UNISYS

4Q14 Financial Release
CEO/CFO Statements
January 29, 2015

Niels Christensen, IRO

Thank you operator. Good afternoon everyone, and thank you for joining us.

Earlier today, Unisys released its fourth-quarter and full-year 2014 financial results. With us this afternoon to discuss our results are Peter Altabef, our President and CEO, and Janet Haugen, our CFO.

Before we begin, I want to cover a few details.

First, today's conference call and the Q&A session are being webcast via the Unisys Investor website.

Second, you can find the earnings press release and the presentation slides that we will be using this afternoon to guide our discussion on our Investor website.

Third, today's presentation, which is complementary to the earnings press release, includes some non-GAAP financial measures. These have been provided in an effort to give investors additional information. The non-GAAP measures have been reconciled to the related GAAP measures and we have provided reconciliations within the presentation.

Finally, I'd like to remind you that all forward-looking statements made during this conference call are subject to various risks and uncertainties that could cause actual results to differ materially from expectations. These factors are discussed more fully in the earnings release and in the company's SEC filings. Copies of these SEC reports are available from the SEC and from the Unisys investor website.

Now I'd like to turn the call over to Peter.

Peter Altabef, CEO

Thank you, Niels, and hello everyone. I'm delighted to be with you on this, my 29th day as CEO of Unisys.

I would like to accomplish several things this afternoon before I hand the call off to Janet, who will review our financial performance for the fourth quarter and full fiscal year. After that, we will take any questions you may have.

I will briefly introduce myself to those of you I have not yet had the opportunity to meet. But, I look forward to doing so in person in the near future.

I will also give you some preliminary observations based on my first several weeks at the company.

Finally, I am going to set out several agenda items, so that you understand my priorities, and can start to measure us against them.

As many of you know, I have spent most of my career with large technology organizations. Most recently, I was CEO of MICROS Systems, a leading provider of point-of-sale solutions to hotels, restaurants and retail. After more than 30 years as a public company, MICROS was acquired by Oracle in September of last year for approximately $5.3 billion.

Prior to joining MICROS in 2013, I spent 16 years at Perot Systems, ultimately serving as CEO from 2004 until 2009. Perot Systems was acquired by Dell in 2009, after which I served as President of Dell Services.

I am proud to have led those organizations, as I am to be leading this one.

Unisys is a long-established IT solutions leader, with a proud heritage of innovation in both services and technology. Our clients include some of the largest, most sophisticated and demanding companies and government agencies in the world. For many of our clients, the solutions we provide are an integral component of how they serve their own customers and constituencies, and how they differentiate themselves in the marketplace.

In the short time I've been here, I have been able to meet just a fraction of my more than 20,000 new colleagues around the world. I have not been surprised to find, however, that we have an extraordinarily capable team of people, energized and focused on our mission.

I believe strongly that Unisys will play an important role in the rapidly-evolving tech landscape. The pace of change in IT solutions has never been greater. This creates a wonderful opportunity for a nimble, responsive, focused company to grow market share. We already have some of the elements we need to thrive in this market, including best-in-class support, innovative solutions and engineering excellence.

To achieve our vision, however, we will need to continue to evolve as a company.

This brings me to the final piece of my discussion this afternoon.

While it is too early for me to report to you any substantive decisions, I do want to set out for you some of my key areas of focus. We will have more to say on these topics in the coming quarters. But I want to at least give you some insight into my priorities.

First is our go-to-market strategy. We have already started to make some important changes to our approach to the marketplace. This includes the composition and organization of our client-facing teams. Over time, we also expect to expand and deepen our industry-specific domain expertise.

Second is our suite of solutions. A core strength of Unisys is our engineering and development talent. That talent drives our technology solutions, but can also be used to develop software and integrated solutions that will be an important differentiator for our services business.

Third, consistent with the items I just mentioned, we are rethinking how we organize ourselves internally, and how we communicate with you and other constituencies about our business. This includes the amount and type of information we provide to our investors. As Janet will discuss, beginning today we will provide additional information about our results on the investor relations section of our website. Please give our Investor Relations team any thoughts or feedback you may have on this topic.

Fourth, in order to be the company we want and need to be, we must ensure that we are operating from a position of strength. We are taking a hard look at every element of our cost base. We will seek to drive operational efficiencies throughout the organization, properly align resources with opportunities, and ensure that we are investing appropriately for the future.

Finally, capital allocation. I think about this topic in three key buckets – internal investment for growth, external investment via acquisitions, and return of capital to shareholders. Each plays an important role in driving shareholder value creation, and we will work to optimize the uses of cash across those categories. Decisions we make about capital allocation will undoubtedly evolve over time, as the company evolves.

Let me stop there, and just say again that it is a privilege to be member of the Unisys team.

At this point, I'll turn the call over to Janet to take you through the numbers. Janet?

Janet Haugen, CFO

Thanks Peter. Hello, everyone. Thank you for joining us on this call.

In my comments today, I will be providing comparisons on a GAAP and non-GAAP basis. Unless otherwise mentioned, the comparisons are on a GAAP basis and the non-GAAP results exclude pension expense.

Let me start with our fourth quarter and full-year 2014 financial results. Please turn to Slide 3.

At the top line, we reported revenue of $906 million in the quarter, which was down 9 percent year-over-year. That includes a 3-percentage-point negative impact from currency on the year-over-year comparisons.

For the full year, revenue of $3.4 billion was down 3 percent; with currency having a 1 percentage-point negative impact on the year-over-year revenue comparisons.

We reported an operating profit of $82 million for the fourth quarter of 2014. And our gross profit margin declined 470 basis points to 27.0 percent. Operating expenses rose 2 percent in the fourth quarter of 2014 compared to the year-ago quarter driven by higher investments in growth programs.

For the full year 2014, on lower revenue, our operating margin decreased 180 basis points to 4.6 percent from 6.4 percent on lower gross profit margins. The decline in profitability is primarily attributable to lower Services margins during 2014 as we were challenged by lower revenue and some problem projects.

Our fourth-quarter 2014 pension expense decreased to $18 million from $24 million in the fourth quarter of 2013. Consistent with our prior estimates, we reported $74 million in pension expense for the full year 2014, compared with pension expense of $94 million in 2013.

For the fourth-quarter of 2014, pre-tax income was $89 million compared to $152 million reported in the fourth quarter of 2013.

Pre-tax income for the full year 2014 was $146 million compared to $219 million in 2013 due to lower revenue and gross margins.

At the tax line, we had a $24 million tax provision in the quarter compared with a $28 million tax provision in the year-ago quarter. For the full year 2014, we had an $86 million tax provision versus a $99 million tax provision in 2013. Our tax provision continues to be highly variable from quarter to quarter and year to year depending on the geographic distribution of our income.

Our fourth-quarter 2014 diluted earnings per common share was $1.24 per share compared to $2.37 in the year-ago quarter. Our fourth-quarter 2014 non-GAAP diluted EPS decreased to $1.60 per share compared to $2.82 in the fourth quarter of 2013.

For 2014, diluted earnings per common share declined to $0.89 per share from $2.08 per share a year ago. Our 2014 non-GAAP diluted EPS was $2.36 per share compared to $3.87 in 2013.

Moving to our fourth-quarter segment revenue, please turn to Slide 4. Services revenue, which represented 80 percent of our revenue in the fourth quarter of 2014, declined 11 percent year-over-year with declines of 10 percent in IT Outsourcing and 11 percent in Systems Integration. Currency had a 3-percentage-point negative impact in the quarter.

On our last earnings call, we provided the amount of opening Services backlog for the fourth quarter. We also provided the range that the opening backlog has represented of a given quarter's Services revenue over the previous eleven quarters. The fourth quarter Services revenue of $721 million was in the middle of the range implied by the amount of revenue in opening backlog at the start of the quarter. Sell-and-bill revenue generated during the fourth quarter of 2014 was significantly lower than in the fourth quarter of 2013. Some of the opportunities we had anticipated during the fourth quarter will be realized over the next few years as others were deferred.

Fourth quarter Technology revenue accounted for 20 percent of our total revenue and rose 1 percent year-over-year; 3 percent on a constant currency basis.

Moving to fourth quarter segment margins, starting with the Services business.

Fourth quarter 2014 services gross profit margin decreased 440 basis points year-over-year to 17.5 percent due to lower revenue, a lower proportion of Unisys Intellectual Property in our revenue, and delivery challenges we faced on a few projects.

Our Services operating margin declined by 590 basis points year-over-year to 3.9 percent reflecting the decline in gross profit and higher operating expenses.

Moving onto Technology margins, we reported a Technology gross margin of 60.4 percent in the fourth quarter, down 100 basis points from the prior year. While Enterprise Class Software and Server revenue rose year-over-year led by a 13 percent increase in ClearPath revenue, there was a lower percentage of this revenue from the higher margin software content. Operating expenses increased as a result of higher investments in our new offerings. As a result of the decrease in gross margin and higher operating expenses, our Technology operating margin declined to 36.3 percent from 40.6 percent in the fourth quarter of 2013.

2014 started off with a challenging first half, but ended with a good second half, particularly in our Technology business. On Slide 5, our full year segment results are shown.

Services revenue declined 4 percent for the full year in 2014; 3 percent on a constant currency basis. For the full year 2014, IT Outsourcing revenue was down 2 percent and Systems Integration revenue was down 1 percent. On a constant currency basis, IT Outsourcing was roughly flat while Systems Integration declined 2 percent.

Our Infrastructure Services revenue declined 19 percent to $347 million for the full year. As we have noted previously, this business provides warranty and support services for our clients' IT infrastructure and has not been a strategic growth area. The revenue decline in this business during 2014 reflected lower volumes on some existing contracts and the conclusion of other contracts that we did not renew.

Technology revenue was up 2 percent for the full year 2014; 3 percent on a constant currency basis. This growth was driven by a 5 percent increase in ClearPath revenue for the year. Revenue from our new Stealth and *Forward!* products remained immaterial.

With respect to Services margins for the full year 2014, on a 4 percent decline in revenue, we reported Services gross margin of 17.5 percent; down 220 basis points from 2013. Our operating margin of 4.2 percent was down 200 basis points compared to 2013.

For the full year, our Technology gross margins increased to 56.3 percent driven by higher revenue. We increased investments in new offerings in this segment in 2014 as discussed in our earlier earnings calls. Higher operating expenses impacted operating margins which declined 200 basis points to 19.1 percent.

Slide 6 shows our fourth-quarter and full-year revenue by geography and client industry.

Revenue in the U.S. and Canada rose 6 percent in the fourth quarter due principally to a strong performance from our U.S. Federal business which I will discuss in a moment. This strong fourth quarter performance drove a modest increase in full year revenue from the U.S. and Canada. This region represented 42 percent of our total revenue for the full year.

In the fourth quarter, international revenue declined 18 percent; 14 percent on a constant currency basis. For the full year, international revenue was down 5 percent; down 4 percent on a constant currency basis.

Revenue in our EMEA region was down 28 percent for the fourth quarter on an as reported basis and 24 percent in constant currency. For the full year, EMEA revenue represented 32 percent of our total revenue and was down 7 percent; 9 percent on a constant currency basis.

The fourth quarter revenue from our Asia Pacific Region declined 34 percent as reported and 32 percent on a constant currency basis principally reflecting lower IT outsourcing revenue. 2014 revenue in the region was down 13 percent as reported and 10 percent on a constant currency basis.

Fourth quarter revenue rose 49 percent in our Latin America region on a reported basis and 56 percent on a constant currency basis as both Systems Integration and Technology were up year-over-year. For the full year, revenue was up 8 percent; 16 percent on a constant currency basis.

Based on today's rates, we anticipate currency to have about a 6-percentage-point negative impact on revenue in the first quarter of 2015 compared to the first quarter of 2014.

From a client industry perspective, our U.S. Federal business accounted for 16 percent of our 2014 revenue. Revenue from the U.S. Federal government increased 18 percent in the fourth quarter of 2014 and up 3 percent for the full year. I will discuss this in more detail in a moment.

Public Sector, defined as all government clients other than U.S. Federal, accounted for 26 percent of 2014 revenue. Public Sector revenue decreased 21 percent year-over-year in the fourth quarter and 5 percent for the full year.

Revenue from Commercial industry clients which represented 35 percent of our 2014 revenue, declined 12 percent in the quarter and was down 6 percent for the full year.

Revenue from Financial Industry clients which accounted for 23 percent of our 2014 revenue declined 9 percent in the quarter and was flat for the full year.

Slide 7 provides more detail on our U.S. Federal government revenue over the past eight quarters.

As noted earlier, compared to the year-ago quarter, our U.S. Federal revenue rose $27 million, or approximately 18 percent, to $178 million, reflecting growth from both Technology and Services.

In the fourth quarter of 2014, revenue from Civilian agencies represented about 37 percent of our revenue base within the U.S. Federal government, while Defense and Intelligence agencies accounted for 42 percent and Homeland Security agencies represented 21 percent.

For the full year, Civilian agencies provided about 42 percent of our U.S. Federal government revenue, Defense and Intelligence agencies represented 32 percent and Homeland Security agencies accounted for the remaining 26 percent.

In a follow-up to our prior comments on the protested award to Unisys of the $460 million, five-year, Border Enforcement Management Systems contract from Customs and Border Protection, we are pleased to report that the protest was resolved in our favor late in the fourth quarter. We are now working to transition this project and expect to begin generating revenue in 2015.

We ended the fourth quarter of 2014 with about $352 million of U.S. Federal services backlog, which was up 1 percent versus the fourth quarter of 2013.

We were encouraged by the slight growth we saw in U.S. Federal Services business during 2014 and will continue to pursue new revenue opportunities in 2015 with a focus on growing this business.

In addition to the information we have just covered and the related slides, we have posted condensed, comparative financial statements and a more detailed view of our revenue by segment, geography, and industry on the investor relations section of our website.

For some comments on Services orders, please turn to Slide 8.

In the fourth quarter, our Services orders increased substantially year-over-year and sequentially.

From a geographic perspective, we saw year-over-year Services order growth in our Latin America, EMEA, and U.S. and Canada regions during the fourth quarter of 2014. Orders in the Asia Pacific region declined in comparison to the fourth quarter of 2013.

We ended the fourth quarter with $4.8 billion in Services backlog, which was flat with the prior year-end and up sequentially. Currency had about a 5-percentage-point negative impact on the year-over-year comparison.

Of our $4.8 billion in Services backlog, we expect approximately $2.0 billion (or 41 percent) will convert into 2015 Services revenue.

Approximately $635 million of the December 31, 2014 Services backlog is anticipated to convert into first quarter 2015 Services revenue. During the past twelve quarters the amount of revenue in backlog at the start of the quarter has typically ranged between 85 and 90 percent of our quarterly services revenue for the quarter and the sell-and-bill revenue has accounted for the remainder.

Moving to cash, please turn to Slide 9 for an overview of our cash flow performance in the quarter and for the year.

We generated $106 million of cash from operations in the fourth quarter of 2014 compared to $141 million in the year-ago quarter. The company generated $121 million in cash from operations during 2014 versus $187 million in 2013. The decline in year-over-year cash generated from operations during 2014 is largely attributable to lower profitability and higher pension contributions.

We contributed $22 million in cash to our defined benefit pension plans in the fourth quarter of 2014 versus $45 million in the fourth quarter of 2013. During 2014, we contributed $183 million compared to $147 million in 2013.

Capital expenditures were $69 million in the fourth quarter of 2014, versus $48 million in the fourth quarter of 2013. Capital expenditures for the full year were $213 million. Year-over-year growth in capital expenditures in the fourth quarter of 2014 and for the full year was led by higher investments in outsourcing assets within our IT Outsourcing business as we won a number of new contracts, and marketable software to support ClearPath, Stealth and *Forward!*. We anticipate full year capital expenditures during 2015 to be in the range of $175 to $200 million.

We generated free cash flow of $37 million in the fourth quarter of 2014 versus $93 million for the same period last year. Our free cash flow before pension cash contributions was $59 million for the fourth quarter of 2014 versus $138 million in the fourth quarter of 2013. During 2014, we had free cash usage of $91 million versus free cash flow generation of $36 million in 2013. Free cash flow before pension cash contributions was $92 million during 2014 versus $183 million in 2013.

Excluding the impact of pension expense, Unisys generated adjusted EBITDA of $150 million for the fourth quarter of 2014 versus $215 million in the fourth quarter of 2013 and $385 million for the full year 2014 versus $471 million in adjusted EBITDA in 2013.

Depreciation and amortization was $43 million in the quarter, compared to $39 million in the fourth quarter of 2013. Full year depreciation and amortization was $169 million in 2014 versus $160 million in 2013. During 2015, we expect full year depreciation and amortization to be approximately $170 million.

Our debt balance was $224 million at December 31, 2014 and is comprised primarily of our $210 million 6.25 percent senior notes due in 2017 which were issued in the third quarter of 2013.

Our cash balance was $494 million at December 31, 2014 compared to $640 million at December 31, 2013. Our cash balance at the end of 2014 was more than two times our debt level.

As we announced in the fourth quarter of 2012, our Board of Directors authorized the purchase of up to $50 million of the company’s common or preferred stock through December 2014. During 2014, $36 million in purchases were made under this authorization. Over the past two years, more than $47 million was returned to shareholders under this program.

Beginning on Slide 10, we provide significant information on our worldwide pension plans, funded position, and expected cash funding levels. Let me just point out a few key take-aways:

The actual returns on assets in the U.S. plan during 2014 were 8.32 percent, versus the expected long-term rate of 7.72 percent. Our actual returns on assets within our international plans were also better than the expected rate of return of 6.45 percent.

Notwithstanding these solid returns, as well as $183 million in contributions, the net deficit in our defined benefit plans at December 31, 2014 increased by $744 million from December 31, 2013, as a result of lower year-over-year discount rates and the impact of changes in mortality assumptions.

We ended 2014 in an underfunded position in our U.S. plan of $1.6 billion, an increase of approximately $500 million from the level at year-end 2013.

We expect to contribute approximately $53 million in 2015 into the U.S. plan and another $76 million into our other plans during 2015 for total contributions of approximately $129 million, approximately $54 million less than what was contributed in 2014. The underfunded position of the international plans at December 31, 2014 rose by approximately $259 million from the prior year-end to $636 million.

A change of 25 basis points in the U.S. discount rate causes an approximate $150 million change in the pension obligation. For international plans, a change of 25 basis points in the discount rate causes an approximate $146 million change in the pension obligation.

With that, let me thank you for your time.