

DXC Technology Company (DXC)

\$35.01 (As of 01/14/20)

Price Target (6-12 Months): **\$37.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 01/13/20)

Prior Recommendation: Underperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:A

Value: A

Growth: B

Momentum: A

Summary

DXC Technology is gaining from strength in the digital business, which received a boost from the acquisition of Luxoft. Partnerships are also helping it expand in the cloud computing space. Further, acquisitions are helping DXC augment revenues amid intensifying competition in the cloud computing and cyber security spaces. However, the company is ailing from persistent weakness in its traditional infrastructure business. Moreover, the GBS segment's margins are expected to contract due to continued digital hiring and expansion of digital capabilities. Also, disruptions related to strategic alternatives that the company plans to undertake are expected to hurt the fiscal 2020 top line. Further, currency headwinds and delays in completion of deals are key concerns. Shares of DXC have underperformed the industry in the past six months.

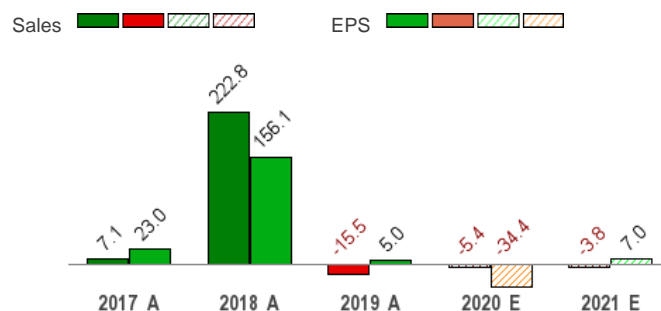
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$69.45 - \$26.02
20 Day Average Volume (sh)	2,699,102
Market Cap	\$9.0 B
YTD Price Change	-6.9%
Beta	2.02
Dividend / Div Yld	\$0.84 / 2.4%
Industry	Computers - IT Services
Zacks Industry Rank	Top 35% (90 out of 254)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	-4.2%
Last Sales Surprise	-1.5%
EPS F1 Est- 4 week change	0.0%
Expected Report Date	02/06/2020
Earnings ESP	0.0%
P/E TTM	4.6
P/E F1	6.4
PEG F1	1.5
P/S TTM	0.4

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	4,735 E	4,801 E	3,716 E	3,828 E	18,888 E
2020	4,890 A	4,851 A	4,906 E	4,994 E	19,641 E
2019	5,282 A	5,013 A	5,178 A	5,280 A	20,753 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$1.44 E	\$1.59 E	\$1.13 E	\$1.35 E	\$5.85 E
2020	\$1.74 A	\$1.38 A	\$1.10 E	\$1.23 E	\$5.47 E
2019	\$1.93 A	\$2.02 A	\$2.23 A	\$2.19 A	\$8.34 A

*Quarterly figures may not add up to annual.

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 01/14/2020. The reports text is as of 01/15/2020.

Overview

Tyson's, VA-based DXC Technology Company was formed by the merger of Computer Sciences Corporation ("CSC") and Enterprise Services Division of Hewlett Packard Enterprise ("HPE") which completed on Apr 1, 2017. While CSC was founded in 1959, HPE came into existence after split of former Hewlett Packard Company in Nov 1, 2015.

Post-merger, the combined entity has become the world's second largest end-to-end IT services providing company after Accenture plc. The firm offers a broad array of professional services to clients in the global, commercial and government markets.

DXC Technology has nearly 6,000 private and public sector clients across 70 countries.

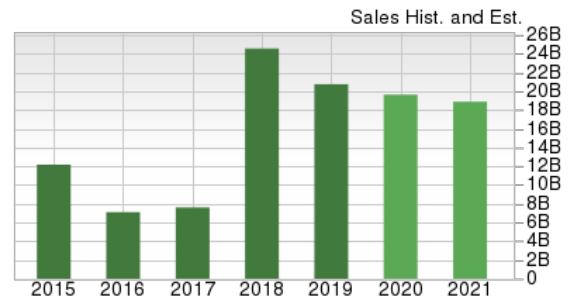
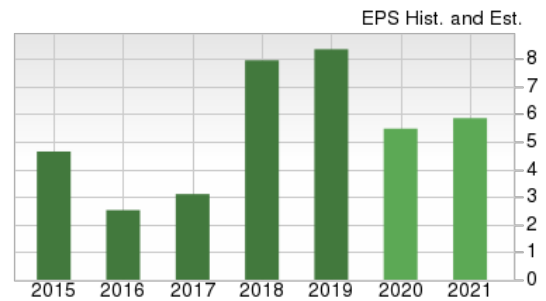
It specializes in information technology (IT) systems consulting – designing, developing, implementing, and integrating information systems. The company also provides business process outsourcing (BPO) and manages key functions for clients, such as procurement and supply chain, call centers and customer relationship management, credit services, claims processing and logistics.

Apart from this, Computer Sciences' IT and management consulting services advise clients on acquisitions, IT security, strategy and business process re-engineering. The company also licenses sophisticated software systems for the financial services markets and provides a broad array of e-business solutions that cater to the needs of large commercial and government clients.

From the starting of fiscal 2019, the company reports results under two operating segments: Global Business Services (GBS) and Global Infrastructure Services (GIS).

Revenues generated in fiscal 2019 came in at \$20.75 billion, down from \$21.73 billion a year ago.

In the IT and professional services market, DXC Technology competes with major companies like IBM, Amazon and Google.



Reasons To Buy:

- ▲ DXC Technology is focusing on the cyber business, cloud computing market and Big Data business. A significant portion of the company's cyber business is contributed by the federal government and, to an extent, the commercial sector. Clients increasingly prefer to rely on cloud-based services as it makes the IT system more agile and productive, which leads to considerable cost savings. The segment is still underpenetrated. Therefore, DXC Technology, being a major player in the space, is expected to benefit from this untapped opportunity.
- ▲ DXC Technology spun-off of its USPS business, subsequently merging it with Vencore Holdings and KeyPoint Government Solutions. Upon completion of the deal, shareholders of DXC Technology received 86% of the combined company's shares, and the company received \$1.05 billion of cash from USPS. The IT services market for both commercial and the U.S. public sectors has been evolving at an accelerating pace. Therefore, DXC Technology's spin-merger move is believed to provide it a customized approach toward handling two different types of clients. The new company has now become one of the top five IT services providers for the U.S. government.
- ▲ DXC Technology is vying on partnerships to enhance its offerings. Notably, the company is looking to expand existing networking-based infrastructure with the benefits of the VMware's hybrid cloud offerings. The move has helped DXC Technology in strengthening its position in the virtualization server market. The partnership enabled the company to offer an efficient and improved hybrid IT environment to drive performance. It has also entered into a partnership with Amazon to develop cloud-based solutions for enterprise and public sector clients. We believe the company's focus on entering into strategic partnerships will help it expand in the cloud computing space and garner additional revenues.
- ▲ DXC Technology, following the footsteps of CSC, is focusing on acquisitions to expedite growth, which is helping it gain access to newer markets and technologies. We believe the acquisitions will further strengthen DXC Technology's position as one of the leading IT services provider in the world. Moreover, acquisitions have helped the company boost revenues amid intensifying competition in the cloud computing and cyber security market.

Following the footsteps of Computer Sciences, DXC Technology is making robust acquisitions to strengthen its portfolio, which should drive growth over the long run.

Reasons To Sell:

- ▼ CSC, prior to the completion of merger with HPE's Enterprise Services business, took additional debt. This has amplified DXC Technology's total long-term liability thereby increasing its interest cost burden. Any rise in interest cost will have a negative impact on the company's bottom-line results. As of Sep 30, 2019, DXC Technology has a total long-term debt (net of current maturities) of \$7.7 billion.
 - ▼ A substantial portion of the company's sales is derived from outside the United States. This exposes the company to exchange rate fluctuations and counterparty default risk. Although the risk is reduced to a certain extent by a netting strategy based on a given currency, some of the fluctuation is likely to persist as more and more services offered by the company are shifted to lower-cost regions.
 - ▼ The company operates in the IT and professional services markets, which are dominated by a large number of companies offering similar services. Some of the major competitors are Accenture plc and IBM Global Services. DXC Technology competes with Amazon Web Services in the cloud computing market. Apart from this, cloud computing service is a growing business where the company faces competition from several small and large players.
 - ▼ The company has a large service contract with the U.S. government. Such contracts are subject to extensive and stringent legal and regulatory hurdles, which are changed from time to time. Also, the time taken to secure a government contract is substantial due to the time-consuming decision-making process. Apart from this, the U.S. government investigates operations at intervals to ensure that the terms and conditions have been properly adhered to. Any deviation may result in huge penalties or contract termination.
 - ▼ The company is experiencing continued decline in its traditional infrastructure business for several quarters. This is keeping the top line under pressure.
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Rising interest expenses due to increased debt burden may dampen its profitability.

Last Earnings Report

DXC Technology Q2 Earnings & Revenues Lag Estimates

DXC Technology reported weak second-quarter fiscal 2020 results wherein both the bottom line and top line lagged the Zacks Consensus Estimate. Moreover, both figures decreased on a year-over-year basis.

The company reported non-GAAP earnings of \$1.38 per share, which missed the consensus estimate of \$1.44. The figure also declined from \$2.02 reported a year ago.

At \$4.85 billion, revenues fell short of the prior-year quarter's number by 3.2% and also slipped 0.8% on constant currency basis. Moreover, the metric lagged the Zacks Consensus Estimate of \$4.92 billion.

Continued decline in traditional infrastructure business, and currency headwinds affected revenues.

Moreover, delays in and loss of several large deals, particularly in the Americas and the U.K., which were expected to close during the fiscal second quarter, hurt the top line.

Quarter in Detail

Segment wise, revenues from Global Business Services ("GBS") jumped 8.2% on a year-over-year basis to \$2.29 billion, reflecting strength in the Luxoft business. Contribution from Luxoft more than offset foreign exchange headwinds, which affected revenues by 2.3%. The acquisition of Luxoft also boosted the company's digital revenues, which soared 52% year over year to \$1.51 billion.

During the quarter, DXC Technology also announced a partnership with Google Cloud to aid and enhance the digital modernization journey of enterprise clients on Google Cloud Platform.

Notably, the company won \$1.9 billion worth of new business awards for the GBS segment.

Global Infrastructure Services ("GIS") revenues during the fiscal second quarter came in at \$2.57 billion, down 11.6% year over year, reflecting a decline in DXC Technology's traditional infrastructure business. A foreign exchange headwind of 2.5% was also a dampener.

During the quarter, the company won \$1.9 billion worth of new business awards for the GIS segment.

In the fiscal second quarter, DXC Technology acquired independent service management and security solutions provider, and leading ServiceNow partner — Syscom. This is expected to boost its security solutions offerings.

Industry IP and BPS revenues witnessed 0.3% year-over-year growth.

Margins

Adjusted EBIT margin was 10.9%, contracting 500 basis points year over year. Continued delays in delivery cost actions, and cost overruns on some European transformation contracts led to weak profit performance. Non-GAAP income from continuing operations was \$492 million compared with \$749 million a year ago.

Balance Sheet and Other Financial Metrics

The company exited the quarter with \$2.88 billion in cash and cash equivalents compared with \$1.90 billion in the previous quarter. Long-term debt balance (net of current maturities) was \$7.7 billion. Adjusted free cash flow was \$739 million compared with \$72 million in the prior quarter.

During the fiscal second quarter, the company returned \$306 million to shareholders through share buybacks and dividend payments.

Outlook

DXC Technology expects currency headwinds, delays in the completion of several deals and pressure from its traditional business to negatively impact fiscal 2020 results, forcing the company to cut view.

Moreover, certain customers are placing revenue opportunities on hold due to delivery execution issues. This is expected to reduce full fiscal year revenues by \$250 million.

Also, a reduction of \$175 million is expected to accommodate the disruptions related to strategic alternatives for three of its businesses (U.S. State, local health and human services business; workplace; and mobility business) that the company plans to undertake.

For fiscal 2020, DXC Technology now estimates revenues of \$19.5-\$19.8 billion instead of \$20.2-\$20.7 billion. Non-GAAP earnings are expected in the range \$5.25-\$5.75 per share, down from previously expected \$7-\$7.5, due to lower revenues and delays in cost savings.

Quarter Ending **09/2019**

Report Date	Nov 11, 2019
Sales Surprise	-1.48%
EPS Surprise	-4.17%
Quarterly EPS	1.38
Annual EPS (TTM)	7.54

Recent News

On Jan 10, 2020, DXC subsidiary, Luxoft, announced a partnership with LG Electronics to accelerate the development of large-scale series production systems. These include digital cockpit systems, rear seat entertainment, cabin and center stack display, in-vehicle infotainment, and the like.

On Nov 4, 2019, DXC announced the buyout of customer experience solutions provider Blueleader. The acquisition is a part of DXC's focus on growth and investment in SAP-based customer experience solutions.

On Oct 23, 2019, DXC announced a partnership with smartShift Technologies to allow SAP customers to modernize, migrate and manage their SAP systems in the hyperscale cloud.

On Sep 12, 2019, DXC Technology appointed Mike Salvino as the new president and chief executive officer, succeeding Mike Lawrie.

Valuation

DXC Technology's shares have lost 38.4% in the past six months, and 42.9% over the trailing 12 months. Stocks in the Zacks sub-industry fell 0.1%, while the Zacks Computer & Technology sector have risen 14.6% in the past six months. Over the past year, the Zacks sub-industry and the sector gained 26% and 33.1%, respectively.

The S&P 500 Index has gained 9.9% in the past six months and 24.5% in the past year.

The stock is currently trading at 6.07X forward 12-month earnings, which compares with 23.28X for the Zacks sub-industry, 22.84X for the Zacks sector and 18.96X for the S&P 500 Index.

Over the past five years, the stock has traded as high as 26.71X and as low as 3.3X, with a 5-year median of 11.36X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$37 price target reflects 6.4X forward 12-months earnings.

The table below shows summary valuation data for DXC

Valuation Multiples - DXC					
		Stock	Sub-Industry	Sector	S&P 500
P/E F 12M	Current	6.07	23.28	22.84	18.96
	5-Year High	26.71	32.37	22.84	19.34
	5-Year Low	3.3	15.6	16.87	15.17
	5-Year Median	11.36	22.18	19.24	17.44
EV/EBITDA TTM	Current	1.79	28.34	12.41	12.12
	5-Year High	15.01	32.87	12.6	12.86
	5-Year Low	1.56	20.85	7.68	8.48
	5-Year Median	6.14	27.64	10.52	10.67
EV/Sales TTM	Current	0.74	5.22	4.33	3.29
	5-Year High	2.58	8.12	4.33	3.3
	5-Year Low	0.53	4.16	2.56	2.16
	5-Year Median	1.1	5.93	3.45	2.8

As of 01/14/2020

Industry Analysis Zacks Industry Rank: Top 35% (90 out of 254)



Top Peers

Accenture PLC (ACN)	Neutral
Amazon.com, Inc. (AMZN)	Neutral
Cognizant Technology Solutions Corporation (CTSH)	Neutral
Genpact Limited (G)	Neutral
Alphabet Inc. (GOOGL)	Neutral
International Business Machines Corporation (IBM)	Neutral
Microsoft Corporation (MSFT)	Neutral
R.R. Donnelley & Sons Company (RRD)	Neutral

Industry Comparison Industry: Computers - It Services				Industry Peers		
	DXC Neutral	X Industry	S&P 500	ACN Neutral	AMZN Neutral	IBM Neutral
VGM Score	A	-	-	D	C	B
Market Cap	8.96 B	3.37 B	24.31 B	132.05 B	926.86 B	120.29 B
# of Analysts	6	5	13	11	13	8
Dividend Yield	2.40%	0.00%	1.76%	1.54%	0.00%	4.77%
Value Score	A	-	-	D	D	A
Cash/Price	0.31	0.06	0.04	0.04	0.05	0.09
EV/EBITDA	3.86	11.99	14.08	17.98	32.33	10.33
PEG Ratio	1.49	1.93	2.06	2.57	2.60	2.06
Price/Book (P/B)	1.03	5.37	3.33	8.46	16.40	6.65
Price/Cash Flow (P/CF)	2.15	15.29	13.62	23.31	36.13	7.20
P/E (F1)	6.40	21.97	18.86	26.55	71.27	10.28
Price/Sales (P/S)	0.44	1.72	2.65	3.00	3.49	1.56
Earnings Yield	15.62%	2.90%	5.27%	3.76%	1.40%	9.73%
Debt/Equity	1.00	0.23	0.72	0.17	0.40	3.40
Cash Flow (\$/share)	16.25	1.39	6.94	8.91	51.74	18.86
Growth Score	B	-	-	C	A	D
Hist. EPS Growth (3-5 yrs)	20.95%	16.94%	10.56%	11.25%	116.18%	-3.75%
Proj. EPS Growth (F1/F0)	-34.43%	9.62%	7.52%	6.31%	27.90%	3.21%
Curr. Cash Flow Growth	1.14%	14.90%	14.88%	8.06%	85.21%	-1.93%
Hist. Cash Flow Growth (3-5 yrs)	21.84%	16.56%	9.00%	9.75%	48.43%	-5.41%
Current Ratio	0.95	1.32	1.23	1.39	1.10	1.09
Debt/Capital	49.91%	37.45%	42.99%	14.60%	28.45%	77.29%
Net Margin	-6.04%	1.78%	11.14%	11.06%	4.27%	10.00%
Return on Equity	18.89%	12.44%	17.16%	33.35%	22.52%	67.12%
Sales/Assets	0.67	0.81	0.55	1.48	1.45	0.55
Proj. Sales Growth (F1/F0)	-5.36%	8.61%	4.18%	6.66%	18.55%	2.94%
Momentum Score	A	-	-	D	F	A
Daily Price Chg	-1.52%	0.00%	0.08%	-0.89%	-1.16%	-0.57%
1 Week Price Chg	1.45%	1.33%	0.39%	-1.02%	0.44%	1.75%
4 Week Price Chg	-5.17%	5.88%	1.93%	2.13%	4.40%	1.19%
12 Week Price Chg	26.25%	16.16%	6.50%	13.69%	5.87%	1.39%
52 Week Price Chg	-42.33%	17.89%	22.56%	41.42%	11.64%	11.57%
20 Day Average Volume	2,699,102	239,746	1,571,506	2,032,784	3,221,894	3,032,016
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	0.00%	0.05%
(F1) EPS Est 4 week change	0.03%	0.00%	0.00%	0.54%	-1.03%	0.18%
(F1) EPS Est 12 week change	-25.06%	-0.70%	-0.52%	0.56%	-18.79%	-0.26%
(Q1) EPS Est Mthly Chg	0.20%	0.00%	0.00%	-0.66%	-2.70%	0.00%

Zacks Stock Rating System

We offer two rating systems that take into account investors' holding horizons: Zacks Rank and Zacks Recommendation. Each provides valuable insights into the future profitability of the stock and can be used separately or in combination with each other depending on your investment style.

Zacks Recommendation

The Zacks Recommendation aims to predict performance over the next 6 to 12 months. The foundation for the quantitatively determined Zacks Recommendation is trends in the company's estimate revisions and earnings outlook. The Zacks Recommendation is broken down into 3 Levels; Outperform, Neutral and Underperform. Unlike many Wall Street firms, we have an excellent balance between the number of Outperform and Neutral recommendations. Our team of 70 analysts are fully versed in the benefits of earnings estimate revisions and how that is harnessed through the Zacks quantitative rating system. But we have given our analysts the ability to override the Zacks Recommendation for the 1200 stocks that they follow. The reason for the analyst over-rides is that there are often factors such as valuation, industry conditions and management effectiveness that a trained investment professional can spot better than a quantitative model.

Zacks Rank

The Zacks Rank is our short-term rating system that is most effective over the one- to three-month holding horizon. The underlying driver for the quantitatively-determined Zacks Rank is the same as the Zacks Recommendation, and reflects trends in earnings estimate revisions.

Zacks Style Scores

The Zacks Style Score is as a complementary indicator to the Zacks rating system, giving investors a way to focus on the highest rated stocks that best fit their own stock picking preferences.

Academic research has proven that stocks with the best Value, Growth and Momentum characteristics outperform the market. The Zacks Style Scores rate stocks on each of these individual styles and assigns a rating of A, B, C, D and F. We also produce the VGM Score (V for Value, G for Growth and M for Momentum), which combines the weighted average of the individual Style Scores into one score. This is perfectly suited for those who want their stocks to have the best scores across the board.

Value Score	A
Growth Score	B
Momentum Score	A
VGM Score	A

As an investor, you want to buy stocks with the highest probability of success. That means buying stocks with a Zacks Recommendation of Outperform, which also has a Style Score of an A or a B.

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