Niels Christensen, IRO

Thank you, operator. Good afternoon everyone, and thank you for joining us.

Earlier today, Unisys released its fourth quarter and full year 2012 financial results. With us this afternoon to discuss our results are Ed Coleman, our CEO, and Janet Haugen, our CFO. Before we begin, I want to cover a few housekeeping details.

First, today’s conference call and the Q&A session are being webcast via the Unisys Investor Website.

Second, you can find the earnings press release and the presentation slides that we will be using this afternoon to guide our discussion on our Investor Website. These materials are available for viewing as well as downloading and printing.

Third, today’s presentation, which is complementary to the earnings press release, includes some non-GAAP financial measures. These have been provided in an effort to give investors additional information. The non-GAAP measures have been reconciled to the related GAAP measures and we have provided reconciliation charts at the end of the presentation.

Finally, I’d like to remind you that all forward-looking statements made during this conference call are subject to various risks and uncertainties that could cause actual results to differ materially from expectations. These factors are discussed more fully in the earnings release and in the company’s SEC filings. Copies of these SEC reports are available from the SEC and from the Unisys Investor Website.

Now I’d like to turn the call over to Ed.

Ed Coleman, Chairman & CEO

Thanks, Niels. Hello, everyone, and thank you for joining us today to discuss our fourth-quarter and full-year 2012 financial results.

Please turn to Page 4 of the presentation to begin our discussion.

We completed another profitable year for Unisys in 2012 with a good fourth quarter.

Led by a strong performance in our technology business, we reported diluted earnings per share of $1.67. On a non-GAAP basis excluding pension expense and debt reduction charges, our fourth-quarter diluted EPS rose to $2.27 from $2.22 in the fourth quarter of 2011.

Our fourth-quarter results closed out a year of continued progress for Unisys in 2012. In an uncertain IT spending environment, we increased our profitability and generated significant cash flow.

For the full year of 2012 we reported diluted earnings per share of $2.84, up from $2.71 in 2011. Our non-GAAP diluted EPS rose to $5.50 from $5.18 in 2011.

Cash flow was also strong in 2012. Before pension contributions, we generated free cash flow of $330 million in 2012, up from $266 million in 2011.

Turning to Page 5 … in 2012, we made continued progress toward our three-year financial goals through 2013.

Against our 2013 goal of increasing our pretax profit to $350 million excluding pension expense, we exceeded that goal in 2012.

We also met our debt reduction goal more than a year ahead of schedule.

We have not yet hit our services operating margin objective of 8-10 percent consistently and predictably. To do so, we must couple revenue growth with continued work to identify ways to operate more efficiently.

Revenue growth continues to be our biggest challenge, with mixed results in 2012.

In our technology business, we exceeded the target of maintaining flat revenue in 2012, growing revenue 3 percent with the benefit of some earlier than expected sales of ClearPath as customers continue to respond positively to recent innovations in our flagship technology platform. Notably, we have now maintained or grown ClearPath revenue in each of the past three years. However, in our services business, we did not achieve our revenue growth targets for systems integration and IT outsourcing due to a challenging IT services market and softness in our U.S. Federal business.

Turning to Page 6 … as we enter 2013, we are taking steps to further improve our performance.
Our goal remains to become a company known for financial strength, where the quality of our services and solutions provides ongoing differentiation and where we are an acknowledged industry leader in our four areas of strength – security; data center transformation and outsourcing (which includes our server business); end user outsourcing and support services; and application modernization and outsourcing.

In recent years we have narrowed our focus to concentrate more effectively on select, target markets. We exited several businesses and changed our business model in certain countries.

In 2013 and beyond, we plan to build on our current geographic and business footprint. To do so, we are developing enhanced and new solutions and are building new sales channels in order to win new customers.

To drive growth, we are making investments to enhance our current solutions to take greater advantage of disruptive industry trends such as cloud, consumerization of IT and mobility, cybersecurity, big data and smart computing, social computing, and IT appliances.

Moving to Page 7 … new solution investments include what we are calling ClearPath Forward and follow-on systems. We are building on our leadership in providing mainframe-class computing functionality and performance on industry-standard Intel Xeon-based platforms to allow customers to add Windows and Linux workloads to their Intel-based ClearPath systems, and provide these new workloads with the mission-critical performance, security, reliability and scalability that they’ve come to expect from ClearPath.

Another investment is in developing new uses for our Stealth Solution Suite of cybersecurity products. We see exciting growth opportunities for Stealth, which we believe is unique in the market in its ability to cloak data, applications and users within a network or data center to help organizations deal with increasingly sophisticated cyber threats. In 2012, Stealth was named by Computer Reseller News as one of the hot products at the Interop technology conference.

Also, we continue to enhance our data center and end user outsourcing services, which have been recognized with placement in the Leaders quadrant of the Gartner Magic Quadrant for help desk services.

To complement and expand our IT outsourcing services, we are investing in application management services, where we see the opportunity to help organizations deal with the challenges of managing their applications in an increasingly decentralized, mobile and cloud-based computing environment.

All of our offerings are in support of our commitment to providing consistently high levels of service quality and customer satisfaction.

Further supporting our growth objectives, we have implemented an improved marketing platform for driving sales campaigns for our key offerings in support of our direct sales force. Following successful test drives of the platform in 2012, we are ready to leverage it more strongly in 2013 and beyond.

Additionally, we are building a reseller channel to reach new customers and grow our revenue. Currently, less than 5 percent of our revenue comes through resellers and distributors, which is quite low relative to other companies in the IT industry. Establishing a strong Unisys reseller channel will allow us to address a larger portion of the IT market.

In 2012 we made a good start in building a reseller channel for Stealth. As this effort progresses and we demonstrate success with the channel, we intend to add other Unisys products to the reseller channel program.

In closing, 2012 was another year of significant profitability and free cash flow generation.

Building on this progress as well as our much stronger financial condition and improved customer satisfaction, we are focused on driving profitable topline growth.

We look forward to reporting on our continued progress in the year ahead.

Thanks for joining us today. Now, here’s Janet to take you through our results in more detail, and then we will be happy to take your questions.

**Janet Haugen, CFO**

Thanks, Ed. Hello, everyone.

In my comments today, I will be referring to certain GAAP and non-GAAP comparisons throughout my remarks. For the fourth quarter comparisons, the non-GAAP results exclude pension expense and debt reduction charges. For the full year comparisons, non-GAAP references exclude pension expense and debt reduction charges in both years as well as a charge related to a Brazilian non-income tax case in the second quarter of 2011.

Now let me start with our overall fourth quarter and full year 2012 financial results. Please turn to Page 9.

At the top line, we reported revenue of $979 million in the quarter, which was down 1 percent year-over-year. Currency had a 1 percentage point negative impact so, on a constant currency basis, revenue was flat.

For the full year revenue of $3.7 billion was down 4 percent; down 1 percent on a constant currency basis.

Based on today’s rates, we anticipate currency to have about a 1 percentage-point negative impact on revenue in the first quarter of 2013 compared to the first quarter of 2012.
We reported an operating profit of $114.6 million for the fourth quarter of 2012. Our gross profit margin improved 80 basis points to 29.2 percent. Operating expenses rose in the fourth quarter of 2012 compared to the year ago quarter as both SG&A and R&D increased. This increase was largely attributable to higher pension expense and investments in growth programs.

For the full year 2012, on lower revenue, our operating profit of $319.2 million was down 2 percent versus 2011. However, the operating margin improved to 8.6 percent from 8.4 percent on higher gross profit margins and lower operating expenses. Higher research and development funding for the full year was more than offset by lower SG&A.

Interest expense in the fourth quarter of 2012 decreased by over 75 percent from $11.4 million in the fourth quarter of 2011 to $2.5 million reflecting the impact of our debt reductions. Interest expense for the full year 2012 was $28 million or 56 percent lower than 2011. As a result of the debt reductions and the refinancing in the third quarter of 2012, we have reduced annual interest expense from about $102 million in 2010 to approximately $10 million going forward. The fourth quarter of 2012 represented the first quarter at this new run rate.

For the full year 2012, we reported other expense of $37.6 million versus $55.5 million during 2011. Debt reduction charges of $85 million in 2011 were $55 million higher than in 2012 but the company had a $25 million swing from foreign exchange gains of $17 million in 2011 to foreign exchange losses of $8 million in 2012.

Our fourth quarter 2012 pension expense increased to $31.5 million from $8.1 million in the fourth quarter of 2011. We reported $108.2 million in pension expense in 2012, compared with pension expense of $34.3 million in 2011.

For the fourth quarter of 2012, pre-tax income was $109.4 million compared to $111.3 million in the fourth quarter of 2011. Our non-GAAP pre-tax income for the fourth quarter was $140.9 million in 2012 compared to $127.0 million in 2011.

Pre-tax income in 2012 was $254.1 million compared to $206.0 million in 2011. Our non-GAAP pre-tax income was $392.9 million in 2012 compared to $339.0 million in 2011. Achieving our revenue growth goals and improving our services operating margins are both important factors in our ability to sustain and grow that level of profitability on a consistent and predictable basis in the future.

At the tax line, we had a $20.5 million tax provision in the quarter compared with a $12.4 million tax provision in the year ago quarter. As I have said previously, our tax provision continues to be highly variable from quarter to quarter depending on the geographic distribution of our income.

We reported net income of $81.8 million in the quarter, versus net income of $94.3 million in the year ago quarter. The non-GAAP net income rose to $112.2 million for the fourth quarter 2012 from $108.6 million in the fourth quarter of last year.

For 2012, net income increased to $129.4 million from $120.5 million for 2011. Non-GAAP net income was $265.4 million in 2012 compared to $242.6 million in 2011.

Our fourth quarter 2012 diluted earnings per common share was $1.67 per share compared to $1.94 in the year ago quarter. For 2012, diluted earnings per common share rose to $2.84 per share from $2.71 per share a year ago.

Our fourth quarter non-GAAP diluted EPS improved to $2.27 per share compared to $2.22 in the fourth quarter of 2011. And our 2012 non-GAAP diluted EPS was $5.50 per share compared to $5.18 in 2011.

Please turn to Page 10 for some context on the progress we have made in recent years in terms of strengthening our operating profitability. This chart shows a view of our trailing twelve month operating profit. Our operating profitability, excluding the impact of pension income/expense, continued to trend up as a result of our improving business mix and sustained cost control efforts. We still have some more work to do to achieve consistent and predictable profitability each quarter.

Moving to our fourth-quarter and full year revenue please turn to Page 11. Services revenue, which represented 82 percent of our revenue in the fourth quarter of 2012, declined 4 percent year-over-year. Currency had a 1 percentage point negative impact in the quarter so services revenue declined 3 percent on a constant currency basis. Services revenue declined 5 percent for the full year in 2012; 2 percent on a constant currency basis.

Fourth quarter Technology revenue accounted for 18 percent of our total revenue and rose 16 percent year-over-year on a reported basis; up 17 percent on a constant currency basis. Technology revenue rose 3 percent for the full year 2012; and was up 6 percent on a constant currency basis.

On Page 12, you can see services revenue and margins.

On our last earnings call, we provided the amount of opening services backlog for the fourth quarter. We also provided the range that opening backlog has represented of a given quarter’s services revenue over the previous six quarters. The fourth quarter services revenue of $806 million was at the high end of the range implied by the amount of revenue in opening backlog at the start of the quarter. Our sell-and-bill business in the quarter returned to levels more consistent with recent quarters after the decrease noted in Q3 2012.

Systems integration revenue for the fourth quarter of 2012 declined 4 percent compared to the year ago quarter. For the full year, systems integration revenue was down 7 percent due largely to declines in our U.S. Federal business.

Within Outsourcing, ITO revenue was down 4 percent versus the fourth quarter of 2011. For the full year, our ITO revenue was down 2 percent.

Our goal remains to grow our systems integration and ITO businesses at market rates.

In the fourth quarter of 2012, services gross profit margin increased 20 basis points year-over-year to 20.2 percent from 20.0 percent.
Our services operating margin declined by 100 basis points year-over-year to 6.6 percent as higher operating expenses associated with increased growth investments offset the improved gross profit.

For the full year 2012, we reported a flat services gross margin of 20.0 percent and a 50 basis point decrease in operating margins to 6.4 percent.

Moving on to Technology revenue and margins on Page 13, Enterprise Class Software and Server revenue in the fourth quarter was up 13 percent year-over-year while sales of Other Technology, all of which is third party product, increased by $4.6 million. Our annual goal is to maintain stable Technology revenue, most importantly in our flagship ClearPath platform which is the largest component of our Enterprise Software and Server business. During 2012, our technology revenue was up 3 percent driven by increased ClearPath revenue. We did benefit from some earlier than expected ClearPath revenue in the fourth quarter. As we have said previously, this business is best measured on an annual basis and we are pleased that we have been able to maintain or grow our ClearPath revenue in each of the past three years.

As a result of the higher proportion of ClearPath sales within the Technology segment, we reported a technology gross margin of 68.1 percent in the fourth quarter, up 220 basis points from the prior year. Our technology operating margin rose to 43.9 percent from 37.7 percent in the fourth quarter of 2011. Our full year gross and operating margins in this segment improved to 63.9 percent and 33.1 percent, respectively, up significantly from 2011.

Page 14 shows our fourth-quarter and full year revenue by geography and industry.

North American revenue declined 5 percent in the fourth quarter. Excluding the U.S. Federal business, our North American revenue was down 3 percent. In 2012, our North American revenue represented 41 percent of our total revenue and declined 7 percent. Revenue from the U.S. Federal government represented 14 percent of total Unisys revenue. Excluding the U.S. Federal Government business, our North American revenue rose by 2 percent in 2012 reflecting higher services and technology revenue.

In the fourth quarter, international revenue rose 6 percent and was up 7 percent on a constant currency basis. For the full year, international revenue was down 1 percent but up 4 percent on a constant currency basis.

Revenue in our European region was up 9 percent in the fourth quarter on an as reported basis and rose 10 percent in constant currency. This was due to a strong Technology performance in the quarter. For the full year, European revenue, which represented 33 percent of our total revenue for the year, was down 2 percent but up 3 percent on a constant currency basis again largely attributable to the strength of our Technology business.

The fourth quarter revenue from our Asia Pacific Region declined 3 percent as reported and 5 percent on a constant currency basis. 2012 revenue in the region was up 8 percent as reported and 9 percent on a constant currency basis reflecting higher services and technology revenue.

Fourth quarter revenue declined 8 percent in our Latin America region on a reported basis but was up slightly on a constant currency basis. For the full year, revenue was down 13 percent; 3 percent on a constant currency basis.

From an industry perspective, Public Sector remained our largest single industry revenue source accounting for 41 percent of 2012 revenue. The 5 percent year-over-year decline in the fourth quarter and the 9 percent annual decline in Public Sector revenue was largely driven by the decrease in our U.S. Federal government revenue. Excluding our U.S. Federal government business, Public Sector revenue declined 3 percent in the fourth quarter, and was down 2 percent for the full year.

Revenue from Commercial industry customers represented 35 percent of our 2012 revenue while the Financial Sector was 24 percent. Our Commercial revenue declined 11 percent in the quarter and was down 2 percent for the full year, while revenue from our Financial Services customers rose 26 percent in the quarter and was up 2 percent for the full year.

Page 15 provides more detail on our U.S. Federal government revenue over the past eight quarters.

In the fourth quarter of 2012, revenue from Civilian agencies and revenue from Defense and Intelligence agencies, each represented 38 percent of our revenue base within the U.S. Federal government.

Revenue from Homeland Security agencies represented the remaining 24 percent of our overall U.S. Federal government revenue.

Compared to the year-ago quarter, our overall U.S. Federal revenue declined $14 million or approximately 9 percent to $148 million. This decline resulted from lower funding on certain services contracts, as well as the loss of some services contracts in prior quarters and lower technology revenue. Sequentially however, we saw a 15 percent increase in revenue due primarily to higher technology revenue.

For the full year, Civilian agencies represented 47 percent of our U.S. Federal government revenue while Defense and Intelligence agencies together accounted for 28 percent and Homeland Security represented 25 percent.

We ended the fourth quarter of 2012 with about $332 million of U.S. Federal services backlog, which was down 8 percent versus the fourth quarter of 2011 but up 1 percent from the third quarter of 2012 as we saw some modest sequential improvement in our services order closure during the final quarter of 2012.

For some comments on services orders, please turn to Page 16.

In the fourth quarter, our services orders declined year-over-year but increased sequentially.

From a geographic perspective, we saw year-over-year services order growth in our Asia Pacific region during the fourth quarter. Orders in our other regions declined in comparison to the fourth quarter of 2011.
We ended the fourth quarter with $5.1 billion in services backlog, which was down 8 percent from December 31, 2011 but flat with the last two quarters. The year-over-year decline primarily reflected reductions in IT outsourcing and business process outsourcing backlog. Currency had about a 1 percentage point positive impact on the year-over-year comparison.

Approximately $640 million of the December 31, 2012 services backlog is anticipated to convert into first quarter 2013 services revenue. During seven of the past eight quarters, we have noted an increase in the level of sell-and-bill business as a percentage of total quarterly services revenue. During that period, the amount of revenue in backlog at the start of the quarter has ranged between 85 and 90 percent of our quarterly services revenue for the full quarter and the sell-and-bill revenue has accounted for the remainder.

At the start of 2012 we reported services backlog of $5.5 billion. Approximately 70 percent of our full year 2012 services revenue was in backlog at January 1, 2012.

We start 2013 with approximately $2.1 billion of services backlog which is expected to convert into 2013 services revenue.

Historically, between 60 and 70 percent of our full year services revenue is in backlog at the start of the year.

Moving to cash, please turn to Page 17 for an overview of our cash flow performance in the quarter.

We generated $153.9 million of cash from operations in the fourth quarter of 2012 compared to $159.5 million in the year-ago quarter. The company generated $261.3 million in cash from operations during 2012 versus $317.2 million in 2011.

We contributed $26.4 million in cash to our defined benefit pension plans in the fourth quarter of 2012 versus $19.1 million in the fourth quarter of 2011. During 2012, we contributed $201.5 million compared to $82.7 million in 2011. The pension funding contributions are reflected in cash flow from operations.

Capital expenditures were $35.9 million in the fourth quarter of 2012, versus $33.3 million in the fourth quarter of 2011. Capital expenditures for the full year were $132.6 million versus $134.4 million in 2011. We anticipate full year capital expenditures during 2013 to be in the range of $150 to $175 million.

We generated free cash flow of $118.0 million in the fourth quarter of 2012 versus free cash flow generation of $126.2 million for the same period last year. Our free cash flow before the pension cash contributions was $144.4 million for the fourth quarter of 2012 versus $145.3 million in the fourth quarter of 2011. Free cash flow before the pension cash contributions was $330.2 million during 2012 versus $265.5 million in 2011.

Depreciation and amortization was $46.2 million in the quarter, compared to $44.9 million in the fourth quarter of 2011. Full year depreciation and amortization was $174.6 million in 2012 versus $194.8 million in 2011. For 2013, we expect full year depreciation and amortization to be in the range of $150 to $175 million.

Excluding the impact of the debt reduction charges and pension expense, Unisys generated adjusted EBITDA of $186.6 million for the fourth quarter of 2012 versus $182.7 million in the fourth quarter of 2011 and $583.8 million for the full year 2012 versus $589.7 million in 2011.

Our debt balance was $210 million at December 31, 2012 and is primarily comprised of our 6.25 percent senior notes due in 2017 which were issued in the third quarter. Our debt was down $149 million year-over-year as a result of a series of debt reduction actions during 2012.

Our cash balance was $656 million at December 31, 2012 compared to $715 million at December 31, 2011. Despite the $149 million net reduction in debt during 2012 and $119 million in incremental pension funding our cash balance was only $59 million below the level reported a year ago.

You can see the progress we have made in the reduction in leverage over the past four years by turning to Page 18.

As we announced in the fourth quarter of 2012, our Board of Directors authorized the purchase of up to $50 million of the company’s common or preferred stock through December 2014. As of today, no purchases have been made under this authorization.

Turning to Page 19, I would now like to provide an update on our worldwide pension plans, funding position, and expected cash funding levels.

At the end of each year, we determine the discount rate that will be used to calculate the present value of our pension liabilities under U.S. GAAP.

The discount rate used to present value the U.S. pension obligation at December 31, 2012 was 4.01 percent down from the December 31, 2011 discount rate of 4.96 percent reflective of the change in interest rates from last year end. This lower discount rate has increased the present value of our U.S. pension plan liabilities at year-end 2012.

A change of 25 basis points in the U.S. discount rate causes an approximate $140 million change in the pension obligation.

Taking into account the net effect of the increase in pension liabilities and the increase in pension assets driven by good market performance, we ended 2012 in an underfunded position in our U.S. pension plans of $1.9 billion which was approximately $265 million above the level at year-end 2011.

The weighted average discount rate used to present value the international pension obligations at December 31, 2012 was 3.92 percent. This rate represented a 73 basis point decrease from the discount rate at December 31, 2011. As is the case with the U.S. plan, the lower discount rate increased the present value of our international pension plan liabilities at year-end 2012.

The underfunded position of the international plans at December 31, 2012 increased by approximately $105 million from the prior year-end. For the major international plans, a change of 25 basis points in the discount rate causes an approximate $122 million change in the pension obligation.
From a U.S. GAAP expense perspective, we expect approximately $93 million in pension expense in 2013, compared with pension expense of about $108 million in 2012.

Please turn to Page 20 for a discussion of our pension funding. From a cash funding perspective, we contributed $202 million of cash in 2012 into our pension plans $111 million into the U.S. qualified plan and $91 million into the other plans.

We expect to contribute approximately $34 million in 2013 into the U.S. plan and anticipate contributing another $112 million into our other plans during 2013 for total 2013 contributions of approximately $146 million.

For 2014, our cash funding estimate for our U.S. qualified defined benefit pension plan is approximately $95 million with an expected contribution of $150 million for 2015. The estimated contributions for 2016 through 2017 are approximately $145 million and $160 million respectively. Beyond 2017, we estimate that these contributions will decline from this level.

These funding estimates for our U.S. qualified defined benefit pension plan are based on current expected asset returns and the funding discount rates used for the U.S. qualified defined benefit plan which have been updated to reflect the published IRS discount rates. The future funding requirements are likely to change based on, among other items, market conditions and future published IRS discount rates.

Also on page 20, we have shown our current estimates for future contributions to international plans. These will be based on local funding regulations and agreements and are likely to change in 2014 and beyond based on a number of factors including market conditions, changes in discount rates and changes in currency rates.

As we have mentioned previously, it is important to note that the discount rates for funding and GAAP purposes are derived on different bases.

In closing, 2012 was the fourth consecutive year of profitability and positive free cash flow generation for the company.

We exited 2012 having achieved our debt reduction goal and significantly reduced our interest obligation.

We exceeded our 2013 goal of increasing pretax profit to $350 million excluding pension expense.

As we move through 2013, we will remain focused on driving toward the financial goals of revenue growth and operating profitability that Ed discussed earlier.

Thank you for your time.