NYSE:UIS Q1 2026 Earnings Call Transcript

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Operator | Conference Operator:

Good morning and welcome to the Unisys Corporation first quarter 2026 earnings call. All participants will be in a listen only mode. Should you need assistance, please signal an operator by pressing the star key followed by zero. After today's presentation, there will be an opportunity to ask questions. To ask a question, you may press star then one on your telephone keypad. To withdraw your question, please press star and then two. Please note, this event is being recorded. I would now like to turn the conference over to Michaela Paworski, Vice President, Investor Relations. Please go ahead.

Michaela Paworski | Vice President, Investor Relations:

Thank you, Operator. Good morning, everyone. Thank you for joining us. Yesterday afternoon, Unisys released its first quarter 2026 financial results. Joining me to discuss those results are Mike Thompson, our CEO and President, and Deb McCann, our Chief Financial Officer. As a reminder, Today's call contains estimates and other forward-looking statements within the meaning of the securities laws. We caution listeners that these statements are subject to risks and uncertainties that could cause actual results to differ materially from those expressed on this call. These items can be found in the forward-looking statement section of yesterday's earnings release furnished on Form 8K and in our most recent Form 10K and 10Q filed with the SEC. We do not assume any obligation to review or revise any forward-looking statements in light of future events. We will also refer to certain non-GAAP financial measures, such as non-GAAP operating profit, that exclude certain unusual or non-recurring items, such as post-retirement expense, cost reduction activities, and other expenses that the company believes are not indicative of its ongoing operations. While we believe these measures provide a more complete understanding of our financial performance, they are not intended to be a substitute for GAAP. Reconciliations for non-GAAP measures are provided in the slides for today's call, which are available on our investor website. With that, I'd like to turn the call over to Mike.

Mike Thompson | CEO and President:

Thank you, Michaela. Good morning, everyone, and thank you for joining us to discuss the company's first quarter 2026 results. We're off to a good start in 2026. Both growth and profitability were modestly ahead of the expectations we provided, keeping us on track to achieve our full-year guidance ranges. Strong new business signings improved our trailing 12-month book-to-bill ratios and will contribute to in-year revenue. While geopolitical events have introduced new uncertainties in the markets, Client budget seems to be loosening a bit, and especially in the commercial sector and in Europe. Project volumes are beginning to materialize on the back of last year's renewal with solid pipeline in place for the remainder of the year. First quarter profit improvement keeps us on track to achieve our full-year free cash flow expectations and reflects our focus on adopting AI and continued workforce optimizations. As expected, our pension deficit and estimates for future cash contributions remain stable due to the actions we took last year to remove the majority of the pension contribution volatility, allowing us to focus on strategic growth and efficiency initiatives. Looking more closely at the first quarter, revenue was up 1% year over year and 3% in our XLNS solutions. Volumes with existing clients were better than anticipated, including a modest pickup in the PC refresh cycle. This helped offset some of the top-line effects from client attrition and modest price pressures created through sharing AI cost savings with clients, which we discussed last quarter. While AI efficiency gains reset market pricing last year, they're benefiting gross margins, which improved 80 basis points in the first quarter, including 170 basis points of XLNS gross margin expansions. During the client signings, our first quarter wins increased confidence in achieving our 2026 performance goals, and we continue to have a higher portion of guided revenue contracted and in backlog compared to a year ago. The first quarter new business TCB was $158 million, up 16% sequentially and 45% year over year. This was our strongest quarter of new business signings since the fourth quarter of 2024, with growth from both new logos and the existing base. Several multi-year contract wins illustrate our ability to gain market share when leading with innovation. For example, we had several notable signings for our agentic service desk powered by our service experience accelerator capabilities. During the quarter, we won a large new scope contract to provide our agentic service desk with one of the world's premier quick service restaurants expanding our existing support to the entirety of their nearly 14,000 restaurants in the United States, with additional growth opportunities around the world. We also signed a new logo on Australia, which will be our first deployment of our agentic service desk in the Asia-Pacific region, where we've landed several recent wins. As a part of this engagement, we will provide elevated IT support to approximately 11,000 employees in Australia's Department of Health, Disability, and Aging, where we now support numerous regulatory functions. This is a multi-year contract which has options extending to 10 years and is structured on delivering against automation and service experience outcomes rather than ticket volumes. The value behind our service experience accelerator is proving to be a compelling point-of-the-sphere solution for new businesses. delivering measurable results and quickly orienting us as an experienced AI partner in moving enterprise AI from concept to reality. Our device subscription service, or DSS, continues to resonate with another first quarter win at a large financial client in the United States. Clients are grappling with evaluating OEMs and hardware costs, understanding device AI capabilities, and forecasting headcount fluctuations, all of which makes our clients more open to our intelligent refresh offering, which simplifies the process and helps offset cost pressures. We have recently expanded our intelligent offering to encompass certain IoT devices through a deeper partnership with Dell. Several key engagements for application development and management also contributed to strong first quarter new business TCB. For example, we expanded our existing services relationships with Nair, Bain's air traffic controller, a client of 30 years. The renewal included a sizable new scope, which involves managing more than 100 of our clients' existing applications across numerous functions, with additional funds budgeted for future projects to design, test, and deploy new applications. Our application capabilities also opened the door at the largest community college system in the United States, with UNICEF signing a new logo agreement to modernize and manage an important student-facing applications that provides their approximately 2 million students with resources and tailored education pathways for more efficient incoming transfers, graduations, and entry into the workforce. This engagement established a solid foundation, which is already leading to additional work expected beginning in the second quarter. We also made progress on our initiatives to cross-sell CA&I application services into our ECS client base. In the first quarter, we signed a renewal with a large Colombian retailer for existing ClearPass Forward managed services that integrated new scope application development work supporting the client's core commercial and inventory applications. Across our segments, TCB renewal rates were strong and above 95% for the total company. We are also seeing some unexpected extensions from attrited clients stemming from the lack of readiness from the new service provider. At one such client, we were awarded a large new scope in the first quarter for infrastructure modernization services. We believe this win demonstrates the desire of some of these clients to remain engaged with us, which we attribute to the deep relationships we've established, our delivery track record, and the broadening awareness of our capabilities. Looking at our go-to-market and pipeline, we've seen a modest pickup in client demand over the past few months and a stronger pickup with new logos where qualified pipeline increased sequentially in XLNS solutions. A number of these opportunities originated from a new initiative within our direct sales organization, which is the development of rapid value assessments for our key AI-enabled solutions. These repeatable assessments help quantify time to value inclusive of estimated timelines and outcome-based pricing scenarios, easing friction associated with returns on AI investments, especially in the mid-market. We're currently utilizing rapid value assessments for our agentic service desk, intelligent operations, and security operations with assessments for agentic application transformation and management and intelligent device refresh in the works. We're also generating more leads by collaborating with alliance partners on development and marketing around a narrower set of solutions which identified overlapping priorities and strong value propositions. These efforts have led some partners to place Unisys more prominently on their roadmaps and using us as their primary and preferred implementation and managed service partner for their technology. And they're directly handing off leads in areas such as enterprise service management, unified endpoint management, and field services to implement technology for smart reading rooms, kiosks, and digital signage. I want to shift the focus to discuss our investments in the business. much of which is concentrated on leveraging artificial intelligence to move into higher valued services and penetrate emerging market opportunities stemming from AI. Our approach towards enterprise AI has been to avoid simply rebranding existing solutions as AI enabled, but instead to use AI to fundamentally transform the outcomes we deliver to our clients, and that positions us well for future-proofing our client relationships. In our XLNS IT services, this involves thoughtfully choosing partnerships to strengthen, enhancing the skills of our workforce, expanding our operational accelerators, and constructing agentic workflows and governance frameworks to deliver secure, reliable results. We have also been proactive about rolling out delivery innovation in our existing base to create measurable results increasing our relevance and thought leadership with clients, prospects, and industry analysts. We're working to maximize that momentum by investing more deeply in our talent. We're expanding our forward-deployed engineering capabilities to increase capability in areas such as agentic application services. We view agentic AI as a major opportunity for organizations to close the modernization gap, especially in public sector and higher education. Expanding our forward-deployed engineering capabilities positions us to take a more prominent role in designing and managing agentic workflows, whether they enhance software applications or replace elements of their functionality. In some cases, we're seeing client interest in expanding these services beyond central IT to reshape business as usual and functions such as HR and finance. As we think about upscaling for AI more broadly, the skills in demand are rapidly evolving almost on a daily basis with the one constant being the pace of change coming from frontier models, hyperscalers, software, and OEM providers. We're committed to maintaining a platform and model agnostic approach that best addresses a given use case within a specific industry for a specific client. At the same time, Significant existing technical debt within IT estates will require subject matter expertise to meet clients where they are today and help them transform and transition their technical debt over time. To do that successfully, we're aligning certain technical resources around key models and platforms to provide specialized consulting to both our external and internal delivery teams. Physical AI infrastructure is another emerging growth vector for Unisys. stemming from demand for AI compute and the rapid build-out of data center capability that's occurring. Data center builds are expanding the need for field technicians knowledgeable in the installation and maintenance of complex AI-focused IT infrastructure. Our large, globally scaled field services organization with cutting-edge training and delivery experience connects humans, data, and AI agents on one trusted platform. In the first quarter, we signed a new business engagement with the leading global OEM to support the build-out of a large US-based data center. While the initial scope is small, it lends credibility to our specialized capabilities for the installation and support of AI infrastructure. AI infrastructure is just one element of our overarching strategy to expand our field service revenue streams. We're continuing to grow hybrid infrastructure volumes and focus on generating opportunities in network equipment and enterprise storage. We're also broadening field services capability in a variety of hardware, most notably within offices, restaurants, retail, and manufacturing facilities. In L&S Solutions, we're approaching AI from both ends, infusing AI functionality directly into the ClearPass Forward ecosystem, while also making it easier to extend ClearPass Forward data and applications to fuel AI in other parts of the enterprise. During the quarter, we put out a new release of AB Suite, which is our low-code development environment for building applications on top of ClearPath. The updates speed development, enhance data encryption, and simplify integration of data with external environments without disruption of mission-critical operations. The release also adds capabilities for generating AI-based synthetic test data allowing developers to rapidly test new functionality while reducing the risk of exposing sensitive data, strengthening security and compliance. In addition to AB Suite release, we launched a new AI developer toolkit with practical guidance for building AI data models within the ClearPath Forward ecosystem. This is the first in a series of targeted client AI-enabled initiatives aimed at reinforcing ClearPath's value proposition and role as a long-term AI-ready platform that clients can rely on for decades. Taking a step back across all our segments, we're seeing AI disrupt the status of the industry and push clients to rethink their solutions and IT providers. This has given us an opportunity to show our agility and step into a more prominent role with clients and partners and accelerate the shift in our brand perceptions. We also hear it in our conversations with and recognition from the industry analysts and advisors that influence client decision making. In the first quarter, Unisys was again named a leader in reports on end-user computing services and mid-market digital workplace solutions by Avasant and Everest. We are also newly included in the HFS report on next-generation IT infrastructure services. which includes providers able to help enterprise reimagine infrastructure specifically for AI-native operations and distributed digital environments. These acknowledgments follow Gartner's elevating unisys to a global leader in digital workplace services. With that, I'll turn the call over to Deb to discuss our results in more detail.

Deb McCann | Chief Financial Officer:

Thank you, Mike, and good morning, everyone. As a reminder, my discussion today will reference slides from the supplemental presentation posted on our website. I will discuss total revenue growth both as reported and in constant currency and segment growth in constant currency only. I will also provide information excluding license and support for XLNS to allow investors to assess our performance outside the portion of ECS where revenue and profit recognition can be uneven between periods due to license renewal timing. Looking at our results in more detail, As Mike mentioned, the year is off to a good start. As you can see on slide six, first quarter revenue was $438 million, up 1.3% year over year, which included an approximate 600 basis point benefit from foreign exchange relative to the prior year period. In constant currency, revenue declined 4.5%, with the largest declines in LNS solutions due to renewal timing and anticipated volume declines in our XLNS solutions. Excluding license and support, First quarter revenue was $372 million, up 3.1% year-over-year, and down 2.9% in constant currency. I will now discuss segment revenue performance in constant currency terms shown on slide six. First quarter digital workplace solutions revenue of $118 million was down 6.5% year-over-year. This decline was better than we had anticipated and reflected the factors we have discussed in previous quarters such as client attrition, pricing dynamics in the industry, and lower base levels of PC field services volumes that are stabilized but down year over year. At the same time, growth in areas such as higher value field services and better than expected volumes help to mitigate some of those effects. For example, our volumes and revenue from high-end enterprise storage have nearly doubled on a year-over-year basis. And as Mike mentioned, we continue to see significant market opportunities across a more diverse set of higher margin field services, including AI infrastructure and IoT devices. We are also pleased with our DWS pipeline, which is up sequentially. First quarter cloud applications and infrastructure solutions revenue was $182 million, representing a 2.4% year-over-year decline. The decrease primarily reflected lower volumes, especially at certain U.S. public sector clients and client attrition. As you may recall, we began seeing public sector clients pull back in the first quarter of 2025 due to uncertainties related to federal funding levels, and those year-over-year headwinds should lessen as we lap declines in subsequent quarters. Within the Enterprise Computing Solutions segment, or ECS, our license and support solutions revenue was $66 million, down 12.4% year-over-year due to the timing of the renewal schedule. There is no change to our expected weighting of 30% of full-year L&S revenue in the first half and approximately 70% in the second half. And we continue to expect $400 million of average annual L&S revenue in 2027 and 2028. Artificial intelligence has been and continues to be a driver of L&S consumption and in turn revenue. And we are evolving our ecosystem with innovations that facilitate enterprise AI both on our platforms and external AI-enabled client environments that can utilize valuable data generated by our systems. We continue to detect no change in client commitment to the ClearPass Forward ecosystem resulting from AI and code refactoring. On the contrary, there are some signs that our ecosystem evolution is leading to certain clients with migration plans re-evaluating specific workloads to retain an outsource management to Unisys, which we attribute to consistent investments in platform modernization and sustainability of our skilled workforce. In our specialized services and next-generation compute solutions, the XLNS portion of the ECS segment, first quarter revenue was $50 million, down 2.5% year over year. This was ahead of our expectations due to improved volumes and additional scope in some of our business process solutions, which partially offset declines from the phasing of project work. Total company TCV was $274 million for the quarter, up 33% year-over-year. New business TCV totaled $158 million, up 16% sequentially and 45% year-over-year. This is the highest level of new business TCV we have had in four quarters. Trailing 12-month book-to-bill was 1.2 times for both total company and Accelina Solutions. We ended the year with backlog of $2.96 billion, up

2.4% from the prior year end. Moving to slide eight, first quarter growth profit was $113 million, and growth margin was 25.7%, up 80 basis points from the prior year. XLNS growth profit was $73 million, and XLNS growth margin was 19.5% in the first quarter, up 170 basis points year over year. Improvement was primarily driven by expanded use of intelligent automation and ongoing workforce optimization. During the first quarter of 2026, a transaction within the company's UK business process outsourcing consolidated joint venture generated $3 million of non-segment revenue and gross margin benefit with no net cash impact. Total company and Exxon S gross margin benefited by 50 and 70 basis points, respectively. The transaction is expected to generate $12 million of gross margin benefit for 2026 evenly among the four quarters. We remain on track to deliver our targeted 150 basis points of annual XLNS growth margin improvement amid a challenging growth backdrop, although our path may not be a straight line. I will now touch briefly on segment growth profit shown on slide eight. EWS segment growth margin was 13.5% in the first quarter compared to 14.2% in the prior year period. Contraction primarily reflects impacts from exited clients and growth in lower margin device subscription service revenue in the quarter, which can have larger components of hardware, but offer a strong entry point for expansion into higher value offerings. DWS margins are expected to improve as we move through the year and benefit from the implementation of delivery initiatives. CA&I segment gross margin was 21.8% in the first quarter, up 230 basis points year over year. The improvement was driven by continued workforce and labor market optimization, along with higher productivity supported by greater use of intelligent automation, especially within our central application capabilities. The segment also benefited from increased project volumes and higher margin solutions relative to exited contracts, as we see continued traction in high-value application services and multi-cloud management. which leveraged more of the latest AI models and tools for delivery. ECS segment growth margins was 46.9% in the first quarter, down 80 basis points year over year. This was driven by lower L&S growth margin due to the timing of license renewals, partially offset by nearly 70 basis points of improvement in SS&C solutions, which was helped by improved utilization in business process solutions. Across our segments, we are providing our associates career pathways and upskilling in emerging technologies, which is supporting our workforce optimization and internal staffing and our low trailing 12-month voluntary attrition of 11.1%. Turning to slide nine, first quarter non-GAAP operating profit margin was 4.5%, up 170 basis points year over year. This was modestly better than the slightly positive margin outlook we provided last quarter, primarily due to execution against our operational efficiency objectives and increased L&S volume. SG&A was $92 million, down $5 million, or 5% year-over-year, keeping us on track to reduce SG&A by $10 to $20 million in 2026. As a reminder, these savings are concentrated in streamlining corporate functions outside of sales and marketing, and most of the restructuring costs to achieve have already been recognized. Adjusted EBITDA was $46 million in the quarter, representing a 10.6% margin, up 130 basis points year-over-year. Gap net loss was $36 million, or a diluted loss of 50 cents per share, while non-gap net loss was $10 million, or a loss of 14 cents per share. Turning to slide 10, capital expenditures totaled approximately $21 million in the first quarter, relatively flat on a year-over-year basis and consistent with our capital light strategy. As a reminder, a significant portion of capital expenditure relates to development for our ClearPath Forward ecosystem, comprising our L&S solutions. Free cash flow was negative $26 million compared to positive $13 million in the prior year period. The decline was driven by the timing of interest payments on our 2031 senior secured notes, with payments now occurring in the first and third quarters. In addition, the first quarter interest payment included interest related to an 18-day stub period. Pre-pension pre-cash flow was $2.9 million in the first quarter, net of $28.2 million of pension and $0.2 million of post-retirement contributions. The quarter included approximately $12 million of contributions to our U.K. pension scheme that are incremental to our previous full-year forecast. our joint venture partners funded these contributions, resulting in no cash impact to Unisys. For the remainder of 2026, we expect cash contributions to all global pension plans of approximately $69 million. Our cash balance is $380 million as of March 31st, compared to $414 million at the end of 2025. Our liquidity position remains strong, supported by significant cash balances, an undrawn $125 million ABL facility, with an accordion feature up to $155 million and no significant debt maturities until 2031. Our net leverage ratio inclusive of pension is 2.9 times down from 3.2 times a year ago. Turning to our global pension plans, based on market conditions, we estimate that as of March 31st, both gap deficit and aggregate expected contributions through 2029 are essentially unchanged from year end. As a reminder, We provide more detailed projections for estimated cash pension contributions and gap deficit at year end. Quarterly updates reflect estimated impacts of asset returns, market conditions, and assumed deficit reduction from contributions. Following our capital structure transformation in mid-2025, which included a $250 million discretionary contribution to our U.S. qualified defined benefit plans, we took actions that removed substantially all volatility from our expected U.S. contributions. This increased stability, along with the existing stability in international contributions set through trusting negotiation, has significantly increased certainty for investors as to our future cash needs and trajectory of deficit reduction. Turning to slide 12, I will now discuss our financial guidance for the full year and the additional color we provide. We are reaffirming our full-year guidance range and expect total company revenue to decline between 6.5% and 4.5% in constant currency, which based on April 30th foreign exchange rates equates to a reported revenue decline of negative 3.5% to negative 1.5%. Guidance assumes ex-LNS revenue constant currency decline of 7% to 4.5% and full-year LNS revenue of $415 million. As a reminder, the timing and exact amount of LNS revenue can be difficult to forecast with precision, as it depends on renewal timing, term, and client consumption levels, among other factors. We are reaffirming guidance for full-year non-GAAP operating profit margin of 9 to 11 percent, which assumes a slight year-over-year increase in L&S gross margin, targeted ex-L&S gross margin improvement of 100 to 200 basis points, and 10 to 20 million reduction in operating expenses. Looking specifically at the second quarter, we expect approximately $450 million of total company revenue on a reported basis, which assumes approximately $70 million of licensed support revenue. Based on these assumptions, we expect second quarter non-GAAP operating margin of approximately 5%. We expect second quarter items impacting GAAP net income of approximately $30 million, primarily related to pension expense. We expect a number of elevated non-cash expenses impacting gap net income and earnings per share later in 2026 related to pension annuity purchases and streamlining certain legal entities, which we will guide on a quarterly basis. Also, as a reminder, in 2025, we removed hedges on our intercompany balances, which could create non-cash FX gains as the U.S. dollar strengthens or losses as the U.S. dollar weakens. These are difficult to guide due to constantly changing rates, but will impact quarterly gap net income. There is no change to our expectation for full year free cash flow of approximately negative $25 million, which translates to positive $72 million of pre-pension free cash flow. This assumes approximate payments of $85 million in capital expenditures, $70 million of cash taxes, $70 million of net interest payments, $30 million in aggregate environmental, legal, and restructuring payments, and $102 million of post-retirement contributions. with approximately $29 million of which is expected in the second quarter. We are focused on continuing to increase our efficiency and profitability during this period to maximize our underlying cash generation levels for investment and capital return. Before we open the line for questions, Mike has a few additional remarks.

Mike Thompson | CEO and President:

Thank you, Deb. I want to reinforce three key points we hope came through in our commentary today. First, our confidence in the guidance ranges we've reaffirmed today is reinforced by our first quarter financial performance, as well as the strength of our client signings, book-to-bill, and backlog position. Second, our L&S solutions are durable, and we are continuing to make investments to modernize our ClearPass Forward ecosystem and solidify our platforms as a key enabler of enterprise AI. Third, artificial intelligence is not only allowing us to provide more cost-effective solutions for our clients, but creates opportunities for us to help enhance our clients' business processes and end-user experience, which creates a variety of new outlets for Unisys. We hope you'll join us on June 2nd to discuss these opportunities and more at our upcoming Investor Day, which you can RSVP for on our investor websites. Operator, you may now open up the line for questions.

Operator | Conference Operator:

Thank you, sir. We will now begin the question and answer session. To ask a question, you may press star then 1 on your telephone keypad. If you are using a speakerphone, please pick up your handset before pressing the star keys. If at any time your question has been addressed and you would like to withdraw your question, please press star and then 2. Again, if you would like to ask a question, please press star and then one now. The first question that we have comes from Rod Bourgeois of Deep Dive Equity Research. Please go ahead.

Rod Bourgeois | Analyst, Deep Dive Equity Research:

Hey, guys. Hey, so it was helpful to hear some of your AI initiatives across your different segments and the accelerator work and the service experience work and so on. I wondered if you could just take us through quickly each of your segments and how AI is, what are the headwinds and the tailwinds from AI and maybe the net effect when you look across how AI is affecting you across your key segments? Thanks.

Mike Thompson | CEO and President:

Great. Hey, Ron, thanks for the question. Good to hear from you. Yeah, look, I think as we've stated in previous calls, We see AI in general as a significant tailwind for not only for us, but I think for the industry in general, but specifically embedded in our segments. And I apologize, I'm fighting a little cold here, so... when we think about the impact in DWS. So we've already talked a little bit around some of the headwinds, which is really just a renewal cycle and the reestablishment and cost sharing of applying AI to that renewal. But moreover, I think we've been able to mitigate a lot of that headwind. Clearly, we've embedded AI into our solutions. We've seen the industry analyst reports on how that's set. So, you know, we think there's some real opportunity there, not only to have that in our solutions, but in our skill sets that we're bringing to market. So we mentioned in our prepared remarks, many opportunities inside of DWS, whether that's infrastructure AI and the build out from a field services perspective, all of the work that we're doing with agent force embedded in Salesforce opportunity and application of AI with our teaming there. And most prominently in DWS would be embedded in our solution experience accelerator and our agentic service desk. So, you know, we're seeing that really resonate, seeing some, you know, nice uplifts in pipeline, et cetera, in that particular business segment. So really happy there. And, you know, clearly we think it's – net-net a positive long-term statement for the industry and for Unisys. From CA&I, you've heard in the prepared remarks in general across the board that the benefit there is clearly around AI application as it applies to modernization, the adoption of AIOps in our intelligent operations framework. and the work we're doing around the agentic build of what we consider to be the action layer or the application or even above the application layer, that's been really growing across the board for us. And we think it's something that will continue to grow and actually probably opens up TAM for us for areas where we can really penetrate with that agentic layer that historically we may not have played in. So really pretty bullish on the application transformation layer embedded in CA&I. And then in ECS, I mean, it's been a powerful story for the last several years. We've talked roughly around 40 million of increase per year over the prior three years of consumption. The work that we've done to continue to embed technology enablement from an AI point of view into the ClearPath Forward ecosystem. We mentioned in particular the developer toolkit for AI that really allows for testing and utilization and I'll say bimodal data transfer has been really important. And we continue to develop the AV Suite to, again, allow for innovation and flexible deployment. So we see the technology continue to enhance the utilization of various aspects of AI in ClearPath. And, again, we've seen that result over the course of the last several years from enhanced consumption, and we see that trend continuing. So really happy with how it's shaping up. Starting to see a little bit of relief, I think, from the macros, which is, again, giving us confidence in our guidance as we said it.

Rod Bourgeois | Analyst, Deep Dive Equity Research:

Just to follow up on AI in your ClearPath Forward business, you've rolled out these new AI releases. Can you talk a little bit about the impetus to develop those AI releases and what the early client reaction is and even to the extent that you're partnering with the AI models on that? Just a little more color on the development of those releases and the reaction in the ecosystem. Thanks.

Mike Thompson | CEO and President:

Sure. Great question. Thanks, Rod. So, look, this is not something that we've picked up in the last three months in reaction to, you know, what's going on in the market. These AB suite releases have happened over the course of the last couple years. This is just the latest release that's going out there. You know, clearly there is an ask and roadmap discussions that we're having with clients, and it's really about, access to data, portability of data, continued consumption of data, and our ability to continue to build out above the, I'll say, the ecosystem layer or what you would consider the hypervisor layer or core layer of data and usage. I'll say the issue du jour there is really about maintaining the support and steady run of the base and utilizing the emerging technology. You know, you talk about frontier models as an example. being able to extract this valuable data that's embedded in the ecosystem and marry that to frontier models to really help our clients continue to take advantage of that data set and do that in a manner so that they're not putting at risk anything in the ecosystem, their run, the resiliency, the security, et cetera. So we see this as, you know, just a continuation of our ClearPath 2050 strategy and it happens to be the emerging technology that's there today, but we do a little bit and continue to work with kind of joint roadmapping on, you know, some of these providers. And it extends beyond Frontier, right? It's also OEM providers, you know, as well as some SaaS applications that sit on top of that ecosystem. So this, again, has been multi-years in the making. And I think from a client perspective, aligned to the expectations that we've set with our clients over the course of managing their roadmaps.

Rod Bourgeois | Analyst, Deep Dive Equity Research:

Thank you very much. Thanks, Rob.

Operator | Conference Operator:

Thank you. The next question we have comes from Mayak Tundin of Needham & Co. Please go ahead.

Mayak Tundin | Analyst, Needham & Co.:

Hi, guys. This is Brandon on from Mayak. And I'm just wondering, given a strong quarter, can you talk a little bit more about the reaffirmed guidance? Is that taking into account some macro uncertainty or buffer? And what are the levers that gets you to the high or low end of the guidance?

Mike Thompson | CEO and President:

Yeah, hey, Brandon, how are you? Thank you for the question. Look, I think, you know, obviously we've reaffirmed guidance. We talked about Q1 being a little stronger than expectations. Kind of early in the year to be thinking about the impact of that. Obviously our guides, constant currency, Deb mentioned in her prepared remarks some of the movement in FX. embedded in that. So we'll have more color in Investor Day around how that relates to whether we're maybe moving towards the higher end of that or where we sit from a guidance perspective. I guess the message that I would want to leave you with is we feel good about Q1. It's a little better than we expected. We assumed in our guidance, as we talked about when we said it, that no real changes in the macroeconomic environment, although it's maybe moving a little more favorably from a macros perspective, I wouldn't consider one quarter to be indicative of the full year. So when we get a little bit more visibility through Q2, clearly at investor day, and then obviously if not investor day at our Q2 earnings, we'll talk about what you know, kind of how we feel about that guidance range.

Deb McCann | Chief Financial Officer:

And to answer as far as some of the levers, I mean, it'll really, you know, the signing momentum, if that continues, and kind of the conversion timing. of that revenue and then, you know, field services volumes, those are probably drivers, you know, we'd be looking for.

Mike Thompson | CEO and President:

Yeah, and just to tie into that, I mean, as we've continued to enhance and improve our gross margin, you know, that we have a lot more control over, obviously, and continue to work our programs and execute against those programs. And then to Deb's point, as these things become revenue recognition in the year and we get to run rate on things that we've already sold and have started to implement. Uh, we're expecting some pull through on margin there as well.

Mayak Tundin | Analyst, Needham & Co.:

Um, great. Great. Thanks. And then you guys also mentioned some cross sale moments. I'm in the quarter. I'm just wondering how big of an opportunity that is for you guys and the dynamics of the cross sales, um, especially with current clients, upgrading it and infrastructure for these AI initiatives.

Mike Thompson | CEO and President:

Yeah, look, I think, look, in general, and I mentioned in my prepared remarks, one specific client where they had 100 applications sitting, you know, kind of on top of our ClearPath Forward ecosystem, and we're helping modernize those applications. And there's a great example of kind of that agentic action layer to modernize that. So we see that biggest cross-sell opportunity embedded in application modernization and and specifically agentic, I'll say agentic AI applied to that action layer, the more of that we see, the more of that we're able to accomplish. And, you know, I think the market's knee-jerk reaction a little bit on SaaS providers, et cetera, you know, we're not a SaaS provider per se, but we certainly, play in the area of supporting SaaS application as solution implementers on a SaaS side. And the ability to use that agentic layer, I think, opens up TAM for us to lean in more heavily in that arena. And the ClearPath Forward ecosystem application construct is really a great proof point of that. We've seen a couple instances of that recently, and we expect that that will continue.

Mayak Tundin | Analyst, Needham & Co.:

Great. Great. Thanks, guys. Thanks, Brandon.

Operator | Conference Operator:

The next question we have comes from Matt Desert of William Blair. Please go ahead.

Mayak Tundin | Analyst, Needham & Co.:

Hi, team. This is Matt on for Maggie Nolan. Congrats on the good results. Can I ask about the strong new business TCV? I think it was up 45% year over year. Strong backlog, too. I guess it's Doug, you touched on it a little bit, but how should we think about conversion timing and ramp periods as well as margin profile of these new wins and your ability to continue to win work at these improved margin levels going forward? Great.

Mike Thompson | CEO and President:

Thanks, Matt, for the question. So, yeah, super happy with the year-on-year uptick there. You know, we mentioned in our prepared remarks about these rapid value assessments Part of our strategy that we implemented at the tail end of last year and have carried through to Q1 this year is really looking at these point-of-spear opportunities and how emerging technology really avails itself not only in the AI embedded in our solutions, but the skills that we've got around that AI implementation and the conversion of technical debt. happy with that uplift. We're seeing some real success, you know, in the top end of the funnel as well. Clearly, the solutions are resonating with clients. Now, these RVAs or rapid value assessments are typically more point of the spear things and are typically a little smaller engagement as a means to open the door. So, we expect that, you know, the transition time will be faster. We also expect that much of that work is really more kind of time and material or outcome-based pricing so that we don't have the typical 18-month transition on some of those. And then it's really about the expansion post that RVA adoption is kind of what our focus is on top of that. So we think it'll be more volume, perhaps a little smaller value, right, of the actual deal because it's point-of-sphere oriented, but gives us a real jump-off point to expand to other aspects of the business. So, again, strong year-over-year TCV growth in that, as well as top of the funnel, you know, pretty happy and aligned to what our expectations were when we made those changes at the tail end of last year.

Deb McCann | Chief Financial Officer:

Yeah, you also asked about margin, and I just think, you know, it's mixed depending on kind of the solutions, you know, that we're signing. You know, I think we mentioned there are some DSFs have lower margins, right, but still are really good entryway into the client.

Mike Thompson | CEO and President:

Yeah, that's a great point, Deb. Thanks for chiming in there. Mix is exactly right, and if the TCD is coming from the RDAs, then they're probably – already at our accelerated margin profile, but as Deb mentioned, you know, a good chunk of that pipeline aligns as we talked about our DSS solution, which have a hardware mix in the solution itself, which kind of impacts the total margin of the contract, but not the services piece of our margin. Really, it's more the pass-through component of the hardware. But all in all, good line of sight, good progress. and feel like the strategy is taking hold.

Mayak Tundin | Analyst, Needham & Co.:

Got it. Thanks for that color. As a follow-up, can I ask about pricing and just consumption pricing? I think IBM discussed the evolution they're seeing in their mainframe platforms to account for MIPS and AI and additional consumption parameters. Are you doing something similar with your pricing in CPF, and how are you maintaining that? your deserved premium here while adapting to these changing market dynamics? Thanks. Sure.

Mike Thompson | CEO and President:

So great question. Look, the pricing discussions that we've had over the last probably four quarters were really pricing discussions as it pertains to XLNS. Your question obviously is LNS pricing. We have not really had pricing pressure on the L&S side. It is a premium service. Our clients view it as a premium service. We continue to get increased consumption out of that business, and most of that consumption increases really based on the comments that I made earlier around enabling the data sharing and testing and the like embedded in what's going on in L&S. Typically from an L&S renewal, as you know, Matt, the revenue recognition and that costing or pricing happens at deal signing, and it's usually for the entire duration of that deal, and it's up front from a perspective of usage or consumption. And we've been able to, over the course of the last five years, and don't expect this to change, get price increases on those licenses, as well as the support of that environment. So it's not really been pricing pressure at all on the L&S side of the business, and we're quite confident that that's going to continue.

Mayak Tundin | Analyst, Needham & Co.:

Great. Thank you.

Operator | Conference Operator:

Thank you. The next question we have comes from Anya Soderstrom of Siddhati. Please go ahead. Hi.

Anya Soderstrom | Analyst, Siddhati:

Thank you for taking my question. So AI seems to be a strong driver for you, but what kind of margin impact do you expect that to have?

Mike Thompson | CEO and President:

Hey, Anya. Thanks for the question. Look, I think we've been pretty consistent that The AI that we've embedded into enabling our solutions continues to have margin expansion and improvement. I think we were probably, what, Deb, almost 600 basis points over the last three years in XLNS. That is a byproduct of embedding that into our into our solutions clearly when we have a new logo and And they're utilizing the new solution immediately we get that impact immediately Through and and and we've talked about last quarter there as an example pushing our agentic service desk into the the entire legacy base of clients we should be about 40% of that base of using our agentic service desk by the end of the year. So we still have some improvements that we expect on margin beyond this year for the existing base, and we expect that we'll continue to offer this solution at an enhanced margin profile. So, you know, if I look at kind of where we are in the adoption of AI into our solutions, We're probably about halfway there in the existing base. And so, again, we're talking about, from our guidance, another 100 to 200 basis points of potential improvement on the XLNS side. And there should still be more in 27 as we continue to deploy our authentic offerings into our existing base.

Anya Soderstrom | Analyst, Siddhati:

Okay, thank you. And then can we just double-click on the opportunities you see with the field services?

Mike Thompson | CEO and President:

Yeah, so that's one we've been continually bullish on, as you know. And it really comes in three flavors. The embedding AI in the way we actually deliver our services from a field service point of view, i.e., location of the technicians, sending data to the technicians on the site, with next best case cause of issues, looking and using data to understand how to do preventive things while on site, et cetera. So that's kind of a base use case of traditional elements and how AI is enhancing that. The second and third I think are actually more exciting, right? One is around the different types of field service deployments. We talked about the work we've been doing on infrastructure and high-end storage and kind of moving up stack from a field service technician perspective. We talked in the prepared remarks around the data center work for installation and maintenance of things like liquid cooling for GPU chip configuration in a data center in general. And we also talked about the expansion of field services to other areas. In general, if you think about conference rooms, kiosks, office environments, et cetera, and the data telemetry around IoT devices and how that ultimately aligns to having a field service orientation. As you know, we're one of the few companies with the kind of global scale and reach from a field services point of view. And we think that that's a differentiator from our perspective. And the alignment of that to our agentic service desk, knowledge management, et cetera, and the skills that we've got globally in field service. We've been investing in that area for several years when I think you've seen a lot of the market kind of curtail some of their investment in that space. we're pretty excited about the opportunity it brings to us.

Anya Soderstrom | Analyst, Siddhati:

Okay, thank you. That was all for me.

Rod Bourgeois | Analyst, Deep Dive Equity Research:

Great. Thanks, Anya.

Operator | Conference Operator:

Thank you. The next question we have comes from Matthew Galenko of Maxim. Please go ahead.

Matthew Galenko | Analyst, Maxim Group:

Thanks for taking my question. I was just hoping you could expand a little bit more on the pipeline for field services around data centers and AI data centers. Thank you.

Mike Thompson | CEO and President:

Hey, Matt, thanks for the question. You know, I mentioned on my prepared remarks that we had won an engagement there. We've been in the hunt for a couple others as well. You know, there's billions of dollars being spent in that space, and our goal is to really have our associate base totally prepared to handle a significant volume as it pertains to data center construct, installation of, you know, racking in there, and obviously the component pieces around immersion cooling, liquid cooling, et cetera. So the pipeline has been, I would say, fairly strong. Our discussions with clients or prospective clients in that pipeline is going – I think, incredibly well. And we're happy about the fact that we are in the hunt for a whole host of opportunities there with some pretty significant players. So, you know, clearly the market awareness of our abilities and skills in that space is out there. And, you know, again, these deals take a little bit of time to materialize, but I guess what I would say to you is that we're certainly getting significant invites and that we've got really good opportunities in the pipeline to expand that opportunity for the company.

Matthew Galenko | Analyst, Maxim Group:

Thank you.

Mike Thompson | CEO and President:

Thanks, Matt.

Operator | Conference Operator:

The next question we have comes from Anna Goschko of Bank of America. Please go ahead.

Anna Goschko | Analyst, Bank of America:

Hi, thanks very much. I have a pension question. So Deb, you mentioned some charges to come later this year related to pension annuity purchases. And I know those purchases help to reduce the overall liability and then in the medium to long term also help to reduce the amount it's going to take to reduce the pension deficit. But it wasn't clear to me that you had already agreed to do the annuity purchases this year. I know those are cashless. So is that kind of a done deal, or is it still something that you're considering?

Deb McCann | Chief Financial Officer:

Yeah, no, it's not a done deal. It's still in our plans. As we laid out last year, we were going to do some annuity purchases. We did some last year. at the end of the year, and our plan was to do more this year, but it's not locked in. And that's why we don't know the exact amount of the charge. It'll depend on the timing. And so that's why, you know, as the year goes on and we get closer to locking that in, we'll give a sense of what that non-cash charge would be.

Mike Thompson | CEO and President:

Yeah. It's Mike. So when we talked about, even when we did the debt, we talked about roughly $600 million worth of pensions, annuities. I think we did debt like $375, something like that. And so this would kind of be the other half of that. You're right that it's cashless to us. As you know, we've done about six of these already. And so when we do them, you make an offer and then you get bids. And there has been high interest in those bids. Normally we get maybe four to seven folks bidding on that, and then it's really a matter of does the bid come through at a rate that we think is worth it from our perspective. So you're right, it is still a little bit market oriented, but our availability to do another one starts in Q3. And so we fully expect to put that offer out in Q3, and we fully expect that we'll get the same level of demand that we've gotten historically, and it really comes down to the economics of the rate.

Anna Goschko | Analyst, Bank of America:

Okay. Okay, great. Understood. And then secondly, I think I asked the same question last quarter, but the debt market has been just very messy for decades. software-related companies and IT-related companies generally. So that's kind of created an opportunity potentially for you to buy back bonds at an attractive rate. I know you've got uses for your liquidity, but you do have a strong liquidity position, so I think you bought back just a tiny bit of bonds in the quarter. and about $2 million, and just wondering if that's something that has continued after quarter end, or just, you know, kind of what your view is on basically tapping that opportunity.

Deb McCann | Chief Financial Officer:

Yeah, so we have, you know, windows where we can purchase, and you're right, we did in Q1 purchase, you know, an immaterial amount and, you know, at an opportunistic value, we feel, and so we'll continue to look at our liquidity, our cash, and you know, assess that as time goes on and as the windows open, you know, that allow us to do that. So we'll continue to keep an eye on that and see, you know, when the price is opportunistic, look at the overall liquidity picture and make that determination.

Anna Goschko | Analyst, Bank of America:

Okay. Okay, great. Well, thank you.

Deb McCann | Chief Financial Officer:

Great.

Operator | Conference Operator:

Thank you. The final question we have is a follow-up from Rod Bourgeois. Please go ahead.

Rod Bourgeois | Analyst, Deep Dive Equity Research:

Yeah, hey, I thought I would just ask, in the public services, you had some delays with the government shutdown and some other decision challenges there. The question is, is that starting to turn? And then similarly on PC refresh, is that also at a point where you should see some upside there as well, or is there still a little bit of a wait and watch going on? Just those updates would be helpful. Thanks.

Mike Thompson | CEO and President:

Sure. Thanks, Rod, for joining back in here. Look, I would say in general, public sector has been more favorable than it has in previous quarters. And I would throw higher ed in that same viewpoint. I think some of the noise has started to settle down and some of that project work is starting to return. So again, I wouldn't say A quarter or a quarter and a half is indicative of the future, but I'm encouraged by what we're seeing as far as the loosening of the belt a little bit here and getting back to a little bit more normalcy in that space. I think they also recognize that in many cases there are significant laggards from a technology perspective. And the utilization of the emerging technologies, specifically this influx of these agentic AI models, can help leapfrog them and get them not only up to date from a technical debt perspective, but catch them up for perhaps multi-year lag effects. So that's been, I think, pretty positive in the market. And then as far as your comment on PC refresh, yes, we saw a little better than expected in Q1. Again, I'm hesitant to say that that is a byproduct or that's going to just continue throughout the remainder of the year, but there are certainly some elements that would suggest that it should, specifically as we talk about the Microsoft licensing component, et cetera. And again, we're coming up against comps of a pretty low year. But I would remind you that, at least for us, the reliance on that refresh cycle is less, and we continue to train and educate the workforce on the infrastructure component of the field services arm that is impacted by those PC refreshes. We've extended that IoT devices to go beyond PC refresh, so it's an important factor, but, you know, when we set our guidance, we expected it to be pretty flat and maybe even still a little declining, and it's actually performed a little better than our expectations.

Rod Bourgeois | Analyst, Deep Dive Equity Research:

Thank you, Gus.

Mike Thompson | CEO and President:

Thanks, Rod.

Operator | Conference Operator:

Thank you. Apologies. The final question we have comes from Sean Parkins of Deutsche Bank. Please go ahead.

Sean Parkins | Analyst, Deutsche Bank:

Hey, guys. Thank you for the call and for the results. I'd like to dig into a little bit more about the data center opportunity that you highlighted to some of the work you have there. Perhaps if you can discuss maybe some of the clients that you're seeing engage with you in those arenas, and then what the go-to-market strategy for your business is there to think about the market opportunity size? Thanks.

Mike Thompson | CEO and President:

Well, thanks, Sean, for the question. I'm not really at liberty to share actual client names, but I would say to you that obviously we're engaged with the OEMs in regards to that, and they're an entryway into the some of these clients and I would say at least for a couple in the pipeline, you know, it's kind of the who's who in that space. So we feel really, again, privileged that those types of clients are engaging with us to talk about the installation and maintenance of such a high profile investment for them, you know, and Again, there are billions of dollars, as you know, being spent in this space. We think there's a really big dam. And we've been using this, I'll say, period of the last 12 months to really make sure our workforce is trained up on the utilization of this new technology, not only on how to deploy it, but clearly the The implementation of racking and cabling and immersion cooling is a pretty technical aspect. And so the recognition of our capabilities to do that puts us in really good stead. And, again, I would just say that, you know, we're talking about some major OEMs and major players in data center build.

Sean Parkins | Analyst, Deutsche Bank:

Thanks. Look forward to hearing more about it at the investor day. Thank you.

Operator | Conference Operator:

Thank you. Ladies and gentlemen, that then concludes today's conference. Thank you for joining us. You may now disconnect your lines.