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Jabil, Inc. (JBL)

Q4 2019 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Greetings and welcome to the Jabil Fourth Quarter 2019 Financial Results and Investor Briefing. At this time, all participants are in a listen-only mode. A question-and-answer session will follow the formal presentation. [Operator Instructions] As a reminder, this conference is being recorded.

It is now my pleasure to introduce your host Adam Berry, Vice President of Investor Relations. Please go ahead sir.

Adam Berry
Vice President-Investor Relations, Jabil, Inc.

Hello, and welcome to Jabil's fourth quarter of fiscal 2019 earnings call and investor briefing. Joining me on today's call are Chief Executive Officer, Mark Mondello; and Chief Financial Officer, Mike Dastoor. Today, Mike will begin by walking us through the fourth quarter results. Following these comments, we will transition into the investor briefing portion of the day where both Mark and Mike will review our strategy and outlook. We will then open it up for your questions. The entirety of today's call will be recorded and posted for audio playback on jabil.com within the Investors section.

Our fourth quarter press release, slides, videos, and corresponding webcast are also available on our website. In these materials, you will find the earnings information that we cover during this conference call. Please note that during the investor briefing portion of the webcast, we will be showing a video. You will need to be logged in to our webcast on jabil.com during today's session to view our slides and the video. Additionally, at the conclusion of today's event, we'll post several videos to our Investor Relations' website in the Events and Presentation section. These videos feature our business leaders and highlight the current state of the end markets they serve.

Before handing the call over to Mike, I'd now ask that you follow our earnings presentation using the slides on the website beginning with our forward-looking statement. During this conference call, we will be making forward-looking statements including among other things those regarding the anticipated outlook for our business. Those statements are based on current expectations, forecasts, and assumptions involving risks and uncertainties that could cause actual outcomes and results to differ materially. An extensive list of these risks and uncertainties are identified in our Annual Report on Form 10-K for the fiscal year ended August 31, 2018 and other filings. Jabil disclaims any intention or obligation to update or revise any forward-looking statements whether as a result of new information, future events, or otherwise.

With that, it's now my pleasure to turn the call over to Mike Dastoor.

Michael Dastoor

Chief Financial Officer, Jabil, Inc.

Thank you, Adam, and good morning everyone. I'll begin today by reviewing our fourth quarter and fiscal year 2019 results. I'm very pleased with our fourth quarter performance. During the quarter, both segments executed extremely well and delivered strong consolidated results. Net revenue for the fourth quarter was $6.6 billion, an increase of 14% year-over-year. GAAP operating income was $189.7 million and our GAAP diluted earnings per share was $0.34. Core operating income came in slightly higher than the midpoint of our guidance during the quarter at $246.1 million, an increase of 16% year-over-year, representing a core operating margin of 3.7%.

Core diluted earnings per share was $0.88, a 26% improvement over the prior year quarter. For the full fiscal year, net revenue was $25.3 billion, up 14% year-over-year. FY 2019 GAAP operating income was $701 million with GAAP net income of $287 million. GAAP net diluted earnings per share was $1.81 for the year. Core operating income was $877 million, an increase of 14% on a year-over-year basis, representing a core operating margin of 3.5%. Core diluted earnings per share for the year was $2.98, an increase of 14% over the prior year. I'd like to call your attention to two items, which impacted our GAAP results during the quarter.

First, we incurred a one-time charge of $6.2 million due to a distressed customer in the networking space. And secondly, as we previously disclosed during the quarter, we exchanged $50 million of iQor preferred stock associated with our divestiture of our aftermarket services business in 2014. The exchange in the preferred stock resulted in a one-time net non-cash charge of $29.6 million. I'll remind you in 2014 we recorded a net gain on the sale of discontinued operations net of tax of approximately $223 million. Now turning to our fourth quarter and FY 2019 segment results, revenue for our DMS segment was $2.4 billion up 2% year-over-year.

This growth was mainly due to another strong performance in our Healthcare business. Core margins for the segment improved 20 basis points year-over-year to 2.9%. Revenue for our EMS segment increased by 23% year-over-year to $4.1 billion driven mainly by the 5G/Wireless, Cloud, Energy and Automotive end markets. Core margins for the segment were 4.3% during the quarter. For the year, our DMS segment revenue was $9.9 billion consistent with the prior year while core operating income for the segment increased 25% year-over-year. This resulted in core margins expanding 80 basis points to 4%.

As an update the seasonal launch within our Mobility business, which began in Q4 is going extremely well. The Mobility team's strong execution throughout the year and their focus on supporting our customer and tightly managing cost has contributed to a strong customer relationship. However, we believe the overall mobility supply chain continues to be overcapacitized for current and future volumes. Even though our DMS margin grew by 80 basis points year-over-year, the overcapacity in Mobility business has been a constraint on DMS margins. Therefore, we are taking steps to proactively optimize our manufacturing footprint. Reducing our capacity will allow us to more efficiently utilize our fixed assets and normalize our cost structure.

As we look forward to FY 2021, we anticipate increased unit volume largely through market share wins. We believe we'll be able to support higher levels of revenue across a more optimized footprint as a result of our ongoing automation efforts and manufacturing process improvements. As such, the non-core expenses associated with our optimization activities are estimated to be $85 million. The cash component is anticipated to be approximately $35 million. Moving to EMS, in FY 2019, revenue increased by 26% year-over-year to $15.4 billion, well above our original expectations for the year as our value proposition has been well received in the areas of 5G/Wireless, Cloud, Energy and Retail Infrastructure.

Core margins for the segment declined 60 basis points year-over-year to 3.1%. This decline as we have discussed throughout FY 2019 was mainly driven by the ramp cost associated with our new business awards and softness in semi-cap. Turning now to our cash flows and balance sheet; as anticipated in Q4 inventory levels contracted sequentially with our days in inventory coming in at 58 days, a decline of six days quarter-over-quarter. Net capital expenditure for the fourth quarter was $165 million and for the full fiscal year came in slightly lower than expected at $787 million.

Our fourth quarter cash flows from operations were very strong coming in at $1.1 billion. As a result of the strong fourth quarter performance and cash flow generation, adjusted free cash flow for the fiscal year came in stronger than expected at approximately $503 million. Core return on invested capital for Q4 was 21.3% and grew by 210 basis points on a year-over-year basis to 21.4% for the full fiscal year. We exited the quarter with total debt to core EBITDA levels of approximately 1.5 times and cash balances of $1.2 billion. As we wrap up fiscal 2019, I am very pleased with our strong fiscal 2019 performance.

Core earnings per share growth of 14%, adjusted free cash flows of $503 million with returns to shareholders via dividends and share repurchases in the fiscal year in excess of $400 million. Moving forward, we hope to build on this positive momentum and expect future growth in both earnings and free cash flow to come through meaningful margin expansion and improved working capital efficiency. Before I turn the call over to Mark for additional color on our 2019 results and outline the strategic drivers of our business in fiscal 2020 and beyond we would like to share a brief video about our people. Let's take a look.

[Video Presentation] (00:10:34-00:12:26)

Mark T. Mondello
Chief Executive Officer & Director, Jabil, Inc.

I appreciate everyone taking time to join us today. I can't help but smile when I see that video. For me, the video speaks volumes. Seeing comments from our folks like true self, differences unite and diversity of thought, as CEO I love it. It's who we are and it's what Jabil is all about. You see, diversity and inclusion is core to our value system. Diversity is about having a seat at the table. Inclusion is about having a voice. And belonging is assuring your voice is heard and respected. This certainly rings true here at Jabil. Our belief system makes a difference, in fact, a huge difference. Thanks to all of our employees. Thank you for just being you. Thanks for keeping each other safe each and every day. And I appreciate all you do.

With that, please turn to slide 11, where we see our financial results for fiscal 2019. Another exceptional year, in fact, a record year in terms of revenue and income. As Mike highlighted, our team generated core earnings per share of $2.98, a 14% increase over fiscal 2018. On top of this, the team doubled free cash flow year-on-year, while returning roughly $400 million to shareholders through buybacks and dividends. During the year, Healthcare, Cloud, Wireless, Energy and Retail were our top-performing sectors; another really nice year, all the way around. Moving to slide 12, I thought it worthwhile to highlight our four-year track record. The fact is, what we're doing is working.

These three bar charts, taken collectively, provide a fantastic backdrop to our ongoing story. A catalyst to our performance is the balance and blend of our income. But as I've said previously, being diversified for the sake of diversification isn't all that special. What is impactful to me is the composition and makeup of Jabil's commercial portfolio, a portfolio comprised of a broad range of exciting products used over a multitude of end markets. I'd now like to turn your attention to where we're headed beginning with slide 13. To start, our team is carrying positive momentum into fiscal year 2020. Our strategy is continuous and remains unchanged. Our path is well-understood by our leadership team and our financial outlook is sound.

During the past three to four years, substantial revenue growth drove earnings while reducing our dependence on any single product or product family. For fiscal 2020, we plan to expand margins primarily through operating leverage and network efficiencies, consistent with our strategy and squarely within our control. As I was preparing for today's session, I asked myself, how will I judge success for our team in fiscal 2020 as we ready ourselves for fiscal 2021? For me, success will be keeping our people safe, assuring remarkable customer care, achieving near-perfect execution, delivering on our financial commitments, and giving back to the communities in which we work.

If our team can accomplish all the above, it'll be a banner year, a year that will make us proud. Moving to slide 14, you'll see the three key areas that have management's attention for fiscal 2020; optimize, execute, and deliver. Let's breakdown each area starting with optimize. To lead in our industry, we must be thoughtful in our planning, yet react quickly, simplifying complexity for our customers. With this in mind we continue to optimize data transfer and information flow across the network of our factories around the world. This advancement is possible due to our unique IT architecture and digital supply chain analytics tool. I believe this to be a real differentiator for Jabil.

While I'm on the topic of optimization, we're driving further simplification of our fixed assets and factory network; in essence, assuring investors an accurate reflection of future earnings. As Mike noted, the charge associated with this proactive action is $85 million and will be largely concentrated around our China footprint. For me, this is an excellent use of both time and funds. A complement to our optimization efforts comes in the way of execution. Inside the four walls of our factories, we pride ourselves on doing the ordinary extraordinarily well. Operationally, we obsess about keeping fixed things fixed. We do so by leveraging our tenured know-how and experience, utilizing machine learning, and employing the power of predictive analytics.

The touch and feel within all of our factories is much the same, making us consistent site-to-site and across our divisions, enabling Jabil to offer solutions unlike others in our industry. As we endlessly pursue our factory of the future, we're continuing to make investments in the areas of automation, robotics and additive manufacturing. So that brings me to management's outlook for fiscal 2020. We plan to deliver a core operating margin of 3.7% on revenues in the range of $26 billion, a 20 basis point margin expansion year-on-year. This translates to $3.45 in core earnings per share, 15% growth when compared to fiscal 2019. On top of this, we plan to deliver free cash flow in excess of $500 million for the year.

Mike will provide more information on fiscal year 2020 during his follow-on comments, where he'll also offer details on our two-year capital allocation framework. All-in-all, I feel good about where we've been but I feel even better about where we're going. If you'll now please flip to slide 19, you'll see management's outlook for fiscal 2020 and 2021 side-by-side. The company is well-positioned to deliver its solid financial results over the coming

24 months whether your vantage point is based on an absolute scale or a relative scale. Today's outlook for fiscal 2021, shows core earnings per share in the neighborhood of $4 and a core operating margin of 4%, a 30 basis point increase relative to our outlook for fiscal year 2020 and a 50 basis point expansion relative to fiscal year 2019.

Now turning to slide 20, I'll address our structure, our team, and our unique Jabil culture. The strength of structure plus team plus culture is paramount and far greater than the simple sum of the parts. Our market-facing divisions are where it all comes together and where solutions are so neatly packaged for our customers. As a team, we loathe mediocrity; we're constantly asking ourselves do we have highest standards inside of Jabil in the solutions and services we provide our customers. The amazing solutions our team brings forward to customers are derived in one or two ways. Either through deep domain expertise found vertically within each division, or what I think about as horizontal solutions, which are sewn together via insightful, unselfish collaboration and cross-talk if you will, between the divisions.

This part isn't easy, but after many years we've mastered the art of non-parochial intercompany sharing, an art that's incredibly important to Jabil in serving our customers. Another hard to replicate dimension of our model is the intimate working relationships each divisional team has with our leaders and employees throughout the company that work outside the divisions. Those folks that run the plumbing assuring the corporation runs smoothly each and every day. This is so fundamental for Jabil. And with this group, there are simply too many leaders to acknowledge individually during this session or I would so to our entire leadership team, thank you for making Jabil, Jabil.

I encourage everyone listening in and participating in today's session to please watch each of the divisional videos. As Adam said at the opening, the videos will be posted on our website. They're informative and illustrate what we're doing and how we're doing it. In closing, our team is tested and proven. Our people are awesome. Customers and shareholders remain at the forefront of our actions and I believe Jabil is making the world just a little bit better, a little bit healthier and safer each day. We have the team and ingenuity to become the most technologically advanced manufacturing and solutions company in the world.

Thank you. I'll now turn the call back over to Mike.

Michael Dastoor

Chief Financial Officer, Jabil, Inc.

Think you Mark. I am excited with the momentum underway within the business and I believe it will carry through to our next two fiscal years as we continue our natural progression towards margin and cash flow expansion. Over the next few minutes, I plan to provide you with a framework that highlights how we will execute on our strategy and deliver on our financial commitments. First, we're fully focused on expanding margins to position the company to deliver higher margins over the last few years we've targeted growth in areas of our business that have higher return profiles that offer accretive margins and strong cash flow streams. At the same time, we're focused on optimizing cost to ensure we are positioned to deliver SG&A leverage across the worldwide Jabil footprint.

Secondly, core earnings per share has gone from $1.86 in FY 2016 to a projected $3.45 in FY 2020, that's a 17% compounded annual growth rate. And finally, we're focused on generating strong free cash flow through optimization of working capital and disciplined CapEx management. These priorities are aligned and focused on delivering long-term value creation. Our performance in FY 2019 gives me confidence that our strategy is working and positions us to deliver on our commitments in FY 2020 and beyond. Next, I'd like to outline our expectations for revenue in FY 2020 by end market, along with our expectations for core operating margin by segment. I first like to discuss what's going on in our DMS business in FY 2020.

We're expecting 10 basis points of margin expansion on low single-digit revenue growth. The key takeaway this year is the considerable mix shift underway in this business. In FY 2020, we anticipate adding $800 million of Healthcare & Packaging revenue to replace $700 million of Mobility Edge Devices and Lifestyle revenue. The decline in our Edge Devices and Lifestyle business is being driven by three factors: technology changes leading to product transitions, end of life of certain products and our decision not to pursue other products that do not meet our margin and cash flow profiles. The strong performance in Healthcare & Packaging is being driven by continued growth in our base business and the continued ramp of our previously announced strategic Healthcare collaboration.

It is worth noting, excluding the ongoing ramp in Healthcare we estimate that our FY 2020 DMS margins will be closer to 4.3%. With all that said, it's also worth noting, beyond fiscal 2020, we anticipate all three end markets to resume growth. We're excited about the diversified and balanced portfolio we're building in our DMS segment and we feel our improving mix will drive more sustainable earnings and cash flow. Turning to EMS, following two years of tremendous growth as part of our diversification efforts, we expect EMS revenues to increase by 4% in FY 2020, as we intentionally shift our focus towards margin expansion and cash flow generation. Within Automotive, the strong year-over-year growth you see is driven by our customers' desire to leverage our capabilities in autonomous driving and electrification.

In semi-cap, during the slowdown the team has done an excellent job of aggressively managing our cost base to current market realities and is focused on the diversified expansion of this business, winning new customers and programs that should position us for a strong FY 2021 once the market recovers. In Wireless and 5G, we continue to see growth in 5G that is being offset by 4G, as the market transitions to newer technology. The 5G market will continue to expand over the next two to three years as the 5G infrastructure continues to roll out worldwide. In Cloud, we have seen significant growth over the last two years. Our Cloud team continues to be focused on U.S. hyperscalers as well as Tier 2 Cloud providers and is well positioned to take advantage of the ongoing shift from ODM to EMS companies, which provide a better value proposition through wider capabilities.

Today, our EMS business serves a diverse blend of end markets in areas that provide confidence in future earnings and cash flows due to longer life cycle of these products, be it Industrial or in regulated markets like Energy. We have deep domain expertise complemented by investments [ph] being made (00:31:01) in capabilities, all of which we believe will result in lower volatility and more predictable earnings and cash flow. Putting it all together in EMS, we expect a healthy 40 basis points of core margin expansion in fiscal 2020. As I mentioned earlier, we're focused on expanding our overall core margins through cost optimization and targeted growth. As a result, we are well-positioned to deliver 20 basis points of core margin expansion in FY 2020.

This expansion will be driven mainly by two factors. First, as you'll recall, we've seen tremendous growth over the last two years adding in excess of $6 billion in revenue to our consolidated results. This growth was driven by our diversification strategy up to now and targeted at end markets that offer more attractive margins and sustainable cash flow profiles. These wins manifested in strong revenue growth as we ramp these complex engineering-led programs. In FY 2020 and beyond, the maturation of these awards begins to contribute to improved profitability. And then as I mentioned earlier in my Q4 remarks, we've taken steps to proactively optimize our manufacturing footprint.

We anticipate these restructuring cost will result in net benefit to consolidated core operating income of $25 million or 10 basis points of core margin expansion in FY 2020 and $40 million in FY 2021. We anticipate the benefits to flow through mainly during the second half of the fiscal year 2020. This is an important consideration as you shape your quarterly earnings expectations for fiscal year 2020. Turning now to our CapEx guidance for fiscal year 2020, net capital expenditures are expected to be $800 million consistent with fiscal year 2019. This will come through a combination of both maintenance and strategic investments for future growth. Let's talk about our maintenance CapEx for a moment.

We now have 100 sites in 30 countries. At this scale, our factories require approximately $550 million in annual maintenance investments. This is inclusive of investments in areas such as IT, automation, and factory digitization, which will drive optimization across our footprint and position us to deliver higher profitability. We are also investing in strategic growth in targeted areas of our business that will deliver strong margin expansion and free cash flow. Our strategic growth CapEx will be targeted in end market such as healthcare, 5G/Wireless, Energy and Industrial, Automotive, Retail, and Packaging. Turning now to the free cash flow, in FY 2020, we will continue to generate strong cash flows as a result of earnings expansion along with our team's ability to execute and efficiently manage working capital.

Working capital improvements will come mainly through improved inventory levels as growth moderates and the component market continues to normalize. These factors coupled with our disciplined CapEx gives me confidence in our ability to deliver adjusted free cash flow of more than $500 million in FY 2020. Turning now to our capital allocation framework; over the next two years, we expect to generate significant free cash flow. Given this dynamic, I thought it would be appropriate to walk you through our capital allocation framework and at a high level, how we plan to deploy our capital over the next two years.

Our capital return framework beyond organic investments will prioritize a commitment to our dividend, share repurchases, and a combination of targeted M&A and optimizing our capital structure. With the $600 million authorization we announced this morning, we are on track to return more than $2 billion to shareholders in the form of buybacks and dividends. So, what does all this mean? We remain comfortable with our ability to generate strong cash flows which will afford us the ability to return capital to shareholders, maintain investment-grade ratings and ensure we maintain an optimal capital structure.

Turning now to our first quarter guidance on the next slide; DMS segment revenue is expected to increase 3% on a year-over-year basis to $3.1 billion while the EMS segment revenue is expected to increase 11% on a year-over-year basis to $3.9 billion. We expect total company revenue in the first quarter of fiscal 2020 to be in the range of $6.65 billion to $7.35 billion for an increase of approximately 8% at the midpoint of the range. Core operating income is estimated to be in the range of $235 million to $285 million with core operating margin in the range of 3.5% to 3.9%. GAAP operating income is expected to be in the range of $128 million to $206 million. Core delivered earnings per share is estimated to be in the range of $0.82 to $1.04. GAAP diluted earnings per share is expected to be in the range of $0.14 to $0.58.

The tax rate on core earnings in the first quarter is estimated to be in the range of 26% to 28%. Turning now to our assumptions for FY 2020 and FY 2021, in order to provide better clarity on our view of the business and market environment over the next few years, we thought it'd be helpful to provide some high level assumptions that are embedded in our targets. As we transition to my final slide 31, you can really begin to see the earnings power of the diversified and the balanced Jabil. We believe we are well-positioned to deliver core margin expansion as our maturing new business awards continue to scale. We believe this focus together with our working capital efficiencies position us to deliver 4% in core margins in FY 2021 along with $4 in core EPS and $600 million plus in free cash flow. And importantly our balanced capital allocation framework approach is aligned and focused on driving long-term value creation to shareholders.

I'd like to thank you for your time today and for your interest in Jabil. I'll now turn the call back over to Adam.

Adam Berry
Vice President-Investor Relations, Jabil, Inc.

Thanks Mike. We will now begin our Q&A session. I'd like to remind our call participants that per our customer agreements, we will not address any customer or product-specific questions. We appreciate your cooperation. We are now ready for Q&A.

QUESTION AND ANSWER SECTION

Operator: Thank you. We'll now be conducting a question-and-answer session. [Operator Instructions] Our first question today is coming from Adam Tindle from Raymond James. Your line is now live.

Adam Tindle
Analyst, Raymond James & Associates, Inc.

Q

Okay. Thank you very much and good morning. Mark, I just wanted to start off with the fiscal 2021 EPS target of $4. I think that implies similar EPS growth as fiscal 2020 mid-teens year-over-year. Hoping you can touch on the composition of that growth from 2020 to 2021, because if we think about from 2019 to 2020 there's some identifiable things driving EPS growth like J&J getting to the full run rate, the EMS costs that burdened last year not repeating and now you've got $85 million of cost take-out. When you thought about guiding fiscal 2021 for the same EPS growth, what are the drivers of that growth that gave you the confidence to guide that far out as we sit today?

Mark T. Mondello
Chief Executive Officer & Director, Jabil, Inc.

A

Thanks Adam. So, I think you touched on a few of them. For us as we look at going from 2019 to 2020 and then 2020 to 2021 certainly normalization in our Healthcare business with what's going on with J&J, I think Mike also shared in his opening remarks and his assumption set that we believe we'll see or start to see a recovery in semi-cap in calendar, summer 2020. So we'll believe that will carry us into 2021. And then I also believe that across a number of our business sectors Adam, the 5G enablement will start, I think for real as we get into early to mid-fiscal 2021 and that will be beneficial as well. And then if I touch on the $85 million that Mike talked about, I think the timing and the use of those funds is quite good at the moment when I think about where our business inside of China sits. So, all-in-all, I stack all that up and that's where we decided to give you guys a look-see at fiscal 2021 and I'm pretty pleased with the outlook. Now we've got to execute. But it's squarely right in front of us.

Adam Tindle
Analyst, Raymond James & Associates, Inc.

Q

Okay. That's helpful. Maybe just as a follow-up for Mike, you had obviously very strong performance in free cash flow, exceeding your original goals for fiscal 2019 and I know this has been a focus. So if you can maybe just touch on some of the discipline you put in place to achieve this? And it does sound like you're expecting kind of the same level of free cash flow in fiscal 2020, but growth is attenuating, so are there offsets or is this just kind of more taking a conservative approach like you did last year? And if you want to wrap it up with the capital allocation and buyback decision which is the largest authorization ever, that'd be helpful?

Michael Dastoor
Chief Financial Officer, Jabil, Inc.

A

So, yeah, Adam extremely pleased with our cash flow performance in Q4 consistent with previous years. Some of the disciplines we put in place on inventory on AR/AP all of those are coming through, working capital efficiencies are improving. There'll be puts and takes as we go forward, obviously, when we do our strategic collaboration, the inventory levels go up a little bit, then they come back down throughout FY 2020. So, there's a lot of efficiencies taking place in the working capital side.

And I feel really good about the $500 million plus that we put out for free cash flow, maybe there's a little bit of conservatism in there but it includes all the other pieces on the optimization side and some of the cash. I think we've mentioned about $35 million of cash will go out on the optimization side as well. So feel good about that. Capital allocation, I think the basis, I think, it lays out a clear path on what we're trying to do over the next two years and I think the starting point is our free cash flow number and the share buybacks and dividends of approximately 60%, we feel is a good target to try and head over the next two years.

Mark T. Mondello
Chief Executive Officer & Director, Jabil, Inc.

A

Hey Adam. This is Mark again. While I was listening to Mike talk – another thing that popped in my head to your question around 2021 is, Adam alluded to it and I think I mentioned it somewhere in my prepared remarks. I think for both sell-side, buy-side and anybody interested in the company taking some time and looking at the videos that were posted or will be posted right after the call will be extremely beneficial in terms of activities that will also contribute to 2020 and 2021.

Adam Tindle
Analyst, Raymond James & Associates, Inc.

Q

Appreciate it and congrats on the strong year.

Mark T. Mondello
Chief Executive Officer & Director, Jabil, Inc.

A

Yeah. Thanks Adam.

Operator: Thank you. Our next question today is coming from Steven Fox from Cross Research. Your line is now live.

Steven Fox
Analyst, Cross Research LLC

Q

Thanks. Good morning. I had two questions. First off, can you talk a little bit more about the process that went into deciding to take some capacity out on the Wireless side? I heard some excess capacity concerns, which I think were there a year ago, but then also you were talking about growth when you get out to fiscal 2021. So is it just a mismatch capacity, different types of programs that came up, made the decision happen? I'd love some color on that and then I had a follow-up.

Mark T. Mondello
Chief Executive Officer & Director, Jabil, Inc.

A

Yeah. Steve, let me take a swing at it and then maybe Mike will add some commentary. What we felt is, is if we look at the leadership team we have in Jabil Green Point today, the work they've done in the last 18 months is fascinating to me. And the fact that we're taking out some capacity is no indication around health of business, lack of health of the business. Where we're positioned is as good today as we've ever been. Market share is in good shape. The team has just done a tremendous job of – for lack of better word, getting more water through a smaller pipe.

And so we looked at all of this and said the timing feels pretty good to take out some capacity. There's a small subset of that capacity that needed to be taken out regardless, but the vast majority is, is we really wanted our kind of our back half of 2020 and certainly 2021 financials to be properly reflected, if you will, for again, lack of a better term. So I think it's really good decision and I think the timelines of the decision is appropriate. And I don't know if you got anything to add Mike?

Michael Dastoor
Chief Financial Officer, Jabil, Inc.
A

And so, some of the automation and manufacturing process improvements that we've put into place over the last 18 months, that makes us – that gives us confidence that we can put in more incremental revenues through a reduced capacity. And we sort of, we feel really good about our market share. There's no loss of market share. In fact, we're gaining market share. So overall, I think it's the right decision and it contributes to DMS margins.

Steven Fox
Analyst, Cross Research LLC
Q

That's very helpful. Thank you for that. And then, just as a follow up, the message came through loud and clear in terms of improving margins and optimizing what you have in terms of programs. But how do you manage the customer relationships going forward, as you execute that, maybe they want to add more to the Jabil pipeline, but that doesn't seem to be in the cards in the next 12 to 18 months? Thanks.

Mark T. Mondello
Chief Executive Officer & Director, Jabil, Inc.
A

Well, I'm not so sure it's not in the cards. I think there's two elements for Mike and I. One is, we continue to improve the overall portfolio both in terms of our right to play in certain markets, selection of certain markets that we think are a bit more stable, a bit more predictable at times longer product life cycles. And then, in addition to that, one of the things that we've done a really nice job of, so Steve, you know well, the last three, four years our hair has been on fire a bit in terms of overall growth for a number of well-thought strategic reasons.

Taking our foot off the gas, I think, is healthy. We've put a lot of pressure on the factories, a lot of pressure on the team. So now it's time to slow the car down just a hair, refine it, polish it up, but in terms of – if we've got good opportunities, I think the way we look at that is reset in hurdle rates for each of our business sectors and business divisions. So, what you could expect is, is if revenue – if we do take on opportunities and revenue creeps up, I think there's a high probability that additional earnings will come with it without any attenuation to margin – either in 2020 or 2021.

Steven Fox
Analyst, Cross Research LLC
Q

That's very helpful. Good luck going forward.

Mark T. Mondello
Chief Executive Officer & Director, Jabil, Inc.
A

Yeah, thanks Steve.

Operator: Thank you. Our next question today is coming from Jim Suva from Citi. Your line is now live.

Jim Suva
Analyst, Citigroup Global Markets, Inc.

Q

Thank you very much guys. If my math is right, it might be wrong, I think the full year fiscal 2020 sales growth rate is slightly under 3%, around 2.7%, but the Q1 outlook is up about closer to 8%. Maybe my numbers are wrong on that, but it seems like you're expecting a strong wind-down or tail off of growth as the year progresses. Is that due to you exiting the business and it looks like this category called Edge Device and Lifestyles is the biggest challenge there? Can you walk us through kind of the linearity? Is my math right and kind of what's going on there? Thank you.

Mark T. Mondello
Chief Executive Officer & Director, Jabil, Inc.

A

Hey Jim, I think your math is right. I think the Q – if you look at the Q1 kind of growth rate, the Q1 growth rate is going to be kind of double digits year-on-year Q1-to-Q1 on the EMS side and then normalizes throughout the year. I think that's twofold. One is Q1 of last year was a little bit of a abnormality because we hadn't ramped any of the new businesses yet. So, the denominator and the growth rate was a little bit distorted.

I think if I think about Q2 and Q3 and Q4, we end up with kind of tougher comps with growth towards the back half of the year based on the timing of the new business ramps and how they laid into 2019. So, part of it is kind of the overall comps year-on-year comparison for 2019. And then as well as the first half of fiscal 2020 which is really kind of the back half of calendar 2019 is also an area where we're completing ramps. So, overall your math is correct and I wouldn't take anything away from that other than it's really about how the comps are measured.

Jim Suva
Analyst, Citigroup Global Markets, Inc.

Q

And then am I correct that the biggest challenge is the subdivision or sub-segment you called Edge Device and Lifestyles that looks like year-over-year is going to be down about $0.5 billion, is that right? And help us just understand that a little bit.

Mark T. Mondello
Chief Executive Officer & Director, Jabil, Inc.

A

I would say in our DMS segment where Edge Device plays, that's a fair observation. And I would say that overall on Edge Device what we call Edge Device and Lifestyle, Jim, there's three items that are playing there. So, I think on our – for lack of a fancier term, our green and blue slide that Mike spoke to you on end market that shows Edge Device Lifestyle for the year-on-year going from about $3.5 billion to $3 billion. I don't remember the exact numbers, but call it down $400 million, $500 million year-on-year, that's for a few different reasons.

Number one is there is a significant number of products in that bucket. So, a number of those products are going through technology changes as things prepare for 5G. Number two is certain products are just plainly going into life. And number three is management's just made some decisions not to pursue follow-on products based on those products not meeting either a margin structure or cash flow priorities. The nice thing about that, Jim, is we peel $400 million; $500 million out of Edge Device and it gets replaced by a really healthy outlook from Healthcare and Packaging. So I think the swap is quite good and really sets a nice platform for us as we move into fiscal 2021.

Jim Suva
Analyst, Citigroup Global Markets, Inc.

Q

Great. And then quickly can you just update us on the Johnson & Johnson transition? Has it – I'm sure it's still transitioning if not fully done would be my assumption, maybe either number of sites or amount of revenues or just where we think about the phase [ph] or inning (00:52:16) of that transition? Thank you so much.

Mark T. Mondello
Chief Executive Officer & Director, Jabil, Inc.

A

Yeah, sure. The – when we first announced the wonderful collaboration with J&J MD, there were some noise out there about geez, you guys going to be able to execute? This is like other big deals done in the industry that maybe didn't turn out so well. I think I said in our June call that Wave 1 and Wave 2 were completed and completed to plan. Those waves had five factory sites and we welcomed all the employees from those sites. Wave 3, Jim is coming along as planned. It'll be integrated and closed on time. In fact the plan is for the end of this month. So all-in-all really, really pleased, lots of hard work. But I think it's a win-win for both Johnson & Johnson and Jabil. And as I said, I think in the June call, revenues from the transaction still look to be in the $800 million to $1 billion range for fiscal 2020.

Jim Suva
Analyst, Citigroup Global Markets, Inc.

Q

Thank you so much for details and clarification. It's greatly appreciated.

Mark T. Mondello
Chief Executive Officer & Director, Jabil, Inc.

A

Yeah. Thanks Jim.

Operator: Thank you. Our next question today is coming from Matt Sheerin from Stifel. Your line is now live.

Matthew John Sheerin
Analyst, Stifel, Nicolaus & Co., Inc.

Q

Yes, thanks. Good morning and thanks for all the details on the subsectors, very helpful. In your outlook you talked about growing the Auto and Semi-cap segment fairly significantly. Is that mostly on the auto side? You talked about continued weakness in semi-cap until basically the end of your fiscal year? So where is that growth coming from?

Mark T. Mondello
Chief Executive Officer & Director, Jabil, Inc.

A

Sure. Thanks for the question Matt. Again in Mike's prepared remarks and his assumptions as we sit today and it's been a moving target, unfortunately it's been a target that's moved [ph] on us (00:54:21) a couple of times to the right. But Alex Parimbelli and his team will oversee that part of our business, has kind of put a little bit of a more stable guidepost in thinking that our semi-cap recovery at least as applicable to Jabil, we should start seeing recovery in summer of calendar 2020 and we think that recovery carries through beyond end of our fiscal 2020 and into 2021. And then on the Automotive side, Mike Loparco and his team, Chad Morley all the folks that run our Automotive business have this really well-positioned, specifically in areas of electrification and sensing around the vehicle. So that's where the growth is coming in both of those sectors combined.

Matthew John Sheerin
Analyst, Stifel, Nicolaus & Co., Inc.

Q

I guess despite the fact that the auto production continues to be weak, is that just incremental program wins basically?

Mark T. Mondello
Chief Executive Officer & Director, Jabil, Inc.

A

Well, it's two things. One, it's always great to have huge wins [ph] at your sale (00:55:22) in terms of market growth. But when we take a look at where we're positioned in the marketplace, it's not just all about vehicle production it's about content per vehicle. And again where we've chosen to participate strategically, content per vehicle for us looks quite good.

Matthew John Sheerin
Analyst, Stifel, Nicolaus & Co., Inc.

Q

Okay, great. And then on DMS, could you talk about the packaging area? I know that's – has not been a big contributor to profits. I know you've had some management changes there. You've had some more optimistic outlook. So can you talk about that business and how that contributes to your op margin increases over the next couple of years?

Mark T. Mondello
Chief Executive Officer & Director, Jabil, Inc.

A

Yeah. I chuckled because I remember sitting here not that long ago, talking about the drag on the company from our Packaging group. And happy to say that, the Packaging business continues to grow double digits in terms of topline, the drag on the company is now gone. And I said in my prepared remarks, I made some comment around one of the things we pride ourselves on is, keeping fixed things fixed. And the lady that we hired out of the packaging industry has turned over the vast majority of our Packaging leadership team.

What she's dove into with her team is a service offering now and a solutions offering now in the packaging space from a company that has massive scale, great capabilities in terms of miniaturization, precision machining, coatings, electrical and electronic assembly and combining that with a pure packaging molding background, and we think our service offering is quite good. So certainly, our Packaging business is planned to be a material contributor as we move into fiscal 2021 and certainly a contributor in helping us get the company to the 4% margin outlook that we talked about for fiscal 2021 as well.

Matthew John Sheerin
Analyst, Stifel, Nicolaus & Co., Inc.

Q

Okay, great. Thanks a lot Mark.

Mark T. Mondello
Chief Executive Officer & Director, Jabil, Inc.

A

Yeah.

Operator: Thank you. Our next question is coming from Mark Delaney from Goldman Sachs. Your line is now live.

Mark Delaney
Analyst, Goldman Sachs & Co. LLC

Q

Yes, good morning and thanks for the detailed presentation and slides. [ph] I was first hoping (00:57:43) to better understand your manufacturing plans and as the company constructed its CapEx plan for fiscal 2020, I'm curious if you're contemplating any increased manufacturing in different geographic locations because the tariffs or maybe just more broadly are you seeing any interest from customers or potential new customers in moving the manufacturing locations?

Mark T. Mondello
Chief Executive Officer & Director, Jabil, Inc.

A

Thanks Mark. So there's a couple of different questions there. In terms of trade/tariff issues, I said back, I think it was the June call that as we sit today no big material impacts to us. As we're sitting now in September, again very little materiality in terms of actual business moves, I think I mentioned something around the fact that there continues to be a deep-rooted supply chain in China. A lot of our customers when they look at the analysis don't see a great payback in terms of moving existing business. And then there's a decent amount of our China revenue that's consumed in other Geo's other than the U.S. so kind of not applicable. With all that said Mark, one of the things that we have taken a hard look at in the last 75, 90, 100 days is, we do think with all the growth we put into the company, general footprint expansion is essential.

And so from a CapEx perspective we're going to continue to expand our footprint and a lot of that expansion is largely outside of China. Most of that expansion is in support of our EMS business. And then there's probably an OpEx component to that Mark. As I think about the overall EMS margins and somebody else earlier in the conversation today was asking about it. Our EMS margins are always, the last number of years, stronger in the back half of the fiscal year versus the front half. This year our EMS margins will also be lighter in the front half versus the back half and a small subset of that is, is we've planned about $10 million, $12 million of OpEx in the first half of the year in terms of EMS as far as footprint expansion strategically. So I hope that answers your question. And by the way, that's all build into our model and our outlook.

Mark Delaney
Analyst, Goldman Sachs & Co. LLC

Q

Yeah. That's all very helpful. Thank you for that. My follow-up question was the outlook for the Enterprise business, lower revenues and the guidance for this year. Is that just more end-market weakness or anything around the programs that Jabil is tied to that we should be thinking about? Thank you.

Mark T. Mondello
Chief Executive Officer & Director, Jabil, Inc.

A

Yeah. I think the answer is yes. We've been participating in that space literally forever. We're very well-positioned in the space with our service offerings. We understand it inside and out. And overall, if I think about the enterprise space collectively, if I set Cloud aside, we're not going to see big growth in that sector of our business. But it's still a very important part of our business, has lots of critical scale. I think the numbers Mike showed on our sector chart is, still a $4 billion business for us. Really good in terms of stable cash flows so all-in-all, pleased with the business. But, yes, your thesis or understanding around the end markets, I think, is correct.

Mark Delaney
Analyst, Goldman Sachs & Co. LLC

Q

Thank you.

Operator: Thank you. Our next question today is coming from Ruplu Bhattacharya from Bank of America Merrill Lynch. Your line is now live.

Ruplu Bhattacharya
Analyst, Bank of America Merrill Lynch

Q

Hi. Thank you for taking my questions. First one, just to clarify the focus on footprint optimization. Are you actually going to use the $85 million to repurpose the factories from one area of DMS to another or are you actually closing factories? And related to that – you've got Mobility revenues declining $200 million in fiscal 2020. Some people think that the next year, fiscal 2021, can be a strong year for 5G-related Mobility. Would you have enough capacity to support that? And could Mobility revenues then grow in fiscal 2021?

Mark T. Mondello
Chief Executive Officer & Director, Jabil, Inc.

A

Hi, Ruplu, it's Mark. Let me take a swing and let Mike add. So on the Mobility side, I think, our outlook 2019 to 2020 you're right, down $200 million. I don't think that's overly material, but directionally it's down. I think we're being somewhat conservative this year in the Mobility business. It's not an indication, as we said earlier, in terms of how we're positioned. It's not an indication of that whole sector for us in terms of market share.

We are quasi-bullish on Mobility for 2021, again, based on 5G. So as I also alluded to earlier, it's really about the incredible job our team's done around Green Point. We're just getting better water flow through smaller pipe and that's due to factory optimization, layouts, efficiencies, automation, robotics. And again some of the CapEx we spent the last couple of years is really starting to pay good dividends for us on the factory floor. So again, I wouldn't read anything into it in terms of how we view the Mobility market or how we view the relationships we have in that area, quite frankly, it's all in relatively good shape. Mike you got anything to add?

Michael Dastoor
Chief Financial Officer, Jabil, Inc.

A

No, I think the biggest factor is that the ability to drive more revenues through our reduced capacity that we're putting in place. I think Mark talked about automation, robotics, all of that's going to take over the next year or so, we'll be able to drive a lot more revenue through a much, much reduced footprint.

Ruplu Bhattacharya
Analyst, Bank of America Merrill Lynch

Q

Okay. Thanks for the clarification on that Mark. Maybe the next question on EMS, you've got the Wireless, 5G, and Cloud revenues flat in fiscal 2020. I would've thought that there would be some 5G build-outs and you would see the stronger growth and you've done a great job with the Cloud business this year. Can you just talk about what you see – how you see that business growing in the next year and why wouldn't we see more growth in that area?

Mark T. Mondello
Chief Executive Officer & Director, Jabil, Inc.

A

Well, we might. I think the Cloud business is relatively new to us. Again, I think Alex and his whole team had done a really nice job there. I think we're looking at it going, okay, let's not get over our skis, so take that as intended. But the Cloud business is in really nice shape for us and we think the outlook is going to be quite good. I think the other thing is remember the $4 billion plus that we're showing is on a net scale. So, one could look at it intuitively and go geez, why is the growth numbers not higher with strong anticipation of 5G? A, we're not going to see a lot of 5G in fiscal 2020. But also the biggest component to that is as we move into 2021 and 2022 is there's going to be some cannibalization of LTE and 4G. So, on a net-net basis, I think our outlook is relatively conservative, but that's why the numbers look like they look.

Ruplu Bhattacharya
Analyst, Bank of America Merrill Lynch
Q

Okay, okay, that makes sense. And for my last question Mike, on the $600 million authorization, what is the cadence of that? I mean how many years is that over and how should we think about the cadence of buybacks? Thanks.

Michael Dastoor
Chief Financial Officer, Jabil, Inc.
A

I think the $600 million is over a couple of years. I think I would – for modeling purposes, I would factor in about – I think we've said 50% to 60% between share buybacks and dividends and the capital allocation framework. So, I'm factoring about $250 million for FY 2020 and $350 million for FY 2021.

Ruplu Bhattacharya
Analyst, Bank of America Merrill Lynch
Q

Thank you so much.

Operator: Thank you. Our next question today is coming from Paul Coster from JPMorgan. Your line is now live.

Paul J. Chung
Analyst, JPMorgan Securities LLC
Q

Hi, thanks. This is Paul Chung on for Coster. Thanks for taking my question. So, first, nice operating margin guidance here for the next years. But your operating margins have been kind of relatively in the 3.5% range for the past three fiscal years. What's given you more confidence that we should see some acceleration here over the next two years? Is this more a function of product mix, some cost efficiency, possibly more – higher margin design work? And then what kind of cushion are you baking in for variables you can't control, particularly, if there's a Global Recession?

Mark T. Mondello
Chief Executive Officer & Director, Jabil, Inc.
A

Sure. So, I think – geez, without trying to sound overly promotional, I think the last three or four years, everything that – not everything, I think lots of what we have talked about we've accomplished. If we go back to a year ago and what we said we would do in 2019, we largely accomplished those goals. If we go back to fiscal 2018, we largely accomplished those goals. And quite frankly our focus the last three or four years has been on top line growth for a lot of the reasons we've talked about for the last 10 to 12 quarters.

I think in the last – with where the growth has gone with the amount of growth and top line we've added to the company for all of the right reasons in my opinion, we as a leadership team now again has taken our foot off the pedal a bit in terms of growth. We're still going to grow. We're going to be bit more selective. And we're going to focus on margins and cash flows. The nice thing about that is, is sometimes growth isn't well within our control. I can tell you that the company has a 50-year track record of operational excellence and with the investments we've made in the factory the last two years, I think Mike in his CapEx slide broke out this year kind of an innovation engineering line item under CapEx.

He did so that – so that you can see from a sustainability standpoint and a technology standpoint in our factories, we're not under-investing in that area. So the good news is for the next 12 to 24 months, a lot of what we're working on in terms of margin and cash flow is squarely in our control and it's something we know how to do really, really well. I would also add to it a comment you made another component of the margin expansion absolutely is the composition of the commercial portfolio, which we feel really, really good about.

Paul J. Chung
Analyst, JPMorgan Securities LLC
Q

Okay. Thanks for that. And then my follow-up is on CapEx levels longer term. As you upgrade more manufacturing sites, it's more automation. Do you kind of see structural change in some of that maintenance CapEx? Does that $550 million kind of maintenance CapEx level come down over time? Or should we just kind of think about 3% of sales as a correct way to kind of model CapEx spend longer term? Thanks.

Michael Dastoor
Chief Financial Officer, Jabil, Inc.
A

So I talked about where we stand today with our sites. There's about 100 sites in 30 countries, that's a big footprint. It will always require some level of maintenance as we go through some of the leasehold improvements, some equipment changeover, keeping up the technologies, factory of the future, IT automation, et cetera. So I think looking forward that $550-million-ish or that 2% sounds about right from a percentage perspective.

Paul J. Chung
Analyst, JPMorgan Securities LLC
Q

Thank you.

Operator: Thank you. Our next question today is coming from Andrew Vadheim from Wolfe Research. Your line is now live.

Andrew Vadheim
Analyst, Wolfe Research LLC
Q

Thank you. Good morning. Taking a look at EMS at 2020 revenue growth the full year guidance for 4% over the 1Q guide of 11% would imply a 2% year-over-year growth for quarters two through four. So I recognize there's a tougher [indiscernible] (01:10:35) in the middle of the year particularly, but why is there such a sizable drop-off and what sort of the linearity for the last three quarters? Could we potentially see a sequential decline, 1Q to 2Q?

Mark T. Mondello
Chief Executive Officer & Director, Jabil, Inc.
A

A sequential decline in EMS revenues?

Andrew Vadheim
Analyst, Wolfe Research LLC
Q

EMS, yeah.

Mark T. Mondello
Chief Executive Officer & Director, Jabil, Inc.

A

Yeah. I think for modeling purposes, it would be good to think about EMS as flat Q1 to Q2, but could there be a sequential decline? There could. I think in our models, we're thinking about Q2 being relatively flat to Q1. And again as I mentioned a lot of that has to do with what you're measuring against last year, so 1Q of 2019 before we started layering in revenues. I don't remember the exact numbers, but 1Q of EMS last year revenue was around $3.5 billion, I think, and I think we ended the year well over $4 billion.

So, again we were ramping business through 2019. Those are the comps that will be compared against sort of stronger comps Q2 through Q4 this year. But all-in-all, I feel really good about our EMS business this year. It's still going to end up growing 3%, 4% year-on-year, so around the $16 billion I think that we gave you and more importantly is, is we'll have – we think a 30 basis point, 40 basis point pickup in margin year-on-year going from the 3.1% last year back into a more normalized range of 3.5%.

Andrew Vadheim
Analyst, Wolfe Research LLC

Q

Thank you. That's helpful. And then just one on the tax rate. Tax rate in the quarter came in a little bit below guidance. And last call, Mark, I think you made a point to discuss that overall [indiscernible] (01:12:25) tax rate had kind of come in higher than they would have – than you'd have liked. But you'd expect to get to more normalized level sort of in F 2020 and F 2021. Was the F 4Q rate sort of on – at that normalized level? Was it sort of the beginning of the normalized level?

Michael Dastoor
Chief Financial Officer, Jabil, Inc.

A

I think the tax rate depends a lot on where the revenues are being generated, like we've said in the past 100 sites, 30 countries, a little bit of a mix shift in – from one country to another that could change the tax rate considerably. We feel good with our guidance going forward in the range of 26% to 28% that we've prescribed for FY 2020. Will it be on the lower end, higher end? Don't know at this stage, but I think we feel good that it's moving in the right direction. It should continue to go down as we look out to our business mix going forward.

Andrew Vadheim
Analyst, Wolfe Research LLC

Q

Thank you.

Operator: Thank you. We've reached end of our question-and-answer session. I'd like to turn the floor back over to Adam for any further or closing comments.

Adam Berry
Vice President-Investor Relations, Jabil, Inc.

That's it for us. Thank you for joining us. The slides and videos will be on our website shortly. And we look forward to talking with everybody soon. This event has now ended.

Operator: Thank you. That does conclude today's teleconference and webcast. You may disconnect your line at this time and have a wonderful day. We thank you for your participation today.