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Xerox Holdings Corp. (XRX)

Q2 2025 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Welcome to the Xerox Holdings Corporation Second Quarter 2025 Earnings Release Conference Call. After the presentation, there will be a question-and-answer session. [Operator Instructions] At this time, I would like to turn the meeting over to Mr. David Beckel, Vice President and Head of Investor Relations.

David Beckel

Vice President & Head-Investor Relations, Xerox Holdings Corp.

Good morning, everyone. I'm David Beckel, Vice President and Head of Investor Relations at Xerox Holdings Corporation. Welcome to the Xerox Holdings Corporation second quarter 2025 Earnings Release Conference Call hosted by Steve Bandrowczak, Chief Executive Officer. He is joined by John Bruno, President and Chief Operating Officer, and Mirlanda Gecaj, Chief Financial Officer.

At the request of Xerox Holdings Corporation, today's conference call is being recorded. Other recording and/or rebroadcasting of this call are prohibited without the expressed permission of Xerox. During this call, Xerox executives will refer to slides that are available on the web at www.xerox.com/investor and will make comments that contain forward-looking statements which by their nature address matters that are in the future and are uncertain. Actual future financial results may be materially different than those expressed herein.

At this time, I'd like to turn the meeting over to Mr. Bandrowczak.

Steven John Bandrowczak

Chief Executive Officer & Director, Xerox Holdings Corp.

Good morning, and thank you for joining our Q2 2025 earnings conference call. The closing of the Lexmark acquisition early July marked an important milestone in Xerox Reinvention. With this transaction, we unite two industry leaders with complementary sets of operations, offering strengths and market reach. Xerox and the Lexmark offering will be combined and optimized to enhance client value, providing the foundation from which we

can expand the penetration of our IT solutions and digital services businesses as we help our clients navigate the increasingly digital nature of document workflows and processes.

I'd like to commend both Xerox and Lexmark teams, who this quarter navigated a challenging operating environment while preparing for an accelerated transaction close and integration timeline.

Summarizing results for the quarter, revenue of around \$1.58 billion was roughly flat with the prior year in actual currency and declined 1.1% in constant currency, inclusive of ITsavvy. Adjusted operating income margin of 3.7% was lower year-over-year by 170 basis points. Free cash flow was a use of cash of \$30 million, reflecting in part a delay in the sale of large portfolio of finance receivables. And adjusted loss per share of \$0.64 declined \$0.93 year-over-year, due in large part to an unfavorable tax rate. This quarter demonstrated the improved resiliency of revenue and adjusted operating income afforded by our Reinvention, specifically the benefits of a more favorable mix of revenue from faster growing businesses and a more flexible and simplified operating structure.

In the second quarter, strong demand for cloud-enablement services at our IT Solutions segment helped offset a brief period of softer demand for print equipment in April and May, amid peak DOGE and tariff-driven uncertainty. And our relentless focus on cost discipline helped preserve adjusting operating income, offsetting the effects of lower than expected sales of print equipment and higher tariff costs. The improved resiliency demonstrated in Q2 provides an affirmation of our strategic direction, the benefits which are expected to be further enhanced through the acquisition of Lexmark.

Our strategic focus this year in anticipation of the close of Lexmark acquisition has been the continued execution of Reinvention, ensuring the full realization of benefits from the ITsavvy and Lexmark acquisition and preserving balance sheet strength. I'll provide a brief update on this quarter's progress in each of these areas.

Starting with the execution of Reinvention. In the second quarter, we advanced a number of Reinvention initiatives aimed at optimizing our commercial offering and simplifying operations, each of which will provide benefits well beyond the Lexmark integration. This quarter, we expanded our inside sales program to cover new territories and product lines, further enabling our direct sales force to concentrate on larger client opportunities. We also reduced the time it takes to process orders at our XBS business unit by four days, improving both time to revenue and client satisfaction. In IT Solutions, we continue to build momentum in the cross-sell of advanced IT offerings in Xerox print client base, an important contributor to this segment's recent strength. And ongoing operational simplification efforts leveraging technology driven efficiencies enabled another double-digit percentage reduction in adjusted organic operating expenses.

We will continue advancing Reinvention initiatives currently in flight and those planned for the future as we progress the phasing of our Reinvention to now include the integration of Lexmark. John will describe the evolution of our Reinvention strategy to incorporate the Lexmark integration in more detail.

Moving to acquisition benefits. The integration of ITsavvy is largely complete and we are ahead of schedule in the realization of the planned strategic and financial benefits associated with that acquisition. The IT Solutions team has embraced the spirit of Reinvention and continuous improvement to find operating synergies beyond those originally contemplated. As an example, Xerox IT Solutions has consolidated the purchase of Xerox Corporation's IT assets, which were previously handled by external partners. The insourcing of Xerox IT spend reduces the cost of Xerox Corporation's IT products and results in an improved status with and higher rebates from IT Solutions' OEM partners.

Moving to Lexmark. The integration of Lexmark is progressing well, aided by the addition of two seasoned Lexmark leaders to the Xerox Executive Committee: Billy Spears, who will lead product development, manufacturing and supply chain for the combined business, and Chuck Butler, who will run the combined Global Business Services organization. Detailed integration planning work had been conducted prior to the acquisition close and is now firmly in execution phase. As we have progressed this work, our confidence in realizing synergies has increased. Accordingly, we now expect cost synergies associated with the Lexmark acquisition to total more than \$250 million from our original estimate of more than \$200 million, all of which remains realizable within the next two years.

Finally, balance sheet strength. The Lexmark acquisition was funded primarily with debt, but results in lower gross debt leverage ratio after accounting for the nearly \$300 million of Lexmark's acquired EBITDA. With the Lexmark acquisition now complete, our top capital allocation priority is the repayment of debt. Following the implementation of cost synergies, which require an upfront cash investment, we expect improved free cash flow from core operations and more than \$600 million of proceeds expected from the reduction of finance receivables between now and the end of 2027 to be deployed to repay debt. This year, we reduced our dividend to place even greater focus on the repayment of debt. We will reevaluate our dividend policy as Xerox gross debt leverage ratio approaches our medium-term target of three times trailing 12-months EBITDA.

Before I hand the call to John, I'd like to put the Lexmark acquisition in context of our broader Reinvention strategy and comment on the improved competitive profile of the combined Xerox and Lexmark businesses. In 2023, we implemented our Reinvention strategy to ensure we are operationally and strategically best positioned to continuously address the evolving workplace needs of our clients. This required reducing or exiting activities and businesses that are not central to our legacy business or development of higher growth, value-add adjacencies such as IT solutions and digital services. Last year, we simplified our business model to enable closer alignment between our businesses and evolving needs of our economic buyer of our workplace solutions. We also established a Global Business Services organization or GBS to centralize key processes and drive continuous operating efficiencies throughout our Reinvention and beyond.

Greater strategic focus and a leaner, more simplified business model freed up the resources and managerial bandwidth to execute and successfully integrate two transformative acquisitions that will contribute to our Reinvention goals of revenue stabilization and a return to double-digit adjusted operating income margins. ITsavvy, which enhances our IT Solutions offering, and Lexmark, which will strengthen and diversify our Print business.

The Lexmark acquisition enhances Xerox position as a leading provider of services-led, software-enabled hybrid workplace solutions. It creates a larger, vertically integrated leader in print and managed print services. And Xerox's portfolio of value added, higher growth adjacencies in IT solutions and digital services provides an important point of competitive differentiation relative to our peers. Combined on a pro forma basis, Xerox generated \$8.6 billion of revenue and more than \$870 million of EBITDA in 2024. Around two-thirds of the revenue comes from recurring sources and more than 10% of the revenue comes from a faster growing IT solutions and digital services businesses.

Xerox is now a top three player in each major print category within its current market, with close to half of the print revenue generated from sales and services associated with A4 devices. A4 is one of the most strategically advantaged parts of the print ecosystem as clients look to refresh their print fleets with smaller, more technology advanced machines. Reinvention is not complete, but the assets and operating model are now firmly in place to achieve our Reinvention goals.

I will now hand over the call to John, who will provide additional context around the strategic advantages of the Lexmark acquisition and an update on Reinvention and our near-term integration priorities.

John G. Bruno

Chief Operating Officer, President & Director, Xerox Holdings Corp.

Thank you, Steve. We are very excited to have closed the Lexmark acquisition and are now in full execution mode with the integration of the two companies. Lexmark strengthens our Print business by adding scale and exposure to faster growing parts of the market like A4 color. These advantages are expected to improve revenue and gross margin in Print, as well as accelerate the growth of our IT and digital solutions businesses.

I'll expand on four specific ways in which the Lexmark acquisition directly benefits our near-term financial outlook on slide 7. Starting with the print market share gains. We expect to leverage the top three position we now hold in all major print categories to expand our share of print related spend with existing and new clients. The overlap between Xerox and Lexmark clients and partners is relatively small, enabling the combined company to sell a broader set of offerings into a larger combined client base, including the 43 Lexmark A4 product configurations that were not previously offered to Xerox clients and partners. We also expect our combined engineering teams to advance the pace of innovation of Lexmark's leading A4 and recently launched A3 platforms. A more diverse and competitive offering is expected to improve win rates, a view that is supported by the positive feedback and excitement we are hearing from clients in just the month since the transaction closed.

Market expansion opportunities in print are expected to contribute to an improved revenue trajectory. We will leverage Lexmark's distribution footprint in the Asia-Pacific region to begin selling Xerox's A3 and high-end products, as well as our suite of software and services where until now we've had no presence. We expect to grow Lexmark's recently launched A3 OEM platform, which addresses a \$12 billion print market.

The Lexmark acquisition also enhances service expansion opportunities. Our print, IT and digital service businesses address stable or growing markets and provide differentiation in a competitive environment. An early focus of our integration efforts will be the standardization and evolution of managed print services. Xerox and Lexmark combined serve approximately 25% of this \$14 billion market. We expect the sharing of best practices and an optimization of our respective service models to result in a combined managed print offering that is more attractive to clients and more profitable to operate.

Beyond print, we'll accelerate our efforts to promote the cross-sell of IT and digital solutions to the combined Xerox and Lexmark client bases. These markets in total are more than 10 times the size of the print market. Cross-sells of IT Solutions to legacy Xerox clients even prior to the acquisition of Lexmark are running ahead of our initial expectations. Year to date, we have generated an IT product and services pipeline of close to \$50 million for more than 80 traditional Xerox print clients. We've barely scratched the surface of this opportunity with IT Solutions penetration of the Xerox print client base currently in the low single digit range. Lexmark adds around 15,000 print clients for our IT Solutions business to target. Most importantly, the Lexmark acquisition provides us with an opportunity to improve profitability with more than \$250 million of identified cost synergies realizable within two years.

Many of the expected synergies will address print product cost enabling improvement in gross margin. Key among the opportunities is the adoption of the Lexmark A3 platform, which reduces our landed product cost for this important segment. We also expect product cost improvements from the transition of Lexmark toner to Xerox technology, which is 30% more cost effective, the integration of Lexmark's more efficient controller technology into Xerox machines and utilization of Lexmark's Mexico facility to optimize global tariff exposure.

I'll now provide an update on Reinvention and its role driving these cost synergies to realization. With the Lexmark acquisition complete, our Reinvention will begin to incorporate the strategic priorities of the combined businesses. The directives of our Reinvention remain in place, and the guiding principles of operating simplification, commercial optimization and growth will continue to influence our approach to the integration of Lexmark. Operational simplification efforts will focus near term on combining our operating capabilities, including our respective global business service functions, consolidating corporate organizations, optimizing labor spend and standardizing technology platforms.

Commercial optimization initiatives address the value proposition and cost to serve of managed print services, the expansion and diversification of Xerox's Print portfolio, and the continued optimization of our regional and channel distribution presence. Product expansion and diversification will be driven by the adoption of Lexmark's A3 technology and the addition of new high-end OEM partnerships, such as the partnership with Kyocera announced today. This partnership provides Xerox with the ability to offer Kyocera's leading cut-sheet inkjet products to our production print clients, strengthening our suite of production print products while ramping Xerox's software and solutions around a more diverse production print ecosystem. As noted in the previous slide, growth initiatives will focus on expanding Xerox's presence in higher growth print markets such as APAC, A4 color and cut-sheet inkjet, as well as the continued expansion of Xerox IT and digital solutions into our client base.

The financial objectives of Reinvention also remain the same, revenue stabilization and return to double-digit adjusted operating income margin. Revenue stabilization will be driven by an improved trajectory in print, supported by stronger Print business post Lexmark and an improved mix of revenue from higher growth businesses. IT services and digital solutions today comprise more than 10% of revenue on a pro forma basis. Over time, we expect these businesses to comprise more than 20% of our revenue.

Revenue stabilization will in turn allow more savings to fall to the bottom line. We continue to expect more than \$700 million of gross cost savings and profit opportunities associated with the Reinvention strategy. When combined with more than \$265 million of Lexmark and ITsavvy acquisition-related synergies, we expect around \$1 billion of savings and profit improvement opportunities to be realized through our Reinvention by 2028, with around half of \$500 million, which have yet to be realized.

Focusing now on Lexmark synergies. The more than \$250 million of gross cost synergies are wide ranging, covering our shared services and global support functions, service delivery, engineering, manufacturing and other organizations. In 2025, we expect to implement synergies with run rate savings of \$100 million to \$125 million, which will result in in-year cash investment of about \$50 million to \$75 million. These initial synergies will be focused on the elimination of duplicative shared service overheads and technology spend. In 2026, the focus of synergies will turn to the optimization of our supply chain, R&D and certain cost and purchasing advantages afforded by larger operating scale. We expect that most of the run rate synergies will be implemented by the end of 2026. And in 2027, we will realize the benefits of a consolidated real estate footprint and IT infrastructure and continue to optimize our managed print delivery structure.

To summarize, the Reinvention through integration has begun. The next phase is expected to strengthen our Print business and drive improved mix of revenue from higher growth businesses, leading to revenue stabilization and a higher flow through of roughly \$500 million of identified cost savings and profit opportunity yet to be realized.

I'll now turn the call over to Mirlanda to discuss this quarter's financial results.

Mirlanda Gecaj

Chief Financial Officer, Xerox Holdings Corp.

Thank you, John. And good morning, everyone. Revenue this quarter was roughly flat year-over-year in actual currency or 1.1% lower in constant currency. Organic core revenue, which excludes ITsavvy and the effects of currency and Reinvention actions, declined around 5% this quarter. This pace of decline was larger than our expectations, reflecting softer print equipment demand in April and May amid peak DOGE and tariff-related uncertainty and to a lesser extent, delays in the sales of OEM supplies due to recently implemented tariffs. Despite these unexpected headwinds, revenue was in line with our guidance due to stronger than expected results at our IT Solutions segment, which benefited from an acceleration in demand and momentum in the cross sale of IT solutions to Xerox print clients.

Turning to profitability. Adjusted gross margin of 29.3% declined around 420 basis points year-over-year. Around 300 basis points of the decline reflected lower financing and other fees associated with the intentional reduction of our finance receivable portfolio and higher product costs. Around 100 basis points of the year-over-year decline was due to the inclusion of ITsavvy, which has a lower gross margin, but similar operating margin profile as the Print business. And nearly 100 basis points of the decline reflected tariff charges net of price related mitigation actions and adverse currency impacts. These effects were partially offset by Reinvention related and other cost reductions.

Adjusted operating margin of 3.7% was 170 basis points lower year-over-year, reflecting lower gross profit and to a lesser extent higher bad debt expense, partially offset by Reinvention savings and other cost reduction efforts, as well as the inclusion of ITsavvy, which carries a lower operating expense base than our Print business. Adjusted operating income of \$59 million was \$4 million below the low end of our Q2 guidance range. Our continued focus on cost control drove operating expenses \$32 million lower year-over-year. Included in operating expenses in the second quarter were \$9 million of Reinvention and transaction related costs and \$14 million of ITsavvy operating expenses. Excluding these costs, operating expenses declined \$55 million, a reduction to our operating expense base of around 12% year-over-year.

Adjusted other expenses net were \$41 million, \$11 million higher year-over-year due primarily to higher net interest expense. Excluded from adjusted other expenses this quarter was \$12 million of net interest expense associated with debt financing that was contingent upon the completion of the Lexmark acquisition. Adjusted tax rate of 528% compared to 25.5% in the same quarter last year. The current year rate reflects an inability to deduct certain losses and expenses, including interest. We continue to assess the impact of the Lexmark acquisition and recent tax flow changes on our effective tax rate for the remainder of the year. We expect the Lexmark acquisition and tax flow changes to contribute favorably to adjusted operating income and adjusted tax rate in future periods.

Adjusted loss per share of \$0.64 was \$0.93 lower than the prior year, primarily due to a higher adjusted tax rate, as well as lower adjusted operating income and higher interest expenses. GAAP loss per share of \$0.87 was \$0.98 lower year-over-year. The increase in GAAP loss reflects a higher tax expense, lower operating income, higher net interest and one-time costs associated with the Lexmark transaction in the current year and insurance proceeds related to a legal settlement in the prior year.

Let me now review segment results. Q2 equipment sales of \$336 million declined 5.6% in actual currency and 6.7% in constant currency. Excluding the effects of Reinvention related actions, equipment sales declined around 3% compared to a decline of around 1% in Q1. The sequential slowdown reflected a period of softer equipment demand in April and May, which was partially offset by a recovery and return to normalized demand conditions in June. Total equipment installations declined 12% due in part to the aforementioned period of demand weakness in the beginning of quarter two and the effects of prior year's Reinvention actions, including geographic and offering simplification.

Entry installations declined 14%, driven in part by a prior year reduction and current year build in backlog for mono devices. Mid-range installations declined 6% as continued strength in sales of the recently launched PrimeLink 9200 series was partially offset by slower demand for other products. Entry and mid-range equipment revenue declined at a slower pace than installations, due to a stronger mix of color devices and the benefits of tariff related price actions. High-end equipment installations and revenue both declined year-over-year, reflecting in part the ongoing evolution of our production print portfolio and high-end offering simplification actions taken last year.

Print post-sale revenue of around \$1 billion declined 9.5% in actual currency and 10.5% in constant currency. Excluding the effect of Reinvention actions, Print post-sale revenue declined around 6% in constant currency. The decline in core print post-sale revenue reflects lower supplies and page volumes offset by growth in digital services. Print segment adjusted gross margin of 31.2% declined 330 basis points year-over-year due to higher product costs, including tariff expenses, lower financing fees, lower managed print volumes and unfavorable equipment channel mix and currency effects, partially offset by Reinvention savings and other cost reduction efforts. Print segment margin of 4.8% declined 240 basis points year-over-year due to lower revenue and gross profit, partially offset by Reinvention savings and other cost controls.

Turning to IT Solutions results. In Q2, IT Solutions revenue and gross profit increased more than 150% year-over-year, reflecting the inclusion of ITsavvy in segment results and strong organic growth from the legacy ITsavvy business. Pro forma for the acquisition of ITsavvy. IT Solutions gross billings, a reflection of business activity, increased 8% year-over-year compared to an increase of 0.4% in Q1. The sequential improvements in billing growth reflect strong PC sale, in part associated with the Windows 11 upgrade cycle and an acceleration in demand for infrastructure and networking products with particular strength in Microsoft Cloud service provider implementations. As Steve and John noted, we're seeing momentum in the cross sale of IT products and services to existing Xerox print clients, which helped contribute to another quarter of double-digit growth in gross bookings, a measure of forward billings.

IT Solutions gross profit grew \$22 million year-over-year. And gross margin of 16.4% expanded 90 basis points compared to the prior year, reflecting the inclusion of ITsavvy. Segment profit grew \$9 million year-over-year due to the inclusion of ITsavvy. Segment profit now reflects the full run rate benefit of annualized synergies.

Let's now review cash flow. Operating cash flow was a use of \$11 million compared to a source of \$123 million in the prior year quarter. The reduction in operating cash flow reflects lower pre-tax cash net income and lower proceeds from finance receivable, partially offset by ongoing improvements in working capital, lower restructuring payments and lower cash taxes. Investing activity was a use of cash of \$18 million compared to a use of \$2 million in the prior year quarter, due primarily to an increase in capital expenditures associated with the implementation of a new enterprise wide technology platform and lower proceeds from the sale of assets.

Financing activity resulted in a source of cash of more than \$600 million, compared to the use of cash in the prior year of \$336 million. Current year financing activity included proceeds from the sale of first and second lien notes, partially offset by the early redemption of a portion of our 2025 notes, the prepayment of a portion of our term loan, and quarterly amortization of other secured debt. Prior year financing activity included the repayment of our 2024 senior unsecured notes and other secured debt payments.

Free cash flow was a use of \$30 million in the second quarter, a \$145 million lower year-over-year. The reduction in free cash flow reflects in part fewer than expected proceeds from the sale of finance receivables due to a delay in the sale of roughly \$100 million of European finance receivables, now expected in quarter three. In the second half of the year, we expect seasonal improvements in adjusted operating income, continued working capital

discipline and benefits from the reduction in finance receivables to drive positive free cash flow. As is typical, we anticipate quarter four to be our seasonally strongest quarter of free cash flow generation. However, as noted, free cash flow in quarter three is expected to benefit from a higher than normal level of finance receivable sales.

Moving to capital structure. We ended Q2 with \$985 million in cash, cash equivalents, and restricted cash, of which around \$500 million reflects proceeds from the sale of second lien notes, which were held in escrow to fund the Lexmark acquisition. Total debt of \$3.9 billion at quarter end increased by more than \$600 million from Q1 levels, due primarily to financing activity associated with the Lexmark acquisition. Around \$1.6 billion of the \$3.9 billion of outstanding debt support our finance assets, resulting in core debt of \$2.3 billion related to the non-financing business.

Adjusted for the Lexmark acquisition, which closed on July 1 and repayment of the August 2025 unsecured notes, total debt was \$4.3 billion and total core debt, which excludes finance and allocated debt, was \$2.7 billion. The Lexmark acquisition increased total debt levels, but resulted in a lower gross debt leverage ratio. On a pro forma basis, gross debt leverage is 5.4 times trailing 12 months EBITDA, more than a half turn lower than our Q1 leverage ratio. Including the more than \$250 million of expected synergies, gross debt leverage would be reduced further to 4.1 times trailing 12 month EBITDA. Our top capital allocation priority remains the reduction of debt, and we continue to target a gross debt leverage ratio of 3 times trailing 12 month EBITDA in the medium term.

Finally, I will address fiscal year 2025 guidance, which now includes Lexmark's expected results beginning July 1. We expect revenue to grow 16% to 17% in constant currency, inclusive of around \$1 billion of Lexmark revenue. As noted, we experienced a recovery in equipment demand in June following a period of softer demand in April and May. While demand conditions are currently stable and expected to remain stable in the absence of further tariff and trade related disruption, our guidance for the second half of the year accounts for a degree of conservatism to reflect the volatile and unpredictable nature of tariff and other government policies.

For the full year, we expect an adjusted operating income margin of around 4.5%, inclusive of \$100 million to \$110 million of adjusted operating income from Lexmark. Lexmark's expected contribution excludes \$10 million to \$15 million of one-time intercompany gross profit eliminations. Relative to prior Xerox only guidance, this updated guidance reflects \$30 million to \$35 million of tariff charges net of mitigation efforts, a delay in the in-year realization of certain Reinvention related gross cost savings, and a more conservative outlook for full year equipment demand, partially offset by a modest amount of Lexmark synergies.

As John noted, our target for Reinvention related growth, cost savings and other profit improvement opportunities remains unchanged at more than \$700 million. However, we expect to realize fewer Reinvention related savings in 2025 than originally expected, as we evaluate the pace and scope of certain Reinvention initiatives relative to Lexmark integration priorities. Any delayed savings in 2025 are timing related and expected to directly benefit adjusted operating income in 2026 or 2027. The high end of the \$30 million to \$35 million range of expected tariff expense net of mitigation efforts reflects tariff rates currently proposed to take effect August 1. The full year tariff impact is larger than previously communicated, due to a brief period of 145% tariffs applied to goods sourced from China, a higher than expected increase in transition costs associated with product move from China to Mexico and a more deliberate rollout of price increases as we await final tariff rates. Assuming rates remain unchanged, we expect to recover the net impact of 2025 tariff expenses in 2026.

Finally, free cash flow is expected to be around \$250 million. The roughly \$125 million reduction in free cash flow relative to the midpoint of prior guidance reflects higher in-year cash tariff expenses and \$50 million to \$75 million of expected cash payments associated with an accelerated implementation of Lexmark synergies. These headwinds are offset by expected improvements in working capital and mild in-year free cash flow accretion from

Lexmark net of incremental interest expense. We continue to aggressively manage working capital to improve the conversion of free cash flow from adjusted operating income.

Free cash flow associated with the Lexmark acquisition is expected to improve in future periods as run rate synergies outpace implementation costs. It is important to note that expected free cash flow in 2025 will be impacted by certain one-time items that are not expected to recur in future years. Current year cash tariff outlays net of mitigation efforts of \$60 million to \$65 million are expected to be recouped over time through future price increases. Synergy implementation costs of \$50 million to \$75 million in 2025 are expected to decline in 2026 and be reduced to less than \$25 million in 2027. And this year, we incurred a roughly \$50 million one-time cash flow headwind associated with changes in inventory ownership terms with a large supplier partner. Excluding the impact of these items, excess pension payments and the expected contribution of finance receivable proceeds, free cash flow conversion from adjusted operating income would approach Xerox's target range of 35% to 40% this year, a range that is expected to be further supported in future periods as adjusted operating income increases and interest expense decreases.

For purposes of modeling results between quarters, in the second half of 2025, we expect stronger than typical seasonal operating income generation in Q4 due to the consolidation of Lexmark, which has a heavier weighting of operating income in Q4 than the legacy Xerox business, and the cumulative benefits of tariff mitigation, Reinvention and synergies savings which are expected to be more heavily weighted to quarter four.

Moving to 2026. To help model results for the combined companies, we are providing preliminary operating expectations for 2026. Starting with revenue. We expect the legacy Xerox Print business to decline at roughly the pace of the broader print market, which we assumed to be low to mid-single digits consistent with recent trends. This expectation reflects the ongoing benefits of various Reinvention related sales productivity and service renewal initiatives, as well as market share growth opportunities afforded by the Lexmark acquisition, offset by a degree of conservatism associated with future integration planning. Lexmark revenue is expected to be relatively flat year-over-year, resulting in another \$950 million of revenue net of intercompany eliminations in 2026. And our IT and digital solution businesses are expected to grow faster than their respective markets as we continue to benefit from growth in the penetration of both types of services within the legacy Xerox Print and now the Lexmark Print client bases. We expect significant year-over-year growth in adjusted operating income resulting from the inclusion of Lexmark, synergy realization, and further Reinvention related savings.

Addressing items that contribute to adjusted operating income, we expect the full year consolidation of Lexmark to add around 50 basis points to 2025 to achieve gross margin in 2026, reflecting Lexmark's gross margin of around 35% excluding intercompany revenue. Adjusted operating income growth is expected to be further supported by at least \$250 million of year-over-year cost reductions from acquisitions synergies, Reinvention savings and ongoing cost discipline.

Moving below operating income. Interest expense is expected to be around \$300 million, reflecting the additional debt used to finance the Lexmark acquisition, offset by the paydown of more than \$200 million of debt in 2026. Further, adjusted tax rate is expected to be around 35% as we benefit from improved adjusted operating income and recent changes in tax policy.

Finally, free cash flow. In 2026, we expect free cash flow to benefit from around \$400 million of cash from the reduction of finance receivables and as noted, better conversion of adjusted operating income to free cash flow, excluding finance receivable benefits.

To conclude, I'm excited to welcome the Lexmark team to Xerox. Lexmark improves our competitive positioning in print and will be an important contributor to Reinvention's financial targets of revenue stabilization and double-digit adjusted operating income margins.

We'll now open the line for Q&A.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] Our first question comes from Ananda Baruah with Loop Capital. You may proceed.

Ananda Baruah

Analyst, Loop Capital Markets LLC

Q

Hey, guys. Yeah, thanks. Good morning and thanks for taking the question. I have probably three, if I could. And thanks for all the great detail. I guess the first one is the June – so you mentioned June, July slowdown. You mentioned it stabilized. And I think you guys mentioned in the prepared remarks that – you mentioned DOGE and tariffs. And so, was there just DOGE related? Was there a meaningful sort of federal component to the softness that you guys had? And then I guess the tariff comment, that sort of speak to that there was broader sort of pricing pressure. You had mentioned tariffs were a little bit more [ph] onerous (00:41:08) than you had anticipated. So do you think it was sort of brand specific pricing that caused it or do you think your customers were just sort of like in wait and see mode, generally speaking, and not related to the pricing? Thanks. And I've got couple of follow-ups. Thanks.

John G. Bruno

Chief Operating Officer, President & Director, Xerox Holdings Corp.

A

That's all right. No problem. It's John. And no, you're spot on. The timing, I just want to be clear, was May, June.

Ananda Baruah

Analyst, Loop Capital Markets LLC

Q

Yeah.

John G. Bruno

Chief Operating Officer, President & Director, Xerox Holdings Corp.

A

And was actually April-May with the June recovery, my apologies. And you're correct in your last component, you have a lot of these environments led and Fed that are dependent upon funding. All right. And so all of those DOGE and DOGE related issues just caused some pause. Nothing has come out as a cancellation. We've seen no cancellations in the pipeline, just the delay.

Ananda Baruah

Analyst, Loop Capital Markets LLC

Q

Got it.

John G. Bruno

Chief Operating Officer, President & Director, Xerox Holdings Corp.

A

And the tariff piece...

Ananda Baruah

Analyst, Loop Capital Markets LLC

That's super helpful.

Q

John G. Bruno

Chief Operating Officer, President & Director, Xerox Holdings Corp.

And the tariff piece for sure. But the tariff piece is not as much as a cost flow through in those particular months as it is an impact of people making decisions as they look at landed cost and the type we had done the same. You can imagine we did the same. When we didn't understand what the destination and the source was on the tariff related products, we had to hold and make some decisions before we let things get shipped to us because we had no idea what we were applying to that actual cost basis. So we wanted to hold until we started getting clarity, and that has been consistent throughout the industry. We've seen and heard that with consistency. That's not unique to us. But those types of things is what gives you the softness in that kind of April, May timeframe, and that's why we saw such a stronger June recovery against both of those related issues.

A

Ananda Baruah

Analyst, Loop Capital Markets LLC

Appreciate that. And then this is more of a clarification, ITsavvy related. On the IT Solutions segment results slide, the ITsavvy impact of 154% constant currency growth, is that against the total revenue growth? I guess, is that to say, John, that the entirety of the growth was ITsavvy related? I'm just trying to foot is sort of what the...

Q

[indiscernible] (00:43:22)

John G. Bruno

Chief Operating Officer, President & Director, Xerox Holdings Corp.

I'm trying to understand the question you – are you saying – because I mean, we had very significant gross billings growing year-over-year in that space. So the answer to question, yes. The IT, the core ITsavvy piece of it and as well as the legacy part of our business combined is what combines to give you that growth. So we saw a strong gross bookings increase and strong gross billings increase against that, and that is against the revenue.

A

Mirlanda Gecaj

Chief Financial Officer, Xerox Holdings Corp.

Yeah, that's correct. Ananda, our – the 150% growth that you see there, it's purely driven to ITsavvy. We do not give guidance for the full IT Solutions segment, but if you were just to look at the legacy IT solution revenue, declined 3%, so the 150% growth came off from ITsavvy including our results in Q2 2025.

A

John G. Bruno

Chief Operating Officer, President & Director, Xerox Holdings Corp.

I will say, though, to add to that and this is why I think this is important, while that is true, that we were – we declined 3%, our legacy gross billings actually grew 13% year-on-year. And that was really due to strong activities in Canada. And that's why we've been trying to focus mostly on our pro forma gross billings and our order activity because that's an indicator of future billings, and both are robust, which is why we provide that number.

A

Mirlanda Gecaj

Chief Financial Officer, Xerox Holdings Corp.

A

That's right. And yeah, and John, gross billings grew actually 8%, which are an indicator of activity [ph] of gross booking (00:44:40) as you said, it's grown even more in Q2 2025.

John G. Bruno

Chief Operating Officer, President & Director, Xerox Holdings Corp.

That's right.

A

Ananda Baruah

Analyst, Loop Capital Markets LLC

Yeah. Thanks for that clarification. That's helpful. And then did I hear accurately that, John, you said mids for ITsavvy, mid-single-digit penetration only into the Xerox customer base...

[indiscernible] (00:45:03)

Q

John G. Bruno

Chief Operating Officer, President & Director, Xerox Holdings Corp.

Low. No, it's actually low. Yeah.

A

Ananda Baruah

Analyst, Loop Capital Markets LLC

Got it.

Q

John G. Bruno

Chief Operating Officer, President & Director, Xerox Holdings Corp.

It's up 5%. That's why we're so encouraged. I mean, we have a – the cross-sell activities have really been embraced by – our investment thesis had always been that our direct sellers across our XBS units would be able to open doors across the thresholds of so many accounts. And they've built a pretty robust pipeline now greater than \$50 million of these types of activities. And we're just seeing the traction we had hoped for. And it's great to see it become realizing it. That's what's driving this growth in the back end.

A

Ananda Baruah

Analyst, Loop Capital Markets LLC

Okay. Great. Thanks. I'll stop there, guys. I appreciate it. Thanks.

Q

John G. Bruno

Chief Operating Officer, President & Director, Xerox Holdings Corp.

No worries.

A

Operator: Thank you. Our next question comes from Erik Woodring with Morgan Stanley. You may proceed.

Maya Neuman

Analyst, Morgan Stanley & Co. LLC

Hi. Awesome. Good morning, everyone. It's Maya on for Erik. I was wondering if you could maybe unpack some of that weakness you saw in April and May broad-based across customer segments or more prevalent in like SMB, for example, and across geographies as well. And then does your full – I understand some conservatism

Q

baked into the back half of the year with your updated outlook. Does that assume demand remains stable and doesn't improve from the end of June or does that take into account an incremental softness in demand from where you exited the quarter?

John G. Bruno

Chief Operating Officer, President & Director, Xerox Holdings Corp.

A

Well, I'll start with it's a little bit choppy, but it's more – enterprise was relatively stable. We saw more of Fed and SLED accounts is where we saw more of the pressure inside the business. And what we really focused on is our installations. A lot of this is changes between quarters and some sequential slowdowns. But when I look at it between our entry products and our mid products, the entry products is really changes in our backlog where our mid declines was really just that softness in April and May. But that was offset as Mirlanda pointed out with very strong growth in our PrimeLink installs, which was 30% plus. So we expect to at least hold our share in the market in future periods and in the high end declines which is self-inflicted. These are the ones that we did on purpose basically, and reflecting the areas of our print product portfolio in the places in which we exited. So we intentionally exit certain segments to reintroduce ourselves back into these segments with the right products.

So that's why the Kyocera – this Kyocera announcement this morning was so important because this cut-sheet inkjet part of production, we wanted to shrink the production portfolio down on products that were declining with higher cost to make ourselves available to go after. And if you look at the market data there, cut-sheet inkjet is about greater than 13% on a compounded annual growth rate forecasted by external analysts between 2025 and 2030. So you take that product and our free flow, our finishing, our remote services, branding and you add that in stabilizing mid, this is why the bookends of this strategy we've talked about so much is critically important in A4 color and, of course, cut-sheet inkjet on the high end of production. So that's kind of the chopiness that we saw through there, both market and product.

Mirlanda Gecaj

Chief Financial Officer, Xerox Holdings Corp.

A

Yeah. But Maya, also to add to John's, right, you clearly pointed out and we mentioned in our prepared remarks, our guidance for the rest of the year has some conservatism on it, right? We saw that softness and we build that into our equipment demand for the rest of the year.

Maya Neuman

Analyst, Morgan Stanley & Co. LLC

Q

Got it. So it's more so on the equipment side is where that...

Mirlanda Gecaj

Chief Financial Officer, Xerox Holdings Corp.

A

Yeah.

Maya Neuman

Analyst, Morgan Stanley & Co. LLC

Q

...incremental conservatism...

[indiscernible] (00:48:40)

Mirlanda Gecaj

Chief Financial Officer, Xerox Holdings Corp.

That's correct.

A

Maya Neuman

Analyst, Morgan Stanley & Co. LLC

Great. Thank you. And then just one last one from me. Apologies if I missed it, but can you remind me, did you guys actually end up implementing price increases over the quarter? I know you guys talked about doing so at earnings last quarter. And if so, were they just for specific products in the US market or is it across the board globally? And what are you hearing from customers on even the potential future price increases?

Q

John G. Bruno

Chief Operating Officer, President & Director, Xerox Holdings Corp.

Well, we were very consistent with our price increases. And, yes, we did implement them to partially offset some of the tariff-related issues as we came into the period. And there's lots of discussions in the industry whether we could apply a tariff surcharge or whether we had to take in price. And you know of the headwinds with regard to potential calling out tariff surcharges. And so we followed suit with price increases in the places in which we could. We had some pushback in the areas of contractual price increases, as you'd imagine, from customers in our post-sale environments. But on our equipment part of our revenue, we apply them as judiciously as we can, and we're going to continue to do that as we go through the period, because we could not adjust the headwind with price increases in the period. That's going to take time to recover. That's going to take us out of 2025 and into 2026, which is precisely why we've provided the guidance there and what we did, because these are the pressures on the operating income. It really comes down to the timing of which we can gain price increases, the tariff related impact of the slowdowns, et cetera, and some of the intentional things that we did. But fundamentally, we have applied those price increases and we have been able to pull them through from an equipment and a transactional revenue perspective.

A

Maya Neuman

Analyst, Morgan Stanley & Co. LLC

Got it. Thank you so much.

Q

Operator: Thank you. Our next question comes from Samik Chatterjee with JPMorgan. You may proceed.

Priyanka Thapa

Analyst, JPMorgan Securities LLC

Hi. This is Priyanka Thapa on for Samik Chatterjee. Got a couple questions on Lexmark. One of them is why is the outlook for Lexmark's revenue in 2026 expected to be flat when they're exposed to growth markets and at east stronger growth markets than legacy Xerox print?

Q

Mirlanda Gecaj

Chief Financial Officer, Xerox Holdings Corp.

Yeah. I could answer that. So from a Lexmark perspective, our expectation of Lexmark being flat, that is better than the industry, which we expect it's reducing by 3%. What drives that is Lexmark is very well positioned in the A4 market, which is an area that is growing to say the least. 80% of their revenue is basically annuity based and gives them an upper hand as it relates to the print market in 2025 and going forward.

A

Priyanka Thapa

Analyst, JPMorgan Securities LLC

Q

All right. And what is the driver of operating margins declining to 4.5% for the full year in 2025 versus 5% before?

Mirlanda Gecaj

Chief Financial Officer, Xerox Holdings Corp.

A

Yeah. So let me unpack a little bit of the operating margin for 2025. When we start with the revenue, we are talking about revenue in 2025 growing 16% to 17%, which kind of includes \$1 billion of Lexmark revenue. What that means is, if we were to go back now to the Xerox legacy, that anticipates roughly 150 basis point lower than prior guidance, which, as we mentioned previously, has a degree of conservatism in the equipment outlook, given the demand softness that we saw in April and May. Also, want to remind again that our full year Xerox legacy guidance includes 400 basis points of headwind from the Reinvention initiatives that we took in the prior year and are flowing through in 2025. As a result, yeah, our implied core revenue will be in a range of Xerox 3% to 4%, a slight improvement from the prior year 4% declined. And we expect to continue to improve that Xerox legacy revenue trajectory driven by market share gains, growth in digital and legacy IT Solutions.

So with that, that has an impact into our 2025 gross and adjusted profit margin. 4.5% in 2025 in relation to the adjusted profit is driven by mainly this decline in top line revenue. Our gross margin is expected to be between 29% and 30%. And the tariffs, right, when we think about sort of the biggest drivers, tariffs is expected to impact our adjusted operating margins, \$30 million to \$35 million, and that is net of our initiatives. That is higher than we initially had discussed in Q1 related to some of our products coming in from China at 145% tariffs. Some of them slipped through. We have higher cost expected for moving our supply chain from China to Mexico as well as, as we're going through our price increase as John mentioned, we're being very balanced in passing those price increases to the customers.

Two-thirds of the decline on the operating profit margin. So one-third, let's say tariffs. One-third would be our slowdown and intentional delays into our Reinvention actions. As we are preparing to integrate and preparing for the synergies with Lexmark, we intentionally are reviewing certain Reinvention initiatives. And so those will get pushed to 2026 and 2027. And then a piece of it was related to our demand softness macro and some of the conservatism that I mentioned we're building into the equipment sales and revenue top line for the rest of 2025.

Priyanka Thapa

Analyst, JPMorgan Securities LLC

Q

That was very helpful. Thank you.

Operator: Thank you. I would now like to turn the call back over to Mr. Bandrowczak for any closing remarks.

Steven John Bandrowczak

Chief Executive Officer & Director, Xerox Holdings Corp.

Thank you, everybody. Recapping today's call, the addition of Lexmark advances our Reinvention by strengthening our Print businesses. A stronger Print business improves Xerox revenue trajectory, and provides the platform from which we can accelerate the growth of IT Solutions and our portfolio of digital services offered as demonstrated this quarter, leading to revenue stabilization. And revenue stabilization is key to realizing the value of our roughly \$500 million of identified gross savings in operating income. And we target a return of double-digit adjusted operating income and substantially higher free cash flow generation.

Thank you, everybody, and have a great day.

Operator: Thank you. This concludes the conference. Thank you for your participation. You may now disconnect.

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