



# Xerox Corporation (XRX)

Updated January 27<sup>th</sup>, 2024, by Josh Arnold

## Key Metrics

<b>Current Price:</b>	\$19	<b>5 Year CAGR Estimate:</b>	6.0%	<b>Market Cap:</b>	\$2.4 B
<b>Fair Value Price:</b>	\$18	<b>5 Year Growth Estimate:</b>	3.0%	<b>Ex-Dividend Date:</b>	03/28/24 <sup>1</sup>
<b>% Fair Value:</b>	108%	<b>5 Year Valuation Multiple Estimate:</b>	-1.5%	<b>Dividend Payment Date:</b>	04/30/24
<b>Dividend Yield:</b>	5.3%	<b>5 Year Price Target</b>	\$20	<b>Years Of Dividend Growth:</b>	0
<b>Dividend Risk Score:</b>	D	<b>Retirement Suitability Score:</b>	C	<b>Rating:</b>	Hold

## Overview & Current Events

Xerox Corporation traces its lineage back to 1906 when The Haloid Photographic Company began manufacturing photographic paper and equipment. Through a series of mergers and spinoffs, the Xerox we know today was formed. Xerox spun off its business processing unit in 2017 (now called Conduent) and now focuses on design, development, and sales of document management systems. The company produces less than \$7 billion in annual revenue and has a market capitalization of \$2.4 billion.

Xerox posted fourth quarter and full-year earnings on January 25<sup>th</sup>, 2024, and results were worse than expected on both the top and bottom lines. Adjusted earnings-per-share came to 43 cents, which was 13 cents light of estimates. Revenue was off 9.1% year-over-year to \$1.77 billion, and missed estimates by \$40 million. In constant currency, revenue was down 10.6%.

Adjusted net income was \$56 million, down from \$90 million a year ago. Adjusted operating margin was 5.4% of revenue, which was down 380 basis points year-over-year. Operating cash flow came to \$389 million, more than double from the year-ago period. Free cash flow also more than doubled to \$379 million.

The company has announced plans to reduce its workforce by 15% this year in order to right size for its lower revenue run rate. As a part of the program, Xerox is targeting \$300 million in operating income over last year's level.

The company was able to reduce its share count by more than 20% in 2023 through aggressive share repurchases, which has helped more than offset fundamental weakness in the business from an earnings-per-share perspective.

## Growth on a Per-Share Basis

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029
<b>EPS</b>	\$3.84	\$3.20	\$2.32	\$3.48	\$3.46	\$3.55	\$1.41	\$1.51	\$1.12	\$1.82	<b>\$2.20</b>	<b>\$2.55</b>
<b>DPS</b>	\$0.98	\$1.09	\$1.25	\$1.00	\$1.00	\$1.00	\$1.00	\$1.00	\$1.00	\$1.00	<b>\$1.00</b>	<b>\$1.00</b>
<b>Shares<sup>2</sup></b>	279	253	254	255	230	213	198	159	156	123	<b>115</b>	<b>90</b>

Xerox has had a difficult time growing revenue and profits and we do not see that changing moving forward. Given that the new base of earnings for 2024 is \$2.20 per share, we expect 3% growth moving forward. We see the restructuring program as a net positive for the stock given Xerox continues to see revenue and guidance weakness. In addition, rapidly improving free cash flow should help continue to reduce the float.

We think the revenue and margin outlooks for Xerox look much better than they have in the recent past, and its buyback program should be able to help alleviate some of the burden when it comes to growth, provided free cash flow recovers as planned; it certainly appears that it will given recent guidance.

The dividend is \$1.00 per share today and we do not forecast any increases coming anytime soon. The dividend was cut after the Conduent spinoff in 2017 and given the above, we do not see management taking the risk of a higher dividend, particularly given the yield is currently in excess of 5%.

<sup>1</sup> Estimated date

<sup>2</sup> Share count in millions

Disclosure: This analyst has no position in the security discussed in this research report, and no plans to initiate one in the next 72 hours.



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## Valuation Analysis

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	Now	2029
Avg. P/E	13.0	14.3	16.8	8.5	8.0	9.0	15.5	15.1	13.0	10.1	8.6	8.0
Avg. Yld.	2.0%	2.4%	3.2%	3.4%	3.6%	3.1%	4.6%	4.4%	6.8%	5.5%	5.3%	4.9%

Xerox's average price-to-earnings ratio in the past decade has been ~11, but we estimate fair value at 8 times earnings given continued revenue weakness and volatile margins. That is ahead of the 8.6 times earnings the stock trades for today, implying a sizable tailwind to annual total returns should the valuation normalize over the next five years. We expect the stagnant dividend and higher valuation to produce a yield around 4.9% in the future and note that the 5.3% yield today is still high. The guidance for 2024 free cash flow suggests dividend safety concerns are no longer an issue, and in fact, that the company can pay the dividend and deleverage quite easily while buying back shares.

## Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029
Payout	26%	34%	54%	29%	29%	28%	71%	66%	89%	55%	46%	39%

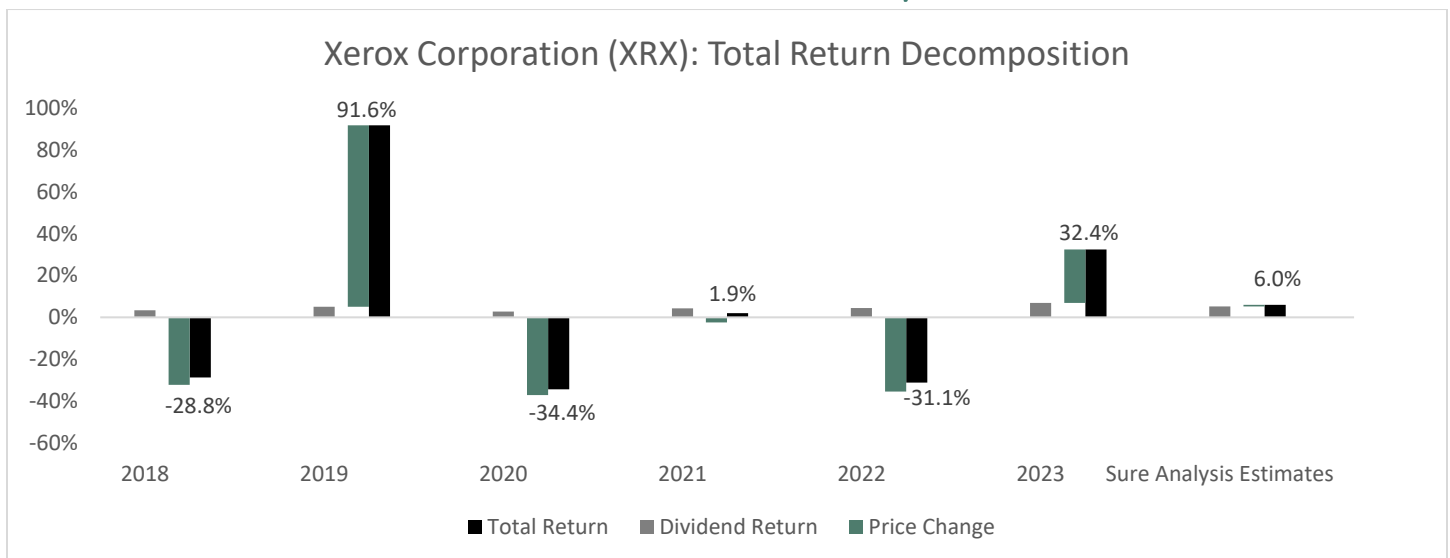
The payout ratio is 46% of earnings now that estimates are higher for 2024. Xerox hasn't said it plans to cut the dividend, and we believe it's sustainable at the current level. We continue to think that Xerox will have a difficult time raising the payout anytime soon given relative earnings weakness, but deleveraging and share repurchases have taken precedence in recent years anyway.

Xerox suffered immensely from the COVID recession, but is showing signs of improvement. Its competitive advantage is in its pure-play focus on document management systems and its very long history in the industry. In addition, it has a highly diversified, global customer base.

## Final Thoughts & Recommendation

In total, we forecast Xerox producing 6% annual total returns in the coming years, which is lower than our last update. The yield will contribute 5.3%, but growth could be modest, and could be reduced by a 1.5% valuation headwind. The stock is now overvalued in our view with a sizable yield, and the earnings picture is improving. We have moved our rating from buy to hold after 2023 results.

## Total Return Breakdown by Year



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## Income Statement Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
<b>Revenue</b>	12,679	11,465	10,771	9,991	9,662	9,066	7,022	7,038	7,107	6,886
<b>Gross Profit</b>	5,110	4,582	4,305	4,071	3,869	3,650	2,626	2,403	2,318	2,314
<b>Gross Margin</b>	40.3%	40.0%	40.0%	40.7%	40.0%	40.3%	37.4%	34.1%	32.6%	33.6%
<b>SG&amp;A Exp.</b>	3,133	2,865	2,636	2,514	2,379	2,085	1,851	1,718	1,760	1,696
<b>D&amp;A Exp.</b>	639	590	563	527	526	430	368	327	270	251
<b>Operating Profit</b>	1,381	1,146	1,148	1,080	1,045	1,147	417	320	212	346
<b>Op. Margin</b>	10.9%	10.0%	10.7%	10.8%	10.8%	12.7%	5.9%	4.5%	3.0%	5.0%
<b>Net Profit</b>	1,013	448	(471)	195	361	1,353	192	(455)	(322)	1
<b>Net Margin</b>	8.0%	3.9%	-4.4%	2.0%	3.7%	14.9%	2.7%	-6.5%	-4.5%	0.0%
<b>Free Cash Flow</b>	1,887	1,463	660	(372)	1,050	1,268	474	561	102	649
<b>Income Tax</b>	198	193	62	468	247	179	64	(17)	(3)	(29)

## Balance Sheet Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
<b>Total Assets</b>	27,658	25,541	18,051	15,946	14,874	15,047	14,741	13,223	11,543	10,023
<b>Cash &amp; Equivalents</b>	1,411	1,228	2,223	1,293	1,081	2,740	2,625	1,840	1,045	519
<b>Acc. Receivable</b>	2,531	838	741	1,160	1,097	1,091	834	912	2,011	1,763
<b>Inventories</b>	934	901	841	915	829	694	843	696	797	661
<b>Goodwill &amp; Int.</b>	11,577	4,291	4,077	4,407	4,232	4,221	4,426	3,498	3,028	2,924
<b>Total Liabilities</b>	16,556	16,075	13,090	10,439	9,621	9,239	8,931	8,556	8,180	7,465
<b>Accounts Payable</b>	1,584	1,342	1,126	1,108	1,073	1,053	983	1,069	1,331	1,044
<b>Long-Term Debt</b>	7,741	7,279	6,316	5,517	5,230	4,282	4,444	4,246	3,726	3,277
<b>Total Equity</b>	10,678	9,074	4,709	5,256	5,005	5,587	5,592	4,436	3,343	2,538
<b>LTD/E Ratio</b>	0.70	0.77	1.28	1.01	1.00	0.74	0.77	0.91	1.11	1.29

## Profitability & Per Share Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
<b>Return on Assets</b>	3.6%	1.7%	-2.2%	1.1%	2.3%	9.0%	1.3%	-3.3%	-2.6%	0.01%
<b>Return on Equity</b>	8.8%	4.5%	-6.8%	3.9%	7.0%	25.5%	3.4%	-9.1%	-8.3%	0.03%
<b>ROIC</b>	5.1%	2.5%	-3.4%	1.7%	3.4%	13.2%	1.9%	-4.7%	-4.0%	0.02%
<b>Shares Out.</b>	279	253	254	255	230	213	198	159	156	149
<b>Revenue/Share</b>	43.29	42.61	42.08	38.94	38.39	38.88	33.21	38.42	45.56	46.18
<b>FCF/Share</b>	6.44	5.44	2.58	(1.45)	4.17	5.44	2.24	3.06	0.65	4.35

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.

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