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Conduent, Inc. (CNDT)

Q4 2019 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good day, and welcome to the Conduent Fourth Quarter 2019 Earnings Call and Webcast. All participants will be in listen-only mode. [Operator Instructions] After today's presentation, there will be an opportunity to ask your questions. Please note this event is being recorded.

I would now like to turn the conference over to Alan Katz, Vice President of Investor Relations. Please go ahead.

Alan Katz

Vice President-Corporate Finance & Investor Relations, Conduent, Inc.

Good evening, ladies and gentlemen, and welcome to Conduent's fourth quarter 2019 earnings call. Joining me on today's call is Cliff Skelton, Conduent's CEO; and Brian Walsh, Conduent's CFO. Following our prepared remarks, we will take your questions. This call is also being webcast. A copy of the slides used during this call was filed with the SEC this afternoon. Those slides, as well as a detailed financial metrics sheet, are available for download on the Investor Relations section of the Conduent website. We will also post a transcript later this week.

During this call, Conduent executives may make comments that contain certain forward-looking statements as defined in the Private Securities Litigation Reform Act of 1995 that by their nature address matters that are in the future and are uncertain. These statements reflect management's current beliefs, assumptions and expectations as of today, February 20, 2020, and are subject to a number of factors that may cause actual results to differ materially from those statements. Information concerning these factors is included in Conduent's Annual Report on Form 10-K filed with the SEC.

We do not intend to update these forward-looking statements as a result of new information or future events or developments, except as required by law. The Information presented today includes non-GAAP financial measures. Because these measures are not calculated in accordance with US GAAP, they should be viewed in addition to and not as a substitute for the company's reported results prepared in accordance with US GAAP.

For more information regarding definitions of our non-GAAP measures and how we use them, as well as limitations as to their usefulness for comparative purposes, please see our press release, which was issued this afternoon and was furnished to the SEC on Form 8-K.

With that I will turn the call over to cliff for his prepared remarks. Cliff?

Cliff Skelton

Chief Executive Officer & Director, Conduent, Inc.

Thank you, Alan. Good afternoon, everyone. Welcome to our Q4 2019 earnings call. I'll start today with a quick overview of the Q4 and full year highlights and we'll then discuss the results of our strategic and operational review. Brian will provide more detail on the financial results and will go over 2020 guidance and we'll close with some Q&A.

We achieved revenue for the full year at the top end of the range and adjusted EBITDA right near the mid-point of that range based on the guidance that we set when I started as CEO. Despite signings for the year being weaker than we would have hoped we're seeing very strong initial signings performance in Q1. January new business signings came in stronger than anticipated. While these may be early signs of increased client confidence, it's still too early to call it more than the beginning of our turnaround journey.

Before we turn to the results of the strategic review I want to point out some additional operational highlights. Last quarter we announced the launch of our three-pronged systemic transformation program with a focus on growth, efficiency and quality of delivery. This has and will result in a series of both tactical and strategic projects and is ubiquitous across all of our businesses and products.

The framework will be used as the execution arm for our strategic and operational review focus areas. Some early efforts produced some quick wins. We improved IT and delivery performance resulting in quality improvements for our clients and their end users. We're beginning to see positive proof points in client satisfaction as well indicated by both anecdotal feedback and our Net Promoter Score rating. These are simply early signs and have not yet developed into consistent trends.

We brought on several senior people to help drive change and help us in our transformation initiative as part of our talent rebuilding efforts. In addition to our new Chief Information Officer and Chief Revenue Officer, we've added a new Head of HR and a new General Counsel and several key General Managers among others. We're driving increased engagement with our associate base and developing a culture that prioritizes client satisfaction, teamwork and performance, intended to result in significant improvements in both client and associate retention.

We also completed a strategic and operational review. The result of the review is a clear plan to invest in our business for revenue stabilization, margin expansion and efficiency opportunities in certain businesses and expansion opportunities in others, which we believe will result in growth via retention and new business signings. We have segmented the offerings into three categories which I will go through in detail in the next slide.

As discussed in previous earnings calls, we believe that a possible divestiture could be a component of improved near-term shareholder value and should be part of our strategic consideration set. As part of the review we considered divestitures including inbound inquiries and utilize tight criteria to see selling a business, even a business we feel great about would create more shareholder value through disposition than it would by retaining.

While we will continue to be opportunistic we do not necessarily need a divestiture to drive meaningful shareholder value which is our goal. We believe our current portfolio coupled with our transformation efforts and improved leadership will position us well over time to drive both top line and EBITDA growth.

Now, let's move to the details of the strategic review on slide 4. As we mentioned in the past two earnings calls, we undertook this review to determine where to focus our investments into the business and to maximize our value proposition. Given our performance in the current valuation assigned by the market, we spent six months completing a thorough analysis and evaluated each of our lines of business to ensure that go-forward Conduent would be well positioned for success.

We took a hard look at what has and has not worked since our spin. We looked at areas that would benefit from different processes and areas that would benefit from investment. We will invest to build stronger offerings and to take advantage of industry trends, and to optimize or enhance other offerings to increase cash flow and to stabilize revenue. This investment will strengthen our portfolio and position the company well for the future.

In terms of funding the transformation we expect to generate meaningful operating cash flow in 2020 and have cash on hand, both of which we can use to fund capital expenditures. We also have a strong balance sheet with an undrawn revolver and reasonable debt leverage ratios. We will continue to consider possible future divestitures or other funding options as well.

Now let's turn to slide 5 to discuss our strategy for the go-forward company. Regarding the spectrum of assets currently within the company we have offerings where we can, first, drive optimization to increase retention into our margin, thus improving productivity and creating better outcomes for our clients. Second, we have solutions and services where we can retain and grow through product enhancements. And lastly, offerings where we can invest a more meaningful amount to expand into current and adjacent markets leveraging new technologies.

The optimize businesses are generally areas of significant scale where we believe that with process improvements, automation, and technology consolidation we can improve the end user experience, reduce our cost of delivery, expand our margins, retain more clients and capture additional volume share. The businesses where we see the potential to enhance our solutions in market share with modest investment tend to have strong client relationships and a long history of servicing the markets we operate in. However, we have technology that needs to be refreshed or modernized.

Lastly, in the areas of the business where we see opportunities to expand our capabilities may require a more meaningful investment but we see the payback is significant. These businesses augmented with new capabilities perhaps supplemented by modest acquisitions will address market dynamics and provide additional growth opportunities.

I'll now provide a quick example of an expansion business and an optimize business.

We've identified healthcare as an expansion opportunity. We've significant scale across the entire healthcare ecosystem of insurance companies, healthcare providers, third-party administrators, pharmaceutical companies and employers who provide health insurance for their employees. We currently leverage our core capabilities to provide services across the healthcare universe.

We provide medical bill review and payment integrity services to 9 of the top 10 health insurers. We offer patient support and clinical trial administration services to 8 of the top 10 pharma companies. We also process over 28 million medical bills each year saving our clients billions of dollars per year. This is tremendous scale in a market that is projected to grow more than 5% annually.

We see an opportunity to leverage our current offerings, bundle existing services and create unique value-add insights and analytics and transact up and down the process value chain to capture competitive market share.

On the other side of the spectrum transaction processing as an example is currently a fairly labor intensive and lower margin business with more challenged secular trends. However, this business provides core capabilities that are critical to commercial and government organizations alike. We believe that with an investment into our solutions and by leveraging AI and machine learning tools we can automate data entry and intake thus creating higher quality, more consistency and lower cost.

These are just two examples of how we're thinking about allocating capital into the business. Along the way is not just what we intend to deliver in order to grow, become more efficient and deliver quality, but it's also how we will deliver. We have established a transformation program focused on disciplined program management to prioritize and sequence both our systemic efforts but also the business specific optimize, enhance and expand efforts. This program will allow for better measurement, governance, execution oversight and capital allocation.

Let's turn to slide 6 to discuss how we will manage and measure success for this transformation. With the aforementioned strategy as the backdrop we have begun to launch a series of projects with increasing levels of investment as funding increases to grow, become more efficient and increase quality. The bellwether metrics necessary to measure the success of these projects will be top line shifts in revenue client and associate retention, reputation and referenceability in the marketplace, improved quality metrics and improved margins.

In some cases these projects will simply enable us to better operate what we have. And in some cases a project or investment will produce a brand new or enhanced product suite. In all cases, our mission is to govern and execute a project-oriented, fully-funded, pivot-to-growth game plan. We will have more to share on specific project examples in subsequent earnings calls.

Finally, people and talent matter a lot. In addition to hiring a new Head of Human Resources, we will soon assign a senior leader to be uniquely focused on associate attrition and engagement. We will implement better and different hiring practices, focused workplace initiatives and endeavors important to our teammates so as to retain and motivate thus improving client relationships. As we see attrition decline employee costs should also come down, bringing up cash to invest back into the business.

We're tracking all of these initiatives with clear and measurable metrics and KPIs. These measurements will be incorporated into our reward and recognition programs. Overall, I am encouraged and motivated to see this through to completion. It is time to execute what we have planned and complete the project planning and funding allocation for the rest. We believe that we have the right strategy and will soon have all the right people in place to win.

I'll now turn the call over to Brian to provide an overview of the financials and our outlook for 2020 beginning on slide 8. Brian?

Brian Webb-Walsh

Chief Financial Officer, Conduent, Inc.

Thank you, Cliff. Before I begin I'll note that throughout this presentation and in the exhibits in the appendix we will provide both GAAP and adjusted numbers which will provide a clean compare by removing the impact of the divestitures that we have completed.

Let's start on slide 8 with an overview of the full year financial results. As Cliff mentioned we ended the year with revenue and adjusted EBITDA in line with our guidance ranges. Adjusted revenue for the year, which excludes completed divestitures, was $4.4 billion down 4.5% compared with full year 2018. On a constant currency basis adjusted revenue was down 4% and at the top end of our guidance range.

Declines were driven primarily by lost business in our commercial and government sectors, price pressure from renewals in our commercial and government sectors and volume pressure in the commercial business. These impacts will partially offset by growth from new business in the transportation sector.

Adjusted EBITDA for the year, which also excludes the impact from completed divestitures, was approximately $493 million, down 7.9% compared with full year 2018 and at the mid-point of guidance. Full year adjusted EBITDA margin was a 11.1% representing a 40-basis-point reduction year-over-year. Year-over-year declines in full year adjusted EBITDA were driven by lower revenue, partially offset by efficiency programs and cost savings in IT, real estate and other corporate spend.

Operating income for the year was a loss of approximately $2.1 billion, primarily driven by goodwill impairments including an impairment in Q4.

Let's move on to our segment summary on slide 9. Commercial revenue for the year came in at $2.4 billion, down 6.5% for the year and down 5.8% in constant currency. These declines were primarily driven by lost business, volume challenges with a few large customer care clients and price pressure associated with one large renewal.

Commercial adjusted EBITDA for the year was $542 million, down 9.4% for the year. This was driven by revenue pressure, partially offset by reduced labor, IT and real estate spend. Adjusted EBITDA margins were 22.7% down 80 basis points.

Government revenue for the year was $1.3 billion, down 6.5% for the year while adjusted EBITDA was $423 million down 6.2% for the year. The revenue and adjusted EBITDA declines were primarily driven by lost business and price pressure from a large renewal we had earlier in the year. Adjusted EBITDA margins for the segment were 33.5%, up 10 basis points when compared to full year 2018 results. Transportation revenue for the year grew to $781 million, which is up 7.1% or 8.2% in constant currency. This increase was primarily driven by new international transit business and increased domestic tolling volumes. Adjusted EBITDA for the segment was $157 million, up 5.4%, primarily driven by revenue growth. Adjusted EBITDA margins for the segment were 20.1%, down 30 basis points compared to 2018. Unallocated shared infrastructure and corporate costs for the year were $629 million. This represents a 3% year-over-year decrease due to reductions in corporate function spend.

Let's now turn to slide 10 to discuss quarterly and full year cash results. Our balance sheet continues to be healthy with $505 million in cash at the end of the fourth quarter. Our current net leverage ratio came in right around our target at 2.1 turns and our revolver remains undrawn with approximately $667 million of capacity available as of December 31.

Q4 operating cash flow and adjusted free cash flow were both strong year-over-year but felt short of our expectations driven by the timing of a few items and higher CapEx. CapEx spend was $57 million for the quarter or 5.2% of revenue and was $215 million for the year or 4.8% of revenue. CapEx came in $9 million lower than 2018. However, as a percent of revenue CapEx was about 60 basis points higher. Adjusted free cash flow was an inflow of $293 million in the quarter, $34 million better than the same quarter in 2018, driven by working capital actions and quarterly timing. Adjusted free cash flow for the year was $57 million or $161 million worse than full year 2018. This is largely due to lower EBITDA, some non-cash items that are benefiting EBITDA but not cash flow and the timing of some transition service agreement payments. Our adjusted free cash flow excludes the impact of the $118 million in payments we made in 2019 related to the Texas litigation settlement. We recently made the final $118 million payment in January. This payment along with normal working capital fluctuations will bring the cash balance down in Q1.

Before we get to our 2020 guidance I'd like to provide some updates on our key sales metrics for the year and the quarter on slide 11. Our renewal rate for the quarter was 76%. The contributors to the lower renewal rate are the loss of an end-user experience contract and a medium-size tolling contract. The renewal rate for the full year was 81% below our target of 90%, of that the impact of the California Medicaid contract was approximately 5 percentage points. New business TCV signings for the quarter were $209 million down year-over-year. While new business signings for the quarter were low, it is also important to note that we had a difficult compare as we signed our largest new business deal for the year in Q4 of 2018. While the Q4 signings numbers are disappointing, as Cliff mentioned, we had a strong start to the year and we expect Q1 2020 new business signings to grow both quarter-over-quarter and year-over-year. A large part of this success will be attributable to our end-user experience team winning a four-year $90 million contract to support a former client. We plan to quickly ramp this contract to revenue and we are encouraged to see a former client returning.

Let's move on to discuss the pipeline. I'll note that we have included the total new business pipeline in addition to the rolling 12-month pipeline. Moving forward we'll focus on the total view of the new business pipeline. Movements of RFPs and deals flowing out of the 12-month window can create what seems to be more volatility than what we are actually seeing in reality. Nonetheless, with both pipeline definitions we are beginning to see a stabilization. As of the end of the quarter our total new business pipeline was $21 billion representing a 15% increase from the same quarter in 2018. We are encouraged to see some signs of progress in Q1 as we transform our sales organization, our sales head count is currently at its highest levels since Q2 as we begin to hire and attract new talent.

Let's move on to slide 12, to discuss guidance for 2020. Our 2020 guidance is consistent with the preliminary outlook we provided last quarter. For 2020 we estimate revenue will be down between 6% and 8% at constant currency. We expect adjusted EBITDA margins to be relatively flat at the mid-point of our range which is between 10.5% and 11.5%. We expect the calendarization margins to be down 50 basis points in the first half of the year and up 50 basis points in the second half of the year at the mid-point of guidance.

Lastly, we expect to convert 15% to 20% of adjusted EBITDA into adjusted free cash flow in the year. This conversion rate is being impacted by an additional payroll cycle in 2020.

Before we move on to Q&A. I'll note that our guidance excludes any incremental growth investments as a result of the strategic review. As Cliff discussed, we see some very attractive investment opportunities within the business but we're still in the planning phase. We plan to update our outlook as we fund these high-ROI investment opportunities. We have made some great initial progress in the next phase of our transformation and I am looking forward to continuing to show progress in the quarters to come.

We will now open up the lines for some questions. Operator?

QUESTION AND ANSWER SECTION

Operator: Thank you. We will now begin the question-and-answer session [Operator Instructions] Our first question will come from Puneet Jain with JPMorgan. Please go ahead.

Puneet Jain
Analyst, JPMorgan Securities LLC

Q

Hi, there. Thanks for taking my question. And I think the growth approach, Cliff, that you shared makes sense. But given that you have all the businesses in there, should we view this as like a move-away from potential divestments?

Cliff Skelton
Chief Executive Officer & Director, Conduent, Inc.

A

I think as I mentioned in the narrative, Puneet – first, thanks for your question. But as I mentioned in the narrative we want to maintain optionality for sure. When we look at possible divestitures as a way to increase shareholder value, it was a pretty simple math equation, if you will. In other words, we looked at the salability of the asset minus a disentanglement cost, minus the tax implications or tax leakage. We wanted to compare that to what we could do internally to grow that particular asset, and of course all assets are not created equal. But what we wanted to do to grow that particular asset and what we're finding at least at this stage, and I want to reemphasize, at this stage, we see our ability to grow the asset set that we have compartmented the way I described in the narrative as a way to create shareholder value more readily than with selling the asset. But we want to remain opportunistic in that examination [indiscernible] (00:22:59) process for sure.

Puneet Jain
Analyst, JPMorgan Securities LLC

Q

Got it. And will you share like revenue growth, margins of some of those individual businesses and in each of – one of those three buckets so we can track how you're doing versus your goals there?

Cliff Skelton
Chief Executive Officer & Director, Conduent, Inc.

A

Yeah, absolutely. As we get this – we've begun to stratify those businesses as I said into the optimize, enhance and expand kind of buckets, and what we see is the investment kind of goes 30-30-40, if you will, as a percentage of the investment dollars, 30%, 30% and 40%, left to right. I wouldn't say that the margins – certainly the margins in the – in the optimize businesses are lower and that's where some of the opportunity is. But we would be happy to share that on a go-forward basis as we develop – as those projects are clear with respect to business cases, timelines and returns, but...

Brian Webb-Walsh
Chief Financial Officer, Conduent, Inc.

A

Yeah. We would look to – in our metrics file include a cut of the data based on those businesses on a go-forward basis.

Puneet Jain
Analyst, JPMorgan Securities LLC

Q

Got it. Got it. And quickly, I know Brian you said like 1Q new bookings will improve on both sequential as well on a year-on-year basis, driven by a win – $90 million win. Should we expect like the underlying momentum to improve throughout the year as sales and operational investments begin to generate returns or Q1 will be like a one-off case driven by one large deal.

Cliff Skelton A
Chief Executive Officer & Director, Conduent, Inc.

Yeah. Puneet, this is Cliff. I'll sort of answer that one. I would say, we do expect Q1 to be strong. The quotas are somewhat linear. And if we continue to see the performance in Q2 and Q3, we see the output in terms of new bookings to be somewhat linear as well. But it can turn lumpy, but right now we see it to be somewhat linear.

Puneet Jain Q
Analyst, JPMorgan Securities LLC

Yeah, no, agree – agree, like bookings can be lumpy, but...

Cliff Skelton A
Chief Executive Officer & Director, Conduent, Inc.

Yes.

Puneet Jain Q
Analyst, JPMorgan Securities LLC

...the underlying momentum should improve it seem like...

Cliff Skelton A
Chief Executive Officer & Director, Conduent, Inc.

Absolutely. Absolutely. Now, I understand your question. That's right.

Brian Webb-Walsh A
Chief Financial Officer, Conduent, Inc.

We expect to deliver year-on-year growth this year for the full year. It could be lumpy by quarter, but we're off to a strong start.

Cliff Skelton A
Chief Executive Officer & Director, Conduent, Inc.

That's right.

Puneet Jain Q
Analyst, JPMorgan Securities LLC

Got it. All right. Thank you.

Cliff Skelton A
Chief Executive Officer & Director, Conduent, Inc.

You bet. Thank you.

Operator: Our next question will come from Shannon Cross with Cross Research. Please go ahead.

Shannon Cross
Analyst, Cross Research Group
Q

Thank you for taking my question. I'm curious can you give us some idea of the size of the incremental investment that you think you will be making since it's obviously not necessarily included in the numbers, and maybe a little bit more specific as to where you will be targeting that investment. And then also sort of as a follow-up, how are you thinking about the need to refinance some of the debt that's coming due in 2022, 2023, just if you can give us an idea of how you're thinking about approaching that, you have some time, but it's always good to be prepared, so thank you.

Brian Webb-Walsh
Chief Financial Officer, Conduent, Inc.
A

Yeah. Okay. Thanks, Shannon. So, we're still in the planning phase of prioritizing and sequencing the incremental investment but we're earmarking approximately $100 million to $200 million over two-and-a-half years, and it would likely start in the back half of this year. We're working still internally on this and with our board. We'd expect about 25% to be OpEx and 75% to be CapEx or restructuring. And once we're through the process we will provide an update to our guidance if necessary. But if we just did the math and all of that it would be between 5% and 10% of incremental OpEx potentially this year and 15% to 30% of incremental CapEx and restructuring this year, if the math was linear but again we're still working on it.

And from a debt maturity perspective, the term loan A and revolver mature in 2022 – in December of 2022 and the term loan B matures in December of 2023. So, we still have some time but we'll start early next year looking at our refinancing opportunities and obviously we want to do it well in advance of the maturity dates.

Shannon Cross
Analyst, Cross Research Group
Q

Thank you.

Cliff Skelton
Chief Executive Officer & Director, Conduent, Inc.
A

Thanks, Shannon.

Operator: Our next question will come from Bryan Bergin with Cowen. Please go ahead.

Jared Levine
Analyst, Cowen & Co. LLC
Q

Hi, yes. This is actually Jared Levine on for Bryan. So, first can you kind of discuss your outlook for growth across transportation, commercial and government for fiscal year 2020?

Brian Webb-Walsh
Chief Financial Officer, Conduent, Inc.
A

Sure. So, I'll just talk compared to kind of the trends we saw in 2019. So, in 2020 we anticipate the transportation growth will dampen as we lap some new business contracts that were ramping last year and as the tolling loss that we referenced in our renewal rate rolls off. In government, we anticipate more pressure likely to be down over 10% revenue decline as we get the full year impact of CA-MMIS, California Medicaid contract rolling off. And then for commercial, revenue was down about 6% year-over-year constant currency in 2019, and we anticipate better performance and that decline moderating in 2020 as we get the impact of new business and we lap some of our losses in the prior year. And then just on margins, we expect margins for the segments to be flat to slightly up as we offset the revenue declines overall with efficiency improvements.

Cliff Skelton
Chief Executive Officer & Director, Conduent, Inc.

A

And within our transportation business...

Jared Levine
Analyst, Cowen & Co. LLC

Q

Got it.

Cliff Skelton
Chief Executive Officer & Director, Conduent, Inc.

A

Within our transportation business as you know there is really four sub businesses, they really not all created equal in terms of the dampening or the growth in some are growing quite handsomely, others are growing a little more slowly or somewhat dampened.

Jared Levine
Analyst, Cowen & Co. LLC

Q

Got you. And then when it came to potential divestitures are there any potential challenges resulting from other notable BPO assets for sale specifically in state and local health?

Cliff Skelton
Chief Executive Officer & Director, Conduent, Inc.

A

No. We had many inbound inquiries across the spectrum of our asset set and we found really no – no showstoppers or speed bumps anywhere in there. As I said earlier, it was more of a what – what we think we can do internally versus what those assets [indiscernible] (00:29:20) on the market and we like what we have in-house.

Jared Levine
Analyst, Cowen & Co. LLC

Q

Okay. Great. Thank you guys.

Cliff Skelton
Chief Executive Officer & Director, Conduent, Inc.

A

Thank you.

Operator: Our next question will come from Mayank Tandon with Needham. Please go ahead.

Mayank Tandon
Analyst, Needham & Co. LLC

Q

Thank you. Good evening. Maybe for Cliff or Brian, just given the ongoing churn in the business and the portfolio what is the level of visibility to the guidance that you provided on revenue? And then also, Brian, maybe you could talk a little bit about the trend line of revenue over the course of the year. You did talk about some of the seasonality on margins but it would be helpful to get a sense of how the revenue will trend over the course of the year as well.

Brian Webb-Walsh
Chief Financial Officer, Conduent, Inc.

A

Okay. Thanks, Mayank. So we have visibility to the mid-point of our guidance and it aligns with our internal plans, our internal budget targets. We still have work to do on the new business side that will drive revenue in the current year. But we're comfortable with the guidance range we've given and we think the Q1 new business signings that we believe we'll see is a good indication of kind of a strong start to the year on bookings. And then as you think about revenue as it progresses through the year we will see – we believe we will see the revenue decline as we get into the last quarter, maybe Q3 moderate a bit as we get more impact from new business.

And then just to add as we think about next year and get into 2021, we believe we can improve significantly the rate of decline and maybe even deliver flat revenue if everything goes as planned, and then we would see growth turning in 2022.

Mayank Tandon
Analyst, Needham & Co. LLC

Q

Great. So on that note, what level of bookings would you have to see this year. And not to put you on the spot but just maybe a sense of the growth in bookings or a dollar number that you have in mind that you could share with us that you would need to generate this year to be able to generate flat revenue in 2021 potentially – or at least show improvement relative to 2020.

Cliff Skelton
Chief Executive Officer & Director, Conduent, Inc.

A

That's a great question, Mayank. The way I look at it is growth flat in 2021 and growth in 2022 is – resonate in both retention as well as bookings. Now we expect bookings this year to be significantly improved from last year, 160%, to be more explicit as what we – what – is what our targets would say. And if we achieved that and – well, that's a little bit of a wag because it kind of depends on expansion versus new bookings. But look what we know we need is a reduction in losses coupled with those bookings to achieve the goal. And so if we stay consistent with what we are on track to achieve and – in 2020 and achieve that again next year with very slight or modest improvements we're going to be where we need to be.

Mayank Tandon
Analyst, Needham & Co. LLC

Q

Okay. And final question on margins. Maybe, Brian, the puts and takes on margins I realized revenue is going to be the key for margin expansion over time, any – I think you want to call out in terms of margins that can provide some color in terms of how we should expect that to run over the course of the year.

Brian Webb-Walsh
Chief Financial Officer, Conduent, Inc.

A

Yeah. First I would say on margins, we have to deal with the revenue decline and we also have to bring back some employee costs that we didn't have last year because of the performance, and so those things will be offset by efficiency drivers that they we're doing in automation, some of the things we'll do in the optimize businesses and in the corporate functions, in our real estate and IT portfolios to drive savings, but they'll be offset by those other issues. And then as we see margin progress through the year, again in my prepared remarks will be down we believe in the first half at the mid-point of guidance about 50 basis points and then up 50 basis points in the second half.

Mayank Tandon
Analyst, Needham & Co. LLC

Q

Okay. Great. That's helpful color. Thank you, guys.

Cliff Skelton
Chief Executive Officer & Director, Conduent, Inc.

A

Thank you.

Operator: [Operator Instructions] Our next question will come from Ashwin Shirvaikar with Citi. Please go ahead.

Ashwin Vassant Shirvaikar
Analyst, Citigroup Global Markets, Inc.

Q

Thank you. Hi, Cliff. Hi, Brian.

Cliff Skelton
Chief Executive Officer & Director, Conduent, Inc.

A

Hey, Ashwin.

Ashwin Vassant Shirvaikar
Analyst, Citigroup Global Markets, Inc.

Q

So the question is – hey – the question is with regards to sort of the transformational pillars chart that you guys put up. And I'm wondering how is this may be different than some of the initiatives that have happened over the past few years in terms of getting [ph] very disciplined (00:33:58) offering development, go-to-market repositioning – process improvements, some of those kind of things seem to be more of the same. Maybe there's a nuance that I'm not necessarily understanding but if you don't mind kind of going through how is this different than before?

Cliff Skelton
Chief Executive Officer & Director, Conduent, Inc.

A

Yeah. Happy to Ashwin. So in previous endeavors here the focus was primarily in the technology space and finding ways to frankly get a lot of efficiency through consolidation of hardware and upgrading of hardware, and in some cases building out some new software and capabilities. My view would be that we didn't always put the right people in process, efforts in play to enable the utilization of those technology investments. This is a very different approach. It's not only a very different approach to execution, but it's a very different approach to where we intend to spend the money.

We looked at it from two different angles. One angle is the systemic pain points across our sales-to-service continuum and where there are hurdles to success, whether it's solutions architecture or go-to-market plan, or certain specifics in our sales or operations. We've identified pain points and we've identified solutions for those pain points that will result in projects, that's part one. Part two is that will be juxtaposed against the business categorization that I mentioned earlier in the narrative where in some cases the business needs are simply more around making a business unit more efficient and driving margins up, in some cases in order to retain clients it's simply a tweak to that to the technology to make sure that we're delivering what we've promised. In other cases there's new opportunities to enhance and go up and down the value chain with a product where we can steal market share. Those were all different approaches, it wasn't that we didn't have business cases before we did, but the follow-through of those business cases weren't quite as rigorous as we thought before.

And then finally the execution of the – and follow-through of the project set is a very different program. We have an enterprise project management office now, we didn't have that before. It's cross-functional but led by the business units, we didn't have that before. We have inspection routines, metrics. It's a completely different environment than we had before. And the efforts are quite different as well.

Ashwin Vassant Shirvaikar
Analyst, Citigroup Global Markets, Inc.

Q

Got it. Got it. And the chart on Conduent growth approach with the optimize, enhance and expand buckets, and I find that quite useful in terms of how to think of the business, it seems to correspond to how I think of your business as well. Am I maybe reading too much into it when I – if I maybe say that the optimize book, it is one, where maybe you have the most problems and hence you're – problems with regards to growth, so you're more focused on margins, your transportation and commercial healthcare offerings might be more developed. Is that a fair way to look at it? Little bit more color on how you arrived at these might be useful.

Cliff Skelton
Chief Executive Officer & Director, Conduent, Inc.

A

Yeah. No, I would not characterize it the way you did necessarily. The way I would characterize it is in the optimize business, think of those as businesses where we don't need a new product to win. The products are fine. What we need is more efficient capabilities. We need to put in AI and machine learning and self-service and fewer process handoffs. And with that we drive value to both our clients and to our margins. We don't – it is not a rebuild, it's a refinement.

The second bucket, the enhancement bucket is, these are business units and products and offerings where our clients are telling us, look in order to retain us, in order to grow more with us, you need to do some tweaks to your technology offerings and modify them to make sure you stay up with the market if not get ahead of the market. And so that's quite a different model.

And then the third model is, in the value chain of a particular capability take claims, for example in the healthcare space, up and down the value chain and the process flow, there are opportunities to take market share away from the competition if we had a different product. And so we're looking – that would be an example of an expand business unit. So, very different. But I would not characterize the optimize businesses as problem businesses at all but more like improvement or optimize or drive margin or sort of simplify kinds of businesses.

Ashwin Vassant Shirvaikar
Analyst, Citigroup Global Markets, Inc.

Q

Got it. That seems to – good to hear. And if I could squeeze one more in and just maybe – maybe just building on a previous question, you have down 6% to 8% rev projection, you're basically still keeping margins flattish which is an accomplishment. I mean, what do you need to see in terms of revenue growth from a exit perspective to make maybe margin improvement in 2021 a believable target?

Brian Webb-Walsh
Chief Financial Officer, Conduent, Inc.

A

So, in the next year or two our focus is going to be to turn revenue around and to make the right investments, and so we actually see margin relatively range bound for the next couple of years as we prioritize revenue. And as we start to get revenue – as we start to get revenue growth, that's when we'll be able to see margin improvement. In long term, we see no reason this business can't get to a 15% margin which we view as industry average, but in the meantime we need to focus turning around the top line and making the investments in the business.

Ashwin Vassant Shirvaikar
Analyst, Citigroup Global Markets, Inc.

Q

Understood. Thank you.

Cliff Skelton
Chief Executive Officer & Director, Conduent, Inc.

A

Yeah. And as you know Ashwin, a lot of sins can be forgiven if we grow top line with respect to margin. So that's the – that's mission number one. So that's where we're going.

Ashwin Vassant Shirvaikar
Analyst, Citigroup Global Markets, Inc.

Q

Yeah. Absolutely, absolutely. Thanks.

Operator: This will conclude today's question-and-answer session. I would like to turn the conference back over to Cliff Skelton for any closing remarks.

Cliff Skelton
Chief Executive Officer & Director, Conduent, Inc.

Well, thank you all for listening today. We're in a quite exciting time here at Conduent, and we certainly have a lot going on as you just heard. I'm very proud of our team. It's been a difficult year in 2019, I'm proud of the team for their hard work. I appreciate the support of all of our stakeholders as we go forward to continue this journey in our pivot to growth. So thank you all very much. Goodbye.

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