia's number 1 online tradespeople marketplace, we have developed a new and improved payment system on Stripe's payment processing platform. Thoughtworks financial modernization solution powered by Stripe, has made the payment experience even simpler and smoother for hipages' tradespeople and their customers. I'm proud that in Q3, Thoughtworks was recognized as the Google Cloud Global Partner of the Year for diversity and inclusion. Striving to be a company that truly reflects the diverse societies we work in has been a priority of ours. We passionately believe that technology must be created by diverse teams that reflect society to better serve society.

Now let me share some details of recent successes with existing clients. PEXA Group, one of Australia's leading property tech organizations, has been working with Thoughtworks since 2021. In August 2023, PEXA signed a further 3-year partnership with Thoughtworks, ensuring work continues on PEXA's most important digital initiatives. At BMW, we have been working together on the BMW connected AI platform, which we have built on top of a micro services platform based on Kubernetes clusters in the AWS cloud. The connected AI platform supports multi-region compliance regulations and provides a standardized, scalable way to support all current and future connected AI use cases. To ensure cost-efficient AI deployments, multi-tenancy and portability between cloud providers were also key design considerations. BMW data scientists now don't have to worry about infrastructure aspects like persistent storage, identity, access and infrastructure security, everything is built into the platform.

We're now live with the first use case around proactive vehicle maintenance management. We're facilitating many more AI use cases, including the BMW intelligent

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personal assistant. We're pleased that in Q3, our client Falabella won the Forrester 2023 Technology Strategy Impact Award for the Americas. Falabella the $14 billion retail and financial services company that operates across Latin America, has been a Thoughtworks client since 2018. Falabella partnered with Thoughtworks to define the company's business agility model and develop an e-commerce product blueprint that evolved into its cloud native digital retail backbone.

This acts as the company's core technology platform across its channels, segments and countries. Google Cloud hosts the multi-tenant DRB. It enables Falabella's store modernization and digital point-of-sale system that unifies its digital search, catalog, card and checkout experiences. Falabella expects the DRB's modern architecture to substantially reduce time to market for new features and increase resilience.

Now let me share a couple of examples of our successes with new clients, with Air Canada, Canada's largest airline. We're partnering to consolidate their disparate design systems into one best-in-class globally aligned design system, iteratively demonstrate its use via rapid prototyping and create a road map for its development and evolution. In the U.K., we're working with a manufacturing company, AkzoNobel, who delivers sustainable and innovative solutions to their customers, communities and the environment to protect future generations. We're partnering with AkzoNobel on their e-commerce platform to improve their scalability and maintain ability in order to support future growth and strategy.

Now in my discussions with clients, they often tell me that two of the things that really differentiates Thoughtworks are our brilliant technologists and our thought leadership. I'm proud to share that we issued volume 29 of the Thoughtworks Technology Radar in October, our biannual report informed by real Thoughtworker experience solving our clients' most complex business challenges. The CTO of Moneysupermarket.com posted what many of our clients tell me. He posted “... in an ever-expanding technology landscape it’s resources like the Technology Radar that help guide us through the maze of options. The research, insights and recommendations truly stand out. And in Q3 Thoughtworks was ranked by Forbes as one of the world's best management consulting firms.

This recognition was based on feedback from clients, and we're delighted to be ranked for the first time in 2023.

Now let me share an update on our people. As we’ve restructured our business during the quarter, taking care of Thoughtworkers has been a top priority. We're pleased that voluntary attrition remains low at 12.2% on a TTM basis in Q3 compared with 12.6% on a TTM basis in Q2. Our head count at the end of Q3 was around 11,000. We continue to selectively higher with a focus on specific skill sets, such as data, infrastructure, in addition to expanding our sales force.

Our Glassdoor rating is 3.93 in Q3. We exceeded industry benchmarks in five of the workplace attributes categories, including career opportunity, culture and values, and senior management.

In Q3, we continued to lead the industry in responsible and ethical technology practices. For example, with our work alongside the United Nations. We're providing guidance on ensuring awareness of bias, transparency and the mitigation of negative unintended consequences in examining emerging technologies. Thoughtworks and the UN team have developed a framework and set of approaches for the responsible creation and management of technology systems and products. I would like to acknowledge the continued support of our Thoughtworkers and thank them for the extraordinary impact they deliver every day. Now let me hand over to Erin.

Erin Cummins
Thank you, Xiao, and thanks to everyone for joining us on today's call. Earlier this morning, we announced our results for the third quarter of 2023. The quarter progressed in line with the expectations we provided in August. Our teams are working closely with our clients on their most strategic initiatives and our overall pipeline remains robust. Our outbound engine is delivering well, contributing 51% of net new contracts in the quarter.

New client acquisition continues to be a strength with 34 new clients in the quarter.

Our restructuring program is progressing according to plan. I'm pleased to report that our fast execution has resulted in $68 million of cost savings on an annualized basis. Our global digital engineering center is operational and is optimizing our delivery capabilities. The DEC is driving efficiencies and improving utilization, which in Q3 was within our target range.

Now let's move on to our results in more detail. Revenues in Q3 were $280 million, representing a year-over-year decline of 16%, in constant currency revenue declined 17%. Acquisitions contributed 1 percentage point to the revenue growth rate in Q3. For the quarter, we saw year-over-year declines of 10% in APAC, 17% in Europe, 18% in North America and 25% in LATAM.

Moving to our industry verticals. Automotive travel and transportation remains our fastest-growing vertical, rising 12% year-over-year. We saw year-over-year declines of 14% within Energy, Public & Health Services, 16% in Financial Services, 23% in Retail and Consumer and 25% in Technology and Business Services. For the third quarter on a TTM basis, around 93% of our business came from existing clients. We currently have 34 clients with revenues greater than $10 million on a TTM basis.

In the third quarter, as a percentage of total revenue, our top five, top 10 and top 50 clients generated 19%, 29% and 67%, respectively. In the third quarter, our annualized average revenue per employee was $99,000, which is above the industry average and is reflective of the highly strategic work that we provide to our clients.

On a trailing 12-month basis, we ended Q3 with bookings of $1.4 billion. This is a 6.7% decline versus Q3 2022. As we have discussed previously, this is primarily due to smaller contract sizes and shorter contract terms. Adjusted gross margin was 37.4% for Q3 compared to 40.7% during the prior year period. Q3 2023 adjusted gross margin included some temporary headwinds related to onshore offshore mix shift as well as mid-single-digit pricing declines on a like-for-like basis.

In the third quarter, our adjusted SG&A as a percentage of revenue was 26.0% compared to 21.2% in the prior year period and 26.5% in Q2 2023. Adjusted EBITDA was $34 million for the third quarter, and adjusted EBITDA margin was 12.0%. Q3 GAAP diluted loss per share was $0.08 compared to a loss of $0.12 in the prior year period. Our adjusted diluted EPS was $0.04 compared to $0.08 for the third quarter of 2022.

We had free cash flow of $4 million during Q3 compared to free cash flow of $28 million in the prior year period. This figure is inclusive of $11 million in restructuring-related cash payments.

We continue to have good liquidity. Our cash balance stood at $87 million as of September 30, 2023, alongside an undrawn revolving credit facility. Our outstanding term loan balance was $297 million as of September 30, 2023.

Now let's turn to our business outlook for Q4. For the fourth quarter of 2023, we expect revenues to be in the range of $265 million to $270 million, reflecting a year-over-year decline of negative 15% to negative 13% or negative 16% to negative 14% in constant currency. Our Q4 guidance is informed by sales cycles remaining elongated and programs of work being broken up into smaller deals. However, we are seeing stability in the pipeline compared to earlier quarters, especially among our larger clients. We expect utilization adjusted for seasonality to continue to trend upwards and billable hours adjusted for seasonality to be consistent into Q4.

For the full year, we now expect revenues in the range of $1.139 billion to $1.144 billion, reflecting a year-over-year decline of negative 12% -- or negative 12% to negative 11% in constant currency. This includes an incremental $4 million of FX headwinds compared to the guidance we provided last quarter.

We expect acquisitions will contribute approximately 1 percentage point to the revenue growth rate in Q4 and 2 percentage points to the revenue growth rate for the full year. We expect adjusted EBITDA margin for the fourth quarter to be in the range of 10.5% to 12.5%. For the full year, we now expect adjusted EBITDA margin of 11.0% to 11.5%.

With respect to our restructuring program, we continue to expect total pretax charges of $20 million to $25 million, of which we have already recorded $16 million through the end of Q3. We continue to expect annualized cost savings of $75 million to $85 million, resulting from our restructuring actions. For the fourth quarter, we expect adjusted diluted EPS to be in the range of $0.02 to $0.04, assuming a weighted average share count of approximately 328 million diluted shares outstanding. For the full year, we now expect adjusted diluted EPS of $0.12 to $0.14, assuming a weighted average share count of approximately 331 million diluted shares outstanding.

Our Q4 guidance incorporates share-based compensation of $17 million. For the full year, we expect share-based compensation will total $65 million. By the end of 2023, we will have fully recognized all share-based compensation related to our IPO.

As mentioned earlier, we are seeing signs of stability across our client base. We intend to provide our guidance for 2024 during our Q4 earnings call next year. But our early expectation is that we will see revenue stability from Q4 into Q1 of 2024, followed by modest sequential growth throughout the remainder of 2024.

In closing, we remain focused on driving digital transformation with our clients. These are long-term strategic initiatives for our clients, and we continue to foster multi-year relationships. With that, I'll turn the call back over to Rob.

Rob Muller
Thanks, Erin. You can find our investor presentation on the Thoughtworks Investor Relations website. We will now move on to Q&A. I ask that you each keep to one question and one follow-up to allow as many participants as possible to ask a question. Operator, would you please provide instructions for those on the call?

[Operator Instructions]

Q&A

Operator
Our first question comes from Maggie Nolan with William Blair.

Maggie Nolan, William Blair
Erin, I wanted to dig into the last comment that you just made there on 2024. Can you elaborate a little on what maybe some of the drivers would be that would get you to that stability in the first quarter and then sequential growth from there?

Erin Cummins
Thanks for the question, Maggie. Yes, definitely. First of all, I will comment on stability generally. We have talked a bit in our prepared remarks already about stability. And on a relative basis, we have seen a more stable pipeline in the last few months, and we're seeing this as a good sign.

The other thing I would highlight that's specific to the fourth quarter is that there is seasonality. And so if we -- and that's because of more public holidays, more vacation time that we typically see and expect in the fourth quarter compared to Q3. So if we

adjust for that moving from Q3 to Q4, we are expecting to see similar -- and then we're not being specific yet. Of course, we'll be more specific in 3 months. These are a critical 2 months or so as we close out the year. But the way things are looking right now, we are seeing signs of stability moving into Q1. And so that's our best view.

We have been investing in demand and marketing overall, and we continue to increase our sales force, as Xiao mentioned earlier. So all of these things are helping build out that picture in 2024. But again, we're not guiding now, we will be more specific in 3 months' time.

Maggie Nolan, William Blair
That's still helpful context, and we'll wait for the formal guidance next quarter. My other question was on the margin profile. I'm hoping you can elaborate a little on what some of the temporary headwinds are that you're seeing with respect to the mix? And maybe just kind of help us understand where offshore and onshore mix is currently given all of the kind of changes that you've put through in the business structurally and operationally?

Erin Cummins
Thanks, Maggie. So just in terms of overall margin, there are temporary headwinds that we're seeing right now. So from a structural perspective, I'll start with what is impacting gross margin. While we have seen utilization improve, particularly from where we were at the start of the year, moving at a higher position from Q1 to Q2 than Q2 to Q3. So we're definitely on the right path.

We've moved more into our target range, but we're not yet at where we want to be, I would say we're at the lower end of that target range. And so that is an area of focus. Both Xiao and I touched on the restructuring and the digital engineering center. And so we're feeling positive about the benefits on utilization, and we believe there is more to come.

I did also touch on pricing. Given the macro environment, we have seen some pressures related to pricing. We are working with our clients where we are seeing more sensitivity due to constrained budgets on the whole. So pricing for us has been a headwind. It's something that as we look forward, we do think that is likely to continue to be a headwind into 2024.

We do believe that normalized supply-demand dynamics will return at some point. But we think that as we move into 2024, that will be a situation that's likely to remain.

And then, again, just to mention on SG&A. Obviously, the restructuring, we've touched on, it's going well. We have worked on executing quickly on that. So we are seeing that benefit to the cost base. Part of that is making the adjustment to where the moves have been from onshore to offshore in terms of work. And we have adjusted for most of that, but there is still friction that we're seeing in gross margin from a headwind perspective that just really relates to transition and handover as these things really take a couple of quarters to fully move through.

And then again, we are seeing efficiencies from our operations where we've reduced, particularly back-office operations. We're still doing more work on that. We'll continue to do that into the next year. But again, in the positive, we are seeing good signs from a pipeline perspective, and we're committed to continuing to invest in our demand and our sales and marketing.

Operator
Our next question comes from Ashwin Shirvaiker with Citi.

Ashwin Shirvaikar, Citi
And in good quarter relative to expectations. It's good to see that. I wanted to ask sort of try to draw a fine line between things not getting worse versus things getting better. If you could sort of walk through either by geography or vertical or project type? Just sort of what sorts of things are in the mode of not getting worse stabilizing versus actually seeing greenshoots and getting better versus neither if you could kind of provide granularity on that would be grade.

Guo Xiao
Sure. Thanks, Ashwin. So I'll start with where things are not getting worse, which means they're similar to what we described last quarter from a client buying behavior perspective. Sales cycle is still long, and we're still seeing additional layers of approval required. The deal size is still compressed, especially initial statement work with ramp-up continuing to be incremental.

And also, the pipeline conversion is still slower than we used to see similar to what we have seen last quarter because the client sentiment is still cautious, budget is tight. So those are the things that’re similar and it's not getting worse. Where we're seeing more

stabilization is, for example, in areas where we have large programs of work going on especially with large clients. We used to see -- when I say used to see in Q2 -- early Q3, especially in Q2, we called out a few unexpected ramp-downs. This has been much less frequent in Q3.

In fact, after the 1 we called out just at the beginning of July, we haven't seen anything at that scale since then. There's still a bit of a rampdown here in their scope reductions, but much less frequent and a much smaller scale. The other thing we're seeing improving a little is that we are hearing from some clients that budget is opening up in some aspects of the market, not all markets for sure, but some of the market, for example, health care, energy, automotive. And then from a geo perspective, APAC is hearing more positive sentiment from a client, and we're seeing some new projects starting there as well, a few $30 million-plus deals across the line recently.

And the other one I want to point out is our overall volume in Q3 is actually consistent with Q2 from an hours-billed perspective, that's another sign of stabilization. Now of course, as Erin mentioned, some of this work is moving towards offshore. So that's putting a little bit of short-term revenue pressure on us. But overall, we're seeing positive momentum in India and Europe, Asia and is offset by some of the similar behaviors in North America, U.K. and Australia.

Operator
Our next question comes from Puneet Jain with JPMorgan.

Puneet Jain, JPMorgan
Can you talk about what you are seeing or what you expect from client budgets early next year, in terms of magnitude and timing? And are there any differences in demand environment that you're seeing across verticals, it seems like TMT, retail, the verticals that were weak early on are stabilizing, but energy, utilities, and financial services are deteriorating.

Guo Xiao
Sure. Thank you, Puneet. First of all, the 2024 budget cycle with our clients, we are having a lot of conversations with our clients about this. Just the overall tone is still very cautious in 2024. I don't think it's as cautious as last year, but it's not significantly better. It's not back to normal. So the time line is still a little bit delayed. There's still a

lot of last-minute decision. We're expecting budget discussions probably continue late into December, even early January.

And the other thing to call out, many businesses, as we have in this discussion are still prioritizing cost reduction programs over growth initiatives in the near future. So we expect any IT budget increases for 2024 to be limited and incremental.

And then to answer your question from a vertical perspective, where we see, I think, the biggest challenge is still tech and retail, as you mentioned. We continue to see further pullback of spending as our clients are going through these tight budget cycles. From our perspective, our clients in financial services are relatively stable on a whole, but obviously, revenue decline was impacted Q-on-Q from some of the client-specific scope reductions we mentioned last quarter, including a large one in Q2. And then energy, public, health care is a strategic focus for us. And then they are more recession resilient. And we're seeing the sector doing reasonably well. But similarly, with a large client ramp down, we called out again last quarter, which was at the beginning of July, that impacted the overall revenue growth from a year-on-year perspective, but we're happy that we're now -- 26% of our portfolio is in energy, public and health care. And finally, automobile travel and transportation remained strong in Q3 with 12% growth and also a positive outlook.

Operator
Our next question comes from Bryan Bergin with TD Cowen.

Bryan Bergin, TD Cowen
I guess the first one, any early learnings you can share here from the centralized delivery structure?

Guo Xiao
For sure. Thanks, Bryan, for the question. So we're seeing -- one of the things Erin called out is the utilization getting back to the range we're aiming for, even though it's still at the lower end of the range. This is largely to do with the DEC, the center we created now that we're managing supply capacity in a more central manner as opposed to each country or even a subsegment in the country doing their own thing. So we're seeing a very obvious improvement on utilization optimization in several regions that they have to get back to the midrange or even getting back to the high end of the range of their utilization, which is a clearly good sign.

From a go-to-market perspective, we are still in the middle of getting through the transition to have the market team be more client-centric and vertical centric. We're definitely seeing signs where our teams are generally spending more time with the client with less internal friction. We do believe that is going to help us to become more intentional and strategic in funding investment in demand generation. Erin can probably comment some of the lessons learned on the operational centralization side of it.

Erin Cummins
Thanks, Xiao. I think the point that I would want to add around the operations side of it would simply be -- we're opening up a lot of opportunities to drive both efficiencies and process improvements in our business. And for us, we're seeing that very much as a win-win. Xiao touched on an example of that from a demand perspective, where decentralization of how we're going to market is actually reducing friction for some of our demand leaders and enabling them to be in front of clients more, and that's a great thing. That's not the only place that we're seeing and I think going through this restructuring and looking for these opportunities, we're refining processes that really, again, not only will provide cost savings by moving into a lower cost part of the business, but just general improvements overall. So on the whole, things are trending very well.

Operator
Our next question comes from Jason Kupferberg with Bank of America.

Tyler DuPont, Bank of America
This is Tyler DuPont on for Jason. It seems like the industry trend of moving towards more cost reduction programs compared to growth seems to have been occurring for the past several quarters now, given the choppy macro understandably, I'd be curious to hear your strategy to sort of capture some of that demand? For example, like how much of the $1.4 billion in bookings is focused on more of the cost takeout initiatives versus your higher bill rate consulting projects? And maybe if you can just sort of how -- speak to how that impacts both the top line and margin profile of the business?

Guo Xiao
Thanks, Tyler. So our clients are definitely more cost conscious. And then their internal priorities moving to cost reduction more than growth initiatives. And then what we've been doing from a service offering perspective is to focus more on offerings that can help to create efficiency and then targeting cost saving programs. For example,

engineering effectiveness programs that we've been rolling out, which is resonating with a lot of our clients in North America and then Europe.

That's targeting building an engineering effectiveness platform to allow our clients to be more efficient with their own internal R&D and then delivery practice. The other thing we roll out is DAMO, digital application management operation services. This is more of the digital version of the traditional support maintenance. It helps our clients to both keep running their digital assets in a modern way, but also put the program in a run mode versus the build mode and then to allow them to reduce cost in the short term, but also paves the way to get back to the build phase when the budget situation, when their priorities start to change.

The other thing I think we do a lot is, as Erin alluded to earlier, is to move a lot of the engineering work to offshore, so that we can deliver more with less. And this is happening across the board, across the verticals. That's how we're seeing some of the top line revenue being affected because even though we're delivering the same hours, it's delivering in a lower cost, lower bill rate country. But at the same time, in the long run, it should be margin accretive because we generally get higher margin with offshore. But in the short term, we're not seeing that margin benefit instantly because of the transition and then -- which also resulted in lower utilization in some of the onshore capacity we have, it's causing also a small dent on the margin side of it.

But overall, we feel that we are working with our clients, helping them with their priorities, and our churn rate is very low. We continue to work with the clients we've been working with for a long time. Our top 10 clients, average tenure is 9 years. We feel confident that if we help them through a difficult time, we're going to be better positioned to ramp up and focus more on the growth initiatives when the times get better.

Tyler DuPont, Bank of America
Okay. Great. That's super helpful, Xiao. And just quickly to follow up on the margin dynamics that you were alluding to. It looks like EBITDA margin was particularly healthy during the quarter, the 4Q guide may be modestly below Street expectations. But how should we be thinking about the moving pieces of the margin story as we look through the rest of the year? For example, when will the offshore margin tailwinds sort of actually hit the business? And just how do we think about margins as we go forward to 2024 and beyond, should we see a more new normal in the low double-digit range?

Or should we anticipate kind of a return to the more mid- to high teens. Just sort of any clarity there would be appreciated.

Erin Cummins
Thanks for the question, Tyler. So how to think about margins, I did touch on a couple of these points earlier, and I think it's worth repeating. So you asked around the offshore tailwinds and how long until we start to see that work through. It's hard to say exactly, but my view is that it will probably take about two more quarters to work through that fully. And so maybe about halfway into 2024.

Things do improve as we move along. So it's not as if we will wait to see the benefits fully until that point. But the impact is -- it's incremental. And so we're focused on seeing those improvements, but at the same time, committed to working with our clients to make this shift.

I touched on utilization before, as did Xiao. We are really pleased to see the improvements in our utilization profile, but we are not done. Similarly to the offshore tailwinds, those won't all come at one time. There's a few supply-demand imbalances that we're working through. Offshore-onshore is one of them, but also a little bit from a skills mix. And so we're continuing to push on that. The digital engineering center, we believe, will continue to deliver results. And so we expect to see that be an improvement to margins overall.

And then again, the restructuring costs we've made a lot of headway already in our overall program. As a reminder, we expect that we will have cost take out on an annualized basis of $75 million to $85 million. The actions we took locked in $68 million already by the end of Q3. So very good progress. Our view right now is we think that we'll be towards the upper end of that, and that certainly will be a benefit in 2024.

On the whole, as I mentioned earlier, I believe that some of the pricing dynamics, supply-demand dynamics that are coming from a more challenged macro will continue to persist into, certainly at least the start of 2024, and so we're not expecting those just to move away. Where this all gets us, in summary is, from a margin perspective, again, not being too specific on numbers. We'll wait for that, but 2023 has been a more challenging year from a margin point of view for reasons that we've talked about. We do think that we will see improvements in 2024, but unlikely to be at the levels of the high teens where we were in '21 and '22.

Operator
(Operator Instructions) Our next question comes from Matthew Roswell with RBC.

Matthew Roswell, RBC Capital Markets
I guess if I get a little more color on your pricing commentary and what you're seeing from the competitors? I mean, is it the competitors that are pulling down pricing? Or is it clients coming back to you and sort of looking for pricing reductions?

Guo Xiao
Sure. It's a little bit of both. With existing customers, where we tend to have large program work, but sometimes with new asset value -- a new statement work getting renewed on the 6 months, annual basis. We're seeing clients coming to us saying that, hey, I got a budget constraint, but I still need to get the same amount of work done, more work done, help me with that. And pricing is often a conversation that resulted in a lower pricing from a discount or giving a short-term discount perspective. So that's one source of the discussion.

With new work, especially a new client, it's becoming very competitive. And that, I think pricing pressure is mostly coming from all over the place from competitions where everyone is shopping their pencils trying to put in a bid that's commercially aggressive, trying to win the deal. So that's where we see the pressure coming from competition.

Matthew Roswell, RBC Capital Markets
Has that competition affected your win rates any?

Guo Xiao
The what rate, sorry?

Matthew Roswell, RBC Capital Markets
The win rates on the contracts?

Guo Xiao
Our win rate actually remains quite stable with both extensions and new work. Our strategy in this current climate is obviously trying to win work and then figure out margin later. So when we get into the bidding situation, especially with the new work we're also becoming very aggressive ourselves from a commercial perspective, it's not just pricing, obviously, the entire commercial model, including outcome-based or

potentially similar type of variant commercial models. Our win rate remains very similar to what we have seen before.

And then as we called out, we acquired [34] new logos in Q3 on top of the 29 in Q2 and 47 in Q1. So still pretty good track record of winning deals and new logos.

Matthew Roswell, RBC Capital Markets
Okay. And then a question for you, Erin. How should we think about fourth quarter free cash flow, especially in regards to potential further cash restructuring charges. And then is there anything as we go into FY '24 and the resumption of sequential growth we should keep in mind around cash flow, maybe working capital needs and things like that?

Erin Cummins
With respect to cash flow for fourth quarter, largely the dynamics that impacted third quarter will be the same in fourth quarter. Matt, you mentioned the restructuring charges. Q3 was impacted by the $11 million in restructuring charges. So as a reminder, on the whole, we expect $20 million to $25 million. So that means we've paid about half of that, a little bit more than half, depending on where you land in Q3, and there will be more in Q4. So those dynamics will be similar, cash flow as a consequence likely to be similar to what we saw in Q3.

In terms of 2024, those are one-time charges, and so cash flow will benefit as a consequence. The cash flow also should be improved by an improving margin profile. And then finally, earlier this year, we did have the payment with respect to the contingent earn-out from our Canada acquisition. And so that is a factor that impacted 2023, but wouldn't continue in 2024.

Operator
There are no further questions at this time. I'd like to turn the call back over to Guo Xiao for any closing remarks.

Guo Xiao
Thank you for joining us today for our [Q3] earnings call.

I would like to acknowledge the continued support of our Board and our shareholders.

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And in closing, I want to thank all Thoughtworkers, clients and partners for the extraordinary impact we're delivering every day together.

Stay well. And we look forward to catching up with you next quarter.

Operator
Thank you for your participation. This does conclude the program, and you may now disconnect. Everyone, have a great day.