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NCR - Q3 2015 NCR Corp Earnings Call

EVENT DATE/TIME: OCTOBER 27, 2015 / 8:30PM GMT

OVERVIEW:

Co. reported 3Q15 non-GAAP EPS of $0.78. Expects 4Q15 reported revenue to be $1.687-1.717b.

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PRESENTATION

Operator

Good day and welcome to the NCR Corporation third-quarter fiscal year 2015 earnings conference call. Today's conference is being recorded.

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

Gavin Bell - *NCR Corporation - VP, IR*

Good afternoon and thank you for joining our third-quarter 2015 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 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 the 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 would like to turn the call over to Bill Nuti.

Bill Nuti - *NCR Corporation - Chairman, CEO and President*

Thanks, Gavin. Good afternoon, everyone, and thank you for joining us today. We had a solid third quarter, as consistent execution by the NCR team generated results in line with the outlook we provided in July. We achieved these results in the face of a worsening currency environment, continued challenges in China and Russia, and more volatile capital markets.

Despite these headwinds, we drove solid performance across our businesses and remain on target to achieve our full-year goals for earnings and free cash flow.

Our growing $1.8 billion software and cloud business, global diversity of industries and markets, along with great employees and partners, are the keys to NCR's success.

Turning now to slide number 3, Q3 revenue was down 2% on an as reported basis. This is lower than the revenue guidance we provided on our Q2 call, due to an additional $30 million of negative affect headwinds during August and September. On a constant currency basis, revenue was up 5%. And at the end of Q3, recurring revenue represented [42%] of total revenue, up 8% constant currency.

Operational gross margin was 29.4% in Q3. This was up 50 basis points compared to last year, primarily due to higher software revenue. Q3 NPOI was $218 million, up 7% on an as reported basis and up 15% on a constant currency basis. Non-GAAP EPS was $0.78, up 16% as reported and up 25% constant currency.

Free cash flow, an area where our investors have been looking for continued progress, has been a great success year-to-date and we are on track to achieve our updated full-year guidance. Free cash flow [excluding] $93 million in recovery related to the Fox River and Q3 2014 was up $67 million compared to last year. We have generated $225 million in free cash flow year-to-date, which is an increase of $141 million compared to the first nine months of last year.

I am now on slide number 4 where we will review our Q3 and year-to-date software-related revenues. Software-related revenue was up 5% on a constant currency basis year-over-year and continues to grow faster than our other revenue stream, especially our cloud business. Our growth in cloud remains a high point in our overall results.

With constant currency revenues up 7% in Q3 and now up 12% year to date constant currency, growing our software-related revenue stream remains a top area of strategic focus as we look to improve our overall margins in a rapidly expanding available market for software in cloud solutions.

Finally, on slide number 5, I will spend a few moments running through some of the key highlights for Q3. Our results for the quarter were driven by our global leadership in our verticals along with solid execution across NCR. This includes operating margin expansion in each of our businesses. Currency volatility, along with China and Russia, continue to be our primary challenges. But we are navigating through them.

Our Q3 earnings were in line with our outlook and we remain on track to achieve our full-year goals. Other key highlights include the performances of each of our businesses which were generally balanced with the exception of Financial Services, who is taking the brunt of FX and the China/Russia impact.

That being said, we don't want to mask the solid performance of this division when you exclude China and Russia, where Financial Services delivered 3% year-over-year constant currency growth. Our Financial Services business continues to generate strong demand in important strategic areas such as software, cloud, branch transformation and security application offers.

In Retail, we are encouraged by the moderate improvement in industry dynamics. In particular, retail spending and how those dollars are being allocated. Growth in Q3 was promising, with revenues up 14% on a constant currency basis. I am generally pleased with Retail's performance to date this year and will continue to innovate improvise solutions to our Retail customers and enable them to run their businesses more efficiently to enhance flexibility and omnichannel solutions in hospitality. Higher software and cloud revenues once again drove year-over-year operating margin expansion and 8% constant currency revenue growth.

This business has made significant progress over the past several quarters and we are pleased with the trajectory going forward.

Another important highlight is our total software revenue, which was up 5% on a constant currency basis during the quarter. With continued strong growth in cloud and important wins across our verticals, we made additional progress executing our transformation to a hardware- enabled software-driven Company. We also continued to build a better NCR through sales and services transformation; and our Company-wide restructuring efforts are benefiting these initiatives.

Finally, strong year-to-date free cash flow places us well ahead of last year. In summary, we had another important and solid quarter and are on track to achieve our full-year target.

I am pleased with the execution of the NCR team. We are driving growth across all of our businesses and are focused on finishing the year strong.

Finally, with regard to recent industry consolidation, we believe the merging of legacy hardware businesses is a good thing for our industry and an important validation of the business strategy we've embarked upon five years ago. NCR is a highly diversified global business, providing a suite of omnichannel solutions and services to customers in a variety of industries, including Financial Services, Retail and Hospitality.

As a true omnichannel solutions provider in Financial Services, NCR -- unlike its ATM competitors -- bridges all banking channels and is actively helping top financial institutions around the globe transform their businesses into asset-light technology-heavy enterprises that engage with their customers, both physically and digitally.

In short, we feel extremely well-positioned and will continue to stay laser-focused on our customers and strategic execution.

Now I would like to turn the call over to Bob to review our performance by segment and our financials. Bob?

Bob Fishman - *NCR Corporation - SVP, CFO and CAO*

Thank you, Bill. I will start on slide 6, which shows our Q3 operational results on an as reported in constant currency basis, which Bill previously discussed.

We experienced unfavorable foreign currency fluctuation during Q3 with impacts of approximately $120 million in revenue, $17 million in NPOI and $0.06 in EPS. FX impact on revenue came in higher than originally expected with an additional $30 million of headwind from our guidance at the beginning of the quarter. Revenue was higher by 5%. NPOI was higher by 15% and non-GAAP EPS was higher by 25%, all on a constant currency basis.

The next slide shows our Q3 GAAP results. The increase in GAAP results is primarily related to the impact of the restructuring program recorded in Q3 2014 as compared to Q3 2015. The restructuring plan charge included in income from operations was $12 million in Q3 2015 and $127 million in Q3 2014.

On slide 8, you will see our Financial Services Q3 results. On a constant currency basis, revenue was flat, due to improvements in the Americas, South Pacific, the Middle East Africa, offset by declines in China and Russia. Excluding China and Russia, revenue was up 3% on a constant currency basis. Operating margin was up 50 basis points at 16.5%. The improvement was due to a favorable mix of revenue and expense management.

We remain focused on profitability through our transformation initiatives, mix shifts and operating margin expansion. We continue to see an increase in our branch transformation revenue, which grew 94% year over year led by North America. Constant currency backlog position grew double digits, driven by branch transformation and Cx Banking. But along with this, inherently slower conversion rates are affecting short-term revenue.

And finally, industry consolidation, as Bill mentioned, is signaling positive indicators for future demand.

The next slide shows our Retail Solutions Q3 results. Revenue was up 7% as reported and up 14% on a constant currency basis, due to improvements in all regions. Operating margin was 8.2%, and increased 330 basis points. Retail operating income increased from the prior year due to higher revenue, including more software-related revenue and expense management. The retail market continues to show signs of improvement, with some regions experiencing slower growth and additional FX headwinds.

We are having success gaining new competitive key accounts globally and we received the Supplier of The Year Award for outstanding service from the Australian supermarket, Coles. Lastly, we are pleased with the positive reaction, our Retail One omni-commerce platform is continuing to receive from the market and our customers.

Turning to the next slide, hospitality revenue was up 8% on a constant currency basis, driven by improvements in the higher margin revenue streams. Operating margin performance was 16.9%, up 80 basis points due to this higher software-related revenue including cloud and professional services revenue. We continue to see success in the SMB market with 4% revenue growth and 8% software-related revenue growth. We are pleased to report that we have deployed 40,000 application sites in the managed SaaS application family, which includes 9,000 Pulse Real-Time application sites.

Software-related revenues continue to drive growth for our Hospitality business, which are up 20% on a constant currency basis in Q3 2015, which includes cloud revenue of 25% on a constant currency basis.

Next, looking at our emerging industry business on slide number 11, revenue was up 2% year over year and up 11% on a constant currency basis, driven by an increase in telecom and technology constant currency revenue. Operating margin was 10.8%, up 90 basis points driven by higher services margins.

On slide 12, you can see the solid growth in cloud revenue on an as-reported basis. On a constant currency basis, cloud was up 7% and software-related revenue grew 5%. Hardware was down 5% as reported, up 4% on a constant currency basis. And other services, which includes our traditional break/fix business, was down by 1% as reported, up 7% on a constant currency basis.

On slide 13, you can see free cash flow for the quarter. Free cash flow for Q3 2015 was $106 million compared to $132 million in the prior quarter. Excluding $93 million in recoveries related to the Fox River in Q3 2014, the increase was mainly due to higher operating cash inflows. On a year-to-date basis, free cash flow was $225 million compared to a free cash flow of $84 million in the prior year. We are maintaining our full-year 2015 free cash flow guidance range of $350 million to $400 million.

Slide 14 is an update on the restructuring plan. We incurred a pretax charge of $36 million in the first nine months of 2015 and expect to incur an additional pretax charge of $20 million to $28 million in Q4 2015. The cash impact was $51 million in the first nine months of 2015 and we expect to pay an additional $20 million to $35 million in Q4 2015.

As far as savings generated, we achieved $18 million in 2014 and estimate approximately $70 million in 2015 and approximately $105 million in 2016. As previously communicated, we expect approximately 50% of the savings to benefit NPOI with the remainder reinvested in the business. We continue to evaluate additional opportunities in connection with this restructuring plan, and will consider implementing initiatives that would generate incremental savings for the Company.

Slide 15 shows our net debt to EBITDA metric, where we closed Q3 with a leverage ratio of 2.9 times. This was benefited from our free cash flow generation in the quarter, which has allowed us to achieve our year-end goals of under three times leverage one quarter earlier than expected.

Slide 16 shows our full-year 2015 guidance. FX headwinds continue. Full-year revenue headwinds of approximately $420 million are now expected, higher by $65 million from guidance in July and $120 million from beginning of the year guidance. NPOI FX headwinds are still expected to be $70 million to $75 million, up $20 million from beginning of the year guidance and EPS FX headwinds are $0.10 higher than the beginning of the year guidance.

We are decreasing our constant currency revenue guidance to 3% to 4% due to continue challenges in certain developing markets and slower backlog rollouts pushing into 2016. We are narrowing our NPOI range to $830 million to $840 million at the lower end of our previous range, primarily due to the lower revenue and the additional $20 million of negative foreign currency impact from our beginning of the year guidance.

Additionally, we are narrowing our non-GAAP EPS range to $2.70 to $2.80, which is at the high end of our previous range due to other expense, prospective tax rate and share count being lower than previously expected. This guidance now includes an expected OIE of $204 million, a tax rate of 24% to 25%, and a share count of 173 million.

Slide 17 shows our updated 2015 full-year revenue guidance by segment. We now expect Financial Services to grow 1% to 2% on a constant currency basis, down from prior guidance due to continued challenges in China and Russia and slower backlog rollouts. We now expect retail solutions to grow 5% to 6%, hospitality to grow 5% to 7%, and emerging industries to grow 5% to 7%, all on a constant currency basis.

On slide 18 you will find our Q4 2015 guidance. I expect as reported revenue will be in the range of $1.687 billion to $1.717 billion, which includes a negative FX impact of roughly 5% compared to the prior year. Revenue is expected to be flat to up 2% on a constant currency basis. I expect NPOI to be negatively impacted by roughly $19 million of FX. Based on the midpoint of the range, NPOI growth is expected to be up 7% on an as-reported basis and up in percent on a constant currency basis.

Now, I will open up the call for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Paul Coster, JPMorgan.

Paul Coster - *JPMorgan - Analyst*

First of all, it's nice to see another decent quarter. But of course, the question which everyone will be asking is what about the strategic review? What can you say about that, please, Bill?

Bill Nuti - *NCR Corporation - Chairman, CEO and President*

Thank you, Paul. First of all, appreciate the kind opening.

On the strategic review, Paul, that is ongoing. We continue to comprehensively look at all of the alternatives we have as a Board. We are balancing both running the business responsibly and to your point making our commitments while also, again, with a lot of rigor looking at every single alternative we have and really giving it enough time for analysis and review.

So it is ongoing. I anticipate it will be ongoing now for the next few months. And we will see where it lands, but right now there has been no change in that particular analysis.

Paul Coster - *JPMorgan - Analyst*

Bill, does it have to come to sort of point of completion or are there items that may fall out of the strategic review that can be executed along the way? And I am particularly sort of interested in Bob's comments about restructuring and how there may be some additional restructuring opportunities ahead, which did not sound like they were part of the strategic review, but I suspect there is some relationship there.

Bill Nuti - *NCR Corporation - Chairman, CEO and President*

Yes, Paul, you will likely see some aspects of the strategic review fall out into near-term actions. And we can't get into that on the phone today, but certainly if there was a smart thing for us to do, we are going to do it. Is there an official ending to the process? I think the answer is yes. But again, I would tell you my learnings out of this is the following.

One, when you take on that kind of a project, it is a 15-hour workday and a lot of weekends so that you can responsively run the business. And secondarily, the depth at which one needs to go for each alternative to give your Board a thorough view is a lot of analysis. It will not stop our Board, however, from taking immediate action on areas that make sense. And one of them may be some amount of additional restructuring.

One of the benefits for Bob and I of going through the process has been we've had access to a number of exceptional resources that have looked inside of our Company at a level of depth that would normally cost us millions of dollars of consulting fees that I think, fortunately for us, we did not have to bear. And we are going to take their advice in some circumstances but make sure it makes sense for the business. And we may decide to extend the restructuring initiative in Q4 or Q1. But we are not quite there yet.

Bob Fishman - *NCR Corporation - SVP, CFO and CAO*

I would say to that point is we are definitely focused on fast payback opportunities that are attractive to investors. As we continue to focus on higher margin, higher growth opportunities, end of lifing products as an example, those continue to be areas how we would become more efficient.

That is all work that continues to be done; and we wanted to leave open the opportunity that we do see some attractive cash payback opportunities that would be available to us.

Paul Coster - *JPMorgan - Analyst*

Okay, great, thanks. I will hop back on the queue.

Operator

Ian Zaffino, Oppenheimer.

Ian Zaffino - *Oppenheimer & Co. - Analyst*

Question beyond the pushout of the backlogs; is that just an emerging markets phenomenon or have you seen that in developed markets, and maybe what areas of the business are you seeing that in?

Bill Nuti - *NCR Corporation - Chairman, CEO and President*

It really is primarily in the financial services area. So I will ask Andy Heyman to comment.

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

In terms of where the backlog right now is -- a little slower than normal, and just to give you some statistics on this, we had earlier in the year anticipated some reduction in the typical backlog conversions based on our contracts were increasingly in the areas of higher branch transformation commitments, higher enterprise software commitments and higher areas in terms of our refreshed ATM fleet called the 80 series.

And we had planned in the back half of the year for about a 50 basis point reduction -- I'm sorry, a 500 basis point reduction in the typical backlog conversions. So think of that as entering a quarter, if you've got $800 million of backlog where there is 50% conversion, we had planned it for about 500 basis points less. What we are seeing is about 1,000 basis points less conversion because of those three areas. There is a higher percentage of more innovative products in the queue right now that customers continue to try to get ready for, if you will, as they come out of R&D into the implementation cycles and those go through typical certifications that can have delays. There could be some R&D areas where we are tightening up, etc.

So that is what has led to slower convergence. And as we look into next year, we think we will start to revert to the mean. But, that is what is causing the backlog delays that you are seeing right now.

Ian Zaffino - *Oppenheimer & Co. - Analyst*

Okay, thank you. And next question would be maybe more -- (multiple speakers)

Bill Nuti - *NCR Corporation - Chairman, CEO and President*

I would add to that point, sorry -- I would add to that point that the backlog growth constant currency is up double digits going into Q4, and I expect it will continue to be strong going into 2016. So, while it is rolling out more slowly because of the focus on these more innovative solutions, the backlog growth is there.

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

Great point, Bob. Thanks.

Ian Zaffino - *Oppenheimer & Co. - Analyst*

Okay, and I guess the follow-up question would be -- maybe this is a [semantical] question, but when you talk about strategic alternatives and maybe where we are headed towards, it seems maybe like a restructuring is most likely.

So, given kind of the advanced stages of this process, is it still appropriate to call it strategic alternatives? Because I guess that would insinuate something probably larger than just a restructuring. And again, maybe we are talking semantics, but I guess my definition or I think most people's definition of strategic alternatives would be greater than just restructuring or just say cost cuts or realigning of some product offerings. Maybe if you help us understand that a little bit better or kind of what your definition might be.

Bill Nuti - *NCR Corporation - Chairman, CEO and President*

I apologize if it came off where we were giving you the impression that the ongoing review would only result in additional restructuring. If that was the case, we would shut it down and move in that direction. That is not the case.

All of the areas that I had previously gone over with you are still under review and possible outcomes well beyond just restructuring.

Ian Zaffino - *Oppenheimer & Co. - Analyst*

That's great, thank you for the clarification. I appreciate this and (multiple speakers). Okay, thank you very much.

Operator

Meghna Ladha, Susquehanna International Group.

Hamza Fodderwala - *Susquehanna Financial Group - Analyst*

Hi, this is Hamza Fodderwala in for Meghna Ladha. Just wanted to get a sense of -- you have cited a headwind from Russia and China of roughly, I think, 200 bps earlier this year in your guidance. What exactly accelerated the weakness here?

Bill Nuti - *NCR Corporation - Chairman, CEO and President*

Andy, can you take that, please?

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

Yes, in terms of Russia and China, they each have unique situations in terms -- if you are referring to what is causing those headwinds. In China, what we've seen is a significant tightening under the government's secure and control mandate to reduce spending; the banks are allowed to invest in with companies that build systems outside of China. They've had R&D that are not indigenous to Chinese companies.

So that has caused banks to significantly reduce spending with companies that are not Chinese companies and instead point it towards local companies. So that has really accelerated the headwind in China.

In Russia, very different story, first of all the macroeconomic conditions in Russia have been very challenged for local financial institutions there. And then, second of all, we have a lot of contracts in US dollars in Russia. And when you have a contract in US dollar as the dollar has strengthened significantly over the last 18 months, it has made it much more difficult for a financial institution in Russia to be able to afford our solution. So it's a bit of a double whammy that is going on in Russia right now.

Hamza Fodderwala - *Susquehanna Financial Group - Analyst*

Okay, and then just a follow-up. I know you mentioned obviously a potential merger between a couple of your competitors. Just wanted to get your sense on the landscape should this transaction go through, and do you think it could help stabilize the pricing environment in Europe?

Bill Nuti - *NCR Corporation - Chairman, CEO and President*

I will make a couple of comments and then ask Andy to give his point of view. First of all, I think on the surface, the strategic rationale of two legacy ATM providers coming together actually makes very good sense. Especially given that there really isn't a lot of geographic overlap for their market presence. So on the surface, I think it makes sense.

Now, both of their CEOs have talked about the importance they place on investing in software, in cloud, in digital banking and using the combination perhaps to build a balance sheet to be able to invest in where customers in the markets they serve, and we serve, are going. Now of course, we've been through that process over the last five years, so we have a unique point of view on that.

I think the challenge for them, if there are challenges, are obvious to all of us in that a merger of that size is extremely difficult to pull off. And I don't envy the geographic proximity issues, the cultural differences within the two companies, the product overlap issues that inevitably you have to face in choosing which product lives and which product does not. The services infrastructure issues that they will have to face, clearly the issue around where they decide to make cost cuts in terms of employees and R&D and there is a lot of fundamental issues that could, if they do not execute well, slow them down in a market that is moving very, very fast.

So again, on the surface, I think it's a good thing. Relative to the challenges, for us, of course, we are now with many of our acquisitions and the assets we have behind us where they want to go, are laser-focused on innovation moving forward in a rapid fashion and I think putting ourselves into a great position in the market. Andy, any other comments?

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

Yes, let me say a couple of things. And at an enterprise level, obviously one of the companies has a retail business, so I want Michael Bayer to also get a chance to say a couple of words. But it is largely about Financial Services with this merger possibility.

First of all, we were not surprised by this news at all. It had been something that we felt might make sense for a number of years, for all the reasons Bill outlined.

What our customers are telling us right now -- and by the way, there has been no shortage of communication between customers and us, based on the recent news -- but what they are saying to us right now is a couple things.

First of all is they've congratulated us just looking at our value proposition, how we have been so focused on a transformation for a number of years, becoming much more software-driven, so much of our revenue streams today in Financial Services do not come from ATMs anymore. We have a very large and growing enterprise software business that in the recent quarter made up about 40% of our software revenues.

So we've been doing a lot of things to change the value proposition. For us, it has changed our operating margins quite substantially, based on that innovation.

The second thing they are telling us is keep doing exactly what you are doing, which makes a lot of sense to us. We feel like the strategy we put in place has really changed the game in the industry. It is not just about physical channels. It is not just about digital channels. We're the ones that they look to to integrate channels seamlessly to help financial institutions control costs and improve revenues. So it's really been working for us.

In terms of your question about pricing, you can never predict what's going to happen out there on pricing. But there's a lot of competition, there always has been in the Financial Services space. There is a lot of spending and a lot of competition.

We don't expect that to change over the course of time. But I would say, just as we are looking at recent activity, that we do think that pricing is probably more stable right now than it was six months ago, that is not to say that that's a new trend either. It is a highly competitive market.

Hamza Fodderwala - *Susquehanna Financial Group - Analyst*

Okay, thank you very much. That's it for me.

Operator

Kartik Mehta, Northcoast Research.

Kartik Mehta - *Northcoast Research - Analyst*

Bill, I don't know if this is a question for you or maybe Andy. I was just wondering if either one of you could comment on digital insight and the growth you're witnessing now, is it part of NCR and maybe some leverage you were able to get because of the ATM business?

Bill Nuti - *NCR Corporation - Chairman, CEO and President*

Yes, sure, first of all I will let Andy do most of the talking, but we are very pleased so far with the progress we're making in DI. Andy, any other further comments from you?

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

Yes, a couple things; first of all, it has been the backbone for us of our whole community financial institution segment play that we've been making for a couple years now. That business will perform extremely well this year for us. The Digital Insight component, which is a subset of how we go to market in the community financial institution space, continues to be growing this year in kind of the mid-single digits.

The key thing to know that we've been talking about is that we believe this is a business that can grow high single digits, low double digits long term like our hospitality SaaS business. And what we've been working on so hard is getting the customer satisfaction model extremely high and our team has done an exceptional job of that. We've grown the net promoter score from negative numbers to very positive numbers in about 12 months.

We are still work -- if you look at the business, there's a lot of growth in end-users, which is great. We have a new module coming to market right now. We went live with it last week, business banking. We see a lot of growth ahead for the business and we just have to work through the erosion of some of the complaints and contracts for prior owners that should be behind us by the first half of next year. So that has been the only headwind in the business. That will be behind us soon enough. So it has been a fantastic acquisition thus far.

Kartik Mehta - *Northcoast Research - Analyst*

So, would that imply DI is going to mid-single digits, and if I look at Financial Self Service numbers on a constant currency basis, would that imply that the overall ATM business was down? And if so, what would you attribute that to?

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

Well, yes, the ATM business is -- when we look at it right now, it goes a little bit back to the backlog story. I would say the ATM business generally speaking, if you think of our businesses, is the ATM business versus the branch business versus DI.

The ATM business is right now -- there is a softness to the point you mentioned, but you have got to look at the Russia/China syndrome that is going on, because that is causing a, depending on the quarter, 300 or 400 basis point impact.

So when you normalize it for that, it is a growth business still. And then the backlog position, because of the points I than that. But it is still a low single digits growth business without Russia/China. Once the backlog starts to revert to the mean in the outer quarters here as we look into 2016, then we are back to what I would call a normal level of growth for the business.

Kartik Mehta - *Northcoast Research - Analyst*

So you are just having two geographies negatively impact you.

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

Two geographies negatively impacting us, along with slower conversion of other markets due to the percentage of contracts that are in these more innovative areas.

Kartik Mehta - *Northcoast Research - Analyst*

Bill, just one last question. Obviously a lot of questions on the strategic review. As you look at it today, has it taken longer than you thought? And if so, as you look back, why do you think so?

Bill Nuti - *NCR Corporation - Chairman, CEO and President*

For sure, it has taken a lot longer than we initially thought. And the reason is twofold. I mentioned these earlier. One is when you are a public company and you need to focus on running the business and running it responsibly, there is only so many hours in the day. And if you devote all of your time to a strategic review, you could take your eye off the ball and we will not let that happen. That's number one.

Number two, the depth of the analysis by alternative has been very comprehensive, more comprehensive than I initially thought, meaning we are going deeper, wider. We are viewing every alternative at a very comprehensive level. And I think in the end, that is the most responsible thing to do. So I would say yes, and for those reasons.

Kartik Mehta - *Northcoast Research - Analyst*

Thank you very much, I appreciate it.

Operator

Gil Luria, Wedbush Securities.

Gil Luria - *Wedbush Securities - Analyst*

Excluding Russia and China, what other countries do you feel have gotten worse in the last few months? And what currencies have been that incremental weight since you reported last time?

Bill Nuti - *NCR Corporation - Chairman, CEO and President*

It's Bill. First of all, I saw you in my office today on CNBC. You looked very handsome, I might add. (laughter)

Gil Luria - *Wedbush Securities - Analyst*

Thank you, I appreciate that. (laughter)

Bill Nuti - *NCR Corporation - Chairman, CEO and President*

And on this question, I'll ask Andy to answer that.

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

Yes, I think let me say a couple of things. First of all, the African nations in general have started -- we started to see some softness there. And I don't know if you caught my comments related to Russia and the fact that there is a lot of contracts we have in Russia on US dollar. It's the same thing with Africa where you might see anything from a 5% to a 12% FX impact there that if a distributor is buying a product from us in US dollars, all of a sudden the same product costs 5% to 12% more, makes it difficult for them to do business. So African nations we've seen softness there this year relative to prior year. And that has been the big one.

And I would say as we look out, while it has not been a material impact yet, we do believe there could be a little bit of softness ahead with a couple of the other BRICs as well down the road. But right now, I would say it's limited to more in Africa and to a smaller extent other parts of Asia.

Bob Fishman - *NCR Corporation - SVP, CFO and CAO*

This is Bob. On the current question, we saw for the full year $65 million more revenue headwind. About two thirds came from three currencies in Brazil, Canada and Australia. Brazil changed by roughly 24% from when we gave guidance in July. And then they were probably 40 currencies that all weakened versus the US dollar. So those with the three big ones. But then it was across the board on the remaining piece. (multiple speakers)

Bill Nuti - *NCR Corporation - Chairman, CEO and President*

The interesting thing is when you take out Russia and China, and you look at Andy's business, he actually grew orders in Q3 ex China and Russia by 5% FX neutral and grew revenue by 3% FX neutral. And so it gives you a sense of the impact of China and Russia this year so far.

Gil Luria - *Wedbush Securities - Analyst*

So let me first -- I wanted to ask Bob another question. Just again, for modeling, below the line, you changed three of the assumptions for the annual guidance -- the share count, the interest expense and the tax rate. Could you go through what are the changes that have happened in those lines to reduce them?

Bob Fishman - *NCR Corporation - SVP, CFO and CAO*

Yes, so previously for other increment expense we had guided [215 to 220]. We now think that number will be close to [204]. Interest expense is down. We also started the year from an OIE perspective building in a little bit more FX volatility on that particular line. And then we saw some favorability in just a couple of other areas around bank fees, as an example. That's why we were able to bring the other income and expense down to that 204 number.

On taxes, we continued to do a good job. We had guided originally to 25% but we now think we will be close to 24%, 25% in terms of the tax rate. And then on the share count, you make assumptions at the beginning of the year. We said [175]. It's looking like it's closer to [173]. And again, that includes a number of assumptions around forfeitures and etc.

Gil Luria - *Wedbush Securities - Analyst*

(multiple speakers)

Bob Fishman - *NCR Corporation - SVP, CFO and CAO*

So those three all help.

Gil Luria - *Wedbush Securities - Analyst*

Got it. Now I just want to circle back to the BRICs and ask, because you have so many feet on the Street in all these different countries, a little bit of the really high-level perspective about what your prospect is for those markets, for the emerging markets, especially the big ones. Is this -- are we looking at a multiyear slowdown after a few decades of growth? Or is this some hesitation or contagion from the Chinese stock market? How do you guys you the macro backdrop for the emerging market businesses that you have, given the specific insight that you have there?

Bill Nuti - *NCR Corporation - Chairman, CEO and President*

I think it is a little bit different by market. In China, to be successful long term, we are going to have to go in the direction that helps us to become more of a local player in the market. So if the regulatory environment does not change in China, and it could, we are going to have to figure out what our long-term strategic plan is around going local. And there are a variety of interesting alternatives there for us. But our goal, by the way, there would be certainly become more software-focused than hardware.

In Russia, it really is a macro and currency headwind that should, over time, abate. Now of course, they are very sensitive to the oil markets in terms of the impact on their economic growth. And clearly, relative to their relationship with the US, that can also feature prominently in our success.

However, my thinking there is that that market will see more stability over time for us than not. But they will have certainly been more challenged, given their macroeconomic situation. I think, for Brazil, we will have to wait and see environment. But they have experienced more of a slowdown there and India is a different market altogether.

I think all in, for us, it's very market-dependent -- I do not expect, by the way, 2016 to see as much of a drag on our revenue from Russia and China, simply because we begin to lap difficult compares by the middle of next year.

So Andy, you may want to give some more commentary on that point.

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

Yes, let me also just that one thing, and we think it's really important. When you look at the BRICs right now for us, they are largely not the places that we have driven the transformation agenda. And where that really shows up is on the gross margin operating income line in each of the four regions.

This year, in 2015, we will see a hit from an operating income perspective for those headwinds. But those should really abate next year and beyond, to Bill's point, even though the revenues may still have some challenges. I would say most of the margin dollars there are where the risks would be. The risk there is much lower on the margin dollar perspective than where the future revenue softness may land with each of the four markets. That is the other thing I would add that I think is really important as we assess the impact on operating income in the outer years here.

Gil Luria - *Wedbush Securities - Analyst*

Got it, thank you very much.

Operator

Matt Summerville, Alembic Global Advisors.

Matt Summerville - *Alembic Global Advisors - Analyst*

I want to talk just one more minute on the ATM business. If you looked at going from kind of a 4% to 6% kind of constant currency to up 1% to 2% comp currency, and you bear in mind that roughly half-ish of the business should be annuities like services, that is a really big reduction in the final quarter of the year if you will, or the final half of the year, relative to your 2Q guidance.

And the whole China and Russia thing is not necessarily quote new, in my view. And then you talked about an industry that is (technical difficulty) make sense of all that it would be extremely helpful. (multiple speakers)

Bob Fishman - *NCR Corporation - SVP, CFO and CAO*

Yes, good, so Matt, good question. Just so you know Matt, we did garble up a little bit at the end of the question, but I think I got the gist of it, which is that I think you're saying, A, in the fourth quarter how did you have a 300 to 400 basis point drop in revenue especially given that you've got a reasonable annuity stream. It's really the backlog conversion. I would say when we look at it, we planned a Q3 and Q4 for backlog conversion rates that were 500 basis points less than last year in both of the quarters, roughly. And where we are landing now is a 1,000 basis point reduction over prior-year period.

So, just to use some real math, and I will just use rough numbers here, in the third quarter we -- in the fourth quarter, where we are now landing, is called 50% to 55% of backlog conversions, a little lower in the third quarter and a little higher in the fourth quarter. So that 50% to 55% compares to last year's 60% to 65%. We had planned on being 500 basis points drop from last year, not 1,000 basis points drop. And 500 basis points call it on roughly $800 million of backlog is in the $40 million plus range per quarter. That is the drop.

We frankly did not do a good job with the modeling there. This outlook here is much more conservative and much more responsible and we planned expenses accordingly.

Matt Summerville - *Alembic Global Advisors - Analyst*

Got it. I appreciate the color. And then just one follow-up, getting back to the whole strategic side of things. I guess at some point you have to be able to kind of put a check in the box and say, this is viable, this isn't viable, this is viable, this isn't viable and so on and so forth. And I feel like we are right back where NCR was six to nine months ago, when some of that stuff started getting discussed, rumored, what have you. I guess, so what boxes have been checked or not checked? Or what opportunities actually appear viable from a strategic standpoint from here going forward?

Bill Nuti - *NCR Corporation - Chairman, CEO and President*

I think it is just too early to give you a check the box view. I think we think all of the options remain viable. And the Board of Directors is looking at them in concert with one another, and the optionality of one versus another in terms of what is best for our shareholders at NCR.

Matt Summerville - *Alembic Global Advisors - Analyst*

Is there a timeframe? You guys talk about having an analyst meeting in September. That sort of got canceled. I am not going to call it last minute, but not all that far in advance of the actual meaning, at least officially. I mean, when can we expect -- and I think there's a lot of folks sort of waiting for this -- when can we expect to hear something more definitive about where this Company goes from here from an inflection standpoint and strategically etc.?

Bill Nuti - *NCR Corporation - Chairman, CEO and President*

Well, I think once the strategic process is completed and we have something of note to say, other than continuing to execute to our plan and execute to our guidance, we will have an investor meeting. But I would tell you that right now, it will either be in Q4 or Q1 is my estimation right now.

Matt Summerville - *Alembic Global Advisors - Analyst*

Great, thanks a lot, guys.

Operator

Prasad Borra, Goldman Sachs.

Prasad Borra - *Goldman Sachs - Analyst*

Probably if we just focus on the free cash flow generation, now you are talking about incremental restructuring measures. Given what you have gone through, in terms of the process and probably had a backup view on which are the elements of the business which can be improved, would you say that there are some additional tailwinds or benefits you can see from a free cash flow perspective which could offset some of the impact from additional restructuring costs?

Bob Fishman - *NCR Corporation - SVP, CFO and CAO*

Yes, without a doubt. We are very focused on the savings that those additional restructuring initiatives, which would drive. So my view is that I would not expect a negative impact in 2016. If anything, we will see incremental free cash flow associated with the restructuring.

Prasad Borra - *Goldman Sachs - Analyst*

Okay, and Bill, you mentioned a lot of new learnings you had probably living the data a lot more, probably getting the [composing] experience which you have probably not explored before. What are the key takings from it? Operationally, what can you do better? And also in terms of probably setting the guidance, are there any lessons to take? Would you be more willing to be conservative in terms of giving guidance and anything you can say from that perspective?

Bill Nuti - *NCR Corporation - Chairman, CEO and President*

I think what we've learned is that we can be a bit more focused on resource allocation and a bit more aggressive on resource allocation where we see higher growth and higher margin expansion. That would be point 1.

Point 2, that we have some amount of inefficiency and level of underproductiveness in certain aspects of the Company that we can go to work on. And I know overall, that our cost structure can be a bit more competitive going forward while driving the kind of growth and bottom line expansion and cash flow that we think we can drive. In terms of guidance, we are meeting our guidance this year. I think we are doing a good job in terms of setting guidance.

On that point, I might add one other thing Bob and I are proud of is the fact that since we gave NPOI guidance in February, we've seen about $20 million to $25 million more of NPOI headwind as a result of FX and we did not take guidance down to [$805 million to $845 million], in that range, to reflect the additional headwinds of ethics. We stuck with our guidance. And we are proud of the fact that we can navigate us through those headwinds and make our guidance.

Prasad Borra - *Goldman Sachs - Analyst*

Okay, thank you.

Operator

At this time, I would like to turn the call back over to Bill Nuti for any additional or closing remarks.

Bill Nuti - *NCR Corporation - Chairman, CEO and President*

Thank you all for joining us and we appreciate the questions as always. We look forward to being in contact with you. If something were to change within the quarter, we will certainly be in contact with you, but otherwise we will look forward to talking to you again in Q1. Good night.

Operator

This does conclude today's conference. We thank you for your participation.
