Hewlett Packard Company

Fourth Quarter 2015 Earnings Conference Call

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CORPORATE PARTICIPANTS

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PRESENTATION

Operator
Good afternoon and welcome to the Fourth Quarter 2015 Hewlett Packard Company Earnings Conference Call. My name is Amy and I'll be your conference moderator for today's call. At this time, all participants will be in listen-only mode. We will be facilitating a question and answer session towards the end of the call. To enter the question queue, please press "*" then "1" on your touchtone phone, to withdraw your question, please press "*" then "2." Should you need assistance during the call, please signal a conference specialist by pressing the "*" key followed by "0." As a reminder, this conference is being recorded for replay purposes.

I would now like to turn the presentation over to your host for today's call, Ms. Diana Sroka, HP Inc., Investor Relations. Please proceed.

Diana Sroka
Good afternoon. I'm Diana Sroka, Head of Investor Relations for HP Inc., and I'd like to welcome you to the fiscal 2015 fourth quarter earnings conference call.

Given we operated as a combined company through the fourth quarter of fiscal 2015, we decided to report our results together today. Going forward, starting with Q1 fiscal 16, Hewlett Packard Enterprise and HP Inc., will report earnings as separate companies. I will outline how the call will flow today since it will be a little different then our typical earnings calls.

Meg will kick things off with Q4 highlights for Hewlett Packard Company and Cathie will follow with additional details. After that, Meg and Tim will review segment results and outlook for Hewlett Packard Enterprise. Then Dion and Cathie will review segment results and outlook for HP Inc. Finally, we will open it up to questions.

Before we begin, let me remind you that this call is being webcast. A replay of the webcast will be made available shortly after the call for approximately one year.

We posted the earnings release and the slide presentation accompanying today's earnings release on our HP Inc.'s Investor Relations webpage at www.hp.com and on Hewlett Packard Enterprise's Investor Relations webpage at www.hpe.com. As always, elements of this presentation are forward-looking and are based on our best view of the world and our businesses as we see them today.

For more detailed information, please see the disclaimers on the earnings materials relating to forward-looking statements that involve risks, uncertainties and assumptions. For a discussion of some of these risks, uncertainties and assumptions please refer to Hewlett-Packard Company's SEC reports including its most recent Form 10-Q. Hewlett-Packard Company's assumes no obligation and does not intend to update any such forward-looking statements.

We also note that the financial information discussed on this call reflects estimates based on information available at this time and could differ materially from the amounts ultimately reported in HP Inc.'s and Hewlett Packard Enterprise's annual report on Form 10-K for the fiscal year ended October 31, 2015.

For financial information that has been expressed on a non-GAAP basis, we've included reconciliations to the comparable GAAP information. Please refer to the tables and slide presentation accompanying today's earnings release.

Finally, each of the unaudited pro forma Hewlett Packard Enterprise and HP Inc. fiscal 2015 non-GAAP diluted net earnings per share and cash flow information presented in this call and the accompanying presentation is based on the estimated contributions of each company to Hewlett-Packard Company's fiscal 2015 non-GAAP diluted net EPS and cash flow as adjusted to give effect to the separation transaction effective on November 1, 2015. The pro forma amounts do not necessarily reflect that the fiscal 2015 non-GAAP diluted net EPS and cash flow of Hewlett Packard Enterprise or HP Inc. would have been had the separation occurred on November 1, 2014. They also may not be useful in predicting the future financial condition and results of operations of the separate companies. The actual financial positions and results of operations may differ significantly from the pro forma amounts reflected herein due to a variety of factors.

With that, let me turn it over to Meg.

Meg Whitman
Good afternoon, everyone. Thanks for joining us today.

The fourth quarter was the final quarter where Hewlett Packard operated as one combined company.

On November 1st, we completed the historic separation and became two separate independent public companies, HP Inc., and Hewlett Packard Enterprise. I couldn't be prouder of how we executed on the incredibly complex separation. Throughout the year-long separation process, we saw no disruption to our customers and partners and we continued to drive the business forward.

And now both companies are off and running. Each company has a clear, well-defined strategy and is well-positioned to win in its respective market.

Before we get into the business segment performance and outlook, I'll let Cathie provide details on the Q4 results of the previously combined company.

Cathie Lesjak
Thanks, Meg.

Hewlett Packard Company net revenue for the quarter was $25.7 billion, down 9% year-over-year as reported or down 3% in constant currency. For the full year, revenue was $103.4 billion, down 7% year-over-year as reported or down 2% in constant currency.

Gross margin was 24.7%, up 0.1 point year-over-year and up 0.9 points quarter-over-quarter with sequential improvements across all of our major business segments. Non-GAAP operating expenses of $4 billion were down 5% year-over-year driven by a reduction in SG&A partially offset by our continued focus on increasing our R&D investments. Non-GAAP operating profit margin was 9.1%, down 0.5 points year-over-year and up 0.5 points sequentially.

With the net expense of $151 million in OI&E, a non-GAAP tax rate of 22.5% and a diluted share count of approximately 1.8 billion shares, we delivered non-GAAP diluted net earnings per share of $0.93 in Q4, within our outlook range. Q4 non-GAAP EPS primarily excludes pre-tax charges of $676 million for separation, $591 million for restructuring, $246 million for amortization of intangible assets and net tax benefits of $803 million.

For the full year, we delivered non-GAAP diluted net earnings per share of $3.59, in line with our previously provided outlook range.

On a GAAP basis, Q4 diluted net earnings per share was $0.73, above our outlook range due to the net tax benefits just mentioned. These were one-time, non-cash entries comprising a number of different items, including the reversal of a previously recorded U.S. tax valuation allowance that I discussed on the Q3 earnings call.

The total separation costs, CAPEX, and associated cash flows expected across FY15 and FY16 in total were originally $2.8 billion, and we now expect $2.4 billion in that same time period. The mix of expenses between one-time separation costs, CAPEX, and incremental taxes was different than planned, with taxes coming in well under our plans in Q4. The 2012 restructuring program is nearly complete with approximately 4,300 people exiting the company in Q415 and just under 56,000 cumulative reductions for the program to date. Even with labor migration, we are down a net 59,000 people over this timeframe.

In Q4, we recorded GAAP only charges of $591 million, approximately $200 million were the final charges associated with the 2012 program and the remainder were associated with the new restructuring program that each company discussed at their respective Security Analyst Meetings in September.

We delivered cash flow from operations of $2.6 billion and free cash flow of $1.8 billion in the quarter. This brings our total free cash flow for the year to $3.3 billion, which is just below our outlook range of $3.5 billion to $4 billion. There was a tailwind from separation costs coming in lower as described. This was more than offset by the following: other receivables including VAT, elevated financing receivables driven by higher HP Financial Services volume, cash outflow for restructuring, and lower earnings.

In Q4, we returned $638 million of capital to shareholders in dividends and share repurchases and $4.1 billion was returned to shareholders for the full year. We returned over 100% of free cash flow to our shareholders in fiscal 15 even excluding the capital return of $750 million that completed our 2014 commitment.

I’ll now turn it over to Meg and Tim to discuss the results of the segments that are now part of Hewlett Packard Enterprise. Then Dion and I will return to share comments on Printing and Personal Systems, the new HP Inc.

Meg Whitman
Thanks, Cathie. As we laid out at our Security Analyst Meeting in September, Hewlett Packard Enterprise has five key priorities for FY 16. We plan to grow top-line revenue in constant currency, drive a year-over-year increase in operating profit, grow free cash flow, continue to execute our innovation roadmap, and stabilize revenue and expand margins in Enterprise Services.

And I'm pleased to say that overall, Hewlett Packard Enterprise is off to a very strong start. First and foremost, the segments that comprise HPE have now had two consecutive quarters of constant currency revenue growth and we believe we are in a strong position to deliver on our plans to grow overall in FY 16 in constant currency.

Also while there is more work to do, particularly in ES, our cost structure is much closer to where it needs to be, thanks to aggressive supply chain management, SKU rationalization and workforce rebalancing.

With respect to cash, we are starting the year with a net cash position at the operating company level and as separation costs wind down, we are well-positioned to increase cash flow in FY 16. The innovation we've been investing in over the past four years is paying off. We've introduced breakthrough new solutions and services that have driven a mix shift in our portfolio towards higher growth products and services. By leaning into new technology, we are ideally positioned to take advantage of market trends that will allow us to continue to take share from our competitors and to drive long-term growth.

Finally, while each business segment faces different challenges and opportunities, the company as a whole is aligning tightly around the four customer transformation areas we discussed at our Security Analyst Meeting. Customers tell us our focus is spot on. I'm confident that our clear strategy will accelerate the significant progress we've already made in our financial performance.

Now, before Tim gets into the financial details, let me provide some highlights from the quarter across each segment.

In Enterprise Group, we performed exceptionally well with strong revenue growth, up 2% as reported or 9% in constant currency, and improved profitability on a sequential basis.

Our industry standard server business was strong with constant currency revenue growth across all regions, driven by solid core growth and increasing demand from tier 1 service providers. Looking forward, we are well positioned to benefit from the server market upswing driven by the growth in cloud and big data.

The networking business also performed well with the Aruba acquisition driving strong cross-selling opportunities across wireless and data center switching.

Storage significantly outpaced the market and we expect that we gained close to a point of share in the third calendar quarter. Our 3PAR All-Flash portfolio is outperforming the competition. 3PAR All-Flash is now a $500 million annualized run rate business and grew triple digits in the fourth quarter. That's larger and growing faster than Pure in their most recently reported quarter. In fact, just last week, Gartner rated 3PAR as the best storage product on the market across every use-case category. This is a powerful recommendation to our customers and partners and will help us continue to drive share gains against our competitors.

Finally, in Technology Services, we continue to see a growing proportion of the business come from high-value services like Proactive Care and Data Center Care while operating margins remained steady.

Turning to Enterprise Services, we had the best performance in Q4 that we've had in years due to a more diversified customer base, stabilized constant currency revenue growth and a significantly reduced cost structure. Revenue declined 2% in constant currency although we grew new logos and saw double-digit growth in strategic Enterprise Services, driven by strength in Helion cloud and security services.

Operating profit was 8% in the quarter, the best performance since 2011. For the full year, both revenue and operating margins were in the range of our outlook. Looking ahead, we have a clear plan in place to get to a longer term sustainable target operating margin of 7 to 9%.

In Software, we delivered strong margins while continuing to take steps to align the portfolio and the go-to-market approach with the four transformation areas. Revenue declined 2% year-over-year in constant currency or flat if you normalize for recent M&A transactions on a pro forma basis. During the quarter, we announced several transactions including the sale of TippingPoint and LiveVault, which will allow us to focus our resources and investments in higher growth strategic businesses.

Finally, our Financial Services business continues to be a differentiator for the company. Hewlett Packard Enterprise Financial Services helps customers by creating consumption-based models to buy new technology or financing programs to transition out of legacy systems. Total FY 15 financing volume increased 9% year-over-year in constant currency.

As I have said before, HPE's innovation engine is humming, and Q4 was no exception. During the quarter, we introduced important new solutions and continue to see strong customer traction across the portfolio. For example, in September, we announced several new security solutions to help customers quickly detect high-risk threats, reduce data breach impact and enhance overall security. We also won several significant new security deals in the quarter, including new wins for our Voltage and Fortify solutions with a major financial services company.

In Enterprise Services, we announced a significant new partnership with Microsoft and HP Inc., to enable Windows 10 adoption and drive employee mobility for the enterprise. As part of the agreement, we will build and sell industry-specific business applications for Windows 10 across key industries, such as retail, energy and transportation. This agreement is a great example of how Hewlett Packard Enterprise and HP Inc. will work together going forward.

In servers, we saw continued strong customer momentum with our leading portfolio of Apollo high-performance compute solutions. We are the clear market leader in high-performance computing and today, more than a third of the market is leveraging HPE compute platforms to process, analyze, and manage data securely.

Cloud is another important growth driver for us, and we saw strong momentum in the quarter. We are the leading cloud infrastructure provider and we see a significant opportunity as enterprises move to a hybrid cloud environment.

In late October, we announced HP Helion OpenStack 2.0, our latest enterprise-grade cloud platform with new lifecycle management and security enhancements. We believe strongly in open standards, and our OpenStack based cloud offerings provide the open, agile and secure hybrid cloud environment our customers are asking for.

We also refined our cloud strategy during the quarter. Our goal is to help customers source, manage, and consume services across traditional, private, public, and managed cloud environments. To that end, we announced in October that we will double down on our private and managed cloud capabilities and sunset our public cloud offering. This is the right move. It plays to our strengths in private and managed cloud. We will continue to extend our cloud infrastructure leadership and integrate the public cloud element for our customers through a strategic, partner-based model.

In line with that approach, we reached an agreement with Microsoft that you'll hear more about during Discover next week. Microsoft shares our view of a hybrid IT approach for enterprises and we both see opportunity to simplify hybrid infrastructure for our customers. Going forward, Microsoft Azure will become a preferred public cloud partner. HPE will serve as a preferred provider of Microsoft's infrastructure and services for its hybrid cloud offerings. Overall, the move to a hybrid cloud environment presents a significant growth opportunity for us and you can expect to hear more about our approach in coming months.

And on that note, I will hand the call over to Tim Stonesifer.

Tim Stonesifer
Thanks, Meg. Hewlett Packard Enterprise finished the year on a strong note, and we are already executing against the financial architecture we laid out at our Securities Analyst Meeting. This calls for solid growth from EG with stable to slightly up margins; stabilizing revenue in ES with strong margin expansion; stabilizing software revenue with good profitability; all while leveraging financial services with their good return on equity.

In Q4, our segments collectively delivered revenue of $14.1 billion, which was up 3% year-over-year in constant currency. This marks the second quarter in a row of delivering year-over-year constant currency growth, and we expect to take share in x86 servers, storage and networking during the third calendar quarter.

For the full fiscal year 2015, we estimate HPE's contribution to HP's total non-GAAP diluted earnings per share to be $1.84, in the middle of the previously provided outlook. Similarly, we estimate HPE's contribution to HP's total free cash flow for the year to be $1 billion, just below the previously provided outlook. We benefited from a push-out of separation costs that was offset primarily by the timing of value-added tax receivables and restructuring payments, along with the higher financing receivables that Cathie mentioned in her remarks.

Now turning to the segments.

The Enterprise Group continued its strong momentum, growing revenue 2% year-over-year or 9% in constant currency. Operating profit improved sequentially by 1 point to 14%, and was down 0.8 points year-over-year, primarily due to currency.

Industry Standard Servers grew 5% year-over-year, or 13% in constant currency, and was up across all geographies in constant currency. The work we have done segmenting the market and delivering innovative products has enabled us to capture more than our fair share of this strong market. We expect server momentum to continue next year but at a moderated pace to give a more difficult comparison.

Business Critical Systems declined 8% year-over-year, but only 2% in constant currency. This was our strongest year-over-year revenue growth in over three years as our mission critical x86 and nonstop platforms offset the challenges from Itanium.

Storage declined 7%, but was flat in constant currency, significantly outperforming the market. Converged Storage grew 17% in constant currency and was 53% of the portfolio. We are now seeing our R&D investments payoff with exceptional growth in all-flash, which has taking over 10 points of share in the last year. We expect the improving mix of Converged Storage to drive overall growth in fiscal year 2016 at improved margins and with better TS attach.

Networking grew 35% year-over-year or 43% in constant currency, and grew high-single digits in constant currency excluding Aruba. The recent strategic moves we've made are already yielding results. The Aruba acquisition is driving incremental opportunities from the campus wireless refresh and we've returned to growth in China following the announcement of our partnership with Tsinghua. We expect to close the Tsinghua transaction in Q1.

TS declined 11% or 4% in constant currency, impacted by a tough compare in consulting from the prior year. Order growth was flat year-over-year in local currency, lighter than expected. This was partially due to customers in China waiting for the Tsinghua transaction to close before signing new multi-year support contracts. Additionally, we had a higher mix of tier 1 service provider growth in servers that attach little support. We are addressing these issues with more value-added services, like proactive care and datacenter care, that are increasing our support attach dollars on a per unit basis.

For the full-year, orders were up 1% in local currency and TS continues to be on track for flat constant currency revenue in fiscal year 16.

In Enterprise Services, revenue declined 9% year-over-year or 2% in constant currency, and was flat when you exclude the top three account runoff. For full fiscal 2015, we saw total bookings growth driven by new logo signings and solid renewals. Our cost actions also delivered strong margin expansion. Profitability was up 1.4 points year-over-year to 8.2% for the quarter, the highest it's been since the second quarter of 2011.

Infrastructure Technology Outsourcing was down 11% year-over-year or down 4% in constant currency. We saw encouraging constant currency growth in EMEA, which was previously our most challenged region.

Application and Business Services was down 5% year-over-year, but grew 1% in constant currency, our strongest constant currency result in over three years. This result is especially encouraging since ABS carries the highest operating margins within ES.

In Software, revenue declined 7% year-over-year or 2% in constant currency, and was flat when normalized for acquisitions on a pro forma basis and divestitures. The team continued to focus on disciplined cost controls, achieving operating margins of 30.1%, down 1.3 points year-over-year due mostly to currency. We enjoyed good revenue growth in security and double-digit revenue growth in big data year-over-year in constant currency when adjusted for acquisitions on a pro forma basis and divestitures. In particular, license revenue for Vertica increased in excess of 50% year-over-year, driven by several large wins in North America. SaaS also grew year-over-year in constant currency and in each business when normalized for acquisitions on a pro forma basis and divestitures.

Going forward, we expect better alignment with the Enterprise Group and Enterprise Services to improve cross-selling opportunities. However, we also continue to expect pressure on the top line, as we evolve our go-to-market efforts towards SaaS and subscription-based offerings.

In Financial Services, revenue declined 11% year-over-year or 4% in constant currency with operating profit declining 1.3 points to 11%. The challenges to both revenue and profitability were entirely due to unfavorable currency and a tough compare. Financing is playing an increasingly strategic role for our customers with volume up 9% in constant currency during fiscal year 2015. Financing volume is a good indicator of future revenue performance. The return on equity remained healthy at 16.4%.

With that, let's turn to the outlook.

On the top line, we expect the momentum of Q3 and Q4 constant currency revenue growth to continue through fiscal year 16. The currency environment continues to be volatile and based on current rates we expect a 3 point headwind to revenue in fiscal year 16.

Before I give our EPS outlook, let me provide some guidance for earning seasonality at the new Hewlett Packard Enterprise. In general, EPS will be backend loaded for a few reasons. First, both Enterprise Services and Software margins normally expand throughout the year from a low in Q1. Second, the benefits we receive from restructuring will continue ramping over time; and finally, the negative impact from dissynergies will decline throughout the year.

With that in mind, we expect non-GAAP diluted net earnings per share to be $0.37 to $0.41 in the first quarter of 2016 and continue to expect full year fiscal 2016 non-GAAP diluted net earnings per share of $1.85 to $1.95. We expect GAAP diluted net earnings per share to be $0.09 to $0.13 in Q1 of 2016 and continue to expect full year fiscal 2016 GAAP diluted net earnings per share of $0.75 to $0.85. We continue to expect free cash flow of $2 [billion] to $2.2 billion for the full year. However, please keep in mind that cash flow is seasonally lowest in the first quarter and in fiscal year ‘16 it will also be impacted by the majority of the remaining separation payments.

Finally, for capital allocation, earlier this month we announced our Q1 dividend of 5.5 cents per share in line with our commitment to distribute approximately $400 million in the form of dividends in fiscal year ‘16. We remain committed to returning at least 50% of our free cash flow for the full year to shareholders in the form of share repurchases and dividends.

In closing, let me say that I am pleased with the progress we are making against the five key priorities we discussed at our Securities Analyst Meeting. The business has momentum and our financial architecture continues to strengthen. In short, I am excited about our prospects and the future of Hewlett Packard Enterprise.

So with that, I’ll turn it over to Dion.

Dion Weisler

Thank you, Tim. The Printing and Personal Systems markets are experiencing challenges right now. As we discussed on the Q3 earnings call and in more detail at the Security Analyst Meeting, we expected to have several tough quarters, and Q4 was indeed a difficult quarter and somewhat weaker than we expected.

Following separation, we remain confident that we are well-positioned for the long-term in the marketplace. The market challenges do not intimidate us and we are keenly aware of what we need to be focused on going forward.

Turning to the results, overall, in Q4 our business performance was mixed. In Personal Systems, we executed well against the expected tough market backdrop, while Printing represented a much greater challenge due to a number of factors that have changed our near-term view of the market and the supplies revenue trajectory.

Before I go into those details on Printing, let me briefly reflect on the Q4 results for Personal Systems. The PC market continued to be tough, especially in consumer where industry channel inventory remained elevated in the market. While we saw improved performance in the U.S., EMEA remained weak with market units declining 22% year-over-year in the third calendar quarter, as we foreshadowed at the Security Analyst Meeting. As I have said in the past, where markets are down, our ability to outperform the market profitably is key. HP gained unit share in calendar third quarter in each of our three regions, achieving 19.7% market share worldwide. We continue to extend our lead in the market with commercial PC share of 23.7%, our highest share position ever, and we managed to do this all while improving Personal Systems operating profit by eight-tenths of a point sequentially to 3.8%.

We believe that innovation and sprinkles of magic are key to differentiation as the PC market goes through consolidation. In Q4, we introduced a robust portfolio of enterprise-class and consumer PCs with a number of form factors and industry firsts. And we announced a partnership with Disney and Lucas Films around *Star Wars: The Force Awakens*, delighting our customers with the launch of our Star Wars Special Edition Notebook PC.

Looking ahead, we expect the PC market to remain challenged for more quarters to come. As expected, Windows 10 has not been a material catalyst for sales yet, but continues to receive favorable reviews. We see the most adoption in the U.S. retail segment and our share here is very strong. We maintain that this new operating system is important for the industry and a contributing factor to support a future hardware refresh cycle.

Turning to Printing, we saw accelerated revenue declines across hardware and supplies and there have been a couple of factors that have changed since the Security Analyst Meeting.

The most significant factor was the continued effects of currency movements that have accelerated pricing pressures even more than we expected in certain profitable segments of the printing markets.

Secondly, the market was somewhat weaker than we expected in the calendar third quarter.

And you are seeing this in our results and you saw it in the results of some of our peers, some of whom have announced their intention to reevaluate strategic options. We do not expect the landscape to improve in the near future and we will constantly assess how the market evolves. In any case, our market leadership and scale serve us well, but we have much more work to do on many dimensions.

Specifically, in hardware, we saw a 17% year-over-year unit decline due to three factors.

Firstly, the hardware market continued to contract with calendar third quarter total units down 6% year-over-year, down more than we expected.

Secondly, pressuring the unit performance was a planned channel inventory reduction. We consciously elevated inventory levels in Q3 in advance of the IT system cutover as part of our separation-related continuity planning. The good news is that with the reduction in Q4, the hardware channel inventory is now within the desired range as we finish the year. So approximately three quarters of the unit decline is linked to the market and channel inventory reduction.

Thirdly, with the market down more than expected, the competitive pricing environment was even more challenging in certain profitable segments where usage is high.

Let me take a moment to outline the impact currency is having on the pricing dynamics in the market. We have seen further reduction in average unit prices in key segments. Our competitors have leveraged currency advantages to drive down pricing and we have responded in kind. This has changed the price points for certain units and means that some units in specific markets were no longer NPV positive, and as we said we would do, we have responsibly been going after profitable share gains and walking away from negative NPV hardware unit deals.

Another consequence of lower average unit price points is that we are attracting buyers that may have different usage patterns than we originally targeted. For example, the pricing of some the Officejet Pro hardware has fallen into price bands that are within reach of home users who typically print less. The unintended result is that we are not getting the yield per unit we would have expected on some of these units.

We see this impacting our supplies revenue trajectory. Q4 15 supplies revenue was not where we expected it to be and we have more work to do. We will accelerate initiatives across all the levers we pull to improve the supplies revenue trajectory. Examples of these initiatives include driving programs to increase ink usage and to increase aftermarket supply share. On ink usage, we expect to accelerate our Instant Ink subscription service with programs that increase our attach rate. In Q4, one of the programs was to expand the number of models and therefore, price points that Instant Ink addresses, ensuring more customers never run out of ink.

We are confident that the fundamentals of the Four Box Model are sound. We believe all of these actions will help improve the trajectory of supplies revenue over time. However, given the unit declines and change in usage patterns the data from our Four Box Model is indicating that we expect the stabilization in ink supplies revenue to be delayed towards the end of 2017 as we drive these initiatives.

We are moving quickly on three vectors.

We remain focused on solutioning the $1 billion of productivity improvements we laid out at the Security Analyst Meeting.

Secondly, we can't compete on price alone, so we are balancing our pricing actions with increased marketing and sales activity to stimulate demand.

And finally, we have to materially change our non-revenue generating cost structure to compete aggressively. This may both accelerate and increase the previously announced restructuring actions.

In closing, we firmly believe in our strategy around core growth in the future as outlined at the Security Analyst Meeting. Let me remind you, we are still the leader in large, consolidating markets. We have scale, innovation, channel reach, and an incredible brand. While the markets are challenging now, we believe the actions we are taking now will protect the core that generates the majority of our cash flow. And of course, we will continue to invest in adjacent market opportunities and our future.

I will now turn it over to Cathie who can provide additional details and our financial outlook.

Cathie Lesjak

Thank you, Dion. Printing net revenue was down 14% year-over-year as reported or down 9% in constant currency. As expected, the year-over-year currency impact was greater than past quarters as favorable long-dated financial hedges matured. From a channel inventory perspective, we have reduced both hardware and supplies levels year-over-year and sequentially, but we are still slightly above target weeks of supply range for supplies. Supplies revenue was down 10% year-over-year as reported or down 5% in constant currency and was 65% of the revenue mix in the quarter.

We had some bright spots in the quarter, including constant currency revenue growth in Graphics. Also Managed Print Services revenue grew double-digits in constant currency year-over-year in Q4, and for fiscal '15, we saw strong growth both as reported and in constant currency in total contract value for our partner MPS offering.

From an operating profit perspective, we delivered 17.4%, down 0.8 points year-over-year. Currency headwinds and competitive pricing were only partially offset by strong supplies mix.

Turning to Personal Systems, revenue was down 14% year-over-year as reported, or down 7% in constant currency. Consumer and Commercial PC units were each down year-over-year, but we outperformed the market in calendar Q3, gaining 0.3 points of share in Consumer and 1.6 points of share in Commercial.

We've done a lot of work to drive to a variable cost structure, which supports our profitability in these down quarters.

Personal Systems operating profit improved sequentially to 3.8% on the strength of gross margins but was down 0.2 points year-over-year as a result of reduced operating expense leverage on lower volumes, despite OPEX reductions and improved gross margins. Gaining cost efficiencies will position us well as the market slowly recovers.

Considering the combined performance of the Printing and Personal Systems segments in the context of the overall Hewlett Packard Company results, we estimate our pro forma contribution to the non-GAAP EPS results for fiscal '15 to be about $0.01 below the baseline range provided at the Security Analyst Meeting. Our pro forma free cash flow contribution to the company was approximately $2.3 billion for fiscal '15, within the range we outlined at the Security Analyst Meeting.

Turning to the financial outlook, beginning in Q1 16, the new HP Inc. will make a reporting change related to pension. For the last several years, we've had pension income. Our pension liabilities and assets are revalued each October 31st based on interest rates and asset values on that day. This can drive non-operational volatility in our pension income from year-to-year. For FY 16, this volatility causes a year-over-year decrease in pension income of approximately $90 million, and we don't expect this to have an impact to FY 16 cash flow. Without a change in reporting method, however, this headwind would have put incremental pressure on our investments, and sub-optimizing our business for non-operational impacts is not in our best long term interest. Specifically, the change relates to the expected performance of the plan assets and interest rate movements, the market related factors in determining pension income or expense. We will exclude these market-related factors from the non-GAAP operational results going forward. With this reporting change, the service costs associated with our pension plan and the amortization of prior service costs will continue to be reported as operational expenses within our non-GAAP results. For more information, please refer to the Investor Relations earnings presentation, which includes a few slides detailing the change. We believe that going forward, this reporting change provides greater transparency to underlying operating results. However, the reporting change will result in a reduction of our non-GAAP EPS outlook, given we will now exclude our non-operational pension income.

Moving to revenue, as discussed at the Security Analyst Meeting, we expect year-over-year constant currency declines to moderate, but currency will continue to be a headwind to revenue of about 3 to 4 points in FY 16. Since then, net currency moves have been unfavorable and we see only incremental pressure to both revenue and operating profit year-over-year. Our non-GAAP tax rate is expected to be about a point lower than the 22 to 23% range provided at the Security Analyst Meeting given the pension reporting change noted. For Q1 specifically, keep the following things in mind.

The Personal Systems and Printing markets continue to be tough.

Supplies revenue will continue to be under pressure as we reduce supplies channel inventory and the supplies revenue trajectory improvement will take longer.

Given the pricing dynamics Dion laid out, we expect printer units to be down double-digits year-over-year as we continue to focus on possible unit placement.

And finally, productivity improvements are expected to ramp throughout the year. Considering these factors, we expect the first half operating profit to be lower than our typical in-year seasonality.

With all that in mind, the HP Inc., Q1 16 non-GAAP net earnings per share outlook is in the range of $0.33 to $0.38, inclusive of the pension reporting change. Our full year fiscal ‘16 non-GAAP net earnings per share outlook is in the range of $1.59 to $1.69. Operationally, our non-GAAP EPS outlook is unchanged but with the exclusion of non-operating pension income, there is a reduction of $0.08 in fiscal ‘16 as compared to what we provided at the Security Analyst Meeting. On a GAAP basis, Q1 16 GAAP net earnings per share outlook range is $0.27 to $0.32 and our full year FY 16 GAAP net earnings per share outlook range is $1.50 to $1.60.

The reduction in the full-year GAAP EPS outlook of $0.05 in fiscal ‘16 from what we provided at Security Analyst Meeting is associated with the following: $0.03 for lower pension income as a result of the revaluation of pension assets and liabilities as of October 31, 2015; and $0.02 is associated with the amortization of intangibles related to the marketing optimization shift to HP Inc. and the separation charges that move from FY 15 to FY 16. For FY 16, we expect our normalized free cash flow to be in the range of $2.9 [billion] to $3.2 billion, consistent with the discussion at the Security Analyst Meeting. However, we are adjusting our free cash flow outlook to a range of $2.4 [billion] to $2.7 billion, down $100 million due to separation payments that slipped from FY 15.

Finally, for capital allocation, we announced earlier this month that we will be paying a dividend of 12.4 cents per share in fiscal ‘16. We remain committed to a total capital return to shareholders for the full year to be at the high end of our overall framework of 50% to 75% of free cash flow. We expect that share repurchases will drive a moderate decline in weighted average shares outstanding beginning in Q1.

With that, let's open it up for questions.

QUESTION AND ANSWER

Operator
We will now begin the question and answer session. As a reminder, to ask a question, please press "*" then "1" on your touchtone phone. To withdraw your question, please press "*" then "2". If you are using a speakerphone, please pickup your handset before asking your question. We request that you only ask one question and one follow-up question.

Our first question is from Katy Huberty of Morgan Stanley.

Katy Huberty
Yes, thanks. Good afternoon. It sounds like some of the businesses, printers in particular, deteriorated as you moved through the quarter and yet DSOs are up three days year-on-year. So can you talk about linearity and just the overall tone of business as you exit at the quarter? And then, I have a follow-up.

Cathie Lesjak
So at the Personal Systems and Printing side of the house, so PPS because we don't have HP Inc., today, at the PPS level, our cash conversion cycle actually was a bit better than what we had laid out for you at the Security Analyst Meeting. And so, from our perspective, we performed very well with respect to working capital.

Katy Huberty
And then, on the enterprise side of the business, how did linearity look versus normal?

Tim Stonesifer
Sure, I mean, as we spoke about at the analyst meeting in 3Q, we had about 30 days and that was a little bit elevated given by the fact of our business continuity plans that we have in place. So as we had anticipated, we have worked those down, and we are sort of in the mid-20s range, and that's what I would think about as you think about 2016.

Katy Huberty
Okay. And then Dion, you mentioned that some of your peers in printing are going through strategic reviews that I imagine, that may over time open up competitive opportunity. But curious, whether you have interest in the near term at looking at any assets, not mentioning any in particular, but looking at some of those assets that may come for sale and driving scale in the printing business? Thanks.

Dion Weisler
Yes, thanks, Katy. Look, obviously as a matter of policy, we don't comment on those sorts of matters, but our general approach to M&A has not changed since we had the discussion at the Security Analyst Meeting. We will continue to look for opportunities that are complementary to our strategy. They will always be returned-based in nature. They will be thoughtful and disciplined and they will land clearly and squarely on the strategy page, so they will be in our core across growth and in the future. Areas that we have talked about have been in the areas of 3D print and material specifically around document workflow solutions, sprinkles of magic, but generally not broadly consolidation plays for consolidation sake.

Cathie Lesjak
So we did talk — let me just add — we did talk a little bit about the fact that there could be some very specific markets in some specific countries that could be of interest to us, as long as it was

kind of in the core areas of emphasis, especially on the Personal System side around Commercial.

Dion Weisler
I would add Katy that obviously there is a lot changing in the market, even since the Security Analyst Meeting on both the Personal System side with Dell EMC, as well as Xerox and Lexmark that present particular opportunities. And as they evaluate their strategic options, I think customers are generally fairly confused and worried, and we are the pillar of stability right now, and we are going to take full advantage of that.

Katy Huberty
Great, thank you.

Diana Sroka
Great, next question.

Operator
Next question is from Maynard Um at Wells Fargo.

Maynard Um
Hi. Thanks, on the HP Inc. side, Lenovo talked about getting more aggressive to take advantage of the disruption both from the split (your split) and Dell's acquisition of EMC – I presume on both PCs and servers. So I am wondering if you are already seeing that, and that's what you are referring to in terms of the competitive environment, or if that's something that you haven't seen and are expecting. Can you just kind of walk through that?

Dion Weisler
I would say, generally speaking, the PC market continues to be tough and consolidation continues to happen. The big four are getting bigger; they are now sort of 62.5% of the total overall market and growing. And I think we've been pretty predictable over the course of the last two years not taking share for share's sake. We did grow in all three regions to 19.7% overall. Commercial share we grew to 23.7%, and that was our highest ever share position. So we remain very disciplined. We walked away from some sizeable Black Friday deals that were not very high calorie, or in fact negative calorie. So I think we continued to execute as we said we would, we continue to segment the market, drive to where the heat is in the market, drive cost out, make sure our channel inventory and particularly aged inventory is well under control. And as we did that, we saw profit margin expansion eight-tenths of a point sequentially to 3.8%, so we are squarely on strategy here.

Cathie Lesjak
And I would say that we didn't see a disruption. Dion went through the details that show that we didn't see the disruption to our business as a result of the split. That was not a factor in how we met customer needs or in the reception that we got from customers.

Meg Whitman
And I think Maynard you asked about servers. I would say the same exact thing there was no disruption to customers. I have to say this split was executed nearly flawlessly and it's a credit to the team across the globe. We've been very successful actually at taking server share as the IBM server business migrated over to Lenovo. We have actually been very good at taking share and also gaining former IBM channel partners, so we have been very aggressive there. And obviously, as I have talked about, as the Dell EMC merger creates uncertainty in the

marketplace, we obviously want to be aggressive there talking about the future of the company, the future of our server business, and of course, the future of storage and networking. Which we feel like we are in really great shape, as I said our innovation engine is humming.

Maynard Um
Okay. And just for my follow-up. For HP Enterprise, I calculate that roughly nearly three quarters of your profits next fiscal year will be recurring. Are there any dynamics in the transactional businesses that make the cash flow less recurring or can we assume that nearly three quarters of your free cash flow is also recurring? Thanks.

Tim Stonesifer
Yes, at a high level, profitability is recurring. So I think you could assume that.

Meg Whitman
Yes, and I don't think there is anything in the dynamics that are different in 2016 than were different in the Hewlett Packard Enterprise segments in 2015, except for the TS it is getting stronger. So TS is up, Financial Services is an annuity, and ES is getting stronger as well. So I would say that ES the contracts are getting a bit shorter, but that shouldn't really affect us in 2016.

Maynard Um
Great, thank you.

Diana Sroka
Thank you. Next question, please.

Operator
Next question is from Toni Sacconaghi at Bernstein.

Toni Sacconaghi
Yes, thank you. I have one for HP Inc. and one for HP Enterprise, please. On the HP Inc. side, you commented on an incremental currency headwind and you also commented on a fundamentally more challenged printing business going forward, including supplies which drive the profit, yet you didn't change your operating EPS guidance for fiscal '16. And I am wondering why? Because the commentary certainly would have suggested that it should be lower, and what the offsets are?

Cathie Lesjak
Thanks, Toni. So we are taking very decisive action in order to counterbalance some of the headwinds that we're seeing in the printing business. And Dion talked a little bit about them in his prepared remarks. I mean we are absolutely maniacally focused on the billion dollars in productivity improvements and making sure that those are getting delivered and frankly getting delivered a little bit earlier in the year. We are also trying to change kind of how we approach the market and the market looks at us by really doing a better job from a marketing perspective and the sales perspective, so that in fact, we are not competing on price alone. We have got a lot of value in the products that we bring to market, and we think that there is an opportunity there. We also think there is an opportunity to improve our supplies market share position, and so we are taking action around, again, marketing and feet on the street, as well as really going after online. And then finally, Dion mentioned the fact that we are restructuring our non-revenue generating cost base. And we will be aggressively taking cost out of kind of the non-revenue generating. We believe that with these actions that will counterbalance some of the incremental

headwind that we saw in the printing market, but clearly, there is now more actions that need to take place in order to deliver the outlook that we provided.

Toni Sacconaghi
And on the HPE side, I was wondering if you could comment on a couple of things. It looked like separation costs had been pushed out from fiscal '15 to fiscal '16. I was wondering if you could comment on the magnitude of that push out as it relates to HPE? And sort of the same question as with HPI, if you have incremental separation costs in fiscal '16 relative to your expectations, why is cash flow not adjusted? And also if you could just confirm what the expected impact of the closure of the Chinese JV will be on your EPS and revenue for fiscal '16 and whether that's in your guidance or not?

Tim Stonesifer
Sure. Okay, let me start out with the cash flow. So from a separation cost, we had about $300 million of favorability from a free cash flow perspective on the E side in 15. 200 of that [$300 million] will move over to '16. So if you look at the overall amount of separation costs we were actually able to work down the overall amount so there will be about a $200 million separation cost increase in '16. If you look at overall free cash flow and the adjustment to '16, we are still holding to the '16 guide. And basically our shortfall was driven by a couple of things. If you think about the financing volumes were higher in our Financial Services business, as well as we had some pressure on VAT receivables that we were unable to collect. That will push over and give us some favorability in '16, which will offset some of the separation costs pressure. So overall, we are sticking to the guide that we provided at SAM.

As far as Tsinghua, we haven't adjusted EPS yet because the deal is not closed, but just to give you some color around that from the remaining 49% that will stick with us we are going to account for that with the equity accounting methods. So you will see that earnings and cash flow impact flow through the other income line and then as far as guide or framing it up from an EPS perspective, we've said historically that we had about $400 million of op profit in that business in 2014, so I think you could use that as a proxy. And then I just take a couple things into account. One would be the timing of the transaction, so when we close it. And then the second thing, I would think about is there will be some stranded costs associated with overhead costs that do not go with the transaction. So similar to dissynergy costs, we will need to work that out of the system and that will take a little bit of time, so that's the Tsinghua impact.

Meg Whitman
And I would just…we expect this transaction to close in Q1. We expect to have all the regulatory approvals by December 31st.

Diana Sroka
Okay. Thank you, Toni. Next question, please.

Operator
Our next question is from Sherri Scribner at Deutsche Bank.

Sherri Scribner
Hi. Thanks. I had a question on the HPE side, thinking about the server business has been relatively strong this fiscal year. Can you talk through your expectations? I know you commented you expected to decelerate somewhat, but do you expect that business to continue to be able to grow in fiscal '16?

Meg Whitman
Yes, we do. I mean, we are seeing very strong momentum that is in part driven by the sale to the tier 1 service providers, but also there is very good strength in our core server market with strong options attached that obviously help the margins. And ISS, just the Industry Standard Server portion, has the best ever product line that we have ever had with Gen9, with Cloudline and Apollo. And these are resonating really well with customers, and importantly, our purpose-built for specific workloads. So I think we've talked about how we are taking our Server business to a workload-focused strategy and as Tim said, ISS grew 5% year-over-year, 13% in local currency and we expect to gain over a point of share in the calendar Q3 of ‘15 and the market we think is going to be healthy. And so, I think we feel very good about the Server business and the reason we don't think it will quite the revenue year-over-year growth that we saw is that we are starting now to lap very strong compares, but at least for the foreseeable future, we feel pretty good about servers.

Sherri Scribner
Okay, great, thanks. And then, a question for Dion in terms of the A3 market, you talked about that a lot at the Security Analyst Day. Does anything that's happening now with the printer market mean that entry into that market moves out, or are you still on your plans to enter that market in about a year?

Dion Weisler
No. We are absolutely on the same course and trajectory that we outlined at the Security Analyst Meeting. We think it represents a strong growth opportunity for our shareholders.

Cathie Lesjak
And I would just add that we are taking decisive action around the core right now. We are not taking our foot off of the accelerator on the core, or on the investments that we are making for kind of the mid-term growth areas around commercial mobility, packaging and copier market, or for the future around 3-D and immersive computing.

Dion Weisler
Exactly. Kind of said another way, we firmly believe in our strategy and there is lots of disruption and change in the market at the moment, and our competitors are pursuing all sorts of options. We will continue to assess how the markets evolve. We will get ourselves in fighting shape inside the core, but we will continue to execute against our strategy.

Sherri Scribner
Thank you.

Diana Sroka
Thank you, Sherri. Operator, next question, please.

Operator
The next question is from Steve Milunovich at UBS.

Steve Milunovich
Thank you. First, I wanted to ask about the profits in the Server business. Obviously, you are pretty bullish on the growth rate, but what’s been happening to the margin in ISS? I assume it’s been coming down. So have you had and do you expect to have operating profit growth in that segment going forward? And I just wanted a little clarification on when you say tier 1 providers,

are those sorts of the big hyperscalers and are you selling them only Cloudline or are you selling them the kind of more fully configured service as well?

Tim Stonesifer
Sure. From a profit perspective, we'd expect margins to be relatively stable actually. There is a lot of work going on in supply chain, on the productivity front, so we have various initiatives going on there that will help offset some of the pricing pressures that we are seeing. As well as if you look at Gen9, as Gen9 becomes a bigger piece of the overall portfolio, those margins are also more attractive than what we had with the Gen8.

Meg Whitman
And as regard the tier 1, these are the big hyperscalers as you described and they continue to grow, and we don't really sell them much other than Cloudline. Now, we sell storage often and some networking, but for the server portion, it's mostly Cloudline. And then you immediately drop down into what we call tier 2, tier 3, tier 4, and they buy a much broader mix than just Cloudline. And the other thing, Steve, that I know you know, is that if you look at Enterprise Group in total, obviously the storage business, which is doing very well with 3PAR and All-Flash, plus the networking business is higher margin than the server business, so the blended average as we said at the Security Analyst Meeting, EG needs to be the growth engine of the company over the next couple years with modestly expanding margins, and the margins will expand with the mix shift. And obviously, of course, with the attach rate that is higher on 3PAR and All-Flash.

Steve Milunovich
That's great. And it's good to see you are getting some credit for 3PAR and Flash. We've certainly heard the same thing that's it's a terrific product. How about on the solution side, I think obviously legacy vendors are under attack from a lot of different directions, but you do have a bit of an ace in terms of the completeness of the product line and I've always had some concern that HP is a bit of piece-parts company, but it seems like you have been emphasizing solutions trying to coordinate the groups more. Are you seeing evidence that customers are beginning to react to that and that's going to put you into good competitive position?

Meg Whitman
So we feel really good about our ability to continue the transformation to a solution-selling company. First of all, because we now have a great server, storage, networking converged offering. But as we move to these four transformation areas that we talked about at the Security Analyst Meeting, this is dead on with customers. I mean these four transformation areas is exactly what virtually every customer is looking for. How do I transform my IT environment to a hybrid environment? How do I secure my digital enterprise? How do I enable analytics — a big data analytics environment? And how do I drive workplace productivity? And we are aligning software services and hardware, or infrastructure, to that. And this is particularly powerful for software because software now has some of the anchor IP in each of these areas and it's also helping us decide what parts of software we want to be in, and what parts we don't. And we talked about LiveVault and TippingPoint. This four transformation area gives us a very good portfolio criteria by which to manage that software business. So I think the transformation areas are absolutely right on for customers and we feel like we've got a pretty good portfolio. And where we have gaps, our first choice will be to do organic innovations. Second choice will be around partnering with our ventures arm, and then finally would be M&A along the lines of a 3PAR, 3Com, Aruba kind of acquisition.

Steve Milunovich

Thank you

Diana Sroka
Thank you, Steve. Next question, please.

Operator
The next question is from Kulbinder Garcha at Credit Suisse.

Kulbinder Garcha
Thank you. A question for Dion first. On the supplies business, what I think I have heard is the market is little bit worse, the pricing environment is tough and inventory levels may be high. I guess, can you speak about the visibility you have in each of those items beginning to improve? And then kind of linked to that is the…I think once upon a time, not long ago you were saying that the supplies business would stabilize by the middle of this year, then it was by the end of ‘16, now it’s by the end of ’17. So this Four Box Model to manage this business which is supposed to give this predictability, it didn’t seem that predictable, I guess. And so, my question is, how much faith do you have in that continued model about our supplies business eventually turning?

Meg Whitman
Thanks, Kulbinder. I guess, I’ll start and then I’ll throw it to Dion to add any additional comments. We have found that our Four Box Model is in fact very good. And as we have collected more big data (and every week we collect new data), we update basically the model. What we saw in Q4 were basically two things that really impacted the model, and impacted when the ink supplies would stabilize and pushed it out to basically late ‘17. The first thing was, we did see incremental competitiveness in key segments, particularly in SMB Ink, and therefore we placed less units. And as a result of that, that's going to have a knock-on effect around ink supplies.

Secondly, what we saw was through aggressive pricing, we took a product that should have been sold into one end user — an end user that, in fact, prints a lot — and we now are selling that product into home users, which just don't print enough. And so, we need to change that, and that’s part of better managing the marketing, better managing basically the price points, and that has a knock-on effect because those were units that we had expected would be very high usage. So we have a lot of confidence in the model, but you have to work the model all the time, and it’s across those four dimensions that we’ve talked about; the installed base, usage, aftermarket share, and then also making sure that we are careful about what we do from the supplies pricing perspective.

Dion Weisler
Yes, absolutely. The only other things that I would add to that is that we just believe that this is the new normal and we have a lot of faith in that Four Box Model that it is an incredibly predictable model, but there are dynamics in the market, competitive dynamics in the market, that just our working assumptions need to change around that this exactly how it’s going to be and as a result of that, we need to go to the gym. We need to get fit. We need to deal with currency the way that it's exposing itself in the market and the ramifications it's having on the marketplace, and do the three things that we talked about: drive those productivity improvements, not fight on price alone (balance marketing and sales), and materially go after non-revenue generating expenses. When we do that, we can turn marginal NPV units that have slipped into negative, back into positive territory, and that will then re-inform the Four Box Model.

Kulbinder Garcha
Okay. And maybe just one very quick question for Meg. Meg, as you've separated now into HP Enterprise, what are your thoughts on industry consolidation and the role that the HP Enterprise perhaps plays in that? Thanks.

Meg Whitman
Yes. So listen, obviously, I think one of the things that validates the decision to separate is these markets are changing enormously. I mean, Dion, talked about a couple of his competitors looking at strategic opportunities. We also obviously see the Dell EMC transaction. What I would tell you is, we feel really good about our strategy relative to what we see Dell and EMC doing. I mean they could not be in more stark contrast. They are getting bigger, leveraging up and doubling down mostly on legacy technology, while our strategy is to get smaller. I've spent the last four years deleveraging the balance sheet and leaning into new technology like converged infrastructure, new server architectures, 3PAR with All-Flash, Aruba, et cetera. So we feel really good about our strategy and our portfolio of assets. And I will underscore what I said before, these four transformation areas is the way we are going to pivot this company to solution selling. ES already solutions sells. EG and Software are moving rapidly towards that solution of driving business outcomes, as opposed to just selling speeds and feeds. And it's a cultural change for this company, but actually I will tell you its underway and I am feeling pretty good about it.

Kulbinder Garcha
Thank you.

Diana Sroka
Thank you, Kulbinder. Operator, we will take a final question, please.

Operator
The last question is from Jim Suva at Citi.

Jim Suva
Thank you and congratulations on your separation. I have one question for Meg, and one question for Dion and/or Cathie.

Meg, I believe you mentioned some of the ES contracts may be getting shorter, did I hear that correctly? And what does that mean to the profitability of such, the ability to invest in such, it seems like it may compress some of that a little bit, but maybe I am wrong on that?

And then the second, or the other question for Dion and/or Cathie would be, I think you had mentioned that you said the PC channel had some elevated inventory, and I believe we heard about this when you are going through the separation and you wanted to have your systems make sure that they converted over, but that was several months ago. So are you referring to excess inventory in the channel from HP? Or others? Or both? Or how should we think about that comment, because I would have thought by now that that PC inventory, or anything due to your separation and IT conversion cycles would have already right-sided themselves. Thank you very much.

Meg Whitman
Yes, let me answer the ES question. So the ES business is changing and you will recall in the old days, in particular the ITO part of the business, you would lose money in the first two years

of the contract, then you'd break even for about three years, and then you would make money in the final four years, but the only problem with that is about year eight the customer would renegotiate and you would miss out on the whole profit of the whole thing. And so, really the markets moved to shorter more strategic relationships in ITO. As opposed to just labor arbitrage, now there is, "how we transform your infrastructure to be more nimble, more agile and lower cost?" And we have talked about a number of our customers for whom we are not just taking their mess for less – in the old days, that's probably what we would have done. Now we are saying, we will help transform your IT environment to be part of this new world order that's going to allow it to be lower cost, more modern and allow you to be more agile. And those contracts tend to be shorter, and we are actually okay with that because we also are very clear now that we are not going to lose money in contracts in years one and two, and these things have to be profitable from the beginning. And that's been a change in the industry, and frankly, a change that we are putting a lot of discipline in. We're very, very focused on only taking deals that are good business for us. And like Dion said in his business, share for share's sake is not interesting to us here. We want to do good profitable deals with customers that we can drive a good outcome for. And you are seeing that, I mean, we said at our analyst meeting, we now have the highest net promoter score in the business – in the services business – and that ultimately and we can see it, is going to translate, I think, into higher new logos and higher TCV.

Dion Weisler
Okay. And to your question on channel inventories, I will step back. Going into quarter four, what I said was industry inventory levels were high, and our inventory levels were also high. As we exit Q4, I would say that industry inventory levels are still elevated, but somewhat lower than they were as the market has begun to digest the Windows 8 inventory, but our inventory position is now backed within the ranges and in good shape with regards to the age profile of that inventory.

CONCLUSION

Meg Whitman
Good, alright. Well, thank you very much to everyone for being on a slightly extended call today, because we wanted to make sure we covered the company and then also Hewlett Packard Enterprise and HP Inc. So thank you very much, and next quarter we will be reporting as two separate companies. So again, thanks for your support and thanks for a little extended time today.

Tim Stonesifer
Thank you.

Operator
Ladies and gentlemen, this concludes our call for today. Thank you.