

Q3 2025 Earnings Call

Company Participants

- Joseph DeNardi, Senior Vice President of Investor Relations and Treasurer
- Prabu Natarajan, Executive Vice President and Chief Financial Officer
- Toni Townes Whitley, Chief Executive Officer

Other Participants

- Analyst
- Cai von Rumohr, TD Cowen
- Ellen Page, Jefferies
- Jason Gursky, Citigroup
- Joshua Korn, Barclays
- Matthew Akers, Wells Fargo
- Seth Seifman, JPMorgan

Presentation

Operator

Good day, and welcome to SAIC's Third Quarter Fiscal Year 2025 Earnings Call. At this time, all participants are in a listen-only mode. After the speakers' presentation, there will be a question-and-answer session. Instructions will be given at that time. As a reminder, this call may be recorded.

I would now like to turn the call over to Joseph DeNardi, Senior Vice President of Investor Relations and Treasurer. Please go ahead.

Joseph DeNardi [{BIO 22467920 <GO>}](#)

Good morning, and thank you for joining SAIC's third quarter fiscal year 2025 earnings call. My name is Joe DeNardi, Senior Vice President of Investor Relations and Treasurer. And joining me today to discuss our business and financial results are Toni Townes Whitley, our Chief Executive Officer; and Prabu Natarajan, our Chief Financial Officer.

Today, we will discuss our results for the third quarter of fiscal year 2025 that ended November 1, 2024. 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. 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. The non-GAAP measures should be considered in addition to and not a substitute for financial measures in accordance with GAAP.

It is now my pleasure to introduce our CEO, Toni Townes Whitley.

Toni Townes Whitley

Thank you, Joe, and good morning to everyone on our call. My remarks will focus on three areas: first, a review of our operating performance in the third quarter; second, an update on the execution of our enterprise growth strategy; and third, our perspective on the potential risks and opportunities from the incoming administration's focus on driving greater efficiency across the federal government.

Our third quarter results reflect solid performance across the business and continued progress against our long-term strategy. We reported third quarter organic revenue growth of 4.3%, as increases from new business and on-contract growth offset an approximately 5-point headwind from contract transitions.

Adjusted EBITDA of \$197 million and margin of 10% reflect solid program performance across our portfolio. Adjusted diluted earnings per share of \$2.61 benefited from strong profitability and an approximately 16% effective tax rate in the quarter. Free cash flow of \$9 million was somewhat softer than what we typically produce in third quarter, due in part to an additional payroll cycle and very strong collections in our second quarter.

Overall, I'm pleased with the financial performance we delivered in the quarter, which allowed us to derisk the revenue challenge we highlighted last quarter, and we now expect full-year revenue growth of 3%, which is slightly ahead of the midpoint of our prior guidance. Prabu will discuss our updated guidance in greater detail in his prepared remarks.

On our enterprise growth strategy, to Bid More, Bid Better, and Win More, we're seeing improved progress on the first phase. With \$22 billion in submitted bids through the third quarter, we now expect to submit more than \$25 billion for the full-year, compared to our prior target of \$22 billion. We expect this momentum to continue in fiscal year '26 and '27, and are increasing our targets for submits in both years.

We now, in fact, see a pipeline to over \$30 billion of submits in fiscal year '27. Our backlog of submitted bids increased to nearly \$19 billion on a trailing 12-month basis in the third quarter, and increased from \$17 billion in the second quarter. While our bookings in the quarter of \$1.5 billion resulted in our trailing 12-months book-to-bill moderating to 0.9, we continue to have good visibility into reaching our target of 1.2 by the first half of fiscal year '26.

Importantly, as you can see on Slide 9, the quality of our pipeline and planned submits is improving as well, and becoming more aligned with our growth vectors, most notably Mission IT and Enterprise IT.

Now, regarding the recent emergence of plans from the incoming administration and the Department of Government Efficiency, let me first acknowledge the uncertainty this has created within the investment community. Given recent commentary from the incoming administration, we expect a renewed emphasis on increasing government efficiency, focused on deregulation, privatization of governmental functions, emphasizing fixed and incentive-based contracts over cost-plus, and certain program eliminations.

While our current revenue with agencies under particular scrutiny by DOGE is immaterial, we are preparing for a broader push for efficiency across the government, which could result in lower funding in certain of our markets. However, we believe that it's important to differentiate this

environment from prior downturns in spending, such as those caused by the Budget Control Act and sequestration, which resulted in arbitrary across-the-board cuts to agency budgets.

We expect the incoming administration's focus to be on driving efficiency through the deployment of technology, a very different approach than what drove sequestration. We believe we're well-positioned for the government transition because we have invested in technology differentiation and commercial offerings that are deployed currently and available to our customers at scale via a wide variety of channels and commercial marketplaces.

As I mentioned previously, our current strategy and pipeline will drive an acceleration in this portfolio shift, and we expect Mission IT and Enterprise IT to represent a greater portion of our revenue in the coming years. We believe this is relevant from a financial standpoint, given the improved margin profile of Mission and Enterprise IT, but also from a strategic perspective.

In an environment where doing more with less is a priority, having scale and capabilities in Mission and Enterprise IT position us well to better weather potential budgetary pressures while enabling efficiency with as-a-service and fixed-price solutions.

As shown on Slide 6, we believe our strategy and business model position us well to respond with agility to new priorities from the incoming administration and a potentially softer revenue environment. The enterprise operating model we've implemented over the past year will allow us to adjust and reallocate our investment budget to key focus areas and respond more quickly to changes in the market.

We intend to manage our cost structure and investments to maximize long-term value while delivering earnings and cash flow durability, which our business model affords. We absolutely believe that our capabilities, expertise, and value proposition position us well to partner with our government customers to drive transformation through the adoption of technology. Our strategy and the investments we're making this year are focused on capabilities and solutions that enable our customers to perform their missions better, faster, and more efficiently.

For example, SAIC is the prime mission integrator for the Air Force on a program called Cloud Based Command and Control, or CBC2, where we partner with commercial companies and cloud services providers to deliver the best possible technology to our customers. The CBC2 system distills data from over 750 sensors into a single user interface to drive a more efficient and effective C2 kill chain. This program is viewed as one of the Air Force's most successful C2 modernization programs in decades.

Similarly, SAIC has partnered with the Office of the Secretary of Defense as the lead integrator on the Joint Fires Network Program, which is transitioning from a rapid development program as INDOPAC's long-range kill chain command and control capability to a formal program of record based on its proven field success. This program is also an example where SAIC leverages the best available commercial technology and quickly integrates that technology into an effective mission solution. Most recently, this capability was integrated in record time to support Valiant Shield, an annual multi-national, multi-domain war game exercise conducted this past June.

We have many other examples such as this across the enterprise where our value proposition to the customer is clear and the capability we enable is impactful. This is particularly so in our civilian business, where, as you can see on Slide 7, the majority of our revenue comes from five agencies which support some of our country's most essential functions, including secure borders, safe airspace, support for our veterans, financial operations, and diplomacy.

As a result, under an administration prioritizing efficiency, we would expect customer adoption of these types of programs to accelerate and help offset potential funding pressures elsewhere. Prabu will provide some details on how we are scenario planning from a cost standpoint, but I wanted to be very clear that SAIC's purpose is to enable our customers to operate more efficiently and effectively through the use of technology. We believe that demand for this value proposition is significant and enduring.

In closing, I want to thank the team at SAIC for their dedication and commitment to executing our strategy and delivering for our customers. The work we have done this year positions us well to both navigate the nearer-term uncertainty and strengthen our place in the market longer-term.

I'll now turn the call over to Prabu.

Prabu Natarajan {BIO 17701667 <GO>}

Thank you, Toni, and good morning to everyone on our call. I'll focus my remarks today on an updated view of our fiscal year 2025 guidance. I'll then discuss some illustrative scenario planning to highlight the earnings and cash flow durability of this business. I'll conclude with our approach to capital deployment, including the new \$1.2 billion share repurchase authorization approved by our Board.

On guidance, we are increasing revenue to a range of \$7.425 billion to \$7.475 billion, representing organic growth of approximately 3% for the year. The improvement versus our prior guidance is largely due to improved on-contract revenue trends and a focus to deliver on our commitments.

As we've said previously, we continue to see FY '26 revenue growth in a range of 2% to 4%, and our expectation is for slower growth in the first half of the year, improving to the 5% range by the end of the year as new business pursuits, which are being submitted this year, convert into revenue next year. Our focus will be to continue driving on contract growth on our existing programs, even as we anticipate growth from new business to inflect next year.

We are reiterating our prior guidance for adjusted EBITDA and free cash flow and increasing our adjusted diluted earnings per share guidance by approximately \$0.40, largely due to a lower effective tax rate and modestly lower share count.

I would now like to discuss Slide 6 and our preparations for a renewed focus on efficiency from the incoming administration. We are preparing for potential changes to the market because it is the prudent thing to do for shareholders and better positions the company to capitalize on opportunities as they materialize.

As we illustrate on Slide 8, we have a highly variable cost structure, a discretionary and flexible budget of indirect investments and very low capital intensity, all of which contribute to our ability to remain agile and produce durable earnings and cash flow through various cycles.

The scenarios on Slide 8 are designed to only be illustrative and provide investors with a perspective on how we could adapt to different revenue environments. To be clear, at this point, we have seen no indication from our customers or the broader market that these scenarios will occur, and we believe our current level of investment is appropriate for the opportunities we have in front of us.

Additionally, if an element of the administration's efficiency efforts is increasing the usage of fixed-price contracts and a transition away from cost-plus work, we believe our track record of delivering healthy margins on this contract type indicates our ability to deliver savings for the customer and strong returns for shareholders.

In fact, more than two-thirds of the \$25 billion to \$30 billion we plan to submit next year is in Enterprise and Mission IT, work which produces higher margins than our engineering and professional service portfolios.

Finally, delivering on our free cash flow and free cash flow per share commitment is a top priority for the company. Our ability to adapt our cost structure to the revenue environment without impacting our ability to respond on the upside and deploying our balance sheet prudently but more aggressively are two key levers we have to hit our free cash flow per share target of \$11 and \$12 in FY '26 and '27 respectively, even with softer revenue trends.

This durability of cash flows gives us confidence that focusing our capital deployment efforts on our share repurchase program is the right strategy to maximize long-term shareholder value. We now expect to repurchase approximately \$500 million of shares this year and will begin executing against our new \$1.2 billion authorization in our fiscal fourth quarter, representing approximately 20% of our diluted shares outstanding.

We continue to target repurchases of \$350 million to \$400 million annually in the coming years with the option of being opportunistic based on market conditions while maintaining capacity for capability-focused M&A and holding leverage at around 3.0x.

Lastly, as you all know, aligning incentive compensation with long-term shareholder value is an area of focus at SAIC. We will continue to evaluate our compensation strategy to ensure that the targets we establish are metrics which maximize our team's focus on creating long-term value for our shareholders.

As Toni indicated, we are preparing to navigate the uncertainty in front of us while remaining focused on executing for our customers, investing in our employees, and delivering for our shareholders.

I will now turn the call over for Q&A.

Questions And Answers

Operator

(Question And Answer)

Thank you. (Operator Instructions) One moment for questions. And our first question comes from Matt Akers with Wells Fargo. Your line is open.

Q - Matthew Akers {[BIO 22271349](#) <GO>}

Hey, good morning, guys. Thanks for the question. I wanted to ask about, you called out the AAV contract resolution in the press release. So, just curious if you could size what the impact of that was this quarter.

A - Prabu Natarajan {[BIO 17701667](#) <GO>}

Hey, Matt. Good morning. Prabu here. Less than 1% to revenue for the quarter. It was about \$13 million -- \$13 million, \$14 million of revenue.

Q - Matthew Akers {[BIO 22271349](#) <GO>}

Okay. Got it. Thanks. And then on the '25 guidance, it looks like you're expecting about 3% kind of at the midpoint here. I think you've talked about something closer to kind of mid-single-digits

as long as the recompetes sort of don't go against you. I guess anything else that's big that you're sort of holding back next year that you see as a recompute risk or just kind of how you're thinking about maybe potential upside to that number next year?

A - Toni Townes Whitley

Hey Matt, it's Toni. Good morning. Hey, listen, I think we've always communicated over the last few quarters that we think '26 -- fiscal year '26 that we would get north of book-to-bill -- north of 1.0 on book-to-bill by the first half and then looking to trend towards more of a mid-single-digit by H2.

If you look at our backlog of submitted bids as well as what we have seen as historic win rates, I think that math is what drives that equation for FY '26, and we don't see -- we have talked about headwinds from recompetes and we came into this year with significant 5% to 6%. We're going into next year with something south of that, but not still we will have some headwinds, but I think we've got all of the metrics that support a mid-single-digit growth by the second half of next year.

A - Prabu Natarajan {[BIO 17701667 <GO>](#)}

Hey, Matt. One other data point here. On the recompute headwinds heading into next year, we expect that to be a little over 2%. And of course, that does not include headwinds from walking away from the compute and store part of Cloud One, which could be an incremental 2% to 3%, but not a recompute headwind, but just a transition headwind, if you will.

So, a little over 2% is still where the recompute headwind is, which is obviously, as Toni said, a lot better than where we were this time last year.

Q - Matthew Akers {[BIO 22271349 <GO>](#)}

Yes. Great. Thank you very much.

A - Prabu Natarajan {[BIO 17701667 <GO>](#)}

Of course.

Operator

Thank you. Our next question comes from David Strauss with Barclays. Your line is open.

Q - Joshua Korn {[BIO 21976043 <GO>](#)}

Hi. Good morning. This is Josh Korn on for David. So, noticed in the slide deck --

A - Toni Townes Whitley

Good morning, Josh.

Q - Joshua Korn {[BIO 21976043 <GO>](#)}

Good morning. So, I noticed in the slide deck, the recompute win rate this year is still below target. So, I just wanted to ask where the win rate is on recompetes, the progress you're making towards the target, and any steps you're taking to improve? Thanks.

A - Toni Townes Whitley

Hey, Josh, it's Toni. Thanks for joining the call. Yes, look, the recompetes win rate, we came in with recompetes a number that had an overhang into this year that affects us throughout the year in terms of that win rate, in terms of the dollar amount. When we lose larger deals, they have a lingering effect on that win rate.

As we just responded to the last question, we're going into next year, we believe, with something closer to a 2%, 2.5% impact of recompetes going in to the next year. We are still working through a new centralized business development process that we put into place this fiscal year, and as we can see, we see some early success in terms of submissions and a better, higher-quality bid. We've identified a couple of the key recompetes that have affected the number this year, and we feel better about where we are going in to next year.

A - Prabu Natarajan {[BIO 17701667 <GO>](#)}

And, Josh, one other data point there would be what we've communicated in the past is that our recompetes win rates have been below our target win rate for recompetes at 90%, less than 90%. And on the new business front, what we've also communicated is that, that win rate is higher than what we would normally see in the industry, which is normal being 30%, and we've been higher than that.

And the reason we focus on the submit volume is that we think about kind of the ebbs and flows between recompetes and new to be a blend, and we can then factor, frankly, the blended win rate at different submit levels to say, what is that yield? And, candidly, the updated submissions perspective for FY '27 is north of \$30 billion, which you can run the math on a blended win rate of 30%, 40%, or 50% between recompetes and new together. So, that's the way we think about it. Hopefully, that color helps you as well.

Q - Joshua Korn {[BIO 21976043 <GO>](#)}

Great. Thank you very much. I'll stick to one.

A - Prabu Natarajan {[BIO 17701667 <GO>](#)}

All right, thank you.

Operator

Thank you. Our next question comes from Seth Seifman with JPMorgan. Your line is open.

Q - Seth Seifman {[BIO 16417112 <GO>](#)}

Hey, thanks very much, and good morning.

A - Toni Townes Whitley

Good morning, Seth.

Q - Seth Seifman {[BIO 16417112 <GO>](#)}

Wanted to ask, starting off about, I guess you mentioned the ability to shift more to fixed-price contracts, and I think that it seems like that's helpful in this environment. SAIC, like all of the peers, still has a sizable amount of cost-plus work.

I guess maybe if you could help people think about, in this environment where there's this idea of shift to fixed-price, what's really realistic? Why is it a decent amount of the work in the sector

cost-plus, and what are the benefits for the customer in terms of having certain types of work be cost-plus as well?

A - Prabu Natarajan {[BIO 17701667](#) <GO>}

You want to start, and I'll add to that? I'll start with that one, Seth. I think big picture, the vast majority, as you noted, of our blend is cost-plus, let's call it roughly even four-fifths of our total mix. And I think part of the success we've had in the organization around transitioning from cost-plus to fixed-price is as-a-service offering is inherently more efficient for the government, as well as generating good returns for companies like SAIC.

And so, we have a track record of converting cost-plus programs into fixed-price, and I'll call two out in particular. GMASS is a program which was a takeaway from one of the primes. We are delivering a fair bit of fixed-priced offerings inside of a cost-plus construct. And then, obviously, MK 48 on our Navy business began as a cost-plus program years ago that is now in full rate, in production as a fixed-price program.

So, we have the track record of delivering that efficiency to our customers. And we also offer a number of software sprints that are fixed-priced inside of our cost-plus program. So, we have a track record of doing it. I think offering it as a fixed-priced offering allows us to get ahead of the cost curves on a multi-year basis to offer the best-of-breed solution to our customers as a systems-agnostic tech integrator. Toni?

A - Toni Townes Whitley

And Seth, I guess I would just add to that. If you look at the overall strategy, we are actually measuring our shift from cost-plus to fixed-price. It is a part of a component of our strategy as we move the portfolio from professional services and engineering more into mission and enterprise IT.

A good portion of our civilian business is in the fixed-price environment. And so, we know and we've already seen how accretive that business can be. And so, we know how to manage both Enterprise IT and Mission IT in a fixed-price environment. And that has been sort of core to the strategy prior to any change in administration.

That was what we have been planning to do over the next few years as indicated in the growth strategy. So, I think at the top-line, not only is it more accretive and is it better for the government, but we're also learning how to embed, if you start with cost-plus, how do you embed labor categories and components of the work to be more fixed-price and introduce more commercial solutions into that fixed-price category.

Q - Seth Seifman {[BIO 16417112](#) <GO>}

Great. Great. That's very helpful. And then maybe as a follow-up, with regard to the book-to-bill target of 1.2, just from a timing perspective, independently of anything the company does or doesn't do, should we think about some of the friction involved in an administration transition as posing some timing risk to reaching that 1.2 in terms of, will contract awards potentially getting pushed out as new folks get placed in agencies?

A - Toni Townes Whitley

Seth, I think that's a fair question. We're watching the market. I would say there's direction and there are both directions that happen. We see some rapidity in the acquisition process in some areas, and maybe some -- a little more tentativeness in others. So, I would say it goes in both

directions where dollars are being pushed as well as there might be a slowing down. So, those somewhat net against each other.

I think maybe the more critical metrics to look at as we land at Q3 with a significant backlog and pending awards. We've got about \$0.5 billion in award value that we have already won that's in protest. When you add sort of where we are as well as we're still submitting, we've indicated that we'll be submitting significantly over our planned submits for the year. So, we'll be submitting in Q4 to close out the year. I think all of that bodes well for us being able to hit our 1.2 in the first half of fiscal year '26.

Q - Seth Seifman {[BIO 16417112 <GO>](#)}

Great. Thanks very much.

A - Prabu Natarajan {[BIO 17701667 <GO>](#)}

Thank you, Seth.

Operator

Thank you. Our next question comes from Jason Gursky with Citi. Your line is open.

Q - Jason Gursky {[BIO 23005879 <GO>](#)}

Hey. Good morning. Just a quick question for you on the mix of the business. You've got a slide there that talks about your exposure to different agencies and communities within the federal government. It looks like the intel community explicitly is pretty small as a percentage of the overall business at about 6%, and DOD is at 71%.

I'm just kind of curious, though, within DOD whether some chunk of that business you would characterize as being more intelligence-focused within DOD? Just give us a little bit of flavor of what your intelligence business looks like holistically and whether you believe that you've got some advantages there and that's a potential further growth vector for you all.

A - Prabu Natarajan {[BIO 17701667 <GO>](#)}

Yes. Fair question, Jason. I think the short answer is yes, there are elements within our DOD business that have characteristics that you could fairly characterize as being intel. And frankly, that actually extends in nearly all of our business groups, whether it's Army intel or Air Force intel. There are elements that I think do link to the 6% that is showing up purely in the intel bucket.

I think one of the growth vectors for us has been kind of the C2 intel market and being a systems of systems integrator, getting data across the forces. JFN is an example we called out. Obviously, CBC2 is an Air Force program, but it has broader applicability. So, there's a fair amount of the work that is overlapping, and one of the ways we're thinking about our investments across the enterprise is not just through the factory, but also investments we're making in areas where the mission shares commonality. And to me, that's the way we're bringing this together at the enterprise level. Toni?

A - Toni Townes Whitley

No, I think that's absolutely right. And quite frankly, when we think about even tucked into our Air Force business right now is our combatant commands, which are really in many ways joint force, joint efforts, and there is intel behind, if you will, supporting all of those.

And so, that 6%, I think it's a fair thing to say that, that is sort of the discrete intel business within intel-named agencies versus the military intel that may be slightly commingled in the DOD number.

Q - Jason Gursky {[BIO 23005879](#) <GO>}

Right. Okay. That's what I figured. And then you've discussed this in various parts through prepared remarks and maybe some answers to some of these questions, but I wonder if we could just step back and look at this from a much higher level and just help us understand this idea that you've got more bids than what you were kind of targeting at the beginning of the year, and the pipeline suggests that the number of bids or the amount, the quantum of bids that you'll be submitting here over the next, call it 24 months, is maybe better than what you originally had expected.

I'm just curious why that doesn't necessarily put upward pressure on your revenue growth targets. So, maybe just kind of, if you're submitting more bids, why won't we see, per se, better growth out of you over the next few years?

A - Toni Townes Whitley

Well, I would say that I'd correlate two things on that. First, you know the timeline of the acquisition process, so submitting more bids in this fiscal year shows up in terms of when the bid is awarded, generally a protest environment that is subsequent to that, and when we actually convert to revenue.

So, what you see is that we're inflecting towards the second half of next fiscal year to start to see the actual revenue impact of the submission that you see this year. So, we have to get ahead of it in terms of building that backlog of pending awards as we've shown in the data. We also have to offset any challenges in terms of a recompetes loss or program transition.

And so, we're trying to net out appropriately. We believe we're coming into fiscal year '26 in a better position than we did in fiscal year '25, having addressed a number of the recompetes challenges. But at the end of the day, we always will offset against losses in other parts of the business or changes in the acquisition approach of the government.

So, it's not our -- we believe we've actually aligned a significant growth number towards the second half of '26 and into '27 with this sort of submission rate. We're pleased that we're moving ahead of pace, and what that says to us is that we're getting to a well-oiled engine and focusing on the execution and conversion of revenue and margin from that.

A - Prabu Natarajan {[BIO 17701667](#) <GO>}

And Jason, the only other data point I would add is, we are guiding to about a 5% growth rate in FY '27. So, we are expecting this business to grow at the mid-single-digit rate. And we grew 7.5% last year in our fiscal '24 organically. So, there's structurally nothing that prevents this business from growing at mid-single digits.

We've got to get some of the headwinds out of the way. And that's what is driving our inflection to about 5% growth by the end of FY '26. So, I think the submit volumes are there. I think, in theory, if the blended win rate holds, then there is no reason for us to not be able to grow. But I think the one other thing I would add is, and we've said this consistently, we are looking for vitamins, not calories.

So, walking away from a Cloud One compute and store contract, which is predominantly, I would say, calories more than vitamins, is a signal that we are really trying to grow EBITDA dollars and converting EBITDA dollars into cash. And frankly, the bet we're making on ourselves is that, that is demonstrating itself through the repurchase program, because we inherently believe that we can actually deliver the kinds of growth rate that we delivered last year at accretive margins.

Q - Jason Gursky {BIO 23005879 <GO>}

Okay. Great. Thanks, everybody.

A - Prabu Natarajan {BIO 17701667 <GO>}

Sure.

Operator

Thank you. Our next question comes from Cai von Rumohr with TD Cowen. Your line is open.

Q - Cai von Rumohr {BIO 1504358 <GO>}

Yes. Thank you so much. So, my understanding is you have two quite large recompetes coming up, Evolve, the State Department contract that was Vanguard, and then S1, which I took together, they're clearly over 2% of annual revenues. Could you give us some update on the status of those recompetes and when you expect decisions?

A - Toni Townes Whitley

Hey, Cai. It's Toni. How are you?

Q - Cai von Rumohr {BIO 1504358 <GO>}

Good. Thank you.

A - Toni Townes Whitley

We -- good. We are -- Evolve, let's just start there on the State Department side. We are continually tracking, as you know. That one continues to move right from our perspective, and we continue to deliver well on that program. So, we're doing all that we can do to meet the -- and exceed the customer expectation, but we have no signal for any change or a new milestone from an acquisition perspective.

And so, we fully expect that, that will continue to move right through fiscal year '26. Again, our strong program performance and delivery is what we're counting on as a great indicator of our ability to recapture that type of work.

Second, on the -- I think the S1 is what you were calling, it's really S3I is what the name is. We feel very -- we feel pretty good about where we stand there. The team has been working that effort. We see that as a potential end of the fiscal year award, and again, getting pretty good signals at this point, but we are watching that carefully and see that it, could it tip into the next fiscal year possibly, but we see that as a close of fiscal year effort.

Q - Cai von Rumohr {BIO 1504358 <GO>}

And is that bigger? I mean, you mentioned, award about 5% this year. That's a very large, large number, isn't it, if you win it?

A - Toni Townes Whitley

Yes.

Q - Cai von Rumohr {BIO 1504358 <GO>}

I mean, because you're bidding all the pieces. Okay. Thank you. And the last one is -- go ahead.

A - Toni Townes Whitley

No, Cai, I just want to make sure, S3I is a number of different, it's four different programs. The first program has come up for re-compete that will close. All in, it is a very large program, absolutely, but I want to make sure you understand there are four different procurements there, of which we expect the first to close by the end of this fiscal year.

A - Prabu Natarajan {BIO 17701667 <GO>}

And the first one, Cai, Prabu here, is the first one is expected to be north of \$1 billion when awarded.

Q - Cai von Rumohr {BIO 1504358 <GO>}

Got it. Okay. And then the last one is protest. Can you update us on where you are with protest that might impact your business, Cloud One, and any others that would be relevant?

A - Prabu Natarajan {BIO 17701667 <GO>}

So, hey, Cai, on protests, I think as we noted, there's about \$0.5 billion of work that we've won that is currently in protest or re-procurement, as the case may be. We are cautiously optimistic that we will have those protests adjudicated, and they were both procurements that went in our favor, either new or takeaways.

And we are expecting in the next couple of quarters to get some adjudication in run-rate revenue, big picture, one way to think about it, run-rate revenue would be an incremental 1% from the two programs as we start out. And that's really all that's open right now on the protest front. We are not currently anything that we protested that we've lost that we're waiting for adjudication on, so.

Q - Cai von Rumohr {BIO 1504358 <GO>}

Got it. Thank you very much.

A - Prabu Natarajan {BIO 17701667 <GO>}

Sure.

Operator

Thank you. Our next question comes from Ellen Page with Jefferies. Your line is open.

Q - Ellen Page {BIO 20331307 <GO>}

Hi, guys. Thanks for the question. Just --

A - Prabu Natarajan {BIO 17701667 <GO>}

Good morning, Ellen.

A - Toni Townes Whitley

Good morning.

Q - Ellen Page {[BIO 20331307 <GO>](#)}

Looking at margins, it looks like federal civil contracted about 80 bps quarter-over-quarter, and it looks more in line with defense and intel. In the quarter, how do we think about the trajectory of margins across the two segments, and what drove that contraction at civil in the quarter?

A - Toni Townes Whitley

You want to start, I'll finish.

A - Prabu Natarajan {[BIO 17701667 <GO>](#)}

I'll start, Toni. Hey, Ellen, thank you for the question. I'm very hopeful that our civilian leaders are listening to this particular question. This is a question we tackle internally a fair bit.

I think what we've signaled, and maybe we'll start there first, is that last year we benefited from a handful of, I would say, non-recurring, one-time would probably be an uncharitable way to describe it, but non-recurring, good outcomes for the company that clearly boosted margins. We've also been signaling that we expect civilian margins to trough this year.

In other words, what we expect to be at the end of the year is going to be circa 12% on the civilian segment margins, and we expect that to be a trough, primarily reflecting the absence of those non-recurring items from last year. From here on out, we expect our civil business to become more accretive. And obviously, we want margins to expand in that business. And given that, that business is predominantly T&M and fixed-price work, our hope and our expectation is that we improve margins by 100 bps to 150 bps over the next few years. So, that's what I would say.

A - Toni Townes Whitley

And I think that's reflective of the submissions from civilian in terms of our pipeline. We're seeing more accretive submissions coming out of civilian business. So, that further supports our expectation that 12% is our low point, and we're moving forward from that and up from that on the civilian business.

A - Prabu Natarajan {[BIO 17701667 <GO>](#)}

Yes, and Ellen, I would just, the reason that they converged so much in the quarter was that AAV settlement obviously benefited defense and intel.

Q - Ellen Page {[BIO 20331307 <GO>](#)}

Thanks. That's helpful. And just on your fiscal '26 expectations, what are you baking in for on-contract growth next year? And how are you thinking about the ability to push that in a potentially more difficult budget environment?

A - Toni Townes Whitley

Well, we've had an excellent year this year in terms of on-contract growth. And as Prabu indicated, we have grown 5%, 6% on on-contract growth this year, and have some similar

expectations, if you will, for next year.

And so, one of the things that has been part of the strategy has been the ability to pivot, not only in our pipeline, but in our contracts, in our current programs, to embed more technology, more commercial capability, disrupting in some areas, some of our own labor-based contracts to bring more commercial solutions, and where we've been able to introduce fixed-price into cost-plus.

That, we're starting to see some lift, as well as obviously being able to just meet the needs of our customer in a much more holistic way. And so, we fully expect to rely on on-contract growth to at least the same extent that we have this year, and possibly some lift depending on where we see unique opportunities next year.

Q - Ellen Page {[BIO 20331307 <GO>](#)}

Thank you. I'll leave it there.

A - Prabu Natarajan {[BIO 17701667 <GO>](#)}

Thanks.

A - Toni Townes Whitley

Thank you.

Operator

Thank you. Our next question comes from Tobey Sommer with Truist Securities. Your line is open.

Q - Analyst

Hi. Good morning. This is Sid on for Tobey.

A - Prabu Natarajan {[BIO 17701667 <GO>](#)}

Good morning, Tobey.

Q - Analyst

I'm just curious if you could potentially quantify how the margin profile of your backlog might be different than your reported margins today, and just how we should think about layering that in as growth from new business potentially inflects?

A - Prabu Natarajan {[BIO 17701667 <GO>](#)}

Yes, I'll start with that one first. I think big picture over the last couple of years, we've consistently expected more from our bid thresholds. And that is for every contract type, cost-plus, fixed-price, and T&M.

And we've moved internal hurdle rates [ph] up, I would say, between 50 basis points and 150 basis points, depending on the contract type. We've also put a lot of emphasis on ensuring that, I'm going to call our D students, are getting the right message in terms of moving up their own operating margin performance on every recompute cycle.

So, we're moving the common base of programs. And that is starting to reflect itself in the backlog of submissions we have, where in general, as we've shared on prior earnings calls, we

are seeing higher margins come through.

One way to think about it is if you ran the blend between defense and civil together, you can see sort of, if you will, segment operating margins sort of at a blended 9%. Our objective is to move that 10, 20, 30 bps over the course of the year, but balancing against the investments we're making in the company to ensure we can drive EBITDA dollar growth over the next several years.

So, it's a little bit of a balance. No reason we couldn't get to 10%, but I think we're trying to calibrate between investing in the business capabilities, as well as generating more returns from the business. Toni?

A - Toni Townes Whitley

And I think as Prabu talks about the hurdle rates, that also goes to deal selection, bid selection. So, we're making conscious decisions if we can't get to that hurdle rate to no bid, and as well to make sure that our execution expectations on margin are monitored and met and incentivized where necessary against what was bid.

And so, I think it's all of that discipline that Prabu speaks to that helps us see not only a slight increase in the accretive nature of our submissions, but the expected revenue that would follow in the P&L going forward.

A - Prabu Natarajan {BIO 17701667 <GO>}

And we're not hesitating taking exception to cash terms and conditions that are not appropriate. So, I think it's just, it's an end-to-end view of, can we live with this contract for the next five years, especially in an uncertain environment, we want to make sure we can drive the right kind of value creation for our shareholders, and that's where the focus is right now.

Q - Analyst

All right. Thank you.

A - Prabu Natarajan {BIO 17701667 <GO>}

Sure.

Operator

Thank you. There are no further questions. This does conclude the question-and-answer session. You may now disconnect. Everyone, have a great day.

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