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Third Quarter Results

Letter from CFO Xavier Heiss

Dear Shareholder,

Thank you for your investment and continued interest in Xerox. In this letter I will provide context for Q3 2024 results, an update on Reinvention and expectations for Q4 2024 and fiscal year 2025.

The benefits of Reinvention are driving improved financial results, albeit at a slower pace than expected. In Q3, revenue fell below our expectations, due primarily to lower-than-expected equipment sales. Despite the shortfall in equipment sales, we are seeing the benefits of Reinvention elsewhere. Total company revenue declines moderated for a second consecutive period, adjusted operating income and margin improved year over year, and we converted more than 100 percent of adjusted operating income to free cash flow.

Equipment sales in Q3 fell below expectations due mainly to delays in the global launch of two new products and lower-than-expected improvements in sales force productivity. Tactical challenges associated with the timing of Hurricane Helene and an increase in competitive activity in certain markets also contributed to the shortfall. Recapping Q3 results further:

- Total revenue declined by 7.5% in actual currency and 7.3% in constant currency, an improvement from prior quarter's approximately 10% decline in constant currency. Fluctuations in current and prior year backlog levels, and the intentional reduction in non-strategic revenue contributed more than 400 basis points of the decline this quarter. When these impacts are removed, total revenue declined low single digits in actual currency, consistent with Q2.
  - Equipment revenue declined approximately 12%, including a 400 basis point effect from backlog fluctuations and geographic simplification actions. This compares favorably to a 15% decline in Q2. Comparisons to Q2 are less favorable when the effects of backlog fluctuations and Reinvention actions are removed, for the reasons noted above.
  - Post sale revenue declined 6.1% in actual currency and 5.7% in constant currency. Excluding the reduction in non-strategic, lower margin paper and IT endpoint device placements and other Reinvention actions, Post sale revenue declined low-single digits, a 200 basis point sequential improvement. The sequential improvement reflects double digit growth in digital and managed IT Services.
- Adjusted operating income margin of 5.2% improved 110 basis points year-over-year due principally to Reinvention-related cost reductions and lower incentive compensation expense, partially offset by the effects of lower revenue and gross profit. Total operating expenses declined $53 million year-over-year, or more than 10 percent, reflecting headcount reduction actions taken in Q1, non-labor reductions in overhead and the flowthrough of cost reductions implemented in the prior year.

Shortfalls in equipment sales this quarter mask the breadth of Reinvention progress made to-date. Notable Reinvention-related improvements this quarter include the following:

- **Customer perception**. Net Promoter Score, a key barometer of client perception, improved 11 points this year in the Americas through greater end-market focus and attentiveness to clients' needs. The increase reflects improved client satisfaction and brand consideration, which we expect will drive an increase in purchase intent over time.

- **Lowered, simplified cost base.** The benefits of a structurally simplified cost base are generating intended results. Adjusted operating income improved this quarter despite reductions in revenue, which include intentional reductions associated with geographic and offering simplification.
- **Revenue mix.** The planned acquisition of ITsavvy improves revenue mix from businesses with higher underlying rates of growth and enables better client outcomes through an improved IT Services offering.
- **Execution of savings unlocks.** During the quarter we made progress across each of the major Reinvention savings unlocks: Geographic, Offering and Operating Model simplification. Of note, we transitioned additional countries to indirect distribution models, consolidated product configurations to improve operating efficiency and restructured a key business process outsourcing contract to ensure all parties are mutually incentivized to structurally lower operating costs over time.

Looking to the remainder of the year, product launch delays are expected to affect equipment sales again in Q4, but to a lesser extent than in Q3. We have analyzed the factors that contributed to the product launch delays and are confident those factors will be resolved as we recalibrate global launch plans. While sales productivity was lower than expected in Q3, we expect an increase in Q4 from ongoing sales efficiency and effectiveness programs.

We are confident the execution challenges that affected equipment sales this year are being addressed and will contribute to an improved equipment revenue trajectory in 2025. However, current year challenges required a reduction to 2024 guidance. We reduced our outlook for revenue from a decline of 5% to 6% in constant currency to a decline of around 10% in constant currency. Adjusted operating margin was reduced from at least 6.5% to around 5%, reflecting the reduction in revenue and, to a lesser extent, delays in the implementation of certain cost reduction initiatives to 2025. Free cash flow was reduced from at least $550 million to a range of $450 million to $500 million, reflecting the after-tax effects of the reduction in adjusted[1] operating income guidance.

This quarter reminds us no single performance indicator or quarterly result defines our Reinvention. Consistent progress in operating efficiency, client perception, services signings and expected sales force productivity gains give us confidence we are on the path to enabling long-term profitable growth through Reinvention.

In 2025, we expect a return to revenue growth, supported by the inclusion of revenues associated with the pending acquisition of ITsavvy, new product launches, improved sales productivity, and growth in digital and IT Services. We also expect growth in adjusted operating income and margin, driven by growth in revenue and incremental gross cost savings from actions implemented in 2024 or expected to be implemented in 2025.

Due to lower-than-expected revenue in 2024, we no longer expect to grow adjusted operating income $300 million above 2023 levels by 2026. However, we continue to expect growth in adjusted operating income and a return to double-digit adjusted operating income margin over the course of our Reinvention.

In summary, 2024 has presented unexpected operating challenges. Despite these challenges, in Q3 we grew adjusted operating income and margin year over year, a trend we expect to continue as we implement further Reinvention actions aimed at simplifying our organization and driving closer alignment to the economic buyers of our products and services.

Xavier Heiss, Chief Financial Officer

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[1] For more detail on Q3 results, please see our press release and earnings presentation.

Q3 2024 Earnings Presentation
Xerox Releases Third Quarter Results

For a discussion of factors that could cause results to differ from our expectations, please refer to the forward-looking statement in our press release. The press release also contains a discussion of the non-GAAP metrics and a reconciliation of those metrics to the most directly comparable GAAP metrics.