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DXC Technology Services, LLC

Q1 Earnings Call

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PRESENTATION:

Operator^ Hello, and welcome to the DXC Technologies Q1 Earnings Call. (Operator Instructions)

I'd now turn the conference over to John Sweeney, VP of Investor Relations. Please go ahead.

John Sweeney^ Thank you. Good afternoon, everybody. I'm pleased that you're joining us for DXC Technologies' first quarter fiscal year 2024 earnings call. Our speakers on the call today will be Mike Salvino, our Chairman, President, CEO, and Rob DelBene, our EVP and CFO.

This call is being webcast at DXC's Investor Relations website, and the webcast includes slides that will accompany this discussion today. Today's presentation includes certain non-GAAP financial measures, which we believe provide useful information to our investors. In accordance with the SEC rules, we provide a reconciliation of these measures to the respective and most directly comfortable GAAP measures.

The reconciliations can be found in the tables, including in today's earnings release, and in the webcast slides. Certain comments we make on the call will be forward-looking. These statements are subject to known 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 quarterly report on Form 10-Q and other SEC filings. I'd now like to remind our listeners that DXC Technology assumes no obligations to update the information presented on this call except as required by law.

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

Mike Salvino^ 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 overall business performance. Next, I will update you on the performance of our GBS and GIS businesses. Rob will then discuss our financial results in detail, provide his perspective on DXC and his focus moving forward, and then discuss our updated guidance. And finally, I will provide some closing remarks before opening the call up for questions.

Before I get into the results of Q1, I want to give you some context. We are taking the right steps to shape DXC into a company that consistently delivers revenue growth and expanded margins, EPS, and free cash flow. We are doing this by focusing on our high-value growth business of GBS and fixing the historical challenges of our GIS business, along with changing the revenue mix so that GBS represents the majority of our revenue.

As we began FY24, we saw resiliency in our business because in FY23, we delivered four quarters of revenue stability in a slowing IT market. Also, we thought customer demand for our work would stay at the buying levels we saw in late FY23 because the work we do is essential to our customers' operation. Currently, we are seeing customer demand for hardware PCs and network devices, along with some project work, either stopped or delayed to the second half of the year at a higher rate than we anticipated.

You will see that the resiliency in our GBS business held up. GBS performed as we had planned and delivered solid growth.

In contrast, GIS did not show the resiliency that we had hoped. Although this is not great news, I would like to point out that a major piece of the revenue shortfall was resale revenue, which is low margin, and we have conscientiously reduced over the last few years to limit our dependency on this type of revenue.

We have made measurable improvements this quarter to proactively change our organization to be more competitive in this market environment. We have changed how DXC engages with the market by moving to an offering-led operating model.

The offering-led operating model moves us from a regional model, where leaders were generalists concerning offerings, to a global operating model, where the leaders are experts and focused 100 percent on growing revenue and margin for their offerings. This model increases our customer coverage and assures we bring the right skills to our customers to deliver and win new work.

As I mentioned last quarter, our analytics and engineering and insurance offerings were early adopters of this model, and they are consistently our highest revenue growth offerings. Our intent is to get this model to work for the other four offerings.

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Now let me discuss our Q1 results and the performance of our GBS and GIS businesses. Our organic revenue growth was minus 3.6 percent, which is about \$75 million lower than the midpoint of our guidance range. Our EBIT margin was 6.5 percent. The lower-than-expected margin was a result of us needing to fine-tune our new operating model to better manage supply and demand. Our free cash flow was better than expected due to our strong execution around our working capital management. Non-GAAP EPS was \$0.63. And finally, after having a strong second half book-to-bill for FY23, we delivered a book-to-bill of 0.89 as we continue to replenish our pipeline. Our trailing 12-month book-to-bill is now 1.03.

Now turning to our GBS business, the GBS business grew 3.3 percent in Q1. We look at GBS as a flywheel for DXC that provides sustainable growth at double-digit margins. It has now grown nine consecutive quarters. Also, GBS is 49.4 percent of our overall revenue. It is still early days, but we have seen the ability to sell new GBS work to longstanding GIS customers. And scaling this will provide a source of upside revenue to our GBS business.

Our GBS offerings are all uniquely positioned in their respective markets. Analytics and engineering is well positioned due to our engineering talent. Our skilled team does not just write code, but they bring the code together in engineering solutions to make things work better. A great example are the solutions we have developed for the dashboards and the cars of BMW and Mercedes.

Our insurance offering is the world's largest provider of insurance software and BPS solutions, working with 18 of the top 20 global insurers. Our unique position is we run the platform for Lloyd's of London. This platform brings together brokers and writers to create insurance policies for the European market.

We are currently using our custom application team to modernize this important platform, which we believe will be another source of revenue growth.

Along with our custom application skills, we have unique capabilities with enterprise application providers like ServiceNow. We run one of the largest instances of the ServiceNow product, and we have used our custom application team to embed ServiceNow into PlatformX, which is our AI tool that monitors and fixes the IT estates of many of our GIS customers. Moving now to our GIS business. As I mentioned, we did not make the progress we had hoped in GIS, and it declined 9.9%.

Let me give you a quick performance recap of our three GIS offerings. Our security offering grew. This offering provides security strategies and valuable resources to both proactively and reactively help our customers protect themselves against security threats.

Cloud ITO experienced the largest decline. Chris Drumgoole, our former COO, and I are working closely together to fix our dependency on underutilized data centers we own, develop a solid pipeline and path to move work to the cloud, and use our unique position in the ITO market to take market share from our competitors and improved economics.

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An example of us taking market share at Better Economics was our recently announced AT&T deal where we will be providing securely managed server, storage, enterprise backup, and maintenance services to AT&T.

After three quarters of consistent revenue in FY23, Modern Workplace declined in Q1. We expected that Cloud ITO and Modern Workplace would perform better in FY24 based on the following three actions we have taken to fix them. First, we managed the disruption from terminated contracts that happened two to three years ago. This work takes multiple years to fall off, and for the most part, it will be out of our numbers after this year.

Second, we bolstered our customer delivery and offshore delivery capability to secure the revenue we maintain and deliver it at better margins. Third, to win more work, we improved our market reputation. For example, Gartner now ranks us as a leader in Modern Workplace.

We invested in tools to be more competitive, like Platform X and Uptime. We are bringing in new work at Better Economics, and we have positioned ourselves to become the partner of choice to cloud providers as they move workloads that are essential to customer operations to the cloud.

All that being said, it will take a little bit more time to get these two offerings to perform as we expected.

Before turning the call over to Rob, I want to comment on our AI capability that we have built into both our GBS and GIS businesses, because we believe we are in position to lead the market in this area. As many of you know, AI has been a passion for me. I brought this passion to DXC, and we have made focused investments in AI every year that I have been CEO.

We have over 10,000 women and men that are trained in AI, and we have AI capability in now four out of our six offerings.

In GBS, we have embedded our AI capability into both insurance and analytics in the engineering offerings. In insurance, DXC Assure uses AI to better serve customers by providing them insights and answers about the most complex policy questions.

In analytics and engineering, Robotic Drive uses AI to enable cars to be self-driving, ranging from driving technology to assist drivers to full driving automation. In GIS, we have developed AI capability in both our Cloud ITO and Modern Workplace offerings.

In Cloud ITO, our Platform X tool uses AI to proactively monitor IT estates to detect and resolve issues with one of our 10,000 bots to avoid costly business disruptions.

In Modern Workplace, AI is built into our uptime platform, which we leverage across 7 million devices. We use AI every time an employee reaches out for assistance and can resolve up to 80% of those interactions without human intervention, along with using AI to predict issues with PCs and reduce the carbon footprint for our customers.

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The bottom line is all of these solutions are at scale, are providing enhanced customer delivery capability, and are driving new revenue for us.

Now, I want to turn the call over to Rob, who has been a pleasure to work with, and I have complete trust that he will transform our finance organization to deliver the financial analytics to make our results more predictable and repeatable.

Rob, over to you.

Rob Del Bene^ Mike, thanks for the introduction, and thank you for the opportunity to be part of the DXC team.

In my brief time here, I've been impressed by the intense focus on delivery excellence, culture, and customers. I can clearly see the strategic and long-term value of the business. I'll now provide you with a quick rundown of our first quarter performance, covering the important highlights of where we executed well and where we fell short of our expectation.

Organic revenue growth for the quarter was down 3.6%, with consistent year-to-year growth for the GBS segment being offset by a greater than expected decline in the GIS segment. In the quarter, we were impacted by slowdown in customer expenditures. This is mainly the resale of IT equipment, such as PCs, networking gear, and servers, and project work.

These are projects that are typically below \$5 million in size and are sold into our existing account base. The GIS segment experienced the bulk of the slowdown. The declines in resale and projects are consistent with what is taking place in the industry with the economic environment impacting spending.

This, we believe, accounted for the bulk of our revenue underperformance versus expectation, with half of the miss in resale and half in project revenues. In the first quarter, the revenue shortfall impacted profitability, particularly since the revenue weakness was not evident until late in the quarter. While the resale revenue provides little to no bottom-line profit, it does provide modest gross profit and absorb overhead. So in the short term, the underrun in resale revenue impacts bottom-line profit.

As communicated by Mike and the team in prior calls, the strategy over the longer term is to reduce resale revenue and focus the team on driving services revenues. The project-based services revenue shortfall has a greater impact on profitability as the resources to deliver the higher revenue levels are already on board.

Reducing this excess capacity will be a focus going forward. Expenses were well managed in the quarter with spending in line with our expectations. Free cash flow for the quarter was negative \$75 million ahead of our expectations due to continued focus on working capital management, including strong collections performance.

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As a reminder, the first quarter is seasonally our lightest free cash flow quarter, as we made previously planned annual vendor payments for software, maintenance, and paid annual bonuses.

Now moving to our key financial metrics. Our first quarter gross margin of 21.1% was up 10 basis points year over year, but below our expectation due to the revenue shortfall. SG&A spending was down 6.5% year to year flat as a percentage of sales. Depreciation and amortization was down 10.5%, lower by 30 basis points. Other income decreased 40 million year to year, lower by 90 basis points driven by two factors, a \$30 million decline in pension income and a lower level of gains on sales of assets, which reduced adjusted EBIT by 17 million year over year.

Taking this all together, adjusted EBIT margin was down by 50 basis points year over year. Excluding pension income and asset sales, the EBIT margin is up 60 basis points year to year. Non-GAAP EPS was down \$0.12 cents compared to the prior year. The EPS reduction was driven mainly by the lower pension income and a lower level of asset sales in the current year.

The higher tax rate compared to the prior year reduced non-GAAP EPS by \$0.08, but this was fully offset by the lower share count resulting from our ongoing share repurchase program.

Now turning to our segment results. Our business mix continues to trend to our higher margin GBS segment. As a percent of total revenue, GBS is now 49.4% up 60 basis points sequentially. We anticipate that this trend will continue and that in a matter of quarters, the GBS segment will be the majority of our revenue. GBS grew 3.3% organically and posted a ninth consecutive quarter of organic growth, which reflects the deep industry-based customer value delivered by the GBS team. The GBS profit margin declined 60 basis points year over year, reflecting the capacity required to continue to drive future growth and the impact of lower pension income.

Turning now to GIS, organic revenue declined 9.9% driven by declines in cloud infrastructure and ITO and moderating declines in Modern Workplace. GIS profit margin decreased 130 basis points year over year driven by the reductions in pension income, reduced gains on asset sales, and revenue impact of clients delaying project-based services. Now let's take a closer look at our offerings. Analytics and engineering revenue performance was up 8.8%, which is slightly ahead of the fourth quarter growth rate. This is very solid performance in the current demand environment.

The book-to-bill was 1.03x and trailing 12-month number is a strong 1.14x. Applications revenue declined 70 basis points, similar to the fourth quarter decline. The trailing 12-month book-to-bill is 1.06x. The application offering team has made good progress expanding our capabilities and success in enterprise applications such as SAP and ServiceNow.

Insurance software and BPS continue to grow with revenue up 5.1%. The insurance SaaS component of the portfolio grew 8.5%. The insurance software and deep insurance industry BPS skills of our team is resonating in the market.

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Security had strong performance of 6.8% year-to-year. Cloud infrastructure and IT outsourcing declined 12.7%. This business was significantly impacted by a slowdown in both resale revenue and project-based services revenue.

The resale reduction accounted for almost 5 points of the revenue decline, while project-based services revenue accounted for 2.5 points. Also impacting revenue is the wind-down of several contracts that terminated some time ago. The headwinds from these contracts will continue throughout the year and combined with the reduced resale revenue will result in ITO in the negative high single-digit range for the remainder of the year.

Now turning to Modern Workplace. Based on our performance last fiscal year, we anticipated moderating declines going forward. However, like cloud infrastructure and ITO, we experienced the slowdown in project-based services that impacted revenue. We have also experienced several clients moving from a virtual model and taking work back in-house, further impacting revenue. These two factors drove the 5% decline in one queue, and we are anticipating continued year-on-year declines for the remainder of the year.

Turning to our financial foundation, which the team has consistently managed, as anticipated three months ago, debt levels increased modestly in the first quarter to \$4.6 billion. We continue to tightly manage restructuring and TSI expense, which was \$21 million in the first quarter. Operating lease payments and the related expenses were \$90 million, down \$16 million year-to-year. We continue to manage new lease commitments in an effort to reduce our real estate footprint.

Capital expenditures ticked up to \$202 million in the first quarter, impacted by planned annual software renewals. Going forward, we expect to continue the progress that has been made lowering our capital requirements and drive free cash flow. Financing lease originations were reduced by \$14 million year-to-year in the first quarter, another indication that we are lowering future commitments.

As a percentage of revenue, capital expenditures and lease originations increased to 7.3% of revenues with the increase due to the annual software renewal.

Turning to capital deployment, we made continued progress on our latest billion-dollar share repurchase program during the quarter. It is important to note that in aggregate, our share repurchase program will be self-funded by our full year 24 free cash flow of \$800 million and additional asset sales.

As you will remember from our last earnings call, we completed our previous billion-dollar share repurchase program in April. We continue to believe DXC presents an attractive valuation. Assuming the current share price, the approximately \$800 million remaining from the billion-dollar program would equate to removing approximately 15% of the current outstanding shares. And please remember, this is on top of the 21% of shares we have already removed from the share base.

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As a result of the areas of weakness that I discussed earlier, we are lowering our guidance. We expect second quarter organic revenue to decline minus 4.5% to minus 5.5%, reflecting the continued difficult economic environment impacting resale and projects, most significantly in ITO and Modern Workplace.

Adjusted EBIT margin of 6.5% to 7%, with the revenue shortfalls continuing to impact profitability. We expect to improve adjusted EBIT margins in the second half of the year as our cost optimization efforts take hold. Non-GAAP diluted EPS of \$0.65 to \$0.70.

Turning to our full year guidance, we are reducing our organic revenue growth to negative 3% to negative 4%. Adjusted EBIT margin is now 7% to 7.5% impacted by the lower revenue and partially offset by cost reductions in the second half of the year.

We are continuing the successful initiatives from fiscal year 23, focusing on staff and contractor optimization, reducing our real estate footprint, and third-party spending. Non-GAAP diluted earnings per share of \$3.15 to \$3.40. Our non-GAAP EPS guidance reflects a tax rate of 29% and our expectations for the timing of our share repurchase initiative. Our non-GAAP EPS guidance does not reflect potential losses on asset sales that we are evaluating. While potential sales drive cash, they may have an associated non-cash book loss. And lastly, free cash flow of \$800 million, down from our previous guidance of \$900 million.

Now before I turn the call back over to Mike, allow me to comment on my immediate priority, which is to produce the metrics and analytics, meaning the financial headlights, to drive predictable and repeatable results.

I will align the financial teams to support the offering-led model and drive enhancements to our processes and systems. The offering-led model, fully supported, will give us transparency of financial performance and financial returns of the offerings, enabling focused operational management, targeted investments, portfolio management, and help us confirm our strategy.

I expect us to make steady progress with this finance transformation. And with that, let me turn the call back over to Mike for his final thoughts.

Mike Salvino^ Thank you, Rob. And let me leave you with a few key takeaways.

GBS is our high-quality growth business that we are proud of and is performing in a tough project-based environment. We are actioning the cloud ITO and Modern Workplace offerings of GAS, which have been impacted by the slowing IT market and are keeping us from making the progress we desire. We are still confident that we will stabilize the performance of these two offerings. We have made improvements in both leadership and our operating model to grow our company and to be even more competitive. We are managing areas that we can control very well, like free cash flow and restructuring in TSI, and the financial analytics that Rob and his team are focused on building will allow us to deliver more predictable and repeatable results.

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We can see the value we are creating in DXC, and because of this, we will continue to deliver on our \$1 billion buyback while maintaining our investment-grade credit profile.

While the execution of any transformation journey is never a straight line, we feel strongly that we are making the right long-term decisions to position DXC for success.

With that, operator, please open the call up for questions.

Operator^ Thank you. (Operator Instructions)

One moment, please, for your first question.

Your first question comes from the line of Brian Bergen of Cowen. Please go ahead. Hi, thanks.

Zack Ajzenman^ Hi, this is Zach Zack Ajzenman on for Brian.

On the quarter, at a higher level, as you think about how demand played out, just looking to dig further into what changed so quickly here in two and a half months just to cause the magnitude of this guidance, and also, as we think about the guidance framework, has anything changed there given the lower visibility that is seemingly an issue here in the current environment?

Mike Salvino^ So, Zach, thanks for the question. The first thing I would draw back to, when we guided, we began FY24, and we saw resiliency in our business, and specifically, I would highlight the fact that we just came off of delivering four quarters of stable revenue, and we saw the slowing environment during Q3 and Q4 last year, but the revenue stayed stable.

The second thing that's really key in this whole situation is the fact that the work we do is essential for our customers, and because of that, we saw the levels of spend continue in terms of hardware, PCs, and also the maintenance projects that go around maintaining these IT estates throughout FY23.

So when we guided FY24, we expected that the revenue could stay stable and that we could continue to play through a slowing IT environment because we had facts around what the revenue was.

So when I look at Q1 and also the full year, basically what we've done, if you take a step back, you will see that GBS is fine. It grew exactly the way we thought it was. We're happy with it. And when you dig into the offerings, the offerings seem to be doing just as well. So the issue that we're talking about here is contained to cloud ITO and Modern Workplace of GIS.

And when I say contained, when I look at the numbers, the numbers basically haven't changed much. We actually thought the numbers would start heading towards mid-negative single digits, and now that you've heard from us, they will stick around high-negative single digits. And there's two reasons for that. The first one is now the resale revenue, and the resale revenue is the revenue we get by selling hardware and PCs and so forth that we've consistently told everybody that's low margin, and our strategy is to take that

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revenue down, and as we take it down, replace it with service revenue. And what's happened is that's accelerated. We've clearly seen that in the quarter. Half of the miss in the quarter, if you look at the midpoint being \$75 million, half of that was resale, and then we carry that thinking all the way through the rest of the year.

And the reason why we carried it through the rest of the year was because we don't plan to chase that low margin revenue. So if it makes sense, we'll do it, but we're not going to all of a sudden try to chase that. And that goes back to the wholesale philosophy that we've had around making sure that we do these new deals at Better Economics. So that's resale revenue.

The second piece is what we referred to as services project work, and that project work typically is the essential maintenance that needs to be done to these IT estates. And what we've seen is those projects have been pushed, and that's the other half of the miss in Q1. And what we did with looking at the project work is we first of all said, look, the clients need to spend this. And what we're seeing is it looks like they will spend it in the back half of this year. The second thing was the operating model. Was we adjusted the operating model, so I'm looking to see the getting the benefits out of that operating model change towards the back half of the year. And what I mean by that is customer coverage. To literally sell these projects, you've got to sit with the client and describe the value, or potentially the risk. And we think that the adjustment in the operating model will move this forward so that we will recover some of this in the back half of the year.

So that hopefully, that takes into account your questions.

Zack Ajzenman^ It does. And just to follow up on free cash flow and related on margins, I guess given the cut on the revenue and earnings, I guess we're surprised the free cash flow view is not reduced even further. So maybe you can speak to the levels that are partly inflating free cash flow here and maybe what you're doing to support expenses without cutting into the bone.

Rob Del Bene^ Yeah, Zack, this is Rob DelBene. Thanks for the question. Look, when we take a look at the EBIT margin that we expect to perform at that level for the remainder of the year, take a look at the working capital levers we have taken all together, we are confident that we could achieve this adjusted level of \$800 million.

So we have cost reduction plans that support the EBIT, the margin, the reduced margin, and we have operational actions and line of sight to deliver working capital and capital expenditure reductions to get to the \$800.

Mike Salvino^ So Zack, let me add to that, because you have seen that we've been focused and will continue to focus on our expenses. We still think there's more room there. In addition to that, we think that our cost takeout initiatives will deliver at the same levels of FY23. If they deliver at the same levels of FY23, then remember, we generated 737, so we're going to be right there.

So we think that's a good guide. So thanks for that question.

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Zack Ajzenman^ Thanks.

Mike Salvino^ Jay, our next question?

Operator^ Your next question comes from the line of Rod Bourgeois of Deep Dive Equity Research. Please go ahead.

Rod Bourgeois^ Okay, guys. Hey, thank you. So when I ask a question about maybe the linearity of what you're seeing in the more cyclical part of your business, this project-based work and this resale work, have you seen any improvement maybe since the quarter closed that gives you a more encouraged outlook as you move into the later stages of the year?

And I guess more specifically on that, you indicated that you do expect some project work to return in the back half of the year, but I think you also earlier said that you think it will take time to essentially get the ITO and the workplace businesses back on track.

So my question is about the linearity of this cyclical demand issue that you have and whether your guidance, your updated guidance assumes that the project-based work will improve meaningfully in the back half of the year. Thank you.

Mike Salvino^ Okay, so Rod, if you take them in both pieces, first of all, the resale revenue, we didn't expect that. So if you didn't expect that to get better throughout the year.

So you will see that in the guide, the majority of the adjustment is around that resale revenue. Because like I said, we've typically seen that it's been around 25% down. We seem to have been able to play through that in Q3, Q4, but we definitely didn't do it in Q1, so we carried that all the way through.

On the project stuff, the project work doesn't always just impact ITO, Cloud ITO and Modern Workplace. So Cloud ITO and Modern Workplace, we're going to go hard after that project work, but there's project work in the other offerings that are performing well. And we expect that we can increase that project work in the back half of the year. So that's basically the guide. So you should take what we're doing in Q1 and push it all the way through the year. And then for resale and for the project-based services stuff, you should see an uptick in the back half of the year.

Rod Bourgeois^ Okay. And I want to ask another question that I'm seeing kind of on the heels of this update that you've given. You definitely saw other big players in the industry have to lower their guidance for the year because of cyclical challenges, Accenture and Mphasis both had big guidance reductions. You also, during that same quarter, had a CFO transition, so I guess it's worth asking if the CFO transition contributed at all to the shortfall in the expectations.

And then perhaps if something was learned about ways to kind of stay in front of that, to be able to track these things, to recognize them ASAP and make adjustments. And I'm really asking that because I do

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think it was a challenging quarter on the macro, but I also want to get these investor questions in about whether the CFO transition had any impact and whether there were some lessons learned.

Mike Salvino^ So Rod, I would say it had zero impact. What I would tell you is that we changed the operating model in the quarter. And the operating model, we went from a regional model, which you know well, right? You've been in the industry for a long, long time. So the regional model allows our leaders to sell any of the six offerings, and they typically will sell the offerings they know best. So if you're trying to drive this sort of change and you really want to get these offerings to move, then the best way to do it is go to a global offering model, which is what we've done.

And what we talked about is analytics and engineering, along with insurance being our flagship two offerings that have embraced the model. The model is working. We can see them driving the growth in revenue and margin. And what our intent is, is to literally get the other four offerings working the same way.

When you also look at the guide, I expect to get benefits out of that in the back half of the year, as we're still working through making some of the adjustments. But I look at the softness that we see in the project work as the challenge to the operating model, nothing else.

Rod Bourgeois^ Got it.

Mike Salvino^ Jay, next question.

Operator^ Your next question comes from the line of Keith Bachman of BMO Capital Markets. Please go ahead.

Keith Bachman^ Hi. Thank you.

Mike, I wanted to play off something you said about asset sales maybe being part of what happens over the next couple of quarters, and to put it in context, if I think about what's going on essentially half of your business, you haven't been able to turn it around. And in particular, workforce management is an area that you look to sell, doesn't seem like you can get enough value for it, decide to turn it around, but it's still really struggling. And your growth would be much improved without something like workforce management.

So I just wanted to revisit on the broader theme, is there a sense of less is more in some areas that you haven't been able to turn around despite having some opportunity to do so over the last year or so or more? Is there more that you could do on, say, getting rid of underperforming assets to try to help the financial condition of the broader DXC?

Mike Salvino^ So, Keith, thanks for that question. What I would say to that is, look, we're always looking at all of the offerings. And the key thing to the offerings is right now we think that we can sell new GBS work on the GIS longstanding customers, all right? And we're really starting to see an uptick of

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that. So anytime you get rid of an asset, that's not the best thing for our customers. So we think collectively that DXC will be better off if we keep everything together. Now, back to your question about us not being able to move cloud and ITO and Modern Workplace over the last several years, it's not like we're not trying to adjust the business. And one of the things I keep calling out is two things, one, data centers, the fact that we're looking to sell those data centers.

And then the second thing is our ability now, because we have delivered for these customers and we haven't sold these assets because we've got an entryway into those customers, the cloud providers like what we're doing. And what we want to do is be the partner of choice to the cloud providers as they're moving that last set of work, which is so essential and critical to our customers to the cloud.

So that's where we're headed. I would tell you more to come, but we are not just sitting here looking at these numbers and not thinking about other things to do, but they do take a little bit of time to get it done. So Keith, that's the answer to that question. Do you have a second one?

Keith Bachman^ I just wanted to go, yes, sir, I do, thank you.

On the free cash flow to EBIT, I heard the answer to a previous question on why the free cash flow performance is better, some working capital tweaks. And I want to ask it in the context of, are those working capital tweaks, are you sort of borrowing from next year's potential free cash flow generation by some of the things that you're doing to support the 800 target versus a more significant degradation associated with the EBIT line?

Rob Del Bene^ Keith, this is Rob. The answer to that is no.

I mean, we think there are operational improvements that will benefit us over the long term, which will help us drive capital savings over time and get the receivables to what we think is the right sustainable future level.

So we are not trying to accelerate anything temporarily. We're more focused on just operational discipline and getting to the right levels, as I said, on a sustained basis.

Keith Bachman^ All right. Thank you very much.

Mike Salvino^ You're welcome. Next question.

Operator^ (Operator Instructions) Your next question comes from the line of Lisa Ellis of MoffettNathanson. Please go ahead.

Lisa Ellis^ Terrific. Thank you for taking my question. Maybe Mike, at a higher level, and you may not really have an answer for this, but just looking at sort of the evolution of DXC revenue trajectory here to start the year, are there any more, I guess, strategic or transformational types of changes you're considering at DXC to maybe help kind of bend the curve here a little bit?

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I know obviously you've done a lot of portfolio adjustments. I'm just thinking about what other things might be on the table, whether they be more on the acquisition side, additional divestitures, kind of creative client deal structurings, et cetera. Just at a higher level, yeah, what are the types of things you might be considering at this point? Thank you

Mike Salvino^ Okay, so Lisa, thanks for the question, and I'll continue with where I went with Keith's question. Yes, there are strategic things that we can do with cloud and ITO, all right, and we look at, along with Modern Workplace, I mean, we've looked at this as a four-step process, and I understand it's taken longer, all right, and that's not lost on me, and that's not lost on our team. It shows that we will achieve value in those two businesses, although it is taking a little bit more time. So the four steps are these. You remember back when we had to deal with the disruption from the terminated contracts.

Both of those businesses had terminated contracts, and Lisa, you know those terminated contracts take two, three years to have that revenue come out of our business. So this should be the last year that that revenue is coming out of our business, which that's a great accomplishment in terms of you can see that the revenue that we have is all stuff that's going to stick, all right, because of the second thing we've done is we really focused on customer delivery, and that customer delivery, we continue to give you an NPS score that is in the industry benchmark, and because of that customer score and delivery, we also look at it and say, from a customer standpoint, what else can we do with that work?

So the next thing we did was the offshore model. So we've definitely scaled our offshore model for delivery of that work and also to increase our customer satisfaction of it.

And then the final thing is deals. So we will not be doing deals that we don't believe, all right, have good economics. So if you think about the hygiene of the business, Lisa, meaning the revenue runoff should be gone, the customers are being delivered, we've gone to an offshore model, all right, and then the last thing is we're not bringing in any new work at not solid economics, then that makes us very, very, let's call it desirable for cloud hyperscalers to partner with.

So if you go look at the last piece of the cloud that has to go, it's all this essential work that's sitting where? It's sitting in data centers, and those data centers we own, and those data centers are not fully utilized. So doing strategic deals around that will definitely move the ball in our GIS business. So that's about as far as I can go with that, Lisa. Like I said, more to come, but we're definitely not sitting here thinking that we're in a situation where we're in a weakened state. We actually think we're actually in a pretty good state, and yeah, the resale revenue accelerated on us. In all honesty, when you look at what we've done to the resale revenue for the last three years, we've taken that now down from 1.4 in fiscal year 2022 to 1.2 in FY23, and now it will be below 1 billion in FY24.

So what does that mean? That means our revenue that we're talking about on these calls every quarter should be higher quality, should be revenue that we can get good margins on. So anyhow, Lisa, that's the way we think about that bits of business, hopefully, that gives you a little bit more context and color.

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Lisa Ellis^ Yeah, very helpful. And then maybe as a follow-up, I'll give you an opportunity to comment a little bit more on your AI passion. Could you highlight, it sounded like the call-outs you made on some of the AI activities you're doing at DXC, are these, I guess, are the initiatives primarily centered around your own operations internally? Are you doing -- starting to engage with clients on things they're looking at doing with their business? Just maybe elaborate a little bit about what kind of you're seeing in terms of ongoing initiatives right now around AI.

Mike Salvino^ All of it, Lisa, is focused on us driving revenue and showing our customers that, look, we are more than a GIS business, that this GBS business is real and we can take our capabilities that we've scaled in the GBS business and apply them to any of the offerings. So let me go through the four that I mentioned on the call.

So if you look at DXC Assure, right, we have a market-dominating play with our insurance business. When you have 18 out of the top 20 do business with you, you want to continue to keep them by doing innovative things. So DXC Assure literally is able to answer some of their most complex insurance questions.

And I don't know about you, but when I look at a lot of my insurance policies, I've got questions around it, and this tool allows us to be able to answer those questions. So again, helps us generate revenue.

Robotic drive is second to none. The fact that we are not only on the wave of self-driving vehicles, but we are leading that wave is fantastic. And when I said that the AI there does two things, it can help a car automatically drive or it will literally give driving type facial recognition and so forth to help assist a driver driving a car. So again, that's our engineering talent, full go.

And then the AI capability we put into GIS is we've talked about Platform X. I mean, ever since I've got here, I've been talking about Platform X that our clients use because a lot of these monitoring tools on these IT estates are outdated. And Platform X is right there, it's current. The AI capability allows us to launch as we detect and we see that something needs to be resolved that allows us to launch one of our 10,000 bots. And there's very little human intervention, clients love it, and we're very happy about that.

And then the final one is uptime. So the uptime tool, like I said in the call, I mean, everybody's sort of doing the call center stuff where you've got these AI agents that can deflect both written and verbal type questions. And what we've seen is the ability to deflect up to 80% of that volume coming in. But the key thing to uptime is it also helps us predict when PCs are going down and then also helps us, from an ESG standpoint, help our customers manage their carbon footprint.

So I really, Lisa, appreciate the call. Like I said, you know it's a passion of mine. You know I've spent a lot of time before I got here on it. I think we are basically on the cusp of leading that industry. And the way we think about it is we're not going to do anything that we can't scale. We're not going to do anything that a customer doesn't see value in. And then obviously it'll help us drive revenue.

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So Lisa, thanks for that call. And look, let me close by saying this. We are still very confident in our business. When I look at GBS, we think we can continue the growth momentum in GBS in a tough project-based market. And we also believe with the actions that I've discussed on this call along with in the prepared remarks, we think we can improve that performance over time. It's just going to take a little bit longer. And when we do improve that performance, the revenue that you will see in that GIS business will be mostly services revenue and not resale revenue.

So with that, operator, please close the call.

Operator^ This concludes today's conference call. You may now disconnect.

Mike Salvino^ Operator, please close the call.

Operator^ This concludes today's conference call.