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NCR - Q4 2014 NCR Corp Earnings Call

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OVERVIEW:

Co. reported 4Q14 non-GAAP EPS of $0.88. Expects full-year 2015 reported revenue to be roughly flat and non-GAAP diluted EPS to be approx. $2.60-2.80. Expects 1Q15 revenue to be roughly flat with prior-year.

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PRESENTATION

Operator

Good day, and welcome to the NCR Corporation Fourth Quarter FY14 Earnings Conference Call.

Today's conference is being recorded.

At this time, I would like to turn the conference over to Gavin Bell, Vice President of Investor Relations. Please go ahead.

Gavin Bell - *NCR Corporation - VP of IR*

Good afternoon and thank you for joining our fourth quarter 2014 earnings call. Joining me on the call today and offering opening remarks are Bill Nuti, Chairman and Chief Executive Officer, and Bob Fishman, Chief Financial Officer. Additionally, available on the call today for Q&A are Andy Heyman, Senior Vice President and President Financial Services, Michael Bayer, Senior Vice President and President Retail Solutions, and Paul Langenbahn, Senior Vice President and President of Hospitality.

Our presentations and discussions today include forecasts and statements that are considered forward-looking statements, as defined in the Private Securities Litigation Reform Act of 1995. While these statements reflect our current outlook, expectations, and beliefs, they are subject to a number of risks and uncertainties that could cause actual results to vary materially.

These risks and uncertainties are described in our earnings release and in our periodic filings with the SEC, including our annual report to stockholders. On today's call, we will be referring to presentation materials posted on our website. We will also be discussing certain non-GAAP financial information, such as free cash flow and results excluding the impact of pension and other items.

Reconciliation of these non-GAAP financial measures to their most directly comparable GAAP measures and other information concerning such measures are included in the presentation materials and in our earnings release. These are also available on the Investor Relations section of NCR's website. A replay of the call will be available later today on our website, NCR.com.

With that, I'd like to turn the call over to Bill Nuti.

Bill Nuti - *NCR Corporation - Chairman & CEO*

Thanks, Gavin. Good afternoon, everyone, and thanks for joining us today.

Our Q4 and full-year results came in within or above our updated guidance from our Q3 call. However, while Q4 was consistent with our internal expectations, 2014 was a challenging year, primarily as a result of retail end market challenges and FX headwinds, and while we navigated through these issues, we were disappointed with not being able to achieve our initial 2014 guidance.

That said, 2014 was also a year of several accomplishments. Financial Services met or exceeded our internal expectations, made meaningful progress in strategic transformation, and continued to gain market share in physical and digital channels.

Our software and cloud businesses experienced significant growth, which allowed us to drive meaningful margin expansion and our services business further pulled away from our competition with improved delivery. We also successfully integrated digital insight, while simultaneously meeting our business plan and upgrading our digital and site cloud infrastructure to provide reliable service on a scalable, secure platform.

While Retail Solutions missed their internal operating income plan by over $100 million, we increased our leadership position in the burgeoning omni-channel software segment. NCR remains positioned at the forefront of consumer transaction technologies and are securely connecting consumers and businesses in more channels and more ways than ever before.

Our global leadership is evidenced by the nearly 550 million transactions we enable around the world each day; of which, now over 20 million are digital transactions and mainly mobile in nature. Today, I'm going to review Q4 and the full-year results, as well as discuss a few areas where NCR made progress in 2014. I'll also speak to 2015 and some of the things we are focused on in the year ahead.

Starting on slide number 3, which summarizes our results for Q4, revenues were up 6% as reported, up 11% on a constant currency basis, and up 5% on an organic constant currency basis. FX headwinds in Q4 negatively impacted revenue by approximately $75 million year-over-year. Revenue growth was driven by Financial Services, as well as software-related revenues.

Our increase in higher margin software revenues drove operational gross margin expansion of 120 basis points to 30.2% in Q4. Operational gross margin was up 10 basis points, excluding Digital Insight. NPOI was $251 million for the fourth quarter, up 14% and non-GAAP EPS was $0.88, up 6% year-over-year. Excluding Digital Insight, NPOI was up 1%.

You can see we also faced FX headwinds in NPOI and EPS during the fourth quarter. Our free cash flow in Q4 was $229 million, which was down year-over-year, but as you'll see on the next slide, higher for the full year.

Slide number 4 shows our results for the full year. Revenues were up 8% as reported, up 10% constant currency, with FX headwinds of approximately $120 million year-over-year. Full-year revenue was up 4% on an organic constant currency basis.

Revenue for the full year was driven mostly by Financial Services, which had a solid year, as well as by growth in software and cloud. Recurring revenues reached 41% of total revenues, which remains an important area of focus for us. Operational gross margin was 29.5% in 2014, an improvement of 100 basis points year-over-year. Excluding Digital Insight, operational gross margin was down 30 basis points.

We generated $820 million in NPOI in 2014, up 14% year-on-year and flat excluding Digital Insight. Non-GAAP EPS was down 2% year-over-year. Organic operational gross margin and NPOI, as well as non-GAAP EPS, were negatively impacted by a challenging retail end market and significant

FX headwinds. Lastly, free cash flow was $313 million in 2014, up $106 million from the prior year, primarily as a result of improved working capital management and $45 million of higher recoveries related to Fox River.

As many of you know, driving increased free cash flow is a major priority of ours. Despite lower-than-expected NPOI, we made progress against that goal this year. Bob will give you more color on that in a few minutes, as well as some insights into our goals for 2015.

Turning now to slide number 5, I'd like to update you on our software-related revenue growth. Q4 software-related revenue was $477 million, up 32% compared to last year and up 8% excluding Digital Insight. Q4 cloud revenue was up 231% in total and up a solid 15% excluding Digital Insight, driven by cloud growth in Hospitality.

For the year, software-related revenues reached $1.75 billion, up 38% year-on-year and up 12% excluding Digital Insight. Cloud revenues for 2014 were up 239% overall and up 15% excluding Digital Insight; again, primarily driven by cloud growth in Hospitality.

As you know, one of our key strategic goals is to increase software-related revenue, particularly cloud, as a percentage of our total revenue. Doing so has a positive impact on higher margin recurring revenue streams, as well as generating improved cash flow. This will continue to be an area of long-term focus.

Turning now to slide number 6, where we can see the multi-year impact our software strategy has had on operational gross margin, which reached 29.5% in 2014. This translates to a 600 basis point improvement compared to 2010. We expect software-related revenue in 2015 will continue to grow at a faster rate than overall revenue, including hardware and other services, thus improving our revenue mix, and a driving gross margin rate expansion.

Slide number 7 shows some of the accomplishments of the NCR team in 2014. First, Financial Services' business performance and transformation, our Financial Services business achieved solid growth, both organically and with Digital Insight. Financial Services gained markets share in strategic segments like smaller financial institutions, improved margins both organically and inorganically via high growth in software and cloud, and transformed our value proposition in retail banking. NCR's customer experience software platform, otherwise known as CXP, is rapidly becoming the secured multi-channel software architecture of choice for banks around the world.

Software and cloud growth continues to give us confidence in improved margins long-term, higher margin recurring revenues and a competitive advantage in the growing omni-channel, omni-commerce software segment. In fact, NCR is now one of the top 100 software companies in the world, according to PWC Global 100 Software Leaders. This is a great accomplishment given just five years ago, software was a very small percentage of our overall business.

Where we are now with software is in part addition of Digital Insight. As many of you recall, we closed on the purchase of Digital Insight a little over a year ago. The addition of Digital Insight transformed our Financial Services business and gives us what we believe is the most comprehensive end-to-end solution for banking across physical and digital channels.

The business delivered solid results in 2014 and we are pleased with the customer's response to our strategy, revenue synergies in the small, mid-sized bank segment, and the traction of our mobile offers. I'm also pleased with the consistent progress made internally to integrate Digital Insight's technology and our people into NCR.

We also took additional steps in 2014 to address our pension exposure. The Phase 3 initiatives we've implemented this year included a retiree lump sum offer and a group annuity purchase. As a result, we reduced our overall pension liabilities and future mandatory cash contributions.

We also made significant progress on Fox River this past fall, including favorable rulings that overturned not only the decision holding us 100% liable, but also the injunction that required us to do the cleanup work.

We also collected $106 million against our API box obligation. Similar to our progress on pension, these developments reduce our risk and improve our overall cash flow. On slide number 8, I'll wrap up by talking about 2015 and some of the key areas we're focused on in the year ahead.

Those of you that follow NCR know a major theme here has been innovation. I believe it is at the heart of everything we do and is key to our ability to consistently deliver value to our customers and empower them for success as consumer preferences evolve on how they connect, interact, and transact with business. Innovation will remain core to what we do in the year ahead, as we take the next steps in our transformation.

The further expansion of our software and cloud revenues continues to be a key area of focus for NCR in 2015. Whether it is advancing our branch transformation solutions or our mobile offerings for retail and hospitality, we will become a more relevant software partner for our customers and enable them to provide the experiences and the transaction capabilities that today's consumers demand. We're also going to advance our strategy of strengthening NCR as a company.

In the year ahead, a major goal of ours is to transform key areas of our Business, most notably, sales and service. The goal of this effort is simple: to be the highest performing sales force we can be complemented by expanded service offers and unmatched service delivery.

Looking at our sales organization, our goal is to continue evolving our sales force into a more software-driven, hardware-enabled, solutions-oriented team. It remains our goal to build a sales organization that is feared by the competition and valued as a trusted advisor by our customers.

Our services transformation really comes down to the innovation of new, higher margin, value added offers complemented by a more productive and efficient service delivery organization. The redesign of our sales and services go to market is meant to complement the dramatic changes in our revenue streams, products, and solutions.

To wrap up, we are happy 2014 is behind us and excited about the coming year and the opportunities ahead for NCR. We're focused on executing our strategic plan to strengthen the value we provide to our customers and position NCR for growth over the long term.

Now, I'd like to turn over the call to Bob to review our performance by line of business and our financials. Bob?

Bob Fishman - *NCR Corporation - CFO*

Thank you, Bill.

I'll start on slide 9, which shows our Q4 and full-year operational results. We have included full-year results on the slides so you will have the information in one source, but I will focus the commentary on Q4 results. Revenue growth for Q4 is up 6% as reported, up 11% on a constant currency basis, and up 5% on a constant currency basis excluding Digital Insight.

As Bill mentioned, the operational gross margin rate was 30.2%, driven by more software-related revenue in the mix. Expenses were slightly higher than the prior year at 16% of revenue. NPOI margin was a 14.2%, up 100 basis points over prior year. EPS was $0.88, up from prior year, despite unfavorable foreign currency fluctuations of approximately $13 million, which roughly $6 million in NPOI and $7 million in interest and other expense.

The effective tax rate in the quarter was 20% and for the year, was 22%. The annual cash tax rate in 2014 was 12%, lower than the effective tax rate, which helps our free cash flow.

The next slide shows our Q4 and full-year GAAP results. The decrease in GAAP results is primarily related to the restructuring plan and pension expense. The restructuring plan charge included in income from operations was $33 million in Q4 2014 and $160 million in full year 2014.

Pension expense was $150 million in Q4 2014, primarily driven by a mark-to-market charge due to the update in the US mortality table. Pension benefit was $99 million in Q4 2013, due to higher discount rates. The $150 million charge in Q4 was non-cash. We have significantly reduced our mandatory pension contributions in future years, which you'll see on slide 23.

Slide 11 is an update on the restructuring plan. As a reminder, we have included at the key initiatives of the plan on this slide. As far as progress to date, we expect the total charge to be approximately $200 million to $225 million with $163 million in 2014. The cash impact is expected to be approximately $100 million to $115 million with $29 million in 2014. As far as savings generated, we estimate approximately $18 million in 2014, $70 million in 2015, and $105 million in 2016.

As previously communicated, we expect approximately 50% of the savings to benefit NPOI, with the remainder reinvested in the business. Additional details on the 2014 P&L charge is included in the non-GAAP reconciliations on slides 32 and 33.

Slide 12 shows of the revenue by segment. As you can see, FX had a significant impact in the quarter. Financial Services was up 20% on a constant currency basis, 9% excluding Digital Insight, which represented very solid organic growth, and Retail Solutions was up 2% on a constant currency basis. Overall revenue was up 5% on an organic constant currency basis. For the full year, Financial Services grew 6% on an organic constant currency basis.

Slide 13 shows the operating margin by segment. Full-year results in three of the businesses were less than we expected when we started the year. Retail Solutions suffered from challenging markets, Hospitality saw weakness in certain global quick service restaurants, and Emerging Industries saw some cost challenges.

Q4 did show some recovery for each of the businesses. Financial Services grew operating margin significantly, both with and without the contribution of Digital Insight. Financial Services full-year operating margin was up 230 basis points, excluding Digital Insight. This was driven by having significantly more software-related revenue in the mix. I will cover segment results in more detail on the next few slides.

On slide 14, you'll see our Financial Services update. On a constant currency basis, revenues were up 9% excluding Digital Insight. Operating income grew 43%, with 55% from Digital Insight and 45% from the core business. Operating margin expansion, excluding Digital Insight, was driven by growth in software and branch transformation and was up 210 basis points.

Excluding Digital Insight, orders were down 11% and backlog was up 1%, as a result of foreign currency fluctuations and challenges in certain countries like Russia and China. As the business continues to transform through more software and services, orders and backlog does not capture all of our revenue streams and therefore, are not the best predictor of future revenue. We are developing a more comprehensive measure that will include services in cloud and plan to share that with you later in the year.

Looking at Digital Insights results, which continue to perform ahead of expectations, Q4 revenues were $93 million and Q4 operating income was $27 million. Our integration plan is on track and our cross-selling program is delivering great results. Our mobile active users finished the quarter at $6.8 million, up 33%.

In summary, Financial Services delivered solid results in 2014, with improved linearity in North America. We believe the combination of NCR and Digital Insight creates a great platform for our customers.

The next slide shows our Retail Solutions Q4 results. Revenue and operating income were down as expected, impacted by redirected IT spend and delays in customer rollouts. Revenue was down 2%, but up 2% on a constant currency basis. Operating margin was 8.9%, which increased 400 basis points from Q3 2014 and was close to the operating margin from Q2 2014.

As expected, orders were down in the quarter, driven by challenges in Tier 1 hardware, offset by software-related growth in North America. Backlog, after adjusting for the cancellation of a customer order in Q4, is down 6% going into the year, due to delays in customer rollouts. While we continue to experience a challenging retail market, Q4 showed some positive signs.

In Q4, we saw continued solid demand for our omni-channel solution. We also experienced strong year-on-year growth in professional services and software maintenance. Additionally, self check out revenue went up 5% in the quarter compared to the prior year.

Turning to the next slide, Hospitality revenues were down slightly by 2%, due to decreased spend by certain global quick service restaurants. However, the higher margin revenue streams were up significantly. Software-related revenues were up 17%, which includes cloud revenues up 19%. Additionally, cloud applications sites increased 16%.

Operating margin performance was 16.9%, up 210 basis points due to this favorable mix of revenues. Our growth in software-related revenue is increasing wallet share with our existing customers through implementation of digital signage, back office, and consumer engagement solutions and services. Our engage platform, which enables restaurant operators to leverage ordering, payment, loyalty, and feedback in one seamless, connected, consumer-driven experience, continues to grow, surpassing 40,000 total application sites and 6,000 online ordering sites.

Next, looking at our Emerging Industries business on slide 17, revenues were $102 million, down 4% year-over-year. Telecom and technology revenues, which make up approximately 2/3 of this business, were flat. Operating income and operating margin continue to be negatively impacted by costs associated with managed service contracts in our telecom and technology business, as well as further investments made in our small business offerings; however, margins did improve significantly versus earlier quarters in 2014.

In telecom, the technology, we had base expansion wins in new portfolios, advanced and managed services, and launched a strategic partnership to deliver a next generation security solution. In our travel business, we delivered a record 37 million mobile airline boarding passes in Q4, up 185% year-on-year.

On slide 18, you can see the solid growth in cloud professional services and total software-related revenue. On an as-reported basis cloud was up at 231% and up 15% excluding Digital Insight. Software-related revenues grew 32% and 8% excluding Digital Insight.

Other services, which as a reminder, includes our traditional break fix business, was down by 3% as reported, up 1% on a constant currency basis and hardware revenue was flat as reported, up 5% on a constant currency basis. For the full-year, software-related revenue was up 38%, hardware was down 1%, and other services were up 1%.

On slide 19, you can see free cash flow for the quarter and year-to-date. Free cash flow for Q4 2014 was $229 million compared to free cash flow of $317 million in the prior quarter. The decrease was mainly due to changes in working capital, restructuring spend, and the timing of cash outflows related to discontinued operation.

We ended the year with free cash flow of $313 million compared to $207 million in the prior year. This was above our revised guidance of $225 million to $275 million, mainly driven by reduced spending relating to the restructuring plan, which will shift into 2015, as well as improvements in working capital. Discretionary pension contributions were $48 million in 2014. These reduced future mandatory contributions and improved free cash flow.

We are guiding to a free cash flow range of $325 million to $375 million in 2015. We expect our capital expenditures in 2015 to be in the range of $215 million to $235 million and discontinued operations to be approximately $35 million. Additionally, we expect our cash tax rate to be approximately 13% in 2015.

On slide 20, you can see our estimated adjusted free cash flow when you add back non-operational items, including the impact of the restructuring plan. We ended the year at 87% of non-GAAP net income. Our goal is to improve adjusted free cash flow to 100% of non-GAAP net income in 2015.

On slide 21, you can see our progress on working capital in the quarter. Our cash conversion cycle improved versus the prior year. We are committed to improve these metrics going forward, with a specific focus on DSL improvement.

Slide 22 shows our net debt to EBITDA metric, where we closed the year a little better than expected, with a net debt leverage ratio of 3.1 times. We expect that most of our free cash flow generation in 2015 will go to pay down debt and continue to drive the business to lower leverage longer term. Our goal is to reduce the leverage ratio to less than 3 times by the end of 2015.

The next slide provides an update on pension. We continue to make progress, reducing our overall pension liability to approximately $4.4 billion at year end, with major reductions in the US coming from our retiree lump sum offer and end of year annuitization. We previously announced that our largest UK plan, the UK London plan, has been sold and full termination is currently expected during 2015 or early 2016, which will remove another $840 million of liability.

Our overall underfunded status is now roughly $200 million after the Q4 mark-to-market adjustment of approximately $150 million, which included an update to the most recent US mortality table. Again, this $150 million was a non-cash charge. The underfunded position at the end of 2014 does include the UK London plan, which is approximately $420 million overfunded and will transfer some time in 2015 or early 2016.

You can see through our proactive work on pension, global cash contributions have significantly decreased to $35 million in 2015. We do not expect any mandatory US pension contributions for the next five years. While the major projects for Phase 3 are complete, we will continue to work on risk reduction projects that drive shareholder value and reduce enterprise risk to NCR.

On slide 24, we give our full-year 2015 guidance. The 2015 revenue guidance is expected to be roughly flat on an as-reported basis, which includes approximately $300 million of negative FX impact. On a constant currency basis, revenue is expected to be up 4% to 6%. Constant currency growth is driven by higher value solutions in Financial Services, Retail Solutions, and Hospitality.

NPOI is expected to be between $830 million and $870 million, primarily due to continued improvements in the software mix across the businesses and the benefit of the restructuring plan, partially offset by approximately $50 million of foreign currency headwind. Non-GAAP diluted EPS is expected to be approximately $2.60 to $2.80, due to higher NPOI offset by foreign currency headwinds and a higher effective income tax rate of 25% versus 22% in 2014.

The higher tax rate is due to audit settlements received in 2014 that are not expected to repeat in 2015. OIE is estimated to be $215 million to $220 million versus $213 million in 2014. Although interest expense is slightly lower, FX continues to be a headwind and interest income is expected to be lower. FX headwinds are expected to have a $0.20 per share negative impact in 2015, which is included in the guidance. We expect free cash flow of $325 million to $375 million, which includes restructuring spending of approximately $70 million to $85 million.

On slide 25, we have our revenue guidance by segment, which again includes significant FX headwinds. On a constant currency basis, Financial Services revenue is expected to grow 3% to 5%, after being up 6% on a constant currency basis in 2014, excluding Digital Insight.

Financial Services will continue to drive higher value solutions, including branch transformation. Retail Solutions is expected to grow 4% to 6% constant currency after being flat on a constant currency basis in 2014. We expect market conditions will improve for our retail offerings in 2015 and will also improve our internal execution.

Hospitality expected to grow 5% to 9% constant currency, after being up 6% constant currency in 2014. Hospitality is not expected to have the negative impact that it saw from the legacy quick service business in 2014. Emerging Industries is expected to be down 2% to up 3%, as we continue to be more selective with our revenue streams.

On slide 26, you will find our Q1 2015 guidance. I expect revenue will be roughly flat with the prior year, which includes a negative FX impact of roughly 5 points or $75 million.

I expect NPOI to be negatively impacted by roughly $10 million of FX. The tax rate is forecasted to be slightly higher than the prior year at 23%, primarily due to discrete benefits in Q1 of the prior year.

Now I'll turn it over to Bill for his closing comments on the quarter.

Bill Nuti - *NCR Corporation - Chairman & CEO*

Thanks, Bob.

I'll sum up on slide number 27. Our Q4 performance was in line with our revised expectations that we laid out for you in our Q3 call. The transformation of NCR continued in 2014, bringing further expansion of our software, cloud, and other recurring revenues. Financial Services was a bright spot in Q4 and for the full year, due to solid demand for our branch transformation solutions, as well as the impact of Digital Insight.

Retail Solutions continued to face challenges, but we are navigating through the headwinds and are focused on driving improved performance from that business. Hospitality had a good Q4 in terms of software and cloud.

During the year, we also continued building a stronger NCR. Our restructuring program is delivering results and we made progress against legacy issues like pension and Fox River.

We are excited about who NCR is today. We have a solid team that is committed to providing value to our customers and we are focused on execution in the year ahead.

Operator, please open up the lines now. Thank you.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Dan Perlin, RBC Capital Markets.

Dan Perlin - *RBC Capital Markets - Analyst*

Hey, guys. Good evening. I just wanted to explore a little bit more on this large client cancellation in the fourth quarter. Is this the legacy self checkout order that we have thought or is there something incremental to it? Is it endemic of the client-specific issues, again just double checking, or is there something in the product that you were delivering that wasn't meeting their goals? Thanks.

Michael Bayer - *NCR Corporation - President & General Manager NCR Retail*

That's a good question, Michael Bayer speaking. No, it was a customized deal, a customized project which we designed in 2013 very close to the customer and we've taken the initial order with the roll out plan, which we [currently selected] and throughout last year, the business climate for that specific customer changed drastically, changed drastically. We've taken the decision to take it out because we couldn't see a possibility for them to finance that deal and get it going. It was a one-off. It has nothing to do with the major product line.

Bill Nuti - *NCR Corporation - Chairman & CEO*

Yes, Dan, it was a non-standard NCR product. It was not in the current product portfolio. We were being asked to build it for them.

Dan Perlin - *RBC Capital Markets - Analyst*

Okay. Can you just elaborate a little bit on how you're thinking about that division? I saw your guidance of 4% to 6%, but I'm thinking in terms of the bifurcation between your self checkout business, which has historically been pretty good and kind of the legacy register business, which has been a bit of an [attriting] asset.

So how are we thinking about the cadence of layering that in throughout the year and what are you seeing that might be good, bad, indifferent relative to the environment that we just came out of last year?

Michael Bayer - *NCR Corporation - President & General Manager NCR Retail*

There were a couple of things which we've done internally, especially as we went through our software product rationalization to get ourselves straight on the product portfolio which we are driving into the market. There was also a lot of activity around self checkout and interesting enough, there are markets now opening within the self checkout space. We are driving upside in countries where we or where others are challenged on other industries, so we have three very successful pilots in self checkout in Russia, with pilots in China on self checkout. We see an uptick in Taiwan.

So very, very interesting signs, those are very interesting signs out of our installed base where we go from a version four, currently we are on version 5 and we are going end of life. So a lot of interest in upgrades in our self checkout portfolio within our existing customers.

With some of the changes, we've already seen early signs of recovery also internally how we go to market, seeing a recovery in Q4 on RPS, software maintenance margins and again, we sold at the first uptick on self checkout. We've got a couple of big managed services deals which we can't talk about yet, but in the final stage or have already been awarded. We have a very, very strong pipeline in North America, also in Canada, which will help us from a constant currency, currency green dollar basis against the currency headwind we face somewhere else in the world.

So the 4 to 6%, also that might look high, are actually not that ambitious from my point of view, given the fact that we compare it against a very lowball last year. It was a challenging year for us, but if you go back into 2013, it doesn't look that prosperous. So I think it's a good reflection of our market position. We already see, especially in North America, customers being through their work on EMV and pin pads and moving back to their normal [buying] behaviors, moving back to their normal priority of business, which is much more favorable to us.

I anticipate and have forecast an update end of Q2 in the second half due to those changes.

Dan Perlin - *RBC Capital Markets - Analyst*

Okay. If I could just ask one more and then I'll hop back in. The 1Q guide for NPOI, once we've adjusted for the ForEx, still a little bit lower than what I would've expected. I'm wondering -- which kind of sets us up again for a little bit of a more back end-loaded year. Is there anything that you can I guess identify for us to help us understand kind of the ramp and then in what area should we be kind of thinking that the first quarter on NPOI is light?

You just had a pretty strong quarter in Financial Services. Is it in Retail or is it Hospitality? I just want to make sure we're level setting that okay. Thanks.

Bob Fishman - *NCR Corporation - CFO*

Yes. I would answer that question by providing a bridge, first on full year and then on Q1. When I think about our guidance, starting from 2014 NPOI of $820 million, we are facing $50 million of FX headwinds so that would bring the prior year, call it, down to $770 million. The restructuring plan that we have in place will help 2015 by roughly $25 million.

You think of that as being the $18 million of savings we got in 2014 compared to the $70 million we'll get in 2015 and then 50% of that dropping to the bottom line. So my starting point is, call, $795 million of NPOI and then going from there, we talk about a midpoint of 5% constant currency revenue growth for the full year in 2015. That typically brings with it somewhere around 15% to 20% flow-through on NPOI and then that's how you get the range on the full-year.

To answer your Q1 question, Q1 is a little lighter. If I do the same math for Q1, I'd start off with last year's $155 million, I would back out of $10 million for FX to get me to $145 million. I'd benefit around $5 million due to the restructuring plan, so that takes me to $150 million. On seeing constant currency revenue growth of around 5% or $75 million, that brings with it a little lower flow-through, call it, 10% to 15% in Q1.

But what if offsetting that is approximately $15 million of headwind, mostly compensation-related as we compare this year to weaker performance in Q1 of last year. So we do need to overcome those headwinds in Q1. Those headwinds are more easily overcome throughout the full-year, but in Q1, the reason you're seeing a little lower NPOI is because of that. I will say this, that NPOI in Q1 reflects about 17% of the full-year NPOI, which is roughly what we've done in the last three or four years.

Dan Perlin - *RBC Capital Markets - Analyst*

Thank you.

Operator

Paul Coster, JPMorgan.

Paul Coster - *JPMorgan - Analyst*

Yes. Thanks for taking my questions. First off, the operating margins in the retail segment were pretty disappointing at times last year and it seemed like you had a more fixed cost base to that business then you would like. Can you talk about how restructuring or other things are making that more variable, if they are at all?

Michael Bayer - *NCR Corporation - President & General Manager NCR Retail*

There were two major contributors to that trend you are pointing to. The first one is related to a restructuring of our professional services business and how we cover our professional services footprint. The second one is really related to a mix, we've seen higher utilization and higher sales in our high end product mix. I'd like to point specifically to connected payments, which was a big success factor for us in the second half of last year. We've now added 6,000 additional stores.

We launched private cloud offering for our top retailers who don't want to be on a multi-tenant cloud, which transacted $1.7 billion payment transactions through our systems on this platform last year and we have passed 10,000 transactions a day in December. So long story short, it was mix and the benefit out of restructuring, especially professional services.

Bill Nuti - *NCR Corporation - Chairman & CEO*

Yes. A couple more thoughts for you on this. First of all, in 2014, one of the areas we did a poor job internally was in the management of PS costs. So when you look at our PS business in 2014, we probably burned through about $20 million of excess costs in PS and that's been right-sized over the course of the last, call it, three months. So that should be helpful to us.

One thing that was encouraging about Q4 for retail was also the improvement in operating margins in the quarter from the prior quarter and from in the prior two quarters, in fact. So I feel better about the job the team is doing there. I feel confident in the outlook that Bob gave you today in that business, as it relates at least to the ability for us to manage fixed costs.

Paul Coster - *JPMorgan - Analyst*

Okay. Two more quick questions, the retail business is more backend-loaded that perhaps all of us would like, but you've alluded in the past to a sort of sequential dependency here on EMV and data security. Why is it that you're not participating in the strength that some of the EMV companies are seeing already in the retail purchasing cycle?

Bill Nuti - *NCR Corporation - Chairman & CEO*

Well, I'd say two things. One is when you think about the front end of a retail store and the technology deployed, a lot of attention and capital has been spent on pin pads and terminals as it relates to preparation for EMV and further on from that tokenization around the meeting the mandate in October. What that does is it takes that amount of money being spent on that technology away from upgrading pause terminals and other peripherals.

What it does, secondly for us, what it has done for us is that, combined it with the entirety of the data security issue, has delayed, in some ways, the focus on driving software on the omni-commerce and omni-channel software deals out. We're seeing some of that come back. We saw some of that in Q4, which was quite positive. We're seeing some of that here in terms of activity in Q1. But those are the two key reasons why we're not participating as much as you might see other vendors in that space.

Paul Coster - *JPMorgan - Analyst*

Okay. Last question really for Bob, the assumptions that go into 2015 guidance, we might as well, I think, know what kind of dollar/euro exchange rate you've assumed so that we can sort of make incremental decisions moving forward. Also, are there any other sort of big macro assumptions that have gone into these numbers in terms of emerging markets or Europe or Asia Pac?

Bob Fishman - *NCR Corporation - CFO*

In terms of the exchange rates and the FX impact that we're giving, those are all based on end of January exchange rates. On the second part of your question, Paul, if you wouldn't mind repeating that for me.

Paul Coster - *JPMorgan - Analyst*

What I want to know is have you assumed sort of the worst of emerging markets at least in Europe? What would be big swing factors in the macro world that would therefore, sort of impact our expectations around the year?

Bob Fishman - *NCR Corporation - CFO*

Yes. Again, when we're talking emerging markets, and I think I'll let Andy give his perspective, you're talking mainly financial. We've alluded to the fact that Russia and China were the big headwinds in 2014 and will continue to be in 2015. But maybe Andy, you can add a little bit more color around how you think about emerging markets and financial?

Andy Heyman - *NCR Corporation - SVP and President of Financial Services*

Yes. I think when you look at it from our perspective and you look at kind of the FX-neutral growth in 2014 being around 6% and then the estimates out there for 2015 being in the 3% to 5% range, really what you're looking at is continued normal healthy growth on the top line for Financial Services, offset by the geopolitical risk, specifically with Russia and China anticipated.

We thought it was prudent to be conservative on those lines given what we're seeing right now. So I think your point about could there be upside if those two countries, in particular, come back, I think the answer is yes to that, although for us to plan on that right now, we don't think would be prudent.

Paul Coster - *JPMorgan - Analyst*

All right. Thank you.

Operator

Ian Zaffino, Oppenheimer.

Ian Zaffino - *Oppenheimer & Co. - Analyst*

Hi, great. Thank you very much. I'm just trying to understand the Financial Services guidance. Can you actually give us it maybe an understanding of, by region, what you're expecting and maybe what's going to outperform the 3% to 5% constant currency, what might underperform? I know you alluded to sort of China, but as you think about Europe, as you think about the US, and also just maybe discussion about bank branch transformation assumptions. Thanks.

Andy Heyman - *NCR Corporation - SVP and President of Financial Services*

Yes. This is Andy, again. So in terms of regionally, for 2014, and you saw some of this in our opening comments, in the developed markets, we had a fantastic year last year. You look at the United States, you look at Brazil, you look at Canada, you look at Western Europe. All of these areas growing high single-digits, low double-digits, same with Middle East and Africa as well.

So really good balanced growth, but other than the situations that we have with Russia and China and then of course some FX issues of that hit us. So as we look at 2015, we really don't see a difference relative to 2014. We think we have more pressure, specifically in Russia and China and we think the other markets that I just mentioned should continue to be mid- to high single-digit growth for most of them with a couple that should hit the low double-digit growth, as well.

In terms of product mix, in terms of what you talked about, again, for us in 2014 versus 2013, branch transformation, in particular, doubled for us. So we had the first year where it was a nine-figure year for us in branch transformation into the mid-100s in terms of revenue.

We see another significant increase in 2015, probably low nine figure levels, call it $100 million or so in 2015, again, of branch transformation growth, and then we also see other high value areas, specifically around omni-channel and security driving continued mix shift for the business. So you can see how our margins expanded the last couple years, we're anticipating a continuation of that as well into 2015.

Ian Zaffino - *Oppenheimer & Co. - Analyst*

Okay. When you talk about the low $100 millions, is that just the machines themselves or does that include sort of the retrofitting in the walls and the wiring and sort of all of the other ancillary pieces that come with it or is that just sort of the machines and then you would add on top of it?

Andy Heyman - *NCR Corporation - SVP and President of Financial Services*

Yes. You're talking branch transformation now?

Ian Zaffino - *Oppenheimer & Co. - Analyst*

Yes. Yes, of course.

Andy Heyman - *NCR Corporation - SVP and President of Financial Services*

First of all, just to be clear, low $100 million, not hundreds of millions, just to be clear. So think about it as in the $130 million-ish range for branch transformation growing into 2015 another $100 million or so and that revenue is in all-in revenue. It includes primarily product revenue. There are some installation services. There's quite a bit of software in terms of content there.

You're looking at an average selling price of something more like 2x the typical type of ATM. Then there's a recurring revenue stream in terms of high-availability service that also goes with that, but it's primarily product revenue.

Ian Zaffino - *Oppenheimer & Co. - Analyst*

Okay. Thank you very much.

Operator

Katy Huberty, Morgan Stanley.

Natalia Kogay - *Morgan Stanley - Analyst*

Thanks for taking the question. This is Natalia Kogay for Katy. It looks like inventory management drove some meaningful improvements in working capital. Can you provide details around what happened during the quarter and whether the strength is sustainable in 2015?

Bob Fishman - *NCR Corporation - CFO*

Yes. Our focus on working capital is really on all three major areas: receivables, inventory, and payables. Inventory was lower. You have to keep in mind, though, that inventory benefited from the restructuring plan. We had talked previously about writing off around $50 million, so inventory is lower by that amount, but that doesn't benefit free cash flow because that's a non-cash item.

But outside of that, that $50 million, the team did a real nice job operationally in terms of both finished goods and raw materials. I'd say I'm even more focused on DSO and so it was encouraging for me to see the one day improvement and we'll continue to be on that path really over the next couple of years in terms of improving accounts receivable. So that would be a bit of a summary. Overall, the cash conversion cycle improved in Q4.

Natalia Kogay - *Morgan Stanley - Analyst*

Thanks and as it relates to your 2015 free cash flow guidance, what is your assumption on working capital performance? Do expected to be a positive or a negative versus 2014?

Bob Fishman - *NCR Corporation - CFO*

For 2015, what we'll see is the same. As revenue grows, the requirement for working capital will grow and it's around that 13% number. So think of revenue growth times the 13%, but then my goal is to improve DSO by a day and that helps that number by $15 million to $20 million. So that's how I think about working capital.

Natalia Kogay - *Morgan Stanley - Analyst*

Thanks. The last question, I guess the question to Bill, midway last year, you spoke about evaluating your product portfolio and looking at some strategic alternatives. Do you have any updates on that front and which areas do you see as non-core to NCR?

Bill Nuti - *NCR Corporation - Chairman & CEO*

We are still looking at that and evaluating opportunities to divest non-core businesses. That's under way. So, no major change there. We'll continue to look at that throughout the year and come back to you at some point when we have more definitive follow-up.

Natalia Kogay - *Morgan Stanley - Analyst*

Thank you.

Operator

Gil Luria, Wedbush Securities.

Gil Luria - *Wedbush Securities - Analyst*

Yes, thanks for taking my question. On your ATM business growth, you're saying that developed economies are going to contribute more than developing economies. That's counterintuitive. How much of that is due to Windows XP upgrades helping with that, which also helps your mix? How long do you think that's going to last?

Andy Heyman - *NCR Corporation - SVP and President of Financial Services*

Yes, this is Andy. So when we look at Windows 7 in terms of developing markets, I would not single that out as a driver for the developed markets right now relative to the developing markets. I think the major thing driving growth in the developed markets right now is the need for our customers to drive costs out of their retail network, while at the same time, transforming their omni-channel experience so they can improve their service to consumers.

That need for banks and other financial institutions is creating an investment cycle for people to go through a much more advanced implementation of a software portfolio and that their branch transformative technologies. So that's really what's going on in Canada and the United States, in the Middle East, and in Western Europe.

In terms of developing markets, it's largely a situation where we've got geopolitical risk that really started to hit us in the fourth quarter and we anticipate could continue to hit us in 2015, mostly targeted towards Russia and China. So hopefully, that helps give a little bit more precise versus just a developed versus developing market story.

Gil Luria - *Wedbush Securities - Analyst*

Sure. Then, in terms of the new headquarters, what's going to be the net outlay after tax benefits for the next couple years? What's the time for a payback on that investment?

Bob Fishman - *NCR Corporation - CFO*

In terms of our headquarters, which was announced, I suppose, earlier in the quarter, our goal there is for an operating lease. The plan is to move into that building sometime in early 2018 and really, that's when the operating lease payment would start. The goal is to have that lease payment to be less than what we would pay for the existing facilities that we're in. So there's a consolidation play here that'll benefit the P&L.

Gil Luria - *Wedbush Securities - Analyst*

No investments until then?

Bob Fishman - *NCR Corporation - CFO*

No, no, in terms of it being an operating lease. So no impact to the free cash flow.

Gil Luria - *Wedbush Securities - Analyst*

Last question about the two free cash flow excluding items, discontinued operation and the pension outlay. Discontinued operation -- do we still have Fox River in there and if not, what's in there and how long is that outlay going to last? On pension, this $35 million level, is that now the run rate that we expect going forward or did that also lap at some point?

Bob Fishman - *NCR Corporation - CFO*

Yes. In terms of a discontinued ops, it's primarily Fox. What you'll see in the 10-K is the reserve for Fox at the end of 2014 is around $40 million, so think of that as being the Fox outlay over the next couple of years.

In terms of pension, that $35 million has come down significantly. You'll remember three years ago that was more like $150 million.

I think there is some improvement that can be made to the $35 million, but it's small. Think of that as $30 million to $35 million on an ongoing basis that reflects primarily the $15 million to $20 million international plans that we have. There are no US contributions expected for the next five years.

Gil Luria - *Wedbush Securities - Analyst*

That has to be a relief. Thank you.

Operator

Meghna Ladha, Susquehanna.

Meghna Ladha - *Susquehanna Financial Group / SIG - Analyst*

Hi. Thanks for taking my question. Bill, last quarter you discussed execution issues as one of the reasons for 2014 weakness. Since then, what steps have you taken that will help NCR avoid the same issue this year?

Bill Nuti - *NCR Corporation - Chairman & CEO*

Primarily, Meghna, if you looked at 2014 in total, I would say, as a year, I would not classify the execution issues, in and of themselves, any greater than a year we've done well or a year we've done poorly. However, they're magnified when you're not meeting your commitments and last year, I would say primarily, the execution issues were in retail.

On that front, as you know, we've made a number of changes to personnel over the course of 2014. I'm happy to say that those changes appear to be quite positive in terms of people, in terms of org structure, in terms of processes, and overall talent.

Now, I would also say that we had to get into some tactical issues in the year like PS costs I described earlier to Paul and other areas around expense management. But I feel a lot better about where we are today vis-a-vis retail execution.

As I look around the Company, I would say while we will have execution issues in 2015, we're all working hard to ensure that they're accretive to what was the 2014 result, meaning they're less than 2014 in terms of impact on the year.

Meghna Ladha - *Susquehanna Financial Group / SIG - Analyst*

Okay. In retail, you talked about expanding Retalix beyond the grocery segment. Are there any new wins that you can potentially discuss today?

Michael Bayer - *NCR Corporation - President & General Manager NCR Retail*

Michael Bayer, speaking. Retalix had product also outside the grocery segment, so our global enterprise and merchandise business is a form of Retalix business where we've see growth, where we've seen cross-sell and upsell within our retail accounts, as well as stand-alone business. There is a PCR business Retalix, Petroleum Convenient, which has ongoing growth globally, especially in Asia.

With of the portfolio rationalization, some of the Retalix products and especially applications will become our core application for our go to market, independent of the segments. So think about that more in terms of what is the best software service or software solution for loyalty moving forward, cross segment rather than thinking about a segment approach when it comes to core product and core platforms.

Meghna Ladha - *Susquehanna Financial Group / SIG - Analyst*

Okay. A question for Bob, how much visibility do you typically have on your pipeline for the year and how comfortable are you with the 2015 guidance that you have put out today?

Bob Fishman - *NCR Corporation - CFO*

I missed the first part of the question. In terms of comfort with regard to what, Meghna?

Meghna Ladha - *Susquehanna Financial Group / SIG - Analyst*

The first one was how much visibility do you typically have on your pipeline for the year and how comfortable are you with the 2015 guidance that you've put out today?

Bill Nuti - *NCR Corporation - Chairman & CEO*

In terms of visibility for the pipeline for the year, I would say right now, Meghna, about 41% of our business falls into the recurring revenue category and then we come into the year with a little over $1 billion in backlog. So think about that as having about 60%-plus of the year in terms of revenue that's quite visible. The rest really comes from sell and bill.

What we've done this year is we have taken a more pragmatic approach with regard to looking at sell and bill in the form of orders and backlog for Q2, Q3, and Q4, to develop guidance. I would classify guidance as responsible. I'm not ultraconservative and not out there in terms of being aggressive. I would say responsible. Bob?

Bob Fishman - *NCR Corporation - CFO*

Yes. One of the reasons why I gave the more detailed bridge earlier in the call was just to focus on the areas that I think are important when analyzing NCR. You have to first acknowledge that there are FX headwinds. After that, include the benefit for the restructuring plan and we will execute very successfully on the restructuring plan and then it really comes down to the constant currency revenue guidance by division.

Hopefully, what has come across on this call is that the numbers that we have are very achievable. We haven't talked a lot about Hospitality. We've talked about Retail. One not being an easier compare, two some momentum coming into the year, we talked about Andy's business in financial seeing good growth in the developed markets, some challenge in Russia and China.

Then when I look at Hospitality, that's a business that grew constant currency 6% last year with significant headwinds on the legacy quick service restaurant. That really should not happen again in 2015, so I feel very good about the 5% to 9%. Then within Emerging, that's just us going after being very selective in terms of us going after the right deals in Emerging. So again, I look at the revenue guidance, am comfortable with that and the margin flow-through.

Meghna Ladha - *Susquehanna Financial Group / SIG - Analyst*

Thank you.

Operator

Kartik Mehta, Northcoast Research.

Kartik Mehta - *Northcoast Research - Analyst*

Good afternoon or evening, Bill. I wanted to get your perspective on Digital Insight, the type of growth you're anticipating for 2015, considering all the new signings that you've been able to get in 2014.

Bill Nuti - *NCR Corporation - Chairman & CEO*

I'd say, first of all, on DI in general, [before I take it] was a good year for us across the board. I was really pleased with the performance of DI in the year. The revenue synergies we were able to achieve in FI were small bank segments, the integration of our technology and people, and so overall, it had a materially positive impact on our business and most importantly, positioned our financial business well for the future. Perhaps Andy, you can comment on 2015 and what you're expecting there as well?

Andy Heyman - *NCR Corporation - SVP and President of Financial Services*

Yes. Of course, we're talking about a SaaS business here which in any one year, given that we're not booking licenses in one-time revenues, it's a lot about investments in two things. One is innovation, new products that you can attach onto existing customers. Two is sales people, adding more sales people to go get more new customers. With both of those, the results become precise per month revenue improvements.

So as we're looking at this year, we're looking at this year as a big growth year in terms of more sales people, more modules, more users signed on from a financial institution perspective and really gravitating towards our long-term model of double-digit growth. For 2015, we think it'll be more tempered than that, probably in the mid- to high single-digit, depending on where things come out in terms of acceleration of deals and implementation of those.

Kartik Mehta - *Northcoast Research - Analyst*

Andy, based on your comments, it seems like you're going to be investing for growth in that business for future. Is that implied that maybe the margins could be impacted negatively or should the margins kind of stay where they were in 2014?

Andy Heyman - *NCR Corporation - SVP and President of Financial Services*

Yes. I would say two things. First of all, when we're talking about the gross margins, you're talking about a business that the more we can drive growth, the more we're able to leverage a fixed cost structure in terms of hosting and support. So our margins ought to gravitate in a positive way on the gross margin line.

From an operating margin perspective, which may have been the heart of your question, I do think 2015 is an opportunity for us to make investments in both the product portfolio and the sales teams. We want to be balanced with that to ensure we don't get ahead of ourselves in terms of what sales people can sell or what products we bill for. So the operating margins, we don't look for great margin expansion on DI in 2015, although 2016 and beyond, we would anticipate that.

Kartik Mehta - *Northcoast Research - Analyst*

Andy, I wanted to make sure I understood what you said in branch transformation, get a clarification. Were you saying expect about $230 million in revenue in 2015 from branch transformation from $130 million at $100 million. Did I understand that correctly?

Andy Heyman - *NCR Corporation - SVP and President of Financial Services*

Yes. You're in the right ballpark. Think of it as the mid-100s, adding another in terms of $100 million-plus, call it, $130 million or $140 million-ish range, add another $100 million onto 2015.

Kartik Mehta - *Northcoast Research - Analyst*

Then I think you said expected that drives about two times the average sales price of a regular ATM and most of that is product. With that implied, and I know this is rough math, but would that implied about 3,500 units or so that you would want to place and 2015 to kind of get to that number?

Andy Heyman - *NCR Corporation - SVP and President of Financial Services*

You're in the right ballpark.

Kartik Mehta - *Northcoast Research - Analyst*

Okay. Bill, just a last question, looking at your ATM results for the year, as you sit back and reflect on it, do you think you gained market share? If so, what regions do you think that occurred?

Bill Nuti - *NCR Corporation - Chairman & CEO*

I do. I think when you look at results for NCR and we have not seen all of our competition yet, but what we've seen so far would suggest we have gained market share, in particular in Western Europe and in the US are areas where I would point to as key markets where we've gained share and in specifically, the branch space overall. Any further comment on that, Andy?

Andy Heyman - *NCR Corporation - SVP and President of Financial Services*

No, I think that's right. When you go to customer share and you look at specific countries, it's very clear we're picking up share. You look at us versus competition where, take Western Europe as a great example, we're talking about high single, low double-digit growth depending on whether you're looking at orders from revenue. Our competitors are not nearly in that range. You go to Canada, you go to Middle East, you go to Africa, you go to the United States, and each of these regions we're picking up material share.

Bill Nuti - *NCR Corporation - Chairman & CEO*

Just to give you, Kartik, a bit more color on that, just to break apart Russia from Western Europe, on the full year 2014, we grew revenues in Europe, Middle East, and Africa, without Russia by 17%. In Q4 alone, it was up 7%. So you can see the impact that Russia is having on our total aggregate growth on the year and on the quarter, but then you can also see that when you take it out, that we're having a solid performance and clearly, share growth in those markets.

Kartik Mehta - *Northcoast Research - Analyst*

Thank you very much. I appreciate it.

Bill Nuti - *NCR Corporation - Chairman & CEO*

Thanks.

Operator

SK Prasad Borra, Goldman Sachs.

SK Prasad Borra - *Goldman Sachs - Analyst*

Hi, thank you for taking my questions. Firstly, can we revisit the topic of synergies between the various divisions? What kind of a back end synergies you have between Financial Services business and the Retail side?

Bill Nuti - *NCR Corporation - Chairman & CEO*

Your question is around the synergies across the divisions. When I think about the synergies across the divisions, I think about the two horizontal groups. Its operations and the supply chain and then it's our services business. Those are the two pieces that provide the synergies, whether it's call centers, whether it's the five manufacturing plants, that's where we see the benefit.

SK Prasad Borra - *Goldman Sachs - Analyst*

Okay. You talked about the professional services business and you mentioned $20 million of excess costs, which we saw in third quarter. When you say excess costs, what was that particularly regarding? Is at the first phase of implementations which you did at some of those retailers not working out and did you have to pay any penalties related to that? When you think about, say, 2015, do you have a good number of, say, Phase 1 of the great deal of projects in the pipeline?

Bill Nuti - *NCR Corporation - Chairman & CEO*

I'll ask Michael to comment in a moment, but I want to clear something up. The $20 million in excess PS cost is really a full year number, not a Q3 number alone. So, it's a full year number. Michael?

Michael Bayer - *NCR Corporation - President & General Manager NCR Retail*

I think what we've seen here is we had efficiency gains as we've had a global operations around service effects, which I thought we are not meeting the requirements of our customers and we are not big enough from a business point of view, so that drove a lot of savings. In terms of the projects, I'm very positive about the projects.

That is also one of the reasons I anticipate a stronger H2 versus H1 in our projection because a lot of these project have started, will start, are awarded, or the process of being awarded and have to be closed before peak season, which depending on the country, you're looking at starting in October or starting in November. So a solid pipeline for PS and anticipate PS and all of the other software-related businesses of Retail to again possibly contribute to the mix of our Retail P&L.

SK Prasad Borra - *Goldman Sachs - Analyst*

Okay. Probably just the last one on retail, in the guidance of the 4% to 6% year-on-year growth you're expecting, what kind of a spending environment are you expecting in Retail in general? Are you expecting the spending to improve in general? You mentioned that some of the spending which got clocked in the security segment, that's a probably coming out now. Do you see signs of that in the fourth quarter itself?

Michael Bayer - *NCR Corporation - President & General Manager NCR Retail*

No, what I've seen it is, quite frankly, a very big [spec]. If you look into the UK, we have almost a price war being started by Tesco, which is impacting the market there; however, even in this challenging environment, you will see retailers in the UK taking investments to catch up to show themselves as innovation leader or to rework the way how they do business.

We have a fantastic new store opening with one of our customers for a self checkout concept where 70% to 75% self checkout customers are targeted for the UK with a very, very positive [treat] bank. So you're going to see innovation still being driven and the market leaders in that innovation retail will track the others also into that whole bucket.

As we said earlier, now the priorities are already starting to shift back in North America as all of the decisions or almost all of the decisions on security, EMV, pin pads, and so on and so forth have been made. We're back to, quote-unquote, normal in terms of user experience, customer experience, and how to improve the multi-channel experience of the end customers of our retailers.

SK Prasad Borra - *Goldman Sachs - Analyst*

That's helpful. Thank you.

Operator

Matthew Lipton, Autonomous Research.

Matthew Lipton - *Autonomous Research LLP - Analyst*

Thanks. Thanks for squeezing me in. Bill, I just wanted to make sure I understood you right. You made an interesting point about the guidance and Retail in particular and that sell and bill, you're using a new formula. I know when the guidance was cut on the third quarter call, part of that was you felt the dynamics of the pipeline were changing. So are using the same methodology for 2015 that you had used back in 3Q when you made the guidance reduction in Retail?

Bill Nuti - *NCR Corporation - Chairman & CEO*

We are. What I would tell you is it that we're going to be talking to you about in a future quarter, perhaps maybe even Q2, is the most important metric today for us is really no longer backlog per se or orders per se. The reason that is because orders and backlog the way we've described it to you in the past does not include key portions of the business.

For example, it does not included file value for services, which is about, on any given day, about 25% of our business. It does not include consumables. It does not include any of the acquisitions, if you will.

So what we're working on now is a really true backlog metric, which would include legacy backlog, as you know it, plus SaaS ACV, or think of it as file value for our cloud business, plus, file value for services, meaning what dollar amount of service contracts do we have in the pipeline for the next 12 months. That will equate to probably over 90% coverage of revenue and we're beginning to look at that now more holistically and using that, as well, to refine our guidance.

Matthew Lipton - *Autonomous Research LLP - Analyst*

Thanks. Last one from me, I guess probably for Andy, I think a lot of people will be surprised that most of the branch transformation revenues are coming from the product side. When you think about it, it might imply that you're actually taking some share. Is it your leadership position in multi-vendor software or the fact that you were the first in the market with that tablet-based strategy? What are some of the things that you think might be allowing you to see outsize unit growth in branch transformation? Thanks.

Andy Heyman - *NCR Corporation - SVP and President of Financial Services*

Yes. In terms of the things that are driving growth in branch transformation, for us, it's very much -- I would boil it down to three things. First of all, we've got a very strong position on the software side that's been evolving towards a true omni-channel capability, so that's the first thing that is resonating with customers. The second thing is the combination of our hardware design and the service offer around that is very difficult to compete with and the scale that we have plays very well in each of our key markets, so that's the second big thing.

The third big thing is execution. These are fairly complex programs that customers are looking at. They have to trust who they're working with when they sign transformative contracts and they want to partner with somebody that they trust can execute both in terms of subject matter expertise, schedule adherence, and quality. Those are the three reasons that we're winning.

Matthew Lipton - *Autonomous Research LLP - Analyst*

Right. Thank you guys.

Bill Nuti - *NCR Corporation - Chairman & CEO*

Thank you all for joining us. We'll see you in April.

Operator

This concludes today's conference. Thank you for your participation.