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JBL.N - Q1 2023 Jabil Inc Earnings Call

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OVERVIEW:

Co. reported 1Q23 revenue of approx. \$9.6b, GAAP operating income of \$362m and GAAP diluted EPS of \$1.61. Expects FY23 revenue to be roughly \$34.5b and core EPS to be \$8.40. Expects 2Q23 total Co. revenue to be \$7.8-8.4b, GAAP diluted EPS to be \$1.44-1.84 and core diluted EPS to be \$1.64-2.04.

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PRESENTATION

Operator

Greetings, and welcome to the Jabil First Quarter of Fiscal Year 2023 Earnings Call. (Operator Instructions) As a reminder, this conference is being recorded. I would now like to turn the call over to Adam Berry, Vice President of Investor Relations. Thank you. You may begin.

Adam Berry - Jabil Inc. - VP of IR

Good morning, and welcome to Jabil's First Quarter of Fiscal 2023 Earnings Call. Joining me on today's call is Chairman and Chief Executive Officer, Mark Mondello; and Chief Financial Officer, Mike Dastoor.

Please note that today's call is being webcast live, and during our prepared remarks, we will be referencing slides. To follow along with the slides, please visit jabil.com within our Investor Relations section. At the conclusion of today's call, the entirety will be posted for audio playback on our website.

I'd now like to ask that you follow our earnings presentation with slides on the website, beginning with the forward-looking statement. During this conference call, we will be making forward-looking statements, including, among other things, those regarding the anticipated outlook for our business, such as our currently expected second quarter and fiscal year net revenue and earnings. These statements are based on current expectations, forecasts and assumptions involving risks and uncertainties that could cause actual outcomes and results to differ materially. An extensive list of these risks and uncertainties are identified on our annual report on Form 10-K for the fiscal year ended August 31, 2022, and other filings. Jabil disclaims any intention or obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

With that, I'd now like to shift our focus to our solid quarter. To kick off the fiscal year, the team delivered approximately \$9.6 billion in revenue, well ahead of our forecast and at the top end of our guidance range, driven by even better-than-expected revenue in automotive, health care and industrial. All other end-markets largely performed consistent to our expectations from 90 days ago.

When you put all of this together, at the enterprise level, revenue grew by 12% year-over-year and 7% sequentially. Core operating income during the quarter was \$461 million, an increase of 15% year-over-year, representing a core operating margin of 4.8%. This is up 10 basis points over the

prior year and in line with expectations. From a GAAP perspective, operating income was \$362 million, and our GAAP diluted earnings per share was \$1.61.

Net interest expense in the quarter came in higher than expectations at \$66 million as the combination of higher interest rates and better-than-expected demand drove our working capital needs higher during the quarter. During the quarter, we also repurchased 2.6 million shares for \$161 million. Core diluted earnings per share was \$2.31, a 20% improvement over the prior year quarter and at the higher end of our range as core operating income grew much faster than net interest expense.

Now turning to the segments. Revenue for the DMS segment was \$5.1 billion, an increase of 8% on a year-over-year basis and ahead of our plan from September, while core operating margin for the segment came in at 5.2%, slightly below expectations as upside strength in automotive and health care was offset by operational inefficiencies associated with mobility in China.

Revenue for our EMS segment came in at \$4.5 billion, an increase of 18% on a year-over-year basis, while core margins for the segment was 4.3%, up 50 basis points year-over-year, reflecting solid operational execution on strong revenue growth.

So in summary, another strong quarter is in the books for Jabil. And I know the team here is extremely proud of the strides we've made to not only improve our business over the last 10 years but also make it stronger and more resilient.

In a moment, I'll turn the call over to Mark and Mike to provide some additional thoughts on our performance in the quarter and update our outlook for fiscal '23. And I think you'll see there's still so much opportunity as we move into fiscal '23 and beyond. Thanks for your time today. It's now my pleasure to turn the call over to Mike.

Michael Dastoor - Jabil Inc. - Executive VP & CFO

Thanks, Adam. As Adam just detailed, our performance in Q1 was quite strong. I continue to be extremely pleased with the strength of our business, which delivered double-digit growth in revenue, core operating income and core diluted earnings per share in the quarter. Our diversified portfolio and continued participation in end-markets with long-term secular trends was once again reflected in our Q1 performance.

I'd now like to walk you through our balance sheet and cash flow performance in the quarter. In Q1, cash flow from operations was \$166 million and net capital expenditures totaled \$164 million. As a reminder, our customers routinely coinvest in plant, property and equipment with us as part of our ongoing business model. We often pay for these coinvestments upfront, which are then later reimbursed to us by customers.

Due to the high dollar value of these coinvestments from our customers and how they are reflected on our cash flow statement, it is important to net the 2 line items shown on the slide to reflect the true CapEx number and what we refer to as net capital expenditures. For the quarter, inventory days came in at 78, down 1 day sequentially on improved working capital management by the team. As a reminder, we offset a portion of our inventory levels with inventory deposits from our customers. Net of these deposits, inventory days were 61 in Q1, also down 1 day from Q4. We continue to be fully focused on bringing this metric down further in FY '23 as some of the supply chain constraints continue to improve. We exited the quarter with total debt to core EBITDA levels of approximately 1.2x on cash balances of \$1.2 billion.

Turning now to our second quarter guidance on the next slide. We expect total company revenue in the second quarter of fiscal '23 to be in the range of \$7.8 billion to \$8.4 billion. At the midpoint, this anticipates DMS and EMS revenue to be \$4.1 billion and \$4 billion, respectively. Core operating income is estimated to be in the range of \$347 million to \$407 million. GAAP operating income is expected to be in the range of \$319 million to \$379 million. Core diluted earnings per share is estimated to be in the range of \$1.64 to \$2.04. GAAP diluted earnings per share is expected to be in the range of \$1.44 to \$1.84. Interest expense in the second quarter is estimated to be approximately \$67 million and for the year to be in the range of \$265 million to \$270 million, which is higher than we forecasted in September due to more conservative interest rate and working capital assumptions.

The tax rate on core earnings in the second quarter is estimated to be approximately 19%.

Moving to the next slide, where I'll offer an update on the end-market demand assumptions that we noted in September. As a reminder, our FY '23 guidance assumed a moderate economic slowdown and some moderation in growth in the second half of our fiscal year. Based on what we know today, our assumptions from a demand perspective remain largely consistent. Across many of our end-markets, demand has been extremely resilient, particularly in areas that continue to benefit from strong secular tailwinds like electric vehicles, health care, renewable energy, infrastructure 5G and cloud. We continue to expect these secular markets to expand in the pace of an economic slowdown.

At the same time, we also continue to expect some consumer-centric end-markets to underperform year-on-year consistent with our thoughts in September. All together, we still expect good growth in FY '23, as you'll see detailed on the next slide. Starting with our automotive business, which continues to outperform despite global supply chain issues as the transition to EV accelerates.

We've seen this rapid acceleration manifest in FY '23, automotive revenue growth expected to be in excess of 40% year-on-year. We're also expecting double-digit year-over-year growth in our health care business, which continues to benefit from an outsourcing of manufacturing trend and has historically been recession-resistant with long product life cycles, accretive margins and stable cash flows. Further, our Industrial business is also expected to expand by double digits this year, fueled by growth in clean and smart energy infrastructure as government legislation, such as the Inflation Reduction Act in the U.S. accelerates investment in the space.

And in 5G Wireless, we continue to expect solid year-on-year growth. Infrastructure rollouts are accelerating, and our localized manufacturing capabilities are leading to growth in other geos such as India. We expect these rollouts to play out over the next several years regardless of near-term economic conditions. Within our Cloud business in September, we detailed our plan to shift certain components we procure and integrate from a purchase and resale model to a customer control consignment service model. This transition, in fact, began in November, which is earlier than our expectations 90 days ago. As a result, revenue will be lower than previously expected as an incremental \$300 million of components was shipped to the new model. This is in addition to the \$500 million of consignment impact we announced in September. Adjusting for this shift, we expect continued robust unit growth in the cloud space in FY '23 and beyond.

In summary, we feel the outlook for our business is solid and expect demand across many of our end-markets to remain strong with year-over-year revenue growth at an enterprise level to be approximately 3% for FY '23 despite an assumed economic slowdown in the second half of the fiscal year.

Now turning to the next slide. We have intentionally structured our business with the aim of delivering core operating margin expansion, sustainable earnings growth, strong predictable cash flows and shareholder returns. With that in mind, while we continue to expect growth in our business despite recessionary headwinds, we have identified certain cost savings mainly in our SG&A and support organization for the second half of our fiscal year as we continue to look at doing more with less. And noncore expenses associated with our optimization activities will be approximately \$45 million, with the benefits expected in the back half of the fiscal year. We anticipate these costs will result in a net benefit to core earnings per share of approximately \$0.10 in FY '23 and \$0.20 in FY '24. This benefit has been considered in our updated core EPS outlook for FY '23 of \$8.40. We expect the cash outlay associated with our optimization efforts to be incurred over the next 2 quarters, and we continue to expect free cash flow of more than \$900 million in the fiscal year.

We expect the momentum underway across our business to continue even in a subdued economic environment and feel the steps we've taken to optimize our business are appropriate and make us stronger.

I would like to wish everyone a safe and happy holiday. Thank you for your time today, and thank you for your interest in Jabil. I'll now turn the call over to Mark.

Mark T. Mondello - Jabil Inc. - Chairman & CEO

Thanks, Mike. Good morning. I appreciate everyone taking time to join our call today. I'll begin by saying thanks to our team here at Jabil. Thank you for your attention to detail, and thank you for the way you care for and accept one another. Your attitude is amazing, and your dedication is incredible.

With that, let's move to our next slide. It's staggering when I think about what our team has built and tailored over the past 5 to 6 years. A large-scale portfolio of business sectors, 8 discrete, yet interwoven sectors, which offer Jabil a high degree of resiliency during times of macro and geopolitical disruption as well as gearing times when we simply welcome the ongoing demands placed on us by our customers.

IN looking at this slide, I think about a world where countless products and a massive number of supply chains need to be created, redesigned or modified, therefore placing Jabil deep in the heart of essential end-markets.

Before moving to our next slide, it's worth revisiting the topic that we addressed during our Investor Day event back in September, the topic being the intentional output of the portfolio you see in front of you with the intention being that no single product contributes more than 5% to Jabil's overall earnings. This result is a good thing. It's a really good thing, especially when we think about dependability and sustainability. It also shines a bright light on the strategic importance of diversification and scale and the clear impact it has when operating our business.

In recognizing our Q1 results, along with our 2Q guide as detailed by Adam and Mike, combined with a watchful eye on the back half of the year, we find ourselves with an updated financial plan for FY '23 and an outlook which has us increasing core earnings per share to \$8.40, an increase of \$0.25 from our forecast roughly 90 days ago.

In addition, we believe that core operating margin will hold at 4.8% for the year on revenue of roughly \$34.5 billion. While free cash flow remains north of \$900 million. Integral to this outlook is the fact that our team is doing an exceptional job of proactively managing costs and controlling what they can control in today's environment.

Moving to our next slide. I'll share thoughts on our path forward. Shown here are fundamental catalysts, which are key to favorable results and future outcomes for Jabil. The unique combination of our approach, structure and experience, our ability to execute, combined with our engineering expertise, financial plans that are grounded in rational assumptions and our commitment to returning capital to shareholders. And rounding on our path forward, maybe it makes sense to step back a bit and think about the past few years. The data suggests that what we're doing is working, a testament of just how well our team is managing the business. I'd now like to transition from our path to our purpose. Here at Jabil, we're never confused about our obligation to deliver a fair return to shareholders. With this obligation well understood, and considering the upcoming holiday season, we're taking a little extra time to heighten our focus on ensuring a meaningful purpose in all we do. We're encouraging our employees to take a deep breath and a short pause, creating a little time for reflection, reflect on our team, reflect on their personal lives and reflect on giving back to those in need.

And speaking a reflection, when it comes to helping those in need, I'm proud to report that our employees around the world just surpassed 1 million hours of personal volunteer time for calendar 2022. What a positive difference created for so many around the world, so many who need it most.

Our team's effort was extraordinary. And in multiple ways, their effort was life-changing. Here at Jabil, we fully embraced the meaning and importance of carrying a purpose, both at home and in the workplace. And we do so with exceptional conduct and care.

I'm just so honored to serve such a strong and steady team. Their approach is responsible and reliable. They value the relationships we have with all of those that we serve. Each day, we welcome the challenges put forth by our customers. And in doing so, Jabil's making the world just a little bit better.

In closing, to all of you here at Jabil, please know that you can be your true self without anxiety or fear recourse each day when you come to work. And to everyone on the call today, I wish you a safe and peaceful holiday season. With that, I'll now turn the call back over to Adam.

Adam Berry - Jabil Inc. - VP of IR

Thanks, Mark. Operator, we're now ready for Q&A.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first questions come from the line of Steven Fox with Fox Advisors.

Steven Bryant Fox - Fox Advisors LLC - Founder & CEO

Two questions, if I could, please. First, on inventories, Mike. A little bit of improvement there quarter-over-quarter, and it looks like you were able to get more components on the auto side. I wonder how close we are to just sort of calling spring in terms of normalizing inventories during the course of the next 12 months. And then I had a follow-up.

Michael Dastoor - Jabil Inc. - Executive VP & CFO

Hey, Steve. Yes, so the inventory days that we just printed, 61 days, down 1 day from Q4. A normalized run rate, Steve, would be around that 55, 57. That's what I expect. Not anytime soon, but that is the ultimate sort of aim. I do expect that 61 days to continue to go down to that 58, 59 level. There will be quarterly nuances, timing nuances, et cetera. But overall, the trend would be in the downward direction, particularly with the supply chain constraints easing, as you mentioned.

Steven Bryant Fox - Fox Advisors LLC - Founder & CEO

That's helpful. And then as a follow-up, I was wondering if you could talk a little bit more of some of the stuff you're doing on the energy infrastructure side. It seems to be supporting some good growth in Industrial from the standpoint of how the new program backlog looks. What your right to play in those markets, whether it's increasing and where you're seeing production interest?

Mark T. Mondello - Jabil Inc. - Chairman & CEO

Steve, that's an area of our business. As you know, it's embedded in our Industrial business. We don't tend to break out all the individual products. But in terms of overall energy management, clean energy, et cetera, that's an area where, if you take a look at our overall Industrial growth, I would say that the growth rate of that component of our industrial business is greater than most of the other industrial business.

So whether it be solar, whether it be off-grid battery storage, whether it be new efficiency of off-grid power generation, mobile power generation, it's an area that's, from a strategy standpoint, very important in the next 3 to 4 years of the overall Industrial business.

I'd equate it -- I don't know that the growth will be as secular as maybe EVs. But 5, 6 years ago, when we made decisions to go hard into the EV market and move a lot of our resources that way, you could think of it a bit the same in terms of our overall Industrial business. That part of our Industrial business is getting a lot of attention.

Steven Bryant Fox - Fox Advisors LLC - Founder & CEO

Any skill set you would point out as to why you guys are winning in that segment in particular?

Mark T. Mondello - Jabil Inc. - Chairman & CEO

Yes. You're welcome. I guess I'd make a general statement and a specific statement. I think one of the interesting characteristics of Jabil is to be really effective in this business over the long term, I think scale matters. And then in one of the slides that we just indexed through, if you look at the overall portfolio today that make up the \$34 billion, \$35 billion of revenue, the balance of the portfolio is substantial.

And so again, coming back to your specific question, when I think about the markets that you're referring to, a, we've got a whole set of engineering staff that are, let's just say, expert in that area. But much like all of our businesses, they also have a vast pool of engineering resources in other sectors that they also get to confer with and talk to and think about being creative in terms of overall solutions in the industrial space. And I think that makes a big difference.

Operator

Our next question is coming from the line of Jim Suva with Citi.

James Dickey Suva - *Citigroup Inc., Research Division - MD & Research Analyst*

You mentioned a little bit of manufacturing challenges with the DMS segment. I assume that has to do with the COVID closures and things. Can you just update us as we sit here now around December 15, have those kind of been back to normalized? Are there still inefficiencies going on? Or any changes in how we should think about those efficiencies and inefficiencies?

Mark T. Mondello - *Jabil Inc. - Chairman & CEO*

Jim, I think for the quarter, so if we backward look to September, October, November with the kind of zero-COVID policy, everything that was in the media around China and then kind of our exposure to that and our experience with that, in very round numbers, I would say that the kind of overall China COVID activities probably impacted Q1 by about \$10 million, give or take. As you've seen recently, and maybe you're referring to this with some recent changes around the zero-COVID policy, we'll continue to manage that in much the same way, being very careful, practical, thoughtful in terms of managing China coming out of a zero-COVID policy.

We've been doing that around the world since January of 2020. I think our protocols around the world and in China are kind of best-in-class. And I think protocols and processes aside, Jim, I give a huge amount of credit to our leadership team and our supervisors on the ground in China. We have a fabulous relationship with our people and our employees, and that in and of itself makes a huge difference. So anyway, that's our intent.

James Dickey Suva - *Citigroup Inc., Research Division - MD & Research Analyst*

And then as a follow-up on a different topic, you mentioned some more consigning. That was kind of the same customer? Or is it expanding more or the relationship getting deeper? Or is it kind of getting broader for the consignment? I'm just kind of curious, it seems like to me, I should think about the consignment as a good thing for like more sticky business and sticky relationships.

Mark T. Mondello - *Jabil Inc. - Chairman & CEO*

Yes. I'm not going to get into customer-specific. I think when it comes to parts of our cloud business, Jim, we've been very, very consistent. And I don't know the first time we came out on a call and started talking about our entry into the cloud business based on our right to play and the solutions that our team wanted to bring forward. But what we talked about maybe back in 2018 and through 2019 and even through 2020 and COVID and on and on and on, we've been extremely consistent with the fact that our value proposition in that area of our business is very geocentric and very asset-light.

And said differently, we do a very good job of aligning variable costs with the puts and takes of the revenue. This is nothing more than that continuing. And the team has done an absolutely fantastic job of growing that business. I think on one of the slides again that we showed, you can see our Cloud business or let's just say, Cloud and 5G and is now \$6 billion, give or take. So I think that's a proxy for how successful they've been. And again, we'll continue, and our intent is to continue to run that an asset-light way.

Michael Dastoor - Jabil Inc. - Executive VP & CFO

And Jim, if I could just add, I think when we gave guidance in September, our assumption was that the consignment would start sometime in March. We actually managed to get it done far earlier in November. So you're seeing an earlier impact of this consignment piece showing up in our -- a little bit in Q1 but mainly in Q2.

Operator

Our next questions come from the line of Shannon Cross with Credit Suisse.

Shannon Siemsen Cross - Crédit Suisse AG, Research Division - Research Analyst

I wanted to understand a little bit more about the decision to reduce costs. I understand there's continued productivity improvements that you can do. But I'm wondering sort of what you saw out there that led you to do this? And how much of it is proactive versus changes you've already seen in customer behavior? And then I have a follow-up.

Mark T. Mondello - Jabil Inc. - Chairman & CEO

I think it's a natural decision. We -- the word's -- I don't know if I'd use the word difficult, but let's just, for lack of a better word, things are a bit choppy right now, a little bit difficult. And whether it's running our business in each sector of our business in a different way based on what customers need, whether it's our execution, whether it's overall cost management, I think when we sat here in August, September, and we're taking a hard look at the year. Our belief is that we should be maybe a bit more cautious to the back half of the year as we sit today.

So Mike and I got together with our leadership team, and I'm really pleased with the outcome. And by the way, this was a hard press by the overall team. We're just being proactive in terms of -- largely in terms of overhead costs and maybe costs that sit on top of the factories. I think that Mike said in his prepared remarks. And I think one thing, I think it's worth differentiating, being proactive in the methods -- in the way we're being proactive in terms of cost management is, to me, way different than say, writing off or writing down assets.

It's really about taking a look at the business, being aggressive and proactive and then being sure that shareholders get a very fair return on that in short order. And I think Mike in his prepared remarks somewhere said, on our cost management and the charge we took in the quarter, investors will get about a dime back at the back half of this year. But more importantly is I think the payback for '24 and into perpetuity will be \$0.20, \$0.25. So I think it's good use of our effort and nice returns for shareholders.

Michael Dastoor - Jabil Inc. - Executive VP & CFO

And Shannon, our business assumptions continue to be extremely robust. I think I highlighted some of the secular trends that we're actually participating in. All of those continue to show very decent growth.

Shannon Siemsen Cross - Crédit Suisse AG, Research Division - Research Analyst

Great. And then just one other question. How -- when you talk to your customers, how are they thinking about geographic distribution of manufacturing these days. Given the challenges in China, I know it's starting to open up again, but obviously, it comes and goes. I'm wondering how much of a discussion customers are having about Eastern Europe and India? And obviously, you're pretty well positioned to help them as they move production around.

Mark T. Mondello - Jabil Inc. - Chairman & CEO

Thank you. Happy holidays to you too. I don't know that there's a general theme. I think we have 400-plus customers, and I think our customers' thoughts are all over the map, and they're doing the best for their business based on their products. Everything -- and this will give you a little bit of a feel for the complexity of it. And by the way, it's why our structure is so efficient and so optimal in terms of customer solutions.

Here at Jabil, we don't run our business on a factory basis. We run it customer by customer, line item by line item. And the reason we do that is, let's just take a product that, let's say, the unit cost is x, but the ability to move that product around the world in terms of distributing the product is very expensive. Well, that would suggest maybe we build it in-region.

We have other products that cost y and moving that product around the world is very small relative to the cost of the product, and we might consolidate that to a single spot in the world. Then you add to it, all the different geopolitical issues, the very unfortunate issue that continues to wane on in the Ukraine. So it's hard for me to go, geez, this is kind of the herd mentality of our customers because the business just doesn't act that way. Also, I would suggest that when you look at our portfolio, and you look at the 8 sectors that we define and then you think about all the subsectors of the business, Again, one of the things I think is a huge strength at Jabil is the diversification. And with that diversification becomes endless amounts of solutions.

And again, I take you back to our approach and our structure. We kind of work with each customer in a very unique way, accommodating their needs. With that being said, I would say that you'll probably see us do some expansion in Eastern Europe. You'll probably see us continue to expand in Mexico. I think we feel pretty good about our footprint in China. And you'll probably see some expansion over the next couple of years in India.

Operator

Our next questions come from the line of Matt Sheerin with Stifel.

Matthew John Sheerin - Stifel, Nicolaus & Company, Incorporated, Research Division - MD & Senior Equity Research Analyst

Yes. I have a question, Mark, regarding your updated revenue guidance for FY '23. You're raising the outlook for auto and health care. Is that related to just better supply conditions or demand related? Why taking that number up -- taking those numbers up?

Mark T. Mondello - Jabil Inc. - Chairman & CEO

We're taking them up because we can. I mean, as we sit here today, one could look at it and go, why would you guys take the numbers up, if you're somewhat cautious about the back half of the year or gosh knows what's going to happen in '23 based on what the U.S. Fed is doing in the markets, et cetera, et cetera. But I think we use very good judgment. Again, a real good charm about Jabil is we break our business up into really, really, really small pieces. And it gives us really good acuity, high resolution of all elements of our business.

So in a more general sense, I think the -- again, referring back to one of the slides that one of us spoke to, is we're -- as we sit today, we're going to -- we think we'll see double-digit growth in the areas of auto and transportation, largely driven by EVs. Health care, I think we showed on the slide would be maybe north of 10%. And then same with our Industrial & Semi-Cap business, largely being led on the industrial side.

And the growth in all 3 of those areas, a, supply chain is getting better and getting better faster. One caveat there is, is legacy semiconductors in the EV space are still tight. But supply chain is getting markedly better. Our ability to gather parts relative to others is very strong. And then in certain aspects of those, based on certain trends, demand is holding reasonably well.

Matthew John Sheerin - *Stifel, Nicolaus & Company, Incorporated, Research Division - MD & Senior Equity Research Analyst*

Okay. Great. And then a question, Mike, regarding the incremental consignment revenue that you talked about. So total \$800 million in revenue going to consignment for your cloud customer. Does that move the needle on gross margin at all? Is there any change in terms of the operating margin or operating income on that business?

Michael Dastoor - *Jabil Inc. - Executive VP & CFO*

So yes, it does move the needle a little bit on margin, but there's been some offsets. I think Adam highlighted some inefficiencies that we had on the mobility side in China, particularly in Q1. We've made some assumptions around further COVID, et cetera, as well in parts of the world, and that does have a little bit of an impact on margin. But you're right, on the consigned side, it has a small margin improvement impact. And that's one of the reasons we pursue this with -- along with the customer.

Mark T. Mondello - *Jabil Inc. - Chairman & CEO*

If I could add to that, here's a real simple way to think about it in very round numbers. Two years ago, the overall op margin for the company was 4.2%. Last year, it was 4.6%. This year, at the beginning of the year, we suggested that the op margin for the year will be 4.8%. We're holding to that 4.8%, which we're proud of. So there's a 20 bps expansion between '22 and '23. About half of that is based on our cost management for the back half of the year as well as continuing to advance our asset-light nature of our cloud business and the other half of that is the lack of a better word, the core business.

But what's interesting is, I don't even like differentiating that because for me, -- all of this activity goes hand in hand with running a good business. So -- but in terms of your modeling and the way to think about it, I think that's a reasonable way to think about it.

Operator

Our next questions come from the line of Ruplu Bhattacharya with Bank of America.

Ruplu Bhattacharya - *BofA Securities, Research Division - Director & Research Analyst*

Congrats on the quarter. My first question is on the DMS segment. Mark, you're seeing strong growth in automotive and health care, and you've taken up those 2 segments combined by \$600 million for the full year. Like you said, the consumer-facing end-markets in that segment are weaker, and you're taking that down by 200 basis points. Net, when I look at operating margin, it's down 10 bps. So my question to you is if the consumer-facing end-markets get weaker, can you talk us through your thoughts on margin risk in DMS? I mean, how -- do you think margins can go lower in that segment? Or what offsets do you have -- and typically, the reason I'm asking this is because typically one would think automotive and health care to be higher-margin end-markets. So if you're seeing a mix shift into that, what's driving the 10 basis points lower? And how do you see risk to that if the consumer-facing markets go lower?

Mark T. Mondello - *Jabil Inc. - Chairman & CEO*

Ruplu, that's a little bit of an open-ended question because I don't know if you mean it this way, but I'll answer it how I understand it, which is if the bottom falls out of all consumer-facing products, could the overall DMS margins go down further? Maybe. As we sit today, I think we've done a reasonably good job of for what we know, handicapping the back half of the year. And you -- the way you stated it is largely correct. We've really kind of haircut and handicap any consumer-facing products. And again, the reciprocal of that is we feel good about industrial, automotive and health care.

If you -- as you're putting your model together for the year, we just reported first quarter -- we just gave you a hard guide on 2Q. As I think about Q3 and Q4, our DMS margins, as you start putting numbers together and do your after calls and whatnot, I think what you'll find is doing the math is to have our DMS business end up being at 5% or 5.1% margin. Whatever it ends up being, Q4 is going to end up being a pretty strong quarter. And I think that's reflective of exactly what you said, which is some of the higher margins in auto and health care.

I would also -- why we're on the topic of the year is let's not be -- let's be sure it's not lost on us. The hard work and the complementary work that our EMS team is doing in terms of their business and margins for the year as well. When we went into 1Q, on the EMS side, we thought margins would be in the 4%, 4.1% range, that came in 4.3%. If you take a look at our guide and do your math on that, you'll see the strong margin returns. And then if you think about the year on the EMS side, last year, I don't remember the exact number, but EMS was 4.2%, 4.3%. Beginning of the year, we thought EMS would be -- for the year, EMS would be around 4.4%, 4.5%. And I think EMS is going to come in closer to 4.6%, 4.7%. So again, let's step back and just have an appreciation for the fact that the business is kind of an entire portfolio. And I say that respectfully I understand your question was around DMS. I hope that helps.

Ruplu Bhattacharya - *BofA Securities, Research Division - Director & Research Analyst*

Yes. I appreciate that. For my second question, if I can ask, Mike, 4.8% operating margin total for the company. Can you help us quantify the inflation pass-through impact on that. I'm assuming like other EMS companies as component costs have gone up, you're passing that through. I'm not sure if it's a dollar for dollar, but if it is, then your revenue should be hurting -- but sorry, your margin should be hurting because of that. And so what would that 4.8% have been if there was no inflation pass-through?

And when we think about modeling margins, if we look back, the Slide 13 that you have, you've kind of shown us the last 5 years and how the margins have progressed since fiscal '19, very strong performance. But I mean, as we model out going forward, what are the puts and takes here? Like I mean you're going to get a benefit as inflation goes down. That should help margins. But what are the other things that can drive margins? And any guidance you can give to -- how do you think about what the target margins can be in the long term?

Mark T. Mondello - *Jabil Inc. - Chairman & CEO*

Ruplu, I'll stop that one for a minute. Wow, that was a lot. Let me bring you back to what I think was the first part of the question, which is, yes, you're correct, in the first quarter, at an enterprise level, margins were 4.8%. I kind of think you answered your own question, which is 1Q of last year, margins were 4.7%. We thought that the first quarter would come in back in August, September. We were guiding and anticipating the margins for Q1 would be 4.8%. They came in right on top of the 4.8%. Again, I'll bring you back to DMS margins, were down about 20 basis points. EMS margins were up 20 basis points. Again, indication of the size, scale, but again, the wonderful diversification we have.

If we didn't have good understandings with our customers in terms of equitable sharing when variable costs go up and down, we wouldn't have delivered the 4.8%. So I don't say that to drive a concern. I say that much in an opposite way, which is the way we have our business set up, the way we have our customer relationship set up are very satisfactory to our leadership team.

In terms of what else could have impacts on the overall margins for the year, it could be anything. On the downside, it could be that -- the macro gets worse on the -- so what do I worry about? Yes, the macro could collapse is that and the other, but then that instability will be there for everybody. What I don't worry about is -- I don't worry about our team's ability to execute. I don't worry about our team in and of itself. I love the portfolio that we have. I don't worry about the size of the market. I don't worry about our ability to continue to gain share. And maybe you wrap all that up, I think our team, both at a factory level and above factory does a really, really nice job of controlling what we can control.

Ruplu Bhattacharya - *BofA Securities, Research Division - Director & Research Analyst*

Got it. I mean I really appreciate all those details. And wondering, maybe now if I can sneak 1 more quick 1 in. I know you've announced Kenny Wilson to be the new CEO effective May 1, and you're going to take on more of a strategy, corporate development role. So can you just talk about

from now until then, what are some of the handover activities you're going to do? And should we think of any change in direction to the company? Or how should we think about this transition? Congrats again on the quarter.

Mark T. Mondello - Jabil Inc. - Chairman & CEO

Well, that's an interesting question. I've been at this a long time, and I'd make this comment not directly around my relationship with Kenny. Whether my relationships with Kenny or Borges or Dastoor or McCoy or JJ or all the folks that you've met, we are -- we have a significantly tight-knit group. We've all been at this a long time. Sometimes that becomes problematic because it feels sometimes like we've complete each other's sentences. So we've got to continue to challenge ourselves so we don't have a group think.

But Kenny has been with us a long time, so has the balance of the team. I don't envision any of this being revolutionary. I think it will be evolutionary. We also added some other new leadership to the team recently with LaShawne and [Christine] in Legal. So I think we'll carry on.

With that being said, as I continue to move more and more throughout the year into an active Chairman role, and you're right, I'll have my hands firmly involved with investors and our foundation and strategy and other stuff, I hope the team takes my 10 or 11 years and is disruptive in a positive sense. I think one of the things that this team has done over and over and over and over in time and time again, over 30 years is I think we're proactive. I think we changed when we need to change, we don't change for the sake of changing.

And I'd say, Kenny and some of the expanded leadership team is probably, in some sense, a little bit more edgy than I can be. And I think that's a good thing. So I think there'll be I think there'll be some good changes. You can think of them as evolutionary, not revolutionary changes because the foundation we've built for this business has never been stronger. And I'm really, really, really looking forward to the next 2, 3, 4 years to see how things shake out.

Operator

Our next questions come from the line of Paul Chung with JPMorgan.

Paul Chung - JPMorgan Chase & Co, Research Division - VP & IT Hardware Analyst

So just on cash flow, you've typically seen more cash investments in 1Q, but you actually squeezed out some free cash flow this quarter. So is this more about timing or maybe less need for working capital investments kind of given elevated build last year? And any comments there in the kind of the shape of free cash flow for the year? And then also on guidance, it remains unchanged. So how are you kind of offsetting the increase in interest expense and kind of cash outlays on optimization? Or was that kind of included in your projections last quarter?

Michael Dastoor - Jabil Inc. - Executive VP & CFO

Yes. So the free cash flow assumptions that we have today that reflect everything reflect -- they reflect the sort of charge that we've taken, the cash outlay associated with that. Don't forget that the savings on the other side of that as well. So there is definitely everything that's out there is reflected in the free cash flow. From a Q1 standpoint, I think it's more timing. We've talked about our CapEx being in that 2.5% range, not much changes from that 2.5% guidance that we provided in September. You'll always have timing differences, you'll have nuances. From a shape of the year perspective, I sort of -- I just use shapes from previous years. I think it will be very similar to that. Obviously, timing moves things here and there a little bit. But overall, we still feel committed to our \$900 million free cash flow number for the year as well.

Paul Chung - JPMorgan Chase & Co, Research Division - VP & IT Hardware Analyst

Got you. And then just a follow-up on op margins in very kind of good progression here over the last 2 years, some nice benefits from cloud consignment, but can you expand on the drivers to get to that 5% mark and kind of the pace beyond fiscal year '23. You're doing some cost

optimization here, but will it be more a function of mix kind of efficiencies or even scale as you guys are approaching \$10 billion in quarterly revenue run rate now.

Michael Dastoor - Jabil Inc. - Executive VP & CFO

I would suggest all of you about, Paul, I think it's definitely a mix, operational efficiency, something we always execute on. We've always invested in the past around automation, robotics, et cetera. So we feel good about that as well. And overall, the margin, does it go beyond 5%, 5.5% as well. We're not stopping at 4.8%, and we're definitely not stopping it at 5% either. So it's something we're actively engaged in and feel very strongly about.

Operator

Our next questions come from the line of David Vogt with UBS.

David Vogt - UBS Investment Bank, Research Division - Analyst

I have a big picture macro question on sort of demand. And you talked about your demand characteristics being relatively consistent with 90 days ago. But I'm trying to square it with your commentary being a little bit more cautious as we move through the back half of this year. I guess my question is when you think about what's happening in the marketplace, we're seeing some intensity drop from a capital per spend in telcos and cloud. How much of your demand visibility or your revenue visibility has to do with elevated backlogs because supply chain has been sort of elevated for quite some time versus the in-period demand that you're seeing today from your customers? And then I have another question.

Mark T. Mondello - Jabil Inc. - Chairman & CEO

David, well, first off, welcome to the group. I think you just started coverage on us, and we look forward to spending more time with you so you can better understand the business. In terms of your questions, there's pent-up demand, but I would caveat answering your question similar to a prior question, which is I don't want to make a blanket statement because, as an example, let's take networking or, say, legacy telco, that part of our business today is about \$3 billion on a \$35 billion base.

So in terms of what type of backlog we see from the telco folks or the networking folks, I guess it's relevant. But in terms of our overall corporate results, I'm not sure how impactful that might be. I think 100%, we have seen pent-up demand and backlog across almost every single area of our business where supply chain constraints existed.

If I could paint it with a broad brush and take this with a degree of inaccuracy, I guess, because I'm trying to paint it with a broad brush across a large-scale portfolio, I think that most of the pent-up demand and the backlog, in general, will probably be alleviated by late 1Q of '23 or into the second quarter of '23 to say the first half of '23. So I think most of the pockets of backlog clear and normalize, as we get back -- as we get to the back half of calendar '23. Again, I don't know if that's helpful or not, but that's kind of a general statement as we look across the business.

David Vogt - UBS Investment Bank, Research Division - Analyst

No, that's helpful. What we're trying to kind of understand is sort of the normal cadence of sort of order trajectory of the business, stripping aside what we've kind of lived through the last couple of years. So that's helpful. We appreciate it.

And then maybe just a final question on cash flow and capital priorities. You've done a great job in terms of returning shareholder capital and managing cash flow over the last couple of years. Does your commentary about the second half or maybe some of the cash used for the restructuring change any of your priorities in the balance of this year? I wouldn't think so, but just wanted to just confirm with you.

Michael Dastoor - Jabil Inc. - Executive VP & CFO

No, there's no change to our capital allocation. We've talked about in September, we have another \$1.1 billion left of our authorization. We continue to use it. We use quite a bit of that in Q1, and we'll be doing in the range of \$150 million, \$200-plus million type of buybacks every quarter. So nothing that happens in the second half for -- also that, that actually be an opportunity to do some more in fact, if things start going south.

Mark T. Mondello - Jabil Inc. - Chairman & CEO

Thank you. We have reached the end of our question-and-answer session. With that, this does conclude today's teleconference. We appreciate your participation. You may disconnect your lines at this time. Enjoy the rest of your day, and happy holidays.

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