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JBL - Q2 2018 Jabil Inc Earnings Call

EVENT DATE/TIME: MARCH 15, 2018 / 8:30PM GMT

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PRESENTATION

Operator

Good afternoon. My name is Ella, and I will be your conference operator today. At this time, I would like to welcome everyone to the Jabil Second Quarter Earnings Call. (Operator Instructions) Thank you.

Beth Walters, Senior Vice President of Communications and Investor Relations, you may begin your conference.

Beth A. Walters *- Jabil Inc. - SVP of Communications & IR*

Thank you very much. Welcome to our second quarter and fiscal year 2018 earnings call. Joining me today on the call are CEO, Mark Mondello; and our Chief Financial Officer, Forbes Alexander. This call is being recorded and will be posted for audio playback on the Jabil website, jabil.com, in the Investors section. Our second quarter press release, slides and corresponding webcast links are also available on our website. In these materials, you will find the financial information that we will cover during this conference call. We ask that you follow our presentation slides on the website beginning with Slide 2, our forward-looking statement.

During this conference call, we will be making forward-looking statements, including those regarding the anticipated outlook for our business, our currently expected third quarter of fiscal 2018 net revenue and earnings results, the financial performance of the company and our long-term outlook for the company. 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, 2017, on subsequent reports on Form 10-Q and Form 8-K and our other securities 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.

Today's call will begin with Mark with his comments on our results and outlook for the business in fiscal 2018. Forbes will follow with comments on our second fiscal quarter results and guidance for our third quarter of 2018. Following our prepared remarks, we will open it up to questions from call attendees.

I'll now turn the call over to Mark.

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

Thanks, Beth. Good afternoon. As always, I appreciate everyone taking time to join our call today. I'll begin by extending my sincere gratitude to each and every employee here at Jabil for making safety their personal priority. Thanks for your care and commitment.

Now let's take a look at our second quarter results. I'm pleased with the quarter and the strong start to fiscal '18. Our team delivered $179 million in core operating income on revenues of $5.3 billion, resulting in core earnings per share of $0.66. Add to this the fact that Jabil's cash flows and earnings are becoming more diversified and less dependent on any single product or product family for that matter, a definitive proof point that our strategy is taking hold.

Another item that stands out for me when I think about the quarter is the fact that revenue overshot the midpoint of our guidance by $400 million, while at the same time, core earnings per share came in $0.04 above the midpoint of our guidance range, largely driven by a favorable tax rate.

So why didn't we see additional margin dollars tied to the higher levels of revenue? Let me try and explain. The additional $400 million of revenue was driven by the abrupt acceleration of 3 near-term market share wins inside of our EMS segment, combined with stronger-than-expected volumes in our Green Point sector. As for the missing margin dollars, this was based on intra-quarter investments we made in our EMS business based on the strength of the business itself, combined with cost overruns in our Packaging business as the team navigated tough challenges within the quarter, challenges that are common when faced with healthy growth. As customary, Forbes will provide more detail around our results during his prepared remarks.

I'd now like to address current business at hand starting with our DMS segment. Our DMS segment earned $83 million during the quarter and $2.4 billion in revenue, representing a 54% increase in earnings on a year-on-year basis. A key catalyst for Green Point's success was less dependency on any 1 particular product type and increased dependency on a broader hardware portfolio.

Thinking about this business as we move into fiscal year '19, I believe the same catalyst will materialize in the form of slightly lower blended margins based on a higher material content on a product-by-product basis. But most importantly, the Green Point business should display less demand volatility and improved fixed cost leverage throughout a given year.

I'm also happy to note that our team is leveraging their mechanics and materials science expertise to now ramp 2 significant program wins, both wins with new customers, 1 customer in the area of nonmobility consumer goods and the other in the area of augmented reality. Although still early days, I bring these new customer wins to your attention based on the potential scale of each.

I'll wrap up our DMS segment with a brief update on our Health Care and Packaging businesses. The teams continue to capture share as they lean into favorable market trends. The demand for affordable, results-oriented health care, in concert with the evolving technology needs being requested from the consumer packaging market, allows us to post strong double-digit growth, thus providing an awfully bright outlook and sustained momentum. Our Health Care and Packaging businesses are profoundly integral to our story as we aim for greater economic stability throughout the Jabil enterprise.

And now I'll speak to the EMS segment. Our EMS team is driving a progressive transformation as they delivered $95 million during the quarter on roughly $2.9 billion in revenue. This transformation denotes the strength of this division as our EMS team leverages end-to-end engineering solutions, deep domain knowledge and exceptional day-to-day operational execution.

As I step back and I look at our EMS business, margins remain solid, while revenue growth for fiscal '18 will now be well above the range we expected. This is good news all in all. But the really good news is 1/2 of this generous revenue growth comes by the way of new customer engagements, engagements that are strategic; engagements that come to us from end markets, which include semi-cap equipment, optical networking, Industrial & Energy, telecom and connected home. Clearly, our EMS team's doing an outstanding job as their value proposition is being well received by the markets they serve.

I'll conclude my prepared remarks specific to our business at hand by offering a few thoughts as I think about the company as a whole. Our forward guidance suggests another strong quarter and sets the foundation for Jabil to deliver core EPS growth of 20% to 25% for the second half of fiscal '18 when compared to the second half of fiscal '17. Furthermore, we remain committed to the objectives we laid out during our September 2016 Investor Day. I bring this up not to dwell on the Investor Day itself, but to highlight the importance of doing what we said we'd do over the mid- to longer term and the positive impact this may have to our valuation.

In summary, we're proud of the results we posted for this quarter as we see our strategy moving front and center. Before I hand the call over to Forbes, a few parting comments. Perhaps as I've said multiple times, shareholders remain at the forefront of our actions. To this end, we have a credible plan based on sound assumptions and historical data, much of which I've shared in today's prepared remarks. Our plan has us shifting a higher percentage of our earnings and cash flows to engineering-rich relationships, which simply offer better financial stability over the long run.

Jabil's leadership remains confident, confident because we are strengthening our business base by selectively expanding existing relationships as well as adding new customer relationships with many top brands. At Jabil, we have the scale, the infrastructure and the talent, which offer us the opportunity to move closer and closer to our aspirational goal, a goal to become the most technologically advanced manufacturing solutions company in the world. As I sit back and I really think about this ambitious goal, I'm humbled and highly encouraged by the progress that we're making.

Thanks. I'll now turn the call over to Forbes.

Forbes I. J. Alexander - *Jabil Inc. - CFO*

Thank you, Mark, and good afternoon, everyone. I'd ask you to turn to Slide 3, where I'll review our second quarter fiscal 2018 results.

Net revenue for the quarter was $5.3 billion, growth of 19% on a year-over-year basis. GAAP operating income is $130 million, with GAAP net income of $37 million. GAAP net diluted earnings per share were $0.21 for the quarter. Core operating income was $179 million, with core earnings per share of $0.66.

Turning to Slide 4 in our segment discussion. In the second quarter, revenue from our Diversified Manufacturing Services segment was $2.4 billion, an increase of 38% on a year-over-year basis, reflecting growth in programs within our Mobility and Lifestyles and Health Care businesses. This represented 46% of total company revenue, and operating income for the quarter was 3.4%.

Our Electronics Manufacturing Services segment revenue was $2.9 billion, an increase of 7% on a year-over-year basis, reflecting growth across capital equipment, Industrial & Energy and automotive customers and represented 54% of total company revenue. Operating income for this segment was 3.3%.

I'd now like to briefly turn to update you on our restructuring alignment plan. This plan continues to remain on track and during the quarter, we recorded approximately $5 million associated with this activity. We anticipate conclusion of this plan and charges of approximately $30 million in the second half of fiscal 2018. As a reminder, this plan will result in an incremental cost savings benefit of $20 million to $30 million in fiscal 2019.

I'd now like to address the recent tax reform. We do not currently expect any significant impact to our core effective tax rate from the enactment of the new U.S. Tax Act. However, in the second quarter, we did record in GAAP earnings a provisional tax expense of $31 million due primarily to the onetime mandatory deemed repatriation or transition tax on previously untaxed foreign earnings. In accordance with the Tax Act, payment of this tax will be spread over the next 8 years starting in fiscal 2019.

We continue to analyze the potential impacts of tax reform. And in particular, foreign earnings can now be accessed in a more tax-efficient manner. Should we determine opportunities are available to return these earnings, we may be required to record tax expenses related to foreign withholding taxes in the second half of fiscal 2018.

Turning now to our cash flows and balance sheet. Our cash flows from operations in the second fiscal quarter were $352 million. And cash flows from operations for the full fiscal year continue to be expected -- to be in excess of $1 billion. Net capital expenditures for the second fiscal quarter totaled $110 million; and for the first half of the fiscal year, $308 million. The full fiscal year remains on track with previous expectations of $700 million. Core return on invested capital for the second quarter was 18%.

I'm also pleased to note that during the quarter, we successfully redeemed our $400 million 8.25% senior notes and priced $500 million of senior notes due in 2020 -- excuse me, due in 2028 with a coupon of 3.95%. At the end of the quarter, total debt-to-EBITDA levels remained at approximately 2x, and cash balances were $941 million.

Turning now to our capital return framework. In the second quarter, share repurchases totaled $132 million. And since the inception of this framework, we've repurchased 25.3 million shares at an average price of $24.71. At the end of the quarter, $225 million remains outstanding on our current stock repurchase authorization. Our plans to return $1 billion by the end of this fiscal year via dividends and share repurchases remain firmly on track.

I'd now ask you to turn to Slide 5 for our review of third quarter fiscal 2018 outlook. The Diversified Manufacturing Services segment revenue is expected to increase approximately 10% on a year-over-year basis to $1.85 billion, while the Electronics Manufacturing Services segment revenue is expected to increase approximately 8% on a year-over-year basis to $3.05 billion. We expect total company revenue in the third quarter to be in the range of $4.75 billion to $5.05 billion or an increase of almost 9% at the midpoint of the range on a year-over-year basis.

Core operating income is estimated to be in the range of $125 million to $165 million, while core earnings per share are estimated to be in the range of $0.35 to $0.55 per diluted share. Our GAAP earnings per share are expected to be in the range of $0.12 to $0.38 per diluted share. The tax rate on core earnings in the third quarter is estimated to be 28%, and the rate for the second half of the year in the range of 27% to 28% based upon the current forecasted mix of earnings.

In closing, we are pleased with the first half of fiscal 2018. We remain very well positioned for the second half of the fiscal year and continued positive momentum as we move into fiscal 2019, momentum that is supported by diversified revenue and income growth within both our EMS and DMS segments.

I'd now like to hand the call back to Beth.

Beth A. Walters - *Jabil Inc. - SVP of Communications & IR*

Thank you, Mark and Forbes. Before we begin the question-and-answer session, I'd like to remind our call participants that at the request of our customers, and as usual, we will not address any customer- or product-specific questions. And we thank you in advance for your cooperation.

Operator, we're ready to begin the Q&A session.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question comes from the line of Adam Tindle.

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

Mark, you alluded to investments in EMS, which is muting some of the normal operating leverage that we might see. Can you help us quantify this in any way? And should this attenuate to allow fiscal '19 EMS operating margin to get back to or above fiscal '17 levels?

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

Adam, well, first off, I think, on the EMS margins themselves, I still feel very good about where we'll end up in fiscal '18 for EMS margins. In terms of the investments we're making, it's widespread. But if I had to take a stab, areas like automotive, Industrial & Energy probably stand out in that group more than any other. But again, the EMS business in total serves, I don't know, 200-or-so customers. So it's spread pretty evenly across the mix. I would say that we made the investments, Adam, based on the fact that early on in the quarter, there was good indications that the business was going to be quite strong. So some of this is nothing more than maybe investments we were looking at more towards the back half of the year that we accelerated.

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

Okay, it makes sense. And Mark, you completed 1 board meeting. I think you've got another one upcoming. You've been diversifying cash flows while still returning cash to shareholders. And just hoping that you can talk about how you and the Board are thinking about a capital allocation framework at this point. Does it make sense to accelerate diversification through more organic investments? And how do you balance this versus returning cash to shareholders?

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

Yes. So I love our capital allocation at the moment. I think it's very reflective of the strength of the cash flows of the business. We as a leadership team, and certainly, in conjunction with our Board, talk about that often. I think about the last couple of years, returning $1 billion to shareholders, making very, very thoughtful organic investments in what largely has been a bunch of tuck-in acquisitions. And I think sometimes the tuck-in acquisitions we do get lost and -- because they're small. And we do, I don't know, half a dozen of those a year. But I think those tuck-in acquisitions over the last 18 months have been pretty vital in both the revenue growth as well as the margins in both divisions, but certainly the EMS segment. In terms of -- we've been pretty muted on, well, the capital returns to shareholders extend beyond this fiscal year. We'll take that up -- we recognize that. We'll take it up with our Board in April and probably have more to say about that in the June call.

Operator

Our next question comes from the line of Matt Sheerin.

Matthew Sheerin - *Stifel, Nicolaus & Company, Incorporated, Research Division - MD*

Just, again, regarding the DMS segment. You've had some nice profitability growth year-over-year. And if you look at the guidance, assuming that the Nypro Healthcare business grows sequentially sort of trying to back into the Green Point number, it looks like it'll be down, I don't know, 30% to 40%. And you've had these cyclical or these quarter-to-quarter swings, obviously, in the May quarter in the past. In terms of profitability, and if you're still targeting sort of that 4% EBIT or operating margin for the EMS segment, it looks like you're still going to be at least modestly profitable in DMS for the May quarter. Is that a good way to think about it?

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

I think it's a great way to think about it. The May quarter, if you assume that we're having rational participation in our Green Point business, widespread in Green Point as well as Mobility, for the last number of years, 3Q has always been a heavy investment quarter in that part of our business. It's still a heavy investment quarter. But if you think about our guide, you think about where we set you in terms of revenue levels, you think about EMS margins kind of on an annual basis being very similar to '17, I think you back into the fact that DMS in terms of absolute profit dollars will be much better and larger than they were in 3Q '17.

Matthew Sheerin - *Stifel, Nicolaus & Company, Incorporated, Research Division - MD*

Okay. Mark, that's helpful. And on your commentary regarding some hiccups with the Packaging business, obviously, due to very strong growth there, are those issues that have been resolved? And in terms of the profitability contribution from Nypro/Health Care to DMS, do you expect that to continue to grow in terms of its contribution?

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

Yes. So for me, it's nothing that has me flustered whatsoever. The Packaging business is growing. There's a lot of moving parts. It's a complicated business, but it's a business I like a lot. To sit here and say all the issues have been resolved, I would say, many of the issues have been resolved. As we move into 4Q and into '19, I expect all the issues to be resolved.

Operator

Our next question comes from the line of Mark Delaney.

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

First question was hoping to follow up on some of the comments, Mark, you made about DMS and your expectations for fiscal '19. I think you said you expect some more stability in your DMS segment next fiscal year, but maybe the trade-off was slightly lower margins. Any quantification or better detail you can provide us on that deal?

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

Sure, Mark. Yes, so I think the comment I made around DMS applies to the whole company. I think you're starting to get a theme here. So I love the vast majority of all of our business in DMS, whether it be Health Care, Packaging or what we're doing today in Green Point. I think the comment I made in my prepared remarks is that across the entire enterprise, Mark, we are looking to drive more and more diversification in cash flows and earnings. I think that's for a couple simple reasons. Number one is we're just not smart enough as a management team to figure out all the puts and takes and what technologies and hardware products and everything else are going to win and lose across the globe today. The other comment I made is we're making some decisions inside of our Green Point business, where I would rather take stronger diversification versus reliance on some single, selected product families. And based on the diversification there, based on the higher material content on a product-by-product basis, some of the product blended margins may be a bit lower. But I think what we end up in -- within the end, Mark, is if we get that right, is we end up with a DMS business with both Green Point, Health Care and Packaging, where we get just a higher level of fixed asset utilization throughout a year. We don't get whipsawed quite as bad, and we're doing that in such a way that we've got certain parts of the overall EMS business that's just growing at faster rates than others. So I -- as I look to fiscal '19 and beyond, I really like the outlook for the DMS sector as well, along with EMS. So I kind of look at '19 going -- if we get a few things going our way, I think it's going to be a nice year.

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

That's helpful. A follow-up question for fiscal '18 outlook. You talked about areas -- a number of areas, especially in EMS, that are driving upside versus your prior views. Are there any areas or markets that you'd call out as being weaker? And any, to better understand, you can help us with in terms of, in the past, when certain end markets softened, it -- oftentimes there's a couple of quarters where things continue to get softer. And just how did Jabil think about that in terms of this guidance for this year if in fact any end markets are weaker than last quarter?

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

Yes, Mark. So I think, again, I'd think I'd answer it this way. That the -- I just -- it's hard to comprehend just how broad-based EMS is. It's just -- it's a business that cuts across, again, so many different brands, so many different customers, so many different products. If I had to characterize again where we're seeing strength: industrial energy, semi-cap equipment, auto, and then it's got a bit of a tail to it. In terms of where we're seeing weakness, touch wood right now, we're not seeing a lot of weakness in really any part of the business. And again, I think that's reflective in the revenue numbers. If you take a look at fiscal year '17, I think, on EMS, DMS segment, we did about $11 billion. And I think if you kind of extrapolate out our 3Q guidance and the annual guidance, you'll get a feel that at the beginning of the year, we thought EMS revenue might be up 3.5%, 4%, and it could very well be double that. So -- and I think what's interesting is there might be some markets we serve in EMS where the markets themselves may be a little bit weak. But what's ironic in that right now is we're actually picking up decent amount of share gains in those markets. So all in all, I feel pretty good about what we're looking at with EMS. And again, this is coming off of fiscal year '17 where the team drove margins to record highs coming off of '16 where they delivered, I don't remember the exact number, but roughly 3.5% up margins. So I like the story there quite a bit.

Operator

Our next question comes from the line of Sean Hannan.

Sean Kilian Flanagan Hannan - *Needham & Company, LLC, Research Division - Senior Analyst of Smart Grid, Electronic Mfg Svcs, IT Components & Electronic Components*

So Mark and Forbes and team, just want to see if I could get a little bit more information on the Nypro business at this point. So you folks certainly entered the year with pretty good growth expectations. We're starting to see some of that. Was hoping maybe we can get some granularity as we separate the path of what's occurring related to Health Care versus Packaging. How does that materialize here for -- as we move through '18? And what are some thoughts on how that could continue in '19? Because I believe that the growth expectations remain fairly healthy for next year as well.

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

Thanks, Sean. So I think what we said in the last number of calls, and I don't recall if I just said it in my prepared remarks a little bit ago, but I think maybe in my prepared remarks this time around, I talked about Health Care and Packaging kind of strong double-digit growth. And I think, in the past number of calls, I've called out kind of a 20% to 25% annual growth rate from, say, '16 to '19 or '20. I didn't exclude those numbers on purpose. I mean, I still think a 20% to 25% CAGR to health care and packaging is where we're at, certainly, through '19 and potentially '20. Sean, we intentionally don't break out Health Care and Packaging at the moment for a variety of reasons. I do think that one of the things I've been talking to Forbes and Beth and Adam about is the last time we did do an Investor Day was coming up on, call it, 18 months ago. I think that there's just a lot of good stuff going on in the company. And we're giving thought to putting together another Investor Day. Let's see if we pull that together. And if we do, I think at that point in time, we'll add a little bit more color around health care and packaging. But again, today, we don't break that out.

Sean Kilian Flanagan Hannan - *Needham & Company, LLC, Research Division - Senior Analyst of Smart Grid, Electronic Mfg Svcs, IT Components & Electronic Components*

Okay. Nice job on the overall diversification, by the way, within DMS. Just want to switch over to EMS then for the follow-up question. The efforts that you have underway that are driving this step-up in growth, you laid out a number of different market segments. There's a fair number of them. And it was surprising to hear such a material, I guess, upshift in the growth expectations for EMS one quarter to the next, particularly given where the magnitude of revenues are that you're already doing today. So just trying to understand a little bit better. How did that materialize so quickly? How do we think about then what's been culled from the opportunity set and what also might remain in terms of bringing in new business as we progress through the year? I don't know if there's anything that's really been kind of pulled forward here, what have you. So just trying to understand that dynamic because I think it's a -- it's a pretty big step.

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

Yes. I'm a little embarrassed by it because I -- on one hand, I'm pounding the drum with Forbes on -- we're driving for less volatility, more predictability, and we are. And I do think, if you just watch this play out for the next couple years, that's what you'll see. It's a little bit surprising to us, and it's really all around acceleration of stuff that we thought might happen in the back half of the year. We're a little bit suspect of it. I thought it might go into '19. And so it's stuff that's been on our radar. It's stuff that, in terms of wins, hit heavier than we thought might in terms of total wins. So it's acceleration. And I kind of scratch my head and say, you know what, our structure, our solution-based approach, one of the things that the team has done is they -- that's approaching a $12 billion business for us. And one of the things the leadership team has done there is they've kept that $12 billion of business really broken up in appropriate smaller bites. And those individual teams really have pulled together wonderful domain expertise, and they've just gone after these markets in a way that's different than we have in the past. And again, touch wood with our scale and our solutions, it seems to be working. So I'll take it while we can get it.

Forbes I. J. Alexander - *Jabil Inc. - CFO*

Sean, if I may add. Mark referenced earlier some of the smaller tuck-in acquisitions that we've done. And I think those are really starting to bear fruit for us and allowing our EMS teams to sell and engage customers in higher value-add content and engineering. And we've been very deliberate over the last 24 months about where we're looking and quietly building those capabilities across the company.

Operator

Our next question comes from the line of Sherri Scribner.

Sherri Ann Scribner - *Deutsche Bank AG, Research Division - Director and Senior Research Analyst*

A lot of my questions have been answered, but I was hoping to get a little more detail on the model, Forbes. If you look at the interest expense line, it ticked up. Can you give us some sense of where you think that number should be, given the changes that you made to your debt structure? And then thinking about the tax rate, 28% seems higher than what you've guided to before. What type of tax rate should we think about on a go-forward basis?

Forbes I. J. Alexander - *Jabil Inc. - CFO*

Yes, of course. Yes. This past quarter, you're absolutely correct. The interest rate was higher. This quarter, what was also included in there was, I think, it was about $2.5 million. It was associated with essentially prepaying our bonds as we swapped those bonds out. So that's a onetime negative event, if you will, to the interest rate there. So as we go forward, I'd model $38 million to $39 million a quarter, which is where we've typically been running. And then on the tax rate, next quarter, a little bit higher than we've been seeing and actually just based on the mix of earnings. We have some tax-advantaged structures in Asia. And obviously, that's an investment quarter for us in Q3 as we ramp within our Green Point operations.

Hence, you start to see these tax -- a little bit higher tax rates in the third fiscal quarter. And that should attenuate a little bit as we go through the end of the year. For fiscal 19, we'll see where that lands, but I'd suggest modeling a 26-type rate for the full fiscal year at this point in time.

Sherri Ann Scribner - *Deutsche Bank AG, Research Division - Director and Senior Research Analyst*

Okay, great. And then just the distressed customer charge that you saw this quarter. Can you give us more detail? And is that something that you expect to be ongoing? Or is that just this quarter?

Forbes I. J. Alexander - *Jabil Inc. - CFO*

Yes, that's a onetime event. And that's associated with our disengagement with Jawbone. So yes, we shouldn't see anything else attributed to that.

Operator

Our next question comes from the line of Ruplu Bhattacharya.

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

Mark, typically, the third quarter is an investment quarter for the mobility segment, and then you have ramps in the third and the fourth quarter. You think this year your investments and the ramp can be easier for you than you've had in prior years and the investment can be lower than what you've had to do in prior years?

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

You know what, you're really, really knowledgeable in the areas where we tend to do a lot of technical ramps in 3Q, and none of them are ever easy. So I wish they were. But I think, again, some of the financial impact, if you look at -- I don't know, if I just use rough numbers, I think last 3Q in DMS, we broke about even at a DMS line level. If you assume and the revenue we gave you in the slide deck today that -- let's assume EMS is about the same margin structure as it was in 3Q of '17, you'll back into some decent profits on a relative basis for the third quarter. If you go back to the 3Q of '16, if I remember right, I think we lost money at an enterprise level for DMS in '16. We broke about even last year. But I think we'll make some good profits this year, and I think that's a sign of Health Care, Packaging and then general diversification within Green Point. But the task at hand, the investments that we're making, especially around the mobility sector, are still pretty challenging. And I look forward to seeing how we do because it's good business for us.

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

Okay. Okay, no, that's helpful. And then just on the EMS side. So it looks like, like you said, I mean, for the full year, you'd probably grow double of what you had thought, maybe 7% year-on-year. How should we think about that going forward into fiscal '19 and '20? I mean, you're seeing strength in so many different end markets, but is that sustainable into the next couple of years?

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

We haven't talked much about '19. If I had to flip a coin right now, I'd say, the top line, that's not sustainable. I think that you have things where the stars align. And to think we can take a $12 billion EMS business and grow it at 6%, 7%, 8% year-on-year, I doubt that's going to happen. But boy, oh, boy, am I pleased with what's in front of us. And we'll see what '19 holds, and maybe we'll talk more about that in the June call.

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

Okay. And my last question for Forbes. I mean, if you can just give us some color on free cash flow for this year and next year. And in general, it's been a while since you've had a dividend increase. So any thoughts on that? I mean, what would be your preference in terms of M&A versus increasing the dividend versus buyback, so in general, capital allocation preferences?

Forbes I. J. Alexander - *Jabil Inc. - CFO*

Yes. And so in terms of free cash flows, I stand by what we talked about in our Analyst Day of late '16. So over that '16, '17 -- excuse me, '17, '18 and '19, generating $3.5 billion of operational cash flow, I think we're firmly on track there. CapEx of about $1.8 billion. So $1.7 billion of free cash flows. We committed to return $1 billion through capital allocation through [to] '18, again, firmly on track. So as Mark answered to an earlier question, we'll continue to work through our thinking there. Our acquisitions, as Mark had noted, are tuck-in in nature. I like that approach. We're seeing growth as a result, engineering capability. So as we move forward, we'll take a look at that. In terms of dividend specifically, I think for anything meaningful there, it'd be a significant move-up. And certainly, I have more of a preference of stock repurchases. And I think our cash flows could certainly continue to support a capital allocation policy. But more on that in the second half of the fiscal year.

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

Yes, maybe I could comment. On the -- one thing I like about what we're doing at the moment is, a, I think it's very reflective of the strength of cash flows because we're able to run the business in, I think, a very prudent way. We're able to give some money back to shareholders. And again, if nothing crash and burns in front of us, the outlook is quite good. So right now, I guess, leaning more towards the share buybacks based on where the share price is. And the other, you get a bit of a benefit there because if hypothetically, we like the way the future looks, it's a good time to lean into the buybacks. And at some point in time, if the share price were to normalize, maybe aligned with how we think the business is going to turn out the next couple of years, then maybe we lean back into the dividend. But the nice thing is, is at that point in time, we'd be paying a dividend on less shares. So I think, all around, I like our approach with what we're doing in M&A. I like our approach with the organic investments. And I -- at this point in time, I have a preference towards the share buybacks.

Operator

Our next question comes from the line of Jim Suva.

Jim Suva - *Citigroup Inc, Research Division - Director*

It's Jim Suva from Citi. On the CapEx for this year, is it still the same dollar amount, but importantly being spent in the same direction? The reason why I asked is -- or allocation. The reason I asked is it sounds like your Packaging business is really getting better strength than anticipated. And as we look ahead, should we start to build in some more support from CapEx in that allocation? Or how should we think about that?

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

Thanks, Jim. I think what we said, either Forbes, I or both of us as we came into the year, the CapEx would be about $700 million. I think that number still feels about right. And I think, in general, our CapEx today that we're spending is probably as equally spread and diversified across the business as it's ever been. So I don't know if that's where you're going with your question. Certainly, Packaging and Health Care are part of that as well as a number of areas in EMS. And I think on the EMS side, the revenue would reflect that. And on the Health Care and Packaging side, if they're growing at 20%, 25% they need a bit of capital as well.

Jim Suva - *Citigroup Inc, Research Division - Director*

Yes, that's exactly the answer to the question. And then my follow-on, though, is with that strength in both your new program wins of EMS and your packaging strength you're seeing, do we need to start to earmark some more money to support those? Or your current plans can support that growth for the foreseeable future?

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

I'll answer it in 2 parts. Number one is I think the $700 million is good for this year. We haven't talked about CapEx for next year yet, so we'll get to that later in the year. In terms of the makeup of CapEx, if I go back to, say, fiscal '15 or '16, I think a large percentage of our CapEx at that point in time and maybe even as far back as '14, was concentrated around maybe single programs. Today, if you were to Pareto-ize the CapEx for '17, and I imagine the same will hold true for this year and '19, you'd see a fairly equally spread, widespread Pareto of the CapEx. So the CapEx makeup today and next year looking much different than it did maybe back in fiscal '14, '15 and even '16.

Operator

Our next question comes from the line of Steve Milunovich.

Thejeswi Banavathi Venkatesh - *UBS Investment Bank, Research Division - Associate Director and Analyst*

This is Tejas on for Steve Milunovich. I was hoping you could talk a little bit more about the new program wins in EMS. You mentioned winning in markets that aren't necessarily growing. I guess, optical fits into that. I was hoping you could give a little bit more color on that. And second, one of your competitors has been saying that medical companies are outsourcing less. Is that something you are seeing?

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

So maybe I misspoke. I don't think I said that our wins in EMS were solely in markets that weren't growing. I think I -- I think maybe I gave a 2-part response to an earlier question. One part of my response is we absolutely are seeing strength in EMS and new program wins in areas of the market that are growing. But then we do have the benefit of -- in maybe areas of -- or end markets that we serve in our EMS business that might not be growing or flat, we're fortunate enough to pick up share. So again, when I look at the Pareto and the makeup of the increase in revenue from '17 to '18, pretty broad based. And that's kind of what I would expect based on our approach for that business.

Thejeswi Banavathi Venkatesh - *UBS Investment Bank, Research Division - Associate Director and Analyst*

And on medical? Are you seeing them outsource less?

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

We've not seen much of a change in terms of medical outsourcing one way or the other.

Operator

(Operator Instructions) We have a question from the line of Amitesh Bajad.

Amitesh Bajad - *RBC Capital Markets, LLC, Research Division - Senior Associate*

Just 1 about the long-term DMS margin target range of 5% to 7%. I guess, how should we think about it? Is there a target revenue rate above which you think the segment would be in the 5% to 7% range or maybe a mix of mobility versus nonmobility?

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

So I still -- I'm still hell-bound on getting our DMS margins to the 5% range, and I know I've been banging the drum on that for a couple of years. I think what we're doing in terms of serving all the different markets in that market quite well, I'm still confident we're going to get there. So I think -- I don't remember when I said it, Amit. But I think I said either in the June call or the September call, I said something about I thought we'd get to the 5% range the first half of '18. I think we missed that by, I don't know, $10 million, $12 million, and never thought we'd get there for the whole year. But I still think the 5% to 7% range long term for DMS is something that we're shooting for.

Amitesh Bajad - *RBC Capital Markets, LLC, Research Division - Senior Associate*

Got it. And on your CapEx of $700 million, how much of that would you say is maintenance versus expansionary?

Forbes I. J. Alexander - *Jabil Inc. - CFO*

Maintenance, roughly $250 million -- something around either $250 million or $300 million.

Operator

There are no further questions at this time. Presenters, you may continue.

Beth A. Walters - *Jabil Inc. - SVP of Communications & IR*

Thank you very much to everyone for joining us today for our fiscal Q2 results. Please feel free to reach out to us with any follow-up questions that you may have. And now we'll let everyone get back to March madness. Thank you.

Operator

This concludes today's conference call. You may now disconnect.
