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DXC Technology Co. (DXC)

Q2 2022 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good afternoon. My name is Julianne, and I will be your conference operator today. At this time, I would like to welcome everyone to DXC Technology's Q2 FY 2022 Earnings Call. All lines have been placed on mute to prevent any background noise. After the speaker's remarks, there will be a question-and-answer session. [Operator Instructions] Thank you.

John Sweeney, Vice President, Investor Relations at DXC, you may begin your conference.

John Sweeney
Vice President-Investor Relations

Thank you. Good afternoon, everyone. I'm pleased that you're joining us for DXC Technology's second quarter FY 2022 earnings call. Our speakers on the call today will be Mike Salvino, our President and CEO; and Ken Sharp, our Executive Vice President and CFO. This call is being webcast at dxc.com/investorrelations website and the webcast includes slides that will accompany the presentation today.

Today's presentation includes certain non-GAAP financial measures, which we believe provide useful information to our investors. In accordance with SEC rules, we've provided a reconciliation of these measures to their respective and most comparable GAAP measures. These reconciliations can be found in the tables included in today's earnings call on the webcast slides.

Certain comments we make on the call will be forward-looking statements. These are known and uncertain risks and uncertainties, which could cause actual results to differ materially from those expressed on the call. A discussion of these risk and uncertainties is included in our Annual Report on Form 10-K and other SEC filings. I'd now like to remind our listeners that DXC Technology assumes no obligation to update the information presented on this call, except as required by law.

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

Michael J. Salvino
President, Chief Executive Officer

Thanks, John. And I appreciate everyone joining the call today, and I hope you and your families are doing well. Today's agenda will begin with an update on our Q2 performance, which shows hard evidence that we are delivering on our transformation journey and building the foundation to make DXC operationally efficient, sustainable and ultimately grow.

Next, I will provide you with additional insights as to the operational work we are performing as we execute our transformation journey. Then I will hand the call over to Ken to share our Q2 financials, guidance and more details of the financial results driven by our strong operational execution. Finally, I will make some closing remarks before opening the call up for questions.

Regarding our Q2 performance, our revenues were \$4.03 billion. Our organic revenue growth continued to show progress as we improved from minus 3.7% in Q1 to minus 2.4% in Q2. Also, I was very pleased to see that the GBS business segment grew for the second quarter in a row from positive 2% in Q1 to positive 3.4% in Q2. We also continue to improve the organic revenue of the GIS business segment from minus 9.1% in Q1 to minus 8% in Q2.

Now all of these results show our organic revenue is on the right trajectory. Our adjusted EBIT margin was 8.6% and was driven by the operational work that we are doing to optimize our business. This is the third straight quarter of both improving organic revenue growth, and sequential margin expansion, and we expect both trends to continue in Q3.

Book-to-bill for the quarter was 0.91, which came in below our goal of one due to the timing of a couple of deals. I'm happy to report that both deals are hybrid cloud/ITO deals and are now closed. We continue to track to a book-to-bill over one year-to-date, and we expect to be back above 1.0 in Q3.

Our non-GAAP EPS was \$0.90 in the quarter, which is up 41% as compared to \$0.64, a year ago. Finally, we are encouraged by the strength of our Q2 free cash flow, which moved us into positive territory. On a year-to-date basis, we have now produced roughly \$100 million in cash.

Now let me turn to the progress we are making on our transformation journey. The first step is inspire and take care of our colleagues. We are executing a people-first strategy and attracting and retaining talent is fundamental to enable our growth. We know our strategy is working. We saw a higher percentage of our employees complete our September employee engagement survey, and we are showing improved and stable engagement scores. These engagement scores give us confidence that we have a motivated workforce, and we will be able to manage attrition, which we've seen an uptick.

To offset this increase in attrition and demand, we hired and on-boarded more colleagues than any other quarter, since I became CEO. Key advantage to our hiring efforts is that we have implemented and are running a virtual-first model. Hiring has been a focus for us and will continue. While hiring improved, we left some open demand and project were unconverted and we are focused on capturing this moving forward.

Focus on the customers is the second step of our transformation journey and continues to be the primary driver of our success in improving our organic revenue growth. A key metric that we measure is our Net Promoter Score, and we are seeing continued improvement. The last time, we gave you our NPS score, was during the Investor Day in June, and it was 18, almost within the industry best practice range of 20 to 30.

Currently, our 12-month rolling NPS score is at the midpoint of the best practice range. This is the most positive our customers have been, since I arrived. This improvement is due to our strong service delivery and gives us the ability to sell up the enterprise technology stack from our GIS business to our GBS business.

Now, let me remind you that the way we will get to grow is to deliver the GIS services that are critical for our customers and build trusted relationships. Once these trusted relationships are built, we can move our customers up the enterprise technology stack towards the services of our GBS business. This is exactly what we are doing.

And the organic revenue trajectory of GIS, GBS and the overall business is great evidence that this strategy is working.

Now, let me turn to our cost optimization program. We continue to make progress in optimizing our cost and delivering for our customers without disruption. I mentioned at the beginning of this call that, we are doing the operational work to make DXC efficient, sustainable and ultimately grow. I've already commented on some of the operational work we are doing, like motivating our colleagues, hiring new talent and implementing a virtual-first model. In addition to this work, we are also improving the efficiency of our service delivery, implementing better IT tools and actively managing our real estate footprint.

Let me provide you with some additional color considering the operational work we are doing with real estate. This quarter, we closed our Tyson facility and are moving to a much smaller footprint in the D.C. area, where our colleagues that need to come into a facility will share a space versus having dedicated space. This work emphasizes, our commitment to a virtual-first model, reduce our carbon footprint, and represents our desire to maintain a much smaller real estate footprint.

Jim will detail out the financial results of all of these operational work that, simply put, this work is allowing us to improve margins from 8% in Q1 to 8.6% in Q2 and gives us the confidence to increase our margin and EPS guidance for FY 2022.

Next, the market is where we are focused on cross-selling for our existing customers and winning new work. As I previously mentioned, we had two significant deals slip into Q3 and are now signed. The great news about these deals is they were both hybrid cloud/ITO deals with long-standing customers. Specifically, we are helping these customers modernize their existing IP estate and building new private cloud capability to run their mission-critical applications.

In Q2, 59% of our bookings were new work and 41% were renewals. The new work continues to increase due to the focus on another piece of our strategy, which is our platinum customer channel. Taking our offerings through this channel is another key foundation piece for growth. We are now starting to see evidence that we are being successful in taking Microsoft, which drives our analytics and engineering services through our platinum customer channel. The evidence is that analytics and engineering grew 17.3% in Q2, which is clearly helping us create growth in our GBS business segment.

Now, let me give you an example of what the Platinum customer of the future looks like at DXC. We have a 14 year relationship with one of the world's largest specialty retailers. Now before I arrived and implemented the strategy, our revenues were roughly \$80 million per year, split one-third GBS and two-thirds GIS. By continuing to deliver our GIS services for this customer, we are offering the opportunity to sell our GBS services. The result is we have increased the total revenue on this account by 13%, and the mix between GBS and GIS is now split 50-50, as we are now providing them analytics and engineering services.

We're in the early innings of this strategy, but we feel confident that we can implement this approach to our other Platinum customers, successfully delivering GIS services and growing GBS services to have a same or more revenue at better margins.

Now let me turn the call over to Ken.

Kenneth P. Sharp

Chief Financial Officer and Executive Vice President

Thank you, Mike. Turning to our quarterly financial performance on slide 11. As you can see, our progress continues. Our organic revenue improved to a decline of 2.4% or a 130 basis point improvement from Q1. This represents our third consecutive quarterly improvement. As you can see, we have come a long way from double-digit organic revenue declines in Q1 FY 2021 to low single-digit declines in FY 2022.

Our adjusted EBIT margin continues to improve as well, delivering 8.6% in Q2, up 60 basis points as compared to the first quarter. Year-over-year, our adjusted EBIT margins have expanded 240 basis points or 460 basis points, excluding the disposed businesses.

Our book-to-bill for Q2 was 0.91, below our goal of one due to timing and remains over one year-to-date. Further, we expect to deliver a book-to-bill of over one for Q3 and for the full year.

Non-GAAP diluted earnings per share was \$0.90, up \$0.06 from Q1, and a healthy 41% increase as compared to the prior year. Our earnings per share expanded due to increased margins, lower interest expense and a lower tax rate.

Moving to our segment results on slide 12. Our GBS segment continued its strong growth performance, posting its second quarter of positive organic revenue growth of 3.4%, an improvement from 2% in the first quarter. The GBS growth is a positive sign as we continue to deliver higher value for our customers. Our GBS business has higher margins and lower capital intensity. So as we grow this business, it has a more positive impact on margins and cash flow.

Our GBS margin was 15.9%, up 150 basis points compared to the first quarter, and up 180 basis points compared to prior year. Our GIS segment organic revenue declined 8%, a full 110 basis point improvement compared to the first quarter and improved 380 basis points compared to the decline from prior year. GIS margin was 5.5%, an improvement of 390 basis points compared to prior year.

Turning to the enterprise technology stack. Analytics and Engineering revenue was \$520 million, up 17.3%. Analytics and Engineering book-to-bill was 0.95 and 1.13 year-to-date. We continue to see high demand in this area. The applications layer was up 1.5%, book-to-bill was 0.94 and 1.13 year-to-date. EPS, our smallest layer of the enterprise technology stack, at \$118 million of revenue, was down 13.7%. Book-to-bill was 0.69 and 0.91 year-to-date.

Cloud and security revenue was \$521 million, down 1.5%. Book-to-bill was at 0.8 in the quarter and 0.82 year-to-date. IT outsourcing revenue was \$1.05 billion, down 9.6%. ITO book-to-bill was 0.81 and 0.92 year-to-date. We expect our ITO decline to continue to gradually moderate as we move through FY 2022. The two deals, Mike mentioned earlier that, slipped out of Q2 that were subsequently closed were in the ITO, and cloud and security layers of our technology stack and would have boosted our GIS book-to-bill for the quarter to over 1.1.

Lastly, modern workplace revenues were \$581 million, down 10.9% as compared to prior year. This is an improvement from last quarter, when modern workplace was down 19.7% year-over-year. Book-to-bill was 1.2 and 1.1 year-to-date.

Next up, let me touch on our efforts to build our financial foundation. This quarter, we made particularly strong progress on strengthening our balance sheet and solidifying our financial position, cash generation and reducing restructuring and TSI expense.

As Mike pointed out earlier, we've made measurable improvements driving our business to improve our financial foundation that will ultimately allow us to increase our deployable cash affording us more opportunities to create value. We reduced our debt from \$12 billion to \$5.1 billion. The refinancing of all of our high rate bonds during the quarter culminates our collective efforts to transform the business, improve its trajectory and strengthen our balance sheet. There is no similar and clear way of seeing the impact that Mike and his team have made improving the operations of the business than what was accomplished with our debt over the last year.

Net interest expense has been reduced from \$83 million in the first quarter of FY 2021 to \$45 million this quarter. With the full benefit of our refinancing, we anticipate interest expense to be reduced to approximately \$33 million in Q3. We also continue to deliver on reducing restructuring and TSI expense, while increasing our margins. This not only improves our cash flow, it also narrows the difference between GAAP and non-GAAP earnings.

Finally, capital lease and asset financing is an area that was overused. In the last year or so, we've significantly curtailed new capital lease originations from \$1.1 billion in FY 2020, and are on track to reduce originations to approximately \$500 million this year. These efforts to better manage this form of financing allowed us to reduce our debt and ultimately our capital lease cash outflows from \$245 million in Q1 FY 2021 to \$177 million this quarter. We expect further reductions in our quarterly cash outflows to around \$150 million per quarter at the end of FY 2022 and further below that level going forward.

We delivered these reductions, while also better managing capital expenditures. Our capital expenditures were reduced from \$225 million in Q1 FY 2021 to \$159 million Q2 FY 2022. Based on our reductions to capital lease originations, a more meaningful metric to demonstrate our progress is CapEx spend and capital lease originations as a percent of revenue.

CapEx and capital lease originations as a percent of revenue were 10.2% for FY 2020, 8% for FY 2021 and now down to 5.3% for Q2 FY 2022. Delivering 5.3% is a good step forward related to better managing our capital spend as it gets us in the peer range, albeit at the top end and is a proof point of our improved operational rigor.

Returning to our debt on slide 16, I want to spend a minute on our recent refinancing. This chart shows how the refinancing further solidifies our financial position. By extending maturities, we now have no bond maturities before FY 2026, lowering maturity towers and reducing annual interest expense and cash outflows by about \$50 million a year.

From our improved balance sheet, let's move to cash flow. Cash flow from operations totaled an inflow of \$563 million. Free cash flow for the quarter was \$404 million, up 33% compared to prior year and moves us to positive free cash flow for the first half of FY 2022 of \$100 million. The second quarter was impacted by previously disclosed cash tax payments related to business disposals, accelerated interest payments due to our refinancing and a payment related to restructuring a vendor relationship to take greater control over our delivery.

Further, as part of our strategy to focus on customers, we were able to better manage working capital in the quarter. As we look to the second half, we expect the fourth quarter free cash flow to be stronger. Our third quarter has two discrete non-recurring cash payments, including a \$60 million payment associated with a legacy vendor has a take-or-pay agreement and a \$90 million payment associated with COVID relief legislation where we deferred certain tax payments and now have opted to accelerate the tax payments to utilize the tax deduction.

Slide 18 shows our trended free cash flow profile. The negative cash flow over the last three quarters was due in large part to absorbing a number of non-recurring cash outflows of over \$1.7 billion to put the business on a better trajectory, building our foundation. These cash outflows include \$700 million tax payment associated with taxable

gains on our divestitures, \$500 million to normalize vendor payments, \$332 million related to ready in the US state local health and human services business for sale, \$114 million to end an AR securitization program, \$88 million to end a value-destructive take-or-pay agreement. The \$1.7 billion headwinds put into perspective, the \$749 million trailing four quarters negative free cash flow.

A key driver of improving cash flow is to continue to reduce our restructuring and TSI spend. Our restructuring and TSI efforts are highly focused, and we believe are a prudent investment in the business, addressing our outsized cost structure in certain countries and to reduce our facilities footprint to align to our virtual model. We remain on track to reduce restructuring in TSI from an average of \$900 million per year over the last four years to \$550 million in FY 2022 and about \$100 million in FY 2024.

I would like to take a moment to update our capital deployment expectations from Investor Day. The Investor Day chart called for 55% of our free cash flow to be used to pay debt and capital lease obligations. As a result of our progress, our cash outflows for debt and capital lease financing are now expected to be about 20% of our free cash flow.

That leaves 80% of our expected free cash flow to invest in our business and/or repurchase our stock. I should note, we like the business we have and believe that we have the right level of investment in GBS and GIS. We believe our technology stack has critical mass and capability at each layer. We believe we will create more value by continuing to focus on driving the transformation journey across our business improving the fundamentals and continuing to build organic growth up the stack, ultimately delivering 1% to 3% organic growth in FY 2024.

Related to acquisitions, our focus is to ensure our platinum channel strategy will be fully vetted and proven out. So eventually, when we are acquisitive with tuck-in sized acquisitions, we will have a clear path to deliver value.

Related to our debt, we have a clear line of sight to achieving our targeted debt level of \$5 billion near term as we have scheduled debt repayments via our capital lease financing and commercial paper. Our preference is to maintain approximately \$2.5 billion of cash on hand to fund an appropriate level of working capital.

When we have cash in excess of \$2.5 billion, we will determine how best to deploy the cash as we do not expect to leave significant levels of excess cash, generating no meaningful returns on our balance sheet for an extended period of time. At this point in our journey, we favor share repurchases as our valuation is attractive.

In Q2, we repurchased \$83 million of our common stock, bringing the FY 2022 year-to-date repurchases to \$150 million or 3.9 million shares. Our share repurchases are a disciplined approach to capital allocation and are expected to be self-funding using a rather simple formulaic approach of deploying cash in excess of \$2.5 billion, when we are at our target debt level of approximately \$5 billion. We remain very focused on our investment-grade credit profile.

Turning to our third quarter guidance. We expect revenue between \$4.08 billion and \$4.13 billion. If the exchange rates were at the same level as when we gave guidance last quarter, our third quarter revenue guidance range would be \$90 million higher. Organic revenue decline improved to down 1% to down 2.5%; adjusted EBIT margin of 8.6% to 8.9%. Non-GAAP diluted earnings per share is expected to be in the range of \$0.88 to \$0.93 per share. We are pleased by our progress as we look to the second half of FY 2022.

I would like to update our current fiscal year guidance. Based on the strengthening US dollar, our revenues are expected to be negatively impacted by approximately \$200 million, which has been reflected in our revised guidance range of \$16.4 billion to \$16.6 billion, reaffirming organic revenue growth at down 1% to down 2%,

increasing adjusted EBIT to a range of 8.5% to 8.9%, increasing non-GAAP diluted earnings per share to \$3.52 to \$3.72 per share and reaffirming free cash flow guidance of \$500 million. We are reaffirming our guidance for FY 2024, and this reflects our strong execution in driving forward on our transformation journey.

Before I turn the call back to Mike, I want to reflect a moment as I'm closing out on my first year at DXC. We are clear-eyed on the value we are driving with the transformation journey. We feel strongly there is more opportunity in front of us to continue to improve the business and the underlying economics.

With that, I will now turn the call back over to Mike for his closing remarks.

Michael J. Salvino

President, Chief Executive Officer

Thanks, Ken. Let me leave you with the following key takeaways. We are building the foundation to make DXC operationally efficient, sustainable and ultimately grow. By focusing on the operational work of motivating our colleges and hiring new talent, moving to a virtual-first model, making service delivery more efficient and implementing better IT tools and reducing real estate, we're able to deliver better for our customers and gives us the ability to sell up the enterprise technology stack to GBS.

The good news is the financial results that Ken just took us through reduced debt, shrinking restructuring and TSI costs, increased margin and EPS and stronger free cash flow are all sustainable and a result of the operational work we are doing. This gives us confidence that we will achieve our FY 2024 double-digit margin guidance.

On growth, Q2 confirms that we're on the right trajectory for growth. Our focus on delivering and fixing the GIS business develop trusted relationships with our Platinum customers we're then taking our GBS offerings to our Platinum customers, selling up the enterprise technology stack. The evidence that this is working is in our organic revenue results of GIS, GBS and the overall company. This also gives us confidence that we will achieve our FY 2024 guidance of 1% to 3% growth.

In closing, I'm confident that by staying focused on our transformation journey of building the foundation, we will continue to deliver in the short term and ultimately deliver our long-term financial targets of margin, growth and free cash flow.

Operator, please open the call up for questions.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] Thank you. Your first question comes from Bryan Keane from Deutsche Bank. Please go ahead. Your line is open.

Bryan Keane

Q

Hi, guys. Good afternoon. I just want to ask about the bookings and demand picture. I guess kind of a two-part question. Obviously, the bookings fell a little bit below one in the quarter, but you didn't have to change your organic growth for the fiscal year and that might just have to be done just due to a timing issue. So can you just explain that a little bit? And then secondly, there was some talk about – it seemed like the demand was strong enough that if you had some more able bodies, you could fulfill even a higher demand. So I just want to understand a little bit of, if you have the right amount of people. And I know you had a big quarter hiring, but just trying to fulfill the demand that you have? Thanks.

Michael Salvino

A

Thanks, Bryan. So look, on book-to-bill, the focus for us is around year-to-date, we're over one. That gives us a lot of confidence. And like Ken said, total year, we should be over one. So I don't see a problem in the demand. That's why I called out a couple of deals. If you look at the couple of deals, they were hybrid cloud and ITO deals. So when you look at our page 13, you would see that, that would push that book-to-bill for GIS up around 1.1. So the deals are there. We're definitely winning in the market.

The comment I made in terms of demand and projects is that when I talked about us getting additional debts, because we're delivering on GIS now, is the fact that it's there for us to take. And I think we got to continue to be more aggressive. You guys know that ever since I've been here, I've been very customer focused. And with that focus, I think we can do even more in the market. So that was the purpose for my comment. We do have the people. I called that out in terms of I think we're managing the attrition well. So I like our positioning and like what we're doing in the market, Bryan.

Bryan Keane

Q

Got it. And then how do you do more? I mean what is that going to take for you guys to fulfill that extra push to grow even a little bit faster? Is there something there that you need to do? Or is that just executing at a high level?

Michael J. Salvino

President, Chief Executive Officer

A

I think it's continuing to deliver and continue to knock on the doors of our Platinum accounts. The reason I gave you guys the example of the Platinum account at the end of my prepared remarks, is the fact that when we are delivering, we do get those opportunities. And when we get those opportunities, you're seeing that now we're growing GBS. I mean, the key green shoot in this whole organic revenue story is the fact that GBS now has grown for the second quarter in a row. Before I got here, that business had never grown. So like what we're doing, have confidence in terms of us being able to compete in the market, and so far, so good.

Operator: Your next question comes from Tien-Tsin Huang from JPMorgan. Please go ahead. Your line is open.

Tien-Tsin Huang

Q

Yeah. Thanks so much. The slides are really helpful. I want to ask on GBS since you mentioned it just the demand environment seems pretty good there, Mike. Do you see continued progress there on the revenue front? Can you bring that into the mid-single digits or higher? And I'd say, on the margin front as well, with the high water market, 15.9, can you bring the margins up even higher from that level? Thanks.

Michael J. Salvino

President, Chief Executive Officer

A

Yeah. I mean that progress, Tien-Tsin, is – that's pretty special because when you look at the top of the stack, which is what we've been saying all along, right? Let's make sure we deliver the critical applications in GIS to make sure we get those at bats [ph], and then start selling through that Platinum channel. So when you look at that – the GBS, I mean, analytics and engineering, I will tell you we can compete with anybody. That 17.3%, that's good work, okay? The second thing is, I know, it's small growth, but applications, that's the second quarter in a row, we've grown applications, too.

So again, we're competing in the high-end work. And what we need to continue to do is make sure that we're also fixing the GIS business. And what you're seeing there is that we got to continue to stay focused on modern workplace. Modern workplace saw some really good results this quarter, going from 19.7 negative to now 10.9.

Now that business is going to continue to be lumpy because we're still seeing some runoffs. But the other thing I'm happy to report is when I look at the ITO business, remember all those customer runoffs we had because of non-delivery and so forth? For the most part, that stuff now is done, and we can start seeing good progress in ITO in the second half of the year, Tien-Tsin.

Tien-Tsin Huang

Q

Okay. That's encouraging here. My quick follow-up just maybe for Ken, just on the – I know good work in reducing the capital lease obligations. On Slide 20, I just want to clarify the excess cash allocations inside the circle there. That means after retaining the \$2.5 billion in cash to run the business? I just want to make sure I understood that. Thanks.

Kenneth Sharp

A

Yeah, that's correct, Tien-Tsin. So we'll keep \$2.5 billion of cash on the balance sheet. And when we have excess cash, we'll deploy it.

Operator: Your next question comes from Jason Kupferberg from Bank of America. Please go ahead. Your line is open.

Jason Kupferberg

Q

Hey. Thanks, guys. Just wanted to start on the organic growth side based on what you're guiding to for Q3, that implies there will be a ramp in Q4 to get to the full year target, which is unchanged. Can you just talk to us a little bit about the visibility on that additional acceleration in the fourth quarter? I think you probably need to get to positive territory in Q4 from that statement? Thanks.

Michael J. Salvino

President, Chief Executive Officer

A

So, Jason, look, the – in terms of what we're doing, the guide in Q3 is not only solid, but also it lines us up directly for FY 2022, and when I look at our strategy in terms of the GIS business and GBS business, look, that's going to get us there. What we're focused on with GIS, just to be specific, when you look at page 12, we're looking to drive that to negative single digits over time.

Now, I keep saying it's going to be lumpy this year. So it's going to sort of hang around the 8% range as we fix modern workplace. So that's sort of the bottom end of the equation when you're looking at organic growth. The top end of the equation is I've also been very clear that GBS now is growing and it's going to continue to grow. So when I look at the business, that's how we're going to get to our minus one to minus two for the full year. And I would tell you the visibility on that is pretty good.

Jason Kupferberg

Q

Excellent. Excellent. So on free cash flow, I'm just curious just regarding the Q3 outlook. I know you called out that there will be a couple of non-recurring items, but how should we be modeling the overall free cash flow in the third quarter? I know, you'll then have typical favorable seasonality in Q4 to get to the full year number, but I want to make sure our expectations are calibrated for the current quarter there. Thank you. Thanks again.

Kenneth P. Sharp

Chief Financial Officer and Executive Vice President

A

Yeah. I mean, we haven't really given quarter-to-quarter free cash flow guidance. But I think if you back those items out, I would expect to be around plus or minus \$50 million positive, maybe \$50 million negative, \$100 million, call it, \$50 million to \$100 million, somewhere in that range.

Operator: Your next question comes from James Faucette from Morgan Stanley. Please go ahead. Your line is open.

Q

This is Jonathan [ph] . Thanks for taking our questions. You mentioned an uptick in attrition. Where across the technology stack are you seeing more or less attrition? And what's contemplated in your guidance on a directional basis as it relates to that?

Michael J. Salvino

President, Chief Executive Officer

A

What's contemplated in our guidance is that, one, we're managing it well. And we're managing incredibly well because ever since I've gotten here, we've taken a people-first strategy. That means we're taking care of our folks. The second thing that we're seeing in the market is the fact that not only our people but future recruits, like our virtual-first mindset.

The third thing is we – we continue to keep a polls on folks why I mentioned the September employee engagement results in terms of we had more people participate and we also have a very motivated workforce. So – and then the last thing that, I think people miss is we're also in the right locations. So when we're looking to hire folks, I do think our footprint is an advantage for us. So having said that, we're doing great on analytics and engineering and being able to keep up with that demand and then our other focus is in application and cloud. So that's the stuff that we're focused on in terms of our market and being able to compete and so far, so good.

Q

Got it. Thanks, Mike. And a quick follow-up. What are you seeing in terms of the pricing dynamics across this technology stack? Presumably, there's some pricing pressure given the mix there and as well as the cost of labor so are able to pass on that pricing to your end customers?

Michael J. Salvino
President, Chief Executive Officer

A

I mean, look, the pricing all you got to do is look at 12. All right, 12, we are definitely getting good margins for our GBS business. And then love the right side of 12, because you will see the discipline in terms of the new deals we're also doing in GIS, okay? So when we grow, this growth will be at good margins. And like I said, that's why I like what we're doing. I mean the EBIT margin progress and us having the ability to raise guidance on both margin and EPS is strong. And on the revenue, we're doing exactly what we said we were going to do.

Operator: Your next question comes from Ashwin Shirvaikar from Citi. Please go ahead. Your line is open.

Ashwin Shirvaikar

Q

Mike, I can't or I guess...

Michael J. Salvino
President, Chief Executive Officer

A

Good, Ashwin.

Ashwin Shirvaikar

Q

So my first question was what percent of GBS currently stems from GIS trusted relationships? And the reason I'm asking is, does it make sense? Or are you making progress on also perhaps building out GBS independent of GIS, just to go out and get its own? And I wanted to figure out the dynamic there.

Michael J. Salvino
President, Chief Executive Officer

A

So look, the thing with GBS. GBS, a lot of that is being fueled by analytics and engineering. So then you take the next cut of the analytics and engineering, and what's fueling analytics and engineering, that's Luxoft, okay? Luxoft, when we bought that, we knew there wasn't a lot of overlap, hence, the reason why I called out in my prepared remarks that we are now starting to see us taking Luxoft through that platinum channel. That's good news because not only did customers and they continue to go get their own customers, but now we're also seeing

conversion on the Platinum accounts. And that's, again, good tenants of green shoots for growth. Hence, the reason why we have confidence that, we'll get the organic revenue where it needs to be.

Ashwin Shirvaikar

Q

Got it. Okay. Understood. And then restructuring in TSI, as I sort of look at what you've done year-to-date and the full year projection, it would seem like the current level probably be maintained for the next couple of quarters. I just want to make sure that's accurate and what leads to sort of the quarter-to-quarter step up, step down. Any particular call outs on what you're specifically doing there? Sorry, if I missed that.

Kenneth P. Sharp

Chief Financial Officer and Executive Vice President

A

Yeah. We've guided the \$550 million for the full year. We're running probably a little bit light of that at this point. What I would say, Ash, when we've taken a very disciplined focus effort on every dollar of spend. So we make sure there's business cases, it's being deployed thoughtfully. So you could see it tick up in the second half of the year to get to the \$550 million, but I would just say, we're working diligently to manage it. So I would say that \$550 million is a good number. But if we don't need the money, we certainly won't spend it.

Operator: Your next question comes from Rod Bourgeois from DeepDive Equity Research. Please go ahead. Your line is open.

Rod Bourgeois

Q

All right. Hey, thanks, guys. So Mike, just a big picture question. I wanted to ask about what stage of turnaround you're in, you clearly have margins on the rise despite all the talent challenges out there. And you actually had a string of five quarters with book-to-bill above one. It was actually a little above 1.1, until you experienced a couple of delays apparently this quarter. So just stepping back, it would be great to hear where this now places you on the turnaround trajectory. Can you give us a sense of what inning you're in and if you're at any kind of inflection point given the progression of clients and what's happening in the pipeline?

Michael J. Salvino

President, Chief Executive Officer

A

Okay. Rod, thanks for that question. I'll stay with your baseball analogy, how about that? And in my mind, we are in the early innings for both, all right, organic revenue and also margin. So let's tackle the margin first because the margin is – the progression is clear that we're delivering. Remember the cost levers that we're dealing with, and they're mostly all related to our people. So the first one is we have a bias towards making sure that our own people do the work for our clients, and customers and set a contractor. So we're very focused on contractor conversion.

Second is, we want to get the right people in the right location. That's why I mentioned the footprint. So that's scaling our GIDCs. Third is the virtual-first model. So that's why, I continue to talk about real estate. We should be minimizing or definitely taking down our real estate footprint. And then the last thing is, let's not have our folks do stuff that we can automate.

So when I look at those four levers of cost, I would say, we're definitely in the early innings because there's still much more to do. That's what gives us confidence that we can reach the double digits in FY 2024. Quite frankly, that's also what gives us confidence to raise the guidance in terms of the margin and EPS for FY 2022.

Now look, on revenue, what I would tell you there is the payoff is going to occur over time, but we're seeing a lot of good things happening. So when I talk about green shoots, green shoot number one is NPS is up, that means customers are happy with our delivery. Second is we're definitely getting to see more of bets. Those at bets are coming, both in terms of the GIS business, but we're now seeing all those at bats happening in GBS. But what will happen is those will convert over time. And the best proof of those that, that's converting is the fact that, we are growing analytics and engineering, we're also growing applications.

So look, when I say the early innings, I would also say that the margin is a little bit ahead of the revenue, but the revenues there. I think over time, you're going to continue to see that the strategy we laid out to deliver the GIS business and to continue to try to grow up the stack, the GBS is one that will serve us incredibly well.

Rod Bourgeois

Q

That's helpful, and thanks for dealing with the baseball analogy. Can you also speak to the competitive landscape that you're seeing? It does seem you have two large infrastructure competitors that are amidst some pretty big distractions. It would be helpful just to hear how your competitive position is tracking in your major markets? Thanks.

Michael J. Salvino

President, Chief Executive Officer

A

When I look at that, I like the hand that we have, Rod. And what I look at it, it's a different set of competitors for GBS than it is GIS. So on GBS, you can see not only are we competing, but we're winning more than our fair share, especially in analytics and engineering. When I look at GIS, look, we just need to stay focused. I mean we're laser-focused on making sure that we take care of those platinum accounts. We also, in those platinum accounts where we can expand, we will. And again, I like our position there, too.

Operator: Your next question comes from Bryan Bergin from Cowen. Please go ahead. Your line is open.

Bryan Bergin

Q

Hey, guys. Good afternoon. Thank you. Question on bookings here. So hoping you can dig in a bit more on GBS book-to-bill performance in the quarter. And then, Mike, just more broadly, you've had a good mix of new work in bookings. But can you comment on renewals? I hear your commentary around GIS discipline. So hoping you could dig in a little bit more there.

Michael J. Salvino

President, Chief Executive Officer

A

Okay. So Bryan, what do you ask – tell me a little bit more about what you're looking for on GBS, the first part of your question?

Bryan Bergin

Q

Yeah. So when we look at GBS book-to-bill in the quarter. So that was 0.9 – 4 or 5 – so just comment there on anything that may have slipped in that segment as well or if it's just some lumpiness? And then on the renewals, anything to tease out around GIS discipline as it relates to renewals in that business?

Michael J. Salvino

President, Chief Executive Officer

A

So look, on the top portion, that's – to be honest with you, that's why we gave you the year-to-date stuff because I'm not really that concerned about it at all. And the fact that I'm guiding towards 1.0 in Q3, we should be fine. In terms of the renewals, I always say, look, we're going to continue to have a healthy dose of both, because we had to continue to renew the work we have, but also win new work. And a lot of that new work is still coming on our existing client base. And that's why I give you both numbers, because when I started this whole endeavor two years ago, people thought that the revenue was going to run away from us. And clearly, we're showing now, it's not. And that's why I continue to show you the renewal number. I always want the new work to be a little bit higher than the renewals. So that's why I like the numbers we've got so far.

Bryan Bergin

Q

Okay. Sure. And then just on the Platinum accounts, so it was a good example you provided. Curious how broad-based are those types of experiences that you're having across the platinum account channel today? How far along are they?

Michael J. Salvino

President, Chief Executive Officer

A

Early innings. Early innings, so those take time to do, right? So think about the journey that we've been on. The first step was to get those customers to believe in us again. The second step was to then deliver for them, all right? And that just doesn't happen overnight. Third step one then was to start talking to them and being proactive and innovative with them. And that's not just one conversation. And the reason I gave you that example is that, that's the way these things can look. They take time. That's why I answered Rod's question the way I did in terms of early innings. But we have confidence that the front-end account executive model that, I'm putting in place is going to be able to deliver those type customers for us in the future.

Operator: Your next question comes from Jamie Friedman from Susquehanna. Please go ahead. Your line is open.

Jamie Friedman

Q

It's Jamie from Susquehanna. I had a couple of kind house keeping questions on FX, but I did want to tease those out, maybe better for Ken. But by the way, this slide 22 disclosure on FX, is a great slide. But I wanted to ask, I see that you're calling out \$200 million of FX impact on the year. Did you say what it is for the Q3? I saw that you had \$57 million in the Q2. So that's the first one. What's the Q3 FX? If you happen to have that, I know it's very detailed. And then is your bookings adjusted for FX too? Because if not, would that have impacted the book-to-bill at all?

Michael J. Salvino

President, Chief Executive Officer

Ken, you take Q2, I'll take the book-to-bill.

A

Kenneth P. Sharp

Chief Financial Officer and Executive Vice President

All right. So the Q3 FX impact is about \$90 million, Jamie.

A

Jamie Friedman

Q

Got it. Okay.

Michael J. Salvino

President, Chief Executive Officer

And Jamie, listen, on the book-to-bill, no. I'm not – that the FX, that flat out is knocking down the deals, all right. And look, the great part about where we are now is we're pretty specific about what we can do in each quarter. And to be able to have that forecast figured out and the deals that we need to land, I really like the fact that we've got that discipline. And that's, quite frankly, why I called out a couple of deals. And better yet, the fact that they're behind us and we're now fully into Q3, that's good news.

A

Jamie Friedman

Q

Got it. I'll jump back in the queue. Thanks for that.

Michael J. Salvino

President, Chief Executive Officer

Go ahead.

A

Operator: We have one last question from Keith Bachman from BMO. Please go ahead. Your line is open.

Keith Bachman

Q

Yeah, Mike and Ken, you guys trying to cut me off?

Michael J. Salvino

President, Chief Executive Officer

No. Go ahead, go ahead. Now you get even more time. So go ahead, you can have three.

A

Keith Bachman

Q

I got my starting two questions lined up.

Michael J. Salvino
President, Chief Executive Officer

A

Okay.

Keith Bachman

Q

But I wanted the first one is in terms of the cash flow and the distribution, essentially, when you reach these targets, you're prioritizing buybacks, it sounds like, over M&A. And I was just wanted to tease that out a little bit. And particularly as you're on your journey here to try to get the positive growth rate, why not tilt a little bit more to selective M&A to try to accelerate that form of growth. And I'm not saying use M&A to get growth, but once you buy some companies, it helps you as you even anniversary get in new areas like Luxoft, but why the emphasis buybacks over a little bit of M&A?

Michael J. Salvino
President, Chief Executive Officer

A

So Keith, I will start and Ken will weigh in. The key thing that Ken said is, we've got what we need. And what got to do is kind of continue to execute what we have, all right? So think about the strategies we're putting in place for growth, all right. Delivering fixed GIS and continue to make sure that we're selling the offerings that we have in applications and analytics and engineering. That's piece one. Piece two is the Platinum customer channel and being able to take new things like Luxoft through that channel.

So my point right now is we've got more than enough to get us to where we need to be for FY 2024. Now having said that, you should have also heard that if something falls in our lap, we will absolutely do it, all right? And look at it, we got the money. And don't take Ken's comments as etched totally in stone. I mean, we can pivot one way or the other. But we definitely think we're undervalued right now. So therefore, we think a good use of the cash is to buy our stock.

The last thing I will tell you is we continue to go through this business and do the hard work around making sure that we don't have any distractions from the enterprise technology stack. So we continue to divest a small piece of those businesses that, quite frankly, we are not 100% focused on our enterprise technology stack. So Keith, I look at that work and I look at how we're undervalued, and I say, okay, best use of the cash right now in the short term buyback, all right? All while we continue to balance that investment grade profile, okay? So I think that balance is important.

Keith Bachman

Q

Yes.

Kenneth P. Sharp
Chief Financial Officer and Executive Vice President

A

And maybe just to add to that, because the conversation around free cash flow versus excess cash, I think it's an important concept. So when we laid it out in Investor Day, we spent some time talking about free cash flow. The reason excess cash comes to the forefront is really what Mike talked about a few seconds ago, which is as we dispose of assets that are non-core or aren't really productive for us, will generate cash, we also want to use that cash to deploy that cash in an appropriate fashion.

Keith Bachman

Q

Okay. Okay. Well, why don't I leave it there? I'll ask my other questions and follow-up, but I appreciate it. Thanks very much.

Michael J. Salvino

President, Chief Executive Officer

A

Hey, Keith, sorry about that.

Keith Bachman

Q

That's okay.

Michael J. Salvino

President, Chief Executive Officer

So look, in closing, what I want to do is thank everybody. We really appreciate your interest in DXC. Look, our team really believes that we are building the foundation to make DXC operationally efficient, sustainable and ultimately grow. And I am confident that we just stay focused on our transformation journey and continue to build the foundation will deliver. So with that, all the best to you and your families. And operator, please close the call.

Operator: Ladies and gentlemen, this concludes today's conference call. Thank you for your participation. You may now disconnect.

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