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Q3 2021 DXC Technology Co Earnings Call

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PRESENTATION

Operator

Good day, everyone, and thank you for standing by, and welcome to today's DXC Technology Third Quarter Fiscal Year 2021 Earnings Call. A quick reminder, that today's conference is being recorded.

At this time, I'd like to turn the floor over to Shailesh Murali. Please go ahead, sir.

Shailesh Murali ***DXC Technology Company - Head of M&A and IR***

Thank you, and good afternoon, everyone. I'm pleased that you are joining us for DXC Technology's Third Quarter Fiscal 2021 Earnings Call. Our speakers on today's call will be Mike Salvino, our President and Chief Executive Officer; and Ken Sharp, our Executive Vice President and Chief Financial Officer. This call is being webcast at dxc.com/investorrelations. And the webcast includes slides that will accompany the discussion today. After the call, we will post these slides to the Investor Relations section of our website.

Slide 2 informs our participants that DXC Technology's presentation includes certain non-GAAP financial measures, which we believe provides useful information to our investors. In accordance with SEC rules, we have provided a reconciliation of these measures to their respective and most directly comparable GAAP measures. These reconciliations can be found in the tables included in today's earnings release and the webcast slides.

On Slide 3, you will see that certain comments we make on the call will be forward-looking. These statements are subject to known and unknown risks and uncertainties, which could cause actual results to differ materially from those expressed on the call. A discussion of these risks and uncertainties is included in our annual report on Form 10-K and other SEC filings. I would like to remind our listeners that DXC Technology assumes no obligation to update the information presented on the call, except as required by law.

And now, I'd like to introduce DXC Technology's President and CEO, Mike Salvino. Mike?

Michael J. Salvino ***DXC Technology Company - CEO, President & Director***

Thank you, Shailesh, and I appreciate everyone joining the call today, and I hope you and your families are doing well. I will walk through today's agenda in a moment. But before I do that, I want to briefly discuss the press release we issued on Monday, February 1.

As we announced last month, we received an unsolicited and nonbinding proposal from Atos to purchase DXC. Our Board reviewed the proposal carefully with our financial and legal advisers and found it to be inadequate and lacking certainty, given the value our Board believes we can create on a stand-alone basis by executing on our transformation journey. After sharing some high-level information with Atos to help them understand why their proposal undervalue DXC, Atos and DXC agreed to discontinue further discussions. We are confident in our transformation journey, and our Q3 results show strong evidence that our team is executing.

We are flattered that Atos saw the value we are creating and clearly has taken notice of our new leadership team and how we are delivering for our customers and winning in the market. I was pleased with how we managed the proposal. As it did not linger, we stayed focused on our business and it helped highlight some areas where we can accelerate our transformation journey and create additional

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value. With the new leadership team in place, I'm looking forward to sharing the details of our FY '22 full year plan and longer-term expectations on our Q4 earnings call. We're also planning an Investor Day to discuss in more detail our plans and introduce you to our leadership team.

Now let me turn to today's agenda. I will start by giving you a quick update on our strong Q3 performance. Next, I will highlight the progress we're making on our transformation journey. Our strong Q3 results were driven by executing against the 3 key areas of our transformation journey, which are focused on customers, optimize cost and seize the market. I will then hand the call over to our new CFO, Ken Sharp, to share our detailed Q3 financial results and guidance for Q4. Finally, I will make some closing remarks before opening the call up for questions.

Regarding our Q3 performance, our revenues were $4.29 billion, approximately $90 million above the top end of our guidance. This is the second straight quarter of revenue stabilization, and we expect this trend to continue in Q4. Our sequential revenue stabilization is positive evidence that we will achieve year-on-year revenue stability. Concerning adjusted EBIT margin, we delivered 7%, also higher than the top end of our guidance. Like revenue, we expect margins to continue to expand in Q4.

Book-to-bill for the quarter was 1.13, underscoring the success of bringing the new DXC, which focuses on our customers and people to the market. This is the third straight quarter that we've delivered a 1.0 or better book-to-bill, and we also expect this trend to continue in Q4. I'm pleased about the level of stability and momentum we are achieving. We have done well attracting talent, improving the environment for our people, strengthening our customer relationships, taking out cost without disruption and continuing to win in the market.

Now before I go through the progress of our transformation journey, I would like to comment on 2 recent hires that have allowed me to finalize our new leadership team. We completed our CFO search and hired Ken Sharp. Ken returns to DXC after being the CFO of Northrop Grumman's Defense Systems business. Prior to that, Ken was SVP of Finance at Orbital ATK and has over a decade of experience in our industry. Ken has a strong operational focus and has led large-scale finance transformations. These skills are important to us as we continue executing on our transformation journey.

We also added Michael Corcoran to our team. Michael has joined us as Chief Strategy Officer and has a track record of transforming and growing businesses. Michael joins us from WPP, where he led strategy and operations. Prior to WPP, Michael was at Accenture, where he spent a number of years with me and created the strategy for Accenture operations. The amount of transformation and industry experience of this team is substantial, and they are the main reason for our strong execution and results. You will hear in a moment why Ken joined DXC and his comments concerning the opportunity to create value do a really nice job capturing why talent joins DXC.

Now I will cover the good progress we are making on our transformation journey, starting with our customers. Our focus on customers continues to be the primary driver of revenue stabilization. As I've said time and time again, when we deliver for our customers and are seen as a trusted partner, customers are more likely to renew existing work and consider us for new work. Let me give you 2 good examples that have happened in Q3. Molson Coors renewed 2 pieces of work with us this quarter. The first is in application management, and the second is across multiple layers of the enterprise technology stack, including ITO, Modern Workplace, cloud and security.

Next, our strong relationship and flexible delivery model led to an expanded agreement with Pacific Life insurance, which includes application development and support for its retirement and life divisions, enabling them to reduce cost and improve efficiency. These are 2 perfect examples of the great job we're doing, strengthening our customer relationships and gives us confidence that we can continue to stabilize revenue.

Now let me turn to our cost optimization program. We will achieve our goal of $550 million of cost savings this year. Our cost optimization program was responsible for our strong adjusted EBIT margin of 7% in Q3. We were able to expand margins despite a 200 basis point headwind from the sale of the U.S. State and Local Health and Human Services business. We have done well optimizing our costs and continuing to deliver for our customers without disruption.

Seize the market is the final area of our transformation journey. In this area, we are focused on cross-selling to our existing accounts and

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winning work with new customers. The 1.13 book-to-bill number that we delivered this quarter is consistent evidence that our plan is working. In Q3, 55% of our bookings were new work and 45% were renewals.

Let me give you a good example of new work with a new customer. We signed a 3-year deal with Ferrari, where we will modernize their IT platforms with services, including security and Modern Workplace. Our ability to deliver a consistent book-to-bill number of over 1.0 in the first 3 quarters of FY '21 is clear evidence that our transformation journey is not only working but we can absolutely win in the IT services market.

Turning now to our healthcare provider software business. We are on track to complete the sale of this business and use the roughly $450 million of net proceeds to pay down debt, further strengthening our balance sheet. Now before I turn the call over to Ken, I would like to thank our people, customers and shareholders for supporting us throughout our transformation journey.

Now let me turn the call over to Ken.

Kenneth P. Sharp ***DXC Technology Company - Executive VP & CFO***

Thank you, Mike. Let me begin by saying how excited I am to join DXC and be part of the team that Mike has assembled. Let me provide you some insight into my thought process on why I joined, which came down to 3 main factors: the team Mike assembled; the transformation journey; and third, the investment thesis of how DXC would create value. After spending time with Mike and the team, I'm convinced that DXC can execute on the investment thesis I was contemplating. This includes stabilizing revenue, expanding margins and delivering free cash flow. When we achieve this thesis, I believe DXC will be successful in unlocking significant value.

Now let me talk about the team Mike assembled. Let's face it. Companies with the best people win. The strength of the team delivering on the transformation journey is clearly visible in our Q3 results. At DXC, there are 3 main areas that our finance team will focus on. First, we will work hard to demonstrate the true earnings power of DXC. We will focus on cash flow, paying particular attention to reducing outflows. We intend to continue investing in our people and delivering for our customers. At the same time, we will be disciplined in reducing spend in areas such as restructuring, transaction and integration, capital expenditures, excess facilities and our outsized overhead.

In the earnings release today, you will see that we're providing organic revenue, something that we feel will help our investors better understand the underlying performance of the business. We believe we will create the most value by growing the underlying business. That means organic growth and at the same time improving cash flow. Second, we are committed to putting in place a disciplined capital deployment program that will maximize the value creation of our cash flow engine. Based on rigorous analysis, we will carefully evaluate the returns associated with capital deployment options.

Now that we've strengthened our balance sheet, we are turning to solidify our cash flow. With a strong balance sheet and a cash flow outlook, we will be in a position to execute a disciplined capital allocation program. Third, we will improve our financial visibility. We are committed to providing annual guidance and our longer-term expectations on our next earnings call. We are also planning an Investor Day to discuss in more detail our longer-term plans and introduce you to our leadership.

Moving on to our Q3 results. In the quarter, DXC exceeded the top end of our revenue, adjusted EBIT and non-GAAP EPS guidance. GAAP revenue was $4.29 billion and $88 million better than the top of our guidance range. Currency was a tailwind of $58 million sequentially and $118 million year-over-year. On an organic basis, revenue increased 1.7% sequentially. Organic revenue declined 10.5% year-over-year due to previously disclosed runoffs and terminations. We expect this to be the high watermark for organic year-over-year revenue declines.

As you will see from our Q4 guidance, we expect to continue delivering stable sequential revenue. And during fiscal year '22, we expect this to translate into year-over-year revenue stability. Adjusted EBIT was $300 million. Our adjusted EBIT margin was 7%, a sequential improvement of 80 basis points despite an approximate 200 basis point headwind from the HHS sale. Non-GAAP income before taxes was $246 million. Non-GAAP diluted earnings per share was $0.84 due to a lower-than-expected tax rate of 10.2%. Using our guidance tax rate of 30%, non-GAAP EPS was $0.65. This was a $0.10 -- this was $0.10 higher than the top end of our guidance range.

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Our Q3 tax rate primarily benefited from the reversal of certain tax reserves related to tax audits, the expectation of higher utilization of foreign net operating losses and the ability to utilize state tax credits related to the HHS sale. In Q3, bookings were $4.9 billion for a book-to-bill of 1.13. Like Mike mentioned earlier, we are encouraged to see 3 consecutive quarters with a book-to-bill greater than 1.0.

Turning now to our segment results. The GBS segment, the top of our technology stack, includes analytics and engineering, applications and the horizontal BPS business. The GBS segment previously included the HHS business, which we sold on October 1 and includes the healthcare provider software business, which we are in the process of selling. GBS revenue was $1.92 billion or 45% of our total Q3 revenue. Organic revenues increased 2.2% sequentially, primarily reflecting the strength of our analytics and engineering business. Year-over-year, GBS revenue was down 7% on an organic basis. GBS segment profit was $273 million and profit margin was 14.2%. Margins improved 10 basis points sequentially despite a headwind of about 300 basis points from the HHS sale. GBS bookings for the quarter were $2.7 billion for a book-to-bill of 1.35.

Now turning to our GIS segment, which consists of IT outsourcing, cloud and security and the Modern Workplace layers of our enterprise technology stack. Revenue was $2.37 billion, up 1.3% sequentially and down 13.2% year-over-year on an organic basis. GIS segment profit was $88 million with a profit margin of 3.7%, a 210 basis points margin expansion over Q2. GIS bookings were $2.2 billion for a book-to-bill of 0.95.

Now before I discuss the details of the enterprise technology stack on Slide 13, I wanted to point out that there is no better slide that drives home the positive impact of our transformation journey. The proof points on the slide include continued revenue stabilization and strengthening of our book-to-bill for each layer of our stack that has been part of the transformation journey since Q1. As you can see in Q1, all 4 layers of our stack had negative sequential growth, whereas we are now reporting sequential growth improvement for all layers in Q3. Also, it is positive to see the revenue mix beginning to change in shifting up the stack.

Now let me drill down one level to comment on the performance of the layers of our enterprise technology stack. IT outsourcing revenue was down 1.8% sequentially, an improvement as compared to Q2 where it was down 4.7%. ITO revenues declined 17.7% year-over-year due to the previously disclosed runoffs and terminations. Book-to-bill was 0.96 in the quarter. We believe building strong relationships with our ITO customers and delivering effective solutions will improve revenue performance. Cloud and security revenue was up 4.7% sequentially and down 1% year-over-year. Book-to-bill was 1.0 in the quarter.

Moving up the stack, the applications layer posted 2.6% sequential revenue growth and was down 9.3% year-over-year. Book-to-bill was 1.5. Analytics and engineering was up 4.6% on a sequential basis and flat compared to the prior year. Analytics and engineering book-to-bill was 1.2 in the quarter. The Modern Workplace and BPS businesses increased 2.6% sequentially and was down 12.6% compared to the prior year. I should note that Q3 positively benefited from increased volume of resales. As you may recall, these 2 businesses were part of the strategic alternatives initiative and are just beginning their transformation journey. As a result, you should expect some unevenness in performance.

Moving on to cash flows on Slide 14. Our cash flow from operations totaled an outflow of $187 million, and adjusted free cash flow for the quarter came in at negative $318 million. As discussed on our prior earnings call, we had cash disbursements of $332 million that impacted free cash flow related to the HHS sale. In addition, during the quarter, we normalized payments to our suppliers and partners. Our effort to normalize our supplier and partner payments is not expected to reoccur and had an approximate $400 million negative cash flow impact in the quarter and $500 million negative cash flow impact through the first 3 quarters of our fiscal year.

We believe treating our partners appropriately will allow us to further leverage the partner ecosystem. If these 2 items had not occurred, our free cash flow would have been more than $700 million higher in the quarter. The company has traditionally reported adjusted free cash flow that adjusts for capital expenditures, restructuring, transaction, separation and integration costs. We are considering changing our free cash flow presentation going forward.

On Slide 15, we detail the efforts we have undertaken to strengthen our balance sheet. As we previously disclosed, we utilized $3.5 billion of net proceeds from our HHS sale to reduce debt. Additionally, we continue to make progress on our plan to sell our healthcare provider

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software business, and we will use the proceeds to pay down debt and further strengthen our balance sheet. Cash at the end of the quarter was $3.9 billion.

Total debt, including capitalized leases, was $6.2 billion for a net debt of $2.3 billion. We expect to make tax payments of approximately $900 million in Q4 related to our divestitures. I would like to emphasize our commitment to an investment-grade credit rating. As you can see, our net debt to EBITDA improved more than 1 full turn from 2.4x at the end of September 2020 to 1.2x at the end of December. We fully expect our leverage ratio to continue to improve.

Moving on to guidance on Slide 16. We are targeting Q4 revenues of $4.25 billion to $4.3 billion, adjusted EBIT margins of 7% to 7.4%, non-GAAP diluted earnings per share of $0.65 to $0.70, net interest expense of $60 million and an effective non-GAAP tax rate of about 28%.

With that, I will now turn the call back to Mike.

Michael J. Salvino ***DXC Technology Company - CEO, President & Director***

Thanks, Ken. And let me share 3 key takeaways on our progress we are making at DXC. First, we're bringing the new DXC to the market and have demonstrated solid momentum in executing on our transformation journey. This is translating into consistent quarter-on-quarter revenue stability, sequential margin expansion and a book-to-bill number of 1 or greater. Second is we are on track to complete the sale of the healthcare provider software business and use the proceeds to pay down debt, further strengthening our balance sheet. Third, with the additions of Ken and Michael, we have built and finalized the new leadership team that is executing on our transformation journey and producing strong results.

In closing, I am pleased with the level of stability and momentum we are achieving. We have done well attracting talent, improving the environment for our people, strengthening our customer relationships, taking out costs without disruption and continuing to win in the market. We expect all of this positive momentum to continue in Q4.

And with that, Greg, please open the call up for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) And our first question is going to come from Ashwin Shirvaikar from Citi.

Ashwin Vassant Shirvaikar ***Citigroup Inc., Research Division - MD & Lead Analyst***

Good to see the progress here. Mike, you alluded to the process of sort of enhancing customer relationships. And I wanted to ask what part of -- to what extent are you still playing defense, which is keeping what is figuring out what your clients want, what their perspective is versus offense? And how successful has the recent push to cross-selling been and so on? And what percent of sold work is sole source? And is there a target for that?

Michael J. Salvino ***DXC Technology Company - CEO, President & Director***

Ashwin, first of all, good to hear you. On the customer relation shifts, the key thing is -- I like Page 13 a lot. That's where we show the enterprise technology stack. And the key testament to customers getting better are the fact that they're giving us more work. So I look at that. And the reason why I wanted to show you that progress was when you look at Q1 this year and the minus 5.7%, you'll see that all of that was negative. And what we have said point time and time again is that we're going to rebuild these relationships, and then we're going to start stabilizing the revenue. So having all 4 of the areas of the enterprise technology stack negative in Q1 and then flipping those to 3 positive with only 1 negative is huge. And that's a testament to what myself and the team are doing. I think the customer relationship area went from an area of weakness to now an area of strength.

And then, Ashwin, just to finish that. When you look at that 1.8% negative ITO, that's probably the number I'm most positive about and proud of on that whole stack because that was the thing when I came in that everybody said that, that was the work that was moving

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away from us. And it's actually not moving away from us anymore. The last thing is this. When I look at the amount of work that we're winning, 55% new work, 45% from renewals, you can see that the renewals are usually sole sourced, and a good portion of the new work also is sole-sourced on those customer relationships.

Ashwin Vassant Shirvaikar ***Citigroup Inc., Research Division - MD & Lead Analyst***

That's great to hear. So I guess the obvious follow-up then becomes, as you look at your emerging sort of business profile, if you will, post the divestitures, including the improving stack. Can you comment on what sort of a normalized margin profile might look like? Or at least help us frame that?

Michael J. Salvino ***DXC Technology Company - CEO, President & Director***

The way I would frame the margin profile is you've seen us all throughout this year continue to expand the adjusted EBIT margin. We also see that there are still levers we can pull. So when I mentioned the fact of what we've gone through over the next 30 days that we've sharpened our pencil on other areas that we can also pull. So those levers would include things like real estate, things like overhead. Ken's all over the overhead. I've talked before about contractor conversion. What that means is I'm going to stop paying a premium for a contractor and hire the person. And then the other thing that I'm excited about is our operation automation, something I've done with in my past. We're done with our pilot. Vinod has done a great job with that. So you should expect from us continued margin expansion.

Operator

Next from Morgan Stanley, we have James Faucette.

James Eugene Faucette ***Morgan Stanley, Research Division - Executive Director***

Mike, building on kind of Ashwin's comments, obviously, you've done a lot to kind of reorient the business. You've highlighted multiple times stabilizing, and that's obviously, I think, been surprising to some people you've been able to do that so quickly. Sitting here today, though, as we look forward, how are you thinking about "where the puck is going?" Like what kinds of abilities or practices do you think are going to be important for DXC to add? And how do you think about going about adding those?

Michael J. Salvino ***DXC Technology Company - CEO, President & Director***

So the -- James, good to hear your voice and thanks for the question. I have said before that when you look at the enterprise technology stack, I like the hand that we have. We've got good scope and scale across the way that our clients think about technology. So when you think about whether it's ITO, cloud security application, analytics and engineering, there's stuff that we have to do there. And look, I know that you're not thrilled about us rationalizing and then delivering. But that focus will allow us to get to where we need to be on revenue growth because we've got too many things going on in the industry right now, and we need more focus.

That, along with the decision that we made to keep our Modern Workplace couldn't be more thrilled that the ecosystem has decided to partner with us, specifically Microsoft, and get into that area with us. Now having said that, we obviously want to see the mix changing, too. We've got to move from the bottom of the stack in terms of the top of the stack. But the other stat I will give you is we still have a customer base where they are aspiring to move roughly 20% of their work over the next 2 years to the cloud, but 80% of that work that is remaining, 60% they want to see modernized.

So look, I like the hand that we have, James. We're going to continue to make sure we're focused on selling the stuff that we have. And then I think I will end with -- you've seen I've got a propensity to buy tactical tuck-ins. I'm not big on buying big things. I'm big on buying things that help me focus on that enterprise technology stack and then I know can scale through our best accounts. So that's where I take the relationships and push it against our offerings. And marrying the two, I should be able to sell more to those best clients.

James Eugene Faucette ***Morgan Stanley, Research Division - Executive Director***

That's very useful. And then I know that you and Ken had both talked about preparing a broader presentation for the investment community at a future analyst meeting, et cetera, but -- and particularly as it relates to capital allocation and returns. But as you think about those type of tactical tuck-ins, is that something that you think you can go through a period of time and/or just be opportunistic? Or is that something that you end up being kind of similar to the big players in the space, doing on a consistent and kind of proscribed basis, at least in terms of proportion of capital allocation?

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Michael J. Salvino ***DXC Technology Company - CEO, President & Director***

I'll stay, James, with what we said in our script, and that's the fact that we plan on coming back in Q4 and showing you our capital allocation strategy. So in that strategy, you'll see our thoughts on dividend, our thoughts on buyback and then our thoughts on investment. And with Ken having 60 days in the seat, 30 of which were spent in the -- dealing with the latest proposal, I just want a little bit more time to go through that.

Operator

Next, we have -- from DeepDive Equity, we have Rod Bourgeois.

Rod Bourgeois ***DeepDive Equity Research - Head of Research and Consulting***

Nice incremental turnaround progress in the December quarter and you're guiding toward revenue stability. But guys, let me ask about the elephant in the room. You apparently just told Atos that its takeover premium was so inadequate that they walked away, even though it seems merging with DXC was Atos' best strategic idea. So to have so clearly pushed off Atos' takeover bid, you have to be banking on a fundamental trajectory for DXC that's more compelling -- seemingly more compelling beyond your outlook for revenue stability. So here's my question. What fundamental improvement drivers are giving you such conviction to turn down the takeover premium today? And I'm not necessarily asking for fiscal '22 guidance. I suspect you're waiting until fiscal '21 is over to do that. But I would like to ask what are the fundamental drivers that are giving you such conviction today about your trajectory and your willingness to turn down the takeover bid?

Michael J. Salvino ***DXC Technology Company - CEO, President & Director***

Rod, thanks. So look, I'll cover three items. The first one is revenue stability. And again, all these things tie back to what we've been saying all along. So on revenue stability, we just delivered our second quarter of revenue stability and have guided towards the third quarter. So we believe we're headed towards revenue stability year-on-year in FY '22. And I think anybody that has followed DXC would say that's pretty strong accomplishment. Second is within revenue stability it's those customer relationships. And I know you all do your customer checks and so forth, and those relationships are becoming deeper and deeper, where they're coming to us as a trusted partner for more work.

The second thing is adjusted EBIT margin that I mentioned to Ashwin. The fact that we are expanding margin and the key thing is sustainability. And we believe that we can keep it sustainable, along with having levers like the facilities, like operational automation, contractor conversion and even overhead to name a few. We think we've still got levers to pull on to continue to expand this thing -- the margin going forward.

And then, look, you can't have revenue and margin without winning in the market. And we think because of the book-to-bill of 1.0 or greater, that the pendulum swung a little bit in our favor. We're seeing the need to fix these IT environments before you can get transformed. We think CIOs are looking at us now and saying the biggest thing that will kill a transformation to anything digital is if the existing environment doesn't work. And that's why I highlighted the green 1.8% in Q3 from a growth standpoint on a sequential basis.

The other thing is this. When you look at our existing customers, there's no doubt they're buying more. And I love the progress that we're making on the ecosystem. That's why when Ken mentioned what we did with our partners, we're now going after our partners the same way we did our customers. We're rebuilding those relationships because that ecosystem is important to us. And again, I'll highlight the fact that Microsoft was willing the team with DXC to get into Modern Workplace. That's a game changer. So that's what we were looking at, Rod. And when you put all that together and take the Board through it, you see more value than what the proposal was all about.

Rod Bourgeois ***DeepDive Equity Research - Head of Research and Consulting***

All right. So great. So it's a good segue to my other question I wanted to ask on. Are you seeing real evidence that DXC's competitive position has improved? If I look at IBM, it's preparing for its spinoff, and that's been a distraction for IBM in the market. And Atos' behavior suggests that its organic prospects are not too encouraging. So you've got 2 major competitors that are in that status. So especially given the competitor backdrop there, I'd really like to know if you're seeing any tangible evidence that your turnaround is helping your competitive position. Can you share any tangible evidence of what's happening on the competitive front?

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Michael J. Salvino ***DXC Technology Company - CEO, President & Director***

So Rod, the first thing is, I'll continue to go back to the book-to-bill number. That's tangible evidence. I mean, keeping that thing up above 1.0 is huge. And then, look, it goes without saying. We recently engaged with a competitor. And when a competitor wants to engage with you, you can rest assured. They've seen, right, good trends for us in the market. So look, that's the tangible evidence. We're very pleased about our position. We're also very pleased that, like I said during the last earnings call or at least I mentioned it just a little bit, is the fact that we're very clear about what we got to go get done. The strategic alternatives, initiatives are over, and it's all about execution now. So Rod, that's how I'd answer your question. Thanks.

Operator

Next question will come from Lisa Ellis with MoffettNathanson.

Lisa Ann Dejong Ellis ***MoffettNathanson LLC - Partner***

First one, Mike, for you, yet another kind of follow-up on the Atos approach. I would imagine as you are that that's probably not the only one of those that you're going to be getting this year. So can you just talk more broadly about how you think about the pros and cons of a larger-scale merger versus what you can do on your own?

Michael J. Salvino ***DXC Technology Company - CEO, President & Director***

Well, look, in terms of what we can do on our own, we really like our chances, okay? We are confident in our transformation journey. And like I've shown, I've laid out a plan, and you guys can see that, Lisa, we're executing against that plan. It was never part of my plan to come here in 16 months and then all of a sudden sell the company. You can't recruit a brand-new leadership team if that's your strategy. So I like our chances in terms of DXC on a stand-alone basis.

Lisa Ann Dejong Ellis ***MoffettNathanson LLC - Partner***

Okay. And then my follow-up is just related to bookings and then also kind of linking that to the sequential improvement in revenues. Both of which, as you've highlighted, are very encouraging. Can you just talk a little bit about the mechanics? I mean bookings have now been running over 1.1 for about 12 months, which should imply some very healthy revenue acceleration at some point. Can you just dimensionalize a bit kind of how that conversion works? Meaning, are you still in a situation where your backlog is weak or low and so you're sort of reselling the bathtub, so to speak? Or you know what I mean. Like what -- how should we think about when the sort of sequential improvement in revenues combined with like the bookings growth kind of come together? Is that still a few quarters out? Or how do you think about that?

Michael J. Salvino ***DXC Technology Company - CEO, President & Director***

Yes. What we're saying is we just delivered the second quarter stability, right? So that stability marries what's happening with the revenue runoff because of the terminations with the positive 1.0 or greater bookings, okay? So just balancing that stuff out. So stability means, obviously, that we're not losing more than we're winning. We also guided towards our third quarter of revenue stability. So we're clearly looking at '22, that year, for year-on-year revenue stability, Lisa. That's -- I mean, I tell my team, it's just math. So what we need to do is continue executing on our transformation journey. So that's the way we look at that.

Operator

Next will come from Bryan Bergin with Cowen and Company.

Bryan C. Bergin ***Cowen and Company, LLC, Research Division - MD & Analyst***

Ken, welcome. I wanted to ask revenue trajectory around the ITO layer. So obviously, the improvement is encouraging here. And curious, whether there's anything notable in the client portfolio, any large deal renewals or impending price down risk to be aware of that would not enable DXC to maintain this type of improvement in the coming periods? And do you view this as a business that can ultimately stabilize, too, specifically the ITO layer? Or are the secular headwinds here just too challenging for such a plan?

Michael J. Salvino ***DXC Technology Company - CEO, President & Director***

I mean, Bryan, I continue to talk about the fact that -- and I gave the stats. I took virtual clarity and I went and studied our best clients. And again, what they told me was they aspire over the next 2 years to move another 20% of the existing work I'm sitting on to the cloud.

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Now after I took them through the analysis that Virtual Clarity does, which is technical feasibility, risk, business case and their ability to deliver, that 20% dropped to 5%. Now I don't much care whether it's 20% or 5%. We need to win our fair share. But Bryan, what that means is there's still a healthy dose of this whole secular runoff. Certainly, that stuff is going to move to the cloud.

But the other thing I would tell you is we are now into the and phase of the cloud journey. Now what is that? The or phase was ITO or cloud, which meant that most of this work on on-prem moved to the public cloud, one or the other. When you're now in the and phase, you're dealing with critical applications, and those critical applications just don't move directly to the cloud. In fact, you're now managing workloads. Sometimes the application will move to the cloud. Sometimes the data will stay there. Why am I going to this level of detail? Because the bottom line is the fact that, that's opportunity for us.

Meaning if clients want to move to the cloud, they need our expertise, knowing how to run what they have to move to the cloud. And then what I'm focused our team on is the existing estates. So when you talk to a number of our customers, you will see that we are building these estate maps, and these estate maps is basically a road map for us to say what else needs to be updated on those environments. And then that is the thing that's helping that green layer get back to 0. Look, I'm not trying to sell to you that the green layer is going to be some sort of growth, but I am selling the fact that, that thing can be stabilized if you take care of your customers. So Bryan, that's the answer to that question.

Bryan C. Bergin ***Cowen and Company, LLC, Research Division - MD & Analyst***

Okay. Makes sense. And then just talk about the workforce. At what stage of the talent refresh are you at? How are you thinking about headcount and hiring here over the next couple of quarters?

Michael J. Salvino ***DXC Technology Company - CEO, President & Director***

So look, I mean, I'm absolutely thrilled about our new leadership team. And when we hire a new leader, I always talk about the fact that they owe me 10 new hires. And we're going to continue to augment the talent that we have in DXC. So we are now going through -- I think the leadership team has rebuilt. I want to get to the middle managers and see how they're doing and then continue to put them into our new operating model that's very customer focused. So Bryan, that's the way I would answer that question, too.

So listen, I want to thank each of you for joining the call today. I couldn't be more pleased about the level of stability and momentum we're achieving by executing on our transformation journey, and we are confident that the momentum we created in Q3 will continue in Q4.

With that, all the best to you and your families. And Greg, please close the call.

Operator

Absolutely, sir. And once again, ladies and gentlemen, thank you for joining us today. That will conclude our call. We do appreciate you dialing in and participating, and you may now disconnect.

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