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EDITED TRANSCRIPT

JBL.N - Q4 2020 Jabil Inc Earnings Call and Investor Briefing

EVENT DATE/TIME: SEPTEMBER 24, 2020 / 12:30PM GMT

OVERVIEW:

Co. reported 4Q20 net revenue of $7.3b, GAAP operating income of $197m and GAAP diluted EPS of $0.44. Expects FY21 revenue to be $26.5b and core EPS to be $4. Expects 1Q21 total Co. revenue to be $6.7-7.3b, GAAP operating income to be $238-283m, core operating income to be $295-335m, GAAP diluted EPS to be $0.79-1.02 and core diluted EPS to be $1.15-1.35.

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PRESENTATION

Operator

Hello, and welcome to the Jabil Fourth Quarter Fiscal Year 2020 Earnings Call and Investor Briefing. (Operator Instructions) As a reminder, this conference is being recorded.

It's now my pleasure to turn the call over to your host, Adam Berry, Vice President, Investor Relations. Adam, please go ahead.

Adam Berry - *Jabil Inc. - VP of IR*

Good morning, and welcome to Jabil's fourth quarter of fiscal 2020 earnings call and investor briefing. Joining me on today's call are Chief Executive Officer, Mark Mondello; and Chief Financial Officer, Mike Dastoor.

We'll begin today with Mike, who will review our fourth quarter and fiscal 2020 results. These slides are currently posted on our website at jabil.com. Following those comments, we will transition to our third annual investor briefing, where Mark will review our business overview and Mike will provide an outlook for our first quarter and fiscal 2021. We will then open it up for your questions.

Please note, to view our investor briefing slides during today's session, you will need to be logged into our webcast at jabil.com. Following today's session, you will find our entire slide deck for both our fourth quarter earnings and investor briefing on our website. 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 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.

Before handing the call over to Mike, I'd now ask that you follow our earnings presentation with 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, such as our currently expected first quarter net revenue and earnings. These 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, 2019, 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.

Michael Dastoor - *Jabil Inc. - CFO*

Thank you, Adam, and good morning, everyone. I'm very pleased with our fourth quarter performance. Both segments executed extremely well and delivered financial results that came in well above the guidance we provided on June '19.

The overperformance was driven mainly by 2 factors. First, during Q4, we experienced fewer COVID-related disruptions than we anticipated in June, which resulted in higher-than-expected throughput in our plants, a more efficient supply chain and lower COVID-related expenses. And second, our teams in both segments quickly moved to capitalize on upside demand, mainly in the mobility, 5G wireless and cloud end markets.

The compounding effects of higher-than-expected sales, improved productivity and lower costs allowed us to deliver strong revenue, core operating income and core diluted earnings per share in Q4, well above our expectations in June.

With that, I'll now review our Q4 and fiscal '20 financial results. Net revenue for the fourth quarter was $7.3 billion, an increase of 11% year-over-year. GAAP operating income was $197 million, and our GAAP diluted earnings per share was $0.44. Core operating income during the quarter was $255 million, well above our expectations in June, driven mainly by the aforementioned higher sales and lower COVID-related impact that came in approximately $25 million lower than anticipated.

Net interest expense during the quarter was $46 million. Our core tax rate for the quarter was 24%. Core diluted earnings per share was $0.98, an 11% improvement over the prior year quarter. For the full fiscal year, net revenue was $27.3 billion, up 8% year-over-year.

FY '20 GAAP operating income was $500 million, with GAAP net income of $54 million. GAAP net diluted earnings per share was $0.35 for the year. Core operating income was $864 million, representing a core operating margin of 3.2%. Core diluted earnings per share for the year was $2.90.

Now turning to our fourth quarter and FY '20 segment results. Revenue for our DMS segment was $2.8 billion, up 17% year-over-year. This growth was mainly due to our mobility and health care end markets. Core margins for the segment improved 60 basis points year-over-year to 3.5%.

Revenue for our EMS segment increased by 8% year-over-year to $4.5 billion, driven mainly by the semi cap, 5G wireless and cloud end markets. Core margins for the segment were 3.5% during the quarter.

For the year, our DMS segment revenue was $10.7 billion, up 8% year-over-year, mainly due to our health care business. Core margins for the segment were 3.9%.

Moving to EMS. In FY '20, revenue increased by 8% year-over-year to $16.6 billion as our value proposition continues to be well received in the areas of 5G wireless, cloud and semi cap. Core margins for the segment were 2.7%.

Turning now to our cash flows and balance sheet. In Q4, inventory days came in better than expected at 56 days, a decline of 11 days sequentially. Net capital expenditures for the fourth quarter were $241 million and for the full fiscal year came in as expected at $796 million. Our fourth quarter cash flows from operations were very strong, coming in at $687 million. As a result, the strong fourth quarter performance in cash flow generation, adjusted free cash flow for the fiscal year came in higher than expected at approximately $461 million. We exited the quarter with total debt to core EBITDA levels of approximately 1.7x and cash balances of $1.4 billion.

To further strengthen our balance sheet, during Q4, we issued a $600 million 3% senior note maturing in January of 2031. We used the proceeds to redeem our $400 million 5.625% senior notes due in December 2020.

We ended Q4 with committed capacity under the global credit facilities of $3.8 billion. With this available capacity, along with our quarter end cash balance, Jabil ended Q4 with access to more than $5.2 billion of available liquidity, which we believe provides us ample flexibility to navigate the current market environment. During Q4, we repurchased approximately 760,000 shares for $25 million, bringing our total year-to-date repurchases to $215 million.

In closing, I'm very pleased with our strong execution and resiliency in a challenging environment, and I'm encouraged by the positive momentum we carry into fiscal '21.

With that, I'll now turn the call over to Mark.

Mark T. Mondello - *Jabil Inc. - CEO & Director*

Thanks, Mike. Good morning. I appreciate everyone taking time to join our call today. I'll begin by offering my sincere gratitude to all of you here at Jabil. Thanks for hanging in there during these trying times, while never compromising the safety of our people. Your response, stamina and attitude have been amazing and so appreciated. Again, thank you all.

Today is our third consecutive year where we not only share our results and give a quarterly guide, but we also provide a complete outlook for the year ahead, so I'll get us started with thoughts on our outlook, and Mike will offer additional detail during his follow-on remarks.

Moving to Slide 11. I'll offer a few thoughts on our approach, beginning with diversity and inclusion. Being that Jabil is a service business, we know that each employee is critical to our success. We also know that each employee has the right to be treated with dignity and respect all day and every day. We operate our business in 30-plus countries, employing people that don't look the same, don't talk the same, people that practice different religions, have different sexual orientations, people with physical limitations and neurodiversities. Diversity and inclusion is top of mind as we employ folks all around the world, but we've got more work to do.

We won't abide racism or lack of human rights. We won't accept discrimination or social injustice. Our team challenges the status quo, and we hold ourselves accountable through action. Most recently, we formed a 9-person council to assist and guide our internal D&I efforts. This council will provide advocacy as we push to improve our own shortcomings. These 9 council leaders are talented and, without a doubt, will make us better.

Consistent with this focus, we're pleased to be a premium sponsor for the upcoming Special Olympics U.S. Games. This sponsorship has evolved into a partnership, granting our employees the remarkable opportunity to engage with the athletes and their coaches. This will also make us better.

In summary, our team continues to safeguard our work environment and ensure that everyone can be their true self without fear or anxiety, without harm or recourse and with full acceptance of our individual differences.

A second aspect of our approach pertains to ESG and sustainability. At Jabil, we aim to always do what's right. This includes doing right by our planet and doing right in helping others. We'll expand our use of clean energy as we strive to reduce our greenhouse gas emissions by 25% within the next 5 to 6 years.

Equally important is the pursuit of our sustainability goals as influenced by the United Nations Decade of Action. We're determined to lead our industry by attaining highest standards in the areas of employee safety, water usage, hazardous waste and supply chain management.

Also we understand what gets measured gets done, so we've applied this mantra to our people and their incredible generosity, which allows us to quantify their contributions as they volunteer their personal time.

Let's now turn to Slide 13. This slide paints a terrific picture, underscoring the effectiveness of our team and the strength of our commercial portfolio. What you see is 2 segments, where 1 plus 1 equals 3; 2 segments that complement one another, both in terms of end markets and capabilities, relevant capabilities that, when properly combined, fuel our services and our solutions; 2 segments that, when placed side by side, suggest resiliency at scale.

So let's break down each segment. Please flip to Slide 14. Roughly 50% of our DMS segment is comprised of Jabil businesses that operate in a regulated-type environment, businesses such as health care and automotive. These end markets share similar certification and validation requirements and must meet certain standards as they bring products to market. At the same time, capital investments align with the longer, more stable product life cycles.

The other half of our DMS segment is also comprised of 2 divisions: our connected devices; and mobility divisions. These divisions excel at high-volume production, advanced material sciences, aesthetically complex molding, precision mechanics and flexible automation. We're excited about the balanced portfolio within our DMS segment, with a focus on expanding margins, while offering reliable cash flows.

Let's now move to Slide 15, where I'll share a few thoughts on our EMS segment. Jabil's ability to combine years of manufacturing know-how and process standards with data analytics set us apart. Our longstanding customers leverage Jabil's unique IT network, as we manage all types of sophisticated global supply chains. Today, we serve a wonderful blend of markets across our EMS segment, markets that include 5G and cloud, industrial and semi cap, digital print and retail, networking and storage. We're excited about the broad range of customers in our EMS segment, with a focus on growing cash flows, while offering stable margins.

Putting this all together, let's look at our outlook on Slide 16. For fiscal '21, we plan to deliver a core operating margin of 4% on revenues of $26.5 billion. This mirrors what we committed to you one year ago. It's important to note that the 4% operating margin on the $26 billion correlates to $4 in core EPS, again, mirroring what we said last September.

Three primary actions give us confidence in our outlook: one, the improved makeup of our commercial portfolio; two, reduced levels of overhead; and three, lower costs associated with COVID. These 3 actions sum to roughly $180 million to $190 million of additional income year-on-year FY '20 to FY '21.

If I step back and think about where we're at today, much of our success here at Jabil is because we place the needs of the customer first, and we do so through nonparochial sharing of all resources and all capabilities. I think about this sharing as frictionless collaboration. When this collaboration is combined with the experience and actions of our team, you have a winning recipe, a recipe which delivers optimized solutions and services to our customers.

I ask that you now please turn to Slide 18. In closing, our outlook for fiscal '21 is indicative of the positive momentum we're carrying into the year. It's an outlook that's grounded by the continuation of our straightforward strategy, a strategy built on 5 basic pillars: ensuring our business mix remains well diversified; obsessing over our customers, while leading with engineering; driving growth through sharing and integrating our capabilities; expanding margins by contouring our portfolio; and leveraging our varied end markets to deliver reliable cash flows.

Lastly, to our entire leadership team, once again, thank you for making Jabil, Jabil. Most importantly, thank you for being your true self. As CEO, I'm honored to serve you year in and year out.

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

Michael Dastoor - *Jabil Inc. - CFO*

Thanks, Mark. I would also like to thank our employees for their hard work, dedication and excellent execution during a challenging FY '20. 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 in the coming year.

As we turn our focus to 2021, our financial priorities remain unchanged. 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 costs to ensure we deliver SG&A leverage across the worldwide Jabil footprint.

Secondly, in FY '21, we're forecasting core earnings per share to improve nearly 40% over FY '20.

And finally, we're focused on generating strong free cash flow through optimization of working capital and disciplined CapEx management.

Next, let's take a look at each of our operating segments, and I'd like to walk you through what we're seeing in the different end markets we serve and how each of these plays a role in delivering our financial targets.

Our DMS team's strong performance over the last few years reflects our improving business mix as a result of our intense focus on diversifying our end markets, products and customers to create a more sustainable business. The team continues to do a tremendous job leveraging our deep capabilities in this segment like tooling, precision mechanics, acoustics, optics, automation and material sciences to capture new opportunities in high-value adjacent markets.

Nowhere is this clear than in our health care and packaging businesses, which have grown tremendously over the last few years through several key wins, including a transformational strategic health care collaboration. Today, we are one of the largest health care manufacturing solutions companies in the world, and we're well positioned to capture future similar opportunities.

In packaging, we are uniquely positioned to benefit from the convergence of electronics and smart and eco-friendly packaging.

As we move to automotive, the bulk of our business focuses on electrification of auto based on a nearly 10-year relationship with the leading electric automotive company in the world. In the near term, this market is recovering faster than we expected just a few months ago. Looking forward, we remain well positioned as demand for increased safety, governmental emission regulations and the race towards electrification and autonomous vehicles are all playing a significant role in shaping the future of driving, as we know it.

Moving to connected devices. As more people worked and learned from home, we saw good demand for products, such as tablets, headphones and smart watches in FY '20. As we move forward into FY '21, we expect this dynamic to remain.

Beyond these devices, we're also continuing to shape the portfolio with products that meet our margin and cash flow profiles. Consequently, this will result in lower revenue for FY '21. Beyond FY '21, we believe the adoption of 5G will provide a further catalyst for future growth.

And finally, within mobility, we remain extremely well positioned across all models and components, as we continue to benefit from our diversification strategy. The out-of-season launch continues to perform extremely well. In tandem with this, the upcoming next-generation launch, which began in Q4, is going extremely well. Our team's technical expertise and focus on operational efficiencies continues to contribute to a very strong customer relationship.

In summary, for DMS, to me, the key takeaway this year is the considerable mix shift underway. In FY '21, health care and packaging is expected to be more than 1/3 of our DMS business, with estimated revenue growth of approximately $600 million in FY '21. Putting it all together for DMS in FY '21, we're expecting an impressive 80 basis points of margin expansion on mid- to high single-digit revenue growth.

Turning now to EMS. The trends in technologies disrupting the IT industry today are numerous and accelerating at a rate never seen before. The interplay between a dramatic increase in bandwidth brought about by 5G and the ever-growing power of computing in the cloud is creating a technology and business ecosystem that is changing at faster rates than earlier generations. All of this is happening in the context of increased consumption of silicon chips, unprecedented change in the retail landscape, additive manufacturing and software-driven architectures.

In digital print and retail, we continue to expect softness during the first half of FY '21 driven by office and retail closures. However, longer term, we are well positioned in these end markets as we partner with our customers to bring next-generation print and retail technologies to market.

Shifting gears to industrial. Demand has been relatively consistent to date, but moving forward, we're seeing signs that new building starts are being delayed, which could have an impact on demand in the first half of our fiscal year. However, in the medium to longer term, we are well positioned to take advantage of favorable macro tailwinds through capturing growth in the smart metering, power conversion and energy storage spaces.

In semi cap, during the slowdown, the team did an excellent job of aggressively managing our costs, while capturing market share and diversifying our business across both the front end and back end. With the ongoing recovery in the space, our efforts over the last 18 months are manifesting in stronger results. We are seeing solid demand. And so far, customers continue to march ahead with new fab plant investments executing to their 2020 and 2021 roadmaps.

In cloud, our unique offering continues to resonate with the hyperscalers, evidenced by the significant growth over the last 3 years, and this growth has only accelerated in the near term as, work and learn from home has significantly increased the demand for cloud infrastructure.

Our customers are looking for much more flexibility in their server and storage hardware supply chains, while greatly reducing their cycle times. The message that is resonating with our customers is our design to dust capability to provide a consistent experience across capabilities, functions and geographies. Keep in mind that when we talk about our design to dust value prop, we can design, create, make and recycle all within the same 4 walls, which is incredibly powerful as security and transparency at every step of the hardware life cycle become continually more important to our customers. Coupled with our vertical integration strategy, this level of engagement creates very sticky relationships with our customers.

It's worth reminding everyone, our cloud business is a bit unique and has been deliberately structured as a geocentric asset-light service offering. With this in mind, in FY '21, approximately $1 billion in components we procure and integrate will shift from the current purchase and resale model to a consignment service model. We will benefit from higher margins and lower cash used in this business as a result of the transition, which will further bolster the asset-light nature of our offering.

Another area undergoing rapid disruption is the 5G wireless end market. Over the last several years, we have invested in accelerated NPI, test processes and R&D, increasing our stickiness with customers and so maintaining our leadership role in the manufacture of base stations and radios, as we transition to a 5G world. We continue to see growth in 5G, offset by legacy wireless as the market transitions to newer technology. In FY '21, we expect 5G infrastructure rollouts to continue, as network operators upgrade their services.

And then finally, within the legacy networking and storage end markets, we expect consistent networking demand, but reduced storage demand driven by cautious overall enterprise spend and the ongoing shift to the cloud. In FY '21, this demand dynamic, coupled with our decision not to pursue other products that do not meet our margin and cash flow profiles, will result in lower revenue.

Following 3 years of tremendous growth, as part of our diversification efforts, we expect EMS revenues to be down year-over-year mainly due to the consignment shift within our cloud business and lower networking and storage revenue. With the current mix of business in EMS, we expect a healthy 80 basis points of core margin expansion in fiscal '21.

Turning to the next slide. As I mentioned earlier, we expect to expand overall core margins through cost optimization and targeted growth. We also anticipate a COVID-related negative impact of approximately $30 million to $50 million for the year, significantly less than FY '20, due to fewer COVID-related disruptions in our plants and the supply chain, along with lower PP&E costs. As a result, at an enterprise level, we are well positioned to deliver 4% in core margins for FY '21.

Turning now to our CapEx guidance for FY '21. Net capital expenditures are expected to be in the range of $800 million, consistent with FY '20. 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 over 100 sites in 31 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 are expected to deliver strong margin expansion and free cash flow. The bulk of our strategic growth CapEx will be in the health care, automotive, 5G wireless, semi cap and packaging end markets.

Turning now to free cash flow. In FY '21, we intend to continue generating 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. These factors, coupled with our disciplined CapEx, gives me confidence in our ability to deliver adjusted free cash flows of more than $600 million in FY '21.

Turning now to our capital allocation framework. 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. We are comfortable with our ability to generate strong cash flows, which will allow us to continue 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 1% on a year-over-year basis to $3.8 billion, while the EMS segment revenue is expected to decrease 15% on a year-over-year basis to $3.2 billion.

We expect total company revenue in the first quarter of fiscal '21 to be in the range of $6.7 billion to $7.3 billion. Core operating income is estimated to be in the range of $295 million to $335 million, with core operating margin in the range of 4.4% to 4.6%.

GAAP operating income is expected to be in the range of $238 million to $283 million. Core diluted earnings per share is estimated to be in the range of $1.15 to $1.35. GAAP diluted earnings per share is expected to be in the range of $0.79 to $1.02. The tax rate on core earnings in the first quarter is estimated to be in the range of 26% to 28%.

As we transition to our final slide, you can really begin to see the earnings power of a diversified and balanced Jabil. Today, our business serves a diverse plan of end markets in areas that provide confidence in future earnings and cash flows. We have deep domain expertise complemented by investments we made in capabilities, all of which gives us confidence in our ability to deliver 4% in core margins in FY '21, along with $4 in core EPS and more than $600 million 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 thank you for your interest in Jabil. I'll now turn the call back over to Adam.

Adam Berry - *Jabil Inc. - VP of IR*

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

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question today is coming from Adam Tindle from Raymond James.

Adam Tyler Tindle - *Raymond James & Associates, Inc., Research Division - Senior Research Associate*

And congrats on a strong finish to fiscal '20. Mark, I just wanted to start on COVID costs. It was, I think, you said $25 million lower than expected in the quarter, so I think, in the quarter, a little under $10 million a month. Thinking about where you sit here towards the end of September, is that still getting better? I'm just trying to understand how much you have to go to get to this $30 million to $50 million that you talked about for the full year in fiscal '21.

And secondly, just to clarify. Is the $50 million or so restructuring program the reason that this came down? Or is that separate and on top of this? I just want to make sure I'm not double counting.

Mark T. Mondello - *Jabil Inc. - CEO & Director*

Adam, thanks for the nice comment. I'll let Mike talk about the restructuring. And maybe, we'll ask you to clarify that a little bit.

In terms of COVID, geez, I am really happy with how we've handled it all in a really, really kind of opaque, murky deal. I mean, we take you back to February. Things were blowing up. I think our COVID costs in February, on a total monthly basis, were like $55 million, $60 million for the month. Then we moved into Q3 and COVID costs were around $50 million. And then Q4, as we were sitting in the June call, I think either Mike or I said Q4 would be around $40 million, $50 million. And as we got into 4Q, June was still kind of along that run rate, that it started to dissipate a bit in July and a more normalized run rate when compared to FY '21 as we are leaving August. And as we continue to index through September, our run rate in September looks to be much like August. So assuming that the whole world doesn't blow up again, at that point, all bets are off. But with everything kind of the way we see it, we feel pretty confident in the $30 million to $50 million.

I think a way to think about those costs are maybe 60%, 65% in the first half of the year and something like 35% to 40% in the back half of the year. With that, maybe you could expand a little bit on the restructuring question. I'll let Mike address that.

Adam Tyler Tindle - *Raymond James & Associates, Inc., Research Division - Senior Research Associate*

Yes. I was just trying to understand, with the restructuring, is that what is helping the COVID cost to get better? Or is the restructuring program on top of this and going to help in Q1?

Michael Dastoor - *Jabil Inc. - CFO*

The restructuring effort is on top of that. Nothing to do with the COVID reduction at all, Adam.

Adam Tyler Tindle - *Raymond James & Associates, Inc., Research Division - Senior Research Associate*

Okay. And maybe just as a quick follow-up. I wanted to understand from a seasonality perspective as we think about fiscal '21. It's just a little bit unusual based on your Q1 guidance to see revenue down sequentially in November quarter for Jabil. So maybe you could touch on why that's occurring. Is that -- is the full move to the consignment shift in Q1 and what it means for the out quarters and also the cadence of margin as that occurs? It looks like you're starting at such a high point, about mid-4% range in Q1, but the full year has guided to around 4%. Just trying to understand the cadence of the drop-off in margins as well.

Mark T. Mondello - *Jabil Inc. - CEO & Director*

Yes. So there's a couple of things in that. One is if I take a look at kind of our DMS business, I think kind of year-on-year Q1 '20 to '21, '21 is in the range of around 1%, so on the DMS Q1 to Q1. And I would think about our DMS business, Adam, more kind of first half to first half just based on timing of some products.

So if I take a look at -- and I don't know the exact numbers, but rough numbers would be kind of DMS first half of '20 to first half of '21, we'll probably see growth in the 6% to 8% range. And then I think if you look at the blue green slide, overall for the year, DMS will be up about $800 million from, call it, 13%, 13.2% up to around 14%. So I wouldn't get too caught up in the Q1 revenue numbers.

And then overall for the enterprise, if we execute well in Q1, like Mike said in his prepared remarks, we expect margins to be around the 4.5% range. If we -- with that same execution kind of total comparison, we could have a 6% handle on our margins for DMS in Q1. So off to a relatively strong start, which is typically how our years kick off.

And I would say, as I think about kind of Q2, Q3, Q4, if I'm thinking about shaping the year at an enterprise level, margins should be pretty stable. So if we kick off with a 4.5 %, I think Q4, we could end somewhere around 4%. And then Q2, Q3, in between in the high 3s, something like that. And if you sum all that up kind of on a weighted average basis, EMS to DMS, we're shooting for 4% overall for the enterprise for '21.

Operator

Our next question today is coming from Ruplu Bhattacharya from Bank of America.

Ruplu Bhattacharya - *BofA Merrill Lynch, Research Division - VP*

And congrats on the strong guide and the $4 target for fiscal '21, which is pretty much what you had guided in fiscal 4Q '19. So that's -- congrats on the guide. Just my first question, conceptually, I'm wondering why add automotive and transport into DMS. So just your thoughts on why that segment was added into the DMS segment.

Mark T. Mondello - *Jabil Inc. - CEO & Director*

I think it's because, every couple of years, Ruplu, we've been on, I don't know, a 5 -- 4-, 5-, 6-year journey. And we disengaged with BlackBerry back in the day. We sold our services business. We were really successful with -- in the mobility sector, and we've been working really, really hard to continue to diversify the portfolio. I don't think that work's ever done.

But where we sit today, if you just kind of sit back and look at the -- for lack of a better word, the portfolio slide and the blue and the green, geez, we've got 8 areas of our business reflected there, and I just love the way it looks. I said something like that in my prepared remarks.

As part of kind of always reshaping or, I think I used the word, contouring the portfolio, we'd like to have businesses together that make sense from a capability perspective and market perspective. And we just felt like automotive and transport fits really well with our health care business in terms of overall regulated markets and then the other shift we made.

And again, I know this can be aggravating to investors because it ends up being a lot to follow. That's not our intention. Our intention is just to give us a good platform again for the next 24 to 36 months. We took our Smart Home business, which had been in our networking storage because a lot of devices in home were networked together, and we moved some of that over to connected devices just because of 5G coming onboard. And when we think about things throughout the home, from a capabilities and an end market perspective, it fit really well into connected devices. The good news is those modest shifts don't change the enterprise level numbers, but that's the logic behind it.

Ruplu Bhattacharya - *BofA Merrill Lynch, Research Division - VP*

Okay. And for my follow-up, just on the EMS segment, just looking at industrial and semi cap. You're guiding year-on-year flat at $3.5 billion. That just seems a little conservative given industrial end markets should improve next year, and I assume semi cap is not a target revenue or margins. It should be improving. So just your thoughts on what are the puts and takes in that segment. Why are you guiding flat revenues year-on-year?

Mark T. Mondello - *Jabil Inc. - CEO & Director*

I don't want to get into all the puts and takes only because, Ruplu, our industrial business has all kinds of puts and takes. I'd say, I'd -- if I were to -- knowing that we're not going to be right on any of these numbers exactly, if I had to handicap industrial and semi cap, I would say, I agree with your comments. If there's -- if we're going to handicap that one way or the other, sitting here today for the year, there's probably more upside than not, I would say, certainly in semi cap, and that's offset by some softness at the moment in industrial.

And I think Mike talked in his prepared remarks about construction starts. Both residential and commercial, we think, will soften a bit certainly through the first half of the year and then regain some momentum towards the back half of the year. But I think you're thinking about that the right way.

Operator

Our next question today is coming from Jim Suva from Citigroup.

James Dickey Suva - *Citigroup Inc. Exchange Research - Research Analyst*

Could you spend a little bit of time talking about the shift to consignment model? And not that there's anything wrong with doing that, but was it -- is it across all your customers or a particular customer driving that? And is it all completed in calendar -- I'm sorry, fiscal Q1 and the revenue impact? Because I believe it would be a -- revenue comes out of the model for it. And then I'm just wondering, does it impact seasonality going forward?

Mark T. Mondello - *Jabil Inc. - CEO & Director*

Thanks, Jim. Sure. So I think it's really important for everybody to understand that our move to consignment wasn't reactionary. It wasn't something that we just thought of. If you go back, and I don't remember when we first started talking about our cloud business, it was 4, 5, 6 earnings calls ago. I remember, at that point in time, we gave it enough attention. We were doing the JJMD deal. And we also -- in one of those calls, we had 2 separate slides, one talking about our JJMD engagement and collaboration, which, by the way, is going very well.

And then we had a slide on cloud. There was a lot of questions at the time about are we getting into white box manufacturing in this set and the other. And we've been very, very consistent in our approach strategically in the cloud business that we are going to go into this in a geocentric service model. It's going to be a very asset light, very agile model, both on the fixed asset and net working capital side.

As that business is scaled through, call it, back half of '19 all through '20, we've always had a thought process in terms of, again, keeping the net working capital asset light as well, so this has been in the works for quite some time. And I would say the consignment model that we went to is largely around our cloud business, and it's largely in place.

So again, if you look at the shape of our EMS business, I think our guide for Q1, per Mike's comments and the press release, is like $3.2 billion for EMS. You compare that to a $3.7 billion Q1 '20, Q1 '21. That's just reflective largely around consignment. And then we also have some intentional reshaping of our networking storage business on top of that. But I would say you can consider it in place, and it will be reflective quarter-to-quarter throughout the year.

James Dickey Suva - *Citigroup Inc. Exchange Research - Research Analyst*

Got you. So you said effectively in place in Q1, so that would mean the revenue impact, it's pretty much all absorbed in Q1. And going beyond Q1, it sounds like revenue seasonality should be closer to normal because it seems like Q1 would be hindered a little bit because of the shift to consignment model, if I understand consignment correctly where you won't recognize the revenue, you're just going to pass that through.

Mark T. Mondello - *Jabil Inc. - CEO & Director*

Yes. I want to be careful that I understand your comment because this is kind of an important topic. The $3.2 billion -- saying it straight up, right, the $3.2 billion guide for EMS in Q1 is fully reflective of the consignment model. So you -- there's no, geez, we're going to come back and go, the $3.2 billion turned into $2.5 billion because of consignment. It's all in. So again, if you take that and you take a look at our Q1 '21 relative to our Q1 '20 on EMS, I think you'll see the distinction there. Q1 '20 in EMS was around $3.7 billion, something like that. Q1 of '21 is $3.2 billion. So again, it's fully reflected.

In addition to that, Jim, I believe that the blue-green slides that we shared, I spoke to it a bit, Mike went a bit deeper, shows our overall company revenue for the year, around $26.5 billion. The EMS segment, which is where our cloud business sits, shows $12.5 billion. So again, overall for the company for the year, $26.5 billion midpoint. About $14 billion of that is our DMS segment. $12.5 billion is our EMS segment. That's where our cloud business sits. Those numbers also are fully reflective of any and all consignment.

James Dickey Suva - *Citigroup Inc. Exchange Research - Research Analyst*

Got you. And my last follow-up is with the U.S. political entity list of can't build to, can't ship to, things like that, is any of that impacting your company? And how should we think about that?

Mark T. Mondello - *Jabil Inc. - CEO & Director*

Well, we talked about that last year. That was a hot topic as we were coming out of '19 into '20. Then COVID kind of dominated everything. But that's something we watch every week, every month. And I think we had talked about the fact that the first half of '19, I may have -- I may be off a quarter or 2, Jim. But directionally, as we exited fiscal '19 going into first half of '20, somewhere in that time frame, when the tariff talks were hot and heavy and relatively new and front headlines, we had said we were going to have a 2- to 3-quarter portion of our business, where we were going to spend upwards of $20 million, $25 million in terms of moving product around for customers.

At that point in time, we had suggested that if the macro holds or even weakens a little bit, all of this product needs to get built, and I can't think of a better place for customers to build it than at Jabil just because of our global footprint.

So we can continue to keep an eye on that. I've mentioned previously that if we kind of collate up all of our business in Mainland China, as we sit today, and I've said this in the past, there are certain parts of that business that we just don't think will move based on the indigenous supply chain and other factors.

We've also said that there's a significant amount of our China revenue today that's China for other parts of the world, non-U. S. And then the China revenue that we have that happens to be products to be consumed and shipped to the U.S., some of that has already shifted. And some of it, customers look at it, and they're comfortable keeping it in China for now.

Operator

Our next question is coming from Steven Fox from Cross Research.

Steven Bryant Fox - *Cross Research LLC - Former Analyst*

Mark, I was wondering if you could talk a little bit about as you -- not to put the cart before the horse and actually hitting $4, but you've been messaging that, that wasn't a major top line driver to getting to $4 over the last couple of years. It was more about improving margins on the different new programs you win -- have won. So can you just talk about how much of that is still holding true? And then as you transition through those new programs, what is the messaging to the go-to-market teams beyond this year? Is it to return to growth, leverage more internally, et cetera? And then I had a follow-up.

Mark T. Mondello - *Jabil Inc. - CEO & Director*

Okay. Well, there's a couple of questions in there, and I appreciate you not putting the cart before the horse, although I think we kind of asked for it because we came out with $4 and the 4%. So we got a lot of work to do to deliver the $4 and the 4%, but we wouldn't have put it out there if we didn't see a clear path.

Yes. For the last 3, 4 years, we've been talking about diversifying the top line, but at the same time, we've been caveating those comments with the fact that we're not going to chase revenue for the sake of chasing revenue. We're going to diversify income and cash flows, which is exactly what I think we've been up to. And I would suggest our team has been quite successful in that.

If I think about FY '21, we're certainly not chasing revenue because, on an absolute basis, some of this is consignment. Revenue is going down. But again, I would say, overall, it is about us kind of continually taking a file and not a chisel and filing the portfolio with a real kind of no-kidding focus on the margins and the cash flows. So that's what we're up to, and we're going to work really hard to do our best to deliver the $4 and the 4%.

Steven Bryant Fox - *Cross Research LLC - Former Analyst*

And then just as a quick follow-up. I understand the accounting math behind the consignment shift, but what does it mean in terms of your ability to drive better engagements with those cloud customers? Is that competitive advantage? Is it something everyone's doing? Or what would you say that means in sort of at the customer level for this shift?

Mark T. Mondello - *Jabil Inc. - CEO & Director*

I would say it's neutral. That one aspect is neutral. It's -- there's -- in our geocentric asset-light service business, there's high dollar components where we don't provide much value. And so having those pass-through materials is distortive to the real returns we should be getting on the value add we provide the customer.

I would say our cloud business is founded on the services our team provides, the geocentric nature of it, the flexibility, the agility. I mean I think about COVID was unplanned. And COVID hits, and all of a sudden, people are working remotely, working from homes. And the ability of our cloud team to react, oh, by the way, as well as our mobility team and our connected devices team, I mean, those volumes spiked up.

So I would say it's -- the most important part of our approach to that model is -- or that business is the model itself and the relationships that we have, Steve.

Operator

Our next question is coming from Mark Delaney from Goldman Sachs.

Mark Trevor Delaney - *Goldman Sachs Group, Inc., Research Division - Equity Analyst*

And congratulations on the strong quarter. The first question was just following up on what Steven was just talking about in the cloud business. And the company has been driving some very nice growth in cloud. I think one customer, in particular, hasn't been good, but Jabil has talked about having a handful of customers in the cloud and some opportunities to grow. Obviously, that's a market that should exhibit growth, but grow as Jabil becomes bigger within the cloud market. Can you give a little bit more what sort of opportunity Jabil sees either in FY '21 or longer term to continue to take share within the cloud business?

Mark T. Mondello - *Jabil Inc. - CEO & Director*

Mark, I really, really appreciate the question. I'm not trying to duck the question, but we're in the process now of varying conversations going on with current customers, hyperscale customers, smaller customers. So I just -- I don't want to get into it on a customer-by-customer basis.

I think what we've said in the past is we've got reasonably good confidence in our approach to the -- to what we're doing in that market overall. And we certainly expect that market to be kind of multi-customer-faceted, if you will, and that's still our path and still our intent.

Mark Trevor Delaney - *Goldman Sachs Group, Inc., Research Division - Equity Analyst*

Okay. No, that's helpful, and I understand the sensitivities. One other question I wanted to understand, I think, is on the mind of one of investors who I speak to is just thinking through some of the cyclical dynamics and the risk that either because some of the geopolitical tensions with China or just with COVID supply chain uncertainties, there's potentially been prebuying taking place in certain end markets. Can you talk about how Jabil is thinking about that risk and what you may have factored in as you were contemplating your 2021 outlook?

Mark T. Mondello - *Jabil Inc. - CEO & Director*

Which risk in particular?

Mark Trevor Delaney - *Goldman Sachs Group, Inc., Research Division - Equity Analyst*

Well, I think in a few areas. One is, to the extent you're helping -- there's many customers in China, and they're worried about some of these geopolitical tension. Have they pulled in? But even just more broadly with -- there's been some uncertainties around what ability has the supply chain been able to service customers and if customers are worried about companies not being able to manufacture or maybe they are prebuilding products because they just didn't know how COVID may impact just the overall supply chain. So had they maybe built -- pulled in any of their plans? So just high level, to the extent you've seen for either COVID or geopolitical reasons, customers building more than maybe they otherwise would have, do you think you've seen any of that? Or did you try and think about that risk at all when you're contemplating your 2021 outlook?

Mark T. Mondello - *Jabil Inc. - CEO & Director*

Okay. I understand the question, and it's appreciated. I would say, if I'm sitting on your side of the table, along with kind of the buy side folks, it's immaterial. I'll give you an example, and I'm not suggesting that there's not pockets that are material. But in the big picture of what we just guided to, our outlook for Q1 and then certainly for '21, I think all those puts and takes, there's a lot of them. I think they're immaterial.

I'll give you an example. There's certainly been -- on Steve Borges business with health care, there's certainly been some upside -- near-term upside in health care through the back half of '20 and probably the first quarter or 2 in '21, demand driven solely by COVID. Yes, there's been a fall-off in this business due to COVID with elective surgeries as an example. You spin all that up and you kind of get kind of a normalized business plan. And the same holds true with some puts and takes in industrial. Same holds true with some puts and takes in connected devices, although that ended up being a net strength.

So I would say, all in all, we don't have a crystal ball, but our Q1 guide and our overall outlook for the year, Mark, we've taken kind of all those puts and takes, we've stress tested it with all the teams, and we feel like we've kind of normalized it to the 4%, the $4 and $26.5 billion of revenue.

Operator

(Operator Instructions) Our next question today is coming from Matt Sheerin from Stifel.

Our next question today is coming from Shannon Cross from Cross Research.

Shannon Siemsen Cross - *Cross Research LLC - Co-Founder, Principal & Analyst*

I had more of a big picture question as you look forward over the next few years. You talked about the investment that you're making in terms of CapEx and maintenance in that within your facilities. But I'm curious, what kind of drivers do you see really improving productivity and providing more of a margin either to you or to your customers from a technology perspective within your factories? And sort of how do you see the -- I don't know, the factory of the future in the next few years? And then I have a follow-up.

Mark T. Mondello - *Jabil Inc. - CEO & Director*

Okay. Shannon, that's a cool question. That's kind of what we're all about. We're a company at the core that builds stuff, and so we're -- if -- I think Mike, when he talked about CapEx in his prepared remarks, talked about a split between growth and maintenance.

I would say in terms of productivity in the factories, that's probably a split between maintenance and growth. We -- I would say we're one of the leading companies that I know of in terms of automation, what I would call flexible automation, what I would call automated -- real, useful automated platforms. You combine that with augmented reality, that will start hitting our factory floors. You combine that with machine learning.

And then the other thing, I think, that sets Jabil apart is, as you take all of that, Shannon, we've got a ton of factories, call it -- we run our -- we largely run most of our business on 35, 40 sites, although we have more. If I take those -- if I take the sites that are most impactful to our earnings, they're all wrapped together in a single holistic IT system, and I don't know that anyone else has that.

So we will always continue to invest and invest aggressively in terms of the technology, the productivity that you alluded to. I think what shareholders should hold us accountable for is with those investments and with the aggression around that type of investing, I would hold us accountable for continued margin expansion and good cash flows.

If I think about the journey we've been on, on top line diversification, where we've been going through that, our margins for 2, 3 years have been stuck around 3.5%. We're starting to see the efforts come through on the margin line. That's why we -- that's why Q1 is looking at 4.5% and the year around 4%. So I think the returns we're getting on those investments are coming through in terms of our bottom line.

Shannon Siemsen Cross - *Cross Research LLC - Co-Founder, Principal & Analyst*

Okay. That's helpful. And then can you talk -- you talked about strength in health care, but maybe if you could be a bit more specific. I know, obviously, there was pressure from electives not happening and benefit from COVID in the near term. But what other key drivers, maybe talk about the Johnson & Johnson relationship, are benefiting health care?

Mark T. Mondello - *Jabil Inc. - CEO & Director*

Well, I don't want to -- the -- yes, I look at the J&J collaboration, and that's kind of business as usual now. We spoke about that for a number of calls. That partnership, the team that's responsible for that, that has gotten so deep. And boy, has that turned out. I think from both sides, we had high expectations. I think it's turning out better than even we expected, and I hope J&J would feel the same.

But the business is so far beyond that. I mean, I think we're talking about health care and packaging combined bumping up towards $5 billion. I think about that business, Shannon. I'll have -- I always have my timing a little bit off, but it's typically directionally correct. Our health care and packaging business in FY -- late '17, early '18 was like a $2 billion business. Then it started bumping up against $2.5 billion. FY '19 health care and packaging was probably closer to $3 billion. Last year, it was closer to $4 billion, and now we're bumping up against $5 billion.

And again, as pleased as we are with the Johnson & Johnson collaboration, it's just -- it's a lot more than that. Steve and his team are focused in areas so broad based today relative to 4 years ago, with things like pharma, the med device, orthopedics, diagnostics, et cetera. And then I think they'll also start to gravitate towards digital analytics and digital diagnosis as well.

And then you add to it, I'm very, very excited about what the next couple of years hold for the -- for our consumer packaging business as well. So that line item, when you look at it on the green-blue slide, again, this is a little bit of a commentary around the whole company, but the health care packaging line is as diverse, both end market and customer base, as it's ever been.

Operator

Next question today is coming from Paul Coster from JPMorgan.

Paul Coster - *JPMorgan Chase & Co, Research Division - Senior Analyst, Alternative Energy & Applied and Emerging Technologies*

Obviously, a lot to like here. I was particularly impressed by the statement of intent around diversity and inclusion, so that was welcome. A couple of quick things. One is it sounded, Mike, like you intentionally called some business in the DMS segment. I think I heard that correct. What was the criteria for doing so? What impact does that have in terms of the year-on-year sort of base percentage growth or headwind, I suppose, in 2021?

Michael Dastoor - *Jabil Inc. - CFO*

Paul, thanks for the question. We did call some. We're constantly reshaping the portfolio as we see it right now on the networking and storage side, in particular. We have been looking at all businesses we have. I think we've declared a couple of years ago that we're focusing on margins, we're focusing on free cash flow, and we're tightening up all our financial metrics around existing and future customers. So that's one of the areas that we've looked at.

In particular, I talked about connected devices as well in my prepared remarks. That's another one where we've gone and called some customers there. So it's all directional. We've said we'll do that, we'll focus on that, and that is exactly what we're doing.

Paul Coster - *JPMorgan Chase & Co, Research Division - Senior Analyst, Alternative Energy & Applied and Emerging Technologies*

And can you quantify in terms of headwinds on the -- for that segment year-on-year?

Michael Dastoor - *Jabil Inc. - CFO*

Yes. If you look at the blue and green slide, I'll just highlight the networking and storage, that's the last line on the blue side. That's down by about $600 million. A lot of that is a simple, straightforward, "Hey, let's get this to our financial metric levels."

And then you have connected devices on the green side as well. That's -- those parts of businesses that are doing really well on the connected devices. And then there's parts that we feel the financial metrics don't justify moving ahead with them.

Paul Coster - *JPMorgan Chase & Co, Research Division - Senior Analyst, Alternative Energy & Applied and Emerging Technologies*

Okay. Got it. And I think, Mark, you mentioned that you're starting to see sort of green shoots in the auto space, especially with electrification, which is good. But it's really confusing monitoring that space at the moment. The big Tier 1s all seem poised, but not active. And instead, you're seeing a lot of small companies kind of sneaking into the space at the moment, and that seems to be where most of the action is. And they're focused on sort of niche markets that seems to have the best payback, perhaps, on electrification. Do you concur that, that's the kind of business that you're seeing now? Or are you actually starting to see the beginnings of the passenger vehicle market kicking into your business?

Mark T. Mondello - *Jabil Inc. - CEO & Director*

What I would concur is it is confusing from the outside in. It's an interesting market. I think -- I don't want to generalize, but a portion of the automotive market is starting to be just a big rolling mobile device, and that's a really good spot for us, and that's where we're focused most of our attention.

We do support legacy automotive technology. But as we continue to look forward, a lot of our attention will be, again, if you just think of the automotive industry in the next 10 years, being a connected device on 4 wheels, that's kind of how we look at it, and that's where we're making most of our investments.

Paul Coster - *JPMorgan Chase & Co, Research Division - Senior Analyst, Alternative Energy & Applied and Emerging Technologies*

Do you think that the inflection point there is in a couple of years still? I mean, that's the impression I get is 2022, 2023 that the action really starts to heat up.

Mark T. Mondello - *Jabil Inc. - CEO & Director*

I would say that's probably best case. Yes, we're thinking somewhere -- I would say volumes and whatnot start to heat up, call it, 2025, something like that. But there's a lot of work. There's a lot of work that goes in between now and then, so we'll be busy.

Operator

Your next question today is coming from Matt Sheerin from Stifel.

Matthew John Sheerin - *Stifel, Nicolaus & Company, Incorporated, Research Division - MD & Senior Equity Research Analyst*

One follow-up question regarding your guidance for the storage and networking segment. I understand that you're reshaping it, walking away from some programs that are not profitable or don't meet your returns goals. But could you talk about how you see those end markets playing out, particularly storage? It sounds like you're looking at your further weakness there because of the move to the cloud.

And then beyond that, we are seeing not as stable, but some of your peers also walking away from some of these programs in the data hub space, where they're not meeting certain metrics and goals. And at some point, it looks like the leverage might swing back to the EMS guys like you, where you make win deals because customers really have nowhere to go.

Mark T. Mondello - *Jabil Inc. - CEO & Director*

Yes. I don't know. I'd look at it quite simply as I want -- I don't ever want to walk away from a relationship, but there are certain relationships where, if we get to a point that customers can provide others than Jabil business and get better value add for it, then so be it.

And I think in the network storage space, it's been a market that we've played in actively since the early '90s. We've got some longstanding relationships that are -- I don't want to lose. But again, if we get to a point where things start to change, our value proposition starts to fall off, there's no reason to force that.

And I think if I think about how well diversified the company is today, when those situations occur, we don't need to force it. I think that, that's a -- of the 8 different business line items you're seeing there on the blue-green slide, that's an area, at least, specific to Jabil that probably isn't going to have a lot of hyper growth to it for some of the reasons you described and others. If I had to handicap it today, again, knowing that our numbers aren't going to be exact, the $2.2 billion we're showing on that line item, I think it might come in a little bit stronger than that. But again, directionally, I think network and storage will be down year-on-year.

Matthew John Sheerin - *Stifel, Nicolaus & Company, Incorporated, Research Division - MD & Senior Equity Research Analyst*

Okay. And Mike, regarding the inventories, which came down nicely and your inventory gains were down, and you did talk about the supply chain being a little bit more efficient than it has been, do you expect to maintain those low inventory levels as we get through next year? And is that part of your pretty strong free cash flow guidance?

Michael Dastoor - *Jabil Inc. - CFO*

Yes. That is certainly part of our guidance. That is part of our assumption. We are constantly working on inventory levels in the organization, and I feel good about continuing to take that down further over the year.

Operator

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

Adam Berry - *Jabil Inc. - VP of IR*

Thank you. That's it for our call today. This call is concluded. Please reach out to us if you have any further questions. Thank you.

Operator

That does conclude today's teleconference. You may disconnect your lines at this time, and have a wonderful day. We thank you for your participation today.
