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Conduent, Inc. (CNDT)

Q1 2021 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Greetings and welcome to the Conduent First Quarter 2021 Earnings Results Conference Call. At this time, all participants are in a listen-only mode. A question-and-answer session will follow the formal presentation. [Operator Instructions] As a reminder, this conference is being recorded.

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

Alan Katz
Vice President-Investor Relations & ESG Reporting, Conduent, Inc.

Good evening ladies and gentlemen, and welcome to Conduent's first quarter 2021 earnings call. Joining me on today's call is Cliff Skelton, Conduent's CEO; and Brian Walsh, Conduent's current CFO; as well as Steve Wood, our current Corporate Controller and incoming Chief Financial Officer. 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 the 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, May 5, 2021 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.

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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

President, Chief Executive Officer & Director, Conduent, Inc.

Thanks, Alan. Good afternoon, everyone, and welcome to Conduent's first quarter earnings call. Thanks for joining us today. It's great to be with you.

Today marks yet another quarter where Conduent has been able to achieve its goals and meet the expectations we discussed in prior earnings calls. As I've mentioned in the past, our goal is to continue working on the fundamentals and pivot our company to growth. We think today marks one step closer to that outcome.

Now before I go through the Q1 financials, I'd like to obviously acknowledge the announcement we made this afternoon regarding our CFO succession. I want to take a minute to thank Brian for his hard work and dedication through the years. I very much enjoyed working with him and I wish him the very best in his new role. At the same time, I'm excited to welcome Steve Wood into his new role as our incoming Chief Financial Officer. I've known Steve for a number of years. He's a great partner and an experienced finance leader who will help drive the organization along the next phase of our journey. Importantly, this is a great example of our succession planning efforts. This transition will be seamless for our associates, our clients and our shareholders.

Now in terms of the call today, I'll present a quick overview of the financial results, our recent signings performance and why we're more confident than ever and why we expect to see a turn in the top line very soon. I'll then turn it over to Brian to run through the more detailed financials. Questions will be at the end, as always. Meanwhile, this slide provides a cross-section of recently received awards and recognition that we're very proud of.

So now let's turn to slide 5 to get started. Q1 was a strong quarter. Revenue and adjusted EBITDA were above both internal and external expectations, with revenue of over $1 billion and adjusted EBITDA of $115 million, equating to an 11.2% margin, up 210 basis points year-over-year. This was driven by revenue growth in our Government payments offerings, new business ramp and a focus on efficiency. Our new business signings in Q1 were also strong, which I'll discuss in more detail on the next slide.

Despite a workforce that is mostly still working from home, operations and technology quality continued to improve, demonstrated by increased uptime and service levels, meeting client expectations. The progress we made in our service delivery has brought us well beyond where we were a couple years ago. In fact, several of our marquee clients recently awarded us with Supplier Excellence Awards, which we're very proud of, including Toyota Financial Services and one other Fortune 100 client.

Lastly, we continued to make progress on improving our culture and our associate engagement. In fact, we were just named to the list of Best Global Company Cultures by Comparably and our Glassdoor ratings are much improved. It's great to see this recognition based on associate reviews, and we remain focused on fostering a strong culture.

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Let's now go through the details on our signings for the quarter. Please turn to slide 6. On our last call, we discussed a new metric, net annual recurring revenue activity. This is a trailing 12-month measurement of the expected annual revenue impact to include signings, losses, price impacts in any contractual volume changes. As a reminder, this isn't a financial impact for a specific time period, but rather a look at what will come into the P&L at some point in the future on a net basis anyway. This is an indicator of the performance on sales as well as client retention. It's an important predictor of future growth once the lingering effects of prior years' losses burn off, and by that I mean losses prior to 2019. This burn-off, COVID dynamics and our continued net revenue gain make growth evident in Q2 of this year on a year-over-year basis.

The net ARR activity metric was $87 million in the trailing 12 months ending Q1. There will be quarters here or there that may be higher or lower, but a consistently positive trend is a key. In terms of the new business ARR and TCV, we had a strong quarter with TCV growing 10% and ARR growing 67% on a year-over-year basis. We think this is important because it shows not only long-term growth, but the singles and doubles needed for 2021 and 2022.

Importantly, Q2 looks good, as we just sold a $178 million deal in our Transportation business in Europe, which will be announced in a press release in the coming weeks. As you can see in the pie chart, our signings were generally split up in proportion to the sizes of our segments. This won't always be the case, but we thought that it might be helpful to show the diversity of our signings, especially given the COVID-19 and its impacts are still somewhat out there in the marketplace. Importantly, a fairly high percentage of our signings were driven by expansion opportunities we see with our existing client base, demonstrating their confidence in us. The real opportunity we see for our future lives in our current portfolio, where there are numerous outsourcing opportunities right at our fingertips.

Now let's turn to slide 7 to discuss some of the progress we've made over the past two years and what outcomes those changes are driving in the business. I won't go through each bullet on the page, but I will hit on some general themes. The thing to remember here, at least in my opinion, is that running and growing a company is always operationalized by focusing on the people, the process and the technology. And we have created concentrated efforts across that spectrum.

Regarding people, talent and teamwork will trump many obstacles. We've made some great progress on top-grading talent and are continuing to bring new talent into the organization. While never done, the high-level heavy lifting is nearly complete. We're focused on our culture, engaging with our associates and focusing on diversity and inclusion. We invested resources to ensure we're developing an environment where all associates feel they can be themselves and valued for their contributions. We've invested in training and development programs for selling and account management to drive stronger engagement in support of our clients.

In terms of process, efficiency programs are key to margin expansion and lower cost of delivery. We're seeing the benefits from utilizing best practices in shared service centers. We've increased our touch points with our clients, and this has enabled additional cross-sell opportunities. We saw this positively impact our signings this past quarter. And this seems like an obvious one, but an outside-in approach is what our clients expect if they're to give us more business. The key is to understand how we can help clients solve their problems as opposed to pushing products and services.

As for technology, investments in our infrastructure and data centers have led to improved platform uptime. We're mostly through our data center migration plan, which is slowly but surely bringing state-of-the-art technology to bear and minimizing legacy platforms and infrastructure. The launch of our command center last year provided

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oversight, coordination and proactive monitoring capabilities to react quickly and ensure seamless delivery of service. Finally, we take an every client every time approach to technology and operations. It's not just about internal efforts, but more about the client and end user experience and impact.

Now, these efforts have driven some important outcomes in terms of growth, efficiency and quality. Our operational improvements have led to better delivery, which in turn has improved client retention. It's never perfect and never will be, but we will never be satisfied in this category. Margins have improved and we continue to invest in incremental system upgrades. Every day new bandwidth is created so we can increasingly focus on growth and we see a real improvement to both internal and external expectations.

Let's turn to slide 8 to quickly discuss why our confidence is increasing based on market opportunity coupled with our improvement efforts. In the Commercial segment, the addressable market is $146 billion. We continue to invest in automation and digitization within our CXM offerings, positioning us to capture share and improve margins. We are definitely seeing revenue improvement and volume upside in our CXM space.

We also have particularly strong offerings in the financial services side of the BPS or what was traditionally called the BPO market, where we are integrating cloud-based software, again, focused on automation and technology integration. Within our health, wellness and benefit administration offerings, we see the opportunity to grow through product and end user interface enhancements. And within the healthcare space, given the size, growth trends and client relationships that we have across the industry, we're very well-positioned for automation around claims processing and services. But even more importantly, we think there are many more BPS and CXM offerings that can be deployed across the healthcare market.

Within the Government space, we see a market opportunity of almost $30 billion. We've seen strong interest in our new offerings around fraud tools, in innovation and our payments capabilities, which can also be utilized in the commercial space. The Government market is growing quickly and we think these new offerings will differentiate us.

Lastly, within the Transportation space, we see a market opportunity of about $11 billion given our current offerings. We see the potential to expand that addressable market size in the coming years through geographic expansion and potential expansion into the commercial marketplace.

Overall, the key takeaway here is there is significant room for growth in the markets in which we currently play. It's simply up to us to take advantage of it.

Now, before I turn it over to Brian to go through the financials, I want to close with just a few final remarks. I'll repeat what I said on our last call, consistency is key. We need to keep delivering on our commitments to our associates, to our clients and to you, our shareholders. I'm confident in our ability to do so. This company is in the pivot. It will be a growth company and we're very close to declaring it so. Our team is leading and we're attracting talent. And we'd love for you all to stay on this journey with us because what we've embarked upon is working.

I'd like to now turn it over to Brian for a detailed look at our financials. And I thank you so much for your time today.

Brian Webb-Walsh

Chief Financial Officer, Conduent, Inc.

Thank you. Before I begin, I want to thank Cliff and the other members of the board of directors for their support and all the opportunities I've been given at Conduent. We've come a long way and the company is now well-

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positioned for its next chapter. I also want to thank the Conduent finance team and all of my colleagues for their hard work and dedication. And lastly, I want to congratulate Steve Wood and wish him the best of luck in his new role. We have worked closely together since his arrival in 2020 and the company will be in good hands with a CFO like Steve. We will work closely together to make sure that this is a smooth transition, and I look forward to watching Conduent success over the coming years.

With that, let's move on to the Q1 results. As we've done in the past, we're reporting both GAAP and non-GAAP numbers. The reconciliations are in our filings and in the appendix of the presentation.

Let's turn to slide 10 to discuss the Q1 2021 P&L. As Cliff highlighted, we finished the quarter strong with revenue of just over $1 billion, down 2.2% year-over-year. The decline was driven by lost business from prior years and was partially offset by increased volumes and new business ramp. The continued progress on our year-over-year revenue trend can clearly be seen in the chart on the slide. We're on the right path and the improvement that we see here is encouraging.

Adjusted EBITDA for the quarter was $115 million, up 19.8% year-over-year, while our adjusted EBITDA margin for the quarter was 11.2%, up 210 basis points compared with Q1 2020. The increase in adjusted EBITDA was driven by our revenue mix and by our continued focus on driving efficiency throughout the organization.

Let's turn to slide 11 to go over the segment results. For Q1, our Commercial revenue declined 8% primarily driven by lost business from prior years and lower volumes due to COVID-19. Adjusted EBITDA declined 11.4% while the adjusted EBITDA margin of 11.8% was down 40 basis points year-over-year. The adjusted EBITDA decline was primarily driven by lower revenue.

Our Government business grew by 9.7% for the quarter. This was primarily driven by revenue related to COVID-19 volumes in our Government payments business as well as the ramp of new business, partially offset by lost business from prior years. Government adjusted EBITDA increased by 19.5% while adjusted EBITDA margins of 28.9% increased by 230 basis points. This margin improvement was due to the revenue mix and efficiency progress.

Our Transportation segment revenue declined by 2.6% compared to Q1 2020 primarily driven by lost business from prior years and COVID-19, partially offset by new business ramp. Adjusted EBITDA was up 58% compared with Q1 2020, driven by a temporary item positively impacting revenue mix and our cost savings progress. Adjusted EBITDA margin for the quarter was 16.3%, up 620 basis points year-over-year. We saw the negative COVID impact in our Transportation segment lessen in Q1 compared with Q4, primarily driven by a continued recovery in tolling volumes.

For the quarter, our unallocated costs were $69 million, 3% higher than the same quarter last year, driven by certain employee costs, partially offset by lower IT and real estate spend. As I discussed on our last call, we continue to look at our operating model, including bringing on new talent. At this time, we don't believe we need to make any changes to our external segment reporting.

I'll note that we've included the detail by segment of our year-over-year growth trends for the past five quarters in the appendix. Our trends in the Commercial and Transportation segments are positioned to further improve moving forward as we lap the COVID-19 impacts and as they lessen overall. Our Government segment is currently benefiting from the federal support of unemployment and pandemic SNAP, which will come down over time.

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Let's now turn to slide 12 to discuss the balance sheet and cash flow. Our balance sheet continues to remain healthy and we have a solid liquidity position. We ended the quarter with $399 million of cash on the balance sheet. As of quarter end, we had approximately $743 million of capacity under the revolver. Our net leverage ratio at the end of the quarter was 2.2 turns, in line with our target of 2 to 2.5. As you can see on the debt maturity table, our first major maturity is at the end of 2022. Refinancing our debt during 2021 remains a priority for us and we're well underway in the process. Should the markets remain attractive, we would expect to refinance our debt in the near term.

One other item to note. We recently repaid the remaining $34 million of outstanding senior unsecured notes. This will be reflected on our balance sheet moving forward. Typically with our seasonality, we are a user of cash in the first quarter. However, we had a much lower cash outflow for the quarter this year compared with last year. Adjusted free cash flow was a use of $33 million for the quarter, an improvement of $68 million compared with Q1 of 2020. This was primarily driven by strong EBITDA performance and less outflow associated with prior year-end working capital tactics. This was also despite an increase in certain employee payments.

CapEx for the quarter was $30 million or 2.9% of revenue, which is lower than we would expect moving forward. We see plenty of opportunity for attractive investments into the business, so you should expect to see the number increase in future quarters.

Let's move to slide 13 to discuss our outlook for Q2 and full year 2021. We have improved our full year revenue range to be between $4.05 billion and $4.15 billion. We continue to see an adjusted EBITDA margin range of between 11% and 11.5%. We also expect to convert approximately 20% of full year adjusted EBITDA to free cash flow. Normalized for the expected CARES Act payment, this number would be approximately 25%. And normalizing both 2020 and 2021, that would be over a 5% improvement year-over-year. We have not changed our outlook on our expected 2021 CapEx spend of $170 million or our restructuring spend of between $40 million and $45 million. In terms of Q2, we would expect revenue in Q2 to be flat to slightly up compared with Q2 of 2020 and we expect adjusted EBITDA margin to be approximately 11%.

Before I close, I want to thank our associates, shareholders and clients for their continued support. Our progress is certainly encouraging. We will now open up the lines for some questions. Operator?

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QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] Our first question today comes from Shannon Cross of Cross Research. Please proceed with your question.

Ashley Ellis
Analyst, Cross Research LLC

Q

Hi. Thank you. This is Ashley Ellis on for Shannon. Cliff, I was wondering, or Brian, if you could talk about what the drivers were behind the sequential increase in ARR this quarter. I understand it fluctuates quarter-to-quarter, but it was up 45%. And I think, Cliff, you mentioned that you expect revenue to grow year-over-year next quarter. What leaves you confident in that and where do you see the biggest drivers? And then I have a follow-up. Thank you.

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

A

Yeah. So, the ARR and the sales number was increased because of a lot more shorter-term deals in our sales efforts. So, you saw 10% growth year-over-year in Q1 as it related to TCV, but 67% growth in ARR. And that's due to a little bit shorter-term and a lot more add-on business than we historically have. So, we think that's a really positive trend for 2021 and 2022. We need a combination of both. We need to see the long-term growth rates from large-deal TCV, which we really see ahead of us in Q2, but we need to see a lot of these singles and doubles to get this ARR rate going for both 2021 and 2022.

As it relates to growth rates and pivot and that sort of thing, as I mentioned in my remarks, I think what you should expect and what we expect in Q2 of 2021 is year-over-year growth in Q2 for that quarter. And that's driven by government stimulus increases and a pretty tough compare from Q2 of 2020 when COVID was just hitting in earnest. And if you noticed, we raised the bottom end of our range up by up to $4,050 million – with a range of $4,050 million to $4,150 million. And so, you can kind of do the math to say, if we finish in the top of that range, which could easily happen, that's – we were at $4,164 million last year. So, you can do the math to figure out that if stimulus volume comes in strong, we're going to see a growth here in 2021. And we're just not going to know enough till the end of Q2 to know that answer.

What's really important, though, back to your ARR point is this net ARR number, which was $87 million this year, and in the $60 million range last rolling 12 months. And that's an indication of all the activities that are creating either positive or negative revenue, not timing related, but it's an indication that growth is on horizon around the corner. So, we're really positive on all the aspects, both ARR, the net ARR number as well as the growth opportunities in the back half of 2021.

Ashley Ellis
Analyst, Cross Research LLC

Q

Okay. Thank you. And then, it's been a couple of quarters that you've called out increased service levels and uptime, just I think general customer satisfaction improving. As we start the new year and a lot of companies are considering digital transformations, are you seeing an increase or a willingness for those customers to give you more business than they would have in the past? I think you touched on increased retention, but are you also seeing expansion of this relationship?

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

A

Yeah. We really are seeing receptivity to a dialogue, which frankly when I got here two years ago was hard to get. We just didn't have the track record and the referenceability and the support in the marketplace due to our technology stability. And we're in a much, much better place here. We're two-thirds to three-quarters away through our data center optimization plan. We've got 1.5 big data centers left to go. That's creating a much more stable upgraded environment. And the result is very, very significant improvements in uptime, very, very significant improvements in incident rates. And we're hearing a lot of great feedback from our clients on that, which makes us get a [ph] meeting (26:00) that a couple years ago we couldn't get. That said, no defect is ever enough. Anything less than 100% is not good enough. We won as many 9s of uptimes as we can get. And that's our mission. But yeah, it's a great question and it's opening doors that we didn't have opened before.

Ashley Ellis
Analyst, Cross Research LLC

Q

And then just one follow-up. As you eventually turn to more consistent stable revenue growth, do you expect that those existing customer relationships will be a key driver or will it be more from net new logos? And that's it for me. Thanks.

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

A

Yeah. I know. It's a great question because in the past, even when we were selling, we weren't retaining. And what you've heard Brian and me talk about is the fact that we've got this legacy burn-off from losses prior to 2019. That is our Achilles heel. We are selling more than we're losing right now. The trouble is that the burn-off from these legacy events from years ago has legs to it. It takes a long time.

So, the direct answer to your question is it's both. It's actually a three-legged stool. It's retaining what we have. It's adding on business for the current clients which we have and we proved in Q1 that we can do much better than we did last year in that category. And it's new logo, new clients. And all three of those contribute to the TCV number – well, the last two contributed to the TCV number. All three contribute to revenue growth.

Operator: The next question is from Bryan Bergin of Cowen. Please proceed with your question.

Bryan C. Bergin
Analyst, Cowen & Co. LLC

Q

Hi. Thank you. Just want to say, Brian, good luck with your new opportunity. And welcome to Steve.

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

A

Thank you, Bryan. Appreciate it.

Stephen Wood
Corporate Controller & Principal Accounting Officer, Conduent, Inc.

A

Thank you.

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Bryan C. Bergin
Analyst, Cowen & Co. LLC

Q

Sure. A question here on the new business signings. Can you comment on the nature of the Commercial new business that you're signing and what areas are standing out as good opportunities for potentially helping you return to growth?

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

A

Yeah. I think the good news in Q1 we saw strong Commercial new business signings growth. As Cliff mentioned, there was good contribution from add-on. And we saw across the board CXM contribution. We saw it in our healthcare offerings. So, we really saw it in a number of areas. But it was good to see good contribution from Commercial in Q1 because we had a lot of Government and Transportation contribution last year. I don't know what you'd add, Cliff.

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

A

Yeah. We saw a couple deals in our HSP platform. We've actually got four big implementations underway right now, which is our claims platform for commercial healthcare. Bryan, we see some real upside opportunity in healthcare. Heretofore I would argue that we just not have – we haven't tapped the breadth of Conduent into the healthcare space. And very shortly we'll be announcing a new leader across the segment for commercial healthcare who comes out of an environment where she was leading a lot of the sales efforts for several of our competitors into the commercial healthcare space. We think there's massive opportunity there. We're just seeing the tip of the spear right now frankly. And while it was a good quarter, there's much more to be had there.

Bryan C. Bergin
Analyst, Cowen & Co. LLC

Q

Okay. And as it relates to COVID, can you just update us or remind us again the impact built into the 2021 outlook by segment? Understanding it's detriment to Commercial, still a benefit to Government. Just how should we be thinking about all these moving pieces as you lap last year issues versus some of the extensions of government programs?

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

A

Yeah. So, first of all, it's a little bit harder to track the exact numbers as we get into the second year of COVID. In the first year, we had a discrete plan that we could track against. And as we lap, it gets a little bit harder. But at the start of the year, we said the $150 million benefit from Government, we expected it to come down and we expected the negative impact in Commercial and Transportation to come up by a similar amount. And we expected it to be roughly still negative around $85 million on a net basis as those two things move in different directions.

As now we're looking at it, we think we're probably a little bit better than that with a little bit more coming from Government than we initially anticipated and probably a little less recovery on Commercial. So, we're maybe getting $30 million to $35 million more than we initially thought. So, instead of being down $85 million for the year, which was similar to last year, maybe we're down $50 million. So that's kind of what we see. But it does get a little bit less accurate as we lap years. So, it's not as precise as it was last year.

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

A

Yeah. If you think about it, Bryan, it was an easier compare to say what's happening in a COVID year versus a non-COVID year than it is to compare COVID year to COVID year. That's where it gets really difficult. But as Brian said, the $85 million headwind we had in 2020 is likely 50-ish in 2021. And depending on how long some of the subsidy environments and Biden's war on hunger and a lot of other things that could come into play in the fourth quarter, who knows, that could be mitigated even more. But that's what we see on the horizon right now.

Bryan C. Bergin
Analyst, Cowen & Co. LLC

Q

Okay. Thank you.

Operator: The next question comes from Puneet Jain of JPMorgan. Please proceed with your question.

Puneet Jain
Analyst, JPMorgan Securities LLC

Q

Hey. Thanks for taking my question. Cliff, can your current margin profile, balance sheet and tech capabilities allow you to close the growth gap versus low to mid-single-digit TAM growth? I want to ask, do you need to do acquisitions of technology capabilities to get there?

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

A

Well, so, Puneet, it's a great question. And what I would say is that if you look at what we gave as a range of 11% to 11.5% on margin for expectation for the year 2021 and $4,050 million to $4,150 million on top line, if we hit higher into that top line, even going over the top line, I think the same tracking happens on margin. So, that's point number one, which has nothing to do with your point on acquisitions. But we think with our continued efficiency plays with partnerships that we have underway with some possible collaboration with other parties we have underway and maybe a few tuck-ins in the second half of the year, we can drive that number up to jump-start the target we put in place over the long term, which is 13% to 15%. So, Brian, I don't know if you have anything to add to that.

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

A

Yeah. I think that's right. I think we still see the long-term targets, where we see the peers, the mid-single-digit revenue growth and the 15% EBITDA margin. And that's what we aspire to over time and it's how do we get there over time. I think in the near term, it's, to Cliff's point, tuck-in acquisitions and maybe over time something a little bit bigger, but it would be more tuck-in in the near-term. And then operating leverage from revenue growth to drive margin up continued moving things to shared services and other process improvement and efficiency plays. That's how we see it.

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

A

But it's a really good point on tuck-ins because if you look at AI and machine learning, we've already got two partnerships in place now. We're looking at others. We've built our own automation platform. The combination of all those will drive margin expansion and maybe a tuck-in or two jumpstarts it even further. Is it required? No. Can it accelerate it? Yes.

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Puneet Jain
Analyst, JPMorgan Securities LLC

Q

Got you. And how much in advance do you typically get termination notice for a contract? How soon your growth rate can begin to reflect benefits of underlying net ARR, which has been positive last two quarters now?

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

A

Yeah. I mean, it...

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

A

Varies.

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

A

It really varies. I mean, [indiscernible] (34:26) in a complicated Government or Transportation contract, it could be five years plus that that's on the plus side would be extreme. And in a simple Commercial kind of call center or [ph] print (34:41) kind of contract, it could be 90 days. It really does depend on how complicated the transition is for the person coming in and replacing you. So, it really does depend. A lot of what's burning off that's legacy losses are complicated system implementations, and it just takes a long time to replace what we're doing for our clients.

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

A

Yeah. I think that's exactly right. In the Government space, typically you get between a year and two years of advance notice depending on the conversion expectations from the incumbent. But as Brian said, sometimes the runoff for the conversion activity can be as long as five years after notification. And so, it's got a long tail. And then in the Commercial space, it's not nearly as long. But the good news is, remember that net ARR number is an annual recurring revenue. It's not a TCV number or a gross revenue number. So, it nets out appropriately. And as long as it's positive, we're going in the right direction.

Puneet Jain
Analyst, JPMorgan Securities LLC

Q

Understood. All the best, Brian, for your future endeavors. Thank you.

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

A

Thank you, Puneet. Appreciate it.

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

A

It's win-win, Puneet, so thank you. And Brian is excited, as are we.

Operator: There are no additional questions at this time. I'd like to turn the call back to management for closing remarks.

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Cliff Skelton

President, Chief Executive Officer & Director, Conduent, Inc.

Listen, I'd like to thank everybody for your time today. It's been great being with you, and I think it was a good quarter. I'd like to again thank Brian for 24 years of service to Xerox and Conduent. I'd like to welcome Steve Wood. Steve and I worked very closely together. He was my CFO in the past. And I assure you that the transition will be seamless and I assure you that we are well-positioned to make you proud of what we're doing here at Conduent in our pivot to growth. And we're really proud of the progress we've made, and we're looking forward to the remainder of the year. Thank you all for your support.

Operator: This concludes today's conference. Thank you for your participation and have a pleasant day.

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