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Q1 2025 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good day everyone, and welcome to the First Quarter 2025 HP, Inc. Earnings Conference Call. My name is Regina, and I will 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 conference. [Operator Instructions] As a reminder, this conference is being recorded for replay purposes.

I would now like to turn the call over to Orit Keinan-Nahon, Head of Investor Relations. Please go ahead.

Orit Keinan-Nahon
Senior Vice President-Finance & Head-Investor Relations, HP, Inc.

Good afternoon, everyone, and welcome to HP's first quarter 2025 earnings conference call. With me today are Enrique Lores, HP's President and Chief Executive Officer; and Karen Parkhill, HP's Chief Financial Officer.

Before handing the call over to Enrique, let me remind you that this call is a webcast, and a replay will be available on our website shortly after the call for approximately one year. We posted the earnings release and accompanying slide presentation on our Investor Relations web page at investor.hp.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 disclaimers in 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 HP's SEC reports, including our most recent Form 10-K. HP 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 now and could differ materially from the amounts ultimately reported in HP's SEC filings.

During this webcast, unless otherwise specifically noted, all comparisons are year-over-year comparisons with the corresponding year-ago period. In addition, unless otherwise noted, references to HP channel inventory refer to Tier 1 channel inventory and market share references are based on calendar quarter information. 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 for those reconciliations.

With that, I'd now like to turn the call over to Enrique.

Enrique Lores

President, Chief Executive Officer & Director, HP, Inc.

Thank you, Orit, and thank you to everyone for joining today's call. Q1 was a strong start to the year. We delivered top line revenue growth, increased momentum across our key growth areas and maintained our focus on positioning HP for long-term success.

Today, I will focus on three main areas. First, our Q1 results and key innovation highlights; second, a deeper dive on our business unit performance; and finally, I will share our outlook for the year ahead, including the actions we are taking to respond to evolving market conditions, while continuing to fuel our long-term growth.

Let me now turn to our Q1 results. Overall, we delivered revenue growth for the third consecutive quarter, up 2% year-over-year. This was largely driven by growth in our Personal Systems, commercial business and key growth areas. Non-GAAP earnings per share of $0.74 was slightly above the midpoint of our guide.

Operating profit margins for both Print and Personal Systems were in line with our expectations. These results demonstrate our ability to deliver on our commitments and execute our strategy to build a stronger HP.

Last quarter, I outlined our ambition to lead the future of work. We know companies need highly productive workforces to drive growth and employees are seeking fulfillment in the work they do. With our robust portfolio of PCs, printers, peripherals and more, we not only have a unique competitive advantage, but we sit at the intersection of this opportunity.

I am pleased to report we are making solid progress against our strategy. We are doubling down on our efforts in the commercial segment and aggressively investing and innovating in new AI and software capabilities. As an example of that, we recently entered into an agreement to acquire strategic assets from Humane. Once completed, we will benefit from their AI-powered platform Cosmos, highly skilled technical team and hundreds of patents.

With this acquisition, we will accelerate our plans to build an intelligent ecosystem across all HP devices, from AI PCs to smart printers and connected conference rooms. We look forward to boosting our technology and innovation organization by integrating the Humane team to HP.

We're also realigning our key growth areas to reflect the shift of our investment focus on the future of work. In addition to hybrid systems, workforce solutions, consumer subscriptions, industrial graphics and 3D, we are now including AI PCs and advanced compute solutions, such as workstations and retail solutions.

Gaming will no longer be one of the key growth areas and will instead be managed as part of our core portfolio because even though it will continue to be a very important business for us, is not directly related to the future of work. Collectively, we expect these realigned key growth areas to continue to grow faster than the core and to be accretive to our margins over time.

Turning to our innovation highlights. In Q1, our vision for the future of work was brought to life at CES with AI-powered innovations. For example, we announced several new models of AI PCs. We are empowering professionals with faster decision making an effective collaboration with the EliteBook Ultra, adapting to how and where people work best, our EliteBook X offers flexibility and enhanced security protection.

And these new PCs now bring HP's award-winning AI companion to our Intel platforms. And for product designers and data scientists, the ZBook Ultra recognized with the best laptop award at CES, can help manage complex projects and datasets with ease. We are strengthening the end-to-end experience of hybrid workers with Thunderbolt Dock. With a quick connect docking experience, employees are instantly connected to their workspace before they even sit down at their desk.

In gaming, we introduced OMEN AI beta, a groundbreaking software innovation that automatically adjusts for optimized performance. Our customer-centric approach also expands our print innovation. To meet the growing demand for convenience, we recently added Smart Tank printers to our HP all-in subscription plans. This all-inclusive print program has strongly resonated with our customers.

In Industrial, we're empowering print providers with new equipment and capabilities. With the introduction of two game-changing HP PageWide presses, we are delivering high-speed, high-quality print production. As we continue to innovate, we remain committed to technology that fosters connections, improves access and support sustainability. In 2024, HP reached nearly 20 million people through digital equity programs and partnerships. And I am proud to share earlier this month, HP jumped to the number two spot on America's Most Just Companies list.

Our progress were driven in large part by how we invest in our employees, support our communities and treat our customers. We were recognized as the leader in our industry for all three.

In a few weeks, we will host Amplify, our flagship conference to engage with customers and partners. This event provides an opportunity to share our vision and the progress we have made including how we are delivering AI-powered innovation and technology experience.

This past quarter, HP led the way in shaping the future of work. Thanks to the dedication of our talented team, and I want to take the opportunity to thank all of them.

Let me now turn to Personal Systems performance for the quarter. Revenue was up 5% year-over-year, with conversion continuing to power the growth more than offsetting a decline in consumer and continued softness in China. We drove share gains in the PC commercial windows market, particularly in high-value categories such as commercial premiums.

However, we lost share in consumer with units down year-over-year. While our strategy is not to gain share for the sake of gaining share, you should expect us to improve our performance through the year in this segment, especially in the premium category.

Worldwide PC commercial revenue grew 10% year-over-year, fueled in part by the growing adoption of AI PCs and the positive impact of the Windows 11 refresh cycles. The AI PC market experienced remarkable momentum achieving a sequential growth rate of 25% in calendar quarter four, and we continued to gain share in this market.

We believe the refresh cycle, combined with an increasing mix of AI PCs will further propel our commercial growth through fiscal year 2025 and beyond. Internally, we are empowering our teams with enhanced AI tools. Going forward, all new PCs we purchase will be AI PC, giving our teams greater insights and helping them better address customers' needs.

In our growth areas, hybrid systems, advanced compute and AI PCs, delivered strong performance with revenue up year-over-year. We believe there is more opportunity here, and we'll continue to prioritize investments in these categories.

Shifting to Print. We saw strong unit growth and share gains in home and specifically Big Tanks. In office, we maintained our share overall, and importantly, gained share in our strategic areas, A4 value and A3. We continue to see a competitive pricing market in office and weak demand in China that will continue to push us to improve our operational execution.

For the Print business, revenue declined 1% in constant currency year-over-year, in line with our expectations. In growth areas, consumer subscriptions revenue and subscribers grew year-over-year. This quarter, we achieved a milestone of 1 million instant paper subscribers with double-digit revenue growth, and we continue to drive revenue growth in industrial graphics.

In Workforce Solutions, momentum continued with revenue growth year-over-year. We had several new managed print wins during the quarter, including Prime Healthcare. This new customer in a growing industry enables us to support variety journey covering 44 hospitals and more than 45,000 employees.

And we saw notable wins in managed device services in multiple verticals, which include automotive, industrial, banking, agriculture and pharmaceuticals in multiple geographies. The range of deals demonstrates our ability to close and manage diverse customer deals around the globe.

Before I close, it's important that I take a moment to share the efforts underway to address the evolving external environment. We have been tracking geopolitical developments and are well prepared to respond to these shifting dynamics. Over the past few years, we have taken proactive measures to ensure manufacturing resiliency.

We have built a globally diverse supply chain, and we are continuing to expand our footprint across multiple countries to meet growing customer demand and bolster multi-source production. We have made significant progress. And by the end of fiscal year 2025, we expect more than 90% of HP products sold in North America will be built outside of China. China will continue to be an important manufacturing hub for the rest of the world.

As we look ahead, we are managing the current tariff increases on China and have included them in our outlook. Should additional tariffs be implemented, we would manage them the same way we have with China, leveraging the flexibility of our global supply chain network, along with cost improvements and pricing actions as needed.

Depending on the scope, while some of our mitigating actions can take a few months lead time we would be focused on fully offsetting over time.

During the first two years of our Future Ready plan, we have made excellent progress across process efficiency, automation, portfolio optimization and operational excellence. This has given us visibility in traditional opportunities aligned to our future of work strategy.

There is even more we can do to reduce our structural costs and we now plan to deliver $1.9 billion in gross annual run rate structural savings by the end of fiscal year 2025. These incremental structural savings will help mitigate macro and geopolitical uncertainty while continuing to support investments in strategic areas. Karen will share more details about this shortly.

I will close by reiterating our confidence in our full year outlook and our ability to deliver on our strategy to lead the future of work. As demonstrated in Q1, we have continued to build strong momentum while taking the measures necessary to mitigate risks, navigate policy changes and importantly, invest in our long-term growth.

Let me now turn it over to Karen.

Karen L. Parkhill

Chief Financial Officer, HP, Inc.

Thank you, Enrique, and good afternoon, everyone. We are pleased with our first quarter results and the solid progress on delivering towards our financial commitments for the year.

We drove revenue growth for the third consecutive quarter with continued strength in the Personal Systems commercial business and momentum in our key growth areas. We also gained share in a stabilizing print market, while executing against our plan to drive strong operating margins.

We have made excellent progress in accelerating our Future Ready plans. And as Enrique said, have increased the gross annualized run rate savings target for the program by the end of fiscal year 2025. And through disciplined execution and rigorous cost management, we delivered on our EPS commitments, while maintaining important investments in strategic areas, including the future of work.

Now taking a closer look at the details of the quarter. Net revenue was up 2% nominally and 3% in constant currency with growth across all regions. In constant currency, APJ grew 5%, Americas grew 3% and EMEA grew 2%.

Gross margin was 21%, down year-over-year due to increased commodity costs. As mentioned last quarter, we have put in place cost reduction and pricing actions to offset these headwinds. However, they will take time to ramp through the year, leading to stronger margins in the second half.

Non-GAAP operating expenses were up year-over-year, reflecting continued investment in key strategic initiatives and our people, offset in part by disciplined cost management, including Future Ready cost savings. All in, non-GAAP operating profit was $984 million, in line with our expectations.

Below the op profit line, non-GAAP net OI&E was also in line with our expectations and flat year-over-year with lower levels of short-term financing activity offset by higher currency-related losses. Finally, with a diluted share count of approximately 960 million shares, our non-GAAP diluted net earnings per share was $0.74.

Now, let's turn to segment performance. We drove solid growth in Personal Systems with revenue up 5%, both nominally and in constant currency from higher commercial volumes and increased ASPs as we continue to take disciplined pricing actions to help mitigate increased component costs.

We are focused on leading the future of work and doubling down on commercial, which represented over 70% of our PS revenue mix for the quarter. We also drove strong performance in key growth areas across AI PCs, Advanced Compute Solutions and Hybrid Systems.

Aligned with our strategy, we drove commercial revenue up 10% on 6% unit growth with stronger pricing and mix shift towards premium in a market that is beginning to show signs of accelerating refresh activity. However, the consumer market remained competitive, with revenue down 7% on lower volume as a result of our strategy to rebalance our portfolio to a more profitable mix.

Our operating margin in PS was 5.5%, in line with the range we guided at the beginning of the quarter and down year-over-year from higher commodity costs that were not yet fully offset by repricing and cost initiatives. We also continued to invest in important strategic initiatives.

In Print, our results reflect our focus on profitable unit placement and disciplined execution. While total Print revenue was down 2%, we increased our market share with strong performance in consumer hardware.

We also drove double-digit revenue growth in Consumer Subscriptions and maintained momentum in Industrial. By customer segment, we grew consumer 5% year-over-year on 7% unit growth and drove share gains with double-digit growth in Big Tank.

In commercial, while units were flat year-over-year, revenue declined 7% in a competitive pricing environment, particularly in China, where the market remains weak. We continued our purposeful focus on profitable long-term unit growth, gaining share in the higher-value categories of A4 and A3 and across all markets in the Americas and EMEA.

We increased market share and drove favorable pricing and supplies, though revenue declined 1% with currency and usage headwinds. And we delivered Print operating margin at the high end of our range, as expected, reflecting rigorous cost discipline in a competitive market.

Now turning to our Future Ready plan. We have continued to drive progress, not only accelerating our initial plan, but also identifying additional initiatives to further reduce costs in our core and drive efficiencies. Given this, we are raising our cumulative gross run rate savings target from $1.6 billion to $1.9 billion by the end of fiscal year 2025.

We expect restructuring charges associated with the plan to increase by approximately $150 million to $1.2 billion and anticipate approximately $400 million in charges this fiscal year as we complete the program. These incremental structural savings will be a key lever to help offset macro and geopolitical uncertainties, while also continuing to fuel investments in our key growth areas and AI innovation, all designed to position us well for long-term sustainable growth.

Now, let me move to cash flow and capital allocation. As expected, our cash flow from operations was approximately $375 million in the quarter, and free cash flow was $70 million. Our results reflect normal seasonality associated with the timing of variable compensation payments and sequentially lower volumes in Personal Systems.

With regard to working capital, as part of the tariff response actions, we purposely produced additional inventory and also took advantage of strategic buy opportunities as part of overall cost mitigations. While these actions will be economically beneficial to the year, they increased our cash conversion cycle.

And as we pay for and sell the increased inventory, we anticipate a further impact in cash conversion, resulting in negative free cash flow in Q2. It is important to note that these are timing impacts only and do not impact our full year outlook. Lastly, we returned close to $400 million to shareholders through both share repurchase and dividends and finished the quarter within our target leverage range.

As we look ahead, we will continue to monitor the evolving geopolitical environment. And as Enrique mentioned, we have been focused for some time on response plans to mitigate potential adverse impacts. In both our full year and Q2 guide, we have accounted for the added cost driven by the current tariffs on China and associated mitigations, including our higher Future Ready cost reductions. I would note that those tariffs mostly impact our Personal Systems business.

Though the environment ahead remains fluid, we will be focused on offsetting any additional tariffs with further leveraging the flexibility of our global supply chain network, along with cost and pricing actions as needed.

We continue to expect non-GAAP diluted EPS to be in the range of $3.45 and to $3.75. FY 2025 GAAP diluted net earnings per share is expected to be in the range of $2.86 to $3.16 including increased restructuring costs for our Future Ready plan.

As we said at the beginning of the year, we expect EPS to be stronger in the second half with consistent levels of sequential growth each quarter. Normal seasonal strength in Personal Systems, combined with the timing of the Windows 11 refresh and increased penetration of AI PCs are catalysts that we expect to drive revenue strength in the back half of the year.

And we continue to execute on our plans to offset commodity costs, including repricing efforts and cost reduction actions that are ramping and will have a more significant impact in the second half. These actions and the overall measures we are taking to deliver incremental structural cost savings from our Future Ready plans are expected to drive EPS improvement throughout the year, particularly in Q4.

There is no change to our beginning of the year projection for print revenue to grow at least in line with the market in fiscal year 2025. And we now expect Personal Systems to grow faster than the market, driven by share gains in commercial.

Our focus on premium categories, including AI PC, is also expected to contribute to increased levels of revenue growth in the second half. We continue to expect PS operating margins to be in the upper half of our 5% to 7% range for the year due to the actions I described earlier as well as the sustained efforts to drive higher ASPs through the increased mix of premium products.

And for Print, we continue to expect our operating margins to be near the top of our 16% to 19% long-term range, as we exercise disciplined cost management and execute on our Future Ready plans.

For the second quarter, we expect non-GAAP diluted EPS to be in the range of $0.75 to $0.85 and GAAP diluted net earnings per share to be in the range of $0.62 to $0.72. In Personal Systems, we expect Q2 revenue to perform better than typical seasonality as we continue to see strength in commercial aligned with our future of work efforts.

And we expect Personal Systems margins to remain in the lower half of the 5% to 7% range given the timing of tariff mitigation. In Print, we expect Q2 year-over-year revenue growth to be in line with full year growth rates and operating margins to remain near the top of our 16% to 19% range, as we continue to focus on profitable unit placement and disciplined cost management.

And just to note, we expect corporate other expense to continue to be higher in Q2, though not as high as Q1 with the timing of some stock compensation expenses. We continue to expect free cash flow to be in the range of $3.2 billion to $3.6 billion for FY 2025 with the second half of the year stronger than the first.

And on capital allocation, we remain committed to returning approximately 100% of free cash flow to shareholders overtime, as long as our gross leverage ratio remains under 2 times, and there aren't better return opportunities.

In closing, we drove solid progress in Q1 against our strategic objectives and full year commitments, while taking action that will help us navigate through the dynamic geopolitical environment. We remain focused on disciplined execution, as we continue to invest for the future and believe we are well positioned to deliver long-term profitable growth.

With that, I would like to hand it back to the operator, and open the call for your questions.

QUESTION AND ANSWER SECTION

Operator: Thank you. And we will now begin the question-and-answer session. [Operator Instructions] Our first question will come from the line of Samik Chatterjee with JPMorgan. Please go ahead.

Joseph Cardoso Q
Analyst, JPMorgan Securities LLC

Hi. Thanks for the question. This is actually, Joe Cardoso on for Samik. I guess first one here is just wondering if you can quantify the impact of the China tariff in the guidance. And how are you expecting that to trend through the year, given the mitigation efforts you outlined?

And then just relative to the latter part in terms of the mitigation efforts, any color in terms of where this production may be heading in terms of essentially moving production a bit out of China, just given kind of the outstanding tariffs currently up in the air? And then I have a quick follow-up. Thank you.

Karen L. Parkhill A
Chief Financial Officer, HP, Inc.

Yeah. Thanks, Joe, for your question. In terms of the tariffs, as a practice, we will include the known impacts in our guide. So in both Q2 and the full year guide, we've included the added costs driven by the current tariffs in China, and those mostly impact our PS business.

I would say, keep in mind, roughly a-third of our revenue is generated in the US. And as Enrique said, by the end of FY 2025, less than 10% of this revenue will come from China and be subject to the tariff. We're not going to quantify. But in terms of what we're doing, we're leveraging our global supply network to mitigate this impact. We are moving production around the world to the network where we've got other places to produce. We're also – have got our higher Future Ready cost reductions that we talked about on the call that will help mitigate and we can take pricing actions as needed.

Enrique Lores
President, Chief Executive Officer & Director, HP, Inc.

A

And let me provide some additional color. This is something you have heard us talking before after COVID, we said we needed to build a more resilient supply chain, and this is what we have done. And to do that, we have built manufacturing facilities in multiple countries. Southeast Asia, other parts of Asia increased the capacity in other parts where we already present. And this is, as Karen said, this is what we are doing. Rebalancing supply chain, and we are now in a much stronger position than we were 3 years ago because we have been really putting a lot of focus on that and driving a lot of changes..

Joseph Cardoso
Analyst, JPMorgan Securities LLC

Q

No, I appreciate the color there, guys, for both of you. I guess maybe the follow-up here is just in terms of the PS growth. Obviously, you guys kind of raised your outlook here in terms growing faster than the market. Just curious if you can rank order, the drivers here, you talked about share gains, perhaps a little bit of pricing, maybe there's a bit of a higher mix on the AI PCs than what you were expecting further. Just wondering if you can flesh that out a bit in terms of where the goodness is materializing for HP? And thanks for the questions.

Enrique Lores
President, Chief Executive Officer & Director, HP, Inc.

A

Yes, of course. I think, first of all is, we expect the market to continue to grow, especially in commercial as we have seen during the last two quarters. And the key drivers of that, first is the aging of installed base, second the Windows 11 refresh and third, to some extent, the penetration of AI PCs. This is what is driving that.

Then in this market, we are performing well, we are driving significant innovation. We have a strong sales team and this has been driving our progress and driving the better competitive position that we have and the improvement that we have made. Of course, pricing is part of it, also because of mix. Our focus, as you know, is to grow in the most profitable premium categories. This is what we are doing, and this is impacting our results, and this will continue to impact our results through the end of the year.

Operator: Our next question will come from the line of David Vogt with UBS. Please go ahead.

Brian Luke
Analyst, UBS Securities LLC

Q

Hi, thanks for taking the question. This is actually Brian Luke on for David. So for my first one, just on Windows end of life. Do you think it's becoming clearer to businesses, what devices they will need as it relates to spec like optimal tops, AI-related use cases or security? In other words, are they becoming more confident in refreshing their devices? Or is the fall deadline still the main driver in businesses decisions? And then I have a follow-up.

Enrique Lores
President, Chief Executive Officer & Director, HP, Inc.

A

Yes, I would say it's both. First of all, what we have seen is that there is an acceleration of the Windows 11 refresh. As I have said in previous calls, one of the key leading indicators for us is the size of the funnel and the funnel has grown significantly in the last 2 quarters, which tells us that customers are really much more aware and much more ready to drive the refresh.

In terms of products they buy, I think they see the need to buy some of the later generation products, both driven by the AI capabilities, but also by the new use models of PC that more and more are used as communication tools, and this has a big influence also in the type of devices that they are building – that they are buying. And in both cases, we have a leading portfolio that is showing at in the progress that we are making in this category.

Brian Luke
Analyst, UBS Securities LLC

Q

Got it. That's helpful. And then for my follow-up, do you have any updates on customer adoption of AI PCs? Like do you still see them composing 20% of PC shipments this year and a 40% to 60% adoption rate into calendar year 2027? And then any change to the 5% to 10% premium versus traditional PCs? Thank you.

Enrique Lores
President, Chief Executive Officer & Director, HP, Inc.

A

Yeah. Of course, yeah, our current expectation is that the penetration this year – at the end of this year will be more in the 25% range, but slightly higher than the 20% you mentioned. We have not changed our projection for two years from now, we continue to expect it to be between 40% and 50%. And then in terms of average selling price, our expectation continues to be that it will be at an average between 5% and 10% higher than what it is today, driven by the penetration of AI PCs.

Operator: Our next question comes from the line of Wamsi Mohan with Bank of America. Please go ahead.

Wamsi Mohan
Analyst, BofA Securities, Inc.

Q

Yes. Thank you so much. First one for Karen. If you – I appreciate all the color you shared about first half versus second half seasonality. But when you look at the second half versus first half, that's a very material increase in earnings, I think, 33%, which has never happened historically despite other times when you have done restructuring. And even if you take into account the run rate and this is at a gross level of restructuring and flow that through at some net rate that you have done historically, it just doesn't add to the full bridge.

So I'm just hoping you could shed some color on what are – which one of these drivers should we really be focused on, especially given the fact that the tariff environment still remains uncertain. And so PC uptake has also been disappointing over the last several quarters. How confident should we feel that this kind of seasonality can be achieved? And I have a follow-up, please.

Karen L. Parkhill
Chief Financial Officer, HP, Inc.

A

Yeah. Thanks for the question, Wamsi. So I'm going to step back and just talk about why we're confident in our EPS guide and the ramp that we talk about between the first and the second half. And I'd start with just a reminder that given the seasonality for our business, EPS is historically stronger in the second half. But specific to this year on top of that, we expect both revenue and cost to improve in the back half.

And on revenue, we expect more pronounced PS seasonality tied to the PC recovery, which includes the Windows 11 refresh and the ramp of AI PCs. We also expect continued mix shift to premium, including a higher penetration of AI PCs as we move through the year, which leads to higher ASPs. And we expect continued momentum in our growth segments that will help improve our margin profile.

And in cost, we expect reduced commodity costs because we're qualifying lower-cost components right now. We're also further driving consolidated volumes through strategic partners that can provide us with a cost advantage. And we've got incremental savings from our Future Ready plan. And then lastly, we've got a step-down in our corporate other cost as we move past the first half of our year. So I'd say all of these things, along with the momentum you've seen already driving our revenue growth the last couple of quarters, give us confidence in this ramp.

Enrique Lores
President, Chief Executive Officer & Director, HP, Inc. A

Let me emphasize a couple of the comments that Karen made. I think versus the analysis that you were describing, Wamsi, there is both improvement on the revenue side and improvement on the cost side. And the combination of both is what drives us – brings us confidence in the guide that we have provided. As Karen said also at the beginning, we are including in the guide the impact of the current tariffs for China. We are not including the rest. We think it's difficult to speculate, and it's hard to know exactly what the tariffs will be. So we are not including that in the guide.

Wamsi Mohan
Analyst, BofA Securities, Inc. Q

Okay. Thanks for that. Could I just ask around the tariff piece, right? So is it – could you just clarify if it's a 10% tariff that you're incorporating in China? Or are there some news this morning of an incremental 10% or are you incorporating a full 20% rate at the moment? That's my clarification.

And just in light of that, if you think that you will have to utilize pricing I mean as you have decoupled your supply chain, let's say, away from China, if other PC makers are unable to do that, would you say you would utilize pricing as a lever to take share? Or how should we think about that? Thank you.

Enrique Lores
President, Chief Executive Officer & Director, HP, Inc. A

Sure. So, first of all, as Karen said at the beginning of the call, we are including only in the guide what is official. And at this point, only the first 10% tariff increase is built into the plan. Depending on what happens, we will – I mean, we need to see what happens now for China or other parts of the world, but we are not including that in the guide.

In terms of how will we manage the situation, you know that our goal continues to be profitable growth, and we look at tariff as another area of cost. And if we have that advantage, we may use it for price, we may use it to create better profit to be able to invest in other areas.

We will see how – depending how the situation goes, we will go one direction or another. Our goal for the rest of the year is to do better than the market, as Karen has explained in the guide. So our expectation is that we will be gaining share, especially in the commercial space, especially in premium.

Karen L. Parkhill
Chief Financial Officer, HP, Inc. A

And I would also say, Wamsi, that with the future tariffs, we plan to use the same playbook that we've already used for the first 10% in China. So should there be more in China, we've got the playbook. Should there be more somewhere else? We're going to run that same playbook.

Operator: Our next question comes from the line of Erik Woodring with Morgan Stanley. Please go ahead.

Dylan Liu
Analyst, Morgan Stanley Taiwan Ltd.

Q

Hi. It's actually Dylan Liu for Erik. So my question is, can you help us better understand when you expect the current commodity cycle to deflect to a tailwind to margins? And would you try to hold pricing at that time? Or would you be willing to pass those savings back to a customer at that time? And I have a follow-up after this.

Enrique Lores
President, Chief Executive Officer & Director, HP, Inc.

A

Yeah. For the full year, we expect commodity will continue to be a headwind for margin for the full year, but we expect to see improvements quarter-over-quarter starting in Q2. That's the best view that we have at this point. And again, how will we use that will depend on the competitive environment. Again, our goal is to drive profitable growth and we will be looking at pricing and other tools depending on what the situation will be.

Dylan Liu
Analyst, Morgan Stanley Taiwan Ltd.

Q

Got it. Thank you. And just to follow up, want to make sure we understand your Personal System comments. So last quarter, you talked about a mid-single-digit unit growth with ASP growth layered on top of that. And is it correct to think that you're now expecting a better than mid-single-digit growth? Or how material is the outperformance you're now embedding in the full year guidance?

Karen L. Parkhill
Chief Financial Officer, HP, Inc.

A

Yeah. I would say right now, we're saying for PS that we expect to continue to gain share, particularly in commercial and grow faster than the market.

Enrique Lores
President, Chief Executive Officer & Director, HP, Inc.

A

And our expectations for the total market have not radically changed versus what we were saying a quarter ago, so no changes there.

Operator: Our next question will come from the line of Michael Ng with Goldman Sachs. Please go ahead.

Michael Ng
Analyst, Goldman Sachs & Co. LLC

Q

Hey. Good afternoon. Thanks for the question. Just as a follow-up to the prior one around Personal Systems growth and the PC market. Can you just talk about what element got better? It sounded like Personal Systems performance in the quarter, was in line. Is the April outlook better than you had originally anticipated? Is it the back half? Any color there would be helpful.

Enrique Lores
President, Chief Executive Officer & Director, HP, Inc.

A

Yes. I think more – it's not only the market that we expect to perform as we were saying a quarter ago, is really the momentum that we see, and this is being translated into results.

If you look at the growth that we had this quarter on commercial of 10%, this clearly an improvement from where we were a quarter ago and when we look at the momentum, the progress that we see in the market, this gives us confidence in the projections that we have shared for the rest of the year.

Michael Ng
Analyst, Goldman Sachs & Co. LLC

Q

Great. Great. Thank you. And I wanted to follow up on the Humane acquisition and the investments in the intelligent ecosystem across the HP devices. Is this a reference and an investment in Workforce Solutions and Desks, if you could just expand on your vision there and the momentum that you think you can get in that piece of the business? Thank you.

Enrique Lores
President, Chief Executive Officer & Director, HP, Inc.

A

Sure. I think it's really the impact of Humane will be beyond Workforce Solutions and that part of the company. When we think that this is a smart acquisition for us, we have got into the company a very talented team with a lot of experience in AI development and a great software portfolio, a great set of total assets that we can integrate into really drive the future of work strategy.

What you will see us doing is use those total assets to accelerate the deployment of AI at the edge and accelerate our plans there and also to accelerate what we call the better-together experience of having our products connecting amongst themselves and offering a much better and radically simpler to experience to our customers.

For example, one of the first areas we're going to be deploying that is in having our PCs and video conferencing rooms connecting in a seamless way, which we know is a big pain point for customers. I'm sure that all of you experienced that when you have to go to a conference room that will be the first area where we will use some of the technologies from Humane. And we expect to do that in the coming quarters.

Operator: Our next question comes from the line of Asiya Merchant with Citigroup. Please go ahead.

Michael Anthony Cadiz
Analyst, Citigroup Global Markets, Inc.

Q

Good afternoon. This is Mike Cadiz for Asiya Merchant at Citi. So can I ask, how do you think about the PC industry growth rate for this year? Some external parties are saying maybe 4% to 5%. We at Citi are saying about 4%. And then if you layer on top of that your price increases, can one relatively safely assume that PCs can see high-single digits this year?

Enrique Lores
President, Chief Executive Officer & Director, HP, Inc.

A

So the answer is, yes. As I said before, our projections for the market continue to be the mid-single-digit growth for units. We haven't changed that, which is aligned with what most of the industry analysts are saying, and we expect pricing to have a positive impact on top of that, and we expect to be growing faster than the market.

Michael Anthony Cadiz
Analyst, Citigroup Global Markets, Inc.

Q

Thanks. And then as my follow-up, could you add more color and characterize PC demand across the different segments like consumer, SMB and large enterprise, please? And that's it for me. Thank you.

Enrique Lores
President, Chief Executive Officer & Director, HP, Inc.

A

Sure. Let me provide some color. Last quarter, we saw growth both in the – in terms of units, both growth in both the consumer and the commercial space. In the consumer space, it was more driven by low-end products. In the commercial space was more balanced.

If I go through segments, we saw growth in the government space. We saw significant growth in the enterprise and SMB spaces, and we only saw a decline in the education category. So overall, fairly solid growth for PCs and again, especially in the commercial – in the more premium categories.

Operator: Our next question comes from the line of Krish Sankar with TD Cowen. Please go ahead.

Steven Kinney Chin
Analyst, TD Cowen

Q

Hi, this is Steven calling on behalf of Krish. My first question is regarding your print business. I guess, Enrique, like I guess given the ongoing strength of the US dollar, I know this is sort of out of your control, but given the pricing power that some of your Japanese competitors have, do you feel like that there could be a longer-term structural disadvantage that you guys have? And are you seeing any of that pricing disadvantage spill over into commercial contract pricing?

Enrique Lores
President, Chief Executive Officer & Director, HP, Inc.

A

Well, we continue to see a very competitive environment on the print side, but not more competitive than what we have seen during the last few quarters. And we are not expecting it to change in the coming quarters, and this is what we're using as a planning assumption. Despite of that and driven by – enabled by the work that we did in cost, we grew share in the print space this quarter, especially in the home side. And our plan continues to be to drive profitable growth and really focus on the more profitable customer side as we have been during the last years.

Steven Kinney Chin
Analyst, TD Cowen

Q

Okay. Thank you for that. And for my second question, I had one for Karen regarding inventories. I just wanted to clarify for the second quarter, just given your comment earlier on negative free cash flow. I was wondering if that was implying further growth in inventories. And if so, is that more on the component side or finished goods side? Thank you.

Karen L. Parkhill
Chief Financial Officer, HP, Inc.

A

Yeah. Thanks for the question. It was not necessarily implying further growth in inventory, though we might take advantage of strategic buys like we do in any given quarter. It was really taking into account the fact that we took on extra inventory that we will pay in accounts receivable this quarter, which will impact our cash conversion cycle.

Steven Kinney Chin
Analyst, TD Cowen

Q

And this was one of the actions that we took to mitigate the impact of tariffs. We grew – we increased the amount of finished goods inventories in the US, so we could respond to tariffs, so we could protect some shipments from a tariff increase.

Karen L. Parkhill
Chief Financial Officer, HP, Inc.

A

But then again, we said that it's not going to impact our full year free cash flow. It's a timing impact only.

Operator: Our next question will come from the line of Aaron Rakers with Wells Fargo. Please go ahead.

Jake Wilhelm
Analyst, Wells Fargo Securities LLC

Q

Hi. This is Jake on for Aaron. Thanks for the question. Maybe to start out, I was wondering if you could just give some additional color around the competitive environment for print within China, maybe specifically around supplies and how that has potentially changed over the last few quarters?

Enrique Lores
President, Chief Executive Officer & Director, HP, Inc.

A

Sure. I'll take the question. So we haven't seen from a supplies competitive perspective a radical change from what we have been in China or actually anywhere else in the world. We – the supplies business is performing well. We have been able to both – to continue to grow share overall, which is one of our key plans, key strategies, as you know, and we are very pleased with the progress we are making overall.

Jake Wilhelm
Analyst, Wells Fargo Securities LLC

Q

Great. Thanks. And maybe just as a follow-up, I think you noted some strength in consumer subscriptions. I was just wondering if you could give some extra color there.

Enrique Lores
President, Chief Executive Officer & Director, HP, Inc.

A

Sure. Thank you. So yes, in terms of our key growth areas, this is one of the areas where we continue to see more solid growth. We had double-digit revenue growth this quarter. We continue to grow the number of subscribers and we highlighted in the call that we are launching additional services, for example, paper, they also are having good traction, and we surpassed 1 million subscribers for our paper program.

And as I have said before, this is a service to deliver paper at the home of our customers and is, I would call premium paper because this is really driven by convenience, not driven by price. We have also expanded the rest of the offering that we have.

And in the all-in program where customers get the printer and also consumables. We have added the Big Tank products which is also a strong differentiator for this category of products in the market. So we are really pleased with the progress we are making in this space. Thank you.

Operator: Our final question will come from the line of Alek Valero with Loop Capital. Please go ahead.

Alek Valero
Analyst, Loop Capital Markets LLC

Q

Hi, guys. Thank you for taking the question. This is Alek on for Ananda. My first question is what kind of back to office assumptions have you baked into your assumptions for Print?

Enrique Lores
President, Chief Executive Officer & Director, HP, Inc.

A

I couldn't – oh, back to office, I think you said, we are not assuming any radical change in terms of those assumptions and that the situation will remain fairly stable in the coming quarters.

Alek Valero
Analyst, Loop Capital Markets LLC

Q

Thank you for that. As a quick follow-up, do you guys have any thoughts on competitors' landscape and AI PCs given that there's new players coming to market, such as NVIDIA, do you potentially view this as a positive for greater AI PC market adoption?

Enrique Lores
President, Chief Executive Officer & Director, HP, Inc.

A

Well, we are working with NVIDIA to integrate their technology into AI PCs. NVIDIA has been, and we expect to continue to be a key partner for us, and you will see us introducing very exciting products with their technology in the coming quarters.

Operator: That will conclude our question-and-answer session. And I'll now turn the call back over to Enrique Lores for closing remarks.

Enrique Lores
President, Chief Executive Officer & Director, HP, Inc.

Perfect. Thank you. Thank you, everybody, for joining the call today. We know it's a little bit later than other times. So I really thank you for staying with us. And I just want to finish by reemphasizing some of the comments we have made today.

First, we are pleased with the results that we achieved in Q1, not only from a financial perspective, but also from a competitive and from an innovation perspective because it shows the way we are going to be going forward.

Second, we are pleased with the momentum that we have in the market, and this is why we maintain the guide that we provided last quarter despite, for example, the incremental tariffs that we have seen in China.

And third, when we look at the future, we are really excited about the opportunity we see in the future of work, and this is really what is driving the innovation and the plans that we have for new products and new services.

Thank you again, and looking forward to talk to you again next quarter. Thank you.

Operator: And that concludes our call today. Thank you all for joining. You may now disconnect.