Sidoti & Company Spring 2018 Investor Conference
May 29, 2018

Peter Altabef, CEO

I want to thank everyone who is here in person as well as those listening on the simulcast. Those of you familiar with, there's a lovely 1937 song from Jerome Kern and Oscar Hammerstein and it's called The Folks Who Live on the Hill. And if you've never heard that song, I recommend it to you. I say that because while The Folks Who Live on the Hill is a pretty song, think of the Unisys team as the people from table 106. And so, if you get bored later in the day, come by table 106 and we can have a one-on-one conversation, the equivalent of The Folks Who Live on the Hill.

We have a few minutes to give you a brief overview of Unisys. Just by a show of hands, how many folks here have some familiarity with Unisys? Some yes, some no. So, I'll go pretty high level. Inder Singh, who is with me, as well as Dan Caine and Courtney Holben. Inder is our CFO. He's going to go a little deeper into the numbers. But again, there's a limit to what we can do in about 30 minutes. But we hope to pique your interest in the company.

The company has been around a while. Unisys dates back 145 years. Unisys was effectively founded in 1873 with the invention of the Remington Typewriter. That is what ultimately became Unisys. The Remington Typewriter was famous for the first commercially developed typewriter with a QWERTY keyboard. That was the beginning of a bunch of firsts for Unisys. Those of you who are familiar with the history of computing will remember the ENIAC, which was actually the first viable computer which was used in World War II to break enemy codes, followed by the UNIVAC, which was the first commercial computer.

So, where has Unisys come to? Well, moving beyond the disclosure, we've come to a really interesting place. So, the vision of the company is to enhance people's lives through secure, reliable advanced technology. It's an interesting vision. Most visions are aspirational. This one is not. This one is real. This is what we do every day. And we execute that vision through our mission statement, which is to provide high-performance, security-centric solutions for the largest businesses and governments on earth. Do we really do that? We really do.

So, those of you who might be familiar with financial transactions, because we're here in New York today, are familiar with The New York Clearing House, which is now simply called The Clearing House, which clears approximately $1 trillion of transactions a day. It's all done on Unisys systems. Those of you who file tax returns have filed tax returns that are processed by the IRS. Much of that work is done by Unisys systems. If you cross the border into the United States, 100% of all the people who come into the United States, land, sea or air, at least in a legal way are verified through systems that have been developed in large part by Unisys and the U.S. Federal Government. And the list kind of goes on and on.

About 48% of our revenue comes from the U.S. and Canada; about 52% is outside. So, we're slightly more than a majority of our revenues outside the U.S. And the way we go to market is by what we call sectors, and you can see the three sectors on this page government, commercial and financial services, but within those sectors in specific industries. And that's very important, because the way clients see you is not through a sector. Nobody says I'm in commercial sector. But they do say, I'm in the travel and transportation industry. So, we work with about 14 of the top 25 airlines. Actually, now I think it's 21 of the top 25 airlines in things such as passenger reservations, in things such as cargo, and they see themselves as in the travel and transportation industry.

So, that's the way we go to market. We go to market with industry expertise in the industries where we choose to play. And then, with that industry expertise, we really wrap three things. We wrap industry-specific solutions,

solutions that actually don't work for any industry other than that specific solution, and that's on purpose because that is to show the industry that we're working with, we care deeply enough and we know deeply enough about them that we actually created solutions that only work for their industry. That gets you a lot of credibility and qualifications.

The second thing we do is we take some more generic capabilities that work across industries and we tune them to be specific about the specific industry. And finally, the third thing we do is we put deep security into all of these offerings, okay. That's what you see on this page. I'll just take you through, as an example, one specific industry and how that all works. So, let's take as an example – we'll just pick one. Let's pick financial services. So, in financial services, you will find very specific industry-focused applications that are our proprietary applications or that are integrated with our proprietary applications.

Elevate is an omni-channel 360-degree system that we launched last year that does that. So do our core banking systems, so do several of our underlying fraud detection systems. We work with about 400 financial institutions around the world, and we do that with these very, very industry-specific applications. But we also provide to them things such as global workspace, which monitors and handles all of the endpoints that they have, whether that's a desktop, whether it's a laptop, whether it's an iPad or an iPhone or whether it's an Apple Watch, that communicates with their core systems.

So, global workspace is really taking care of all of the employees or associates of a company and the devices that communicate, whether it's a BYO device or whether it is a device owned by the company. We do that for millions of people around the world, including financial services. And then finally, underneath all of those is the security that we have, and we build in leading security into everything we do, whether it's Elevate, whether it's core banking, whether it's Digital Workspace.

Security is a hot topic, and there are probably – we're at table 106. There are probably about 95 people out there saying they're security folks. Unlikely they have been doing it as long or as well as we have. And that in part is a product of both the legacy of the company and the company's tradition of innovation. Why do I say legacy, because this company became a computing technology company in effectively the 1940s. And in the 1940s, the only thing you worked for was large governments or large organizations, the UNIVAC, the first commercial computer.

So, security in that old, if you will, mainframe era was absolutely integral to everything that happened. Companies born in the 1980s and the 1990s, especially the 1990s and the 2000s, where you don't have the security mindset in the first iteration of the Internet, didn't really have that. And they have spent billions and billions of dollars retrofitting security back into their stuff, trying to make the Internet more stable, trying to make their applications more secure.

We never had to do that, because our mentality, not just the stuff we invented in the 1940s, but all the stuff we've done since have been based with security built-in. As an example, ClearPath Forward, which is our operating system that runs things such as the IRS and Lloyds – a large part of Lloyds Bank's infrastructure, Banamex in Mexico, ClearPath Forward is the only operating system according to the NIST, which is the organization that measures this stuff, that has never been forcibly hacked. It's the only operating system in the world that has never had data forcibly extracted.

So, that's an example of the kind of security we have. Our Stealth product of cybersecurity and biometric security is the only product that has been certified to work on Amazon AWS, Microsoft Azure and has been certified by something called the common core to travel with top secret classified data in the 28 largest Western governments in the world. The only system is Stealth. So, security is a big deal to us.

I'll run through the next few slides and then let Inder take over. 2017, a part of a progression for us as the company has become more focused. You can see that in terms of client renewals. We renewed about 97% of our clients. Those of you familiar with Net Promoter Score, who understand the way that works for B2B, know that B2B companies have an average Net Promoter Score of about 22. IT companies in that category uphold an even more impressive score of 18, and I'm being somewhat facetious. 18 is not a great score. But our score is 43, which is more than twice the score of our industry peers, and that is leading to that kind of renewal rate. It's also leading to references and those references create opportunities for new business.

We launched or re-launched nine industry application products and a new version of suite of Stealth in the last 15 months, and we strengthened our, if you will, more leveraged transactions that we tweak to apply to each individual industry. Finally, we started to grow revenue again. That has been part of the turnaround at Unisys. Unisys has not been a revenue growth story for a while. We grew in the fourth quarter by 3.2% and we are forecasting growth for all of 2018 in the middle of our guidance range. That is the first time – assuming that we succeed with that middle of the guidance range, it will be the first time the company has grown revenue since the year 2003. So, it has been a long time coming.

And you might wonder, well, how's that going to happen? Why is that turnaround happening? Yeah, your customers are more satisfied, you have new products, but show me kind of the evidence of that. And this slide does that. So, total contract value in our industry is measured by the amount of revenue you expect when you sign a contract for the length of the contract. So, if you signed a contract that would give you $50 million over the three-year term of that contract, that's a $50 million contract. But if it's a five-year contract, it would be whatever revenue is under the contract in the five years. So, total contract revenue varies depending on the length of the contract, as well as the revenue per year.

Annual contract revenue, which is the second column, is the revenue you expect to get in the next 12 calendar months after you sign a contract. And in our business, it's not so straightforward as well if it's a five-year deal for $50 million, it's $10 million a year, because you often are implementing new systems, you're implementing new processes. And so, you don't necessarily actually get revenue or at least not full revenue for up to six to nine months. So, the annual contract value actually can be less than your average contract value. But we use annual because we really kind of want to know what revenue is coming on stream in the next 12 calendar months. And you can see that year-on-year, our TCV as a company went up 8% in total contract value.

Then, we have something called new business that went up 89%. So, what is new business? So, we divide our contracts or our business into four categories. Two of them, renewals and extensions, are working for existing clients, doing the same or similar things. An extension would be, it's a five-year contract, it's running out, we do the same work for another five years. That would be a renewal. An extension would be, well, we're doing that work in Australia, now let's do that work in Singapore as well. So, that would be an extension.

Really important in our business to have renewals and extensions, but where you have the most dynamism is in new business. So, new business has two categories. One category is new clients, clients that you haven't served before or you haven't served for years. The other is what we call new scope. So, that is where you have an existing client, but you're selling them something entirely different than what you've done for them before. So, that would be – as an example, we might have a financial services client that is using ClearPath Forward, and then all of a sudden we sell them Stealth. That selling of Stealth would be new scope.

So, you can see total contract value for the new stuff, new clients, new scope, went up 89% year-on-year for the full-year. For annual contract value, we had a 22% growth in annual contract value for the company and a 93% growth in new business. And then, our pipeline, both total company and new business, up between 54% and 66%. And there you can see specifically our security pipeline at almost $700 million and our industry application pipeline at over $700 million. So, substantial opportunities for this company going forward.

Another kind of sign of the resurgence of Unisys is in our backlog. Our backlog is the amount of revenue under contract that we have not yet performed. So, if you have a five-year contract and you've already done one year, you have four years of backlog left. Our backlog as of the end of 2017 increased 10.3% over the backlog at the end of 2016. That was the first time we had had a 10% increase in year-end backlog since the year 2000. So, substantial stuff underway at Unisys.

If we have to talk about where the company is and what we really focus on in just a couple of slides or really even a couple of columns, this is it. We're very focused on very specific services. We are not all things to all people. We build security into everything we do, and we have this idea of an integrated solution by industry, where yes, we do some leveraged stuff that we make very specific for that industry, but we also add stuff that only applies to that industry. We think these three taken together distinguish us from a very crowded field. Will we win every single engagement? No, but we don't have to.

We are a $2.8 billion company in a field, if you include both software and IT, of about $1.4 trillion. So, we can do just fine with a little distinction, and we believe we have that. Finally, we started last fall to really show our three to five-year business model. The company had not previously done this. We wanted to give folks a sense of where the company we believe it was heading, what we thought was achievable and do that in more than simply providing guidance for the next calendar year.

Inder is going to go over this in more detail. But as you can see, befitting a company that has now moved to the positive in some of these metrics, these look like relatively modest goals, right. Service – overall company growth, 2% to 4%; non-GAAP operating margin in the 9% to 12%. Inder is going to talk about that a little bit. These goals are very significant for us. When you look at our EBITDA, you look at our valuations, you look at our metrics, performing at this level is a big deal for this company and we believe is a significant change.

With that, I'm going to hand it over to Inder.

Inder Singh, CFO

Thank you very much, Peter. I wanted to thank all of you for being here today and thanks for those who are listening in on the webcast as well. I'm going to use a couple of slides to highlight some of the things that Peter mentioned, but also some of the progress we've made at the financial dimension, so that you have some context for that as well. So, I think Peter touched on some of these points already. But from a company standpoint, we're focused on three things from a financial guidance standpoint that we've been telling the Street, which is around revenue growth, improving profitability, driving up cash flow.

In addition, we've been very focused on, what I'll say, is actively managing our pension obligations, as well as our capital structure. And we've made progress on many of these dimensions. As you see on here, behind our views around revenue, as Peter mentioned, is that we have launched these industry-specific application products and services on top of the leveraged services that we also offer to these industries, and they serve to differentiate us in the marketplace. We think that those two things together with the new products, new solutions that we have just launched over the last year frankly position us for revenue growth.

As far as improving profitability, a couple of years ago in 2015, our operating margins were in the 5.8% range. If you think about what Peter mentioned as 9% to 12%, that's a nice lift from where we were just a short time ago. We do think that we're on our way to that. I'll show you in a minute how that progress is coming along. But we need to maintain from here really a continuous focus on increasing our profitability year after year after year.

Of course, as revenue grows, that will also help unlock operating leverage, as you all know. But we do believe that the mix of products and the steps that we've taken on the cost side position us well for further expansion in profitability. And then, cash flow for all the obvious reasons for a company our size with some of the investment needs that we have to grow the company, as well as some of the obligations that we have on the pension side, has been a focus for us for the last couple of years, and we've made steady progress, we believe, on that dimension as well.

We did, as you saw when we reported last year, begin to make some pretty decent, I would say, solid progress on managing our pension obligations as well. So, we think we're firing on all of these cylinders. We do believe that that progress has to continue. There's more work to do for sure, but these are the initiatives that we've been focused on as a company and the initiatives that actually help drive a lot of the investment choices we make, as well as how we calibrate success against these metrics.

So, how have the last two years looked? Well, this company began to give guidance at the beginning of 2016 after several years of not having actually provided financial guidance to Wall Street. And then, we gave guidance again in 2017. As you'll see on the slide, both years, we either met or exceeded the guidance that we gave. So, for revenue for 2017, as this shows, we guided for a range of $2.65 billion to $2.75 billion, and we came in towards the higher end of that at $2.74 billion.

For margins, we had given guidance of 7.25% to 8.25%, and we came in at 8.5%. Again, that 8.5% compares to the 5.8% that I mentioned previously. And then, cash flow, we had guided to a range of $130 million to $170 million, and we were in at $199 million. Would love to have seen that at $200 million. The year before, we had done more than $200 million. So, we're glad to see the progress, but also frankly the consistency that the cash flow has demonstrated.

And then last, but certainly not least on this page, we were successful in raising capital last year and recapitalizing the company from a capital structure standpoint, and at the same time, bringing down the projected pension cash obligations that we have over the next 10 years. So, we saw the GAAP deficit actually come down by $390 million last year, and we raised $440 million of bonds in the market as you probably know. We also saw the pension cash requirements come down by $350 million last year. These are projections for the next 10 years of course in terms of what we think we'll have to invest.

And then, we also extended access to an ABL, which is undrawn, but it gives us more capital, should we need it as the company grows to fund and fuel the growth of the company. So, all-in, the pension deficit, which was $2.17 billion at the end of 2016 was $1.78 billion at the end of 2017. So, after two years of giving guidance and either meeting or beating the numbers that we provided, we gave guidance for this year as well. So, for 2018, we began the year – and this is guidance that we provided on our earnings call as of February 8. We guided for revenue to be in a range of $2.7 billion to $2.825 billion. And as Peter noted, the higher end of that range – the upper end of that range would constitute growth. In fact, even the midpoint of that range would point towards growth.

GAAP revenue will be slightly higher than that, because we benefit from the adoption of ASC 606, which is the new rev rec requirement for all companies, and in our case, it actually helps us. From a margin and a profitability standpoint, we guided for non-GAAP operating profit to be in the 7.75% to 8.75%. Again, GAAP operating profit will be even higher than that at 9.5% to 10.5%. But we're trying to compare apples-to-apples, so we're trying to give you guidance that is consistent with the way we've measured 2017 and 2016. And adjusted EBITDA margin expands in line with operating margin.

So, the guidance that we've given for 2018, we think, is another good forward step towards this three to five-year model that Peter talked about. That model assumes that we grow in the 2% to 4% range. It depends on which industry analyst you follow and look at, but the Gartners and the IDCs and those companies of the world are the ones that measure the market, and they believe the market is growing somewhere in the low single-digit range, perhaps 2-ish-percent. So, 2% to 4% would be pretty good growth for us to achieve, because we do think we're positioned well in some of the higher growth segments of that market.

We do expect to have non-GAAP operating profit margin expand to the 9% to 12% range, as Peter noted, with Services contributing to that, as well as Technology. Technology for us is a highly profitable business. It has become much more of a software business than it used to be even five or seven years ago. A decade ago, perhaps it was a mainframe business. So, that has gone through a tremendous transformation to the point where the basket of portfolio elements we have in that Technology business, we think, position it for either stable or growth in that Technology segment going forward.

One thing that investors ask us quite often is because of the importance of your Technology segment, is it volatile? Is it something that you can predict? And what we wanted to show you was based on publicly available information, you can actually do this chart yourselves as well. As a percent of total year revenue, this shows you how each quarter has tracked for the last three years. And as you can see, it’s not as volatile in the sense that the band in which any given quarter is has about a 2-point or maybe 3-point spread for Q1, Q2 and Q3. And then, yes, Q4 is a little wider. It is our fourth quarter, our fiscal year-end, and therefore, just as for every other tech company, it can be a little less predictable.

And frankly, this Tech business, which had been declining five years ago, for the last two years has stabilized and shown growth. So, I’m not surprised to see that we have some strength showing up in some of those fourth quarters. So, to answer the question straight on in terms of can it be volatile, sure, there can be an outlier. And you can see a red dot on there that shows you one particular quarter in that three-year period that was outside of this envelope. And we had three particular renewals, large tech clients that all decided to renew in that quarter. And so, that quarter ended at being 33% of the full-year.

But for the most part, it’s a couple of point range and we would expect 2018 to not deviate from that. So, if we think about 2018, the guidance we provided was that it would be a 40% first half, 60% second half year. And if you try to sort of fit that into this graph, it would suggest a couple of quarters, two or three quarters in fact in the 20% range, if you will, 20%, 20%, 20% and then perhaps 40%. So, again, we’re looking for a strong fourth quarter.

Why? Because we have pretty good line of sight to the exact clients that expect to renew by month, by a quarter. They may not always choose to do exactly when we expect them to renew. They could do it a little earlier, perhaps a little later, but our plan for the year is established based on client level visibility. So, it’s pretty good visibility to this line of business. And again, I wanted to take away from the notion that it’s volatile. That said, our Q1 tends to be among one of the lower quarters, as you can see, as this chart will demonstrate. So, no surprise that you have a strong Q4, Q1 is a little bit lower, the sales team gets back into gear and the year progresses from there.

One other thing I want to point out, which is not necessarily relevant on this chart, but is relevant to our story, and when we guided for this year, we did indicate that a year ago in Q1, we had a particularly profitable transaction that lifted our operating margins in Q1 of 2017. So, when we think about Q1 of 2018, we wanted to remind you of what we said on earnings, which is that, that faces a tough margin compare. That one particular transaction accounted for just north of 200 basis points of operating profit contributions in Q1 of 2017.

So, that said, we look for this year to unfold in much the same way as our other years have. And then, I know – and I’m sensitive to time here. We are actively managing our pension obligations. But I would also remind you we have tax assets and we are trying to make sure that we are optimizing our position from a capital structure and a cash flow standpoint both as it relates to being proactive and thoughtful about managing our pension obligations with the right asset mix and the right investments to drive down the deficit over time, and at the same time, we have $1.55 billion of tax assets that we intend to make sure that we align and utilize to the benefit of our investors and the ability for us to invest in our business.

Those are the slides that I had. We can wrap it here if it’s okay, and if there are any questions, we can maybe field a question or two. Thank you.