
**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549**

FORM 10-Q

(Mark One)

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 2018**
OR

**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
FOR THE TRANSITION PERIOD FROM _____ TO _____
COMMISSION FILE NUMBER 001-33089**

EXLSERVICE HOLDINGS, INC.
(Exact name of registrant as specified in its charter)

DELAWARE
(State or other jurisdiction of
incorporation or organization)

**280 PARK AVENUE, 38TH FLOOR,
NEW YORK, NEW YORK**
(Address of principal executive offices)

82-0572194
(I.R.S. Employer
Identification No.)

10017
(Zip code)

(212) 277-7100

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company or an emerging growth company. See the definitions of "large accelerated filer", "accelerated filer", "smaller reporting company" and "emerging growth company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer	<input checked="" type="checkbox"/>	Accelerated filer	<input type="checkbox"/>
Non-accelerated filer	<input type="checkbox"/>	Smaller reporting company	<input type="checkbox"/>
Emerging growth company	<input type="checkbox"/>		

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

As of October 30, 2018, there were 34,256,695 shares of the registrant's common stock outstanding, par value \$0.001 per share.

TABLE OF CONTENTS

ITEM		<u>PAGE</u>
	Part I. Financial Information	3
1.	FINANCIAL STATEMENTS	
	Consolidated Balance Sheets as of September 30, 2018 (Unaudited) and December 31, 2017	3
	Consolidated Statements of Income (Unaudited) for the Three months and Nine months ended September 30, 2018 and 2017	4
	Consolidated Statements of Comprehensive (Loss)/Income (Unaudited) for the Three months and Nine months ended September 30, 2018 and 2017	5
	Consolidated Statements of Equity (Unaudited) for the Nine months ended September 30, 2018 and 2017	6
	Consolidated Statements of Cash Flows (Unaudited) for the Nine months ended September 30, 2018 and 2017	7
	Notes to Consolidated Financial Statements (Unaudited)	8
2.	Management’s Discussion and Analysis of Financial Condition and Results of Operations	40
3.	Quantitative and Qualitative Disclosures About Market Risk	54
4.	Controls and Procedures	54
	Part II. Other Information	54
1.	Legal Proceedings	54
1A.	Risk Factors	54
2.	Unregistered Sales of Equity Securities and Use of Proceeds	54
3.	Defaults Upon Senior Securities	55
4.	Mine Safety Disclosures	55
5.	Other Information	55
6.	Exhibits	56
	Signatures	57

PART 1. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

EXLSERVICE HOLDINGS, INC.
CONSOLIDATED BALANCE SHEETS
(In thousands, except share and per share amounts)

	As of	
	September 30, 2018 (Unaudited)	December 31, 2017
Assets		
Current assets:		
Cash and cash equivalents	\$ 97,636	\$ 86,795
Short-term investments	144,878	178,479
Restricted cash	4,679	3,674
Accounts receivable, net	164,307	135,705
Prepaid expenses	10,325	9,781
Advance income tax, net	7,700	8,801
Other current assets	24,302	29,582
Total current assets	453,827	452,817
Property and equipment, net	67,675	66,757
Restricted cash	3,499	3,808
Deferred tax assets	12,201	8,585
Intangible assets, net	114,799	48,958
Goodwill	357,533	204,481
Other assets	32,779	36,369
Investment in equity affiliate	2,824	3,000
Total assets	\$ 1,045,137	\$ 824,775
Liabilities and equity		
Current liabilities:		
Accounts payable	\$ 4,310	\$ 5,918
Current portion of long-term borrowings	12,318	10,318
Deferred revenue	7,600	10,716
Accrued employee costs	46,638	55,664
Accrued expenses and other current liabilities	67,084	61,366
Current portion of capital lease obligations	221	267
Total current liabilities	138,171	144,249
Long term borrowings	288,309	50,391
Capital lease obligations, less current portion	261	331
Income taxes payable	8,721	13,557
Deferred tax liabilities	13,352	—
Other non-current liabilities	21,875	16,202
Total liabilities	470,689	224,730
Commitments and contingencies (Refer to Note 25)		
Preferred stock, \$0.001 par value; 15,000,000 shares authorized, none issued	—	—
ExlService Holdings, Inc. Stockholders' equity:		
Common stock, \$0.001 par value; 100,000,000 shares authorized, 37,703,974 shares issued and 34,253,291 shares outstanding as of September 30, 2018 and 36,790,751 shares issued and 33,888,733 shares outstanding as of December 31, 2017	38	37
Additional paid-in capital	344,720	322,246
Retained earnings	480,387	427,064
Accumulated other comprehensive loss	(114,330)	(45,710)
Total including shares held in treasury	710,815	703,637
Less: 3,450,683 shares as of September 30, 2018 and 2,902,018 shares as of December 31, 2017, held in treasury, at cost	(136,609)	(103,816)
Stockholders' equity	574,206	599,821
Non-controlling interest	242	224
Total equity	574,448	600,045
Total liabilities and equity	\$ 1,045,137	\$ 824,775

See accompanying notes to unaudited consolidated financial statements.

EXLSERVICE HOLDINGS, INC.
CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)
(In thousands, except share and per share amounts)

	Three months ended September 30,		Nine months ended September 30,	
	2018	2017	2018	2017
Revenues, net	\$ 231,124	\$ 192,345	\$ 648,209	\$ 564,435
Cost of revenues ⁽¹⁾	152,157	123,077	429,907	365,883
Gross profit⁽¹⁾	78,967	69,268	218,302	198,552
Operating expenses:				
General and administrative expenses	28,704	26,545	85,610	75,007
Selling and marketing expenses	16,490	12,196	45,593	38,631
Depreciation and amortization	14,099	9,582	35,185	28,489
Total operating expenses	59,293	48,323	166,388	142,127
Income from operations	19,674	20,945	51,914	56,425
Foreign exchange gain, net	1,385	637	3,414	1,905
Interest expense	(2,475)	(482)	(3,719)	(1,380)
Other income, net	2,466	2,796	8,232	8,495
Income before income tax expense	21,050	23,896	59,841	65,445
Income tax expense	5,739	2,819	6,796	7,202
Loss from equity-method investment	62	—	176	—
Net income attributable to ExlService Holdings, Inc. stockholders	\$ 15,249	\$ 21,077	\$ 52,869	\$ 58,243
Earnings per share attributable to ExlService Holdings, Inc. stockholders:				
Basic	\$ 0.44	\$ 0.62	\$ 1.53	\$ 1.72
Diluted	\$ 0.43	\$ 0.60	\$ 1.50	\$ 1.66
Weighted-average number of shares used in computing earnings per share attributable to ExlService Holdings, Inc. stockholders:				
Basic	34,458,520	33,838,374	34,472,232	33,834,392
Diluted	35,207,991	35,043,987	35,217,814	35,048,672

(1) Exclusive of depreciation and amortization.

See accompanying notes to unaudited consolidated financial statements.

EXLSERVICE HOLDINGS, INC.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE (LOSS)/INCOME (UNAUDITED)
(In thousands)

	Three months ended September 30,		Nine months ended September 30,	
	2018	2017	2018	2017
Net income	\$ 15,249	\$ 21,077	\$ 52,869	\$ 58,243
Other comprehensive (loss)/income:				
Unrealized (loss)/gain on effective cash flow hedges, net of taxes (\$3,596), \$314, (\$7,969) and \$3,895, respectively	(8,348)	524	(21,218)	8,216
Foreign currency translation (loss)/gain	(18,373)	(3,030)	(44,403)	10,813
Reclassification adjustments				
Loss/(gain) on cash flow hedges, net of taxes \$19, (\$604), (\$1,183) and (\$1,497), respectively ⁽¹⁾	46	(1,375)	(2,890)	(3,397)
Retirement benefits, net of taxes (\$4), \$30, (\$6) and \$77, respectively ⁽²⁾	(34)	42	(109)	135
Total other comprehensive (loss)/income	\$ (26,709)	\$ (3,839)	\$ (68,620)	\$ 15,767
Total comprehensive (loss)/income	\$ (11,460)	\$ 17,238	\$ (15,751)	\$ 74,010

(1) These are reclassified to net income and are included either in cost of revenues or operating expenses, as applicable in the unaudited consolidated statements of income. Refer to Note 17 to the unaudited consolidated financial statements.

(2) These are reclassified to net income and are included in other income, net in the unaudited consolidated statements of income. Refer to Note 20 to the unaudited consolidated financial statements.

See accompanying notes to unaudited consolidated financial statements.

EXLSERVICE HOLDINGS, INC.
CONSOLIDATED STATEMENTS OF EQUITY (UNAUDITED)
(In thousands, except share and per share amounts)

	Common Stock		Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive (Loss)	Treasury Stock		Non - Controlling Interest	Total Equity
	Shares	Amount				Shares	Amount		
Balance as of December 31, 2017	36,790,751	\$ 37	\$ 322,246	\$ 427,064	\$ (45,710)	(2,902,018)	\$ (103,816)	\$ 224	\$ 600,045
Impact of adoption of Topic 606	—	—	—	454	—	—	—	—	454
Balance as of January 1, 2018	36,790,751	37	322,246	427,518	(45,710)	(2,902,018)	(103,816)	224	600,499
Stock issued on exercise/vesting of equity awards/business acquisition	913,223	1	5,163	—	—	—	—	—	5,164
Stock-based compensation	—	—	17,311	—	—	—	—	—	17,311
Acquisition of treasury stock	—	—	—	—	—	(548,665)	(32,793)	—	(32,793)
Non-controlling interest	—	—	—	—	—	—	—	18	18
Other comprehensive loss	—	—	—	—	(68,620)	—	—	—	(68,620)
Net income	—	—	—	52,869	—	—	—	—	52,869
Balance as of September 30, 2018	<u>37,703,974</u>	<u>\$ 38</u>	<u>\$ 344,720</u>	<u>\$ 480,387</u>	<u>\$ (114,330)</u>	<u>(3,450,683)</u>	<u>\$ (136,609)</u>	<u>\$ 242</u>	<u>\$ 574,448</u>

	Common Stock		Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive (Loss)	Treasury Stock		Non - Controlling Interest	Total Equity
	Shares	Amount				Shares	Amount		
Balance as of December 31, 2016	35,699,819	\$ 36	\$ 284,646	\$ 382,722	\$ (75,057)	(2,071,710)	\$ (60,362)	\$ 193	\$ 532,178
Impact of adoption of ASU 2016-09	—	—	5,999	(4,546)	—	—	—	—	1,453
Balance as of January 1, 2017	35,699,819	\$ 36	\$ 290,645	\$ 378,176	\$ (75,057)	(2,071,710)	\$ (60,362)	\$ 193	\$ 533,631
Stock issued on exercise/vesting of equity awards	825,873	1	4,275	—	—	—	—	—	4,276
Stock-based compensation	—	—	16,771	—	—	—	—	—	16,771
Acquisition of treasury stock	—	—	—	—	—	(649,020)	(32,336)	—	(32,336)
Non-controlling interest	—	—	—	—	—	—	—	14	14
Other comprehensive income	—	—	—	—	15,767	—	—	—	15,767
Net income	—	—	—	58,243	—	—	—	—	58,243
Balance as of September 30, 2017	<u>36,525,692</u>	<u>\$ 37</u>	<u>\$ 311,691</u>	<u>\$ 436,419</u>	<u>\$ (59,290)</u>	<u>(2,720,730)</u>	<u>\$ (92,698)</u>	<u>\$ 207</u>	<u>\$ 596,366</u>

See accompanying notes to unaudited consolidated financial statements.

EXLSERVICE HOLDINGS, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)
(In thousands)

	Nine months ended September 30,	
	2018	2017
Cash flows from operating activities:		
Net income	\$ 52,869	\$ 58,243
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	35,345	28,771
Stock-based compensation expense	17,311	16,771
Unrealized gain on short term investments	(5,423)	(4,437)
Unrealized foreign exchange (gain)/loss, net	(14,375)	446
Deferred income tax benefit	(986)	(5,417)
Allowances for doubtful accounts receivable	(620)	2,706
Loss from equity-method investment	176	—
Others, net	193	12
Change in operating assets and liabilities:		
Accounts receivable	(9,354)	(22,064)
Prepaid expenses and other current assets	(3,344)	5,194
Accounts payable	(1,414)	371
Deferred revenue	(5,199)	(8,155)
Accrued employee costs	(7,680)	(915)
Accrued expenses and other liabilities	(436)	267
Advance income tax, net	(4,228)	(2,607)
Other assets	(5,984)	1,241
Net cash provided by operating activities	46,851	70,427
Cash flows from investing activities:		
Purchase of property and equipment	(30,070)	(26,759)
Business acquisition (net of cash acquired)	(231,918)	(724)
Purchase of investments	(57,957)	(197,897)
Proceeds from redemption of investments	79,536	54,238
Net cash used for investing activities	(240,409)	(171,142)
Cash flows from financing activities:		
Principal payments on capital lease obligations	(105)	(133)
Proceeds from borrowings	245,000	—
Repayments of borrowings	(5,083)	—
Acquisition of treasury stock	(32,793)	(32,336)
Proceeds from exercise of stock options	1,084	4,276
Net cash provided by/(used for) financing activities	208,103	(28,193)
Effect of exchange rate changes on cash, cash equivalents and restricted cash	(3,008)	1,802
Net increase/(decrease) in cash, cash equivalents, and restricted cash	11,537	(127,106)
Cash, cash equivalents, and restricted cash at beginning of period	94,277	220,394
Cash, cash equivalents, and restricted cash at end of period	\$ 105,814	\$ 93,288
Supplemental disclosure of cash flow information:		
Non-cash investing and financing transaction		
Restricted common stock issued for business acquisition	\$ 4,080	\$ —

See accompanying notes to unaudited consolidated financial statements.

EXLSERVICE HOLDINGS, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

September 30, 2018

(In thousands, except share and per share amounts)

1. Organization

ExlService Holdings, Inc. (“ExlService Holdings”) is organized as a corporation under the laws of the state of Delaware. ExlService Holdings, together with its subsidiaries and affiliates (collectively, the “Company”), operates in the Business Process Management (“BPM”) industry providing operations management services and analytics services that help businesses enhance revenue growth and improve profitability. Using its proprietary platforms, methodologies and tools, the Company looks deeper to help companies improve global operations, enhance data-driven insights, increase customer satisfaction, and manage risk and compliance. The Company’s clients are located principally in the United States of America (“U.S.”) and the United Kingdom (“U.K”).

2. Summary of Significant Accounting Policies

(a) Basis of Preparation and Principles of Consolidation

The unaudited consolidated financial statements have been prepared in conformity with United States generally accepted accounting principles (“US GAAP”) for interim financial information, the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by US GAAP for annual financial statements and therefore should be read in conjunction with the audited consolidated financial statements and footnotes thereto included in the Company’s Annual Report on Form 10-K for the fiscal year ended December 31, 2017.

The unaudited consolidated financial statements reflect all adjustments (of a normal and recurring nature) that management considers necessary for a fair presentation of such statements for the interim periods presented. The unaudited consolidated statements of income for the interim periods presented are not necessarily indicative of the results for the full year or for any subsequent period.

The accompanying unaudited consolidated financial statements include the financial statements of ExlService Holdings and all of its subsidiaries. The standalone financial statements of subsidiaries are fully consolidated on a line-by-line basis. Intra-group balances and transactions, and income and expenses arising from intra-group transactions, are eliminated while preparing those financial statements. The un-realized gains resulting from intra-group transactions are also eliminated. Similarly, the un-realized losses are eliminated, unless the transaction provides evidence as to impairment of the asset transferred.

Accounting policies of the respective individual subsidiary and associate are aligned, wherever necessary, so as to ensure consistency with the accounting policies that are adopted by the Company under US GAAP.

The Company’s investments in equity affiliates are initially recorded at cost and any excess cost over proportionate share of the fair value of the net assets of the investee at the acquisition date is recognized as goodwill. The proportionate share of net income or loss of the investee is recognized in the unaudited consolidated statements of income.

Non-controlling interest is the equity in a subsidiary not attributable, directly or indirectly, to the parent and it represents the minority partner’s interest in the operations of ExlService Colombia S.A.S. Non-controlling interest consists of the amount of such interest at the date of obtaining control over the subsidiary, and the non-controlling interest’s share of changes in equity since that date. The non-controlling interest in the operations for all periods presented were insignificant and is included under general and administrative expenses in the unaudited consolidated statements of income.

(b) Use of Estimates

The preparation of the unaudited consolidated financial statements in conformity with US GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the unaudited consolidated financial statements and the unaudited consolidated statements of income during the reporting period. Although these estimates are based on management’s best assessment of the current business environment, actual results may be different from those estimates. The significant estimates and assumptions that affect the financial statements include, but are not limited to, allowance for doubtful receivables, recoverability of dues from statutory authorities, assets and obligations related to employee benefit plans, deferred tax valuation allowances, income-tax uncertainties and other contingencies, valuation of derivative financial instruments, assumptions used to calculate stock-based compensation expense, depreciation and amortization periods, purchase price allocation, recoverability of long-term assets including goodwill and intangibles, and estimated costs to complete fixed price contracts.

EXLSERVICE HOLDINGS, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS—(continued)

September 30, 2018

(In thousands, except share and per share amounts)

(c) Employee Benefits

Contributions to defined contribution plans are charged to the consolidated statements of income in the period in which services are rendered by the covered employees. Current service costs for defined benefit plans are accrued in the period to which they relate. The liability in respect of defined benefit plans is calculated annually by the Company using the projected unit credit method. Prior service cost, if any, resulting from an amendment to a plan is recognized and amortized over the remaining period of service of the covered employees.

The Company recognizes its liabilities for compensated absences depending on whether the obligation is attributable to employee services already rendered, relates to rights that vest or accumulate and payment is probable and estimable.

Effective January 1, 2018, the Company adopted Accounting Standards Update ("ASU") No. 2017-07, Compensation -Retirement Benefits (Topic 715), Improving the Presentation of Net Periodic Pension Cost and Net Periodic Post Retirement Benefit Cost. Pursuant to this, the Company retrospectively adopted the presentation of service cost separate from other components of net periodic costs for each period presented. The interest cost, expected return on plan assets and amortization of actuarial gains/loss, have been reclassified from "Cost of revenues", "General and administrative expenses" and "Selling and marketing expenses" to "Other income, net". Refer to Note 20 to the unaudited consolidated financial statements for details.

(d) Cash and Cash Equivalents and Restricted Cash

The Company considers all highly liquid investments purchased with an original maturity of ninety days or less to be cash equivalents. Pursuant to the Company's investment policy, surplus funds are invested in highly-rated debt mutual funds, money market accounts and time deposits to reduce its exposure to market risk with regard to these funds.

Restricted cash represents amounts on deposit with banks against bank guarantees issued through banks in favor of relevant statutory authorities for equipment imports, deposits for obtaining indirect tax registrations and for demands against pending income tax assessments (refer to Note 25 to the unaudited consolidated financial statements for details). These deposits with banks have maturity dates after September 30, 2019. Restricted cash presented under current assets represents funds held on behalf of clients in dedicated bank accounts.

Effective January 1, 2018, the Company adopted ASU 2016-18, Statement of Cash Flows (Topic 230), Restricted Cash. Pursuant to this adoption, for the purpose of unaudited statements of cash flows, the Company includes in its cash and cash-equivalent balances those amounts that have been classified as restricted cash and restricted cash equivalents for each period presented.

(e) Revenue Recognition

Revenue is recognized when services are provided to our customers, in an amount that reflects the consideration we expect to be entitled to in exchange for our services.

Revenue is measured based on consideration specified in a contract with a customer and excludes discounts and amounts collected on behalf of third parties. The Company recognizes revenue when it satisfies a performance obligation by providing services to a customer.

Taxes assessed by a governmental authority that are both imposed on and concurrent with a specific revenue-producing transaction, that are collected by the Company from a customer, are excluded from revenue.

Adoption of ASU 2014-09 Topic 606, "Revenue from Contracts with Customers" (Topic 606)

On January 1, 2018, the date of initial application, the Company adopted Topic 606 using the modified retrospective method by recognizing the cumulative effect of initially applying Topic 606 as an adjustment to the opening balance of equity, resulting in an increase of \$454, primarily due to new contract acquisition costs. The initial application scopes in those contracts which were not completed as of January 1, 2018. Results for reporting periods beginning January 1, 2018 are presented under Topic 606, while prior period amounts are not adjusted and continue to be reported in accordance with Company's historical accounting under Topic 605. The key area impacted upon adoption of Topic 606 relates to the accounting for sales commissions costs. Specifically, under Topic 606 a portion of sales commission costs have been recorded as an asset and recognized as an operating expense on a straight-line basis over the life of the contract. Prior to adoption, the Company was expensing sales commission costs as incurred.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS—(continued)

September 30, 2018

(In thousands, except share and per share amounts)

Nature of services

The Company derives its revenues from operations management and analytics services. The Company operates in the business process management (“BPM”) industry providing operations management and analytics services helping businesses enhance revenue growth and improve profitability. The Company provides BPM or “operations management” services, which typically involve transfer to the Company of business operations of a client, after which it administers and manages those operations for its client on an ongoing basis. The Company also provides industry-specific digital transformational services related to operations management services, and analytics services that focus on driving improved business outcomes for clients by generating data-driven insights across all parts of their business. The Company also provides care optimization and reimbursement optimization services, for its clients through its healthcare analytics solutions and services. The Company offers integrated solutions to help its clients with cost containment by leveraging technology platforms, customizable and configurable analytics and expertise in healthcare reimbursements to help clients enhance their claims payment accuracy.

Arrangements with Multiple Performance Obligations

The Company’s contracts with customers do not generally bundle different services together except for software and related services contracts, which are not significant, involving implementation services and post contract maintenance services. In such software and related services contracts, revenue is allocated to each performance obligation based on the relative standalone selling price.

A separate contract is generally drafted for each type of service sold, even if to the same customer. The typical length of a contract is 3 to 5 years for our operations management contracts.

Type of Contracts

- i. a) Revenues under time-and-material, transaction and outcome-based contracts are recognized as the services are performed. When the terms of the client contract specify service level parameters that must be met (such as turnaround time or accuracy), the Company monitors such service level parameters to determine if any service credits or penalties have been incurred. Revenues are recognized net of any penalties or service credits that are due to a client.
b) In respect of arrangements involving subcontracting, in part or whole of the assigned work, the Company evaluates revenues to be recognized based on guidance on “Principal versus agent considerations” in Topic 606.
- ii. Revenues for Company’s fixed-price contracts are recognized using the time-elapsed output method because the Company transfers control evenly during execution of its projects. Determining a measure of progress requires management to make judgments that affect the timing of revenue recognized. The Company regularly monitors its estimates for progress on completion of a project and records changes in the period in which a change in an estimate is determined. If a change in an estimate results in a projected loss on a project, such loss is recognized in the period in which it is identified.
- iii. Revenues from the Company’s software and related services contracts, which are not significant, are primarily related to maintenance renewals or incremental license fees for additional users. Maintenance revenues are generally recognized on a straight-line basis over the annual contract term. Fees for incremental license fees without any associated services are recognized upon delivery of the related incremental license.
- iv. Revenues from reimbursement optimization services having contingent fee arrangements are recognized by the Company at the point in time when a performance obligation is satisfied, which is when it identifies an overpayment claim and the same is acknowledged by its customers. In such contracts, the Company’s consideration is contingent upon the actual collections made by its customers and subsequent potential retraction claims. Based on guidance on “variable consideration” in Topic 606, the Company uses its historical experience and projections to determine the expected recoveries from its customers and recognizes revenue based upon such expected recoveries. Any adjustment required due to change in estimates are recorded in the period in which such change is identified.

EXLSERVICE HOLDINGS, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS—(continued)

September 30, 2018

(In thousands, except share and per share amounts)

Unbilled receivables represents revenues recognized for services rendered between the last billing date and the balance sheet date. Unbilled receivables also include revenues recognized from reimbursement optimization services when the Company identifies an overpayment claim and the same is acknowledged by its customers, however not invoiced at the balance sheet date. Accordingly, amounts for services that the Company has performed and for which an invoice has not yet been issued to the customers are presented as a part of contract assets as accounts receivable.

The Company has deferred revenue attributable to certain process transition activities, with respect to its customers where such activities do not represent separate performance obligations. Revenues related to such transition activities are contract liabilities classified under “Deferred Revenue” in the Company’s consolidated balance sheets and subsequently recognized ratably over the period in which the related services are performed. Deferred revenue also includes the amount for which services have been rendered but other conditions of revenue recognition are not met, for example where the Company does not have persuasive evidence of an arrangement with customer. Costs related to such transition activities are contract fulfillment costs, and thereby classified under “Other Current Assets” and “Other Assets” in the consolidated balance sheets, and are recognized ratably over the estimated expected period of benefit, under Cost of Revenues in the consolidated statements of income.

Other incremental and direct costs incurred for acquiring contracts, such as sales commissions are contract acquisition costs and thereby classified under “Other Current Assets” and “Other Assets” in the consolidated balance sheets. Such costs are amortized over the expected period of benefit and recorded under Selling and marketing expenses in the consolidated statements of income.

Any upfront payments made to customers are contract assets and classified under “Other Current Assets and Other Assets” in the consolidated balance sheets. Such costs are amortized over the expected period of benefit and are recorded as an adjustment to transaction price and reduced from revenues.

Reimbursements of out-of-pocket expenses received from clients are included as part of revenues.

Payment terms

All Contracts entered into by the Company specify the payment terms and are defined for each contract separately. Usual payment terms range between 30-60 days. The Company does not have any extended payment terms clauses in existing contracts. At times, the Company enters into fixed price contracts and software licenses involving significant implementation wherein the milestones are defined such that the Company can recover the costs with a reasonable margin.

Variable Consideration

Variability in the transaction price arises primarily due to service level agreements, cost of living adjustments, and pre-payment and volume discounts.

The Company considers its experience with similar transactions and expectations regarding the contract in estimating the amount of variable consideration that should be recognized during a period.

The Company believes that the expected value method is most appropriate for determining the variable consideration since the company has large number of contracts with similar nature of transactions/services.

Allocation of transaction price to performance obligations

The transaction price is allocated to performance obligations on a relative standalone selling price basis. Standalone selling prices are estimated by reference to the total transaction price less the sum of the observable standalone selling prices of other goods or services promised in the contract. In assessing whether to allocate variable consideration to a specific part of the contract, the Company considers the nature of the variable payment and whether it relates specifically to its efforts to satisfy a specific part of the contract.

EXLSERVICE HOLDINGS, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS—(continued)

September 30, 2018

(In thousands, except share and per share amounts)

Practical expedients and exemptions

We do not disclose the value of unsatisfied performance obligations for (i) contracts with an original expected length of one year or less and (ii) contracts for which we recognize revenue at the amount to which we have the right to invoice for services performed.

(f) Recent Accounting Pronouncements

In February 2016, the Financial Accounting Standards Board ("FASB") issued ASU No. 2016-02, Leases (Topic 842), which requires the identification of arrangements that should be accounted for as leases. In general, lease arrangements exceeding a twelve months term should be recognized as assets with corresponding liabilities on the balance sheet of the lessee. This ASU requires recording a right-of-use asset and lease obligation for all leases, whether operating or finance, while the income statement will reflect lease expense for operating leases and amortization and interest expense for finance leases. The balance sheet amount recorded for existing leases at the date of adoption of this ASU must be calculated using the applicable incremental borrowing rate. The new guidance is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. The Company is currently evaluating the impact that the adoption of this guidance will have on its consolidated financial statements and the implementation approach to be used.

In June 2016, FASB issued ASU No. 2016-13, Financial Instruments - Credit Losses, which requires a financial asset (or a group of financial assets) measured at amortized cost basis to be presented at the net amount expected to be collected. The allowance for credit losses is a valuation account that is to be deducted from the amortized cost of the financial asset(s) so as to present the net carrying value at the amount expected to be collected on the financial asset. The new guidance is effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. The amendment should be applied through a modified retrospective approach. Early adoption as of the fiscal years beginning after December 15, 2018 is permitted. The Company is currently evaluating the impact that the adoption of this guidance will have on its consolidated financial statements.

In June 2018, FASB issued ASU No. 2018-07, Compensation-Stock Compensation (Topic 718): Improvements to Non-employee Share-Based Payment Accounting. This ASU involves several aspects of the accounting for non-employee share-based payment transactions resulting from expanding the scope of Topic 718, Compensation-Stock Compensation, to include share-based payment transactions for acquiring goods and services from non-employees. The amendments in this ASU affect all entities that enter into share-based payment transactions for acquiring goods and services from non-employees. This ASU is effective for public business entities for fiscal years beginning after December 15, 2018, including interim periods within that fiscal year. Early adoption is permitted, but no earlier than an entity's adoption date of Topic 606. The adoption of this ASU is not expected to have any material effect on the Company's consolidated financial statements.

In July 2018, FASB issued ASU No. 2018-11, Leases (Topic 842), which provide entities with an additional (and optional) transition method to adopt the new leases standard. Under this new transition method, an entity initially applies the new leases standard at the adoption date and recognizes a cumulative-effect adjustment to the opening balance of retained earnings in the period of adoption. Consequently, an entity's reporting for the comparative periods presented in the financial statements in which it adopts the new leases standard will continue to be in accordance with current GAAP (Topic 840, Leases). The new guidance is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. The Company is currently evaluating the impact that the adoption of this guidance will have on its consolidated financial statements and the implementation approach to be used.

In August 2018, FASB issued ASU No. 2018-13, Fair Value Measurement (Topic 820): Changes to the Disclosure Requirements for Fair Value Measurement. The amendments in this ASU modify the disclosure requirements on fair value measurements in Topic 820, based on the concepts in the Concepts Statement, including the consideration of costs and benefits. The amendments in ASU are effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. An entity is permitted to early adopt either the entire standard or only the provisions that eliminate or modify requirements. The adoption of this ASU is not expected to have any material effect on the Company's consolidated financial statements.

EXLSERVICE HOLDINGS, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS—(continued)

September 30, 2018

(In thousands, except share and per share amounts)

In August 2018, FASB issued ASU No. 2018-14, Compensation-Retirement Benefits-Defined Benefit Plans-General (Subtopic 715-20): Changes to the Disclosure Requirements for Defined Benefit Plans. The amendments in this Update remove disclosures that no longer are considered cost beneficial, clarify the specific requirements of disclosures, and add disclosure requirements identified as relevant. The amendments in ASU are effective for fiscal years beginning after December 15, 2020. An entity is permitted to early adopt this Update. The adoption of this ASU is not expected to have any material effect on the Company's consolidated financial statements.

In August 2018, the FASB issued ASU No. 2018-15, Intangibles - Goodwill and Other - Internal-Use Software (Subtopic 350-40): This ASU aligns the requirements for capitalizing implementation costs incurred in a hosting arrangement that is a service contract with the requirements for capitalizing implementation costs incurred to develop or obtain internal-use software (and hosting arrangements that include an internal-use software license). Accordingly, the ASU requires an entity (customer) in a hosting arrangement that is a service contract to follow the guidance in FASB Accounting Standard Codification Subtopic 350-40 on internal-use software to determine which implementation costs to capitalize as an asset related to the service contract and which costs to expense. The ASU 2018-15 also provides guidance on amortization and impairment of any costs capitalized, along with new presentation and disclosure requirements. The new guidance is effective for fiscal years beginning after December 15, 2019. Early adoption is permitted and both prospective and retrospective transition methods are allowed. The Company is currently evaluating the impact that the adoption of this guidance will have on its consolidated financial statements.

(g) Recently Adopted Accounting Pronouncements

In May 2014, FASB issued ASU No. 2014-09 (Topic 606) "Revenue from Contracts with Customers." Topic 606 supersedes the revenue recognition requirements in Topic 605 "Revenue Recognition" (Topic 605), and requires entities to recognize revenue when control of the promised goods or services is transferred to customers at an amount that reflects the consideration to which the entity expects to be entitled to in exchange for those goods or services. The Company adopted Topic 606 as of January 1, 2018 using the modified retrospective transition method. Refer to Note 4 to the unaudited consolidated financial statements for details.

In August 2016, FASB issued ASU No. 2016-15, Classification of Certain Cash Receipts and Cash Payments. The amendments apply to all entities that are required to present a statement of cash flows under Topic 230. The amendments are an improvement to US GAAP because they provide guidance for each of the eight issues, thereby reducing the current and potential future diversity in practice. The amendments are effective for fiscal years beginning after December 15, 2017 and interim periods within those annual periods and should be applied using a retrospective transition method to each period presented. The Company has adopted the guidance retrospectively to each period presented. The adoption does not have any material effect on the presentation of its unaudited consolidated statements of cash flows.

In November 2016, FASB issued ASU No. 2016-18, Statement of cash flows (Topic 230) - Restricted cash. The amendments apply to all entities that have restricted cash or restricted cash equivalents and are required to present a statement of cash flows under Topic 230. The amendments in this update require that a statement of cash flows should explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. The amendments are effective for fiscal years beginning after December 15, 2017 and interim periods within those annual periods and should be applied using a retrospective transition method to each period presented. Early adoption is permitted with an adjustment reflected as of the beginning of the fiscal year in which the amendment is adopted. The Company has adopted the guidance retrospectively to each period presented. The adoption does not have any material effect on the presentation of its unaudited consolidated statements of cash flows. Refer to Note 6 to the unaudited consolidated financial statements for details.

In January 2017, FASB issued ASU No. 2017-04, Intangibles-Goodwill and Other (Topic 350) - Simplifying the Test for Goodwill Impairment, which eliminates Step 2 from the goodwill impairment test. A goodwill impairment will now be the amount by which a reporting unit's carrying value exceeds its fair value, however, the loss recognized should not exceed the total amount of goodwill allocated to that reporting unit. The ASU is effective for annual and interim periods in fiscal years beginning after December 15, 2019. Early adoption is permitted for interim or annual goodwill impairment tests performed after January 1, 2017 and should be applied prospectively. The Company has adopted the guidance effective January 1, 2018. The adoption does not have any material effect on its unaudited consolidated financial statements.

EXLSERVICE HOLDINGS, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS—(continued)

September 30, 2018

(In thousands, except share and per share amounts)

In March, 2017, FASB issued ASU No. 2017-07, Improving the Presentation of Net Periodic Pension Cost and Net Periodic Post-retirement Benefit Cost. The ASU amends ASC 715, Compensation — Retirement Benefits, to require employers that present a measure of operating income in their statement of income to include only the service cost component of net periodic pension cost and net periodic post-retirement benefit cost in operating expenses (together with other employee compensation costs). The other components of net benefit cost, including amortization of prior service cost/credit, and settlement and curtailment effects, are to be included in non-operating expenses. The update also stipulates that only the service cost component of net benefit cost is eligible for capitalization. The amendments are effective for fiscal years beginning after December 15, 2017 and interim periods within those annual periods and should be applied using a retrospective transition method to each period presented. The Company has adopted the guidance retrospectively to each period presented. Refer to Note 2(c) and Note 20 to the unaudited consolidated financial statements for details.

In May 2017, FASB issued ASU No. 2017-09, Compensation - Stock Compensation (Topic 718): Scope of Modification Accounting. This ASU provides guidance on the types of changes to the terms or conditions of share-based payment awards to which an entity would be required to apply modification accounting. Modification accounting is required only if the fair value, the vesting conditions, or the classification of the award changes as a result of the change in terms or conditions. The amendments in this ASU are effective for all entities for annual periods, and interim periods within those annual periods, beginning after December 15, 2017. Early adoption is permitted, including adoption in any interim period, for public business entities for reporting periods for which financial statements have not yet been issued. The amendments in this ASU should be applied prospectively to an award modified on or after the adoption date. The Company has adopted the guidance effective January 1, 2018. The adoption does not have any material effect on its unaudited consolidated financial statements.

EXLSERVICE HOLDINGS, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS—(continued)

September 30, 2018

(In thousands, except share and per share amounts)

3. Segment and Geographical Information

The Company operates in the BPM industry and is a provider of operations management and analytics services. The Company has eight operating segments, which are strategic business units that align its products and services with how it manages its business, approaches its key markets and interacts with its clients. Six of those operating segments provide BPM or “operations management” services, five of which are industry-focused operating segments (Insurance, Healthcare, Travel, Transportation and Logistics, Banking and Financial Services, and Utilities) and one of which is a “capability” operating segment (Finance and Accounting) that provides services to clients in our industry-focused segments as well as clients across other industries. In each of these six operating segments, the Company provides operations management services, which typically involve transfer to the Company of the business operations of a client, after which it administers and manages those operations for its client on an ongoing basis. The remaining two operating segments are Consulting, which provides industry-specific transformational services related to operations management services, and Analytics, which provides services that focus on driving improved business outcomes for clients by generating data-driven insights across all parts of their business.

The Company presents information for the following reportable segments:

- Insurance
- Healthcare
- Travel, Transportation and Logistics (“TT&L”)
- Finance and Accounting (“F&A”)
- Analytics, and
- All Other (consisting of the Company’s remaining operating segments, which are the Banking and Financial Services, Utilities and Consulting operating segments).

The chief operating decision maker (“CODM”) generally reviews financial information such as revenues, cost of revenues and gross profit, disaggregated by the operating segments to allocate an overall budget among the operating segments.

The Company does not allocate and therefore the CODM does not evaluate other operating expenses, interest expense or income taxes by segment. Many of the Company’s assets are shared by multiple operating segments. The Company manages these assets on a total Company basis, not by operating segment, and therefore asset information and capital expenditures by operating segment are not presented.

The July 2018 acquisition of SCIOinspire Holdings Inc. (“SCIO”) is included in the Analytics reportable segment.

Revenues and cost of revenues for the three months ended September 30, 2018 and 2017, respectively, for each of the reportable segments, are as follows:

	Three months ended September 30, 2018						
	Insurance	Healthcare	TT&L	F&A	All Other	Analytics	Total
Revenues, net	\$ 64,303	\$ 20,375	\$ 17,278	\$ 24,517	\$ 21,944	\$ 82,707	\$ 231,124
Cost of revenues ⁽¹⁾	43,524	15,797	9,958	14,917	14,323	53,638	152,157
Gross profit ⁽¹⁾	\$ 20,779	\$ 4,578	\$ 7,320	\$ 9,600	\$ 7,621	\$ 29,069	\$ 78,967
Operating expenses							59,293
Foreign exchange gain, interest expense and other income, net							1,376
Income tax expense							5,739
Loss from equity-method investment							62
Net income							\$ 15,249

⁽¹⁾ Exclusive of depreciation and amortization.

EXLSERVICE HOLDINGS, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS—(continued)

September 30, 2018

(In thousands, except share and per share amounts)

	Three months ended September 30, 2017						
	Insurance	Healthcare	TT&L	F&A	All Other	Analytics	Total
Revenues, net	\$ 59,608	\$ 18,871	\$ 18,496	\$ 21,642	\$ 19,984	\$ 53,744	\$ 192,345
Cost of revenues ^{(1)*}	39,174	12,072	9,996	12,634	13,571	35,630	123,077
Gross profit ^{(1)*}	\$ 20,434	\$ 6,799	\$ 8,500	\$ 9,008	\$ 6,413	\$ 18,114	\$ 69,268
Operating expenses*							48,323
Foreign exchange gain, interest expense and other income, net*							2,951
Income tax expense							2,819
Net income							\$ 21,077

⁽¹⁾ Exclusive of depreciation and amortization.

Revenues and cost of revenues for the nine months ended September 30, 2018 and 2017, respectively, for each of the reportable segments, are as follows:

	Nine months ended September 30, 2018						
	Insurance	Healthcare	TT&L	F&A	All Other	Analytics	Total
Revenues, net	\$ 193,018	\$ 62,989	\$ 53,326	\$ 72,717	\$ 66,732	\$ 199,427	\$ 648,209
Cost of revenues ⁽¹⁾	129,984	49,752	31,026	44,189	44,587	130,369	429,907
Gross profit ⁽¹⁾	\$ 63,034	\$ 13,237	\$ 22,300	\$ 28,528	\$ 22,145	\$ 69,058	\$ 218,302
Operating expenses							166,388
Foreign exchange gain, interest expense and other income, net							7,927
Income tax expense							6,796
Loss from equity-method investment							176
Net income							\$ 52,869

⁽¹⁾ Exclusive of depreciation and amortization.

	Nine months ended September 30, 2017						
	Insurance	Healthcare	TT&L	F&A	All Other	Analytics	Total
Revenues, net	\$ 173,784	\$ 56,726	\$ 53,374	\$ 63,694	\$ 62,547	\$ 154,310	\$ 564,435
Cost of revenues ^{(1)*}	117,675	36,687	30,457	37,398	42,629	101,037	365,883
Gross profit ^{(1)*}	\$ 56,109	\$ 20,039	\$ 22,917	\$ 26,296	\$ 19,918	\$ 53,273	\$ 198,552
Operating expenses*							142,127
Foreign exchange gain, interest expense and other income, net*							9,020
Income tax expense							7,202
Net income							\$ 58,243

⁽¹⁾ Exclusive of depreciation and amortization.

EXLSERVICE HOLDINGS, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS—(continued)

September 30, 2018

(In thousands, except share and per share amounts)

*The Company early adopted ASU 2017-12, Derivative and Hedging (Topic 815), Targeted Improvements to Accounting for Hedging Activities. Pursuant to this adoption, effective January 1, 2017, the resultant foreign exchange gain/(loss) upon settlement of cash flow hedges are recorded along with the underlying hedged item in the same income statement line as either part of “Cost of revenues”, “General and administrative expenses”, “Selling and marketing expenses”, “Depreciation and amortization”, as applicable. Refer to Note 17 to the unaudited consolidated financial statements for details.

Revenues, net of the Company by service type, were as follows:

	Three months ended September 30,		Nine months ended September 30,	
	2018	2017	2018	2017
BPM and related services ⁽¹⁾	\$ 148,417	\$ 138,601	\$ 448,782	\$ 410,125
Analytics services	82,707	53,744	199,427	154,310
Total	\$ 231,124	\$ 192,345	\$ 648,209	\$ 564,435

⁽¹⁾ BPM and related services include revenues of the Company's five industry-focused operating segments, one capability operating segment and the consulting operating segment, which provides services related to operations management services. Refer to segment disclosure above.

The Company attributes the revenues to regions based upon the location of its customers.

	Three months ended September 30,		Nine months ended September 30,	
	2018	2017	2018	2017
Revenues, net				
United States	\$ 191,671	\$ 158,501	\$ 536,956	\$ 462,676
Non-United States				
United Kingdom	29,901	26,824	85,397	81,857
Rest of World	9,552	7,020	25,856	19,902
Total Non-United States	39,453	33,844	111,253	101,759
	\$ 231,124	\$ 192,345	\$ 648,209	\$ 564,435

Property and equipment, net by geographic area, were as follows:

	As of	
	September 30, 2018	December 31, 2017
Property and equipment, net		
India	\$ 33,995	\$ 39,143
United States	24,689	16,371
Philippines	6,000	8,217
Rest of World	2,991	3,026
	\$ 67,675	\$ 66,757

4. Revenues, net

Adoption of ASU 2014-09 Topic 606, “Revenue from Contracts with Customers”

On January 1, 2018, the Company adopted Topic 606 using the modified retrospective method and applied its guidance to those contracts which were not completed as of January 1, 2018. Results for reporting periods beginning after January 1, 2018 are presented under Topic 606, while prior period amounts are not adjusted and continue to be reported in accordance with our historical accounting under Topic 605. The Company recorded a net addition to opening equity of \$454 as of January 1, 2018 due to the cumulative impact of adopting Topic 606, primarily due to contract acquisition costs.

EXLSERVICE HOLDINGS, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS—(continued)

September 30, 2018

(In thousands, except share and per share amounts)

The adoption of Topic 606 did not have a significant impact on the measurement or recognition of revenues during the three and nine months ended September 30, 2018.

Refer to Note 3 to the unaudited consolidated financial statements for revenues disaggregated by reportable segments and geography.

Contract balances

The following table provides information about accounts receivable, contract assets and contract liabilities from contracts with customers:

	As of	
	September 30, 2018	December 31, 2017
Accounts receivable, net	\$ 164,307	\$ 135,705
Contract assets	\$ 5,766	\$ 2,643
Contract liabilities		
Deferred revenue (advance payments portion)	\$ 7,481	\$ 9,311

Accounts receivable includes \$71,538 and \$49,125 as of September 30, 2018 and December 31, 2017, respectively, representing amounts not billed to customers. The Company has accrued the unbilled receivables for work performed in accordance with the terms of contracts with customers and considers no significant performance risk associated with its unbilled receivables.

Contract assets represents upfront payments made to customers.

Contract liabilities represents that portion of deferred revenue for which payments have been received in advance from customers including revenues attributable to certain process transition activities for which costs have been capitalized by the Company as contract fulfillment costs. The contract liabilities are included within deferred revenues in the consolidated balance sheet and are recognized as revenue as (or when) the performance obligation is fulfilled under the contract.

Revenue recognized from the carrying value of contract liabilities as of December 31, 2017 during the three and nine months ended September 30, 2018 was \$1,644 and \$8,025, respectively.

Contract acquisition costs

The Company had contract acquisition costs of \$1,087 as of September 30, 2018. As of January 1, 2018, the Company capitalized \$454 as contract acquisition costs related to contracts that were not completed. Further, the Company capitalized an additional \$186 and \$858 during the three and nine months ended September 30, 2018, respectively, and amortized \$72 and \$225 during the three and nine months ended September 30, 2018, respectively. There was no impairment loss in relation to costs capitalized. The capitalized costs are being amortized on a straight-line basis over the life of contract.

Contract fulfillment costs

The Company had deferred contract fulfillment costs relating to transition activities of \$4,179 and \$2,769 as of September 30, 2018 and December 31, 2017, respectively. The Company capitalized an additional \$1,455 and \$2,140 during the three and nine months ended September 30, 2018, respectively, and amortized \$335 and \$730 during the three and nine months ended September 30, 2018, respectively. There was no impairment loss in relation to costs capitalized. The capitalized costs are being amortized on a straight line basis over the life of contract.

Consideration received from customers, if any, relating to such transition activities are classified under Contract Liabilities and are recognized ratably over the period in which the related performance obligations are fulfilled.

EXLSERVICE HOLDINGS, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS—(continued)

September 30, 2018

(In thousands, except share and per share amounts)

5. Earnings Per Share

Basic earnings per share is computed by dividing net income to common stockholders by the weighted average number of common shares outstanding during each period. Diluted earnings per share is computed using the weighted average number of common shares plus the potentially dilutive effect of common stock equivalents (outstanding stock options, restricted stock and restricted stock units) issued and outstanding at the reporting date, using the treasury stock method. Stock options, restricted stock and restricted stock units that are anti-dilutive are excluded from the computation of weighted average shares outstanding.

The following table sets forth the computation of basic and diluted earnings per share:

	Three months ended September 30,		Nine months ended September 30,	
	2018	2017	2018	2017
Numerator:				
Net income	\$ 15,249	\$ 21,077	\$ 52,869	\$ 58,243
Denominators:				
Basic weighted average common shares outstanding	34,458,520	33,838,374	34,472,232	33,834,392
Dilutive effect of share based awards	749,471	1,205,613	745,582	1,214,280
Diluted weighted average common shares outstanding	35,207,991	35,043,987	35,217,814	35,048,672
Earnings per share attributable to ExlService Holdings Inc. stockholders:				
Basic	\$ 0.44	\$ 0.62	\$ 1.53	\$ 1.72
Diluted	\$ 0.43	\$ 0.60	\$ 1.50	\$ 1.66
Weighted average potentially dilutive shares considered anti-dilutive and not included in computing diluted earnings per share	256	—	161,792	151,961

6. Cash, Cash Equivalents and Restricted Cash

For the purpose of unaudited statements of cash flows, cash, cash equivalents and restricted cash comprise of the following:

	As of	
	September 30, 2018	September 30, 2017
Cash and cash equivalents	\$ 97,636	\$ 87,665
Restricted cash (current)	4,679	1,913
Restricted cash (non-current)	3,499	3,710
	\$ 105,814	\$ 93,288

7. Other Income, net

Other income, net consists of the following:

	Three months ended September 30,		Nine months ended September 30,	
	2018	2017	2018	2017
Interest and dividend income	\$ 523	\$ 322	\$ 1,160	\$ 1,317
Gain on sale of mutual funds	2,180	2,556	7,007	6,777
Others, net	(237)	(82)	65	401
Other income, net	\$ 2,466	\$ 2,796	\$ 8,232	\$ 8,495

EXLSERVICE HOLDINGS, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS—(continued)

September 30, 2018

(In thousands, except share and per share amounts)

8. Property and Equipment, net

Property and equipment, net consist of the following:

	Estimated useful lives (Years)	As of	
		September 30, 2018	December 31, 2017
Owned Assets:			
Network equipment and computers	3-5	\$ 78,693	\$ 77,587
Software	3-5	63,668	59,325
Leasehold improvements	3-8	37,079	38,857
Office furniture and equipment	3-8	19,354	19,667
Motor vehicles	2-5	556	638
Buildings	30	1,097	1,245
Land	—	718	815
Capital work in progress	—	10,407	9,184
		211,572	207,318
Less: Accumulated depreciation and amortization		(144,285)	(141,059)
		\$ 67,287	\$ 66,259
Assets under capital leases:			
Leasehold improvements		\$ 712	\$ 941
Office furniture and equipment		7	167
Motor vehicles		550	710
		1,269	1,818
Less: Accumulated depreciation and amortization		(881)	(1,320)
		\$ 388	\$ 498
Property and equipment, net		\$ 67,675	\$ 66,757

Capital work in progress represents advances paid towards acquisition of property and equipment and cost incurred to develop software not yet ready to be placed in service.

The depreciation and amortization expense excluding amortization of acquisition-related intangibles recognized in the unaudited consolidated statements of income was as follows:

	Three months ended September 30,		Nine months ended September 30,	
	2018	2017	2018	2017
Depreciation and amortization expense	\$ 7,381	\$ 6,095	\$ 20,759	\$ 17,997

Effective January 1, 2017, the depreciation and amortization expenses set forth above includes the effect of foreign exchange gain/(loss) upon settlement of cash flow hedges, amounting to (\$33) and \$125 for the three months ended and \$160 and \$282 for the nine months ended September 30, 2018 and 2017, respectively. Refer to Note 17 to the unaudited consolidated financial statements for further details.

EXLSERVICE HOLDINGS, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS—(continued)

September 30, 2018

(In thousands, except share and per share amounts)

Internally developed software costs, included under Software, was as follows:

	As of	
	September 30, 2018	December 31, 2017
Cost	\$ 7,625	\$ 2,571
Less : Accumulated amortization	(1,950)	(976)
	\$ 5,675	\$ 1,595

9. Business Combinations, Goodwill and Intangible Assets**SCIOinspire Holdings Inc.**

On July 1, 2018, the Company, through its wholly owned subsidiary ExlService.com, LLC ("Buyer") and Buyer's wholly owned subsidiary, ExlService Cayman Merger Sub, completed the acquisition of SCIO pursuant to an Agreement of Merger dated April 28, 2018 (the "Merger Agreement"). ExlService Cayman Merger Sub, merged with and into SCIO, with SCIO surviving the merger as a wholly-owned subsidiary of the Buyer.

SCIO is a health analytics solution and services company serving over 100 healthcare organizations representing over 130 million covered lives across the continuum including providers, health plans, pharmacy benefit managers, employers, health services and global life sciences companies. The acquisition is expected to significantly strengthen the Company's capability in the high growth cost optimization and care optimization markets. The acquisition of SCIO is included in the Analytics reportable segment.

The preliminary estimated aggregate purchase consideration was \$245,491, including estimated cash and cash equivalents acquired and incorporating estimated post-closing adjustments. The aggregate base purchase consideration payable at closing of the merger was \$236,500 based on completion of diligence, which was adjusted based on, among other things, SCIO's cash, debt, working capital position and other adjustments as of the Closing as set forth in the Merger Agreement. To finance the acquisition at Closing, the Company utilized its revolving credit facility in the amount of \$233,000, issued 69,459 shares of restricted common stock of the Company in the amount of \$4,080 and paid the balance with available cash on hand.

Pursuant to the Company's business combinations accounting policy, the total estimated purchase consideration for SCIO was allocated to identifiable net tangible and intangible assets based upon their preliminary fair values. The excess of the estimated purchase consideration over fair value of identifiable net tangible and intangible assets was recorded as goodwill. The preliminary purchase price allocation is subject to change during the one-year measurement period as the Company obtains additional information about these net tangible and intangible assets. In order to allocate the consideration transferred for SCIO, the fair values of all identifiable assets and liabilities must be established. For accounting and financial reporting purposes, fair value is defined under ASC Topic 820, "Fair Value Measurement and Disclosure" as the price that would be received upon sale of an asset or the amount paid to transfer a liability in an orderly transaction between market participants at the measurement date. Market participants are assumed to be buyers and sellers in the principal (most advantageous) market for the asset or liability. Additionally, fair value measurements for an asset assume the highest and best use of that asset by market participants. Use of different estimates and judgments could yield different results.

EXLSERVICE HOLDINGS, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS—(continued)

September 30, 2018

(In thousands, except share and per share amounts)

The Company's preliminary purchase price allocation to net tangible and intangible assets of SCIO is as follows:

Assets:	
Cash and cash equivalents	\$ 10,026
Restricted cash	2,790
Accounts receivable	19,924
Other current assets	1,798
Property and equipment	1,824
Other assets	1,751
Intangible assets	
Customer relationships	47,800
Developed technology	28,900
Trade names and trademarks	3,700
	118,513
Liabilities:	
Current liabilities	(11,679)
Deferred tax liabilities	(19,052)
Other non-current liabilities	(200)
	(30,931)
Net assets acquired	\$ 87,582
Goodwill	157,909
Total purchase consideration	\$ 245,491

The fair values of the trade names and trademarks intangible assets were determined by using an "income approach", specifically the relief-from-royalty approach. The basic principle of the relief-from-royalty method is that without ownership of the subject intangible asset, the user of that intangible asset would have to make a stream of payments to the owner of the asset in return for the rights to use that asset. By acquiring the intangible asset, the user avoids these payments. Therefore, a portion of SCIO's earnings, equal to the after-tax royalty that would have been paid for the use of the asset, can be attributed to the firm's ownership. The trade names and trademarks are being amortized on a straight-line basis (which approximates the economic pattern of benefits) over the estimated economic life of 3 years.

The fair values of the developed technology intangible assets were also determined by the relief-from-royalty approach. Similarly, this approach is based on the assumption that in lieu of ownership, a firm would be willing to pay a royalty in order to exploit the related benefits of the technology. Therefore, a portion of SCIO's earnings, equal to the after-tax royalty that would have been paid for the use of the technology, can be attributed to the firm's ownership of the technology. The technology assets are being amortized on a straight-line basis (which approximates the economic pattern of benefits) over the estimated economic life of 5 years.

The fair values of the customer relationships were determined by using an "income approach", specifically the Multi-Period Excess Earnings Method ("MPEEM"). The MPEEM is a specific application of the discounted cash flow method. The principle behind the MPEEM is that the value of an intangible asset is equal to the present value of the incremental after-tax cash flows attributable only to the subject intangible asset after deducting Contributory Asset Charges ("CAC"). The principle behind a CAC is that an intangible asset 'rents' or 'leases' from a hypothetical third party all the assets it requires to produce the cash flows resulting from its development, that each project rents only those assets it needs (including elements of goodwill) and not the ones that it does not need, and that each project pays the owner of the assets a fair return on (and of, when appropriate) the value of the

EXLSERVICE HOLDINGS, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS—(continued)

September 30, 2018

(In thousands, except share and per share amounts)

rented assets. The customer relationship assets are being amortized on a straight-line basis (which approximates the economic pattern of benefits) over the estimated economic life of 10 years.

The goodwill recognized is attributable primarily to expected synergies from continuing operations of SCIO and the Company. The amount of goodwill recognized from SCIO's acquisition is not deductible for tax purposes. The goodwill has been assigned to our Analytics reportable segment based upon the Company's assessment of nature of services rendered by SCIO.

Supplemental Pro Forma Data

The Company completed the acquisition of SCIO on July 1, 2018 and accordingly SCIO's operations for the period from July 1, 2018 to September 30, 2018 are included in the Company's consolidated statements of income. SCIO contributed revenues of \$19,205 for the period from the completion of acquisition through September 30, 2018. The Company does not allocate other operating expenses, interest expense or income taxes by legal entity, and therefore the Company has not presented earnings of SCIO for the period from the completion of acquisition through September 30, 2018. The following unaudited pro forma results of operations have been prepared using the acquisition method of accounting to give effect to the SCIO acquisition as though it occurred on January 1, 2017. The pro forma amounts reflect certain adjustments, such as amortization of intangible assets acquired, interest expense related to borrowings not assumed by the Company and stock based compensation expense. The unaudited pro forma financial information is presented for illustrative purposes only, is based on a preliminary purchase price allocation, and is not necessarily indicative of the results of operations that would have actually been reported had the acquisitions occurred on January 1, 2017, nor is it necessarily indicative of the future results of operations of the combined company.

	Three months ended September 30,		Nine months ended September 30,	
	2018	2017	2018	2017
Revenues, net	\$ 231,124	\$ 210,263	\$ 689,269	\$ 615,157
Net income	\$ 15,395	\$ 19,580	\$ 51,666	\$ 51,820
Earnings per share:				
Basic	\$ 0.45	\$ 0.58	\$ 1.50	\$ 1.53
Diluted	\$ 0.44	\$ 0.56	\$ 1.47	\$ 1.47

Health Integrated, Inc.

On December 22, 2017, a wholly owned subsidiary of the Company entered into an Asset Purchase Agreement to acquire substantially all the assets and assumed certain liabilities of Health Integrated, Inc. ("Health Integrated"), a company based in Tampa, Florida. The initial purchase price consisted of \$22,577 in cash including working capital adjustment. The purchase agreement allows sellers the ability to earn up to \$5,000 as earn-out, based on the achievement of certain performance goals by the acquired Health Integrated business during the 2018 calendar year. The earn-out was fair valued at \$920 as of December 31, 2017. As of September 30, 2018 fair value of earn-out is Nil.

A portion of the purchase price otherwise payable was placed into escrow as security for the post-closing working capital adjustments and the indemnification obligations under the Asset Purchase Agreement.

Health Integrated provides dedicated care management services on behalf of health plans. Its services include case management, utilization management, disease management, special needs programs and multichronic care management. Health Integrated serves millions of lives in the Medicaid, Medicare, and dual eligible populations. It is known for its strong capabilities in improving member health status through behavioral change. Accordingly, the Company paid a premium for the acquisition, which is reflected in the goodwill recognized from the purchase price allocation. The acquisition of Health Integrated is included in the Healthcare reportable segment.

EXLSERVICE HOLDINGS, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS—(continued)

September 30, 2018

(In thousands, except share and per share amounts)

The Company finalized its purchase price allocation for the acquisition based on their fair values as set forth below:

	Amount
Tangible Assets	\$ 5,475
Liabilities	(5,733)
Identifiable Intangible Assets:	
Customer relationships	6,760
Developed technology	1,510
Trade names and trademarks	570
Goodwill	14,229
Total purchase price	<u>\$ 22,811</u>

The amount of goodwill recognized from the Health Integrated acquisition is deductible for tax purposes.

The customer relationships from the Health Integrated acquisition are being amortized over the weighted average useful life of 7.0 years and developed technology and trademarks are being amortized over the useful life of 1.0 year and 2.0 years, respectively.

Acquisition-related costs

Acquisition-related costs are being expensed as incurred and are included in general and administrative expenses in the unaudited consolidated statements of income. The Company recognized acquisition-related costs, which were incurred to effect business combination, for its SCIO and Health Integrated acquisitions of \$323 and \$457 during the three months ended September 30, 2018 and 2017, respectively, and recognized \$1,230 and \$505 for the nine months ended September 30, 2018 and 2017, respectively.

Goodwill

The following table sets forth details of the Company's goodwill balance as of September 30, 2018:

	Insurance	Healthcare	TT&L	F&A	All Other	Analytics	Total
Balance as at January 1, 2017	\$ 38,110	\$ 19,276	\$ 12,983	\$ 47,537	\$ 5,326	\$ 63,538	\$ 186,770
Acquisitions	—	15,957	—	—	—	—	15,957
Currency translation adjustments	223	—	696	835	—	—	1,754
Balance as at December 31, 2017	\$ 38,333	\$ 35,233	\$ 13,679	\$ 48,372	\$ 5,326	\$ 63,538	\$ 204,481
Acquisitions	—	—	—	—	—	157,909	157,909
Measurement period adjustments*	—	(1,728)	—	—	—	—	(1,728)
Currency translation adjustments	(93)	—	(1,380)	(1,656)	—	—	(3,129)
Balance as at September 30, 2018	<u>\$ 38,240</u>	<u>\$ 33,505</u>	<u>\$ 12,299</u>	<u>\$ 46,716</u>	<u>\$ 5,326</u>	<u>\$ 221,447</u>	<u>\$ 357,533</u>

* Subsequent to December 31, 2017, adjustments of \$1,728 have been made to the Health Integrated amounts of net tangible assets acquired and the earn-out with the corresponding offsets to goodwill. These adjustments are within the measurement period and have been accounted for prospectively. These adjustments did not have a significant impact on the Company's unaudited consolidated statements of income, balance sheets or cash flows.

EXLSERVICE HOLDINGS, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS—(continued)

September 30, 2018

(In thousands, except share and per share amounts)

Intangible Assets

Information regarding the Company's intangible assets is set forth below:

	As of September 30, 2018		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Finite-lived intangible assets:			
Customer relationships	\$ 129,788	\$ (52,570)	\$ 77,218
Leasehold benefits	2,545	(2,425)	120
Developed technology	44,677	(13,043)	31,634
Non-compete agreements	2,045	(1,899)	146
Trade names and trademarks	9,642	(4,861)	4,781
	<u>\$ 188,697</u>	<u>\$ (74,798)</u>	<u>\$ 113,899</u>
Indefinite-lived intangible assets:			
Trade names and trademarks	\$ 900	\$ —	\$ 900
Total intangible assets	<u>\$ 189,597</u>	<u>\$ (74,798)</u>	<u>\$ 114,799</u>

	As of December 31, 2017		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Finite-lived intangible assets:			
Customer relationships	\$ 82,165	\$ (43,667)	\$ 38,498
Leasehold benefits	2,888	(2,596)	292
Developed technology	15,835	(8,749)	7,086
Non-compete agreements	2,045	(1,780)	265
Trade names and trademarks	5,951	(4,034)	1,917
	<u>\$ 108,884</u>	<u>\$ (60,826)</u>	<u>\$ 48,058</u>
Indefinite-lived intangible assets:			
Trade names and trademarks	\$ 900	\$ —	\$ 900
Total intangible assets	<u>\$ 109,784</u>	<u>\$ (60,826)</u>	<u>\$ 48,958</u>

The amortization expense for the period is as follows:

	Three months ended September 30,		Nine months ended September 30,	
	2018	2017	2018	2017
Amortization expense	<u>\$ 6,718</u>	<u>\$ 3,487</u>	<u>\$ 14,426</u>	<u>\$ 10,492</u>

The remaining weighted average life of intangible assets is as follows:

	(in years)
Customer relationships	7.89
Leasehold benefits	0.67
Developed technology	4.54
Non-compete agreements	0.97
Trade names and trademarks (Finite lived)	3.16

EXLSERVICE HOLDINGS, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS—(continued)

September 30, 2018

(In thousands, except share and per share amounts)

Estimated future amortization expense related to intangible assets as of September 30, 2018 is as follows:

2018 (October 1 - December 31)	\$	6,702
2019		24,250
2020		16,884
2021		15,175
2022		13,760
2023 and thereafter		37,128
Total	\$	<u>113,899</u>

10. Investment in Equity Affiliate

On December 12, 2017, the Company acquired preferred stock in Corridor Platform Inc. (“Corridor”), a big data credit risk management platform for \$3,000. The Company has determined that based on its ownership interest and other rights, Corridor is an equity method affiliate. The Company has the right and option to acquire additional preferred stock from Corridor as per the terms of the agreement. The Company's proportionate share of net loss for the three months and nine months ended September 30, 2018 was \$62 and \$176, respectively.

11. Other Current Assets

Other current assets consist of the following:

	As of	
	September 30, 2018	December 31, 2017
Derivative instruments	\$ 1,928	\$ 10,938
Advances to suppliers	800	2,451
Receivables from statutory authorities	13,274	7,598
Contract assets	1,248	401
Deferred contract fulfillment costs	1,460	474
Others	5,592	7,720
Other current assets	<u>\$ 24,302</u>	<u>\$ 29,582</u>

12. Other Assets

Other assets consist of the following:

	As of	
	September 30, 2018	December 31, 2017
Lease deposits	\$ 8,428	\$ 8,776
Derivative instruments	270	7,361
Deposits with statutory authorities	6,025	6,492
Term deposits	5,209	6,909
Contract assets	4,518	2,242
Deferred contract fulfillment costs	2,719	2,295
Others	5,610	2,294
Other assets	<u>\$ 32,779</u>	<u>\$ 36,369</u>

EXLSERVICE HOLDINGS, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS—(continued)

September 30, 2018

(In thousands, except share and per share amounts)

13. Accrued Expenses and Other Current Liabilities

Accrued expenses and other current liabilities consist of the following:

	As of	
	September 30, 2018	December 31, 2017
Accrued expenses	\$ 43,521	\$ 43,235
Derivative instruments	7,870	555
Client liabilities	6,831	8,982
Other current liabilities	8,862	8,594
Accrued expenses and other current liabilities	\$ 67,084	\$ 61,366

14. Other Non-current Liabilities

Other non-current liabilities consist of the following:

	As of	
	September 30, 2018	December 31, 2017
Derivative instruments	\$ 9,947	\$ 322
Unrecognized tax benefits	892	892
Deferred rent	7,501	8,176
Retirement benefits	2,423	3,377
Others	1,112	3,435
Other non-current liabilities	\$ 21,875	\$ 16,202

15. Accumulated Other Comprehensive Loss

Accumulated other comprehensive loss consists of amortization of actuarial gain/(loss) on retirement benefits and changes in the cumulative foreign currency translation adjustments. In addition, the Company enters into foreign currency exchange contracts, which are designated as cash flow hedges in accordance with ASC topic 815. Changes in the fair values of forward contracts are recognized in accumulated other comprehensive loss on the Company's consolidated balance sheet until the settlement of those contracts. The balances as of September 30, 2018 and December 31, 2017 are as follows:

	As of	
	September 30, 2018	December 31, 2017
Cumulative foreign currency translation (loss)	\$ (102,808)	\$ (58,405)
Unrealized (loss)/gain on cash flow hedges, net of taxes of (\$4,239) and \$4,918, respectively	(12,176)	11,932
Retirement benefits, net of taxes of (\$80) and (\$74), respectively	654	763
Accumulated other comprehensive loss	\$ (114,330)	\$ (45,710)

EXLSERVICE HOLDINGS, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS—(continued)

September 30, 2018

(In thousands, except share and per share amounts)

16. Fair Value Measurements

Assets and Liabilities Measured at Fair Value

The following table sets forth the Company's assets and liabilities that were accounted for at fair value as of September 30, 2018 and December 31, 2017. The table excludes accounts receivable, accounts payable and accrued expenses for which fair values approximate their carrying amounts.

As of September 30, 2018	Level 1	Level 2	Level 3	Total
Assets				
Money market and mutual funds*	\$ 113,147	\$ —	\$ —	\$ 113,147
Derivative financial instruments	—	2,198	—	\$ 2,198
Total	\$ 113,147	\$ 2,198	\$ —	\$ 115,345
Liabilities				
Derivative financial instruments	\$ —	\$ 17,817	\$ —	\$ 17,817
Total	\$ —	\$ 17,817	\$ —	\$ 17,817
<hr/>				
As of December 31, 2017	Level 1	Level 2	Level 3	Total
Assets				
Money market and mutual funds*	\$ 162,906	\$ —	\$ —	\$ 162,906
Derivative financial instruments	—	18,299	—	18,299
Total	\$ 162,906	\$ 18,299	\$ —	\$ 181,205
Liabilities				
Derivative financial instruments	\$ —	\$ 877	\$ —	\$ 877
Fair value of earn-out consideration	—	—	920	920
Total	\$ —	\$ 877	\$ 920	\$ 1,797

* Represents short-term investments carried on fair value option under ASC 825 "Financial Instruments" as of September 30, 2018 and December 31, 2017.

Derivative Financial Instruments: The Company's derivative financial instruments consist of foreign currency forward exchange contracts. Fair values for derivative financial instruments are based on independent sources including highly rated financial institutions and are classified as Level 2. Refer to Note 17 to the unaudited consolidated financial statements for further details.

Fair value of earn-out consideration: The fair value measurement of earn-out consideration is determined using Level 3 inputs. The Company's earn-out consideration represents a component of the total purchase consideration for its acquisition of Health Integrated. The measurement was calculated using unobservable inputs based on the Company's own assessment of achievement of certain performance goals by Health Integrated during the 2018 calendar year. The earn-out was fair valued at \$920 as of December 31, 2017. As of September 30, 2018, fair value of earn-out is Nil.

EXLSERVICE HOLDINGS, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS—(continued)

September 30, 2018

(In thousands, except share and per share amounts)

17. Derivatives and Hedge Accounting

The Company uses derivative instruments and hedging transactions to mitigate exposure to foreign currency fluctuation risks associated with forecasted transactions denominated in certain foreign currencies and to minimize earnings and cash flow volatility associated with changes in foreign currency exchange rates. The Company's derivative financial instruments are largely forward foreign exchange contracts that are designated as effective hedges and that qualify as cash flow hedges under ASC 815. The Company had outstanding cash flow hedges totaling \$364,395 as of September 30, 2018 and \$300,757 as of December 31, 2017.

Changes in the fair value of these cash flow hedges are recorded as a component of accumulated other comprehensive income/(loss), net of tax, until the hedged transactions occurs. The Company early adopted ASU 2017-12, Derivative and Hedging (Topic 815), Targeted Improvements to Accounting for Hedging Activities. Pursuant to this adoption, effective January 1, 2017, the resultant foreign exchange gain/(loss) are recorded along with the underlying hedged item in the same line of consolidated statements of income as either part of "Cost of revenues", "General and administrative expenses", "Selling and marketing expenses", "Depreciation and amortization", as applicable.

Prior to January 1, 2017, the resultant foreign exchange gain/(loss) on settlement of cash flow hedges and changes in the fair value of cash flow hedges deemed ineffective were recorded in "Foreign exchange gain, net" in the consolidated statements of income.

The Company also enters into foreign currency forward contracts to economically hedge its intercompany balances and other monetary assets and liabilities denominated in currencies other than functional currencies. These derivatives do not qualify as fair value hedges under ASC 815. Changes in the fair value of these derivatives are recognized in the unaudited consolidated statements of income and are included in foreign exchange gain/(loss). The Company's primary exchange rate exposure is with the Indian Rupee, the U.K. pound sterling and the Philippine peso. The Company also has exposure to Colombian pesos, Czech Koruna, the Euro, South African ZAR and other local currencies in which it operates. Outstanding foreign currency forward contracts amounted to \$140,055 and GBP 18,044 as of September 30, 2018 and amounted to \$98,967 and GBP 17,947 as of December 31, 2017.

The Company estimates that approximately \$6,158 of net derivative losses included in accumulated other comprehensive loss ("AOCI") could be reclassified into earnings within the next twelve months based on exchange rates prevailing as of September 30, 2018. At September 30, 2018, the maximum outstanding term of the cash flow hedges was 45 months.

The Company evaluates hedge effectiveness at the time a contract is entered into as well as on an ongoing basis. For hedging positions that are discontinued because the forecasted transaction is not expected to occur by the end of the originally specified period, any related amounts recorded in equity are reclassified to earnings.

The following tables set forth the fair value of the foreign currency exchange contracts and their location on the consolidated financial statements:

Derivatives designated as hedging instruments:	As of	
	September 30, 2018	December 31, 2017
Foreign currency exchange contracts		
Other current assets	\$ 1,712	\$ 10,892
Other assets	\$ 270	\$ 7,361
Accrued expense and other current liabilities	\$ 7,870	\$ 481
Other non-current liabilities	\$ 9,947	\$ 322
Derivatives not designated as hedging instruments:		
Foreign currency exchange contracts		
Other current assets	\$ 216	\$ 46
Accrued expense and other current liabilities	\$ —	\$ 74

EXLSERVICE HOLDINGS, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS—(continued)

September 30, 2018

(In thousands, except share and per share amounts)

The following tables set forth the effect of foreign currency exchange contracts on the unaudited consolidated statements of income and accumulated other comprehensive loss for the three and nine months ended September 30, 2018 and 2017:

Forward Exchange Contracts:	Three months ended September 30,		Nine months ended September 30,	
	2018	2017	2018	2017
Gain/(loss) recognized in AOCI				
Derivatives in cash flow hedging relationships	\$ (11,944)	\$ 838	\$ (29,187)	\$ 12,111
Gain/(loss) recognized in unaudited consolidated statements of income				
Derivatives not designated as hedging instruments	\$ (4,268)	\$ (678)	\$ (9,837)	\$ 2,095

Location and amount of gain/(loss) recognized in unaudited consolidated statements of income for cash flow hedging relationships and derivatives not designated as hedging instruments

	Three months ended September 30,			
	2018		2017	
	As per unaudited consolidated statements of income	Gain/(loss) on foreign currency exchange contracts	As per unaudited consolidated statements of income	Gain/(loss) on foreign currency exchange contracts
Cash flow hedging relationships				
Location in unaudited consolidated statements of income where gain/(loss) was reclassified from AOCI				
Cost of revenues	\$ 152,157	\$ (76)	\$ 123,077	\$ 1,564
General and administrative expenses	\$ 28,704	12	\$ 26,545	280
Selling & marketing expenses	\$ 16,490	6	\$ 12,196	23
Depreciation & amortization	\$ 14,099	(7)	\$ 9,582	112
		\$ (65)		\$ 1,979
Derivatives not designated as hedging instruments				
Location in unaudited consolidated statements of income where gain/(loss) was recognized				
Foreign exchange gain/(loss), net	\$ 1,385	\$ (4,268)	\$ 637	\$ (678)
	\$ 1,385	\$ (4,268)	\$ 637	\$ (678)

EXLSERVICE HOLDINGS, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS—(continued)

September 30, 2018

(In thousands, except share and per share amounts)

	Nine months ended September 30,			
	2018		2017	
	As per unaudited consolidated statements of income	Gain/(loss) on foreign currency exchange contracts	As per unaudited consolidated statements of income	Gain/(loss) on foreign currency exchange contracts
Cash flow hedging relationships				
Location in unaudited consolidated statements of income where gain/(loss) was reclassified from AOCI				
Cost of revenues	\$ 429,907	\$ 3,260	\$ 365,883	\$ 3,860
General & administrative expenses	\$ 85,610	523	\$ 75,007	711
Selling & marketing expenses	\$ 45,593	56	\$ 38,631	71
Depreciation & amortization	\$ 35,185	234	\$ 28,489	252
		<u>\$ 4,073</u>		<u>\$ 4,894</u>
Derivatives not designated as hedging instruments				
Location in unaudited consolidated statements of income where gain/(loss) was recognized				
Foreign exchange gain/(loss), net	\$ 3,414	\$ (9,837)	\$ 1,905	\$ 2,095
	<u>\$ 3,414</u>	<u>\$ (9,837)</u>	<u>\$ 1,905</u>	<u>\$ 2,095</u>

18. Borrowings

On October 24, 2014, the Company entered into a credit agreement that provided for a \$50,000 revolving credit facility (the "Credit Facility"). On February 23, 2015, the Company increased the commitments under the Credit Facility by up to an additional \$50,000. The Credit Facility had a maturity date of October 24, 2019 and was voluntarily pre-payable from time to time without premium or penalty. On November 21, 2017, the Company prepaid all outstanding amounts, including accrued interest and fees, and terminated all commitments, under the Credit Agreement.

On November 21, 2017, the Company and each of the Company's wholly owned material domestic subsidiaries entered into a Credit Agreement with certain lenders, and Citibank, N.A. as Administrative Agent (the "New Credit Agreement"). The New Credit Agreement provides for a \$200,000 revolving credit facility (the "New Credit Facility") with an option to increase the commitments by up to \$100,000, subject to certain approvals and conditions as set forth in the New Credit Agreement. The New Credit Agreement also includes a letter of credit sub facility. The New Credit Facility has a maturity date of November 21, 2022 and is voluntarily pre-payable from time to time without premium or penalty. Borrowings under the New Credit Agreement were used to repay amounts outstanding under the Credit Facility and may otherwise be used for working capital and general corporate purposes, including permitted acquisitions. On July 2, 2018, the Company exercised its option under the New Credit Agreement to increase the commitments by \$100,000 thereby utilizing the entire revolver under the New Credit Facility of \$300,000, to fund SCIO acquisition. The incremental commitments were made pursuant to (and constitute part of) the existing commitments and shall be subject to the terms and conditions applicable to the existing commitments as set forth in the New Credit Agreement.

Depending on the type of borrowing, loans under the New Credit Agreement bear interest at a rate equal to the specified prime rate (alternate base rate) or adjusted LIBO rate, plus, in each case, an applicable margin. The applicable margin is tied to the Company's total net leverage ratio and ranges from 0% to 0.75% per annum with respect to loans pegged to the specified prime rate, and 1.00% to 1.75% per annum on loans pegged to the adjusted LIBO rate. The revolving credit commitments under the New

EXLSERVICE HOLDINGS, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS—(continued)

September 30, 2018

(In thousands, except share and per share amounts)

Credit Agreement are subject to a commitment fee, which is also tied to the Company's total net leverage ratio, and ranges from 0.15% to 0.30% per annum on the average daily amount by which the aggregate revolving commitments exceed the sum of outstanding revolving loans and letter of credit obligations.

Obligations under the New Credit Agreement are guaranteed by the Company's material domestic subsidiaries and are secured by all or substantially all of the assets of the Company and our material domestic subsidiaries. The New Credit Agreement contains affirmative and negative covenants, including, but not limited to, restrictions on the ability to incur indebtedness, create liens, make certain investments, make certain dividends and related distributions, enter into, or undertake, certain liquidations, mergers, consolidations or acquisitions and dispose of assets or subsidiaries. In addition, the New Credit Agreement contains a covenant to not permit the interest coverage ratio or the total net leverage ratio, both as defined for the four consecutive quarter period ending on the last day of each fiscal quarter, to be less than 3.5 to 1.0 or more than 3.0 to 1.0, respectively. As of September 30, 2018, the Company was in compliance with all financial and non-financial covenants listed under the New Credit Agreement.

As of September 30, 2018, we had outstanding debt of \$300,000, of which \$12,000 is expected to be repaid within the next twelve months and is included under "current portion of long-term borrowings" and of which \$288,000 is included under "long-term borrowings" in the unaudited consolidated balance sheets. As of December 31, 2017, we had an outstanding debt of \$60,000, of which \$10,000 was included under "current portion of long-term borrowings," and the balance of \$50,000 was included under "long-term borrowings" in the consolidated balance sheets.

The Company incurred certain debt issuance costs, which are deferred and amortized as an adjustment to interest expense over the term of the debt. The unamortized debt issuance costs as of September 30, 2018 and December 31, 2017 was \$1,364 and \$773, respectively, and is included under "other current assets" and "other assets" in the consolidated balance sheets.

Borrowings also includes structured payables which are in the nature of debt, amounting to \$627 and \$709 as of September 30, 2018 and December 31, 2017, respectively, of which \$318 and \$318 is included under "current portion of long-term borrowings", \$309 and \$391, respectively, under "long-term borrowings" in the consolidated balance sheets.

19. Capital Structure

Common Stock

The Company has one class of common stock outstanding.

During the three months ended September 30, 2018 and 2017, the Company did not acquire any shares of common stock from employees in connection with withholding tax payments related to the vesting of restricted stock.

During the nine months ended September 30, 2018 and 2017, the Company acquired 45,646 and 65,003 shares of common stock, respectively, from employees in connection with withholding tax payments related to the vesting of restricted stock for a total consideration of \$2,790 and \$3,016, respectively. The weighted average purchase price per share of \$61.12 and \$46.40, respectively, was the average of the high and low price of the Company's share of common stock on the Nasdaq Global Select Market on the trading day prior to the vesting date of the shares of restricted stock.

On December 30, 2014, the Company's Board of Directors authorized a common stock repurchase program (the "2014 Repurchase Program"), under which shares were authorized to be purchased by the Company from time to time from the open market and through private transactions during each of the fiscal years 2015 through 2017 up to an annual amount of \$20,000.

On February 28, 2017, the Company's Board of Directors authorized an additional common stock repurchase program (the "2017 Repurchase Program"), under which shares may be purchased by the Company from time to time from the open market and through private transactions during each of the fiscal years 2017 through 2019 up to an aggregate additional amount of \$100,000. The approval increased the 2017 authorization from \$20,000 to \$40,000 and authorizes stock repurchases of up to \$40,000 in each of 2018 and 2019.

During the three and nine months ended September 30, 2018, the Company purchased 155,837 and 503,019 shares of its common stock, respectively, for an aggregate purchase price of approximately \$9,657 and \$30,003, respectively, including

EXLSERVICE HOLDINGS, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS—(continued)

September 30, 2018

(In thousands, except share and per share amounts)

commissions, representing an average purchase price per share of \$61.97 and \$59.65, respectively, under the 2017 Repurchase Program.

During the three and nine months ended September 30, 2017, the Company purchased 160,033 and 584,017 shares of its common stock, respectively, for an aggregate purchase price of approximately \$9,004 and \$29,320, respectively, including commissions, representing an average purchase price per share of \$56.26 and \$50.20, respectively, under the 2014 and 2017 Repurchase Programs.

Repurchased shares have been recorded as treasury shares and will be held until the Board of Directors designates that these shares be retired or used for other purposes.

20. Employee Benefit Plans

The Company's Gratuity Plans in India ("Gratuity Plan") provide for lump sum payment to vested employees on retirement or upon termination of employment in an amount based on the respective employee's salary and years of employment with the Company. Liabilities with regard to the Gratuity Plans are determined by actuarial valuation using the projected unit credit method. Current service costs for the Gratuity Plan are accrued in the year to which they relate. Actuarial gains or losses or prior service costs, if any, resulting from amendments to the plans are recognized and amortized over the remaining period of service of the employees.

In addition, the Company's subsidiary operating in the Philippines conforms to the minimum regulatory benefit which provide for lump sum payment to vested employees on retirement from employment in an amount based on the respective employee's salary and years of employment with the Company (the "Philippines Plan"). The benefit costs of the Philippines Plan for the year are calculated on an actuarial basis.

Components of net periodic benefit cost:

	Three months ended September 30,		Nine months ended September 30,	
	2018	2017	2018	2017
Service cost	\$ 431	\$ 491	\$ 1,293	\$ 1,469
Interest cost	173	166	526	494
Expected return on plan assets	(117)	(112)	(359)	(330)
Amortization of actuarial (gain)/loss	(37)	72	(114)	212
Net periodic benefit cost	\$ 450	\$ 617	\$ 1,346	\$ 1,845

On January 1, 2018, the Company adopted ASU 2017-07, Improving the Presentation of Net Periodic Pension Cost and Net Periodic Post-retirement Benefit Cost. Pursuant to this, the Company presented service cost separately from other components of net periodic cost for all periods presented. The interest cost, expected return on plan assets and amortization of actuarial (gain)/loss, have been reclassified from "Cost of revenues", "General and administrative expenses" and "Selling and marketing expenses" to "Other income, net".

EXLSERVICE HOLDINGS, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS—(continued)

September 30, 2018

(In thousands, except share and per share amounts)

The effect of the retrospective presentation change related to the net periodic cost of our defined benefit Gratuity Plan on applicable lines of our unaudited consolidated statements of income was as follows -

	Three months ended September 30, 2017			Nine months ended September 30, 2017		
	As revised	Previously reported*	Effect of change Higher/(Lower)	As revised	Previously reported*	Effect of change Higher/(Lower)
Location in unaudited consolidated statements of income						
Cost of revenues	\$ 123,077	\$ 123,189	\$ (112)	\$ 365,883	\$ 366,216	\$ (333)
General and administrative expenses	\$ 26,545	\$ 26,558	\$ (13)	\$ 75,007	\$ 75,046	\$ (39)
Selling and marketing expenses	\$ 12,196	\$ 12,197	\$ (1)	\$ 38,631	\$ 38,634	\$ (3)
Other income, net	\$ 2,796	\$ 2,922	\$ (126)	\$ 8,495	\$ 8,870	\$ (375)

* Adjusted for the impact of adoption of ASU 2017-12. Refer to Note 17 of the unaudited consolidated financial statements.

The Gratuity Plan in India is partially funded and the Philippines plan is unfunded. The Company makes annual contributions to the employees' gratuity fund established with Life Insurance Corporation of India and HDFC Standard Life Insurance Company. They calculate the annual contribution required to be made by the Company and manage the Gratuity Plans, including any required payouts. Fund managers manage these funds on a cash accumulation basis and declare interest retrospectively on March 31 of each year. The Company earned a return of approximately 7.8% per annum on these Gratuity Plans for the nine months ended September 30, 2018.

Change in Plan Assets

Plan assets at January 1, 2018	\$ 6,915
Business acquisition	210
Actual return	652
Employer contribution	1,191
Benefits paid	(859)
Effect of exchange rate changes	(899)
Plan assets at September 30, 2018	<u>\$ 7,210</u>

The Company maintains several 401(k) plans (the "401(k) Plans") under Section 401(k) of the Internal Revenue Code of 1986 (the "Code"), covering all eligible employees, as defined in the Code as a defined contribution plan. The Company may make discretionary contributions of up to a maximum of 4% of employee compensation within certain limits. The Company made provision for 401(k) Plans amounting to \$645 and \$487 for the three months ended September 30, 2018 and 2017, respectively, and \$2,630 and \$2,051 for the nine months ended September 30, 2018 and 2017, respectively.

On behalf of the Company's employees in India, the Philippines, Bulgaria, Romania, the Czech Republic, South Africa, Colombia and Singapore, the Company contributed \$2,003 and \$1,845 during the three months ended September 30, 2018 and 2017, respectively, and \$5,670 and \$5,350 during the nine months ended September 30, 2018 and 2017, respectively, for various defined contribution plans.

EXLSERVICE HOLDINGS, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS—(continued)

September 30, 2018

(In thousands, except share and per share amounts)

21. Leases

The Company finances its use of certain motor vehicles and other equipment under various lease arrangements provided by financial institutions. Future minimum lease payments under these capital leases as of September 30, 2018 are as follows:

2018 (October 1- December 31)	\$	127
2019		192
2020		135
2021		89
2022		27
2023 and thereafter		12
Total minimum lease payments		582
Less: amount representing interest		(100)
Present value of minimum lease payments		482
Less: current portion		(221)
Long term capital lease obligation	\$	261

The Company conducts its operations using facilities leased under operating lease agreements that expire at various dates. Future minimum lease payments under such agreements expiring after September 30, 2018 are set forth below:

2018 (October 1- December 31)	\$	5,590
2019		21,188
2020		18,779
2021		16,734
2022		14,399
2023 and thereafter		35,706
	\$	112,396

Rent expense

The operating leases are subject to renewal periodically and have scheduled rent increases. The Company recognizes rent expense on such leases on a straight-line basis over cancelable and non-cancelable lease period determined under ASC topic 840, Leases:

	Three months ended September 30,		Nine months ended September 30,	
	2018	2017	2018	2017
Rent expense	\$ 6,596	\$ 6,362	\$ 19,075	\$ 18,168

Deferred rent

	As of	
	September 30, 2018	December 31, 2017
Cancelable and non-cancelable operating leases	\$ 8,508	\$ 8,959

Deferred rent is included under "Accrued expenses and other current liabilities" and "Other non-current liabilities" in the consolidated balance sheets.

EXLSERVICE HOLDINGS, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS—(continued)

September 30, 2018

(In thousands, except share and per share amounts)

22. Income Taxes

The Company determines the tax provision for interim periods using an estimate of its annual effective tax rate adjusted for discrete items, if any, that are taken into account in the relevant period. Each quarter, the Company updates its estimate of annual effective tax rate, and if its estimated tax rate changes, the Company makes a cumulative adjustment.

The Company recorded income tax expense of \$5,739 and \$2,819 for the three months ended September 30, 2018 and 2017, respectively. The effective tax rate increased from 11.8% during the three months ended September 30, 2017 to 27.3% during the three months ended September 30, 2018 primarily as a result of recording of excess tax benefits related to stock awards of \$3,488 pursuant to ASU No. 2016-09 during the three months ended September 30, 2017 compared to \$288 during the three months ended September 30, 2018.

The Company recorded income tax expense of \$6,796 and \$7,202 for the nine months ended September 30, 2018 and 2017, respectively. The effective tax rate increased from 11.0% during the nine months ended September 30, 2017 to 11.4% during the nine months ended September 30, 2018 primarily as a result of: (i) excess tax benefits related to stock awards of \$5,438 pursuant to ASU No. 2016-09 during the nine months ended September 30, 2018 compared to \$7,169 during the nine months ended September 30, 2017, (ii) reversal of uncertain tax position of \$3,153 during the nine months ended September 30, 2017, offset by (iii) an adjustment of \$4,836 during the nine months ended September 30, 2018 reducing the provisional transition tax on the mandatory deemed repatriation of accumulated earnings and profits ("E&P") of foreign subsidiaries recognized during the year-ended December 31, 2017, and (iv) a reduction in the U.S. federal corporate tax rate from 35.0% to 21.0% effective January 1, 2018.

The SEC staff issued Staff Accounting Bulletin ("SAB 118"), which provides guidance on accounting for the tax effects of the U.S. Tax Cuts and Jobs Act of 2017 (the "Tax Reform Act"). SAB 118 provides a measurement period that should not extend beyond one year from the Tax Reform Act enactment date for companies to complete the accounting under ASC 740. In accordance with SAB 118, a company must reflect the income tax effects of those aspects of the Tax Reform Act for which the accounting under ASC 740 is complete. To the extent that a company's accounting for certain income tax effects of the Tax Reform Act is incomplete but it is able to determine a reasonable estimate, it must record a provisional estimate in the financial statements. If a company cannot determine a provisional estimate to be included in the financial statements, it should continue to apply ASC 740 on the basis of the provisions of the tax laws that were in effect immediately before the enactment of the Tax Reform Act.

The deemed repatriation transition tax (the "Transition Tax") is a tax on certain previously untaxed accumulated and current E&P of the Company's foreign subsidiaries. The Company was able to reasonably estimate the Transition Tax and recorded an initial provisional Transition Tax obligation of \$27,236, with a corresponding adjustment of \$27,236 to income tax expense for the year ended December 31, 2017. On the basis of additional technical research and analysis, the Company recognized a measurement-period reduction of \$4,836 to the Transition Tax obligation, with a corresponding adjustment of \$4,836 to income tax expense during the nine months ended September 30, 2018. As of September 30, 2018, a total Transition Tax obligation of \$22,400 has been recorded, with a corresponding adjustment of \$22,400 to the income tax expense. However, the Company continues to gather additional information to more precisely compute the amount of the Transition Tax, and its accounting for this item is not yet complete because of, among other things, changes in the interpretations and assumptions, additional guidance that may be issued by the Internal Revenue Service ("I.R.S."), and actions the Company may take. The Company expects to complete its accounting within the prescribed measurement period.

This inclusion of foreign untaxed earnings resulted in previously taxed income (PTI) which may be subject to withholding taxes and currency gains or losses upon repatriation. The Company does not intend to distribute PTI of its foreign subsidiaries and has not recorded any deferred taxes related to its investment in foreign subsidiaries. The Company estimates that future domestic cash generation will be sufficient to meet future domestic cash needs and has specific plans for use of the subsidiaries earnings. If, in the future, the Company changes its intention regarding the repatriation of PTI, additional taxes may be required and should be recorded in the period the intention changes.

As noted at year-end, the Company was able to reasonably estimate and record provisional adjustments associated with the corporate rate change in the amount of \$1,949. The Company has not made any additional measurement period adjustment related to this item during the nine months ended September 30, 2018 because it continues to evaluate potential method changes and implications of certain provisions of the Act, as well as additional guidance provided by the tax authorities. The Company continues to gather additional information and expects to complete its accounting within the prescribed measurement period.

EXLSERVICE HOLDINGS, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS—(continued)

September 30, 2018

(In thousands, except share and per share amounts)

23. Stock-Based Compensation

The following costs related to the Company's stock-based compensation plans are included in the unaudited consolidated statements of income:

	Three months ended September 30,		Nine months ended September 30,	
	2018	2017	2018	2017
Cost of revenues	\$ 1,116	\$ 1,109	\$ 3,579	\$ 3,448
General and administrative expenses	2,187	2,601	7,536	7,541
Selling and marketing expenses	2,041	1,998	6,196	5,782
Total	\$ 5,344	\$ 5,708	\$ 17,311	\$ 16,771

As of September 30, 2018, the Company had 3,210,120 shares available for grant under the 2018 Omnibus Incentive Plan, which was adopted by the Company's stockholders in September 2018, at which time new awards under the Company's 2015 Amendment and Restatement of the 2006 Omnibus Award Plan were not permitted to be made.

Stock Options

Stock option activity under the Company's stock-based compensation plans is shown below:

	Number of Options	Weighted Avg Exercise Price	Aggregate Intrinsic Value	Weighted Avg Remaining Contractual Life (Years)
Outstanding at December 31, 2017	259,563	\$ 18.03	\$ 10,985	2.76
Granted	—	—	—	—
Exercised	(60,435)	17.93	2,640	—
Forfeited	—	—	—	—
Outstanding at September 30, 2018	199,128	\$ 18.06	\$ 9,586	2.09
Vested and exercisable at September 30, 2018	199,128	\$ 18.06	\$ 9,586	2.09

The unrecognized compensation cost for unvested options as of September 30, 2018 is Nil.

Restricted Stock and Restricted Stock Units

Restricted stock and restricted stock unit activity under the Company's stock-based compensation plans is shown below:

	Restricted Stock		Restricted Stock Units	
	Number	Weighted Average Fair Value	Number	Weighted Average Fair Value
Outstanding at December 31, 2017*	182,267	\$ 42.64	1,046,999	\$ 42.26
Granted	—	—	429,132	60.72
Vested	(41,640)	37.89	(397,112)	39.23
Forfeited	(14,620)	47.91	(80,228)	51.08
Outstanding at September 30, 2018*	126,007	\$ 43.60	998,791	\$ 50.69

* As of September 30, 2018 and December 31, 2017 restricted stock units vested for which the underlying common stock is yet to be issued are 155,753 and 146,112, respectively.

As of September 30, 2018, unrecognized compensation cost of \$41,224 is expected to be expensed over a weighted average period of 2.67 years.

EXLSERVICE HOLDINGS, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS—(continued)

September 30, 2018

(In thousands, except share and per share amounts)

Performance Based Stock Awards

Performance based restricted stock unit (the “PRSUs”) activity under the Company’s stock-based compensation plans is shown below:

	Revenue Based PRSUs		Market Condition Based PRSUs	
	Number	Weighted Average Fair Value	Number	Weighted Average Fair Value
Outstanding at December 31, 2017	113,190	\$ 48.13	113,174	\$ 60.80
Granted	55,268	60.58	55,262	70.97
Vested	—	—	—	—
Forfeited	(21,179)	51.51	(21,176)	63.78
Outstanding at September 30, 2018	147,279	\$ 52.32	147,260	\$ 64.19

As of September 30, 2018, unrecognized compensation cost of \$9,328 is expected to be expensed over a weighted average period of 1.91 years.

24. Related Party Disclosures

The Company provides consulting services to PharmaCord, LLC. One of the Company’s directors, Nitin Sahney, is the member-manager and chief executive officer of PharmaCord, LLC. The Company recognized revenue of \$10 and \$225 in the three months and nine months ended September 30, 2018, respectively, and \$701 and \$1,506 in the three months and nine months ended September 30, 2017, respectively, for services provided.

As of September 30, 2018 and December 31, 2017, the Company had accounts receivable of \$5 and \$140, respectively, related to these services.

25. Commitments and Contingencies**Fixed Asset Commitments**

At September 30, 2018, the Company has committed to spend approximately \$4,980 under agreements to purchase fixed assets. This amount is net of capital advances paid in respect of these purchases.

Other Commitments

Certain units of the Company’s Indian subsidiaries were established as 100% Export-Oriented units or under the Software Technology Parks of India (“STPI”) scheme promulgated by the Government of India. These units are exempt from customs, central excise duties, and levies on imported and indigenous capital goods, stores, and spares. The Company has undertaken to pay custom duties, service taxes, levies, and liquidated damages payable, if any, in respect of imported and indigenous capital goods, stores and spares consumed duty free, in the event that certain terms and conditions are not fulfilled. The Company’s management believes, however, that these units have in the past satisfied and will continue to satisfy the required conditions.

The Company’s operations centers in the Philippines are registered with the Philippine Economic Zone Authority (“PEZA”). The registration provides the Company with certain fiscal incentives on the import of capital goods and requires ExlService Philippines, Inc. to meet certain performance and investment criteria. The Company’s management believes that these centers have in the past satisfied and will continue to satisfy the required criteria.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS—(continued)

September 30, 2018

(In thousands, except share and per share amounts)

Contingencies

U.S. and Indian transfer pricing regulations require that any international transaction involving associated enterprises be at an arm's-length price. Accordingly, the Company determines the appropriate pricing for the international transactions among its associated enterprises on the basis of a detailed functional and economic analysis involving benchmarking against transactions among entities that are not under common control. The tax authorities have jurisdiction to review this arrangement and in the event that they determine that the transfer price applied was not appropriate, the Company may incur increased tax liability, including accrued interest and penalties. The Company is currently involved in disputes with the Indian tax authorities over the application of some of its transfer pricing policies for some of its subsidiaries. Further, the Company and a U.S. subsidiary are engaged in tax litigation with the income-tax authorities in India on the issue of permanent establishment.

The aggregate disputed amount demanded by Indian tax authorities from the Company primarily related to its transfer pricing issues for years ranging from tax years 2003 to 2015 and its permanent establishment issues ranging from tax years 2003 to 2007 as of September 30, 2018 and December 31, 2017 is \$16,407 and \$18,065, respectively, of which the Company has made payments or provided bank guarantee to the extent \$7,863 and \$8,573, respectively. Amounts paid as deposits in respect of such assessments aggregating to \$6,035 and \$6,499 as of September 30, 2018 and December 31, 2017, respectively, are included in "Other assets" and amounts for bank guarantees aggregating to \$1,828 and \$2,074 as of September 30, 2018 and December 31, 2017, respectively, are included in "Restricted cash" in the non-current assets section of the Company's consolidated balance sheets as of September 30, 2018 and December 31, 2017.

Based on the facts underlying the Company's position and its experience with these types of assessments, the Company believes that its position will more likely than not be sustained upon final examination by the tax authorities based on its technical merits as of the reporting date and accordingly has not accrued any amount with respect to these matters in its consolidated financial statements. The Company does not expect any impact from these assessments on its future income tax expense. It is possible that the Company might receive similar orders or assessments from tax authorities for subsequent years. Accordingly even if these disputes are resolved, the Indian tax authorities may still serve additional orders or assessments.

In March 2017, the Company was named in a putative class action lawsuit filed in California, which included several causes of action seeking damages but did not include a monetary demand. The Company filed its answer in April 2017 vigorously denying the allegations. Both parties agreed to participate in a court-approved mediation which occurred in March 2018. The parties reached an agreement in principle whereby the Company, without any admission of wrongdoing or liability, would pay \$2,400 to settle the litigation, which amount has been accrued under "General and administrative expenses" for the nine months ended September 30, 2018. The agreement remains subject to final court approval, which is expected to occur in the fourth quarter of 2018 although there can be no guarantee as to approval or timing.

26. Subsequent Event

On October 1, 2018, the Company entered into an investment agreement (the "Investment Agreement") with Orogen Echo LLC (the "Purchaser"), an affiliate of The Orogen Group LLC, relating to the issuance to the Purchaser of \$150,000 in an aggregate principal amount of 3.50% Convertible Senior Notes due October 1, 2024 (the "Notes"). The transactions contemplated by the Investment Agreement, including the issuance of the Notes, closed on October 4, 2018. The Notes bear interest at a rate of 3.50% per annum, payable semi-annually in arrears in cash on April 1 and October 1 of each year. The Notes are convertible at an initial conversion rate of 13.3333 shares of the common stock per \$1,000 principal amount of the Notes (which represents an initial conversion price of approximately \$75 per share). The Company may elect to settle conversions of the Notes by paying or delivering, as the case may be, cash, shares of the Company's common stock or a combination of cash and shares of the Company's common stock.

The Company entered into a second amendment (the "Amendment") to its Credit Agreement, effective as of November 21, 2017, as amended, among the Company, as borrower, with certain lenders, and Citibank, N.A. as Administrative Agent to, among other things, permit the issuance by the Company of the Notes, and settlement upon maturity or conversion thereof, in accordance with the Investment Agreement, the indenture dated as of October 4, 2018 and the other documents entered into in connection therewith. The Company used the proceeds from the sale of Notes to repay a portion of its outstanding borrowings under the New Credit Facility.

ITEM 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

You should read the following discussion in connection with our unaudited consolidated financial statements and the related notes included elsewhere in this Quarterly Report on Form 10-Q and our audited consolidated financial statements and the related notes included in our Annual Report on Form 10-K for the fiscal year ended December 31, 2017. Some of the statements in the following discussion are forward looking statements. Dollar amounts within Item 2 are presented as actual, approximated, dollar amounts.

Cautionary Note Regarding Forward-Looking Statements

This Quarterly Report on Form 10-Q contains forward-looking statements. You should not place undue reliance on these statements because they are subject to numerous uncertainties and factors relating to our operations and business environment, all of which are difficult to predict and many of which are beyond our control. These statements often include words such as “may,” “will,” “should,” “believe,” “expect,” “anticipate,” “intend,” “plan,” “estimate” or similar expressions. These statements are based on assumptions that we have made in light of our experience in the industry as well as our perceptions of historical trends, current conditions, expected future developments and other factors we believe are appropriate under the circumstances. As you read and consider this Quarterly Report on Form 10-Q, you should understand that these statements are not guarantees of performance or results. They involve known and unknown risks, uncertainties and assumptions. Although we believe that these forward-looking statements are based on reasonable assumptions, you should be aware that many factors could affect our actual financial results or results of operations and could cause actual results to differ materially from those in the forward-looking statements. These factors include but are not limited to:

- our dependence on a limited number of clients in a limited number of industries;
- worldwide political, economic or business conditions;
- negative public reaction in the U.S. or elsewhere to offshore outsourcing;
- fluctuations in our earnings;
- our ability to attract and retain clients including in a timely manner;
- our ability to successfully consummate or integrate strategic acquisitions;
- restrictions on immigration;
- our ability to hire and retain enough sufficiently trained employees to support our operations;
- our ability to grow our business or effectively manage growth and international operations;
- any changes in the senior management team;
- increasing competition in our industry;
- telecommunications or technology disruptions;
- our ability to withstand the loss of a significant customer;
- regulatory, legislative and judicial developments, including changes to or the withdrawal of governmental fiscal incentives;
- changes in tax laws or decisions regarding repatriation of funds held abroad;
- ability to service debt or obtain additional financing on favorable terms;
- legal liability arising out of customer contracts;
- technological innovation;
- political or economic instability in the geographies in which we operate;
- cyber security incidents, data breaches, or other unauthorized disclosure of sensitive or confidential client and customer data; and
- adverse outcome of our disputes with the Indian tax authorities.

These and other factors are more fully discussed in our Annual Report on Form 10-K for the fiscal year ended December 31, 2017. These and other risks could cause actual results to differ materially from those implied by forward-looking statements in this Quarterly Report on Form 10-Q.

The forward-looking statements made by us in this Quarterly Report on Form 10-Q, or elsewhere, speak only as of the date on which they were made. New risks and uncertainties come up from time to time, and it is impossible for us to predict those events or how they may affect us. We have no obligation to update any forward-looking statements in this Quarterly Report on Form 10-Q after the date of this Quarterly Report on Form 10-Q, except as required by federal securities laws.

Executive Overview

We are an operations management and analytics company that helps businesses enhance revenue growth and improve profitability. Using proprietary platforms, methodologies, and our full range of digital capabilities, we look deeper to help companies transform their businesses, functions and operations, to help them deliver better customer experience and business outcomes, while managing risk and compliance. We serve our customers in the insurance, healthcare, travel, transportation and logistics, banking and financial services and utilities industries, among others.

We operate in the business process management (“BPM”) industry and we provide operations management and analytics services. Our eight operating segments are strategic business units that align our products and services with how we manage our business, approach our key markets and interact with our clients. Six of those operating segments provide BPM or “operations management” services, five of which are industry focused operating segments (Insurance, Healthcare, Travel, Transportation and Logistics, Banking and Financial Services, and Utilities) and one of which is a “capability” operating segment (Finance and Accounting) that provides services to clients in our industry-focused segments as well as clients across other industries. In each of these six operating segments we provide operations management services, which typically involve transfer to the Company of the business operations of a client, after which we administer and manage those operations for our client on an ongoing basis. Our remaining two operating segments are Consulting, which provides industry-specific digital transformational services related to operations management services, and Analytics, which provides services that focus on driving improved business outcomes for clients by generating data-driven insights across all parts of their business.

We present information for the following reportable segments:

- Insurance,
- Healthcare,
- Travel, Transportation and Logistics,
- Finance and Accounting,
- Analytics, and
- All Other (consisting of our remaining operating segments, which are our Banking and Financial services, Utilities and Consulting operating segments).

Our global delivery network, which include highly trained industry and process specialists across the United States, Latin America, South Africa, Europe and Asia (primarily India and the Philippines), is a key asset. We have operations centers in India, the U.S., the Philippines, Bulgaria, Colombia, South Africa, Romania and the Czech Republic.

Consistent with our growth strategy, on December 22, 2017, we acquired substantially all of the assets and assumed certain liabilities related thereto of Health Integrated, Inc. (“Health Integrated”).

The acquisition of Health Integrated is included in the Healthcare reportable segment. Health Integrated provides dedicated care management services on behalf of health plans. Its services include case management, utilization management, disease management, special needs programs and multichronic care management. Health Integrated serves millions of lives in the Medicaid, Medicare, and dual eligible populations.

The July 2018 acquisition of SCIO is included in Analytics reportable segment. It provides health analytics solution and serving over 100 healthcare organizations representing over 130 million covered lives across the continuum including providers, health plans, pharmacy benefit managers, employers, health services and global life sciences companies.

Revenues

For the three months ended September 30, 2018, we had revenues of \$231.1 million compared to revenues of \$192.3 million for the three months ended September 30, 2017, an increase of \$38.8 million, or 20.2%. For the nine months ended September 30, 2018, we had revenues of \$648.2 million compared to revenues of \$564.4 million for the nine months ended September 30, 2017, an increase of \$83.8 million, or 14.8%.

We serve clients mainly in the U.S. and the U.K., with these two regions generating 82.9% and 12.9%, respectively, of our total revenues for the three months ended September 30, 2018, and 82.4% and 13.9%, respectively, of our revenues for the three months ended September 30, 2017. For the nine months ended September 30, 2018, these two regions generated 82.8% and 13.2%, respectively, of our total revenues and 82.0% and 14.5%, respectively, of our total revenues for the nine months ended September 30, 2017.

[Table of Contents](#)

For the three months ended September 30, 2018 and 2017, our total revenues from our top ten clients accounted for 36.7% and 38.3% of our total revenues, respectively. For the nine months ended September 30, 2018 and 2017, our total revenues from our top ten clients accounted for 37.9% and 38.7% of our total revenues, respectively. Our revenue concentration with our top clients remains consistent year-over-year and we continue to develop relationships with new clients to diversify our client base. We believe that the loss of any of our ten largest clients could have a material adverse effect on our financial performance.

Our Business

We provide operations management and analytics services. We market our services to our existing and prospective clients through our sales and client management teams, which are aligned by key industry verticals and cross-industry domains such as finance and accounting. Our sales and client management teams operate from the U.S., Europe and Australia.

Operations Management Services: We provide our clients with a range of operations management services principally in the insurance, healthcare, travel, transportation and logistics, banking and financial services and utilities sectors, among others, as well as cross-industry operations management services, such as finance and accounting services. We also provide services related to operations management, through our Consulting services that provide advice regarding transformational initiatives.

Our operations management solutions typically involve the transfer to the Company business operations of a client such as claims processing, clinical operations, or financial transaction processing, after which we administer and manage the operations for our client on an ongoing basis. As part of this transfer, we hire and train employees to work at our operations centers on the relevant business operations, implement a process migration to these operations centers and then provide services either to the client or directly to the client's customers. Each client contract has different terms based on the scope, deliverables and complexity of the engagement.

We have been observing a shift in industry pricing models toward transaction-based pricing, outcome-based pricing and other pricing models. We believe this trend will continue and we have begun to use such alternative pricing models with some of our current clients and are seeking to move certain other clients from a billing rate model to a transaction-based or other pricing model. These pricing models place the focus on operating efficiency in order to maintain our gross margins. In addition, we have also observed that prospective larger clients are entering into multi-vendor relationships with regard to their outsourcing needs. We believe that the trend toward multi-vendor relationships will continue. A multi-vendor relationship allows a client to seek more favorable pricing and other contract terms from each vendor, which can result in significantly reduced gross margins from the provision of services to such client for each vendor. To the extent our large clients expand their use of multi-vendor relationships and are able to extract more favorable contract terms from other vendors, our gross margins and revenues may be reduced with regard to such clients if we are required to modify the terms of our relationships with such clients to meet competition.

Our existing agreements with original terms of three or more years provide us with a relatively predictable revenue base for a substantial portion of our operations management business, however, we have a long selling cycle for our services and the budget and approval processes of prospective clients make it difficult to predict the timing of entering into definitive agreements with new clients. Similarly, new license sales and implementation projects for our technology service platforms and other software-based services have a long selling cycle, however ongoing annual maintenance and support contracts for existing arrangements provide us with a relatively predictable revenue base.

Analytics: Our Analytics services focus on driving improved business outcomes for our customers by generating data-driven insights across all parts of our customers' business. We also provide care optimization and reimbursements optimization services, for our clients through our healthcare analytics solutions and services. We also offer integrated solutions to help our clients in cost containment by leveraging technology platforms, customizable and configurable analytics and expertise in healthcare reimbursements to help clients enhance their claim payment accuracy. Our teams deliver predictive and prescriptive analytics in the areas of customer acquisition and lifecycle management, risk underwriting and pricing, operational effectiveness, credit and operational risk monitoring and governance, regulatory reporting, payment integrity and care management, and data management. We actively cross-sell and, where appropriate, integrate our Analytics services with other operations management services as part of a comprehensive offering set for our clients.

We anticipate that revenues from our Analytics services will grow as we expand our service offerings and client base, both organically and through acquisitions.

Critical Accounting Policies and Estimates

For a description of our critical accounting policies and estimates, refer to “Management’s Discussion and Analysis of Financial Condition and Results of Operations – Critical Accounting Policies and Estimates” and Note 2 to the consolidated financial statements included in our Annual Report on Form 10-K for the fiscal year ended December 31, 2017. For Revenue Recognition refer to Note 2 to the unaudited consolidated financial statements contained herein.

Results of Operations

The following table summarizes our results of operations for the three and nine months ended September 30, 2018 and 2017:

	Three months ended September 30,		Nine months ended September 30,	
	2018	2017	2018	2017
	(dollars in millions)		(dollars in millions)	
Revenues, net	\$ 231.1	\$ 192.3	\$ 648.2	\$ 564.4
Cost of revenues ⁽¹⁾	152.2	123.1	429.9	365.9
Gross profit⁽¹⁾	78.9	69.2	218.3	198.5
Operating expenses:				
General and administrative expenses	28.7	26.5	85.6	75.0
Selling and marketing expenses	16.4	12.2	45.6	38.6
Depreciation and amortization	14.1	9.6	35.2	28.5
Total operating expenses	59.2	48.3	166.4	142.1
Income from operations	19.7	20.9	51.9	56.4
Foreign exchange gain, net	1.4	0.6	3.4	1.9
Interest expense	(2.5)	(0.4)	(3.7)	(1.4)
Other income, net	2.5	2.8	8.2	8.5
Income before income tax expense	21.1	23.9	59.8	65.4
Income tax expense	5.7	2.8	6.8	7.2
Loss from equity-method investment	0.1	—	0.2	—
Net income attributable to ExlService Holdings, Inc. stockholders	\$ 15.3	\$ 21.1	\$ 52.8	\$ 58.2

(1) Exclusive of depreciation and amortization.

Three Months Ended September 30, 2018 Compared to Three Months Ended September 30, 2017

Revenues.

The following table summarizes our revenues by reportable segments for the three months ended September 30, 2018 and 2017:

	Three months ended September 30,		Change	Percentage change
	2018	2017		
	(dollars in millions)			
Insurance	\$ 64.3	\$ 59.6	\$ 4.7	7.9 %
Healthcare	20.4	18.9	1.5	8.0 %
Travel, Transportation and Logistics	17.3	18.5	(1.2)	(6.6)%
Finance and Accounting	24.5	21.6	2.9	13.3 %
All Other	21.9	20.0	1.9	9.8 %
Analytics	82.7	53.7	29.0	53.9 %
Total revenues, net	\$ 231.1	\$ 192.3	\$ 38.8	20.2 %

Revenues for the three months ended September 30, 2018 were \$231.1 million, up \$38.8 million or 20.2%, compared to the three months ended September 30, 2017.

Revenue growth in Insurance of \$4.7 million was primarily driven by expansion of business from our new and existing clients of \$5.4 million. This was partially offset by \$0.7 million attributable to the depreciation of the Indian rupee against the U.S. dollar during the three months ended September 31, 2018 compared to the three months ended September 31, 2017. Insurance revenues were 27.8% and 31.0% of our total revenues in the three months ended September 30, 2018 and September 30, 2017, respectively.

Revenue growth in Healthcare of \$1.5 million was primarily driven by our acquisition of Health Integrated in 2017, contributing \$3.7 million. This was partially offset by lower revenues of \$2.2 million due to the termination of certain client contracts. Healthcare revenues were 8.8% and 9.8% of our total revenues in the three months ended September 30, 2018 and September 30, 2017, respectively.

Revenue decline in Travel, Transportation and Logistics ("TT&L") of \$1.2 million was primarily driven by net lower volumes from our existing clients of \$0.9 million. The remaining decrease of \$0.3 million was attributable to the depreciation of the Indian rupee and Philippine peso against the U.S. dollar during the three months ended September 31, 2018 compared to the three months ended September 31, 2017. TT&L revenues were 7.5% and 9.6% of our total revenues in the three months ended September 30, 2018 and September 30, 2017, respectively.

Revenue growth in Finance and Accounting ("F&A") of \$2.9 million was driven by net volume increases from our new and existing clients of \$3.4 million. This was partially offset by \$0.5 million attributable to the depreciation of the Indian rupee against the U.S. dollar during the three months ended September 31, 2018 compared to the three months ended September 31, 2017. F&A revenues were 10.6% and 11.3% of our total revenues in the three months ended September 30, 2018 and September 30, 2017, respectively.

Revenue growth in All Other of \$1.9 million was primarily driven by higher revenues of \$3.1 million in the Consulting operating segment and \$0.3 million in our Utilities operating segment, partially offset by lower revenues of \$0.6 million in our Banking and Financial Services operating segment. This was partially offset by \$0.8 million due to the depreciation of the Indian rupee against the U.S. dollar. All Other revenues were 9.5% and 10.4% of our total revenues in the three months ended September 30, 2018 and September 30, 2017, respectively.

Revenue growth in Analytics of \$29.0 million was primarily driven by our acquisition of SCIO in July 2018 contributing \$19.2 million. The remaining increase of \$9.8 million was attributable to recurring and project based engagements from our new and existing clients. Analytics revenues were 35.8% and 27.9% of our total revenues in the three months ended September 30, 2018 and September 30, 2017, respectively.

Cost of Revenues and Gross Margin: The following table sets forth cost of revenues and gross margin of our reportable segments.

	Cost of Revenues				Gross Margin		
	Three months ended September 30,		Change	Percentage change	Three months ended September 30,		Change
	2018	2017			2018	2017	
	(dollars in millions)						
Insurance	\$ 43.5	\$ 39.2	\$ 4.3	11.1 %	32.3%	34.3%	(2.0)%
Healthcare	15.8	12.1	3.7	30.9 %	22.5%	36.0%	(13.5)%
TT&L	10.0	10.0	—	(0.4)%	42.4%	46.0%	(3.6)%
F&A	15.0	12.6	2.4	18.1 %	39.2%	41.6%	(2.4)%
All Other	14.3	13.6	0.7	5.5 %	34.7%	32.1%	2.6 %
Analytics	53.6	35.6	18.0	50.5 %	35.1%	33.7%	1.4 %
Total	\$ 152.2	\$ 123.1	\$ 29.1	23.6 %	34.2%	36.0%	(1.8)%

For the three months ended September 30, 2018, cost of revenues was \$152.2 million compared to \$123.1 million for the three months ended September 30, 2017, an increase of \$29.1 million, or 23.6%. Our gross margin for the three months ended September 30, 2018 was 34.2% compared to 36.0% for three months ended September 30, 2017, a decrease of 180 basis points (“bps”).

The increase in cost of revenues in Insurance of \$4.3 million was primarily due to an increase in employee-related costs of \$4.5 million on account of higher headcount and wage inflation, technology and infrastructure costs of \$0.6 million and travel costs of \$0.2 million, partially offset by lower professional fees and other operating costs of \$0.3 million and currency movements net of hedging of \$0.5 million. Gross margin in Insurance decreased by 200 bps during the three months ended September 30, 2018 compared to the three months ended September 30, 2017.

The increase in cost of revenues in Healthcare of \$3.7 million was primarily due to an increase in employee-related costs of \$3.1 million and technology costs of \$0.7 million related to our acquisition of Health Integrated in 2017, partially offset by currency movements net of hedging of \$0.2 million. Gross margin in Healthcare decreased by 1350 bps during the three months ended September 30, 2018 compared to the three months ended September 30, 2017, primarily due to the impact of acquisition of Health Integrated and the termination of certain client contracts.

The cost of revenues in TT&L were flat during the three months ended September 30, 2018 compared to the three months ended September 30, 2017. Gross margin in TT&L decreased by 360 bps during the three months ended September 30, 2018 compared to the three months ended September 30, 2017, primarily due to lower volumes in existing clients.

The increase in cost of revenues in F&A of \$2.4 million was primarily due to an increase in employee-related costs of \$2.0 million on account of higher headcount and wage inflation, technology and infrastructure costs of \$0.4 million and travel costs of \$0.2 million, partially offset by currency movements net of hedging of \$0.3 million. Gross margin in F&A decreased by 240 bps during the three months ended September 30, 2018 compared to the three months ended September 30, 2017, primarily due to higher operating expenses associated with the initiation of services for new clients.

The increase in cost of revenues in All Other of \$0.7 million was primarily due to an increase in employee-related costs of \$1.2 million on account of higher headcount and wage inflation, partially offset by other operating costs of \$0.1 million and currency movements net of hedging of \$0.4 million. Gross margin in All Other increased by 260 bps during the three months ended September 30, 2018 compared to the three months ended September 30, 2017, primarily due to higher revenues in our Consulting operating segment.

The increase in cost of revenues in Analytics of \$18.0 million was primarily due to an increase in employee-related costs of \$13.4 million on account of higher headcount and wage inflation, including incremental cost related to our acquisition of SCIO in July 2018 of \$9.8 million. The remaining increase was attributable to technology and infrastructure costs of \$1.2 million, travel costs of \$0.8 million, professional fees of \$0.6 million and other operating costs of \$2.6 million, partially offset by currency movements net of hedging of \$0.5 million. Gross margin in Analytics increased by 140 bps during the three months ended September 30, 2018 compared to the three months ended September 30, 2017, primarily due to higher revenues.

Selling, General and Administrative (“SG&A”) Expenses.

	Three months ended September 30,		Change	Percentage change
	2018	2017		
	(dollars in millions)			
General and administrative expenses	\$ 28.7	\$ 26.5	\$ 2.2	8.1%
Selling and marketing expenses	16.4	12.2	4.2	35.2%
Selling, general and administrative expenses	<u>\$ 45.1</u>	<u>\$ 38.7</u>	<u>\$ 6.4</u>	<u>16.7%</u>
As a percentage of revenues	19.6%	20.1%		

The increase in SG&A expenses of \$6.4 million was primarily due to an increase in employee-related costs of \$6.6 million, including incremental costs of \$4.6 million related to our Health Integrated acquisition in 2017 and SCIO acquisition in July 2018 and other costs of \$0.3 million. This was partially offset by currency movements net of hedging of \$0.5 million.

Depreciation and Amortization.

	Three months ended September 30,		Change	Percentage change
	2018	2017		
	(dollars in millions)			
Depreciation expense	\$ 7.4	\$ 6.1	\$ 1.3	21.1%
Intangible amortization expense	6.7	3.5	3.2	92.7%
Depreciation and amortization expense	<u>\$ 14.1</u>	<u>\$ 9.6</u>	<u>\$ 4.5</u>	<u>47.1%</u>
As a percentage of revenues	6.1%	5.0%		

The increase in intangibles amortization expense of \$3.2 million was primarily due to amortization of intangibles associated with our Health Integrated acquisition in 2017 and SCIO acquisition in July 2018. The increase in depreciation expense of \$1.3 million was due to depreciation related to our new operating centers commenced during 2017 to support our business growth and depreciation associated with our acquisitions.

Income from Operations. Income from operations decreased by \$1.2 million, or 6.1%, from \$20.9 million for the three months ended September 30, 2017 to \$19.7 million for the three months ended September 30, 2018. As a percentage of revenues, income from operations decreased from 10.9% for the three months ended September 30, 2017 to 8.5% for the three months ended September 30, 2018.

Foreign Exchange Gain/(Loss). Net foreign exchange gains and losses are primarily attributable to movement of the U.S. dollar against the Indian rupee, the U.K. pound sterling and the Philippine peso during the three months ended September 30, 2018. The average exchange rate of the U.S. dollar against the Indian rupee increased from 64.45 during the three months ended September 30, 2017 to 70.67 during the three months ended September 30, 2018. The average exchange rate of the U.K. pound sterling against the U.S. dollar remained flat at 1.31 during the three months ended September 30, 2017 and September 30, 2018. The average exchange rate of the U.S. dollar against the Philippine peso increased from 50.82 during the three months ended September 30, 2017 to 53.53 during the three months ended September 30, 2018.

We recorded a net foreign exchange gain of \$1.4 million for the three months ended September 30, 2018 compared to the net foreign exchange gain of \$0.6 million for the three months ended September 30, 2017.

Interest expense. Interest expense increased from \$0.4 million for the three months ended September 30, 2017 to \$2.5 million for the three months ended September 30, 2018 primarily due to higher borrowings to finance our SCIO acquisition in July 2018 and higher interest rates under our New Credit Facility (as defined below in “Liquidity and Capital Resources-Financing Arrangements”).

Other Income, net.

	Three months ended September 30,		Change	Percentage change
	2018	2017		
	(dollars in millions)			
Interest and dividend income	\$ 0.5	\$ 0.3	\$ 0.2	62.4 %
Gain on mutual fund investments	2.2	2.6	(0.4)	(14.7)%
Other, net	(0.2)	(0.1)	(0.1)	(189.0)%
Other income, net	<u>\$ 2.5</u>	<u>\$ 2.8</u>	<u>\$ (0.3)</u>	<u>(11.8)%</u>

Other income, net decreased by \$0.3 million, from \$2.8 million for the three months ended September 30, 2017 to \$2.5 million for the three months ended September 30, 2018, primarily due to lower yields on our mutual fund investments of \$0.4 million. This decrease was partially offset by an increase in interest and dividend income of \$0.2 million during the three months ended September 30, 2018 compared to three months ended September 30, 2017.

Income Tax Expense. The effective tax rate increased from 11.8% during the three months ended September 30, 2017 to 27.3% during the three months ended September 30, 2018 primarily as a result of a recording of excess tax benefit related to stock awards of \$3.5 million pursuant to ASU No. 2016-09 during the three months ended September 30, 2017 compared to \$0.3 million during the three months ended September 30, 2018.

Net Income. Net income decreased from \$21.1 million for the three months ended September 30, 2017 to \$15.3 million for the three months ended September 30, 2018, primarily due to higher income tax expense of \$2.9 million, higher interest expense \$2.1 million, decrease in income from operations of \$1.2 million and other income, net of \$0.3 million, partially offset by a higher foreign exchange gain of \$0.8 million. As a percentage of revenues, net income decreased from 11.0% for the three months ended September 30, 2017 to 6.6% for the three months ended September 30, 2018.

Nine Months Ended September 30, 2018 Compared to Nine Months Ended September 30, 2017

Revenues.

The following table summarizes our revenues by reportable segment for the nine months ended September 30, 2018 and 2017:

	Nine months ended September 30,		Change	Percentage change
	2018	2017		
	(dollars in millions)			
Insurance	\$ 193.0	\$ 173.8	\$ 19.2	11.1%
Healthcare	63.0	56.7	6.3	11.0%
Travel, Transportation and Logistics	53.4	53.4	—	—
Finance and Accounting	72.7	63.7	9.0	14.2%
All Other	66.7	62.5	4.2	6.7%
Analytics	199.4	154.3	45.1	29.2%
Total revenues, net	<u>\$ 648.2</u>	<u>\$ 564.4</u>	<u>\$ 83.8</u>	<u>14.8%</u>

Revenues for the nine months ended September 30, 2018 were \$648.2 million, up \$83.8 million or 14.8%, compared to the nine months ended September 30, 2017.

Revenue growth in Insurance of \$19.2 million was driven by expansion of business from our new and existing clients. Insurance revenues were 29.8% and 30.8% of our total revenues in the nine months ended September 30, 2018 and September 30, 2017, respectively.

Revenue growth in Healthcare of \$6.3 million was primarily driven by our acquisition of Health Integrated in 2017 contributing \$13.6 million. This was partially offset by lower revenues of \$7.3 million due to the termination of certain client contracts. Healthcare revenues were 9.7% and 10.1% of our total revenues in each of the nine months ended September 30, 2018 and September 30, 2017, respectively.

[Table of Contents](#)

Revenue growth in TT&L was flat during the nine months ended September 30, 2018 compared to the nine months ended September 30, 2017. TT&L revenues were 8.2% and 9.5% of our total revenues in the nine months ended September 30, 2018 and September 30, 2017, respectively.

Revenue growth in F&A of \$9.0 million was driven by net volume increases from our new and existing clients. F&A revenues were 11.2% and 11.3% of our total revenues in the nine months ended September 30, 2018 and September 30, 2017, respectively.

Revenue growth in All Other of \$4.2 million was primarily driven by higher revenues of \$8.7 million in the Consulting operating segment, partially offset by lower revenues in our Utilities operating segment of \$2.4 million and Banking and Financial Services operating segment of \$1.8 million and a net impact of foreign exchange loss of \$0.4 million primarily due to the depreciation of the Indian rupee and appreciation of U.K. pound sterling against the U.S. dollar during the nine months ended September 30, 2018 compared to the nine months ended September 30, 2017. All Other revenues were 10.3% and 11.1% of our total revenues in the nine months ended September 30, 2018 and September 30, 2017, respectively.

Revenue growth in Analytics of \$45.1 million was driven by our acquisition of SCIO in July 2018, contributing \$19.2 million. The remaining increase of \$25.6 million was attributable by our recurring and project-based engagements from our new and existing clients and \$0.4 million attributable to the net impact of the appreciation of U.K. pound sterling against the U.S. dollar during the nine months ended September 30, 2018 compared to the nine months ended September 30, 2017. Analytics revenues were 30.8% and 27.3% of our total revenues in the nine months ended September 30, 2018 and September 30, 2017, respectively.

Cost of Revenues and Gross Margin: The following table sets forth cost of revenues and gross margin of our reportable segments.

	Cost of Revenues				Gross Margin		
	Nine months ended September 30,		Change	Percentage change	Nine months ended September 30,		Change
	2018	2017			2018	2017	
	(dollars in millions)						
Insurance	\$ 130.0	\$ 117.7	\$ 12.3	10.5%	32.7%	32.3%	0.4 %
Healthcare	49.7	36.7	13.0	35.6%	21.0%	35.3%	(14.3)%
TT&L	31.0	30.5	0.5	1.9%	41.8%	42.9%	(1.1)%
F&A	44.2	37.4	6.8	18.2%	39.2%	41.3%	(2.1)%
All Other	44.6	42.6	2.0	4.6%	33.2%	31.8%	1.4 %
Analytics	130.4	101.0	29.4	29.0%	34.6%	34.5%	0.1 %
Total	\$ 429.9	\$ 365.9	\$ 64.0	17.5%	33.7%	35.2%	(1.5)%

For the nine months ended September 30, 2018, cost of revenues was \$429.9 million compared to \$365.9 million for the nine months ended September 30, 2017, an increase of \$64.0 million, or 17.5%. Our gross margin for the nine months ended September 30, 2018 was 33.7% compared to 35.2% for nine months ended September 30, 2017, a decrease of 150 basis points (“bps”).

The increase in cost of revenues in Insurance of \$12.3 million was primarily due to an increase in employee-related costs of \$10.9 million on account of higher headcount and wage inflation, technology and infrastructure costs of \$1.3 million, travel and other operating costs of \$1.7 million, partially offset by lower professional fees of \$1.3 million and currency movements net of hedging of \$0.4 million. Gross margin in Insurance increased by 40 bps during the nine months ended September 30, 2018 compared to the nine months ended September 30, 2017, primarily due to higher revenues and margin expansion in existing clients.

The increase in cost of revenues in Healthcare of \$13.0 million was primarily due to an increase in employee-related costs of \$11.7 million, technology and infrastructure costs of \$3.0 million, on account of our acquisition of Health Integrated in 2017, partially offset by decrease in other operating costs of \$1.3 million and currency movements net of hedging of \$0.4 million. Gross margin in Healthcare decreased by 1,430 bps during the nine months ended September 30, 2018 compared to the nine months ended September 30, 2017, primarily due to the impact of acquisition of Health Integrated and the termination of certain client contracts.

The increase in cost of revenues in TT&L of \$0.5 million was primarily due to an increase in employee-related costs of \$0.6 million and other operating costs of \$0.3 million, partially offset by currency movements net of hedging of \$0.4 million. Gross margin in TT&L decreased by 110 bps during the nine months ended September 30, 2018 compared to the nine months ended September 30, 2017.

Table of Contents

The increase in cost of revenues in F&A of \$6.8 million was primarily due to an increase in employee-related costs of \$4.9 million on account of higher headcount and wage inflation, technology and infrastructure costs of \$1.2 million, and travel costs of \$1.0 million, partially offset by currency movements net of hedging of \$0.3 million. Gross margin in F&A decreased by 210 bps during the nine months ended September 30, 2018 compared to the nine months ended September 30, 2017, primarily due to higher operating expenses associated with the initiation of services for new clients.

The increase in cost of revenues in All Other of \$2.0 million was primarily due to an increase in employee-related costs of \$2.0 million on account of higher headcount and wage inflation and other operating costs of \$0.3 million, partially offset by currency movements net of hedging of \$0.3 million. Gross margin in All Other increased by 140 bps during the nine months ended September 30, 2018 compared to the nine months ended September 30, 2017, primarily due to higher revenues in our Consulting operating segment.

The increase in cost of revenues in Analytics of \$29.4 million was primarily due to an increase in employee-related costs of \$21.1 million on account of higher headcount and wage inflation, including incremental cost related to our acquisition of SCIO in July 2018 of \$9.8 million. The remaining increase was attributable to technology and infrastructure costs of \$2.3 million, professional fees of \$0.9 million, travel costs of \$1.1 million and other operating costs of \$4.3 million, partially offset by currency movements net of hedging of \$0.3 million. Gross margin in Analytics increased by 10 bps during the nine months ended September 30, 2018 compared to the nine months ended September 30, 2017, primarily due to higher revenues.

Selling, General and Administrative (“SG&A”) Expenses.

	Nine months ended September 30,		Change	Percentage change
	2018	2017		
	(dollars in millions)			
General and administrative expenses	\$ 85.6	\$ 75.0	\$ 10.6	14.1%
Selling and marketing expenses	45.6	38.6	7.0	18.0%
Selling, general and administrative expenses	\$ 131.2	\$ 113.6	\$ 17.6	15.5%
As a percentage of revenues	20.2%	20.1%		

The increase in SG&A expenses of \$17.6 million was primarily due to an increase in employee-related costs of \$12.8 million, including incremental costs of \$8.1 million relating to our Health Integrated acquisition in 2017 and SCIO acquisition in July 2018. There was a further increase of \$5.1 million due to continued investments in strategic initiatives, product development, digital technology, advance automation and robotics, partially offset by currency movements net of hedging of \$0.3 million.

Depreciation and Amortization.

	Nine months ended September 30,		Change	Percentage change
	2018	2017		
	(dollars in millions)			
Depreciation expense	\$ 20.8	\$ 18.0	\$ 2.8	15.3%
Intangible amortization expense	14.4	10.5	3.9	37.5%
Depreciation and amortization expense	\$ 35.2	\$ 28.5	\$ 6.7	23.5%
As a percentage of revenues	5.4%	5.0%		

The increase in intangibles amortization expense of \$3.9 million was primarily due to amortization of intangibles associated with our Health Integrated acquisition in 2017 and SCIO acquisition in July 2018. The increase in depreciation expense of \$2.8 million was due to depreciation related to our new operating centers commenced during 2017 to support our business growth and depreciation associated with our acquisitions.

Income from Operations. Income from operations decreased by \$4.5 million, or 8.0%, from \$56.4 million for the nine months ended September 30, 2017 to \$51.9 million for the nine months ended September 30, 2018. As a percentage of revenues, income from operations decreased from 10.0% for the nine months ended September 30, 2017 to 8.0% for the nine months ended September 30, 2018.

Foreign Exchange Gain/(Loss). Net foreign exchange gains and losses are primarily attributable to movement of the U.S. dollar against the Indian rupee, the U.K. pound sterling and the Philippine peso during the nine months ended September 30, 2018. The average exchange rate of the U.S. dollar against the Indian rupee increased from 65.12 during the

Table of Contents

nine months ended September 30, 2017 to 67.61 during the nine months ended September 30, 2018. The average exchange rate of the U.K. pound sterling against the U.S. dollar increased from 1.28 during the nine months ended September 30, 2017 to 1.35 during the nine months ended September 30, 2018. The average exchange rate of the U.S. dollar against the Philippine peso increased from 50.31 during the nine months ended September 30, 2017 to 52.64 during the nine months ended September 30, 2018.

We recorded a net foreign exchange gain of \$3.4 million for the nine months ended September 30, 2018 compared to the net foreign exchange gain of \$1.9 million for the nine months ended September 30, 2017.

Interest expense. Interest expense increased from \$1.4 million for the nine months ended September 30, 2017 to \$3.7 million for the nine months ended September 30, 2018 primarily due to higher borrowings for our SCIO acquisition in July 2018 and higher interest rates under our New Credit Facility.

Other Income, net.

	Nine months ended September 30,		Change	Percentage change
	2018	2017		
	(dollars in millions)			
Interest and dividend income	\$ 1.1	\$ 1.3	\$ (0.2)	(11.9)%
Gain on mutual fund investments	7.0	6.8	0.2	3.4 %
Other, net	0.1	0.4	(0.3)	(83.8)%
Other income, net	<u>\$ 8.2</u>	<u>\$ 8.5</u>	<u>\$ (0.3)</u>	<u>(3.1)%</u>

Other income, net decreased by \$0.3 million, from \$8.5 million for the nine months ended September 30, 2017 to \$8.2 million for the nine months ended September 30, 2018 primarily due to lower interest and dividend income on our mutual fund investments of \$0.2 million.

Income Tax Expense. The effective tax rate increased from 11.0% during the nine months ended September 30, 2017 to 11.4% during the nine months ended September 30, 2018 primarily as a result of: (i) excess tax benefits related to stock awards of \$5.4 million pursuant to ASU No. 2016-09 during the nine months ended September 30, 2018 compared to \$7.2 million during the nine months ended September 30, 2017, (ii) reversal of uncertain tax position of \$3.2 million during the nine months ended September 30, 2017, offset by (iii) an adjustment during the nine months ended September 30, 2018 of \$4.8 million in reducing the provisional transition tax on the mandatory deemed repatriation of accumulated earnings and profits ("E&P") of foreign subsidiaries recognized during the year-ended December 31, 2017, and (iv) a reduction in the U.S. federal corporate tax rate from 35.0% to 21.0% effective January 1, 2018.

Net Income. Net income decreased from \$58.2 million for the nine months ended September 30, 2017 to \$52.8 million for the nine months ended September 30, 2018, primarily due to decrease in income from operations of \$4.5 million and higher interest expense of \$2.3 million, partially offset by higher foreign exchange gain of \$1.5 million. As a percentage of revenues, net income decreased from 10.3% for the nine months ended September 30, 2017 to 8.2% for the nine months ended September 30, 2018.

Liquidity and Capital Resources

	Nine months ended September 30,	
	2018	2017
	(dollars in millions)	
Opening cash, cash equivalents and restricted cash	\$ 94.3	\$ 220.4
Net cash provided by operating activities	46.9	70.4
Net cash used for investing activities	(240.4)	(171.1)
Net cash (used for)/provided by financing activities	208.1	(28.2)
Effect of exchange rate changes	(3.1)	1.8
Closing cash, cash equivalents and restricted cash	<u>\$ 105.8</u>	<u>\$ 93.3</u>

As of September 30, 2018 and 2017, we had \$105.8 million and \$93.3 million, respectively, in cash, cash equivalents and restricted cash. We do not intend to distribute previously taxed income (“PTI”) of our foreign subsidiaries and accordingly have not recorded any deferred taxes related to our investment in foreign subsidiaries. We estimate that future domestic cash generation will be sufficient to meet future domestic cash needs and have specific plans for use of the subsidiaries earnings. If, in the future, we change our intention regarding the repatriation of PTI, additional taxes may be required and should be recorded in the period the intention changes.

Operating Activities: Cash flows provided by operating activities were \$46.9 million for the nine months ended September 30, 2018 as compared to cash flows provided by operating activities of \$70.4 million during the nine months ended September 30, 2017. Generally, factors that affect our earnings—including pricing, volume of services, costs and productivity—affect our cash flows used or provided from operations in a similar manner. However, while management of working capital, including timing of collections and payments affects operating results only indirectly, the impact on the working capital and cash flows provided by operating activities can be significant.

Cash flows generated from operating activities decreased by \$23.5 million from \$70.4 million for the nine months ended on September 30, 2017 to \$46.9 million for the nine months ended September 30, 2018. This decrease was primarily due to an increase in working capital of \$37.6 million during the nine months ended September 30, 2018 as compared to \$26.7 million during the nine months ended September 30, 2017, due to an increase in accounts receivables, prepaid expenses, advance tax, other current assets and a decrease in accrued employee costs, deferred revenue and accounts payable.

Investing Activities: Cash flows used for investing activities were \$240.4 million for the nine months ended September 30, 2018 as compared to cash flows used for investing activities of \$171.1 million for the nine months ended September 30, 2017. The increase of \$69.3 million was primarily due to higher cash used for the business acquisitions of \$231.2 million during the nine months ended September 30, 2018. This was partially offset by net proceeds from investments of \$21.6 million during the nine months ended September 30, 2018 as compared to net purchase of investments of \$143.7 million during the nine months ended September 30, 2017.

Financing Activities: Cash flows provided by financing activities were \$208.1 million during the nine months ended September 30, 2018 as compared to cash flows used for financing activities of \$28.2 million during the nine months ended September 30, 2017. The increase in cash flows provided by financing activities was primarily due to net borrowings of \$239.9 million (net of repayments) under our New Credit Facility (as described below in “Financing Arrangements”) during the nine months ended September 30, 2018, partially offset by lower proceeds from exercise of stock options of \$3.2 million during the nine months ended September 30, 2018.

We expect to use cash from operating activities to maintain and expand our business. As we have focused on expanding our cash flow from operating activities we expect to continue to make capital investments, primarily related to new facilities and capital expenditures associated with leasehold improvements to build our facilities, and purchase telecommunications equipment and computer hardware and software in connection with managing client operations. We incurred \$30.1 million of capital expenditures in the nine months ended September 30, 2018. We expect to incur capital expenditures of between \$35.0 million to \$40.0 million in 2018, primarily to meet our growth requirements, including additions to our facilities as well as investments in technology applications, product development, digital technology, advanced automation & robotics and infrastructure.

In connection with any tax assessment orders that have been issued or may be issued against us or our subsidiaries, we may be required to deposit additional amounts with respect to such assessment orders (refer to Note 25 to our unaudited consolidated financial statements herein for further details). We anticipate that we will continue to rely upon cash from

[Table of Contents](#)

operating activities to finance our smaller acquisitions, capital expenditures and working capital needs. If we have significant growth through acquisitions, we may need to obtain additional financing.

Financing Arrangements (Debt Facility)

On October 24, 2014, we entered into a Credit Agreement that provided for a \$50.0 million revolving credit facility ("Credit Facility"). We had an option to increase the commitments under the Credit Facility by up to an additional \$50.0 million which we exercised on February 23, 2015, via an amendment to the Credit Agreement under the same terms and conditions which were available in the Credit Agreement. The Credit Facility had a maturity date of October 24, 2019 and was voluntarily pre-payable from time to time without premium or penalty. On November 21, 2017, we prepaid all outstanding amounts, including accrued interest and fees, and terminated all commitments under, the Credit Agreement.

On November 21, 2017, we and each of our wholly owned material domestic subsidiaries entered into a Credit Agreement with Citibank, N.A., PNC Bank, N.A., JPMorgan Chase Bank, N.A., Bank of America, N.A. and the lenders party thereto from time to time, with Citibank, N.A. serving as administrative agent (the "New Credit Agreement"). The New Credit Agreement provides for a \$200.0 million revolving credit facility (the "New Credit Facility"). The Company has an option to increase the commitments under the New Credit Agreement by up to \$100.0 million, subject to certain approvals and conditions as set forth in the New Credit Agreement. The New Credit Agreement also includes a letter of credit sub-facility. The New Credit Facility has a maturity date of November 21, 2022 and is voluntarily pre-payable from time to time without premium or penalty. Borrowings under the New Credit Agreement were used to refinance Credit Facility and may otherwise be used for working capital and general corporate purposes of the Company and its subsidiaries, including permitted acquisitions. On July 2, 2018, the Company exercised its option under the New Credit Agreement to increase the commitments by \$100.0 million thereby utilizing the entire revolver under the New Credit Facility of \$300.0 million, to fund SCIO acquisition. The incremental commitments were made pursuant to (and constitute part of) the existing commitments and shall be subject to the terms and conditions applicable to the existing commitments as set forth in the New Credit Agreement.

Refer to Note 18 to our unaudited consolidated financial statements herein for further details on our debt facilities.

As of September 30, 2018, we had outstanding debt of \$300.0 million, of which \$12.0 million is expected to be repaid within the next twelve months and is included under "current portion of long-term borrowings" and the balance of \$288.0 million is included under "long-term borrowings" in the unaudited consolidated balance sheets. As of December 31, 2017, we had outstanding debt of \$60.0 million, of which \$10.0 million was presented under "current portion of long-term borrowings" and the balance of \$50.0 million was presented under "long-term borrowings" in the unaudited consolidated balance sheets.

Subsequent to the end of the quarter, on October 4, 2018, the Company issued 3.50% Convertible Senior Notes due 2024 in an aggregate principal amount of \$150.0 million to Orogen Echo LLC, an affiliate of The Orogen Group LLC. See Note 26 to the unaudited consolidated financial statements contained herein. Additional details, including as to the Investment Agreement pursuant to which the Notes were issued, the Notes, and the Indenture governing the Notes, including conversion features and other obligations, are set forth in the Company's Current Report on Form 8-K filed with the Securities and Exchange Commission on October 4, 2018.

Off-Balance Sheet Arrangements

As of September 30, 2018, we had no off-balance sheet arrangements or obligations.

Contractual Obligations

The following table sets forth our contractual obligations as of September 30, 2018:

	Payment Due by Period					Total
	Less than 1 year	1-3 years	4-5 years	After 5 years		
	(dollars in millions)					
Capital leases	\$ 0.3	\$ 0.3	\$ —	\$ —	\$ 0.6	
Operating leases ^(a)	21.5	36.4	28.1	26.4	112.4	
Purchase obligations	5.0	—	—	—	5.0	
Other obligations ^(b)	2.0	3.3	2.3	3.2	10.8	
Borrowings:						
Principal payments	12.3	40.3	98.0	150.0	300.6	
Interest payments ^(c)	10.2	18.5	13.8	5.3	47.8	
Total contractual cash obligations^(d)	\$ 51.3	\$ 98.8	\$ 142.2	\$ 184.9	\$ 477.2	

(a) Represents minimum lease payments payable for cancellable and non-cancellable lease period.

(b) Represents estimated payments under the Gratuity Plan.

(c) Interest on borrowings is calculated based on the interest rate on the outstanding borrowings as of September 30, 2018.

(d) Excludes \$0.9 million related to uncertain tax positions, since the extent of the amount and timing of payment is currently not reliably estimable or determinable.

Certain units of our Indian subsidiaries were established as 100% Export-Oriented units under the “STPI” scheme promulgated by the Government of India. These units are exempt from customs, central excise duties, and levies on imported and indigenous capital goods, stores, and spares. We have undertaken to pay custom duties, service taxes, levies, and liquidated damages payable, if any, in respect of imported and indigenous capital goods, stores, and spares consumed duty free, in the event that certain terms and conditions are not fulfilled. We believe, however, that these units have in the past satisfied and will continue to satisfy the required conditions.

Our operations centers in the Philippines are registered with the “PEZA.” The registration provides us with certain fiscal incentives on the import of capital goods and requires that ExlService Philippines, Inc. meet certain performance and investment criteria. We believe that these centers have in the past satisfied and will continue to satisfy the required criteria.

Recent Accounting Pronouncements

For a description of recent accounting pronouncements, refer to Note 2—“Recent Accounting Pronouncements” to the unaudited consolidated financial statements contained herein.

ITEM 3. Quantitative and Qualitative Disclosures About Market Risk

During the three months ended September 30, 2018, there were no material changes in our market risk exposure. For a discussion of our market risk associated with exchange rate risk and interest rate risk, see Item 7A “Quantitative and Qualitative Disclosures about Market Risk” in our Annual Report on Form 10-K for the fiscal year ended December 31, 2017.

ITEM 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in the reports we file or submit under the Securities Exchange Act of 1934, as amended (the “Exchange Act”) is recorded, processed, summarized and reported within the time periods specified in the U.S. Securities and Exchange Commission’s rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer (“CEO”) and Chief Financial Officer (“CFO”), to allow timely decisions regarding required disclosure. In connection with the preparation of this Quarterly Report on Form 10-Q, our management carried out an evaluation, under the supervision and with the participation of the CEO and CFO, of the effectiveness and operation of our disclosure controls and procedures as of September 30, 2018. Based upon that evaluation, the CEO and CFO have concluded that, as of September 30, 2018, our disclosure controls and procedures were effective.

Changes in Internal Control over Financial Reporting

During the three months ended September 30, 2018, there was no change in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

In making its assessment of the changes in internal control over financial reporting during the three months ended September 30, 2018, our management excluded an evaluation of the disclosure controls and procedures of SCIO which we acquired on July 1, 2018. See Note 9 to the unaudited consolidated financial statements contained herein for details of our acquisition.

PART II. Other Information

ITEM 1. Legal Proceedings

In the course of our normal business activities, various lawsuits, claims and proceedings may be instituted or asserted against us. We believe that the disposition of matters currently instituted or asserted will not have a material adverse effect on our consolidated financial position, results of operations or cash flows. Please refer to Note 25 to the unaudited consolidated financial statements contained herein for details regarding certain contingent liabilities.

ITEM 1A. Risk Factors

We have disclosed under the heading “Risk Factors” in our Annual Report on Form 10-K for the fiscal year ended December 31, 2017 a number of risks which may materially affect our business, financial condition or results of operations. You should carefully consider the “Risk Factors” set forth in our Annual Report on Form 10-K for the fiscal year ended December 31, 2017 and the other information set forth elsewhere in this Quarterly Report on Form 10-Q. You should be aware that these risk factors and other information may not describe every risk facing our Company. Additional risks and uncertainties not currently known to us may also materially adversely affect our business, financial condition and/or results of operations.

ITEM 2. Unregistered Sales of Equity Securities and Use of Proceeds

Unregistered Sales of Equity Securities

For information on the sale of unregistered securities during the quarter ended September 30, 2018, see Note 9 to the unaudited consolidated financial statements contained herein. Such securities were issued in reliance on an exemption from the registration requirements of the Securities Act of 1933, as amended (the “Securities Act”), provided by Section 4(a)(2) of the Securities Act as a private offering. Such issuances did not involve public offerings, and were made without general solicitation or advertising. Except for the foregoing, we did not sell any of our equity securities during the three months ended September 30, 2018 that were not registered under the Securities Act.

[Table of Contents](#)**Use of Proceeds**

None.

Purchases of Equity Securities by the Issuer

During the three months ended September 30, 2018, purchases of common stock were as follows:

Period	Total Number of Shares Purchased	Average Price Paid per share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Approximate Dollar Value of Shares That May Yet Be Purchased Under the Plans or Programs⁽¹⁾
July 1, 2018 through July 31, 2018	51,200	60.56	51,200	16,554,300
August 1, 2018 through August 31, 2018	55,037	60.31	55,037	13,235,025
September 1, 2018 through September 30, 2018	49,600	65.27	49,600	9,997,699
Total	155,837	61.97	155,837	—

(1) On February 28, 2017, the Company's Board of Directors authorized an additional common stock repurchase program (the "2017 Repurchase Program"), under which shares may be purchased by the Company from time to time from the open market and through private transactions during each of the fiscal years 2017 through 2019 up to an aggregate additional amount of \$100 million. The approval increases the 2017 authorization from \$20 million to \$40 million and authorizes stock repurchases of up to \$40 million in each of 2018 and 2019.

ITEM 3. Defaults Upon Senior Securities

None.

ITEM 4. Mine Safety Disclosures

Not applicable.

ITEM 5. Other Information

None.

Table of Contents

ITEM 6. Exhibits

The following exhibits are being filed as part of this Quarterly Report on Form 10-Q:

- 3.1 [Amended and Restated Certificate of Incorporation of the Company, as in effect on the date hereof \(incorporated by reference to Exhibit 3.1 of the Company's Current Report on Form 8-K \(File No. 1-33089\) filed on October 25, 2006\).](#)
 - 3.2 [Fourth Amended and Restated By-Laws of ExlService Holdings, Inc., as in effect on the date hereof \(incorporated by reference to Exhibit 3.2 to the Company's Current Report on Form 8-K \(File No. 1-33089\) filed on February 28, 2017\).](#)
 - 31.1 [Certification of the Chief Executive Officer of ExlService Holdings, pursuant to Rule 13a-14\(a\) of the Exchange Act, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.](#)
 - 31.2 [Certification of the Chief Financial Officer of ExlService Holdings, pursuant to Rule 13a-14\(a\) of the Exchange Act, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.](#)
 - 32.1 [Certification of the Chief Executive Officer pursuant to Rule 13a-14\(b\) of the Exchange Act and 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.](#)
 - 32.2 [Certification of the Chief Financial Officer pursuant to Rule 13a-14\(b\) of the Exchange Act and 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.](#)
 - 101.INS XBRL Instance Document
 - 101.SCH XBRL Taxonomy Extension Scheme
 - 101.CAL XBRL Taxonomy Extension Calculation Linkbase
 - 101.DEF XBRL Taxonomy Extension Definition Linkbase
 - 101.LAB XBRL Taxonomy Extension Label Linkbase
 - 101.PRE XBRL Extension Presentation Linkbase
-

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934 the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Date: November 1, 2018

EXLSERVICE HOLDINGS, INC.

By: /s/ VISHAL CHHIBBAR

Vishal Chhibbar
Chief Financial Officer
(Duly Authorized Signatory, Principal Financial and Accounting Officer)

SECTION 302 CERTIFICATION

I, Rohit Kapoor, certify that:

1. I have reviewed this Quarterly Report of ExlService Holdings, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 1, 2018

/s/ Rohit Kapoor

Rohit Kapoor

Vice-Chairman and Chief Executive Officer

SECTION 302 CERTIFICATION

I, Vishal Chhibbar, certify that:

1. I have reviewed this Quarterly Report of ExlService Holdings, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 1, 2018

/s/ Vishal Chhibbar

Vishal Chhibbar

Chief Financial Officer

CERTIFICATION PURSUANT TO

18 U.S.C. SECTION 1350,

AS ADOPTED PURSUANT TO

SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report of ExlService Holdings, Inc. (the "Company") on Form 10-Q for the period ended September 30, 2018 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Rohit Kapoor, Vice-Chairman and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

- (a) the Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (b) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Rohit Kapoor

Rohit Kapoor

Vice-Chairman and Chief Executive Officer

November 1, 2018

CERTIFICATION PURSUANT TO

18 U.S.C. SECTION 1350,

AS ADOPTED PURSUANT TO

SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report of ExlService Holdings, Inc. (the "Company") on Form 10-Q for the period ended September 30, 2018 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Vishal Chhibbar, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

- (a) the Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (b) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Vishal Chhibbar

Vishal Chhibbar

Chief Financial Officer

November 1, 2018