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Science Applications International Corp.

(SAIC)

Q1 2022 Earnings Call

CORPORATE PARTICIPANTS

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

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

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

OTHER PARTICIPANTS

Sheila Kahyaoglu
Analyst, Jefferies LLC

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

Matthew Akers
Analyst, Wells Fargo Securities LLC

Gavin Parsons
Analyst, Goldman Sachs & Co. LLC

Tobey Sommer
Analyst, Truist Securities, Inc.

Seth M. Seifman
Analyst, JPMorgan Securities LLC

David Strauss
Analyst, Barclays Capital, Inc.

Cai von Rumohr
Analyst, Cowen and Company

MANAGEMENT DISCUSSION SECTION

Operator: Welcome to SAIC's First Quarter Fiscal Year 2022 Earnings Call. 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 and thank you for joining SAIC's first quarter fiscal year 2022 earnings call. My name is Shane Canestra, Vice President of Investor Relations. And joining me today to discuss an exciting announcement and our business and financial results are Nazzic Keene, SAIC's Chief Executive Officer; and Prabu Natarajan, our Chief Financial Officer. Today, we will discuss our results for the first quarter of fiscal year 2022 that ended April 30, 2021.

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. In addition we issued a separate press release today regarding the company's intention to acquire Halfaker and Associates. 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 defer 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. We appreciate you joining us today to discuss SAIC's strong start to fiscal year 2022 and our positive outlook for the rest of the year. We have a lot of good news to share today including the exciting announcement that we've entered into a definitive agreement to acquire Halfaker and Associates, expanding our reach in the public sector health market. We will also discuss our solid first quarter financial performance and strong business development results as we continue executing on our strategy for long-term shareholder value creation, but I would like to start with the acquisition announcement.

We've often talked about our strategic interest in profitably growing our business in the public sector health market, further expanding opportunities for long-term value creation. The acquisition of Halfaker and Associates does exactly that. As outlined on page 5 of the supplemental presentation, Halfaker and Associates, founded in 2006, is a mission-focused, pure-play health IT company. This acquisition fills a frequently discussed gap in our portfolio, immediately accelerating our strategy in the very attractive growing public sector health market. This combination will immediately increase SAIC's customer and market access, and directly aligns with our strategic focus and capability expansion in IT modernization, digital and cloud transformation, and data accountability and analytics.

SAIC will now have one of the largest and most compelling suite of digital transformation offerings in the government services space. And while Prabu will cover the financial details, I would like to highlight that their financial profile is accretive to SAIC with strong revenue growth and low-double-digit EBITDA margin. And with over four years of 2020 revenue in backlog, they offer strong revenue visibility through SAIC's fiscal year 2024.

Please turn to slide 6. Also headquartered here in Northern Virginia, Halfaker and Associates is home to over 550 highly skilled, credentialed and mission-focused professionals. As I mentioned, they serve several critically important federal health customers with a large presence in the Department of Veterans Affairs where they are a top 5 IT provider on the $22 billion T4NG vehicle.

They also serve valued customers in the Centers for Medicare and Medicaid services, Department of Health and Human Services, and health customers in the Department of Defense. As you can see on this chart, they provide some of the most in-demand services across the federal government today. We remain confident that priorities such as digital services, data analytics, cyber security and cloud solutions will continue to draw investment from our customers.

Prabu, could you please discuss the financial details of the Halfaker and Associates acquisition?

Prabu Natarajan

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

Thank you, Nazzic, and good afternoon, everyone. As you can see on slide 6, the Halfaker and Associates transaction has an attractive financial profile that continues SAIC's upward progress in multiple financial areas. They generated approximately $166 million of calendar 2020 revenues and are expected to grow in the mid- to high-single-digit growth rates in the current year. Margins run in the low-double-digit EBITDA range due to the entire portfolio being fixed price and time and materials contracts. Halfaker and Associates has good cash generation that will be additive to SAIC's attractive profile. And as Nazzic mentioned, they have high visibility into their future revenue stream with over four times their 2020 revenues in backlog and relatively low recompete risk for the next few years providing confidence in continued growth.

Please turn to slide 7. Let me provide a financial overview of the transaction. With an all-cash purchase price of $250 million, including about $30 million to $35 million in tax assets, SAIC is acquiring this business at under 10 times calendar 2021 adjusted EBITDA after adjusting for the tax assets. This acquisition is accretive to our fiscal 2022 revenue growth rate, adjusted earnings per share, and free cash flow. We have not included any cost synergy assumptions in the acquisition model.

We expect to fund the transaction with cash on hand and incremental debt, adding about a fifth of a turn of leverage to our existing ratio. With only a modest increase to leverage, we will continue to have capital deployment flexibility throughout this year and we do not expect this acquisition to have any material impact to our capital deployment flexibility. We have made tremendous progress on de-levering following our acquisition of Unisys Federal, and we'll continue to make progress going forward. We expect the transaction to close in the second quarter of this year, subject to customary closing conditions including regulatory approvals.

For your modeling purposes, we expect the transaction to generate between $90 million and $100 million of incremental revenue in fiscal year 2022, which is not included in our guidance today. We will update our guidance to reflect this acquisition after it closes and in our September call.

Nazzic, back to you.

Nazzic S. Keene

Chief Executive Officer & Director, Science Applications International Corp.

Thank you, Prabu. Let me briefly discuss our results for the quarter. As reported in our press release today, SAIC's first quarter results reflect strong performance across the board. The team delivered strong revenue and profitability, excellent cash flow, and outstanding business development results. Organic growth for the first quarter was 2.6%, and adjusted EBITDA margin was 9.8%, an all-time high.

SAIC continues to deliver strong cash flow and we are allocating capital for value creation. We have a balanced customer portfolio that allows us to remain agile when government priorities change. With a third of our annual revenue coming from federal civilian customers, we are well positioned in several agencies targeted for increased investment through this recent budget request. SAIC is responding to the increased investments proposed by the administration and the enduring long-term technology needs of our nation. Our balanced portfolio, further strengthened by this acquisition, bolstered by our refresh strategy, will continue to produce long-term sustainable value creation.

Prabu will now discuss the details of our first quarter results and financial outlook for the rest of the year.

Prabu Natarajan

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

Thank you, Nazzic, and good afternoon, everyone. SAIC delivered a quarter of strong performance across all business development and financial measures. I see the foundation being laid for future success through strong financial alignment and execution in line with our strategy. SAIC's results for the first quarter of fiscal year 2022 reflect robust contract awards, increased organic revenue growth, strong profitability and free cash flow.

Let me start with our strong business development results. Net bookings for the first quarter were approximately $4.2 billion translating to a quarterly book-to-bill of 2.2 times and a trailing 12-month book-to-bill of 2.0 times. The most significant contributions to our quarterly bookings are disclosed in our press release today.

At the end of the first quarter, SAIC's total contract backlog stood at nearly $24 billion, up 11% from the fourth quarter and 43% from a year ago. At the end of the first quarter, the value of submitted proposals was $18.1 billion, down from last quarter, reflecting our business development success in the first quarter. Approximately 60% of the value of submitted proposals is for new business opportunities and we continue to invest for future growth in a year of relatively low recompetes.

Let me now turn to financial results for the quarter. Our first quarter revenues of approximately $1.9 billion reflect growth of 7% as compared to the first quarter of last fiscal year due to six weeks of incremental Unisys Federal revenues, new business contracts, primarily supporting IT modernization for a US Air Force customer, and increased revenues on existing contracts. Excluding the impact of the Unisys Federal acquisition, first quarter revenue grew organically by 2.6%.

First quarter adjusted EBITDA was $184 million, a $47 million increase from the prior year. Adjusted EBITDA margin was 9.8% after adjusting for $10 million of acquisition and integration costs. First quarter margin performance was very strong across the business and the quarter favorably benefited from the timing of indirect costs and the non-recurring but favorable benefit from the settlement of prior year indirect rates. For the quarter, COVID-19 negatively impacted adjusted EBITDA by about $4 million.

Net income for the first quarter was $81 million and diluted earnings per share was $1.38 for the quarter, inclusive of the first quarter acquisition and integration costs of $10 million. Excluding these costs as well as amortization of intangibles and net of a tax rate of approximately 23% in the quarter, our adjusted diluted earnings per share was $1.94.

First quarter free cash flow was $164 million, a quarter of strong cash generation, and days sales outstanding at the end of the quarter were 57 days, down 2 days from the fourth quarter. During the first quarter, we deployed $71 million of capital through share repurchases, dividends, and capital expenditures.

In addition, we continue to de-lever, making mandatory debt repayments, and ended the quarter with a net leverage ratio of just under 3.5 times. We prioritized share repurchases over voluntary debt repayment in the quarter. As announced in our press release today, our board of directors has approved a quarterly cash dividend of $0.37 a share, payable on July 30 to shareholders of record on July 16.

Now turning to our forward outlook, as noted in our press release today and slide 10 of the presentation slides. Based on first quarter performance and our outlook for the rest of the year, we have updated our guidance to the following: revenues between $7.15 billion and $7.3 billion, raising the lower end of our previous range, reflecting lower estimated full-year COVID impacts of approximately $150 million, down from $150 million to $200 million. Our updated revenue guidance reflects 1% to 3% organic revenue growth in fiscal 2022 including this impact.

Additionally, for your modeling purposes, I'd like to remind you of the seasonality of our revenue profile where we typically see lower revenues in the second quarter due to employee holidays and summer vacations.

Adjusted EBITDA margins between 8.7% and 8.8%, again raising the lower end of our previous range, reflecting our strong Q1 performance. On EBITDA dollars, we now expect COVID to have approximately $10 million of impact in fiscal 2022, down from $10 million to $15 million, consistent with the change in our revenue estimates.

Adjusted diluted earnings per share between $6.15 and $6.40, raising both the top and bottom end $0.15 above our previous range, reflecting our strong start to the year. Free cash flow unchanged at between $430 million and $470 million. Summing up, we are pleased with our strong performance of Q1 and look forward to solid execution over the remainder of the year.

Nazzic, back to you for concluding remarks.

Nazzic S. Keene

Chief Executive Officer & Director, Science Applications International Corp.

Thank you, Prabu. I want to take a moment to thank all of our 26,000 employees for their dedication to our customers through an incredibly unique and challenging year. We at SAIC are optimistic about our future. Hopefully, you hear that from both Prabu and myself. We have worked to capture that energy and optimism in our new branding campaign titled Bring on Tomorrow. We are excited about the future and what we can and will do to advance our customers' missions, support our talented employees, and drive value for our shareholders. Our optimism lies not only in what the future will bring to SAIC, but also with what SAIC will bring to the future. We are excited to Bring on Tomorrow.

Operator, we're now ready to take questions.

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] Your first question is from the line of Sheila Kahyaoglu with Jefferies.

Sheila Kahyaoglu
Analyst, Jefferies LLC

Q

Good evening, everyone. Thanks for the time, Nazzic and Prabu, and Shane, of course. So I guess to start off on your core business, your profitability was really good in the quarter, 9.8% EBITDA margins. Your guidance for the full year is 8.7%, high-8s basically. Why does everything get worse from here outside of Q2 seasonality?

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

A

Thanks for the question, Sheila. So, as I mentioned in my prepared remarks, there were some non-recurring but favorable items that benefited Q1. We specifically referred to the settlement of prior year indirect rates as well as an under-run on our overall indirect spend at the first quarter. And as you step back and kind of adjust sort of our operating performance in the quarter for those items, we get to operating margin rate that's in the high 8% rate. I'd say that's sort of roughly in line with where we ended Q4 of FY 2021.

So I'd say in line with that, so what that would imply for the rest of the year is EBITDA margin rates that's roughly in the mid 8%. I'd say there is first quarter here behind us. We have three quarters left. And our guidance today, I'd say, is a balanced view of the risks and the opportunities ahead of us for the rest of the year. And as I've often said, the team's incentivized to do better over the course of the year. And I think we're pleased with the strong performance to start the year. And hopefully, we're poised to have a really good year.

Sheila Kahyaoglu
Analyst, Jefferies LLC

Q

Okay. Yeah, we saw some of those incentives come out in the proxy. And then just in terms of the acquisition, is the $166 million in revenues enough to make a dent in the health business for Bob?

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

A

Yes. I missed the last part. And that's to make a...

Sheila Kahyaoglu
Analyst, Jefferies LLC

Q

No. In terms of the health acquisition, $166 million in sales, I think you mentioned, Nazzic, in your remarks. Is that enough to actually build a health business with that sort of scale?

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

A

Yeah. My take is and our take is that this is a perfect acquisition at the right time at the right price. It is extremely strong cultural fit to SAIC, very mission-focused, very purpose-driven organization. And when we marry it with our modest health business, it will give us a very strong position in a couple of key customers as well as some very compelling contract vehicles. So we're very pleased with this acquisition and very excited about the opportunity to bring on this company into SAIC.

Sheila Kahyaoglu
Analyst, Jefferies LLC

Q

Okay. Thank you very much.

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

A

Thank you.

Operator: Your next question is from the line of Joseph DeNardi with Stifel.

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

A

Hi, Joseph.

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

Q

Thanks. Good evening.

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

A

Hey, Joe.

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

Q

Maybe just one on the acquisition. It looks like that T4NG contract is a substantial portion of that business. So can you talk about what you all expect to be able to do with that contract that Halfaker couldn't do on their own? Should we expect greater market share from you all? And do you think kind of the current dynamics affecting the health market right now result in that contract being larger than expected over time? Is that part of the thesis as well?

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

A

Well, that – so a couple of comments that you made are exactly right on. That particular contract, the T4NG, is a very important contract in the health space serving the veterans organization. So, for us, we did not have that vehicle obviously. So it was a very important part of the acquisition thesis and allows us great access for the next several years to be able to sell – cross-sell SAIC services into that vehicle.

So that was a very important part of this acquisition. And we believe that the two companies coming together really position us well. They've got – Halfaker has great market access, great relationships and as well as compelling solutions and services. But then when you layer in the breadth of SAIC's capabilities in the sales domain, in the solution domain, we believe that it creates a great opportunity for us to expand our presence.

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

Q

Okay. That's helpful. And then, Prabu, maybe just on the labor market, can you talk about what you're seeing there in terms of productivity and what your expectations are for that over the next few quarters as, I don't know, maybe employees are able to take time off and do that sort of thing to the extent that they weren't able to in the past year or two? Thank you.

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

A

Yes. So, as you've noted, we're all looking at what the future looks like as we come out of what we hope to be the backside of this particular pandemic cycle and we're all very optimistic. We're seeing a couple of things. We did have great productivity, and a lot of folks put in a lot of extra hours, and I'm very appreciative to the SAIC employees that did that over the course of this last year. But we are seeing things come back to a more normalized environment, and we're very pleased for that. Any expectations we would have in leave and time-off are put into our guidance and are already factored in, but we're not seeing a significant shift in any behavior.

For our normal business, Q2 tends to be an opportunity for employees to take more time off as it falls across holidays and vacation cycles. And again, that's factored into our guidance as well. So we're very pleased with the performance of the SAIC employees and look forward to a more normative environment over the course of the next many months.

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

Q

Thank you.

Operator: Your next question is from the line of Matthew Akers with Wells Fargo.

Matthew Akers
Analyst, Wells Fargo Securities LLC

Q

Yeah. Hi, guys. Good afternoon.

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

A

Good afternoon.

Matthew Akers
Analyst, Wells Fargo Securities LLC

Q

Yeah. Congrats on the deal. I wanted to ask, I guess, on kind of the bid process for this deal. Were there any other kind of competitive bidders here? It looks like you got a pretty reasonable price on it. And then I guess also on Halfaker, I guess, are there any – other than T4NG that you mentioned, any big contracts that are either potential recompetes coming up or kind of big drivers of growth here that we should watch going forward?

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

A

Terrific. This is Nazzic. So it was a competitive process, as most sales – most acquisitions are in our space. And we're very, very pleased to have been selected by Halfaker to go forward. Again, I'll touch on a couple of things. In addition to the price which is obviously always important, we also look very heavily at cultural fit and very pleased with the culture of the organization. I had the privilege of meeting with the CEO. We've met with a senior team. And again, the cultural fit is so important in the services business, but it's a purpose-driven culture, a mission-oriented culture which is very consistent with SAIC. So, very, very pleased with that and very happy that they've selected us to continue their journey.

As it relates to the contracts, obviously T4NG is a critical contract. And as I alluded in my – or I mentioned in my remarks, we have about four years of revenue in backlog. So I feel very good about our position. And there really isn't, in the near term, any significant recompete that would cause any kind of material change in the revenue profile of the business. Did that answer all your questions?

Matthew Akers
Analyst, Wells Fargo Securities LLC

Q

Yeah. That's great. Thank you. And I guess if I could do one more, I guess, on the COVID impact to revenue. So I think you guys had $33 million impact in the quarter, $150 million for the year. So, I guess, implies there's still a lot left to go. I think, last quarter, you guys had talked about that mostly wrapping up, I think, in the first half of your fiscal year. Is that still the right way to think about it or has that shifted out a little bit?

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

A

Yeah. I mean I think that's still the right way to think about this, Matt. I'd say taking the first quarter number and sort of pro rating it across the year would not get you to $150 million obviously. But I think within the updated expectation of $150 million, I think we still notionally see some element of risk there in the supply chain portfolio. And I think while the quarterly impact was lower than prior quarters, I'd say there's still some uncertainty around the sustainability of the buying patterns at these levels.

And previously, we talked about thinking about weekly revenue for this business in that $10 million to $15 million range a week. I'd say when we provided guidance a few months back, we were probably near the bottom of that range, a little over $10 million. And where we are right now is about the middle of the range. So I'd say still a far way to go to get to the top of the range here. But that sort of is what gives us an element of caution as we think about the full year. And as virus appears to have one step ahead of us at every turn it seems like, so we're cautious about the way we're thinking about it and that's why we've lowered our expectation for full year or we're still holding about $150 million for the year.

Matthew Akers
Analyst, Wells Fargo Securities LLC

Q

Got it. Okay. Thank you.

Operator: Your next question is from the line of Gavin Parsons with Goldman Sachs.

Gavin Parsons
Analyst, Goldman Sachs & Co. LLC

Q

Hey. Good afternoon.

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

Hey, Gavin.

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

Hi.

Gavin Parsons
Analyst, Goldman Sachs & Co. LLC
Q

Hey, guys. If organic growth was 2.6% in quarter, the midpoint of your updated guidance implies just 1% for the rest of the year. This was your toughest comp. Currently book-to-bill is 2.0 times. The COVID headwind diminishes going forward. So I guess what drives the slowdown in organic over the rest of the year and were there any one-time items or pull-forward that you had this quarter?

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

Yeah. Gavin, thanks for the question. Prabu here. I'll take this one first. So I'd say if you think about the Q1, there's clearly seasonality in the revenue pattern here. Q1 tends to be one of our stronger quarters along with Q3, I'd say. And Q2 and Q4 tend to be weaker quarters primarily due to the holidays within those quarters. So I would say a little careful on annualizing Q1 across four quarters to get to a number that would imply a total year number of higher than $7.3 billion. But I'd say as we're thinking through it, the immediate impact we saw for the year was on the COVID side, so we've reflected that in the updated guidance. I'd say we continue to see some progress as we go through the rest of the year.

As we've previously flagged, we do see some ramp in growth rates in the second half of the year, primarily associated with both our AMCOM, now we call them S3I contracts, as well as the Army rich contract. We do see that ramp occurring still in the second half of the year. But I'd say there is a fair amount of variability as we sit here right now in Q1 and we'd love to be having this conversation over the course of the next several quarters. But I'd say, still early in the year, we've got some three quarters to go, so.

Gavin Parsons
Analyst, Goldman Sachs & Co. LLC
Q

Okay. So it sounded like there's still some variability that could drive you to the higher low end of the range outside of the COVID.

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

Correct.

Gavin Parsons
Analyst, Goldman Sachs & Co. LLC
Q

Okay. Great. Maybe similar question on margins maybe to what Sheila asked earlier. But given you didn't adjust the one-time benefit out of the first quarter, I assume that's in guidance for the year. But you only raised the margin guidance by the change in the COVID impact. So, does that imply you see a worse margin for the rest of the year than you were previously expecting?

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

A

Well, so I'd say, what this implies for the rest of the year is margin rates in the mid 8%. I'd say on the indirect rate benefit that we booked in Q1, some of that was in our forecast for the year. It ended up occurring a quarter or two earlier than we expected. We don't actually expect the indirect rates to under-run on a full-year basis, so we actually do expect that to trend back up. So as we think about pressures on margin rate, and if you align that with the fact that the supply chain business, as it continues to recover, brings in margin at a lower rate than the rest of the portfolio, so as you put all those factors together, you end up with a little more pressure on margin rate in the back half of the year, and that's why we're holding the increase to margin rate guidance to about 10 basis points right now at the low end.

Gavin Parsons
Analyst, Goldman Sachs & Co. LLC

Q

Got it. And one more quick one, if I could. You mentioned that 60% of the submitted pipeline is new business. Do you have a sense for how much of what you've won over the last year or so has been new versus recompete since the call-outs in the press release were pretty heavily recompete tilted?

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

A

So, yeah, I'd say typically – I've referred to high levels of recompete win rates on the last call, and I'd probably sort of leave it there for now. Our win rates are competitive and they're good, but we typically don't disclose them.

Gavin Parsons
Analyst, Goldman Sachs & Co. LLC

Q

Okay. Thank you.

Operator: Your next question is from the line of Tobey Sommer with Truist Securities.

Tobey Sommer
Analyst, Truist Securities, Inc.

Q

Thank you. I have a question for you about the book-to-bill. A long time ago, a decade or more ago, it was a very good modeling tool to forecast future revenue growth, and that relationship has sort of been decoupled, not just at SAIC but seemingly the group. How do you use that in your planning and forecasting so that we can utilize what in the quarter was a very robust number seemingly and use it to forecast more accurately? Thanks.

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

A

Yeah. So you're absolutely right. Book-to-bill is an indicator and it's a reasonable leading indicator to get us assessment of the bookings we're bringing in and certainly as you dissected it can be informative as you think about the periods of performance and things like that. But it is not a dollar-for-dollar indicator around future growth. And so we do pay attention to it obviously. We report on it. We look to it. But there's – things like the period of performance on very sizeable contracts can absolutely move your book-to-bill in a very material way and we've seen some of that with some of our bookings, especially in the S3I, where they've been longer. But it doesn't necessarily have a direct correlation on a growth rate.

So I totally agree with your assessment. It is something we pay attention to as an indicator. But until you layer in all your contracts and your backlog and the roll-off, it really is just part of that analysis that gets done. We're very pleased with our book-to-bills, running very strong the last year. And we've got a very strong pipeline as you've heard and have good confidence in our ability to sustain strong book-to-bill. But again it is an indicator, certainly not the indicator.

Tobey Sommer
Analyst, Truist Securities, Inc.

Q

Thanks. And could I get a sense for what's the margin profile looks like in sort of the bid pipeline and in recent wins including the AMCOM recompete wins? I just want to try to be able to use that color to inform the margin outlook going forward. Thank you.

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

A

Yeah. Prabu here, Tobey. So I'd say the margin rate implied in the pipeline and importantly in the way we think about the business here really is in line with where the business is right now. Having said that, we are always striving to create differentiation in what we're bidding such that we continue to move up the margin rate curve as we bid new work. And especially with new work that has a development period associated with it, I think we tend to see lower rates early on in the program in the period of performance and we start to ramp over the period of performance. So we think about it over the life of a contract, but I'd say directly to your question, I'd say we would expect sort of our pipeline and our BD efforts to be continuously driving us upstream on margin rate. So we're taking on more accretive work as we go on.

Tobey Sommer
Analyst, Truist Securities, Inc.

Q

Thank you.

Operator: [Operator Instructions] Your next question is from the line of Seth Seifman with JPMorgan.

Seth M. Seifman
Analyst, JPMorgan Securities LLC

Q

Okay. Thanks very much. Good afternoon, everyone.

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

A

Good afternoon.

Seth M. Seifman
Analyst, JPMorgan Securities LLC

Q

I was wondering if you could talk about what's the level of exposure that you have to Afghanistan that's baked into the guidance for the year.

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

A

Yeah. We have very minimal exposure in Afghanistan. So, nothing material.

Seth M. Seifman
Analyst, JPMorgan Securities LLC

Q

Okay. Okay. Great. And then, when you look at the pipeline for the remainder of the year, I guess, we just see a reasonable opportunity to – putting aside the acquisition, a reasonable opportunity to exit the year with a larger backlog than you have right now.

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

A

Yes. Yes, I would agree with that assessment. We have a very strong pipeline. We've secured decent strong win rates and we've got a good combination of recompetes as well as new business. So I would agree with your assessment.

Seth M. Seifman
Analyst, JPMorgan Securities LLC

Q

Great. Thanks very much.

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

A

Thank you, Seth.

Operator: Your next question is from the line of David Strauss with Barclays.

David Strauss
Analyst, Barclays Capital, Inc.

Q

Thanks. Good afternoon.

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

A

Hi, David.

David Strauss
Analyst, Barclays Capital, Inc.

Q

So I know it's still early days here and we've got to go through the markup process, but can you comment a little bit on how you thought the budget looks for you all, I guess, both from a DOD perspective and a civil agency perspective?

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

A

Yes. So, as you noted, it is early days, for certain. We obviously pay attention to the requests that are being put forward in the conversation. I would say, at this juncture, we don't see any material impact on our business from the budget. We certainly see some positive trends. As an example, the continued focus on IT modernization and some of the work that's being accelerated across the federal government in that arena, we believe, is a positive sign for us, and certainly the conversation around O&M, we believe, is a positive indicator for SAIC. But at this juncture, it is still, as you said, very early and we're not seeing anything that has a material impact.

David Strauss
Analyst, Barclays Capital, Inc.

Q

Okay. And, Prabu, I guess, a question, given the deal, could you talk or could you give us kind of how we should expect deleveraging to go from here? I think your prior target was 3 times at the end of the year. And what does this do for your outlook from a share repurchase standpoint?

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

A

Yeah. So, thanks for the question, David. I'd say, at this point, we don't see a material impact to our ability to continue to be in the market to buy shares. We had committed to getting our leverage ratio to about 3 times. I'd say in a low interest rate environment, we're comfortable running that leverage ratio a little bit higher as needed. As we mentioned, this particular acquisition increases our leverage by a fifth of a turn and it's incredibly cheap debt, as I mentioned.

So I'd say pretty comfortable running it where it is right now. I think in terms of just a plan to de-lever, I'd say we'd notionally get to that roughly 3x sometime in FY 2023 and no better way to do it than to grow earnings quickly. So we're certainly committed to getting there, but I'd say probably sometime in the second half of FY 2023.

David Strauss
Analyst, Barclays Capital, Inc.

Q

Okay. And last one I had, the 10% of revenues that I think you talked about the last quarter that were up for recompete this year, where does that percentage stand now?

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

A

It's a little bit lower now. I'd say there is one recompete that's out there that's still pretty material. It's NASA NICS. We call it NASA AEGIS now. And that is expected to be, I'd say – we'll have more clarity in the summer timeframe on that one. And that's the FY 2022 look for this year.

David Strauss
Analyst, Barclays Capital, Inc.

Q

All right. Thanks very much.

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

A

Okay, thank you.

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

A

Thank you.

Operator: We have a follow-up question from Gavin Parsons with Goldman Sachs.

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

A

Go ahead.

Gavin Parsons
Analyst, Goldman Sachs & Co. LLC

Q

Hey. Thanks. I just wanted to ask an update on the three contracts you used to talk about all the time – EDIS, CCE, and FSG 80. Those at a full run rate, have those wrapped up or are those still contributing growth drivers?

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

A

I think at this juncture, they're all ramping up and on track to do exactly that. I don't think they're at full capacity yet.

Gavin Parsons
Analyst, Goldman Sachs & Co. LLC

Q

Okay, great. And then probably you mentioned the guidance in the second half depends on the ramp-up or the run rate of SDI and risks. There's a – as of the contracts I mentioned before, there had been a dynamic of slippage to the right. Is there any cushion in there for that or do you have a good amount of confidence in the pace of the ramp-up of those?

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

A

Yeah. It's a good question, Gavin. I mean the way we really do think about the plan process is to be thoughtful about the things that will require a ramp. Especially if there's a lot of hiring in place, we want to make sure that we have a plan that we can execute starting from day one. And so I'd say we've fairly encapsulated the range of possibilities around the ramp time for these programs and are therefore comfortable with the way we're scheduled this out for the rest of the year.

Gavin Parsons
Analyst, Goldman Sachs & Co. LLC

Q

Okay. Thanks again.

Operator: Your next question is from the line of Cai von – and I'm not sure how to pronounce your last name – with Cowen.

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

A

Hi Cai.

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

A

Hi Cai.

Cai von Rumohr
Analyst, Cowen and Company

Q

Okay. Good try. Thanks. So apologize joining a little bit late, but – so could you – if you gave it, could you give again the bids awaiting decision?

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

The $18.2 billion, Cai.

Cai von Rumohr Q
Analyst, Cowen and Company

$18.2 billion. Thank you very much.

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

It was down a little bit from...

Cai von Rumohr Q
Analyst, Cowen and Company

And then...

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

...from year-end, but that's because of the things we had in Q1.

Cai von Rumohr Q
Analyst, Cowen and Company

Right. And...

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

Yeah.

Cai von Rumohr Q
Analyst, Cowen and Company

Exactly. Exactly. And then a number of folks the last quarter basically sort of complained about transition to the administration and kind of delayed bookings. Obviously you had good bookings. What are you seeing for the next two quarters? Are we going to have like a super flush or are we going to see the normal seasonal pickup? What should we look for?

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

Yeah. I mean what we're seeing today is really just a normal environment. We're not seeing anything that's overly slow or anything that's overly aggressive. So we're seeing a normal cadence of RFPs, of bid processes, and of awards in our space and our customers.

Cai von Rumohr
Analyst, Cowen and Company

Q

If I look at history, normal would say comfortably above 1 time in Q2 and Q3. Yes?

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

A

Well, we're not – I'm not going to give guidance on a book-to-bill. We're very pleased with the bookings and the book-to-bill that we've been able to appreciate these last four quarters and actually before that. So we're very pleased with where we sit today. I'm very pleased with the performance of the organization on business development and pursuing bids.

As we all know, book-to-bill is lumpy. And so it's very hard to predict anything at the quarter level because that really becomes the outcome of a customer's decision and schedule. But I will tell you that as we look at the pipeline, as we look at the submissions, as we look at our past performance, that I'm comfortable with our ability to maintain a strong book-to-bill going forward.

Cai von Rumohr
Analyst, Cowen and Company

Q

Great. And then could you comment on protest? Specifically, I think you had four contracts you lost toward the end of the year, and two of those were in protest. Did you win those protests and do you have any other protests either on the offensive or the defensive side?

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

A

So, Cai, I'd say nothing unusual. There was one where the protest was sustained. It's back into a cycle of competition again. I'd say we're just watching this with everybody else, but I'd say that's probably the only update we have since year-end, one of them where the protest was sustained.

Cai von Rumohr
Analyst, Cowen and Company

Q

Thank you very much.

Operator: And I would like to turn it back over to the company for any closing remarks.

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

Thank you very much for your participation in SAIC's first quarter fiscal year 2022 earnings call. This concludes the call, and we thank you for your continued interest in SAIC.