DXC Transforming from Value to Growth

Price $35.38   **Growth Holding**   **September 15, 2021**

- Compelling Valuation
- The "NEW" DXC is strategically positioned for growth stabilization and subsequent acceleration.
- New management team leads to a cultural shift and record-high employee satisfaction.
- Nearly half of all Fortune 500 firms contract DXC across 650,000 servers and 3,000 petabytes of data.
- Benefiting from move to the cloud and permanent remote work.

Investment Thesis

DXC Technology (DXC) is a global IT services provider running critical systems for over half of the Fortune 500 companies across 70 countries. DXC is the merged company from Hewlett Packard Enterprise and Computer Sciences Corporation (CSC). DXC has revamped its image since 2020, pioneering itself as the "NEW" DXC, including a new roadmap and improvements to employee satisfaction and customer service.

While DXC has not yet seen massive revenue growth with its new strategy, it has seen a 300% increase in earnings-per-share (EPS), significant delevering, and margin expansion. For this reason, we believe that DXC is a good choice for long-term capital appreciation.

Products

DXC manages an incredibly complex IT environment for many firms, with over 650,000 servers and 3,000 petabytes of data, through its Enterprise Technology Stack.

The Enterprise Technology Stack includes business and insurance processing services, analytics and engineering, applications, cloud architecture, IT outsourcing, and security.

DXC provides proprietary insurance software and platforms across the entire spectrum of insurance services. DXC is the administrator of 13 million insurance policies and interacts with 250 million customers each year.

Analytics and engineering use data insights from the existing business to assist firms in developing solutions to firm-level problems, automate or increase efficiency with new software, and assist firms in innovating new products or services.

Applications is a service meant to modernize existing applications. This includes managing, optimizing, and modernizing applications. DXC aids customers, with many saving 40% on operations costs compared to previous applications and 50% increases in time-to-market efficiencies.

As an IT business, security is critical for DXC. Customers need to trust that DXC's systems and services do not put their business at risk for attack.

DXC's cloud services assist firms in migrating to the cloud or hybridizing existing IT infrastructure with cloud components to increase efficiency. This can assist firms in IT costs and simplify infrastructure, as DXC has partnerships with 200 industry-leading companies, including Amazon Web Services, Oracle, and VMware.

IT outsourcing can often be cheaper than in-house IT services. DXC manages and simplifies existing IT infrastructure while also allowing customers to modernize IT by moving much of it to the cloud.
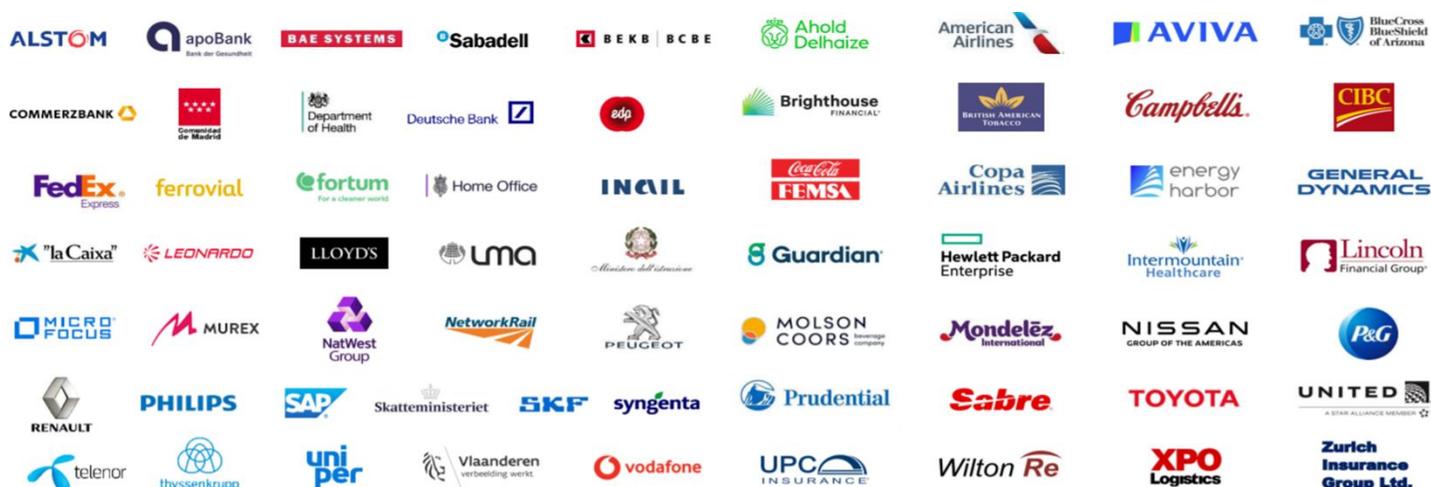
"Platinum" clients, Investor Day 2021

Improvements and Strategy

DXC's strategy for growth involves 3 pillars. FY2021 was the "stabilization" phase; this included a $7 billion reduction in debt and a margin increase from 2.2% to 7.5%. Through adjustments in scaling and efficiency, DXC has managed $550 million in savings. In addition, the stabilization phase largely included increasing employee satisfaction, which according to DXC, was at

an all-time low. They have seen a large increase in employee engagement and approval of the firm's direction. Leadership improvements mean that DXC is firmly heading in a new direction.

FY2022 will be the "foundation" phase, establishing and nurturing relationships with clients to ensure a long-term dedicated base. The foundation phase includes much smaller margin expansions, more stable sales growth, and more disciplined financials.

FY2023 and beyond is the acceleration phase. The acceleration phase includes high projected growth for the analytics and engineering, security, cloud, and insurance businesses. The remaining businesses act as the stable base for DXC to grow from.

In FY 2020, DXC acquired an 83% interest in Luxoft, a Swiss digital service provider whose existing services include strategic consulting, proprietary software development, and engineering services.

Risk

While DXC has 2675 accounts in total, the "platinum" 175 makes up most of the revenue. The IT industry is fiercely competitive, and DXC is still transitioning to higher value-added capabilities. Should they fall behind in services or pricing or be unable to reach their development targets, they could lose significant amounts of revenue.

Security breaches through DXC's services could significantly reduce the trust DXC has with its clients, some of whom are large financial institutions, governments, and healthcare providers.

Metrics

57% of Q1 FY22 bookings were new clients, and 43% were renewals. Earnings per share increased 300% year over year, but revenues were down 8%. The revenue decreases are due to the sale of DXC's healthcare software business to Italian firm Dedalus and the expiration of low-margin or unprofitable contracts.

FY2022 has a guidance of $500 million in free cash flow, of which 10% will go toward investing in the business, 35% will go into share buybacks, and 55% will go toward lease and debt repayment. Currently, DXC has no plans for dividends but has stated that once its valuation is in line with the sector, it will reassess.

DXC Technology (DXC)	FY2021	E2022	E2023
Price-to-Sales	0.5	0.5	0.5
Price-to-Earnings	14.6	9.8	8.3
EV/EBITDA	5.0	4.6	5.0

Estimated Next 12 Months	Price-to-Cash-Flow	Price-to-Sales	Price-to-Earnings
DXC Technology (DXC)	8.5	0.5	9.2
International Business Machines (IBM)	8.5	1.6	12.0
Leidos Holdings (LDOS)	13.0	0.9	14.0
Cognizant Technology Solutions (CTSH)	14.0	2.1	17.6
Booz Allen Hamilton Holding (BAH)	14.8	1.3	18.5
Infosys (INFY)	27.7	5.6	29.8
Accenture (ACN)	21.5	4.0	34.0
Tata Consultancy Services (TCS)	31.2	7.1	34.7

DXC Technology (DXC)
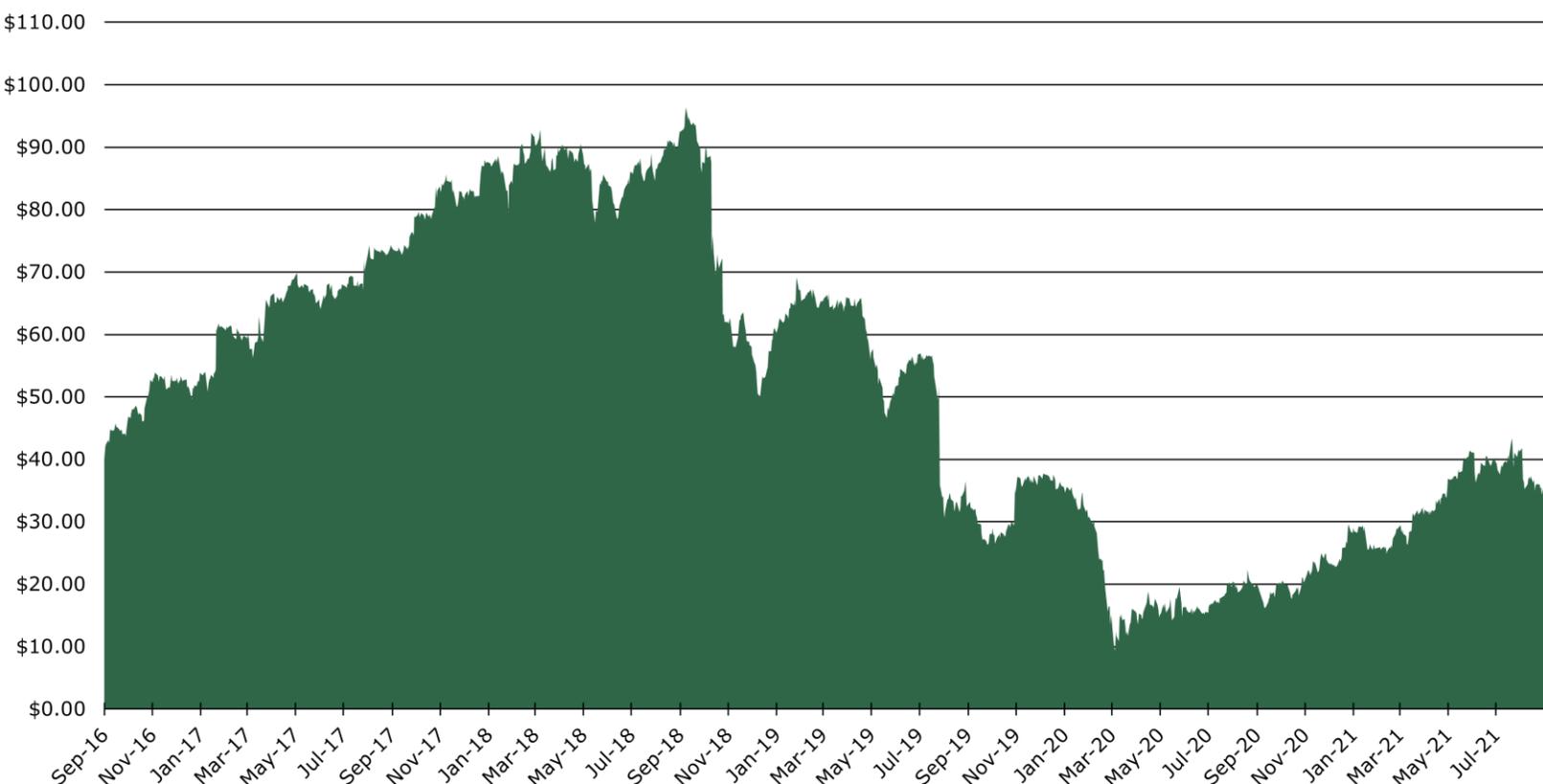
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