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DXC.N - Q1 2021 DXC Technology Co Earnings Call

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OVERVIEW:

DXC reported 1Q21 GAAP revenues of \$4.5b and non-GAAP EPS of \$0.21. Expects 2Q21 revenues to be \$4.40-4.45b and non-GAAP EPS to be \$0.30-0.35.



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PRESENTATION

Operator

Good day, and welcome to the DXC Technology's First Quarter Fiscal Year '21 Earnings Call. Today's conference is being recorded.

At this time, I would like to turn the conference over to Shailesh Murali. Please go ahead, sir.

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

Thank you, and good afternoon, everyone. I'm pleased that you are joining us for DXC Technology's First Quarter Fiscal Year 2021 Earnings Call.

Our speakers on today's call will be Mike Salvino, our President and Chief Executive Officer; and Paul Saleh, our Chief Financial Officer. This call is being webcast at dxc.com/investorrelations and the webcast includes slides that will accompany the discussion today. After the call, we will post these slides on our Investor Relations section of DXC's website.

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

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

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



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

Thank you, Shailesh, and I appreciate everyone joining the call today. I hope you and your families are doing well as we all continue to navigate through the COVID-19 pandemic. I'm going to start today's call by giving you an update on our Q1 performance and how we are progressing on our transformation journey to position DXC for growth.

Paul will then share our financials for Q1, our guidance for Q2 and update you all on our strategic alternatives, including the recent sale of our health care provider software business. Then I will make some closing remarks before opening the call up for questions.

I was very pleased with our performance during the quarter, which has allowed us to have a strong start to FY '21. Our revenues came in higher than we thought in May, highlighting the resiliency of our business during COVID-19. Margins also came in higher, underscoring the effectiveness of our program to optimize costs. And our book-to-bill for the quarter was 1.2x, underscoring that we are successfully bringing the new DXC, which focuses on our customers and our people to the market. This new approach is allowing us to cross-sell our capabilities to our existing customers, win new logos and renew existing work. Our results in Q1 show that DXC is very relevant to our customers, especially during tough times.

Now I'd like to discuss our transformation journey and give you some specifics concerning how we are doing in the 3 key areas, which are: focus on our customers; optimize cost; and seize the market opportunity. Our focus on customers is really starting to pay off. Simply put, this focus allowed us to deliver higher revenue in Q1 and will enable us to stabilize revenue in Q2.

Let me give you an example. This week, we renewed and expanded our relationship with Sabre, an account where our standing was not in good shape. We brought the new DXC to the account and now we are looking forward to working with Sean, his leadership team at Sabre, along with Google, to transform and modernize Sabre's IT estate to the Google Cloud. I'm happy to report that with the Sabre signing and us working through the final details with 2 other accounts, we have successfully fixed 38 of the identified 40 challenged accounts. We have rebuilt these relationships, and we are winning more work.

Let me give you some stats. 31 out of the 40 accounts have given us new work in excess of \$10 million since the start of the program in Q3 of FY '20. We are now done with this program and this customer-centric mindset is fundamental to the new DXC. Our people are the cornerstone to delivering for our customers. The investment we made to enable 99% of our workforce to work virtually has resulted in DXC delivering on our customers' expectations during the COVID-19 pandemic.

The Australian Tax Office is a great example of where our people delivered for a key customer during COVID-19. DXC helped the Australian Tax Office deliver wholesale changes to systems and operations in 2 weeks to support troubled businesses and workers. The CIO commented, the way our teams collaborated and worked as one was truly inspiring.

I'm also extremely proud of how our people handled the ransomware attack which impacted the exchanging business. Our team immediately implemented a series of containment and remediation measures, got our customers up and running, and kept our customers updated every step of the way. Under the leadership of our new CIO, Chris Drumgoole and Mark Hughes, who runs our Security business, our people did a great job of resolving the situation quickly and protecting the interest of our customers and DXC.

Among the many thank you notes we received from our customers, Lloyd's Market Association summed it up the best saying, "The transparent and collaborative way in which DXC has addressed the challenge has been first class." I would like to thank all of our people as they are clearly engaged and delivering for our customers.

Now let me turn to our cost optimization program, where we continue to make good progress. Here, we were able to move faster than anticipated, simplifying our management layers and taking the appropriate steps to rightsize our cost structure to our revenue. We have achieved better-than-expected margins in Q1 due to these efforts. We're on track to achieve our goal of taking out \$550 million this year and ensuring our people are focused on making business impact for our customers. We expect to expand our margins from Q1 to Q2.

Finally, let me comment on the third key area of our transformation journey, which has seized the market opportunity. We are focused on cross-selling to existing accounts and winning work with new customers. Our book-to-bill ratio of 1.2x this quarter is good evidence that we are indeed seizing

new market opportunity. The Q1 bookings were comprised of 1/3 new work and 2/3 renewals. New work was generated through a combination of cross-selling to our existing customers and winning work from new customers. Let me give you an example of each.

Zurich Insurance Group is an example of cross-selling new work to an existing customer. At Zurich, we expanded our relationship, we are helping them transform and modernize their applications and security globally. A great example of new work from a new customer is ivari, where we were selected to help modernize ivari's legacy systems, provide policy administration and customer support services.

Also, I don't want to ignore our renewals, as they are solid evidence that we are delivering for our existing customers, who are willing to make additional multiyear commitments to DXC. All of this is evidence that our strategy is working, and we expect to hit a book-to-bill of 1x in Q2.

Now before I turn the call over to Paul, I want to reiterate. I was pleased with our performance in Q1, and we are well positioned for Q2. Now let me turn the call over to Paul.

Paul N. Saleh - DXC Technology Company - Executive VP & CFO

Well, thank you, Mike, and greetings, everyone. Before I cover our financial results for the first quarter, I'd like to echo Mike's comment about our performance. We delivered results which were ahead of the revenue and profit targets we shared with you on our last earnings call. Now this is clear indication that we are making solid progress on our transformation journey.

Now our business has proven to be more resilient in this COVID environment, and our offerings are clearly relevant to our customers. Now however, our first quarter results may not reflect the progress we're making due to the lag effect from prior terminations, price downs and runoffs. We expect these headwinds to subside starting in Q2.

Now turning to business under strategic reviews. We remain on track to close the sale of our State and Local Health and Human Services business in the current quarter, which will allow us to reduce debt and further strengthen our balance sheet. The recent agreement to sell our health care software business will further enhance our financial flexibility.

Although we're quite encouraged by the progress we're making on multiple fronts, we're still operating in an uncertain COVID environment. As a result, it's not yet the time to provide you with full year guidance, but we will continue to update you on our progress on a quarterly basis. So for the second quarter, we expect revenue to stabilize, margins to improve in our bookings to continue to reflect the relevance of our new DXC in the market.

So now let me turn to our first quarter financial results. I'll start by covering the items that are excluded from our non-GAAP results. In the first quarter, we had restructuring costs of \$72 million on a pretax basis or \$0.24 per diluted share. These costs relate to the cost optimization program we discussed previously. Also in the quarter, we had \$110 million on a pretax basis or \$0.32 per diluted share of transaction-, separation- and integration-related costs, and those were primarily driven by the external spend associated with the assets under strategic review.

Now in the first quarter, amortization of acquired intangibles was \$148 million on a pretax basis or \$0.45 per diluted share. Excluding the impact of these special items, our non-GAAP income before taxes from continuing operations was \$107 million for the quarter, and our non-GAAP EPS was \$0.21, which is higher than we had indicated during our last earnings call. Our non-GAAP EPS in the quarter was impacted by a higher-than-expected tax rate of 45%, reflecting our mix of income and accrual related to a return to provision adjustment associated with prior tax filings as well as the valuation allowance in certain foreign jurisdictions.

Turning now to our first quarter results in more detail. As always, all revenue comparisons I'll discuss will be in constant currency. GAAP revenue in the first quarter was \$4.5 billion, representing a sequential decline of 5.7%, but an improvement over the guidance we provided during our last earnings call.

Our revenue for the quarter reflect the resiliency of our business with a lower-than-anticipated impact from COVID during the quarter. Currency in the quarter was an incremental headwind of about \$40 million sequentially and \$101 million compared with the prior year. Adjusted EBIT in the quarter was \$190 million. Adjusted EBIT margin was 4.2%, reflecting the acceleration of some of our cost-optimization initiatives.

For the quarter, we delivered \$60 million of cost-optimization savings, which is about \$45 million better than originally planned. This helped offset a \$36 million in accruals related to the resolution of certain prior customer disputes. And at this time, I'm able to report that we have dealt with the vast majority of outstanding disputes.

Non-GAAP EPS was \$0.21 in the quarter. And as I previously mentioned, our EPS was impacted by the higher-than-usual tax rate of 45%. Normalizing for a tax rate of 28%, EPS would have been \$0.28. In the quarter, bookings were \$5.3 billion for a book-to-bill of 1.2x.

Turning now to our segment results. I'll start with the GBS segment, which includes the 2 top players of our enterprise technology stacks: analytics and engineering as well as the applications business. The GBS segment for now also includes 3 businesses under strategic review. The U.S. State and Local Health and Human Services business, the health care software business, which we recently agreed to sell to Dedalus and the horizontal GBS business.

GBS revenue was \$2.17 billion in the quarter, down 5.2% sequentially. Year-over-year, GBS revenue was up 2.5%, reflecting the acquisition of Luxoft. In the first quarter, GBS profit was \$215 million, and our profit margin was 9.9%. Excluding the impact of dispute-related accruals of \$26 million, the profit margin for GBS would have been 11.1%. GBS bookings for the quarter were \$3.5 billion for a book-to-bill of 1.6x.

Turning to our GIS segment. Our GIS segment consists of the ITO and the cloud and security layers of our enterprise technology stack. It also includes our Workplace and Mobility business. GIS segment revenue was \$2.33 billion in the first quarter, down 6.1% sequentially and 12.4% year-over-year. The decline was primarily driven by the impact of prior terminations, price down and runoffs that we previously discussed.

GIS segment profit in the quarter was \$23 million and profit margin was 1%, reflecting the timing of our cost actions. Now we expect margins to improve for the remainder of the year as we execute on our cost-improvement plans and align our cost structure to revenue. GIS bookings for the quarter was \$1.8 billion for a book-to-bill of 0.8x.

Now let me comment on the performance of the layers of the enterprise technology stack. Let me highlight again that in the first quarter, the revenues in each layer of the stack and the ensuing sequential and year-over-year comparisons are not truly indicative of the trajectory of the business, and this is due to the lag effect from prior terminations, price down and runoffs.

ITO revenue was down 5.2% sequentially and down 18.7% year-over-year, driven by the terminations, price down and runoffs we discussed previously. Book-to-bill was 0.6x in the quarter, reflecting the timing of large contract awards, which typically take at least 6 to 9 months to negotiate and close. Now we are encouraged by the progress we're making in the ITO layer, which is evidenced by the strength of our qualified pipeline. And we are targeting a book-to-bill of 1x for the second quarter.

Cloud and security revenue was down 11.1% sequentially and down 6% year-over-year. The revenue decline in this layer of the stack was driven primarily by runoffs as well as deferral of project-related spending. Book-to-bill was 1x in the quarter. Moving up the stack, the application layer was down 8.7% sequentially and down 7.5% year-over-year. The decline was primarily driven by some terminations and project completions as well as delayed work in industries most impacted by COVID such as travel, hospitality and consumer goods. Book-to-bill for this layer of the stack was 1.5x in the quarter, reflecting a number of long-term applications management contract renewals.

In the analytics and engineering layer of the stack, revenue was down 2% sequentially, primarily due to delays in project work. Year-over-year, revenue was up 52.1%, driven by the acquisition of Luxoft. Book-to-bill in the quarter was 1.3x.

Turning now to the business under strategic review. We remain on track to sell the U.S. State and Local Health and Human Services business to Veritas in the current quarter. We completed and delivered audited carve-out financials for the business, which was an important closing milestone. And as we discussed previously, we plan to use the after-tax proceeds from this transaction to pay down debt.

Additionally, on July 20, we reached an agreement to sell our health care software business to Dedalus Group for \$525 million in cash. This was an opportunistic transaction as Dedalus was looking to broaden its software portfolio, we were able to realize an attractive value for the assets. Now this transaction is expected to close by our fiscal year-end, and we plan to use the after-tax proceeds of \$425 million to \$450 million to pay down debt.

Now turning now to the horizontal BPS business and the workplace assets. We continue to be in discussions with interested parties. The strategic evaluation process has taken longer than anticipated due to the current COVID environment. But we are focusing also on finding the right strategic fit for our customers and employees. And so as part of this process, we're also evaluating the benefit of retaining these assets. But we expect to make a final decision on the best path forward for these assets by our next earnings call.

Turning to other financial highlights. Adjusted free cash flow in the quarter was a negative \$28 million, reflecting the timing of annual payments of software licenses and maintenance and also a slight increase in working capital in the current COVID environment. We expect adjusted free cash flow to be positive in the second quarter.

Our capital expenditures, including the payment on capital leases, was \$382 million in the quarter or 8.5% of revenue. Cash at the end of the quarter was \$5.5 billion. Our total debt, including capitalized leases, was \$12 billion for a net debt to total capitalization ratio of 38.4%.

As we stated previously, we plan to use the proceeds from the sale of the U.S. State and Local Health and Human Services business to pay down debt. On a pro forma basis, total debt, including capital leases would have been less than \$5.5 billion at the end of the first quarter. Now this assumes we had a minimum cash balance of \$2 billion, which is a more normalized level, absent this COVID environment.

During the quarter, S&P and Fitch revised their ratings of DXC to BBB- and BBB, respectively, but upgraded our credit outlook from negative to stable. Now we remain committed to maintaining a strong financial position consistent with an investment-grade credit profile. The after-tax proceeds from the sale of the health care software business will only serve to enhance our financial flexibility.

So in closing, we expect revenue to stabilize in the second quarter in the range of \$4.4 billion to \$4.45 billion. Margin in the second quarter should improve sequentially to 5% to 5.5%, reflecting additional contributions from our cost-optimization initiatives. We are targeting our non-GAAP EPS in the second quarter to be \$0.30 to \$0.35 based on an effective tax rate of about 35%.

And with that, I'll now turn the call to Mike for his closing remarks.

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

Thanks, Paul. In summary, we had a positive start to the year.

Now let me share with you 3 key takeaways. First, on customers. I am pleased to say that we have fixed the challenged accounts, and those issues are behind us, which was one of my top priorities when I started with DXC. We have rebuilt our customer relationships and reinstalled confidence in our delivery capabilities, enabling us to stabilize revenue. Our people in the new leadership team are key to this turnaround. They are fully engaged, and their efforts are being recognized by our customers.

Second, on profitability, we are making clear progress on our cost-reduction target of \$550 million for this year. We are ahead of plans, but clearly, this is not the end state. We know the industry profitability benchmarks and have a number of levers that we will execute over time to close our gap. Beyond this year, the opportunities that we have already started include: the consolidation of real estate and data centers; the use of technology, like Bionix, across more of our delivery footprint; and finally, further optimization of our organization through permitting, offshoring and contractor conversion.

Third, on the market, we are making good progress capturing an opportunity that is unique to us. In challenging times, we've seen customers turn to us for their IT needs because they know us, they trust us, and we've delivered for them for years.

So in closing, we believe the positive momentum that we created in Q1 will carry over to Q2 and will be another positive step forward on our transformation journey. And with that, operator, please open the call up for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) And we will take our first question. This will come from Lisa Ellis with MoffettNathanson.

Lisa Ann Dejong Ellis - MoffettNathanson LLC - Partner

Good stuff here on the results this quarter. Look, I know this revenue stabilization quarter-to-quarter is a key factor. Everyone's watching very closely. Mike, I know you highlighted some things like the 40 challenged accounts. But can you maybe give a little bit more commentary?

I know you've mentioned in the past, the top 200 accounts. Just what are the factors giving you confidence that we're going to see this revenue stability when we get into 2Q?

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

Lisa, thanks for the question, and always good to hear from you. The -- look, ever since I started securing the customers, and it's not just the 40, right? It's all of our customers. Around making sure that they had confidence in not only our delivery, but also how we were dealing with them.

So when I talk about the new DXC, I talk about it being focused on our people and our customers because we've always said, right, if you lose the people, you lose the business. So we're very focused on that. Our people are engaged. Our customers are seeing it. And based on that, we feel very good about the stability of the revenue. And that's what we're saying around Q2. I think that's going to be the step in the right direction.

And then specifically, what we mean by stabilized revenues is that you ought to expect that we'll be either flat or slightly up quarter-on-quarter.

Lisa Ann Dejong Ellis - MoffettNathanson LLC - Partner

Okay. And then -- good. Maybe for my follow-up, just a question on talent. I know you just highlighted that. And I know DXC doesn't disclose talent metrics like headcount, attrition or utilization. But can you give us a sense for how those metrics are trending? Maybe like voluntary attrition, in particular, just over these last few quarters, how are you feeling about the morale and the labor base?

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

So let me give you -- one, let me give you even a different stat. When I started, we took an employee engagement survey, we recently finished that. We've got our Board meeting next week, and employee engagement is significantly up. Significantly. And they're actually seeing the fact that the town halls that I'm doing, the town halls that the leadership team is doing, the engagement on how we've dealt with them during COVID-19 and also social injustice, it matters. And they're definitely paying attention. I can't thank them enough. Because without them, right, we don't stabilize this revenue. Without them, we don't deliver for the customers.

So very pleased with how our employees are engaged.



Lisa Ann Dejong Ellis - *MoffettNathanson LLC - Partner*

Excellent. And nice results in a tough environment.

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

Thanks, Lisa.

Operator

And we will take our next question. This will come from Rod Bourgeois with DeepDive Equity Research.

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

So I want to ask more about where you're going with margins. I recognize there's definitely a bunch of COVID impacts and moving parts with your divestitures. But at the same time, you're citing revenue stabilization and progress on your cost actions. So it would be great to get your thoughts on your margin prospects for the rest of fiscal '21. If you can say a little bit even beyond Q2, that would be really helpful.

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

Rod, thanks. And again, always good to hear your voice. The -- first, let me give you some context, right? The -- when you look at what we're doing, first of all, we're managing a transformation journey. Second now, we have added another strategic alternative that we're managing. And then obviously, we're managing COVID-19. And I think we're doing that incredibly well, meaning we're making very good progress.

So again, I don't think it's the right time to give guidance. But here's what I can tell you. I've got the entire organization focused on expanding margins. And that's what you're going to see in Q2 and should continue to see quarter-on-quarter for the rest of the year. Now why do I say that? I say that because we're making very good progress against the \$550 million in cost savings.

Now beyond that, we still have the multiple levers that I talked about in my prepared comments. And that's stuff that we're already working on, like consolidation of real estate and data centers, right? I mean, we -- what we want to do with our employee base is to find a new employee experience. So the folks that are working virtual are incredibly excited about that. And that will allow us to deal with the consolidation of real estate.

Second is the use of technology, all right? You know that's part of my playbook. You know I've used that in my past. Bionix is very good, but there's more technology that we can put on this delivery footprint with Vinod.

And then last, we are very focused around starting to optimize the organization. The organization was not ready to optimize when we started here at DXC, okay? Now we've got things stabilized with customers, all right? We like where the revenue is. So us now looking at pyramiding and also offshoring the rate -- make sure we've got that right mix is important.

And then, look, I talk a lot about the employees, okay? And we are very focused on contractor conversion because it's very hard to build a culture if a significant portion of that workforce is contractors. And we're definitely all over that, all right? And the contractor base sees it and feels it.

So what I would say, Rod, summarizing that whole thing, is that, look, all of these points will help us close the gap on the industry benchmarks. So I'm pretty pleased with where we're going, not only immediately, but also long term.



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

Great. And just a quick follow-up. You mentioned the Sabre deal. I'm very interested in that contract since Sabre had earlier announced they were moving to Google Cloud. It seems significant now that Sabre is now signing a deal with DXC, too.

Can you talk more about that situation, particularly if it's indicative of what's going on at other accounts? Is the Sabre situation, a case of a customer-facing challenges to switch away from a legacy service provider? Or is that just the case of DXC fixing a customer relationship? Can you just elaborate there?

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

Okay. So look, Rod, on Sabre, we're thrilled, right? We're thrilled to be working with Sean, we're thrilled to be working with Google, and it wasn't just fixing a relationship, right? When I talk about the new DXC, it was literally bringing our analytics, our apps, our cloud and security and our ITO capability to showcase in front of Sabre. So when you look at that deal, the thing I like best about that deal, which is indicative of other deals, large deals that we've got in the pipeline is its full enterprise stack.

Now what do I mean by that? It's got every single layer in the stack that we show. Roughly 70% of it is ITO. Roughly 40% of it is cloud and security and apps. And then the final 15% is analytics and engineering. So we're thrilled, right, by that deal.

The other thing I will tell you is this, the industry continues to talk about the cloud, the cloud, the cloud, all right? And we believe in the cloud. We always have believed in the cloud. We think that the industry, though, is going to take a very balanced approach. What we talked about during the last earnings call, is that we've used virtual clarity across 135 of our top 200 accounts. And over the next 2 years, those clients aspired to move 20% of that critical work, which is where the industry is now, moving critical work to the cloud, which won't happen overnight.

But when you went through the process of technical feasibility, risk, business case and the ability to execute, that cloud percentage dropped to 5%. And what was telling about all that analysis is the existing ITO work, our clients wanted 60% of the remaining work to be modernized.

Now why do I tell you all that? I tell you all that because it's a balanced approach, it's an and, right? You got to do ITO and you've got to be able to do cloud. And what I had a client tell me this quarter, was what DXC is, is the engineers for engineers. Like, we know how to do the engineering work, whether it's on-prem or in the cloud.

So like I said, I like the Sabre deal, not just because it got us back in to a client that was moving away. But more importantly, it's a full enterprise stack deal. So that's probably more than you wanted to hear, but those are my thoughts on the Sabre deal.

Operator

And we will take our next question. This will come from James Faucette with Morgan Stanley.

Jonathan Lee - *Morgan Stanley, Research Division - Research Associate*

This is Jonathan on for James. Congrats on the quarter. Can you talk through some of the mix of work you're seeing from the challenged accounts and potentially some of the pricing considerations in those accounts?

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

So Jonathan, thanks. So first of all, on the pricing, I just talked about our margin, all right? So we are very focused on obviously growing revenue and stabilizing that revenue, but also making sure those margins are good, all right? So we like the margins we're getting with the new work, and we're incredibly disciplined around that.



Now the work on the challenged accounts is, again, full enterprise stack. I mentioned during the last earnings call that we were pursuing our top 200 accounts to cross-sell. That's one of the reasons why you spend all this time to make sure these customer relationships are rebuilt. I've said it over and over again, that clients give trusted people that have delivered for them more work. And what we're seeing is we're seeing the work across the stack. We're seeing it in the analytics and engineering offering, primarily fueled by not only DXC but Luxoft.

We're also seeing it with cloud and security and apps. And then the final piece is, again, as people move to the whole virtual mindset, as people started to take real notice to the ITO layer. So in some cases, we've helped them shore up that layer. In some cases, we've, quite frankly, shut down some of the ITO layer because we can see great ways to get cost savings. So that's what we see. And that's just not for the 40 accounts, all right, but it's also across our top accounts, Jonathan.

Jonathan Lee - *Morgan Stanley, Research Division - Research Associate*

Appreciate the color there. Can you also walk through the puts and takes around horizontal BPS and the considerations you're taking there in terms of evaluating potentially keeping that asset? I believe that, that disclosure was sort of net new.

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

Yes. I mean, look, the way I always look at these alternatives -- and first and foremost, is it the right thing for our customers? And is it the right thing for our people, okay? And you know my background pretty well. I'm pretty deep in BPO, all right? And if I can't feel comfortable with that, and if I can't feel comfortable with the value that we're getting out of that, then we think we can create shareholder value by keeping it. That's clearly one of my strengths in my past, and I can see clear to fixing that business if we need to.

Now having said that, you shouldn't take away that we're still not trying to work deals, okay? And we've got a few working immediately, and like Paul said, we plan on landing both the BPS and the workplace strategic alternatives. Basically before the next earnings call, Jonathan.

Operator

And we will take our next question. This will come from Ashwin Shirvaikar with Citi.

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

I guess, first, good to see -- it's good to see the quarter-to-quarter progress, both the strategic and tactical. I wanted to start by asking you about your thoughts on what is your target leverage? Because I'm thinking post HHS and the health care software sales and the associated paydown, shouldn't you be getting to an appropriate level of leverage where other uses of cash become more likely?

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

So Ashwin, the -- thanks for that question, all right, and much like the guidance, I'm not going to talk about the alternative use of the cash, whether it be dividends, whether it be buybacks, whether it be potential acquisitions. Because, again, where we are is we're laser-focused, right? This quarter-to-quarter progress that you all have seen now is a lot of work, okay? And couldn't be more thrilled with the progress that we're making.

But with the transformation journey we got going on with now the 4 strategic alternatives and COVID-19, look, we just don't think it's the right timing to comment on that.

Paul N. Saleh - *DXC Technology Company - Executive VP & CFO*

Ashwin, what I would add is that we're just really, as we mentioned all along, we're committed to an investment-grade credit profile. And our balance sheet, as you heard today, as in stronger. We have quite a bit of liquidity, and all these transactions are going to the 2 -- particularly the 2 that are been teed up already, will enhance our financial flexibility.

Longer term, again, we're going to work to maintain that solid financial position and the debt-to-EBITDA of 2x or less would be probably our targets.

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

Understood. The second question is about the \$550 million in cost savings. And I ask this because one of the prior versions of cost-cutting and optimization, the cuts went too fast, cut too deep, it hurt customers, hurt employees.

So when you say you're doing it faster, how are these cost-optimization initiatives different? How they smarter, what specific actions are you now taking? Any incremental color there?

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

Okay. So the key thing is this, right, is with the \$550 million in cost reductions, we're focused on the delayering. And what I said in the last call is that, look, what I've seen in this, okay, and it's key, right? Because you can't fix customers and take the cost out, right? You would hear some rumblings. But what I noticed in my detailed reviews that I did in the first 6 months, is we've got layers within DXC that are causing complexity and confusion. And I validated that with our customers. Almost, to using individual names to say, have you seen these folks show up on the account, okay?

And look, what I want to do is I want to make sure, and this is what we're doing, is that our detailed folks that are doing the work have a direct line to our customers and our account teams. And that's what we're doing. We're cleaning that up. And so I'm very proud about the work we've done. I'm also very proud about how we've simplified the organization because that's incredibly important.

The second thing I would say is this, we're being very transparent with our people, okay? I do monthly town halls with our people. We talk about it. I've talked about what we're doing, where we're going. And the specific words are we want our people to be making customer impact.

So I would say 3 things. One, the delayering is key. Two, is customer impact, right? If you're not making customer impact, then I want to understand what we're doing. And then the last thing is the fact that we're simplifying the organization, Ashwin, and I think that's basically the right way of looking at the \$550 million and why we're being successful this time around versus last.

Operator

And we will take our next question. This will come from Jason Kupferberg with Bank of America.

Jason Alan Kupferberg - *BofA Merrill Lynch, Research Division - MD in US Equity Research & Senior Analyst*

Good afternoon. I know you're targeting the book-to-bill of 1.0 in the second quarter. I was just curious if your expectation is that, that would be weighted towards GBS again, similarly to Q1? Or do you think it will be more balanced based on what you're seeing around near-term pipeline conversion?



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

No. So it definitely will not be focused on GBS. It will be much more balanced between GBS and GIS. Actually, when I look at them, they're both at 1x. So it should be very balanced. But I like -- remember what Paul said about the ITO pipeline. Those deals take a little bit longer to do. But when you get them like Sabre, they're meaningful. And that pipeline with our focus has grown significantly. We expect to harvest that.

Jason Alan Kupferberg - BofA Merrill Lynch, Research Division - MD in US Equity Research & Senior Analyst

Great. Okay. Well, that's good to hear. Maybe just sort of a follow-up along those lines. I know that pre-COVID, you guys have talked about investing \$100 million into the legacy IT outsourcing business. Can we just get an update on those investment plans? Is that all still on track, over what period of time? It sounds like maybe you're starting to see some fruits from that.

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

I mean, Jason, that's done, right? I mean, so when I said that basically, our focus on our customers is really starting to pay off, that investment is what's making that work, all right? So us getting closer to those customers, making sure that the folks on the account team have the tools, the training and then making sure that we also not only use that \$100 million on people, but also some of the automation, helps us basically move that forward.

The last thing, as I said on the last call, is that we are rewarding our folks, all right? In fact, it's this month. We're rewarding our folks that are doing the detailed work, all right? What I call layers one through 4, with pay increases. And again, I think that's incredibly important that the leadership of DXC recognize and rewards our folks for the work they're doing. And that's what's happening.

Jason Alan Kupferberg - BofA Merrill Lynch, Research Division - MD in US Equity Research & Senior Analyst

Congrats on the quarter.

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

Thanks, Jason.

Operator

And our next question will come from Darrin Peller with Wolfe Research.

Darrin David Peller - Wolfe Research, LLC - MD & Senior Analyst

All right. Just to hone in a little more on the bookings. Again, it's obviously great to see the 1.2 and then the 1.0 for next quarter. But when we think about the types of contracts you're having, obviously, 1/3 is new.

Can you give us a little bit more of a sense of the actual -- from a horizontal standpoint or a workflow standpoint? What exactly is the -- is resonating with your clients the most that you're offering that you're winning over others? And just maybe consider also thinking about both for this quarter, what's going on for next quarter and then the pipeline in a similar question.



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

Okay. So Darrin, back to the pipeline. The pipeline, like Paul said, we're seeing an increase in pipeline, obviously, across the board, most significant in ITO. Okay? The second thing is what I would say is the analytics and engineering capability that we have is significant. And I was actually a little bit surprised with how resilient it was.

So when we looked at our pre -- our COVID numbers, all right, pre actually sailing into this quarter, we thought that piece of the business was going to be impacted more, and it wasn't. In fact, they did very well, okay? The second thing is exactly what I said about the ITO and the cloud. What we're seeing is we are the engineers of engineers. What that means is as people move to the cloud, they need our help, and it's a balanced approach. My view of the cloud business right now is the easy stuff move to the public. That was the first 25%.

Now what we're dealing with is we're dealing with the critical applications. Those don't move to the cloud quick. That doesn't mean that the cloud does not play a pivotal role in it. It absolutely does. But it's definitely, right, a balanced approach, and that's what we're seeing. We're seeing some of that work move to the cloud, other of the work, they want it modernized. Our clients want the ITO, the IT estate modernized.

So Darrin, hopefully, that gives you a flavor. It's a balanced pipeline. We expect to deliver a balanced book-to-bill across GBS and GIS next quarter, but we do feel confident about that 1x.

Darrin David Peller - Wolfe Research, LLC - MD & Senior Analyst

Okay. I'm trying to get a sense of what your clients think that you have that really your competitors don't have, and that's why they're choosing you in those new logos, that 1/3 of the bookings that's new. Sounds like it is a lot of what you're saying around the analytics, though. And obviously, your capabilities on the cloud conversions as well.

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

Well, it's also -- look, it's the ability to migrate, right, the ITO work. Okay. I mean, this ITO business is, right, a favor for us because every single client we walk into, not everything is in the cloud, all right? So the net-net is us being able to deal with mainframes, us being able to deal with AS/400s, us being able to deal with that kind of stuff that not all of our competition has, Darrin. That's unique, okay? And then when we can show up, speaking the cloud for Google, for Microsoft, for VMware, for Amazon, that's huge, okay? So that's why I keep saying it's an and story.

Darrin David Peller - Wolfe Research, LLC - MD & Senior Analyst

Got it. That actually makes a lot of sense. Just -- and a quick follow-up is on -- when you talked about how you're done with really trying to fix the challenged accounts, what are the implications of that? I mean, it seemed like you were uncovering different issues. For the first couple of quarters. You came as CEO, Mike. But now that you're done, do you feel like you can really put that to rest. There's no other issues you're expecting to uncover and just look forward now.

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

No. I mean, look, Darrin, for as many times as I -- if you just think about basically a week of my time. Probably every day that goes by, I'm on a customer call, in some fashion. Could be a status call, could be me just checking in. And then, look, I'm constantly sending these customers e-mails about what's going on, all right? And they would tell me if stuff was not working. Because they've got every opportunity to, all right? And they certainly are engaged.

And in fact, they're more acquisitive than I thought about what other capability does DXC have, and us being able to get out there and tell that story is huge, okay? So again, like the position we're in, like the fact that the customers are engaged. What I would finish with is this, this new DXC

thing is not like a logo. It is what we believe in, okay? And part of that is around being customer-focused. So when I mentioned about that customer centricity mindset is built in, that's where we're going. So I do not expect us to go backwards, all right?

So again, that's the culture that we're dealing with.

Operator

And we will take our next question. This will come from Bryan Bergin with Cowen.

Jared Marshall Levine - *Cowen and Company, LLC, Research Division - Research Associate*

This is actually Jared Levine on for Bryan. Can you give us a quick update on how the workplace and mobility business performed in the quarter?

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

Paul, the details of the workplace mobility business, again, we saw the demand. We converted 2 very nice deals that were up over \$200 million in TCv in the quarter, one for a large electronics company, another one for a pharmaceutical company, where, Jerry (sic) [Jared], we showed up in their time of need. And that allowed us, right, to compete even better for that work because we delivered.

So Paul, would you add anything about the performance of the workplace business?

Paul N. Saleh - *DXC Technology Company - Executive VP & CFO*

Yes. On the revenue side in constant currency, I think it was down about a few points. Close to 4 points, 4%, more again, timing of some of the things in the first quarter in the COVID environment of what customers we're looking to do. So -- but overall, I think the pipeline also is pretty strong right now.

Jared Marshall Levine - *Cowen and Company, LLC, Research Division - Research Associate*

Okay. Great. And are there any other opportunistic sales within the portfolio being evaluated at the moment?

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

Jerry, listen, again, our focus is on those 4. The fact that we added another one, we've got a lot of work, and we're doing great at it. We certainly will always look to unlock value in our portfolio, especially as we continue to focus on the enterprise technology stack. So that's how I'd answer that question.

So listen -- yes, thanks, Jerry. What I'd like to do is I want to thank each and every one of you for joining the call. And I'd like to highlight that, look, our strategy to position DXC for growth has always been based on taking care of our customers and our people. This focus has allowed us to make good progress on our transformation journey in Q1, and we are confident that this momentum will continue in Q2.

So with that, I want to wish you and your families all the best. And operator, please close the call.

Operator

This concludes today's call. Thank you for your participation. You may now disconnect.



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