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CNDT.OQ - Q1 2024 Conduent Inc Earnings Call

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CORPORATE PARTICIPANTS

Clifford A. Skelton *Conduent Incorporated - President, CEO & Director*

Giles Goodburn *Conduent Incorporated - VP of Corporate FP&A and IR*

Stephen Henry Wood *Conduent Incorporated - Executive VP, CFO & Principal Accounting Officer*

CONFERENCE CALL PARTICIPANTS

Marc Riddick *SIDOTI & Company - Analyst*

Patrick Joseph McCann *NOBLE Capital Markets, Inc., Research Division - Research Analyst*

Michael Mathison *Singular Research - Analyst*

PRESENTATION

Operator

Greetings, and welcome to the Conduent First Quarter 2024 Earnings Announcement. (Operator Instructions) As a reminder, this conference is being recorded.

It is now my pleasure to introduce your host, Giles Goodburn, Vice President of Investor Relations. Thank you. Please go ahead.

Giles Goodburn - *Conduent Incorporated - VP of Corporate FP&A and IR*

Thank you, operator, and thanks, everyone, for joining us today to discuss Conduent's first quarter 2024 earnings. We hope you had a chance to review our press release issued earlier this morning. Joining me today is Cliff Skelton, our President and CEO; and Steve Wood, our CFO. Today's agenda is as follows: Cliff will provide an overview of our results and our business update, Steve will then walk you through the financials for the quarter as well as providing a financial outlook. We will then take Q&A, and Cliff will then provide his closing comments.

This call is being webcast, and a copy of the slides used during this call as well as the press release were filed with the SEC this morning on Form 8-K. This information as well as the detailed financial metrics package are available on the Investor Relations section of the Conduent website.

During this call, we may make statements that are forward-looking. These forward-looking statements reflect management's current beliefs, assumptions and expectations 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 U.S. GAAP, they should be viewed in addition to and not as a substitute for the company's reported results. For more information regarding definitions of our non-GAAP measures and how we use them as well as the limitations to their usefulness for comparative purposes, please see our press release.

And now I would like to turn the call over to Cliff.

Clifford A. Skelton - *Conduent Incorporated - President, CEO & Director*

Thank you, Giles. Good morning, everyone, and welcome to Conduent's Q1 2024 earnings call. Today, we're happy to report that we have analyst Q&A at the end of our session, as Giles has mentioned, as well as the normal report from myself and our CFO, Steve Wood.

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Q1 marks, yet another quarter on our journey that, like others, fought through things like COVID, the shift to a largely work-from-home model and the many changing winds in the economic stage. As Steve and I have previously discussed, we're very clear eyed on what we have to do to take this company from what was an operational turnaround to a more narrow, nimble and growing company. We've said a couple of things. One, rationalization of our portfolio will help us reduce drag and create bandwidth. It will also free up capital for the purpose of reducing debt, buying back our stock and other opportunities.

We said there would be pain before gain. The timing of divestitures is not perfect and some margin deterioration will take place in the near term and then expand to normality. 2024 in our plan is the trough year in both revenue and EBITDA, exacerbated by an average sales year, if you will, in 2023, a phenomenon experienced by many of our competitors as well. Our growth trajectory expectations in 2025 and 2026 will require different talent. We're making progress in mitigating that. More to come in our next earnings on that subject.

Suffice it to say that we're adding and changing talent at the senior levels of the company. We have to revitalize our sales engine, which we are doing. While timing is always a factor and Q1 performance lagged, the first half of the year will be reasonably strong. Again, while we must execute well, it doesn't take a lot of examination to understand the growth enabled by a different talent base, a stable operating platform, cash generated by divestitures and the interlocked cost takeouts, of course, with reduced debt makes for a more valuable company. That's the journey we're 1/3 into.

So what about the Q1 numbers? Q1 was a strong revenue quarter for us at $921 million, exceeding expectations. As you may recall, Steve guided Q1 revenue to be down 2% to 3% year-over-year, and we were essentially flat. He guided adjusted EBITDA margin to be below our full year guided range, and that's where we landed at 7.5%, in line with expectations. Now for what it's worth, the year-over-year EBITDA compare is a little misleading because of a onetime item in Q1 of 2023, without which we'd have been in striking distance to flat year-over-year.

While we're quite pleased with our revenue and EBITDA performance, we're less pleased with the timing of sales. Q1 missed expectations, primarily driven by the timing of new business ARR. As you know, we talk about sales in 3 categories: New logos, new capability and add-on. We definitely saw some new logo and new capability business slip to Q2. The engine is now moving us in the right direction. We have and are developing partnerships with other outsourcing firms in the CX space, especially to drive sales. Our client partnership teams are beginning to penetrate that white space in our portfolio, and we're teamed up with partners such as Microsoft for GenAI across the BPO and CX arenas to enhance quality, throughput and efficiency.

With respect to net ARR, that number was still positive at $17 million, but lower than desired. And that's not worrisome given the Q1 to Q2 timing and the fact that this trailing 12-month number can be unduly influenced in either direction by a large deal rolling off. Steve is going to talk about that further as well as implications for Q2.

As I mentioned, we believe the first half sales should be reasonably strong with some tailwinds in our Commercial business especially, some weakness in our Government business and kind of down the fairway in Transportation. Net-net, with the kind of diverse platform we have here at Conduent, the cycles often offset one another. And thus far, 2024 reflects those offsets. Last year, we had some weakness in Commercial and strength in Government. This year, the opposite. Regardless of lumpiness is sometimes accompanied by luck, unluck and one-timers that can often skew the narrative.

Now speaking of narratives, Steve will get deeper on the subject in his remarks, but the divestiture activities associated with our rationalization efforts and the resulting financial reporting will take on a new reporting challenge of its own. As these divestitures monetize in the P&L, we will be transparent on the revenue, EBITDA and cash. But as I mentioned, margins in a given divested business can vary considerably, especially in this high interest rate era. Thus, we must pay attention to the timing expectations. Weather in this cyclical variation will be important as 2024 finishes, setting the new baseline for the future RemainCo. Therefore, as you can imagine, there will be some challenges in comparing the remainder of 2024 to previous years. But this is the foundation for our future and part of the plan.

Regarding divestiture activities, there's a lot going on. We closed our Curbside Management and Public Safety business in a sale to Modaxo for $230 million plus debt. As part of Constellation Software, Modaxo is a global collection of technology companies passionate about changing the

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face of public transportation. We will begin the transition ASAP, and we will partner up in the process. We're also well on our way to closing the BenefitWallet asset transfer and expect the final tranche to transfer this month.

We've definitely been busy in the M&A arena. There is more to examine and more to do on that portion of our journey. Thus far, we've used proceeds for debt repayment and will continue to do so in the near term with increasing optionality over time. We're also around $44 million into our prescribed $75 million stock buyback plan previously discussed.

We remain committed to reaching the outlook performance previously discussed, particularly on top line. Again, we must continue to improve on the new logo, new capability sales going forward, and we'll continue our disciplined approach to cost containment while bringing in some new senior talent. We will stay focused on EBITDA margins as we drive out stranded costs and modify how we work so that we optimize our cost structure. Profitable growth is a mission, and we've learned that there is always cost refinement opportunity in a transaction-driven company.

We also see partnerships in GenAI is becoming even more important in the future. Despite some of the hype you see in the marketplace, real progress is being made. As you may be aware, we collaborated with Microsoft on an initiative to drive innovation using Microsoft Azure OpenAI services. We now have 3 projects underway, all showing progress and promise and hope to go live on all 3 in the near term.

As always, efficiency improvement becomes even more important in a more focused, narrower company. In addition to teaming with Microsoft, we partnered with Oracle regarding our electronic benefits and tolling platform database with Oracle, now in the Azure cloud. Think of this as a multi-cloud or cloud within a cloud now that technology providers are becoming less proprietary and more dedicated to joint outcomes for their clients. This Oracle database cloud now running in Azure allows for reduced latency, reduced complexity and a more efficient model on a unit cost basis.

We also continue to achieve recognition for our culture and our products and our services. NelsonHall placed us as a leader in customer experience services transformation and for the third year in a row, we're in the GovTech Top 100. Finally, Newsweek recognized Conduent as one of America's Greatest Workplaces for Women and Diversity in 2024.

Now this journey is just that, a journey with puts and takes. We have more work to do, as I mentioned, but we're on the flight path to the growth zone we previously laid out. Our associates, 57,000 of them, work hard every day for our clients. Our client base is loyal. That client base includes roughly half of the Fortune 100. Now we have the products. We have the people. We will soon have more of the talent we need. We just have to stay the course and we will.

Thank you for being here. I'll now turn it over to Steve Wood for the financial details.

Stephen Henry Wood - *Conduent Incorporated - Executive VP, CFO & Principal Accounting Officer*

Thanks, Cliff. As we have done in the past, we are 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 5. Before we launch into a discussion on the quarter itself, I want to highlight again the progress that we're making towards our $1 billion of deployable capital 2025 that we've previously laid out to you in our investor briefing and again in our Q4 earnings update earlier this year.

As Cliff mentioned, we announced earlier today that we have closed the sale of our Public Safety and Curbside Management businesses. We're closing in on a third transaction that we'd expect to close within the quarter, and that will take us somewhere near the midpoint of the range we had earmarked for you for after-tax divestiture proceeds.

To date, we've deployed around 30% or $300 million of our $1 billion target against debt prepayment and share repurchases, and I'll cover more of this detail in a minute in my presentation. Suffice to say, we're where we said we'd be vis-a-vis this key component of our overall strategy as we narrow our business around a core set of solutions that we believe can deliver long-term growth.

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As a result of these transactions, our reported numbers will start to deviate from the HoldCo guide that we laid out at the beginning of the year. And so I want to outline the approach that we're going to take for the balance of the year in terms of how we report and guide the remainder of 2024, how we lay out the quarterly progression as well as how we continue to reassert the medium-term outlook that we talked about in our investor briefing last year and again in our Q4 earnings call last quarter.

Firstly, the approach that we're intending to take for this quarter is to compare Q1 performance on a HoldCo basis. There's only a small fragment of BenefitWallet assets that weren't retained during Q1 with the first transfer happening on March 7. And so there's about a net $3 million negative impact in the quarter, top and bottom line, as we think about Q1 performance against last year.

When we come to Q2 and for the remainder of the year, we'll be backing out the completed divestitures and reporting on an adjusted basis with our normal reconciliations back to GAAP in our filings and in the appendix of our presentations. Later in this presentation, I'll give you our expectations as to how this will look for Q2 on an adjusted basis, consistent with our past practice of guiding the upcoming quarter.

In our Q2 earnings, we'll be updating our full year guidance to be on an adjusted basis, considering completed divestitures and expected progress on removing stranded costs which is underway. It's important to note here that we will continue to work on removal of stranded costs throughout 2024 and into 2025. And so the annualization of these won't be fully reflected in our numbers until the back end of 2025. Finally, we'll continue to provide you with an updated walk to our 2025 exit rates so you can bridge between our actuals, our 2024 guide and the 2025 exit rate outlook we've laid out.

Let's get into the slides. Turning to Slide 6 and reviewing our key sales metrics. As Cliff mentioned earlier, Q1 did turn out lighter than we expected in terms of new business sales with ACV coming in at $99 million as compared to $125 million in the 2023 compare. We did have some deals earmarked to close in Q1 that have pushed into Q2 or later. As a result of this, we're expecting sequentially to be stronger in the second quarter at approximately $150 million of ACV and putting us at approximately $250 million of ACV for the first half of the year. This will still be behind our pacing for 2023 because in Q2 2023, as a reminder, we booked our large transit contract with the State of Victoria in Australia, which yielded $65 million of ACV.

Our full year expectation on ACV attainment is around $650 million and that's about 2% higher than 2023. Despite the softer performance in Q1, there are some encouraging signs. We're seeing renewed urgency to address costs through outsourcing both in the CX and BPaaS spaces where we play strongly with a broad set of offerings, and we expect this to translate into more opportunities as we go through 2024. The net ARR activity metric, our combined measure of wins, losses, pricing effects and other contractual changes, was positive this quarter but substantially lower at $17 million. There's going to be a roller coaster effect emerging in this metric as we go through this year that is worth spending a few minutes explaining.

Based on the above full year sales outcome, we expect the metric to stand at around $100 million by the end of 2024. However, there was pronounced asymmetry in our notified losses last year with them being far more weighted towards the back half of the year, and additionally, the effect of the Australia transit deal which yielded around $48 million of ARR in the second quarter of last year. What you're going to see is this net ARR activity metric going negative in the second quarter and then recovering strongly in the third and fourth quarters, firstly, as the Australia transit deal rolls out of the trailing 12 months and then as the more elevated losses in the back half of 2023 also roll out of the metric.

As I said, full year expectation is that we exit the year with this metric standing at around $100 million, and that's the important number to anchor on. This is based on our current view of Conduent before we take out divestitures. However, I don't believe that divestitures will have a material impact on the shape of this roller coaster effect as we progress through 2024. As a reminder, this trailing 12-month measure does not predict the timing of revenue, but is based on the timing of notification and, as such, will fluctuate as you have just seen from quarter-to-quarter.

Turning to Slide 7. We've covered many of the metrics on the previous slide, but just a couple of extra pointers here to comment on. It was a lighter quarter on renewals, but our win rate remains solid. NRR sales performance was more in line with expectations. And as I said earlier, it was the new business ARR deals that slipped and drove the lower outcome. Our average contract length in the quarter was 2.5 years, reflecting the lack of large recurring deals in the quarter.

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Now let's turn to Slide 8 and discuss our Q1 2024 financial results. Revenue for Q1 2024 was $921 million as compared to $922 million in Q1 2023, essentially flat and down very slightly on a constant currency basis. I'll cover the segment level hydraulics in a minute, but the overall view is that we continue to make progress with flattening the historic revenue declines and moving the business through a transition phase and then towards a trajectory of growth. We're not quite there yet, but we're getting closer.

You'll see when we dive into the segments that Transportation had a better quarter with full bore on our large transit implementation in Australia. And so there's a strong contribution from implementation revenues associated with that. New business revenue ramped, including the impact of the transit deal, exceeded lost business rolling off. But there was a slight drag from volumes, mainly in Commercial. Adjusted EBITDA was $69 million for the quarter as compared to $90 million in Q1 2023. And the adjusted EBITDA margin of 7.5% was down 230 basis points year-over-year as compared to Q1 2023, most of that related to the booking last year in the first quarter of a favorable legal settlement for $17 million which we called out at the time.

In the quarter itself, there weren't any large unusual items. But you'll see when we cover the segments in a minute, there was some variation there driven by mix and other factors.

So let's now turn to Slide 9 and go over the segment results. For Q1 2024 Commercial segment revenues were $483 million, down 4.9% as compared to Q1 2023. There's about a $3 million headwind in that number because of the beginning of the transfer of the BenefitWallet assets at the end of the first quarter this year, which reduced our float revenue with an offset due to higher interest rates this year as compared to last. Other than that, the top line story for the Commercial segment this quarter is one of working off the effect of some prior year lost business. We expect the growth gap to narrow due to improving sales performance and the segment coming closer to flat as we exit 2024.

Adjusted EBITDA for the Commercial segment in Q1 2024 was $70 million, up 7.7% as compared to Q1 2023. And the adjusted EBITDA margin of 14.5% was up 170 basis points year-over-year, driven by operational efficiency with an offset as noted above due to the start of the roll-off of the BenefitWallet assets. Clearly, as we complete this divestiture, you'll see a reset in the Commercial margins due to the high-margin nature of the BenefitWallet business. And this will be partially offset over time through our work to remove stranded costs and drive other operational efficiencies and improved operating leverage and margin mix as the segment begins to move to growth.

Unrelated to the Commercial segment EBITDA but still highly relevant to the overall picture, in Q2, you'll begin to see lower interest expense as we're deploying the proceeds from this divestiture to reduce debt.

For the Government segment, Q1 2024 revenues were $258 million, down 2.3% as compared to Q1 2023. The decreases were primarily due to some lost business from prior year, slightly lower volumes in our Government Payments business, partially offset by new business ramp and the effect of a prior year item that was non-repeating. Adjusted EBITDA for the Government segment in Q1 2024 was $55 million, down 33.7% year-over-year. As noted on the prior slide, this compare included the benefit last year from the portion of a legal settlement recognized in cost of services for $17 million. That item aside, the remainder of the variation in margin is driven by the slightly lower payment volumes.

Transportation segment revenues in Q1 2024 were $180 million, up 20% year-over-year. The implementation ramp from our large transit project in Australia accounted for around $19 million of this year-over-year impact. The balance of the improvement in the quarter was both better add-on revenue performance as well as the non-recurrence of the project retiming that occurred on some of our implementations this time last year. For the Transportation segment, adjusted EBITDA for the quarter was $8 million as compared to $3 million in Q1 2023. And the adjusted EBITDA margin was 4.4%. The predominant driver was the lack of the same impact last year on this project retiming with an offset from a slightly less favorable revenue mix.

Let's turn to Slide 10 and discuss the balance sheet and cash flow. Our total liquidity position remains strong with close to $1 billion in cash and available revolving credit facility. We ended the quarter with approximately $424 million of total cash on balance sheet, and our $550 million revolving credit facility is almost completely unused at this point. Our net leverage ratio decreased slightly to 2x and is comfortably inside our current target range of 2 to 2.5x. Notwithstanding our recent prepayments against our Term Loan B, which I'll talk about in a minute, we have no significant debt repayments until 2026.

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Capital expenditure in the quarter was 2.6% of revenue and we expect it to be about 3% of revenue or slightly below that as we progress through 2024, although individual quarters may fluctuate slightly. As a reminder, we updated this metric last year to include capital spent on product software, which hit operating cash flow. We received the final $22 million of our federal tax refund related to 2018 during the quarter.

In the quarter, we repurchased 4.8 million shares at an average price of $3.48. As you will see from our filings, we also prepaid $164 million against our Term Loan B at the end of the quarter. And subsequent to that, in April, we prepaid a further $95 million. In aggregate, we have current approval to repay debt up to $464 million from the initial proceeds of the divestiture program announced, and we will continue to provide further updates as necessary as we continue with the divestiture program.

Let's now turn to Slide 11 and cover our outlook for 2024. Firstly, it's important to reiterate that we continue to execute on the financial framework I laid out last March in our investor briefing. And the key message that Cliff and I are both conveying is confidence in our path to deliver the $1 billion of deployable capital by the end of 2025 associated with the revenue growth and margin targets we outlined.

Turning to the outlook itself. You'll see that our HoldCo guidance that we gave in our Q4 earnings presentation remains how we think about the business, where we're going to stay the course as is for the remainder of 2024. But as you heard me say earlier, this is the last quarter that it makes sense for us to give you this HoldCo view. Next quarter, we'll be withdrawing this and modifying our guide to show you the adjusted view of our business without divestitures we've announced that will close in 2024. And this will become the basis of our 2024 guidance. In a minute, I'll give you a range for Q2 as a marker. But as I said, more detail to come in the Q2 earnings call.

Slide 12 is important because it gives you the walk from where we are now to that exit rate in 2025 and remains how we think about the journey we're on over the next 20 months or so. And on that slide, you can see the various piece parts of the work we have to do. The loss of EBITDA from the divested businesses will drive what Cliff described as a trough in 2024. And you'll see that recovering as we progress through 2024 and 2025 and work our way into the $100 million of cost efficiency related to stranded costs and other simplifications that we'll be able to make to our operating structure as we continue to narrow the focus of the business.

Add to that our expectations of revenue growth as we move through 2025 and opportunities to drive margin expansion as we continue to work on our mix of business, and you'll get back to that midterm outlook. And again, to reiterate, we're well on our way to generating the $1 billion of deployable capital with around 30% of that already deployed against debt prepayment and share repurchase.

In terms of Q2, adjusted for the 2 divestitures completed, we expect adjusted revenue to be in the range of $795 million to $810 million. And seasonally, it's also usually the low point of our installed base of revenue. And we would expect adjusted EBITDA margin for the second quarter to be in the low single-digit percentages as we are early in our work to remove stranded costs. Clearly, you will see this move up as we go through the quarters, as I mentioned earlier. Finally, as we've started to pay down debt, you'll also see our interest expense line reduce in the second quarter. And annually, based on the approximate $450 million of approval that we have to pay down debt, we'll see a saving on interest expense line of approximately $45 million annualized at current interest rates.

A lot going on here, but we hope we've laid out the pieces for you in enough detail, clearly with more to come in Q2 earnings. Additionally, we've got a busy conference schedule in the New York area in the second quarter. So continue as you do to reach out to Giles and the team for more information on that.

That concludes my financial remarks for the quarter. Operator, I'll hand it back to you.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) The first question is coming from Pat McCann of NOBLE Capital Markets.

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Patrick Joseph McCann - *NOBLE Capital Markets, Inc., Research Division - Research Analyst*

Thanks for taking my questions, guys. My first question is really for Cliff. How are you feeling about the performance of the new business signings as well as the overall macro trends, particularly through the lens of how the economy affects the Commercial segment?

Clifford A. Skelton - *Conduent Incorporated - President, CEO & Director*

Pat, thanks for the question. We haven't done Q&A in a while, so thanks for being a little easy on us as we get going again. Listen, 2023 felt a little tight in terms of the macro trends and propensity to buy, and it's feeling like it's starting to loosen up in 2024. The propensity to buy seems to be loosening up. Cost reduction efforts from our clients and the client base is becoming more profound and we're seeing that start to open up. Now we had a slow start as we mentioned -- Steve and I both mentioned, but we see Q2 being strong and the remainder of the year being strong. So I'm feeling pretty positive about it. Like I said, we had a slow start, but we're positive about the rest of the year and we do see the macro trends becoming more favorable.

Patrick Joseph McCann - *NOBLE Capital Markets, Inc., Research Division - Research Analyst*

Excellent. And then to turn over to the financials. Could you comment on what we should expect for progression over the rest of the year when it comes to divestiture activity and debt retirement?

Clifford A. Skelton - *Conduent Incorporated - President, CEO & Director*

Let me start with activities for the remainder of the year and just say, obviously, we can't get into specifics. But I can say we're not done and we're still in the heat of the battle on M&A activities. Steve can comment here on use of proceeds and timing.

Stephen Henry Wood - *Conduent Incorporated - Executive VP, CFO & Principal Accounting Officer*

Yes. So I think -- the way that we think about it is the way that we've laid it out in the mid-term outlook slide. We've talked about essentially the quantum of revenue that we see being divested, the margin characteristics that we see being divested. The proceeds that we've already announced, which is around $495 million of after-tax proceeds. And you heard in my remarks that we're expressing a degree of confidence that we can get into around the midpoint of the range of $600 million to $800 million that we earmarked in essentially our waterfall to the progression of $1 billion of deployable capital.

And I would say at this point, Cliff mentioned that the early priority is debt repayment. We have an amount approved of somewhere in the region of $450 million. And so we'll be working through that. And then clearly, we'll be talking further -- later in the year on how we think about capital allocation when that becomes pertinent against divestitures as we continue on the progress. That's how we're thinking about it.

Clifford A. Skelton - *Conduent Incorporated - President, CEO & Director*

Lots of activity, Pat, obviously, and it will continue through the rest of the year.

Patrick Joseph McCann - *NOBLE Capital Markets, Inc., Research Division - Research Analyst*

Got you. And if I could ask just one more quick follow-up to that and then I'll pass the floor along. Just -- when it comes to the M&A environment, when you're looking to make more divestitures, how do you view the current environment? Specifically when it comes to, I guess, getting fair value for the businesses you would be divesting, how is that looking right now?

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Clifford A. Skelton - *Conduent Incorporated - President, CEO & Director*

Look, I don't think there has ever been a situation where we were worried about valuations and fair value. I think it has been pretty consistent, even when money was tighter, as it's starting to loosen up here a little bit or at least conceivably starting to loosen up, the whole PE environment is starting to open up and the appetite is increasing. So inbounds are voluminous, if you will, and opportunities are quite strong. So you know as well as I do what's happening in the economy and the whole private equity kind of landscape. It's feeling more sanguine and we're seeing that. But from a valuation perspective, we haven't seen any much inconsistency. But Steve, any thoughts on that?

Stephen Henry Wood - *Conduent Incorporated - Executive VP, CFO & Principal Accounting Officer*

What I would add to that is you'll have seen from what we're doing is we're divesting really quite discrete assets within the portfolio. And Conduent has got a lot of assets in the portfolio, it's a very broad portfolio of assets that were put together over a period of time. And so our approach is to target things that, I would say, have scarcity value on the outside and also potentially don't create the 1 plus 1 equals 3 internally in terms of being synergistic to the way that we think about cross-sell and how we sort of build the RemainCo portfolio for the business.

And so because we've been very targeted and because the assets are more discrete, I think we're pleased with the valuations that we're getting for the assets. And then clearly, we're divesting these at multiples that are considerably above where we are. And I think as we go along that journey, clearly, you'll continue to see us targeting these discrete assets where we expect to get strong multiples for them. Because the alternative to that is we'll keep them in the portfolio.

Clifford A. Skelton - *Conduent Incorporated - President, CEO & Director*

Yes. Just one topper to that, Pat. We said a year ago that our criteria for what we would consider divesting was based on several different things. One was scarcity value, as Steve just said. One was sort of growth versus anchor inside of our own portfolio and how fast -- everything is growable. But how fast is it growable or recoverable? And then finally, from a technology perspective, where do we have technology that we could capitalize on internally versus synergistically capitalized externally? All those went into the math equation as we considered what we might or might not divest and what we might or might not keep in RemainCo.

Patrick Joseph McCann - *NOBLE Capital Markets, Inc., Research Division - Research Analyst*

Excellent, most helpful. I appreciate it. And I will -- I'll pass the floor along. Thanks, guys.

Stephen Henry Wood - *Conduent Incorporated - Executive VP, CFO & Principal Accounting Officer*

Thanks, Pat.

Operator

(Operator Instructions) The next question is coming from Michael Mathison of Singular Research.

Michael Mathison - *Singular Research - Analyst*

Hi. Congratulations on executing the divestitures. You're marching right along and looks very good. My questions kind of relate to revenue opportunities for RemainCo. You mentioned you have a collaboration, actually 3 of them, underway with Microsoft. I just want to clarify, is that related to your payments business, these collaborations? And do you see that particular collaboration is driving cost reductions or revenue opportunities by offering more capabilities? I'm kind of curious what that's really driving toward.

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Clifford A. Skelton - *Conduent Incorporated - President, CEO & Director*

Yes. So thanks, Michael. The collaboration that you're referring to is specific to Microsoft and GenAI and utilizing their platform in a co-marketing partnership and -- or go-to-market partnership as well as utilizing that technology. And we have 3 very strong pilots underway. One is in document management. We would think of that as our claims process, mostly in healthcare. We've got a big one around customer experience. Like many in the industry, people see real opportunities with GenAI in terms of voice-to-text and all kinds of different streamlining opportunities in the customer experience arena and utilizing GenAI that solve problems so you don't need a human.

When you refer to payments, the one endeavor we're underway with in the payment industry is on fraud reduction. We think GenAI can help us very significantly in fraud reduction, in determining early signs of fraud through the volumes of data that the compute can digest and then feed information to our associates so that we can early turn those fraud opportunities before they actually manifest. And so that's the one payment area where our partnership with Microsoft is driving AI improvement.

Michael Mathison - *Singular Research - Analyst*

Great. Thanks for all that detail. If I could just turn to one of the other partnerships you announced with Oracle, moving your tolling database to the cloud, I heard a reference to unit cost savings. Just to put some flesh on that, what percent savings did you achieve?

Clifford A. Skelton - *Conduent Incorporated - President, CEO & Director*

It's probably not a question I can answer with specificity or should answer with specificity. But let me -- what the partnership with Oracle inside of Azure is doing for us is speeding up the process and reducing latency in the cloud by taking Oracle's database in the cloud into Azure's cloud and then allowing our processing speed to increase by a significant margin. It's probably not prudent for me to say exactly what that marginal improvement is or what the unit cost savings is. But obviously, if you can go faster, you can go cheaper. And so that's the model we're pursuing. But it's incremental. There's no breakthrough here. It's all incremental. It's a continuum.

Michael Mathison - *Singular Research - Analyst*

Great. Well, thanks again, and congratulations again.

Clifford A. Skelton - *Conduent Incorporated - President, CEO & Director*

You bet. Thanks, Michael.

Operator

(Operator Instructions) The next question is coming from Marc Riddick of SIDOTI & Company.

Marc Riddick - *SIDOTI & Company - Analyst*

I wanted to sort of dig into a little bit around -- the commentary around the cost reduction efforts and the urgency that you're seeing maybe from customers. I was wondering if you could spend a little time talking about that and maybe sort of how that sort of plays into your expectation of driving sales?

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Clifford A. Skelton - *Conduent Incorporated - President, CEO & Director*

Every CEO and CFO that I'm familiar with is looking for efficiency. We wouldn't be doing our job if we weren't. But especially as the economy is, forward thinking people are starting to say, "Well, when this thing starts slowing down a little bit, I'm going to have to start reducing cost." And a lot of folks are thinking about outsourcing. We're seeing a lot of that in the healthcare industry, for example, where pressure is increasing. And they're starting to free up on ways to outsource. Countries they might not have imagined going to before, they're starting to consider going to, from an offshoring perspective.

So we're just -- that feeds right into our sweet spot in terms of outsourcing. But like everybody else, we're in the same boat internally in terms of driving efficiencies and unit cost reduction. So the bottom line is we're seeing our clients and potential clients think about how we can help them either consolidate outsourced vendors, go to countries we're not in today and reduce their costs and improve their own unit cost so that they can drive EBITDA, at least the improvement if nothing else.

Marc Riddick - *SIDOTI & Company - Analyst*

Yes. That's very helpful. And then switching gears, I was wondering on one of the comments was around behavior of certain industries as far as within Commercial that you're seeing. Were there any particular call-outs that were maybe performing better than others as far as industry verticals? Or how should we think about the differentiation of activity?

Clifford A. Skelton - *Conduent Incorporated - President, CEO & Director*

Well, I mean, look, obviously, technology continues to be growing as fast as you can imagine. We're seeing some tightening in healthcare, travel and sort of the logistics areas where they are a lot more focused on cost reductions. And as I said earlier, the appetite for offshoring, the appetite for outsourcing is increasing. So those are the 3 areas where we see opportunities for Conduent because of the challenges we're seeing in those 3 industries.

Marc Riddick - *SIDOTI & Company - Analyst*

Okay. Great. And then I guess -- the last one for me is sort of a big picture question around interest rates and expectations now relative to maybe 6 months ago. Are you getting a sense as far as how that is affecting client behavior as of yet? Or are you seeing any changes that are specifically tied to those changes of expectations?

Clifford A. Skelton - *Conduent Incorporated - President, CEO & Director*

Well, look, I'll let Steve fill in any gaps. But I don't -- like I said, I think anticipation of interest rates and any kind of Fed moves seems to be on the margins affecting outsourcing appetite. But we're not -- other than that how interest rates affect our own P&L, which Steve touched on in his remarks, and the selling of our BenefitWallet asset, we don't see -- there's nothing monumental from a landscape perspective going on with interest rates that are affecting us. Steve, I don't know if you've got any thoughts on that.

Stephen Henry Wood - *Conduent Incorporated - Executive VP, CFO & Principal Accounting Officer*

The only other thing I can think to add by way of comment there is I think this -- I talked about this renewed urgency that we're seeing to try and drive cost efficiency. And so at some level, I think that, that could be an indicator, as you suggested, that maybe thought processes have changed around the sort of forward look of the interest rate environment and maybe it being a bit higher for a bit longer, and therefore, the need to drive cost efficiency.

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And that urgency is good for us because we play into a lot of those opportunities in our BPaaS and our CX businesses, but without wanting to be the person that's trying to predict where that's going to go. I think maybe those -- you can tie those two things together.

Marc Riddick - *SIDOTI & Company - Analyst*

Great. Thank you so much.

Clifford A. Skelton - *Conduent Incorporated - President, CEO & Director*

Thanks, Marc.

Stephen Henry Wood - *Conduent Incorporated - Executive VP, CFO & Principal Accounting Officer*

Thanks, Marc.

Operator

Thank you. At this time, I would like to turn the floor back over to Mr. Skelton for closing comments.

Clifford A. Skelton - *Conduent Incorporated - President, CEO & Director*

Thank you, Donna. Listen, I'll leave you all with a couple of thoughts, just to reiterate what Steve and I both said during our remarks. We outlined our plan a year ago and we're on it as it was described a year ago. That said, we have to execute. And we have been executing. We need to continue to execute over the course of the next 2 years, especially the remainder of 2024 and 2025. We have to continue to divest these non RemainCo assets. It's very important that we continue to execute on our plan and not drag our feet there, and we won't. But we're going to do it the right way for the right valuation.

We've got to sell. We've got to sell more, we got to partner more and we've got to grow. And that's the course we're on. We're bringing in talent to help us do that. And so you're going to -- more to come there when we get to Q2. As Steve mentioned, we've got stranded cost to take up. The one thing we know how to do here at Conduent is manage expenses and take costs out, and we're on that. And then finally and probably most importantly, we've got to meet client demand, and we've got to retain clients, and that's getting better. But it's ultimately the most important thing we do is take care of our clients.

So all of that's very simple to say, it's motherhood and apple pie in many ways, but it's not always that easy to do. We're getting there. And I appreciate everybody paying attention to our company, and thank you all for joining today.

Operator

Ladies and gentlemen, this concludes today's event. You may disconnect your lines or log off the webcast at this time, and enjoy the rest of your day.

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