Alight Fireside Chat at Morgan Stanley Technology, Media and Telecom Conference
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Jeff Hoffmeister: Great. Thank you, everyone, for joining. I'm Jeff Hoffmeister from Morgan Stanley. It's my pleasure to have the management team of Alight here, Stephan Scholl, CEO, and Katie Rooney, CFO. So maybe why don't I let you both do quick introductions on yourself, and then maybe from that, Stephan, maybe just give for the group just a 2-, 3-, 4-minute overview of the business overall.

Katie Rooney: Katie Rooney, CFO. Been with the company since 2009, so through a lot of the cycles we've been through, if anyone has questions on that.

Stephan Scholl: Great. Hi, everybody. Stephan Scholl, CEO. This month marks the 2-year anniversary, and I should maybe start at the starting point. When I came in, I really saw that the pandemic created a dislocation in the market around how employers viewed the relationship with their employees. And I've been doing this for 25 years in the software technology industry, and I have been largely focused on helping corporations drive client transformation. All the digital disruption that happened around best of breed to enterprise, perpetual to cloud--all of that, largely, I did for 20-plus years in client-facing systems and felt finally that one of the biggest holdouts left for transformation is the human capital management space.

And so we're really driving towards a two-pronged strategy. One is the eyeballs, the fact that we have 30 million employees as a platform play opportunity to build a better relationship with really puts us into a category of one in the space that we're in. So I think that's, we can talk a lot about that, and that's what we call Worklife, or you might hear about it as a business process, as a service offering. But that's strategy number one, is whoever gets to own the relationship with 30, 40, 50 million employees on items related to health and well-being, it's a pretty big advantage.

Two is content to then support that relationship. And so the content we already have is largest health provider in terms of benefits in the United States; 401(k) administration, second-largest administrator of 401(k)s; HSA contributions. So when you think about health and well-being, global payroll, second-largest provider of global payroll in the world. So when you start going down the list of the things that we do on content, that's a pretty powerful two-pronged approach.

We started our journey in public markets just in July of last year. We were pretty clear in our 3-year plan from last January. And so what you're going to hear us talk more about today is that plan of 3 years that we started last January. We're well on our way to getting to our commitments of what we said, which is to double-digit growth by 2023. This year we'll hit north of $3 billion, $650 million to $660 million of EBITDA, and free cash flow of about $500 million. And that's on servicing half the Fortune 500 and 70 of the Fortune 100 clients in the United States.

Jeff Hoffmeister: Why don't we do a balance of the high level to make sure everyone understands, and then the nitty-gritty of the last couple of quarters. Let's take the high level for a little bit longer. Expand on the value proposition, not only to your customers, but to their employees. So when you're having these customer conversations, what's resonating?

Stephan Scholl: I think the--I gave an interview on CNBC and I call it the matrix moment, a little bit of the red pill-blue pill discussion, where prior to COVID, we all were part of the cultural

fabric that corporations built, especially here in California in the tech world. You know, free food and beautiful campuses and the great physical experience, so when you walked into an office and saw your colleagues, you felt really excited that the company was here to help me and support me.

Lo and behold, one day to the next, we all ended up at home and with family and friends, and you start seeing the fragility of the world that we're in and you started needing more help on health and well-being related matters, and you started calling up your company and realized there wasn't enough support there. Fragmented ecosystem. In major corporations around the world, it's between 40 and 70 different systems and touchpoints that it takes for a company to provide these services.

Everybody woke up to what I was saying earlier around, "We need to consolidate, we need to simplify," and so the ask from employers--because again, we serve so many of them. In my first 30 days, I talked to 40 of the C-suite clients in my biggest organization, my biggest client base, and they all said, "Please help us. We need to rise above administration, connect the dots across a fragmented system, and help my employees get better advice around making the right benefits tradeoffs, whether 401(k) I should put more money there versus an HSA," getting better advice on some of the second opinion. You know, "Elective surgery was completely blown up with the pandemic, so now I'm sitting with knee surgery, back surgery. Costs are escalating. How do you navigate that world?"

And then, of course, there's the dynamic of life events--getting divorced, single moms at home with kids. Financial well-being was a huge crisis for a lot of people, and it manifested itself through our programs. You could see it in anxiety, depression and mental illness. We've all read enough about the mental illness category and that's probably the best example I use, which is, is that a health crisis or is it a financial crisis? And the answer is it's both. Yet in order to get an aggregate view of an employee across those two worlds, you have to connect a lot of data.

So we've taken it upon ourselves through Worklife, through our cloud-based deployments, to really connect the dots of data so that we can really see the full picture of an employee and provide the right advice along that journey.

Jeff Hoffmeister: So let's use that as a launch point for Worklife. And you've talked about a grander vision strategy. You touched on some of it here, but elaborate a little bit on how you think about this as a platform going forward.

Stephan Scholl: So to us--I think you all heard it this morning from the whole notion of Peacock being a streaming service and you're hearing about great corporations focusing on owning the relationship of the platform, because then building out content becomes almost an easier play.

So you saw us make two acquisitions last year on the retirement space. We lose 250,000 to 300,000 people to retirement on our existing platform. Through Worklife, monetizing that relationship will be important.

The second opinion example with ConsumerMedical is a great opportunity for us to broaden the experience away from just a single-pillar process to now a more enterprise process.

Jeff Hoffmeister: BPaaS is a term that you've been championing. Everyone has a little bit of a different understanding of it. How do you think about it? And then let's talk about BPaaS specifically in terms of your results last year and, obviously, the strength and talk about how you see that going forward.

Stephan Scholl: I was very intentional about that word versus saying the word "SaaS," because it will never be a pure plug-and-play. When you think about health and well-being, we want to make sure when you need to talk to a doctor or a specialist, you get to that person as fast as possible. When you look at the 180 million interactions that we have, a lot of those can move online to a digital door front. When it comes to our call centers getting calls on, "Am I covered for psychiatry service?" you want a call or text or get messaging or have information in your space of comfort. And that technology didn't exist before.

The notion of logging into Worklife at midnight and you want to ask some questions and get some really informed, specific answers to, "What am I covered for? Which doctor can I go see?" people don't want to talk to somebody they don't know about these topics. So that digital door front of meeting an employee where they want to be met and moving to a mobile phone--for us, that is where you have to get to, and that's the fundamental premise of BPaaS, is getting that Worklife platform.

But you always will need service delivery at some point to do that. And I know many SaaS company CEOs that wish they could walk back the targets they've set on gross margin contribution, because they realize in order to get to growth, you need a healthier balance between software, pure-play software, and service delivery capability, which is we're right in the middle. We're not a services company, we're not pure-play software--right in the middle of leveraging software and services.

Jeff Hoffmeister: Maybe one for both of you. As you look at BPaaS results the last year and what you've talked about for this year, obviously strong growth continuing. What headwinds are there, but also, how should people get comfortable with the tailwinds as well?

Katie Rooney: Yes, if you think about--Stephan said it--we set a 3-year agenda, really a transformation agenda, last January in terms of our financials. And in 2021 we said we were going to grow 1% overall, with BPaaS obviously higher than that. And I think we ended up landing the year at closer to 7%. That did include--Stephan said it--if you think about the Retiree acquisition we made, it's heavily Q4 weighted. So that did have about $123 million of revenue from that deal. But even outside of that, we grew 3.5% ahead of--excluding our hosted business--ahead of where we said we were going to be. So we're starting to see some of those tailwinds.

Jeff, I think part of that was in terms of what drove that outperformance. We had $390 million of BPaaS revenue last year, ahead of where we expected to be. We had over $600 million of bookings in BPaaS, 50% higher than we expected to be. So that's going up to $680 million to $700 million this year. So $1.3 billion of BPaaS bookings, which are helping drive that outperformance on revenue. That's $390 million of BPaaS revenue growing. It will be over $500 million this year. So I think that's a good indicator as we see the demand and the product side of BPaaS really playing through. That's giving us more confidence into 2022, because we now have over 80% of our 2022 revenue under contract because it's a higher subscription base. It historically has been closer to 75%. So again, I think the tailwind is we see that demand. As we see that picking up, that's helping us get more comfortable in the projections--the 3-year projections, honestly--that we outlined last January.

Jeff Hoffmeister: Yes. Let's talk about go-to-market, and maybe we just start with the go-to-market strategy. And then specifically to some of your recent comments about adding to the team and what that means going forward, if you would.

Katie Rooney: Do you want to start on team additions? Sorry, say the first part again?

Jeff Hoffmeister: The first part, why don't you level-set for everyone just how you go to market. I think most people know that, but just start with that. And then you've made some very specific points about adding headcount and obviously trying to lean forward and be aggressive. So maybe both of those.

Katie Rooney: I think the two, if you think about the investment strategy and where we've been focused on how do we drive this transformation has been in our commercial go-to-market and end product. And so three key areas of focus for us on how we go to market is--we've changed them a little bit--is now we have a new logo team. Historically, it was one team selling to everyone. So we now have a great, strong new logo team. We've built out the middle-market capability because in that space, you sell through brokers often, and so building out the feet on the street, those relationships, has been important. And then also some of the value engineering teams.

We're changing the discussion with the client, so it's less about just, again, a services buy and more about how we can drive an outcome for them. And those teams are really helping us think differently about how we change that discussion with our clients and elevate those discussions within the client base to deliver them.

Stephan Scholl: I would say the biggest change was literally the 30 days when I arrived virtually in March of 2 years ago was move to a structure that has a commercial orientation, so sales. I was stunned. 85% win rate for RFPs at Alight. It was pretty comfortable, yet no net new sales team, no enterprise true capability of selling, yet they won incredible amounts of business just because of the capability and the size and scale of who Alight was.

So I said, "Wow, imagine if you could build a net new sales team, a midmarket sales team, an enterprise sales team." The notion of treating AT&T different than a midmarket account sounds obvious. We did some of that, but we needed to do a lot more of segmenting our top clients.

The second one and of equal and, frankly, being a technology product guy by background, is development. We built, and I ripped out all the pieces of engineering and R&D and put it under one person named Greg Goff. He was my first hire. Because at the end of the day, we need to evolve our platform, our technology footprint, and our capability to be much, much more cloud-dependent. I said this last year.

Super thankful to Andy Jassy in his old role, because that was--he was the one who helped drive my last company in 2014. We were the foundation business software company for AWS in 2014 at Infor and driving this huge transformation to cloud. Nobody thought we could so it, and you know that story super well and what happened there.

So that help to driving a technology-forward agenda has really been the core to why we are where we are today. We've delivered more in '21 with health cloud, wealth cloud, payroll cloud and Worklife Version 2 now, done more engineering and R&D development in the last year than we had in the last 4 years combined. And so that will continue with the horsepower. We've hired and spent thousands of people and hundreds of millions of dollars in capital and operating budget to really drive a new technology agenda.

And then, of course, the third pillar is delivery, back to that BPaaS offering. You've got to change your delivery function to provide the new level of service in a differentiated fashion, because I think that's a huge advantage over anybody else who wants to come into this space. You can't just build software and product and say, "Here, you go run it and figure out how to do it." You need the strong delivery function. So those three pillars were core to our transformation.

Jeff Hoffmeister: So I want to come back to both midmarket and the tech platform, but maybe first we'll go back to the really, really granular. So Katie, I'm going to come back to you on organic growth rate, which you alluded to before, talk about not only this past quarter, but how you look forward.

Katie Rooney: Yes, I think I addressed that as you thought about where the revenue was around BPaaS and really, our excitement about where we are heading into 2022. And so we've said it. Historically, we've been a low to mid-single-digit organic grower. Going forward, we'll be a mid to high-single digit organic grower. And you're seeing some of that through the accelerated growth in BPaaS.

We also will go live at the end of this year with a contract to service the Federal Thrift, and 6 million people on top of the 30 million we have today. That's obviously a nice tailwind heading into 2023 as well. And so I think we feel good about where we are. I think the piece we keep coming back to is--Stephan said it--we are finding that right balance, as you think about top line and bottom line, making sure we're putting the capital where we need to, to help drive this opportunity in the market.

Stephan Scholl: Yes, it's pretty exciting. When you started in January with our investor road show, I told somebody you're going to go from 1% to 7% to 10%. The fact that we got to revenue to 4% on our own very quickly and sold $600 million of bookings on a $395 million target, that was like an aha! moment for a lot of people. And that, of course, as a revenue waterfall, gets us comfortable. By the way, on a newer, on a dollars basis on a higher baseline in '22. So we're committing to 6% to 7% revenue growth on the higher baseline, which includes M&A, of course, which I think, hopefully, creates some excitement. And then as Katie said, with Thrift, we're well on our way to being a double-digit grower, which was always the stated objective from last January, was to get there. And that's the North Star for us.

Jeff Hoffmeister: Let's talk about margins a little bit. Katie, you just alluded to them. And then I want to come back to M&A to your comment, Stephan, in terms of how we should think about it. Maybe we started with margins, though, Katie.

Katie Rooney: Yes, if you think about the margin profile of the business, we've said we've got to find the best mix of services and product. And so that will start with a gross margin mentality. We have a long-term target of getting ourselves closer to 60%. That will happen over time, obviously, but the challenge, I think, as you see in 2022, is with the Federal Thrift going live in the back half of the year, but that requires investment upfront. We have had some headwinds in some of the professional services business in terms of the one-time revenue, the cost base around that, significant demand for talent in that space. And we've been investing. And so I think those three dynamics really, as you think about 2022, will be a bit of a headwind in the first half and then start becoming more of a tailwind later in 2022. So we've said EBITDA margins will be flat this year and then really start growing in '23 as we see some of those trends reverse.

Stephan Scholl: People have asked a lot, "Why do you keep the services piece?" And I respond back, when you think about our first strategy of Worklife, at the core of it--I stay away from the word AI because everybody uses it; it's been overused--but at the end of the day, it's about the data architecture. And when you think about me piecing together the fact that I implement base HR and position management and some of the US payroll for Workday, that data architecture combined with my piece of data is just a--I call it the 100% data map. That's why I love that business.

So we're not going out and doing as much as we used to because the Workday business is doing well. The services companies are doing well. I'm repurposing that business, which

is a people-based business to help me with the data architecture to sell one Alight. So that creates some short-term financial headwinds. You are seeing we've got almost a double-digit growth in services on the subscription side, 9% or 10%, somewhere in there, which is exciting because you're seeing us take some of those project-based type dollars and wrapping them up into more outcomes-based agreements. So that's why I'm in that business.

But that's going to cause, on the EBITDA side especially, and the talent pool is a very scarce talent pool because we have VSKs that are certified. But we're willing to play in the long game on that. It's worth the short-term pain to drive through that.

Jeff Hoffmeister: Let's talk about the platform, the data, and you've talked about investing and putting a lot of effort into it since the 2 years since you've been here. So talk a little bit about what data's coming in, what you're doing with it. You just alluded to it. But try and give people a sense for essentially all that you're ingesting and what you're doing to move the platform forward.

Stephan Scholl: Yes, the use cases are pretty varied and powerful, and you've seen some of the big deals that we've won publicly stated. PwC, here's a multi-hundred-thousand person organization seeing that across their network of people. They need to provide them with a better capability not just on, "What deductible should I have on benefits?" The decision to make a deductible on benefits is not just a standalone decision. It comes down to how much money do you make, how healthy are you, where are you and what stage in life are you at, what critical insurance profile do you have? So you have to look at the payroll data, you have to look at what do you have in HSA, you have to look at your wealth profile of 401(k)s.

So when you look at the plethora of data and systems which, by the way, most of that content is ours already, and you can now make tradeoff decisions. I have so many CEO meetings with some of our largest clients where they sit here and say, "I can't believe I just spent billions of dollars in healthcare. My low-income employee population making $40,000 and below all have a $1,000 deductible." It's completely counterintuitive. Yet if you're at home at $40,000, it's the lowest cost-per-month fee, and you pick that aspect because it's just the natural thing to do.

Well, what if we covered you with some other aspects around critical insurance? We told you, you could actually do gross-to-net deductions better, so you can actually pick a $500 plan because it's more tax deductible. So all those tradeoffs happen on the health side. I hope we're all feeling the same thing, which is Dr. Google is not the place to go to get a second opinion on back surgery or knee surgery. And I can't tell you how many use cases I get, people calling us up and saying, "Why did I get a $500 out-of-network fee? I had an accident on the side of the road, banged up my knee, had to go to the doctor." "Well, who did you ask?" "Well, I Googled it," or, "I went to the hotel concierge and I got"-- we all lived that, right?

So the notion of having Worklife on your platform, you open up the Worklife experience on your phone. "Hurt my knee." Elisa looks, and we already have this today, which is we know your network, we know what's in and out of network, we know the doctors. We already have all that data, and based on your situation--obviously, if it's critical, call 911. But most of the cases aren't that, and so giving that capability to, in an emergency, provide the right service.

And then second opinion. I gave, because it's so still in my head, this letter we got, I don't know, 8 weeks ago or so from this woman who said, "Thank you for saving my life." A major corporation implemented our clinical solution, and she had scoliosis, which is spinal surgery and a huge cost to the company, huge cost to her lifestyle. The doctor

recommended the next version of surgery. They implemented us and they said, "Well, no, before we send the money, please get a second opinion from Alight." They sent us all the doctor's forms and we went and looked at everything. "Well, you should get this new blood work test done." And lo and behold, we found out she actually had osteoporosis, as an example. So that's lifestyle change. It's not procedural, it's not medical, so scoliosis to osteoporosis. There's millions of examples like that in this country that, A, are cost-saving, but more importantly, life-saving because you're asking the right question.

Jeff Hoffmeister: Let me pause and see if there are any questions from the audience before I keep going. Yes, sir?

Unidentified Participant: So as you think about developing the platform, I guess how do you think about prioritizing, and maybe it's not mutually exclusive, but adding additional products to support--yes, I'll call them products to support employees versus, like more simplifying the navigation/building in that capability around getting them to the right answer versus just offering them something different.

Stephan Scholl: Yes, I think that is, if you log into--I wish we could do a demo. Katie has on her phone--first of all, it's all in one place. The notion of your benefits, your payroll data, all the data sits in health and wealth-related asks in one area. I think just that starting point is a moment that most probably here, very few of you have. So I think that's a great point.

Then it's a question of how do you decide on tradeoffs on what do you do with the money available? Where do you put it? And that starts off a whole discussion. What are some of your aspirations in terms of where you want to be? So all that analytics and use case capability will sit in Worklife, if that's what your question is. Is that?

Katie Rooney: I think prioritization, too.

Unidentified Participant: Yes, just in terms of adding new content.

Stephan Scholl: So the clinical piece, for example, is one that super excites me. So we have a lot of benefits-only clients. So when you think about Worklife accessing benefits and accessing their 401(k)s, now adding the clinical content is a huge next step in saying--because the number-one issue in my space, outside of the integration of these best-of-breed products, is engagement. So it's cause and effect. You can come at it from--there's great software companies that are great software providers and do what they do, yet their engagements are--like EAP, employee assistance. I still get the visceral response from many CHROs that say, "What's your EAP engagement?" And I said 1% to 2%, and they said, "No, half of 1%," yet they pay a PEPM model, per employee per month.

That use case, you go down the list from navigation to second opinion to benefits--obviously, the list goes on. So the whole intent is to drive engagement through Worklife to a much, much higher level. And so our use cases have seen--Katie has the stats better than I do--it's incredible, what we've seen in just a short period of time with Worklife.

Katie Rooney: And the answer is both. We've got to do both.

Jeff Hoffmeister: Katie, inflation. It's tough to avoid it today these days. Talk a little bit about the impact on your business.

Katie Rooney: I'd say a couple of things. The two areas in particular where we see pressure is in the professional services business, as I talked about, also in some of our call centers, if you think about just the environment there. In the majority of our contracts, we have ECI provisions, so call it on average about 3%, for example, that you start sharing in that, which helps alleviate some of that pressure for us.

And we're also trying to change the way in which we deliver. We call it our project Optimus program. But some of this is how do we--back to Stephan's point--engage with our employees to help offset some of that pressure. So listen, we do see it. That's the reality, I think, for most right now. But I also think the team's doing a great job as we think about, one, the protections we have today, but also how we changed the way in which we deliver.

Stephan Scholl: As much as I talk about the advantages to the client moving to a digital door front with 180 million interactions, and when somebody wants to do a password reset or file transfers for 401(k)s or get more information, moving away from the phone to an online digital door front will help us on our cost base, and it will be a better experience. So we're all going to win in that scenario.

Jeff Hoffmeister: Maybe in a 2-minute span, two topics: international and M&A. You alluded to M&A before. You talked about international most recently on your quarterly call. Touch on both of those, if you would.

Stephan Scholl: Despite the pandemic, I've been able to travel internationally because I see what happens in the US is not just a US phenomenon. The notion of well-being, the notion of anxiety and depression, is not just here in the United States. And I use this story because it just was about 7 weeks ago where I met with the CEO of a major company in Germany. And he said, "Stephan, this is fascinating." And then he said this whole clinical side of things. He said, "Our doctors in Germany must just be that much better than in the United States," because nobody questions anything in Germany when it comes to back surgery, knee surgery, whatever. Here we're all questioning it and we all want second opinions. So I know it's coming over there despite different funding models. But if you just get it right in the UK, DAX region and France, you've solved four of the most economic dynamics. And we know the recipe.

Our advantage is we already have thousands of people--sales, development, delivery--based in Spain and based in Poland and based in the regions. So we've done the hardest part. We know workers' councils' rules. We've just got to get more product, and that's our goal internationally. But I think what's happening here is just our opportunity, because of our size and scale, to take advantage of the international markets.

Jeff Hoffmeister: Yes, awesome. Thank you both for coming today. We really appreciate it.

Stephan Scholl: Thanks for having us.

Katie Rooney: Thank you. Thanks, everyone.