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Science Applications International Corp.

(SAIC)

Q2 2020 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good day and welcome to the SAIC Fiscal Year 2020 Second Quarter Earnings Call. Today's conference is being recorded. At this time, I would like to turn the conference over to Shane Canestra, SAIC's Vice President of Investor Relations. Please go ahead, sir.

Shane P. Canestra

Vice President-Investor Relations, Science Applications International Corp.

Good afternoon. My name is Shane Canestra, SAIC's Vice President of Investor Relations, and thank you for joining our second quarter fiscal year 2020 earnings call. Joining me today to discuss our business and financial results are Nazzic Keene, SAIC's Chief Executive Officer; Charlie Mathis, our Chief Financial Officer; and other members of our management team.

This afternoon, we issued our earnings release, which can be found at investors.saic.com, where you'll also find supplemental financial presentation slides to be utilized in conjunction with today's call. Both of these documents, in addition to our Form 10-Q to be filed soon, should be utilized in evaluating our results and outlook along with information provided on today's call.

Please note that we may make forward-looking statements on today's call that are subject to known and unknown risks and uncertainties that could cause actual results to differ materially from statements made on this call. I refer you to our SEC filings for a discussion of these risks, including the Risk Factors section of our Annual Report on Form 10-K and Quarterly Reports on Form 10-Q.

In addition, the statements represent our views as of today, and subsequent events may cause our views to change. We may elect to update the forward-looking statements at some point in the future, but we specifically disclaim any obligation to do so.

In addition, we will discuss non-GAAP financial measures and other metrics, which we believe provide useful information for investors, and both our press release and supplemental financial presentation slides include reconciliations to the most comparable GAAP measures.

It is now my pleasure to introduce our CEO, Nazzic Keene.

Nazzic S. Keene

Chief Executive Officer & Director, Science Applications International Corp.

Thank you, Shane, and good afternoon. SAIC took another positive step forward in the second quarter of fiscal 2020, keeping our attention on operational performance, progressing on the integration of the Engility acquisition, and delivering strong financial and business development results. While Charlie will discuss the financial results in greater detail, our second quarter reflects strength and a contract portfolio that is aligned to key areas of our market, with strong profitability and free cash flow generation.

The second quarter delivered revenues of $1.6 billion, in line with our expectations and equating to a 43% total revenue growth from the prior-year quarter. Strong adjusted EBITDA margins were 8.4% for the second quarter, up 90 basis points from last year. The cash generation profile of the company continues to be compelling, with second quarter and first half cash flow providing continued confidence in our full-year target and enabling capital deployment for shareholder value creation.

Net bookings for the quarter were approximately $1.9 billion, excluding about $400 million of single award IDIQ vehicles, translating to a quarterly book-to-bill of 1.2. On a pro forma basis, SAIC's trailing 12 months book-to-bill is 1.1.

During the quarter, SAIC was awarded contracts in past quarters valued at over $1 billion of recompete and new business from U.S. national security and intelligence customers. These awards also demonstrate the intersection of two areas of significant opportunities for growth: space and IT modernization. It is very exciting to see the continuing buildup momentum as a stronger SAIC goes to market with these important customers. Additionally, SAIC was awarded a recompete contract valued at $117 million from NASA to continue providing a variety of IT services to support the National Center for Critical Information Processing and Storage.

Also in the recompete category was a $93 million contract award from the U.S. Navy to support electronic warfare activities. Awarded during the quarter but not immediately contributing to bookings was a new business award of $106 million single-award IDIQ contract with the Defense Intelligence Agency to provide media management and analysis efforts across the science and technology directorate.

SAIC continues to operate in a favorable market environment in the closing months of government's fiscal year 2019, and looking forward, into fiscal 2020. As appropriations are enacted, we do not expect significant shifts in budget priorities, and SAIC is well aligned in areas of national importance and funding, such as space-related missions, IT modernization, and readiness, among others.

Although a few customers have expressed concerns around facing the potential continuing resolution to start the government fiscal year, for now, proposal activity remains strong, as demonstrated in the momentum we see in our business development activities. Customer demand and our pipeline of qualified pursuits is expanding, although we have also seen delays in some contract awards due to protests or new business that has not materialized.

At the end of the second quarter, SAIC's total contract backlog sit at approximately $13.9 billion, up about 3% from the first quarter. Funded backlog was approximately $2.6 billion. The estimated value of SAIC's submitted proposals awaiting award is $13.4 billion, up from the end of the first quarter. Approximately 75% of submitted proposals are for new business, an indicator of a favorable market environment, our low level of recompetes this fiscal year, and the potential for SAIC to accelerate growth over time.

Before turning the call over to Charlie, I'd like to provide you an update on the integration of Engility. As I mentioned in our June call, we have successfully achieved all of the year one cost synergies and are on track to realize year two synergy targets next year. In fact, we recently achieved another critical milestone: the successful integration of many business systems, which is key to achieving our year two cost synergies. This is a significant achievement in the integration process, and I believe one of the earliest acquisition-related systems integrations in our space. I want to personally thank the team for their tremendous effort and success in achieving this important milestone.

Through the end of the year, we will focus on two additional integration milestones: harmonizing employee benefits and rationalizing our facility footprint. We have more work ahead of us, but I'm very proud of the newly combined team and what we've accomplished so far.

Charlie, over to you for our financial results.

Charles Alexander Mathis

Executive Vice President & Chief Financial Officer, Science Applications International Corp.

Thank you, Nazzic. Our second quarter revenues of approximately $1.6 billion reflect total revenue growth of 43%, which were due to revenues associated with the Engility acquisition. Organic revenue therefore was flat year-over-year, although adjusting for about $30 million of revenue dis-synergies in the quarter, organic revenue growth increased approximately 2%.

As a reminder, we have previously communicated an approximate $100 million of revenue dis-synergies for the full fiscal year due to elimination of prime sub revenue, lower revenue on cost-plus contracts due to cost synergy achievement, and other factors.

Second quarter adjusted EBITDA margins were again strong at 8.4% as a percentage of revenues, up 90 basis points from the prior year. Second quarter adjusted EBITDA was $134 million, a $50 million increase from the prior year. Adjusted EBITDA excludes $6 million of integration-related cost in the quarter. Second quarter margins, similar to our first quarter, was due to strong program performance and the favorable effect of accelerating our net cost synergies.

Net income for the second quarter was $57 million, and excluding $6 million of integration cost, as well as amortization of intangibles, our adjusted diluted earnings per share was $1.35 for the second quarter, an increase of 11% from the prior-year quarter. In addition, the year-to-date adjusted EPS accretion is also 11%. Diluted earnings per share was $0.96, inclusive of the $6 million of integration cost I just mentioned. The effective tax rate for the quarter was approximately 23%, consistent with our previously communicated and reaffirmed today expected full-year rate of 22% to 24%, with a cash tax rate also unchanged at 13% to 15%, benefited by the tax assets acquired from Engility.

Second quarter operating cash flow and free cash flow were a very strong $95 million and $90 million, respectively, due to excellent cash collections and reduced working capital. Historically, our second quarter cash flow is the seasonally lowest cash generation quarter of the year due to an additional payroll cycle as compared to the other three quarters and two income tax payments. I am very pleased with the free cash flow generation we have achieved since the close of the acquisition.

Free cash flow for the quarter is $114 million increase from last year, and on a year-to-date basis, has increased approximately $200 million over the first half of last year. In addition, we have achieved approximately 60% of our full-year target to date. Days sales outstanding at the end of the quarter were 59 days.

During the second quarter, we deployed $156 million of capital, consisting of $133 million to repurchase approximately 1.6 million shares, $21 million in dividends, and $2 million of mandatory debt repayment. With regards to share repurchases, we announced in early July $100 million negotiated buyback from one of our private equity shareholders, KKR, that repurchased approximately 1.2 million shares from them directly at a discount to the previous date's closing price. We believe this acceleration of our capital deployment plan in fiscal year 2020 is in the best interests of long-term shareholders. We will continue to be thoughtful and disciplined with regards to the deployment of capital for shareholder value creation.

I should note that our board of directors will meet in mid-September and will consider capital deployment opportunities going forward, including our next quarterly dividend that is typically payable to shareholders in October.

Now turning to our forward outlook, we exceeded our expectation for revenue in the first half of the year, but we are cautious about a revenue increase in our second half. As Nazzic mentioned, our outlook is impacted by the potential for a continuing resolution, new business that has been protested or has not materialized, and higher revenue dis-synergies, partially due to accelerated cost synergy achievement. We expect second half revenues to be consistent with our first half revenues of $3.2 billion. This revenue outlook for the year does not impact our longer-term outlook, as contract award opportunities and business momentum is building.

I'm very pleased with the strong margin and cash flow performance in the first half of the year, which gives us confidence in our full-year outlook. As far as margins, our full-year adjusted EBITDA margin is expected to increase about 80 basis points from the prior-year standalone SAIC adjusted EBITDA margin of 7.5%, which is at the middle to upper end of our previously communicated expectations. Our more favorable outlook on margins is due to our first half performance, better than expected cost synergy achievement, and continued focus on operational and program performance.

Our free cash flow target remains at $425 million for the fiscal year. With our strong first half collections, working capital improvements, and continued focus on achieving additional balance sheet synergies, we are confident we can meet or exceed this goal for the year.

Nazzic, back to you for concluding comments.

Nazzic S. Keene

Chief Executive Officer & Director, Science Applications International Corp.

Thanks, Charlie. I am very excited to have officially become the Chief Executive Officer at the beginning of August. With our new scale and reach, SAIC has the opportunity to be a stronger partner for our customers with an expansive portfolio of solutions. We also have a deeper bench of talent and expertise in our company, which allows us to create a differentiated experience for our employees, with broader career development options. With these new opportunities, the leadership team and I are taking a fresh look at our long-term business strategy, the initiatives to execute on that plan, and the key performance indicators to gauge success.

As we refresh our long-term strategy to shape our priorities, there are three areas that have my immediate attention: the successful integration of Engility, driving profitable revenue growth, and winning our war for talent. As you know, these three items are not mutually exclusive in the government services space. Our success will be enabled by our talented employees who are inspired by purpose and are driven to grow our company by bringing innovative solutions to solve our customers' toughest mission challenges.

We have recently announced some leadership changes that reflect this intensified focus on our employees. We welcomed two new board members to SAIC: Carol Goode and Yvette Kanouff. Both Carol and Yvette are proven strategic leaders who've established their careers in [ph] high tech (00:14:05) companies in Silicon Valley in the San Francisco Bay Area. They bring diverse perspectives and fresh ideas, and we are excited to get their counsel as we shape our talent and solution strategies. I look forward to working with these two strong leaders, and I am confident they will have an immediate impact on our organization and our ability to deliver business results.

As a newly integrated organization led by a strong leadership team, SAIC aims to leverage our new market opportunities and employ the best talent in the industry. With a strong foundation of passionate and skilled team members, we are in a position to change our growth trajectory. SAIC is focused on three tenets for success: inspire employees, accomplish customer missions, and reward shareholders.

Operator, we're now ready to take questions.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] We'll go first to Edward Caso with Wells Fargo.

Edward S. Caso
Analyst, Wells Fargo Securities LLC

Q

Hi, good evening. I'm hoping that you have a positive answer to this question, just curious how your operations are doing down in Charleston, South Carolina given the Dorian hurricane?

Nazzic S. Keene
Chief Executive Officer & Director, Science Applications International Corp.

A

Yeah. So at this point – hi, Ed; it's Nazzic. At this point, we've closed the facility and certainly wanted to support all the employees being able to get to a safer place. I have not heard of any catastrophic issues at this point, but it's something we pay tremendous attention to up and down the East Coast over the course of these last few days, but we appreciate you asking. It is very important to us.

Edward S. Caso
Analyst, Wells Fargo Securities LLC

Q

Great. And one – and different question, what bookings do you have or what awards do you have that are still in protest, or how big is that number? [ph] Actually one (00:16:12) that's still in protest.

Charles Alexander Mathis
Executive Vice President & Chief Financial Officer, Science Applications International Corp.

A

About $1 billion.

Nazzic S. Keene
Chief Executive Officer & Director, Science Applications International Corp.

A

We have a couple, and about $1 billion still in protest.

Edward S. Caso
Analyst, Wells Fargo Securities LLC

Q

Thank you.

Nazzic S. Keene
Chief Executive Officer & Director, Science Applications International Corp.

A

Thanks, Ed.

Operator: And we'll go next to Jon Raviv with Citi.

Jon Raviv
Analyst, Citigroup Global Markets, Inc.

Q

Hey, guys. Thank you. On the sales outlook for the year, can you just give us a little more detail on essentially what's going on? You mentioned a few things driving that revised outlook for the year. Kind of what new business is not materializing? Is that SAIC stuff? Is it Engility stuff? Is it integrated opportunity stuff? Is it mostly timing where it flips? Is it things that you expected to win but you lost? Like just give us some more sense of why it looks like you have finished the year below the sales target you identified on the last call.

Charles Alexander Mathis
Executive Vice President & Chief Financial Officer, Science Applications International Corp.

A

Yes. Thanks, Jon. So let me just clarify and give some additional color on that. So we expect revenues to be consistent with the first half of $3.2 billion. We're cautious in increasing the revenue outlook for the second half, and the factors are three, the first of which is we are anticipating higher revenue dis-synergies for the full year. Partially related to our success and accelerating the cost synergies, we're expecting revenue dis-synergies of $120 million now, up 20% from our previous expectations. As you know, reducing costs lowers revenue on our cost-plus contracts and we're approximately 60%. However, this is a one-time impact of our FY 2020 growth, it's about a 2% headwind to the revenue growth, the $120 million.

With the acceleration of the cost synergies that have strengthened our market outlook for the year, and as I mentioned previously, we expect an 80 basis point increase from last year's standalone SAIC, and this is to the middle upper end of the margin range that we previously communicated.

Now the other two factors that are impacting the revenue outlook are items that Nazzic mentioned, which are the protest in new business not materializing, and think here of a particular Air Force contract that was awarded back in the spring, it's gone through a protest cycle and more, and continues to go through that. And also, a few – and I'll emphasize the word few – customer concerns around our continuing resolution to start a fiscal year. We do see this as a timing issue. We do not see this impacting the long-term revenue outlook.

The pipeline proposal is very strong. We're encouraged by the strength of the company, more profitability of $13.5 billion of proposals awaiting to be awarded, of which 75% of these are new business. So, we feel confident with the long-term outlook there.

Jon Raviv
Analyst, Citigroup Global Markets, Inc.

Q

I'm sorry, did I miss the third factor?

Charles Alexander Mathis
Executive Vice President & Chief Financial Officer, Science Applications International Corp.

A

The third factor was the – a few, and again...

Jon Raviv
Analyst, Citigroup Global Markets, Inc.

Q

[ph] Oh, I see (00:19:35).

Charles Alexander Mathis
Executive Vice President & Chief Financial Officer, Science Applications International Corp.

A

...emphasizing on a few customer concerns around the CR to start the fiscal year.

Jon Raviv
Analyst, Citigroup Global Markets, Inc.

Q

Yeah. Okay. Thanks. Thanks very much for that thorough answer. And then just on the free cash flow, you mentioned that first half performance thus far has been quite strong. Is there any timing helping that, the performance in first half 2020? And then also thinking more towards the [ph] approaching 522 (00:19:56), what are some of the drivers of sustainability thereafter? We know there's a tax boost in there, but what about things like working capital? Thank you.

Charles Alexander Mathis
Executive Vice President & Chief Financial Officer, Science Applications International Corp.

A

Yeah. So thanks for that. And I can tell you, I'm extremely pleased with the outstanding job that our operation and finance teams did to achieve this. They've been really focused and continue to make progress on the process improvements. And with the two companies combined, we're getting paid timely. We're looking to incorporate some of the best practices from the combination of the companies. And so I'm very pleased.

I know those people are probably listening to this call, so I can tell them, again I'm very pleased with their achievement the first half of the year. They achieved 60% of the goal. And we're sticking with the [ph] 425 (00:20:53) right now. We do have a systems conversion that just was completed this month. And although it went incredibly well, we'll wait another quarter to see how the cash collections [indiscernible] (00:21:06) before increasing our outlook. Our longer-term outlook remains intact as we said. And so, yes, we believe in – we will get to the $500 million by year three that we outlined earlier in the year.

Jon Raviv
Analyst, Citigroup Global Markets, Inc.

Q

Thanks. I'll hop back in the queue.

Operator: And we'll go next to Matthew Sharpe with Morgan Stanley.

Matthew Sharpe
Analyst, Morgan Stanley & Co. LLC

Q

Good afternoon. I was just wondering if you guys could give us a sense of how the current quarter bookings are shaping up, being that it tends to be a higher volume period with the end of the government fiscal year at the end of this month.

Nazzic S. Keene
Chief Executive Officer & Director, Science Applications International Corp.

A

Yeah, this is Nazzic. So, yes, historically, Q3 for us tends to be a higher bookings quarter, and we're seeing proof point to that as we go into the quarter with the activity over the last couple of quarters and getting things into submit state. So we feel very confident with our third quarter bookings. Again, [ph] there was the nuances (00:22:12) that we navigate is looking at these contract awards, as well as these single-award IDIQs. We still have many customers that tend to use single-award IDIQs as their contract vehicle of choice. So, yes, we do believe we're going into the quarter with strong position from a sales perspective, [ph] and typically have a (00:22:32) strong quarter.

Matthew Sharpe
Analyst, Morgan Stanley & Co. LLC

Q

And then on the Air Force EDIS contract which you just alluded to a few moments ago, and then the Department of Justice Asset Forfeiture Program, do you guys have any color around those programs in terms of when they might be resolved or awarded? I know that they were probably expected last month or so and they've dragged out a little bit longer than expected.

Nazzic S. Keene
Chief Executive Officer & Director, Science Applications International Corp.
A

Yeah. So the short answer is, we don't exactly know when those things are going to transpire. Certainly on the DOJ one could happen any time, and so we're continuing to look at that. As it relates to EDIS, they are going through their process, and so that will probably take another weeks or months at this point, but it's hard to tell.

Matthew Sharpe
Analyst, Morgan Stanley & Co. LLC
Q

Got it. And then just one last one, if I could, on the integration of Engility, it seems as though you guys are, at this point in time, well ahead of schedule on cost takeout or cost synergies. Are you seeing any opportunity at this point in time to beat your initial targets or upside to where you thought you might be?

Nazzic S. Keene
Chief Executive Officer & Director, Science Applications International Corp.
A

Yeah. So totally agree with your statement on where we sit today. So we're very pleased. I'm very pleased with where we are. We just did a system conversion. We've done – the organization is fully integrated as I've shared with you before, and a lot of those decisions were made very, very early on in our acquisition cycle. So, extremely pleased with how the companies have come together, and we're seeing great proof points in going to market together as well, as we look to leverage the capabilities across the entire portfolio to drive a stronger proposal activity and drive incremental growth opportunities.

As it relates to the cost synergies, yes, we are ahead of plan. We're very, very happy about that, and we'll continue to look at every opportunity we can to drive additional cost out of the equation. That's certainly top of mind for us. But as we do that, we also want to balance the need to invest in growth, and so we're looking at the trade space that exists to drive the profitability that we aspire to drive and that we've communicated as a result of this acquisition, but also look to invest in growth to drive the long-term value creation.

Matthew Sharpe
Analyst, Morgan Stanley & Co. LLC
Q

Great. Thanks. I'll get back in the queue.

Nazzic S. Keene
Chief Executive Officer & Director, Science Applications International Corp.
A

[ph] Thank you (00:25:00).

Operator: We'll go next to Cai von Rumohr with Cowen and Company.

Cai von Rumohr
Analyst, Cowen and Company, LLC
Q

Thanks so much and great quarter.

Nazzic S. Keene
Chief Executive Officer & Director, Science Applications International Corp.
A

Thanks, Cai.

Cai von Rumohr
Analyst, Cowen and Company, LLC
Q

So could you give us a little more color on the revenue guidance? Normally, your third quarter is stronger than your fourth. Is that kind of a pattern, or is there going to be something different? And how much of the shortfall would you say is at Engility as opposed to heritage SAIC?

Charles Alexander Mathis
Executive Vice President & Chief Financial Officer, Science Applications International Corp.
A

Hey, Cai, this is Charlie. I would just say that we don't really give the guidance [ph] before (00:25:41) quarterly revenue [ph] as they're (00:25:43) fairly consistent expectations third and fourth quarter, and we don't break out the Engility right now as fully integrated into the company. And so we're looking at one company [ph] and declines their (00:25:59) revenue that goes down with SAIC.

Cai von Rumohr
Analyst, Cowen and Company, LLC
Q

When you say revenues consistent third and fourth quarter, you mean third quarter should be close to the fourth, or consistent with prior patterns where the third was better than the fourth?

Charles Alexander Mathis
Executive Vice President & Chief Financial Officer, Science Applications International Corp.
A

I would just say that they're consistent quarter-to-quarter.

Cai von Rumohr
Analyst, Cowen and Company, LLC
Q

Okay.

Charles Alexander Mathis
Executive Vice President & Chief Financial Officer, Science Applications International Corp.
A

[indiscernible] (00:26:21).

Cai von Rumohr
Analyst, Cowen and Company, LLC
Q

And then margins in the first quarter, you had $8 million of favorable EACs, and you said this is kind of above average normal; normal is $4 million. How much was it in the second quarter, and what's your outlook now for the year for EACs?

Charles Alexander Mathis
Executive Vice President & Chief Financial Officer, Science Applications International Corp.
A

It was $4 million EAC favorable adjustments in Q2, and that's the kind of normal run rate that we've seen, and we would continue to expect that in the second half of the year.

Cai von Rumohr
Analyst, Cowen and Company, LLC
Q

Terrific. And last one on cash flow, I'm a little confused. I mean, you talked of strong collections, and yet the DSOs were 59 days in the first (sic) [second] (00:27:01) quarter, and you talked of the seasonal pressure of accounts payable, but it doesn't look like a payroll. It doesn't look like you kind of made any large payroll, and it doesn't look like there were two tax payments. So, maybe you can kind of explain those items if you would.

Charles Alexander Mathis
Executive Vice President & Chief Financial Officer, Science Applications International Corp.
A

Yeah. So the collections that we had were actually favorable from the combined company, when you look at combining Engility and SAIC, the DSOs, we're actually pleased with the 59 days there. There was also a reduction in working capital for the quarter of managing different aspects of working capital and inventory that also attributed to what was just an exceptional quarter, an exceptional first half, and our free cash flow generation.

Cai von Rumohr
Analyst, Cowen and Company, LLC
Q

And [ph] just so we're (00:28:08) going to have the extra payroll because it doesn't look like it hit this quarter when it normally does, and did you have the two tax payments in those quarter?

Charles Alexander Mathis
Executive Vice President & Chief Financial Officer, Science Applications International Corp.
A

Yes. Yes, we did. Yes. And the additional payroll, yes, I believe that that did also hit for the quarter. So, the good news on the tax payment side is that because of our cash tax rate being so low due to the Engility tax assets that we acquired, there is less impact to an additional tax payment in the quarter. So it's – I can just say, Cai, that there is tremendous focus on collecting timely, ensuring that we have billings outstanding and we get the billings out on time and that they're accurate, so that the customer pays without disputes, and so [ph] that where (00:29:17) collections are extremely good and there's continued focus on that, and continuing look at the process improvements that we have.

Cai von Rumohr
Analyst, Cowen and Company, LLC
Q

Terrific.

Charles Alexander Mathis
Executive Vice President & Chief Financial Officer, Science Applications International Corp.
A

So we're very, very pleased with – very pleased with...

Cai von Rumohr
Analyst, Cowen and Company, LLC
Q

Okay.

Charles Alexander Mathis
Executive Vice President & Chief Financial Officer, Science Applications International Corp.
A

...the results so far.

Cai von Rumohr
Analyst, Cowen and Company, LLC

Q

Thank you very much and a nice quarter.

Nazzic S. Keene
Chief Executive Officer & Director, Science Applications International Corp.

A

Thanks, Cai.

Charles Alexander Mathis
Executive Vice President & Chief Financial Officer, Science Applications International Corp.

A

Thank you.

Operator: And we'll go next to Sheila Kahyaoglu with Jefferies.

Sheila Kahyaoglu
Analyst, Jefferies LLC

Q

Hey. Thank you. Good afternoon. Just – Charlie, thank you for sizing the items that are hitting the $150 million impact for revenues this year. I guess, when you think about the protests and the delays in the contracts, how do you think about that changing, if at all, your 3% revenue growth CAGR through 2022, and how should we think about growth accelerating next year?

Charles Alexander Mathis
Executive Vice President & Chief Financial Officer, Science Applications International Corp.

A

Yeah. So we have confidence in our longer-term revenue outlook that we've laid out. As I mentioned, we have items that are impacting FY 2020 specifically, namely the $120 million of revenue dis-synergies. So again, as we look forward, we're encouraged by the strength in company, more profitable company at $13.5 billion of proposals waiting awards, which is up to the amount of 75% related to new business. So we're confident that we can hit this long-term revenue outlook. That has not changed, and a lot of these protests, contract delays being awarded is a timing issue, so that's not impacting our longer-term views.

Nazzic S. Keene
Chief Executive Officer & Director, Science Applications International Corp.

A

Yeah. The other thing I would add, just to give some color, Charlie touched on this, but if we look at – as I look at what's happening in the company around the development of the pipeline, the execution of the pipeline, the opportunity to leverage the best of both companies to drive revenue synergies and revenue opportunities, we are seeing those, we are seeing those come to fruition to the pipeline, and certainly, this juncture may happen in the early stages of submit.

So we are seeing some good momentum there. And as Charlie mentioned, the majority, vast majority of what we have in the submit state even today is for new business. So, as we continue to win our fair share of opportunities that are really in sweet spots for SAIC, we have confidence in growth over the course of next couple years.

Sheila Kahyaoglu
Analyst, Jefferies LLC

Q

Thanks for that, Nazzic. And I guess just to touch on that, you said $13 billion of bids and 75% are new business. Can you give us an idea of where you're bidding, and just to tie it into margins, first half margins are 8.4% EBITDA. Your target is [ph] 8.8%. Of course, you're (00:32:03) already at that high end. You'd previously stated second half would be better. I guess does anything prohibit you from continuing to expand margins?

Nazzic S. Keene
Chief Executive Officer & Director, Science Applications International Corp.

A

No. So certainly the different programs have different margin profiles. And as we have a significant portion of our portfolio in a cost-plus structure, that in and of itself provides some guardrails, I would say. But as we look at here, an example would be the IT modernization that is top of mind for us, something that SAIC felt that, in some cases, those proposals are submitted on fixed price basis gives us higher confidence of being able to generate greater profitability over the months and years to come, but it – we continue to drive sales across the entire portfolio but are very, very focused on some key areas that has – where we are stronger because of the Engility acquisition.

We've touched on those areas like space; the space domain, we're seeing good traction. And that's across from a DOD, across the intel community, across the civilian part of the portfolio, where we see great opportunities based on what we know to be the government and certainly this administration's priorities, and we believe those are enduring. So we've got some great opportunities to drive growth as we look forward kind of coming out of this year.

Sheila Kahyaoglu
Analyst, Jefferies LLC

Q

Great. Thanks. Thank you.

Operator: We'll go next to Gavin Parsons with Goldman Sachs.

Gavin Parsons
Analyst, Goldman Sachs & Co. LLC

Q

Hey, good afternoon, everyone.

Nazzic S. Keene
Chief Executive Officer & Director, Science Applications International Corp.

A

Hello.

Gavin Parsons
Analyst, Goldman Sachs & Co. LLC

Q

Just on the customer CR concerns, some of your peers have sounded a little bit more optimistic about a two-year budget deal. I know we got a little bit of a sense of your exposure to shutdown on specific agencies at the beginning of this year. But would you say that's a more recent development like in the last few weeks or so, or is it just that you're inherently more – the work that you do is kind of more exposed to – or sensitive to a shutdown or a CR?

Nazzic S. Keene
Chief Executive Officer & Director, Science Applications International Corp.

A

So, I would say, I think it's a great question. And again, I think as Charlie mentioned, we're not seeing this concern across the entire portfolio by any means. We've just heard from a couple of customers that have some interesting work to start that they don't believe they can start until this particular item is resolved. So, it is – for us, it is isolated, but it is in a couple areas that have caused some headwinds as we go to the back half of the year. But I'm not hearing anything systemic. My sense is it's customer by customer depending on what needs to get done.

Gavin Parsons
Analyst, Goldman Sachs & Co. LLC

Q

Okay. Great. And then on book-to-bill, I appreciate there's a – somewhat of a different definition versus some of your peers, and this may be an oversimplification, but if I strip out the revenue headwinds, organic has kind of been 0% or so for the last 12 months. In the trailing 12 months, both funded and total book-to-bill has been about 1. So what kind of book-to-bill do we need to see for you to kind of accelerate growth to hit that 3% target or surpass it? I mean, what do we need on a funded or a total book-to-bill to see growth accelerate on a reported basis rather, not stripping out all those one-time pieces?

Charles Alexander Mathis
Executive Vice President & Chief Financial Officer, Science Applications International Corp.

A

Hey, Gavin, this is Charlie. I think a book-to-bill of the way we currently report it is 1.2 in that range gets us into that low-single-digit revenue growth. I would also emphasize that we don't include in the book-to-bill the single-award IDIQs of which are a bit over $3 billion in the last 12 months. So, we think that the pipeline for business is there in order to hit the longer-term outlook that we've given.

Nazzic S. Keene
Chief Executive Officer & Director, Science Applications International Corp.

A

And the only other caution I would give, and I know we've talked about this before, is book-to-bill is an indicator, it certainly isn't the indicator. And so we have to look at what's in the submit status, how much of the submits are new business versus recompete, and then obviously, take in consideration, as Charlie mentioned, the differences between single-award IDIQs and contract vehicles and the way that we categorize those. So, it's obviously something we pay a tremendous amount of attention to, it's important, but I think looking at book-to-bill in isolation doesn't necessarily tell the story either way quite candidly.

Gavin Parsons
Analyst, Goldman Sachs & Co. LLC

Q

Okay. Thank you.

Operator: We'll go next to Joseph DeNardi with Stifel.

Joseph William DeNardi
Analyst, Stifel, Nicolaus & Co., Inc.

Q

Yeah, hey. Good evening. Charlie, sorry to beat this horse to death, but just on $150 million, how much of that should we just kind of write off and how much should we move into FY 2021?

Charles Alexander Mathis
Executive Vice President & Chief Financial Officer, Science Applications International Corp.

A

So I would – look, most of this is a timing issue that we laid out here on these points. The one on the additional cost synergies is headwinds for this particular year that won't carry forward next year, and the remaining of those are really delays of awards or that are in protest. So I would think that these would obviously flow into next year as revenue stream.

Joseph William DeNardi
Analyst, Stifel, Nicolaus & Co., Inc.

Q

So do you think $50 million goes away and $100 million shows up next year?

Nazzic S. Keene
Chief Executive Officer & Director, Science Applications International Corp.

A

Well, this is Nazzic. So certainly, some of it actually goes away. So if you think about the prime sub relationships that existed prior to close of the transaction, those get pushed through the system and those are gone forever. Same with, to some extent, same with the impact of the cost takeout, you take the cost out that [ph] it will cost us construct (00:38:10). It also has an impact on revenue. So, I would consider those to be more isolated events that as we go the next year, certainly much of that will be behind us. So that's how I would think about this as you look at the kind of mapping.

Joseph William DeNardi
Analyst, Stifel, Nicolaus & Co., Inc.

Q

Okay. And then just on that customer feedback on concerns around the CR, can you talk about which customers specifically that you're hearing that from? Is it kind of intel, defense, [indiscernible] (00:38:39), any color there?

Nazzic S. Keene
Chief Executive Officer & Director, Science Applications International Corp.

A

No, I prefer not to do that. I will tell you that it's not isolated. Again, it's not a vast majority. It's just a few customers that are hesitant to start anything until the final budget cycle gets – kind of gets through the system. So – but again, it's not widespread. We're not hearing across the board but I probably prefer not to attribute it to any particular customer.

Q – [0795LW-E Joe DeNardi]>: Okay. Thank you.

Nazzic S. Keene
Chief Executive Officer & Director, Science Applications International Corp.

A

Thank you.

Operator: We'll go next to Tobey Sommer with SunTrust.

Jasper Bibb
Equity Research Associate, SunTrust Robinson Humphrey

Q

Thanks. This is Jasper Bibb on for Tobey today. We are hoping you could share how you view the logistics and supply chain business as part of the overall portfolio, and if you could provide some color on the outlook for that segment, that would be great. Thanks.

Charles Alexander Mathis
Executive Vice President & Chief Financial Officer, Science Applications International Corp.

A

Yeah. So it's Charlie. The logistics and supply chain business has actually been performing very well for this year, and it's consistent, it generates a ton of cash, it's a very stable business, very well run, although the margins there are lower, and it creates about a 40 to 50 basis points headwind to our overall portfolio in the margin side. But the economics of the supply chain business is quite well, and it's been performing well.

Jasper Bibb
Equity Research Associate, SunTrust Robinson Humphrey
Q

Okay, great. Thank you.

Operator: We'll go next to Josh Sullivan with Seaport Global.

Josh Sullivan
Analyst, Seaport Global Securities LLC
Q

Good afternoon. Yeah, so I understand here you had some customers preparing for the CR. But what are your expectations for the CR, if it comes in a full quarter, [ph] is that encompassed then in guidance here?

Nazzic S. Keene
Chief Executive Officer & Director, Science Applications International Corp.
A

Yeah. So obviously, I probably [ph] know (00:40:42) everything you know [ph] about (00:40:44) the CR [indiscernible] (00:40:45), so we all hope that this process goes through, the budget – the two-year budget cycle comes to a conclusion. If it doesn't, I would expect a relatively short CR, again we'll navigate it as we need to. And we don't see it as a significant impact to our business. Again, I touched on the fact we probably have a couple of contracts, and we do have a couple that are new work and are hesitant to start until this is resolved, but we've navigated the CR many, many times over the course of the last several years and so we don't see it as a high risk or high impact to business.

Josh Sullivan
Analyst, Seaport Global Securities LLC
Q

Okay, great. And then can you just comment on the Polaris JV and if that will be a [ph] successful product-like (00:41:25) kind of margin profile?

Charles Alexander Mathis
Executive Vice President & Chief Financial Officer, Science Applications International Corp.
A

Yeah. So that's the vehicle program that we're doing with Polaris, the joint venture. And this is one of which – this is very different from what we've done in the past with our vehicle platforms. And first, I would just want to clarify that aspect of it. This is one of which we are providing a similar type of work that we did with the MRAP upgrades, the C4ISR type of work, things that we've done very, very well over a number of years. And we're looking to do similar work there on this vehicle platform. We think we have a very good competitive vehicle, we're very excited about it. The margins would be similar to what we've done work previously. And I think we are going to have a couple of those on display at AUSA.

Nazzic S. Keene
Chief Executive Officer & Director, Science Applications International Corp.
A

Yeah, I do want to [indiscernible] (00:42:30) what Charlie said, and that is, it is a different type of program. So we did make a pivot after – as we've closed out last year, and [ph] if (00:42:39) we kind of rethought about what made the most sense for us in these major programs of record in manufacturing a vehicle.

And so we've elected to take a very different posture and position, and this is a great example of that where it's a proven vehicle. It is – and our role is really to help engineer it, to strengthen the C4ISR, and work with our partner in delivering a strong vehicle versus us owning the manufacturing of something along those lines. So it is a very different type of work for us as it relates to a previous vehicle platform, but very consistent as Charlie mentioned with the core capabilities inside of SAIC if you think about engineering and C4ISR, and I think it plays very well to those strengths.

Josh Sullivan
Analyst, Seaport Global Securities LLC

Q

Great. Thank you. Look forward to seeing at AUSA. Thanks.

Operator: We'll go next to Jon Raviv with Citi.

Jon Raviv
Analyst, Citigroup Global Markets, Inc.

Q

Okay. Thanks for the follow-up. On the $500 million target in FY 2022, just following up on that topic, how sustainable is that? I mean, we know there's a tax boost that rolled off at some point, but what other things are getting into that point beyond just profit growth? Is there working capital that rolls off? Just, again, trying to get an idea of how sustainable the $500 million is.

Charles Alexander Mathis
Executive Vice President & Chief Financial Officer, Science Applications International Corp.

A

No, it's a very sustainable number. There's nothing in there. There are tax assets that roll off in year seven, I think this is year three, where they start rolling off or coming down. So it's – we see it as sustainable. And also, I would like to mention on here the fact that we do have the $300 million optionality, when you exclude the dividends and exclude the mandatory debt payments over that three-year period of optionality for capital deployment over that three-year period as well. So, we see the $500 million continuing to grow as our profits will grow beyond year three.

Jon Raviv
Analyst, Citigroup Global Markets, Inc.

Q

Thanks for that clarification. And on deployment, with the acceleration of the FY 2020 repo plan with the ASR couple months ago, should we expect minimal activity through the rest of the second half, or is that something you're still going to evaluate in a couple weeks with the board meeting?

Charles Alexander Mathis
Executive Vice President & Chief Financial Officer, Science Applications International Corp.

A

With the strong free cash flow, we expect additional deployments in the second half, but we don't communicate our detailed future capital deployment plans. We'll be discussing that with our board of directors in the near future and get back to you on that.

Jon Raviv
Analyst, Citigroup Global Markets, Inc.

Q

Okay, great. If I could squeeze one more in just on, Nazzic, you talked about revisiting or maybe putting your [ph] stand (00:45:26) on the long-term business strategy today to include looking at some of the KPIs. Can you just set context for us? So what do you perceive – what's the starting point? What do you perceive to be the long-term business strategy now? What are the KPIs right now and where is that conversation starting, so to speak?

Nazzic S. Keene
Chief Executive Officer & Director, Science Applications International Corp.

A

Sure. Great questions. So really the driving factor for stepping back and refreshing our strategy with the acquisition of Engility, so this gives us a very different position in the market and some key areas that we believe will drive more than average growth. And so the objective was to set back, take a look at our existing strategy. Engility closed many of the gaps, if you think about greater access to the intel community, greater access to the space missions. And so what we're doing now is just taking a fresh look, and with the intent of getting better clarity and visibility on where the growth is going to come for the next one, two, five years, and also then aligning our resources and our investments to facilitate and drive that growth.

And so that's how we're thinking about it right now. Again, I don't – it's not going to be a radical right turn. I think SAIC is exceptionally well-positioned in a terrific market, and the type of work that we do and the solutions that we bring to bear are very consistent with the national priorities. And so we just want to take a fresh look, step back, and ensure that we absolutely are focused in the right areas now that we are a bit different company with Engility joining the SAIC family, and that really is what's driving that. Does that help?

Jon Raviv
Analyst, Citigroup Global Markets, Inc.

Q

Yeah. Thanks. Thanks a lot, Nazzic.

Nazzic S. Keene
Chief Executive Officer & Director, Science Applications International Corp.

A

Okay. Sure.

Operator: We'll go next to Joseph DeNardi with Stifel.

Joseph William DeNardi
Analyst, Stifel, Nicolaus & Co., Inc.

Q

Yes. Thanks for the follow-up. Nazzic, can you just talk about kind of how pleased you are thus far with talent retention and Engility? And then just more broadly, from an M&A appetite standpoint, are you in a position, do you have the capacity to do more acquisitions now, do you want to wait? What's your feeling there? Thank you.

Nazzic S. Keene
Chief Executive Officer & Director, Science Applications International Corp.

A

You bet. So on the people side and the attrition side, I'm very pleased with where we sit today, and we've monitored this, as you could probably imagine, our assets are our people. And so we monitor this on a very regular basis and has been – we've been doing that since we closed the transaction. But the decisions we made early on, the blending of the leadership teams, the full integration from a organizational standpoint of the companies happening on day one really contributed to – I believe attributed to our ability to retain the talent that we need, and especially as we think about [ph] the cleared (00:48:08) resources that are so critical to our business.

So, I'm extremely pleased with where we are. And – but with that being said, we're not – I'm not considering it done or considering it finished until we get through this year, get to the next couple milestones, and really begin to see the revenue opportunities that I know we'll be able to see as we go into next year. So that's that on the people side.

On the M&A side, so from a capacity standpoint, we absolutely have the capacity. The strength of SAIC now as a result of the Engility acquisition, Charlie touched on the cash profile, and so we certainly have the capacity. My first and foremost priority is to continue the successfully integration of Engility, and so that comes first. But with that being said, you can't always control what comes to market when, and we'll continue to look at M&A opportunities that would facilitate growth in either in capability sets or in customer [ph] assets (00:49:04), and so we keep our eyes open, we continue to engage in conversations when something comes across the desk to make sure that it's something that you either want to take look at or not, but I will tell you, it's not our highest priority as we sit here today.

Joseph William DeNardi
Analyst, Stifel, Nicolaus & Co., Inc.

Q

Thank you.

Operator: At this time, I would like to hand the call back over to our speakers for any additional or closing remarks.

Shane P. Canestra
Vice President-Investor Relations, Science Applications International Corp.

Thank you very much for your participation in SAIC's second quarter fiscal year 2020 earnings call. This concludes the call, and we thank you for your continued interest in SAIC.

Operator: That does conclude today's conference. We thank you for your participation.