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# Unisys Corp. (UIS)

Q2 2022 Earnings Call

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## MANAGEMENT DISCUSSION SECTION

**Operator:** Good day and welcome to the Unisys Corporation Second Quarter 2022 Earnings Conference Call. All participants will be in a listen-only mode. [Operator Instructions] After today's presentation, there will be an opportunity to ask questions. [Operator Instructions] Please note this event is being recorded.

I'd now like to turn the conference over to Courtney Holben, Vice President, Investor Relations. Please go ahead.

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**Courtney Holben**

*Vice President-Investor Relations, Unisys Corp.*

Thank you, operator. Good morning everyone. This is Courtney Holben, Vice President of Investor Relations. Thank you for joining us. Yesterday afternoon, Unisys released its second quarter 2022 financial results. I'm joined this morning to discuss those results by Peter Altabef, our Chair and CEO, Deb McCann, our CFO and Mike Thomson, who will participate in the Q&A session in his new role as COO.

Before we begin, I'd like to cover a few 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 morning to guide our discussion as well as other information relating to our second quarter performance on our investor website which we encourage you to visit.

Third, today's presentation which is complementary to the earnings press release includes some non-GAAP financial measures. The non-GAAP measures have been reconciled to the related GAAP measures and we have provided reconciliations within the presentation.

I'd also like to remind you that all forward looking statements made during this conference call including any references to guidance or color regarding expected future financial performance, are subject to various risks and uncertainties that could cause the actual results to differ materially from our expectations. These factors are discussed more fully in the earnings release and the company's SEC filings. Copies of those SEC reports are available from the SEC and along with other materials I mentioned earlier on the Unisys investor website. Unisys does not assume any obligation to update the information presented on this call, except as Unisys deems necessary and then only in a manner that complies with regulation FD. With that, I'd like to turn the call over to Peter.

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## Peter A. Altabef

*Chair & Chief Executive Officer, Unisys Corp.*

Thank you, Courtney, and good morning, everyone, and thank you for joining us to discuss our second quarter results. In addition to exceeding consensus on all key metrics in the second quarter, we grew revenue in constant currency and grew ACV and TCV signings and pipeline. Perhaps most significantly, we are showing momentum within our key focus areas of modern workplace, within digital workplace solutions and digital platforms, and applications within cloud applications and infrastructure solutions. I will explain all of those terms in a few minutes. And then Deb will provide detail on our financial results as we welcome her to her first earnings call with Unisys. But first, I'll give some insight into the business.

Starting with Digital Workplace Solutions or DWS. Our primary focus is in higher growth, higher margin solutions that help clients streamline and optimize collaboration to maximize employee productivity and engagement, which we refer to as a modern workplace. Our focus on these proactive experience based elements differentiates us in the market. We refer to DWS solutions not included in modern workplace as traditional workplace.

Our DWS business is positioned to take market share as we shift our mix to modern workplace, and we expect constant currency revenue and profitability for DWS to improve year-over-year and sequentially in the second half of the year. During the quarter we expanded our modern workplace offerings through our relationship with 1E, a mobile device management software provider, which allows us to leverage their Tachyon platform to experience based solutions and makes us a preferred consulting and managed services provider for 1E. Our client Lenovo recently honored us with an award for excellence in premier support in Asia Pacific, and we were also named as a finalist in six categories at the Help Desk Institute Awards, of which we won two.

In the second quarter we signed a new logo for DWS work with a large American beverage company. That work includes our full suite of both modern workplace and traditional workplace solutions. We also signed a new scope managed services contract with a large financial services institution also involving modern and traditional workplace. As part of this contract, we will help to transform the client's communication systems for a hybrid work, Microsoft Teams Environment, leveraging Power Suite, our software for managing and securing collaboration and communications platforms within our modern workplace business.

Shifting to Cloud, Applications & Infrastructure Solutions, or CA&I, momentum continued in this segment during the quarter. We have revised the name of this segment because applications are an increasingly important part of our growth story. We undertook a thorough search for the right acquisition fit to bolster our applications capabilities and presence in the market, and we acquired CompuGain in December of last year.

We are working to shift the mix of revenue in CA&I toward higher growth, higher margin, hybrid and multi-cloud management, cyber security, application modernization, cloud native application development and data analytics and insights, which we are now referring to as the digital platforms and applications piece of CA&I. The remaining

part of this segment and the refinement of our digital platforms and applications and modern focus areas really are part of the sharpening of our go-to-market approach for this business.

As we increase awareness of our capabilities in CA&I, we expect constant currency revenue and profitability upside both year-over-year and sequentially for the second half. As part of our improvements to our digital platforms and applications offering, during the second quarter, we released a new version of our cloud platform with enhanced automation features, including core visibility solutions, incident prevention optimization and tickets and operations automation.

Also, within digital platforms and applications, we enhanced our containerization capabilities, database migration to AWS and Azure, leveraging cloud-native tools, environment monitoring and assessment capabilities as well as our hybrid cloud security services. We're being recognized in the industry for our solutions and during the quarter we were named a leader in the US, in Brazil and in the US public sector in ISG's 2022 Provider Lens for Private/Hybrid Cloud and Data Center Services and Solutions.

I'll now highlight three contracts within digital platforms and applications that we signed during the quarter. First, we signed a new logo contract with one of the largest public K-12 school systems in the United States to provide a cloud ready application to increase the effectiveness and efficiency of processing, evaluating, submitting and tracking claims needed for reimbursement of services rendered to students.

We also signed a new logo contract with the New South Wales Department of Communities and Justice in Australia for their -- for a new biometric security system based on stealth identity. This system will improve the speed of processing inmates, staff and visitors as they move within New South Wales correctional centers. This cybersecurity win is supportive of one of our key growth areas within digital platforms and applications. Finally, we signed a new scope contract with a large financial institution in the secondary mortgage market to support its transition from on-prem legacy applications to the public cloud.

Turning to Enterprise Computing Solutions or ECS, this segment is ahead of expectations for the year as several clients renewed ClearPath Forward licenses earlier than anticipated. Outside of ClearPath Forward licenses, we see opportunities for growth in ECS related services, in specific proprietary financial services and travel and transportation industry applications and in next generation compute to advancing our capabilities related to quantum edge and server-less computing systems, although these opportunities are in the early stages. We released a new version of our ClearPath Forward data exchange solution during the quarter, which enhanced Azure capability, increased automation, improved processing speed and upgraded compliance capability.

Also in the quarter, we signed a new scope ECS services contract with the US State Unemployment Insurance Agency to migrate legacy applications to modern software and architecture and deploy workloads to the cloud to streamline the agency's ability to make changes to its unemployment insurance applications to interface with its ClearPath Forward environment. As we turn to discuss specific metrics for the company and each of our segments, Deb and I will also provide some metrics related to both the focus areas of modern workplace and of digital platforms and applications, and we expect to provide additional details on these focus areas in future calls.

As we look across the company, the transformation of our solution portfolio and go to market approach is driving improvement in leading revenue indicators. Total company ACV grew 25% year-over-year, DWS ACV grew 15% year-over-year and CA&I ACV grew 63% year-over-year. Given clients increasing preference for shorter duration contracts, we focus more on ACV than TCV, but second quarter TCV also grew 12% year-over-year. The weighted average expected gross margin associated with those contracts signed in the quarter was again higher than in the prior year period.

While ACV grew, it did not grow as much as anticipated as the number of contracts we were expecting to sign in the quarter have been delayed. Total company pipeline grew 30% year-over-year. DWS pipeline increased 20% year-over-year, and within that the modern workplace pipeline more than doubled year-over-year. CA&I pipeline grew 45% year-over-year, and within that digital platforms and applications pipeline more than doubled year-over-year. The pipeline for modern workplace and digital platforms and applications now amounts to approximately \$1 billion of our total \$6 billion pipeline.

The investments we have made in our sales and marketing initiatives contributed to these results. And our upcoming brand transformation will amplify awareness for the company and our solutions. On the sales front, we have invested in direct sales, client management consulting and in our partner network. With respect to marketing initiatives, we have increased the size of our industry analyst and third party advisor team, and we hosted an industry analyst and advisor event in June. 100% of the advisors who completed our post-event survey said they would include Unisys in client discussions. We have been making progress in marketing even before the brand launch. We initiated a digital advertising campaign at the end of 2021 targeting clients and prospects to drive awareness and engagement. And these groups are demonstrating increased interest in learning about Unisys and our solutions. We are seeing more than double the industry benchmark levels for engagement and web visitors are downloading nearly twice as much content from our site as previously.

With respect to brand, we are engaged in the most significant brand transformation since the formation of Unisys in 1986. While keeping the Unisys name, we have created a new brand platform, both visual and verbal that will launch in the fourth quarter of this year. The campaign is designed to refresh everything from our brand differentiation to our employer value proposition. The campaign will amplify awareness and extend across all touch points, target audiences and content, including advertising Unisys.com thought leadership publications, marketing collateral, demand generation, public relations, social media, pitch decks, sales materials and recruiting materials.

We're looking forward to the results of our rebranding and we think those results will include driving sales, building our reputation, engaging our associates, recruiting new talent, and enhancing our corporate culture. We have also taken a targeted approach to this initiative, aiming to maximize impact efficiency.

Turning to workforce management, the cost of labor remains elevated across the industry. In the first half of the year, attrition, the competitive talent market and inflation drove the cost of labor higher in parts of our business. We're seeing signs of improved talent availability and expect attrition to level off in the second half of the year. Redeployment of internal talent to fill open roles has been enabled by our career development programs. These programs which include new leadership and technical development opportunities have resulted in our people earning 28% more certifications in the first half of 2022 than in the prior year period.

We're also improving the efficiency of our internal deployment process through automation that accelerates the movement of internal talent into open roles. We expect the combination of market forces, lower attrition, and enhanced ability to deploy internal talent to stabilize the cost of labor in the second half of the year. We are also expanding our focus on campus hiring globally as we transition our labor pyramid to be weighted more heavily toward lower cost early career talent.

Our DEI efforts are continuing to gain traction. We were named in the Top 20 of America's Best Employers for Women by Forbes and received a score of 100 on the 2022 Disability Equality Index. Turning to ESG, we recently announced a goal of net zero greenhouse gas emissions for Scope 1 and 2 by 2030. This aligns with Science

Based Targets initiative's Business Ambition for 1.5 degree centigrade and builds on the company's participation in the Carbon Disclosure Project and the UN Global Compact.

At this time we do not have much information to share but we are aware of a recent apparent cyber attack involving our software lab environment. Our internal security team with the assistance of a leading cyber defense firm is actively taking steps related to this incident. We have also engaged with law enforcement authorities. At this time, there are no service disruptions either for our operations or for our clients.

So in summary, demand drivers such as digital transformation, hybrid work models and migration to cloud remain robust and our strategy is showing momentum in our focus areas. Progress in signings has been slower than expected, though, and foreign exchange rates have also deteriorated since our last call. Because of this, as well as increased labor costs, we are lowering our revenue and profitability guidance for the year. That said, we expect revenue and profitability both as reported and in constant currency to grow year-over-year and sequentially in the second half.

With that, I'll turn the call over to Deb to discuss our financial results.

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## Debra McCann

*Chief Financial Officer & Executive Vice President, Unisys Corp.*

Thank you, Peter, and good morning, everyone. I am excited to be here today for my first earnings call since joining Unisys in May, and I look forward to getting to know our investors and analysts better in the coming quarters.

In my discussion today, I will refer to both GAAP and non-GAAP results. As a reminder, reconciliations of these metrics are available in our earnings material. Additionally, I'll provide the total company revenue on an as reported basis, as well as constant currency and we'll provide segment level revenue on a constant currency basis.

As Peter highlighted, our strategy continues to gain momentum. We are encouraged by the year-over-year increases in ACV, TCV and pipeline in the quarter and the fact that we grew revenue year-over-year in constant currency and beat consensus on all key metrics. That said, progress has been slower than expected in part due to delays in contract signing, which has resulted in less opportunities for [indiscernible] (19:31) revenue growth and margin expansion related to mix shift as well as increased labor costs, which impacted profitability in parts of our business.

Foreign exchange created an additional revenue headwind. None of these elements impact our long term strategy and we expect our contract signed to-date this year and anticipated second half signings including ECS licenses will drive year-over-year and sequential revenue and profitability improvements in the second half.

We also anticipate that our sales and marketing initiative will further contribute to a year-over-year improvement in second half signings and we still expect year-over-year improvement to free cash flow for the full year 2022. With that as a backdrop, I'll provide more insight into our second quarter results. Total company revenue beat consensus growing 2.8% year-over-year in constant currency or flat as reported and our focus areas of modern workplace and digital platforms and applications grew year-over-year.

Several clients renewed ECS licenses earlier than anticipated, resulting in a 11.3% year-over-year constant currency growth in that segment. We are now anticipating better full year ECS results than originally indicated with full year 2022 revenue expected to be down low single digits year-over-year in constant currency.

As a reminder, the majority of ECS revenue timing depends on the number and size of contracts up for renewal in a given quarter, as opposed to renewal rates themselves, which remain over 95%. We believe there is future upside in the segment in ECS related services, specific proprietary industry applications and with next generation compute capability.

Moving to CA&I, our momentum continued with revenue growth for the segment of 8.7% year-over-year in constant currency driven by our higher growth, higher margin digital platforms and applications which increased to approximately 29% of CA&I's revenue from approximately 20% in the prior year period. We see meaningful incremental opportunity within the segment specifically related to digital platforms and applications in which our acquisition of CompuGain significantly enhanced our capabilities. We are increasing awareness of our offerings in this market and these efforts along with the 63% year-over-year increase in second quarter CA&I ACV are expected to drive accelerated year-over-year growth going forward in the segment.

Next, let's discuss DWS, which is positioned with the right solutions and go-to-market tools to be successful. Our experienced focused differentiation in modern workplace is being recognized in the industry and has helped drive our 15% year-over-year DWS ACV growth. New business within DWS has been growing, although slower than expected, as a number of new contracts have been delayed. We are also continuing to feel the impact of the roll off of the traditional workplace contracts that we exited in 2021, which totaled \$24 million in the second quarter. As a result, our DWS revenue was lighter than expected in the quarter, down 11.7% year over year in constant currency. Excluding the impact of the exited contracts and currency, DWS revenue grew 5.7% year over year. We expect the exited contracts will impact Q3 by \$20 million and Q4 by \$11 million.

We are encouraged that we continue signing new logo contracts for our modern workplace solutions as it highlights our ability to move up the value chain. Modern workplace solutions revenue increased to approximately 14% of DWS revenue in Q2, from approximately 4% in the prior year period. With respect to the company overall, as we look to the second half of the year, we expect revenue in the third quarter to be up 50 to 150 basis points year over year in constant currency, though, down 375 to 475 basis points year over year, as reported, in part as a result of ECS renewal timing. With more significant constant currency and reported revenue growth in the fourth quarter, leading second half revenue to be up year over year overall. Supporting these revenue expectations are the ACV and pipeline detail we provided as well as our backlog.

Total company backlog as of June 30th declined from \$2.9 billion at the end of the first quarter to \$2.7 billion primarily due to FX. Of the total company revenue expected in the third quarter, approximately 75% is already in backlog. Despite the positive momentum and encouraging leading indicators supporting a strong second half, the delayed signings and FX deterioration since the last earnings call have led us to lower our revenue growth guidance for the year from our original range of 5% to 7% to 2.5% to 4.5% on a constant currency basis or negative 1% to positive 1% as reported. Approximately 350 basis points of the change versus our original range was due to foreign exchange and approximately 250 basis points was due to contract signing delays. In the past, foreign exchange did not have a large impact on our revenue growth while at current rates it now has approximately a 350 basis point impact year-over-year, which is why going forward we will be providing revenue growth guidance in both constant currency and as reported.

Moving to profitability. Total company gross profit was \$148 million, up 4.1% year-over-year, and gross margin was 28.8%, up 130 basis points. ECS profit was up 16.1% year-over-year, which led gross margins from the segment to be up 460 basis points year-over-year. As a reminder, ECS costs are relatively fixed both year-to-year and throughout the year. Given that the key components of costs are the labor to support the platform and the

amortization of software development costs, so the timing of license renewal can also have a significant impact on profitability.

DWS gross margin decreased 240 basis points year-over-year to 13%, largely driven by higher cost of labor due to the competitive talent market and inflation. We expect productivity improvements and more efficient staffing models, stabilizing cost of labor as well as mix shift to drive year-over-year improvement in DWS gross margin in the second half of 2022 and future years. Within CA&I gross profit margin was 5.5% versus 11.1% in the prior year period impacted by higher labor costs. We are increasing standardization and adding automation across our CA&I solutions which is expected to improve efficiency, scalability and profitability in the second half of 2022 and future years.

Total company non-GAAP operating profit margin was 9%, down 70 basis points year over year relative to our stated expectation of being down 450 basis points to 550 basis points. Adjusted EBITDA margin was 17.6% down 60 basis points year-over-year relative to our stated expectation of being down 450 basis points to 550 basis points.

The year over year comparisons were impacted by the higher cost of labor in the parts of the business that I noted, and increased investments in sales and marketing that contributed to the ACV, TCV and pipeline growth Peter mentioned with those impacts partially offset by the level of ECS signings in the quarter.

In addition to the productivity improvements, stabilizing cost of labor, mix shift and increased automation, I mentioned, the timing of ECS licenses is expected to contribute to profitability, improving growth year over year and sequentially in the second half.

However, due to the split of those ECS licenses between the third and fourth quarter, we expect total company non-GAAP operating profit and adjusted EBITDA margin to be down approximately 375 basis points to 475 basis points year over year in the third quarter. We then expect these two metrics to be up meaningfully year over year in the fourth quarter.

As we continue to refine our cost structure and real estate footprint, we expect \$5 million to \$10 million of associated charges in the third quarter. Based on these expectations and primarily driven by inflationary impacts such as increased cost of labor and the delay in signings that has impacted the shift to higher margin solutions, we are lowering our full year non-GAAP operating profit margin guidance in the original range of 9.5% to 10.5% to 7.5% to 9% and adjusted EBITDA margin guidance from our original range of 18% to 19% to 16% to 17.5%. Approximately 100 basis points of this was related to the increased cost of labor, with the balance related to delayed signings.

Going forward, we expect to continue providing a similarly sized guidance range given increased volatility in macroeconomic environments, including foreign exchange. Our net loss of \$17.1 million or \$0.25 per diluted share improved versus a net loss of \$140.8 million or \$2.10 per diluted share in the prior year period, largely due to the company taking a settlement charge in the prior year period related to pension liability reduction initiatives, partially offset by a tax-related benefit. Non-GAAP net income was \$16.2 million or \$0.24 per diluted shares versus \$46 million or \$0.68 per diluted share in the prior year period, largely driven by an increase in taxes year-over-year due to the jurisdictions in which income was earned.

Moving to cash flow related items, CapEx in the quarter was \$25 million versus \$23 million in the prior year period. Free cash flow was impacted by the timing of collections related to ECS licenses in both periods. As a



result, free cash flow was negative \$59 million, which was down \$78 million year-over-year. We continue to see free cash flow expansion as important and expect year-over-year improvement in the metric for the full year 2022.

Although we do not give free cash flow guidance, we can give you a sense of where we expect to end 2022, which is a range of \$35 million to \$75 million, up relative to \$32 million in 2021. Our current expectation is for CapEx to be \$90 million to \$115 million for the full year. We had a healthy cash balance of \$380 million as of the end of the quarter, which is above our working capital needs. Overall, we are excited about the momentum we are seeing in the business, reflected in the improvement in go-to-market metrics we've noted.

While some of the signings, revenue and profitability progress we anticipated making by this point in the year has been delayed, we feel good about the underlying demand drivers in our areas of focus. We believe we have the right solutions to effectively address them and see the market recognizing this. We look forward to the completion of our sales and marketing initiatives planned for the second half of the year and the additional momentum that we expect these to drive.

With that, I'll turn the call back over to Peter. Peter?

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### Peter A. Altabef

*Chair & Chief Executive Officer, Unisys Corp.*

Thank you, Deb. With that, I would note that for the Q&A session, in addition to Deb, we are joined today by Mike Thomson in his new role as Chief Operating Officer. We'll be happy to respond to any questions you may have. Operator, would you please open the call for questions?

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## QUESTION AND ANSWER SECTION

**Operator:** Thank you. We will now begin the question and answer session. [Operator Instructions] At this time, we will pause momentarily to assemble the roster. Our first question comes from Rod Bourgeois with DeepDive Equity Research. Please go ahead.

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### Rod Bourgeois

*Analyst, DeepDive Equity Research*

Q

Okay. Hey, thanks. So, hey, I'd like to ask about pension. I'm wondering if you can just give an update on your pension in light of the latest market conditions. Any kind of interim pension estimates would be helpful as we've definitely received a round of pension questions of late. Thanks.

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### Debra McCann

*Chief Financial Officer & Executive Vice President, Unisys Corp.*

A

Okay. Great. Thanks, Rod. On – for calculations of both the GAAP accounting deficit as well as the cash contributions for our US qualified defined benefit pension plan, we only perform this valuation analysis at the end of each year based on year end data. International contributions are determined by tri annual negotiations and are typically based more upon affordability than macroeconomic factors.

Given the current market trends, we believe our accounting deficit with US and international combined should improve from year end 2021 because calculations mark to market liabilities using a higher discount rate due to rising interest rates which we expect will more than offset the deterioration in asset values.

However, as you probably know with regarding US cash contributions, a material deterioration in the value of our US qualified defined benefit pension plan assets as well as any changes in pension legislation, discount rates or economic or demographic trends could require us to make cash contributions to these plans in the future. On our Q4 call early next year, once our valuation analysis is complete we will update our expectations. But based on deterioration in both the equities and the fixed income market this year we may be required to make additional cash contributions to our US qualified defined benefit pension plans in the future.

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**Rod Bourgeois**

*Analyst, DeepDive Equity Research*

Q

Okay, great. That's helpful. Hey, I want to dig into the causes of the signings delays and I guess I wonder, is it possible that some of the signings delays are due to Unisys working carefully on contractual terms and pricing and to what extent are macro changes contributing to the signings delays? So more color on that would be really helpful.

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**Peter A. Altabef**

*Chair & Chief Executive Officer, Unisys Corp.*

A

Yeah Rod, thanks very much for the questions. It's actually pretty hard to dissect inside specific contract negotiations because they're all relatively unique. We do, a fair amount of our revenue is what we consider long term. So 82% of our revenue are long term contracts. Only about 18% are project works. So on the macroeconomic side, when you have people who are not sure we're in a recession, we're not in a recession, outside the US still represents about 55% of our revenue. And, particularly in Europe, there are more questions there. So I would say that some of the delays as I'm going through in my head, the contracts that have been delayed, I think certainly macroeconomics plays a pretty big role there. I think that in terms of the pricing for those contracts, I'd actually turn it over to Mike, who has been more involved in exactly how our pricings is.

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**Michael M. Thomson**

*President & Chief Operating Officer, Unisys Corp.*

A

Yeah. Hey, Rod, thanks for the question. I would really echo the comment that it's probably a lot more to do with the macroeconomic environment. We've done quite a bit of work in the analysis of contract signings. As you know, we really spend a lot of time ensuring that we've got the right [indiscernible] (34:56) and those types of things in our contracts. But I wouldn't – our contracting process is not really elongating or delaying those signings, in fact, we're trying to expedite those contracts signed by really breaking those contracts into various buckets, right. So you've got these large extended contracts, which clearly take a lot more time and effort to get through. But we also have plenty of these fast track contracts that might be things like professional services, augmentation and things like that. So I would definitely concur with Peter in that. It's a lot more to do with the uncertainty in the environment and probably thoughts around duration of contract than it is our processes.

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**Peter A. Altabef**

*Chair & Chief Executive Officer, Unisys Corp.*

A

The one item I would add to that Rod, which isn't necessarily on your list, but as we think about those deals that we have, when we think – when you go back to that sort of pipeline, our pipeline has grown significantly in both DWS and in CA&I, but most significantly in the focus areas, right. So the pipeline has doubled in the focus areas of modern workplace and digital platforms and software. And so, then not to say that that's new, but as Deb talked about, that's a fast – those are fast growing focus areas for us.

And so, we're quickly making a name for ourselves in those areas. But I think it does take a little bit, especially when you're really moving into those higher growth areas to get all of that traction in a timely manner. So I would say we're really happy with the ACV growth in those areas. We're very happy with the pipeline growth. But I think some of that is going to grow a little more slowly than some of the traditional solutions.

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**Rod Bourgeois**

*Analyst, DeepDive Equity Research*



Thank you.

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**Operator:** Our next question comes from Jon Tanwanteng with CJS Securities. Please go ahead.

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**Lee Jagoda**

*Analyst, CJS Securities, Inc.*



Hi. Good morning. It's actually Lee Jagoda for Jon. So just starting, appreciating that a lot of these contract signings delays are related to the macro. As you transition to higher growth, higher margin type work, are you able to kind of give us any, some representative examples of some of the new stuff that you're signing, the target margins on that stuff versus the target margins you may have had one, two or three years ago. And then whether the current labor situation and inflation situation is able to be built into those new contracts to get you to those target margins? And then the last piece of my 19 part question here is, are you gaining, losing or maintaining share as a result of the new way that you're going after work?

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**Peter A. Altabef**

*Chair & Chief Executive Officer, Unisys Corp.*



Well, so I'll start and then I'll hand it over to Mike for a little more detail on some of the sub questions. With respect to target margins, as I mentioned in my remarks, the target margins for the deals we're signing in the first quarter and in the second quarter are higher than the target margins of the period before. And part of the reason they're higher is because we are selling a higher mix of higher margin work, and both in DWS, modern workplace and in Cloud, Applications & Infrastructure that digital platforms and software group are both higher margin.

So as we sell more of those focus area items, we are going to get higher margins and we expect to get those higher margins going forward. And I'll let Mike talk specifically about the pricing, because we are dealing with inflation in several different ways and it's largely depends on what our client preferences are. But we are covering ourselves from inflationary pressure. Some of those are through [ph] clauses (39:22) and some of those are through expected adjustments in pricing over time. But I'll let Mike deal with it.

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**Michael M. Thomson**

*President & Chief Operating Officer, Unisys Corp.*



Yeah. Thanks Lee for the question. Yeah, I think Peter gave you the good highlights here. And one of the things I would note is, when you look at our weighted average expected gross margin associated with contracts, we signed in the quarter, they're higher than the prior year period, right. So that tells us that we are getting the proper margin profile on a higher labor cost base, meaning, clients are obviously paying the higher pricing that we're passing through in regards to the labor costs.

Now we do have an increased labor costs year-over-year. We're looking at it being approximately \$20 million of increased labor costs to support those new contract work, but, I think the important factor here, and we noted it a couple of times is when you look at the pipeline growth and the ACV growth, it's more than doubled in both of our target focused areas. And so I don't think you've seen actually the mix shift yet for those new signings at the

higher margin, because some of it is still in the pipeline and some of it is new ACV and the labor costs have already hit us. So there is a bit of a timing mix between when the labor costs hits to when we see that pricing come through. And that's a little bit of the pressure that you're seeing now.

The other thing I'd mention around pricing is we do a lot of public sector work roughly 34% of the work that we do is in public sector. That is a little bit insulated from some of the macro economic conditions because it's driven a little bit more by the budgets, and they don't necessarily change in the short term. So we have a little bit of prevention there. Peter mentioned that roughly 80% or more of our revenue [indiscernible] (41:21) already in backlog. So we would expect over time to see that margin profile continue to improve based on the multiples that we're seeing in the new business improvement.

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**Peter A. Altabef**

*Chair & Chief Executive Officer, Unisys Corp.*

A

Yeah. So, Lee, let me just tie though your question and Rod's question together, and then make sure that Mike and I are being clear because I think – I want to be clear because otherwise we can lose some stuff [ph] on the themes (41:46) of all the answers. So when I go back to the first quarter and when Mike and I were having a discussion on the first quarter that everybody was expecting and seeing early indications of inflationary environment, everybody was seeing indications of labor shortage, particularly in the IT field, right.

So I think our clients were also seeing that and our clients were, I would say, relatively receptive to the idea that we were putting in [indiscernible] (42:19) clauses. We were increasing prices because of inflation, et cetera. What's happened since and this may be where you and Rod are coming from, so I want to recognize it, as it is happening. What's happened since is two things. First, I think we all believe that that labor market is loosening. So there is still inflationary pressure, not as much as it was back in April, right. A lot has happened between April and August.

So the inflationary pressure has decreased a bit as people are going back into the workforce. [indiscernible] (43:00-43:25) part of the answer. Do we think that all of that mix of inflation changes, labor changes, recession changes, currency changes, do we think that as affecting the timing of contracts? Yes, that's what we said. Is part of that because there is a bit of a delay in getting clients to agree to the pricing? I think the answer to that is yes. But again, it's very hard to attribute motives to a client on a specific deal or anything. But when you think about all of those things at once, it is actually quite likely that, that our efforts to maintain pricing is causing some of the delay. We do not believe that that's making us less competitive. So we're not seeing that in a decrease of win rates, but we are seeing that in a longer period of contracts signed. Lee, I don't know if that helps. And Rod I may have misunderstood your question. So I don't know if that helps you as well.

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**Operator:** The next question comes from Joseph Vafi with Canaccord. Please go ahead.

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**Joseph Vafi**

*Analyst, Canaccord Genuity LLC*

Q

Hey, guys. Good morning. Congrats on the new roles, Deb and Mike. Maybe we'll just start first. I know you added the A to CA&I, could you just kind of go into a little more detail on kind of how big applications is now, kind of some of the, perhaps the growth rates there. I know your cloud business is one of your faster growing pieces overall, and how it may stack up there. And then I have a quick follow up.

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**Peter A. Altabef**

*Chair & Chief Executive Officer, Unisys Corp.*

A

Yeah, so thanks very much for the question. I want to start with saying that you are exactly right. It is a name change only. So the segment that was formerly Cloud and Infrastructure is now called Cloud, Applications and Infrastructure. It's exactly the same stuff. We added the word applications because although we have always had applications revenue in there, with the acquisition of CompuGain in December and with the changes in the marketplace, frankly, we think that long term for IT solutions providers like ourselves, the Infrastructure piece of the cloud will be large and will grow, but the applications side of the cloud will be larger and growing faster.

So we really worked last year to make sure that we felt we had the right, or enough scale on the application side and that led with the acquisition of CompuGain. So what we have done is, is to say, okay, so within the larger segment of what we're now calling Cloud, Applications, and Infrastructure, what is the focus area there. And what we're doing there is we're not actually singling out just applications, right, we've now created a focus area of called digital platforms and applications.

So digital platforms and applications is broader than just applications because it is what we really consider kind of the pure cloud infrastructure piece of that as well, as well as, and I went through the definition in my remarks, some very, very higher growth elements of that, of the overall [indiscernible] (47:09) So if we look – so the answer to the question is we're not breaking out applications alone, but we are breaking out the revenue for you of DPA as a focus area of CA&I. And going forward, I mean, we gave you some information on these focus areas, but as I said in my remarks, we're going to give more and more specifics because we really want all of you on the call to understand, we intend to beat market growth rates, but the market growth rates between modern workplace and traditional workplace are very different. And the modern growth – and the growth rates in the market between DP&A and classic infrastructure are very different.

So, one of the insights that Deb brought to the company was we really have to break this out for you guys. So because if you just aggregate all of DWS and all of CA&I, we're kind of missing the story, which is to show that we believe we're going to grow faster on both elements within those segments. But those elements are very different. So Deb, and if we look at just DPA as a portion of CA&I and how that has grown, I think you gave the percent of what it is this quarter compared to a year ago, right.

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**Debra McCann**

*Chief Financial Officer & Executive Vice President, Unisys Corp.*

A

Right. Yes, that's true. This year, right now, it's about for this quarter 29%, the revenue of the CA&I business and this time last year, it was 20%. So definitely growing and we'll continue as Peter mentioned in his script as time goes on, we'll give even more metrics on that.

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**Peter A. Altabef**

*Chair & Chief Executive Officer, Unisys Corp.*

A

Right. And the market growth of that area versus [indiscernible] (48:56) infrastructure is so different we just need to break it out for you.

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**Joseph Vafi**

*Analyst, Canaccord Genuity LLC*

Q

Sure, sure. That's great. Thanks for all that color. Thanks, Deb. And then just CapEx for the year, I know you're continuing to work to bring some of the capital intensity down just kind of -- just wanted to get some further thoughts on that topic. Thanks.

**Debra McCann**

*Chief Financial Officer & Executive Vice President, Unisys Corp.*

A

Right. So as I had mentioned CapEx, we plan on being about \$90 million to \$115 million for the year, which does put us more in that 5% of revenue area, which I think is more typical for our industry related to our peers. So I think, in the past it was higher, closer to 7% to 8%. So I think we're moving more in the range of where we should be and will most likely be going forward.

**Joseph Vafi**

*Analyst, Canaccord Genuity LLC*

Q

Great. Thanks a lot, guys.

**Operator:** Our next question comes from Matthew Galinko with Maxim Group. Please go ahead.

**Matthew Galinko**

*Analyst, Maxim Group LLC*

Q

Hi. Good morning. Thank you for taking my questions. For the new deals that you are getting through, is there anything distinguishing about the customers, the customer need or the mix of services that are getting them through versus the stuff in the pipeline that's being delayed, it sounds like by, from your view macro issues.

**Michael M. Thomson**

*President & Chief Operating Officer, Unisys Corp.*

A

Hey, Matt. This is Mike. I'll take that one. Good to hear from you. I wouldn't say that there is a distinction in the demographic data of the customers, right. I guess the first thing I would say is that for the deals that are getting through and being signed, they are elongated and the ones that we've signed actually started a little earlier in the process. Well, the interesting thing specifically when we talk about the elements in DWS or modern workplace, and I think Peter alluded to this in his prepared remarks, they are for the full stack, right.

We've signed several deals where they've taken both sides of the coin, right. So you've got the traditional workplace as well as the modern workplace. And I think the demographic of the deals where we've had success, were the ones where we can continue to illustrate the experience aspect of it. And they've actually been much richer and deeper contracts and more inclusive of everything that we have to offer. And I would say the ones that have been signed also across our segments, right? So we have a CA&I component and a DWS component.

So I think strategically that's what we wanted. And when we look at deals like that, we seem to have a quicker turnaround or more success rate on those particular deals. And our real focus is getting invited to more, right. It's not a matter of whether we can facilitate it. It's how many more we can get invited to, because our win rate has been pretty consistent in those areas. And we feel really good about the solutions, the offerings, and the quantity and quality of what's being asked for and what we're providing. So I think it's a little bit more Matt tied into that full deal versus these one off components that are driving the success rate in the modern workplace.

**Matthew Galinko**

*Analyst, Maxim Group LLC*

Q

Thanks. Yeah that was a great answer and hit on everything. So I appreciate that. I guess my follow up is on the, on ECS, pulling renewals a little earlier, is that more from the second half of the year or is that pulling forward from beyond 2022?

**Peter A. Altabef**

*Chair & Chief Executive Officer, Unisys Corp.*

A

Yeah, Matt, let's get into the details on that. The answer is it's a little of both. We don't control this. And depending on the needs of the clients, it's pretty obvious we can be [ph] fooled. (53:29) And in this particular quarter, we had some renewals and extensions that we were anticipating signing this year. We even had some that we were not anticipating signing this year at all and signing in the future that were – that the client wanted to sign. So, we are – we hope we're very client responsive in all of our business. When it comes to ECS, given the size of those contracts and the importance, we're especially client responsive. And that's what happened this quarter. Deb?

**Debra McCann**

*Chief Financial Officer & Executive Vice President, Unisys Corp.*

A

Yup. No, I think that's right, Peter. Not too much more to add, but just as I mentioned in my remarks, just to reiterate, our expectation is for the full year that ECS will be down low single digit year-over-year in constant currency is our expectation, now, I think, before, we gave you a bigger decline, but because of the factors Peter mentioned, that's where we stand right now.

**Peter A. Altabef**

*Chair & Chief Executive Officer, Unisys Corp.*

A

The other thing I would point out is, again, as we are, I think, becoming a bit more sophisticated in the way we're looking at each of these segments, as I mentioned in ECS, it's not just about renewals of ClearPath Forward anymore. We've identified three future, if you will, revenue streams tied to specific offerings. We've talked in the past on these calls about what we call ECS services and those are the services that are associated with whether it's ClearPath Forward or other ECS proprietary applications.

There's a big market for that, and we expect to take advantage of that and to serve customers in a more powerful way on the services side. Think of the applications that our clients have that sit on top of ClearPath Forward as an example. We're only doing a fraction of the modernization and maintenance of those applications. We think we can do more for our clients. And then, we've talked in today about two more offerings and revenue streams. One is what we call those industry specific applications that we've had those for a while. Things like cargo, things like air traffic, things like financial services, applications. And we're really looking at invigorating some of those and the revenue and market share that is attached to those.

And then, the third element of that is really around next-generation compute. There are few organizations that are as capable as or well-positioned as ours to really help our clients on the journey to quantum, both offensive and defensive to serverless technologies, et cetera. And so again was – as we get further down the road here and start kind of isolating these growth areas, as Deb is kind of restructuring this for us, you'll hear us talk about ECS in a lot broader way than just talking about ClearPath Forward renewals and that's going to be an important part of our future.

**Operator:** Our next question comes from Anja Soderstrom with Sidoti. Please go ahead.

**Anja Soderstrom**

*Analyst, Sidoti & Co. LLC*

Q

Hi, thank you for taking my questions. Most of them have been addressed already, but I'm just curious. You mentioned, you added talent availability has improved. Where do you see that talent coming from?

**Peter A. Altabef**

*Chair & Chief Executive Officer, Unisys Corp.*

A

Well. So, I would say it's really coming from almost all geographies. Some of it is, I think, macroeconomics and some of it is because of the stuff we're doing. So, on the macroeconomic stuff, I do think there's a realization in the marketplace that there are not – the gap between the number of tech jobs that are available and the number of people who are qualified is actually shrinking. And that's because, as we all see in the paper, there are some organizations that are decreasing their hiring of people.

So that's a macroeconomic event that is making life a little easier on us. It's not easy, but it's easier. As we think about our own attrition, our attrition continued to tick up this quarter on a sequential basis, but it ticked up only a little bit, 60 basis points, and that is the smallest tick-up we have had on a sequential basis since the first quarter of 2021. So, we really are seeing, kind of a leveling off of that. And then the flip side of that, it's not all about macroeconomics. Some of it is what we're doing. So we issued a press release earlier in the quarter about a program that we've had for 14 years, called the Unisys Innovation Program in India that used to be called Unisys 2020. It's a remarkable program where we go out to students throughout India and get them involved in innovative processes and projects. And then we have winners and we give job offers, but it's not really so much about the job offers as it is about it's a very prestigious competition.

Well, this year we had an almost 13% increase in the number of people submitting entries into that program. And so, that's something we've had for a while. But I would say we're kind of putting that on steroids. And similarly, when we talk about our campus programs and our other outreach programs, I just think we're doing more internally as an organization to really be up our game in terms of recruiting as well as retention.

33% of our job openings were filled by internal candidates this quarter. That's the highest number I can remember. And it goes to the efforts I mentioned that we're really working hard at retraining people and positioning them for next-generation jobs as we get more clients doing that kind of work. We'd much rather retrain our people than hire from the outside. So it's a combination of macroeconomics and I think what we're doing internally, I hope that helps. Mike, any other thoughts on that?

**Michael M. Thomson**

*President & Chief Operating Officer, Unisys Corp.*

A

The only other element I would add is just the branding and the clear focus on attraction of talent and how we're positioning ourselves in the marketplace, but I think you've covered every other element of it.

**Peter A. Altabef**

*Chair & Chief Executive Officer, Unisys Corp.*

A

And on the branding piece, good of that is to come. We talked about that as really kind of all the work is done frankly. We know exactly what the branding campaign is going to look like. We know the statements. We know whatever thing is going to visually be. We're now really setting up, if you will, [ph] the dominos (01:00:45) start that in the fourth quarter. But I would [ph] following that (01:00:49) Mike said which refer back to my remarks as much as I talked in my remarks about how we believe that campaign will really kind of show our clients and particularly our prospective clients what we do. It will also show prospective employees what we do. We don't see that branding campaign [indiscernible] (01:01:13) only at prospective clients. It's kind of equally weighted to prospective, we call, our employees associates, but that's a very important part of what we are doing, as Mike pointed out.



**Operator:** This concludes the question and answer session. I would like to turn the conference back over to Peter Altabef for any closing remarks.

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## Peter A. Altabef

*Chair & Chief Executive Officer, Unisys Corp.*

Thank you so much, operator. I really appreciate all the questions today. I want to thank Deb for joining us as Chief Financial Officer. I also want to thank Mike for using that opportunity to really excel as Chief Operating Officer. We have a pretty awesome leadership team. We will be available to our investors and shareholders on an ongoing basis as we always are. And I would like you to think a little bit more about those focus areas, what it means for us, how we're trying to show you the power of those focus areas. And as Deb and I both mentioned, we're going to give you more and more information about those in the future. With that, I want to thank everyone again for joining our call.

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**Operator:** The conference is now concluded. Thank you for attending today's presentation. You may now disconnect.

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