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OVERVIEW:
Co. reported 4Q17 total revenues of $2.7b and adjusted EPS of $1.04. On 01/31/18, Co. announced its agreement with Fujifilm to combine XRX with its longstanding JV Fuji Xerox.
Operator

Good morning, and welcome to the Xerox Corporation Fourth Quarter 2017 Earnings Release Conference Call, hosted by Jeff Jacobson, Chief Executive Officer. He’s joined by Bill Osbourn, Chief Financial Officer.

During this call, Xerox executives will refer to slides that are available on the web at www.xerox.com/investor.

At the request of Xerox Corporation, today’s conference call is being recorded. Other recording and/or rebroadcasting of this call are prohibited without the express permission of Xerox. (Operator Instructions)

During this call, Xerox executives will make comments that contain forward-looking statements, which, by their nature, address matters that are in the future and are uncertain. Actual future financial results may be materially different than those expressed herein.

At this time, I would like to turn the meeting over to Mr. Jacobson. Mr. Jacobson, you may begin.

Jeffrey Jacobson - Xerox Corporation - CEO & Director

Good morning, and thank you all for joining our call. We have 2 very exciting and important announcements to cover.

First, today, we reported strong fourth quarter results that demonstrate the successful execution of our strategic priorities. We also announced a transformational transaction in which Xerox will combine with Fuji Xerox, our long-standing joint venture with Fujifilm, to create a global leader in innovative print technologies and intelligent work solutions. We will spend the majority of the time we have today providing details on this value-enhancing combination. However, before we do so, I’d like to spend a few minutes taking you through the highlights of our fourth quarter and 2017 results.

Turning to Slide 6. I am pleased to report that Xerox had a strong quarter that reflects the significant progress the company has been making. We delivered improvement across all key performance metrics. Xerox generated $2.7 billion in total revenues during the quarter, up 0.5% year-over-year or down 2% in constant currency. This compares to a 5.6% decline on a constant currency basis through the first 9 months of the year and, as we
anticipated, represented a meaningful improvement to our revenue trajectory. This was driven by a 5% increase in revenue within our strategic growth areas.

Importantly, equipment sale revenue grew 4.3% or 1.5% at constant currency, which is the first quarter showing constant currency growth since the second quarter of 2013. This was enabled by our focus on capturing the growth opportunities in the marketplace. To do so, we expanded our channel reach, introduced new products for our graphic communications and high-end customers, and successfully delivered our largest ever new product launch.

Our Strategic Transformation drove solid operating profit margin of 14.4% in the fourth quarter, up 20 basis points over last year, while supporting our investments in future revenue initiatives. As a result of our improving performance, we realized adjusted EPS of $1.04, up $0.04 over last year. Note that due to an estimated $400 million noncash charge related to the enactment of U.S. tax reform, GAAP EPS was a loss.

Our solid performance during the quarter enabled us to deliver on our commitments for the full year and put us in a position of strength as we enter 2018.

Turning to Slide 7. With these results in mind, I would like to take a step back and discuss the broader transformation that has been taking place at Xerox in the past year. When we held our Investor Day a little over a year ago, before the spinoff of Conduent, we laid out a comprehensive strategy focused on achieving 2 goals: first, increasing margins and enabling investment through our ongoing Strategic Transformation cost and productivity program; and second, improving our revenue trajectory while increasing our participation in growing market segments.

This was intended to create a new Xerox that is more competitive and better positioned amidst the changing industry environment. Our progress in 2017 is a clear demonstration that we are delivering on our commitments and our strategy is working. We made progress toward improving our revenue trajectory by focusing on the strategic growth areas in production color, A4 multifunction devices and Managed Document Services, which represented 40% of our full year revenue in 2017, up 2 percentage points over last year.

Our new ConnectKey portfolio received highly positive customer reception. Coupled with the expansion of our channel reach through the addition of 65 new dealer partners, this important launch drove improved fourth quarter equipment sales. We exceeded the annualized gross cost-savings target under our Strategic Transformation program by $80 million, reaching $680 million in 2017. As a result, we delivered operating margin expansion despite currency headwinds, while significantly enhancing our cost competitiveness. These cost savings also allowed incremental investments in our business and growth opportunities.

Finally, as previously announced, we took important actions to optimize our capital structure this year, including pension contributions and the elimination of account receivables sales programs. While these actions had a near-term impact on our cash flows, they will simplify our business, drive future savings and put us in a better position to immediately generate stronger cash performance. As a result of how well we executed our plans, we closed the year in a much better position operationally and financially than we entered it. And we feel great about the solid foundation we have built as we aim to deliver another year of continuous improvement in 2018.

Turning to the next slide, you’ll see a more detailed breakdown of the progress we have made on our Strategic Transformation program, which we initiated in the beginning of 2016. Our focused and disciplined process has delivered over $1.2 billion in cumulative gross cost savings to date against our original target of $1.1 billion by 2017. We expect to realize $1.7 billion in savings by year-end 2018 on a cumulative basis, exceeding the $1.5 billion we initially targeted. You’ll find more details on our solid 2017 performance and 2018 guidance in the earnings release and supplemental presentation we put out this morning. We’ll take your questions regarding our fourth quarter results during Q&A.

I’ll now shift my focus to the transaction we announced this morning. Turning to Slide 10. This morning, we announced our agreement with Fujifilm to combine Xerox with our long-standing joint venture, Fuji Xerox. As many of you know, we currently have a 25% equity ownership in the existing Fuji Xerox joint venture, with the remaining 75% owned by Fujifilm. In many ways, Xerox and Fuji Xerox perfectly complement each other geographically and in our competitive strengths.
Fuji Xerox is a leading player in the Document Technology business with an estimated $9.6 billion in 2017 revenue. They serve large, stable markets such as Japan as well as fast-growing markets in China and Asia Pacific. They hold the #1 market share in Asia and are widely recognized for their industry-leading R&D, manufacturing and sales platform. They also have a robust product portfolio, with 40% of revenues coming from growing market segments in Graphic Communications and solutions and services.

The transaction we are announcing today will bring together 2 companies and will create a global leader in innovative print technologies and intelligent work solutions. Together, we will be able to better innovate, compete in fast-growing markets and deliver significant benefits for our customers, employees and shareholders.

Before I explain the enhanced prospects of the combined company, I’ll provide some background on what the joint venture structure looks like today and why we firmly believe that this is the best path forward for Xerox.

Moving to Slide 11. While the Fuji Xerox joint venture has certainly been among the longest lasting and most fruitful partnerships in the history of the technology industry, there are significant opportunities to improve the operational and financial aspects of the relationship. The transaction creates a combined company that will be dramatically stronger and more competitive than either company is on a stand-alone basis. I would like to highlight the key dynamics inherent in the current joint venture as we believe it provides important perspective into the value of this transaction.

Fuji Xerox is our most important supplier and a key partner in our R&D efforts. The company also has excellent manufacturing capabilities and an attractive technology portfolio with impressive solutions in inkjet, industrial print and workplace solutions. However, our ability to market and capitalize on these assets is somewhat constrained under the current joint venture structure for a number of reasons. Our inability to benefit from the growing Asian markets is an obvious one. But there are other inefficiencies and limitations that come with having 2 separate product portfolios, R&D road maps and supply chains.

The combination will allow us to break down these barriers of value creation and align the long-term strategic vision of the 2 companies. We will also be able to remove duplicative costs in R&D and corporate functions, and fully consolidate our supply chain to improve our cost position globally. This will significantly improve our global go-to-market competitiveness, which should drive increased revenue opportunities.

By gaining uninterrupted access to each other’s IP and technology, we will be able to expand the breadth and reach of our offerings and streamline product portfolio strategies to better coordinate our innovation road maps. We believe this is the natural evolution of our joint venture with Fujifilm and will create a much more efficient partnership structure, driving toward one common goal of delivering world-class, innovative solutions for customers.

For further background, shareholders can find additional information about the current structure in the 8-K we filed this morning, which includes the existing joint venture agreement.

Let's move to Slide 12 for an overview of what this transaction means from a financial and valuation perspective. We believe this transaction has the opportunity to unlock substantial unrealized value for Xerox shareholders. Xerox shareholders today own 100% of Xerox, which include our 25% equity ownership in the Fuji Xerox joint venture. We neither control nor consolidate this equity stake in our income statement, and it is carried on the balance sheet at book value. Besides the operational inefficiencies I just described, this structure creates complexity in reporting as well as in how our investors model the joint venture interest. We believe this is resulting in a valuation disconnect in the marketplace about the true value of this joint venture interest.

Consolidating the entire Fuji Xerox with Xerox will allow us to create a much simpler and clearer financial profile and realize the full value of this joint venture interest. Investors will be able to see our global financial results on a consolidated basis and value it appropriately.

At the time of closing, Xerox shareholders will receive a $2.5 billion special dividend or approximately $9.80 per share. Beyond this substantial immediate cash return, they will own 49.9% of a much stronger and more competitive company. Further value will be created by capitalizing on significant growth and margin expansion opportunities, including $1.7 billion of cost savings by 2022, including $1.25 billion attributable to transaction cost synergies and $450 million attributable to Fuji Xerox’s cost-reduction program.
To demonstrate the value that will be unlocked through these transaction synergies, here, we have applied an illustrative industry multiple of 7 to 8x EBITDA to 100% of the $1.25 billion cost synergies. Our shareholders will get the benefit of 49.9% of that amount. When we discount back to today, that would equate to about $12 per Xerox share. This new value represents nearly 40% of our share price, and that's on top of about $9.80 per share of cash dividend, making this a highly value-enhancing transaction for our shareholders.

Let's now move to Slide 13. We have been taking decisive actions to better position Xerox and have considered multiple options and scenarios to drive the greater shareholder value. We firmly believe that this combination is the best way to create value for our company and shareholders. Here are the reasons why. By combining with Fuji Xerox, we are creating a global industry leader with approximately $18 billion in annual revenue, adding significant scale and reach to our current market leadership. We believe this is the right strategic evolution of our long-term alliance as it will allow us to optimize the current operating structure for greater efficiency and global competitiveness.

We are projecting to deliver substantial cost savings for the combined company totaling at least $1.7 billion in annual savings, with $1.2 billion to be achieved by the end of the second year post close. The combined company will also have an accelerated path to delivering revenue growth, with direct access to fast-growing geographies as well as the ability to participate in future growth markets such as industrial printing and emerging intelligent work solutions.

Combining the IP strengths and world-class R&D capabilities of the 2 companies will drive innovation in areas that customers are most focused on and which will address future demand. In addition, we will be able to leverage Fujifilm's highly value-added intellectual property portfolio and innovation capabilities. And finally, we will have increased financial flexibility to deploy capital towards strategic growth investments and capital returns over time. I will detail each of these compelling reasons for the combination shortly. But before that, I want to delineate the value-enhancing components of this combination for our shareholders.

Moving to Slide 14. We see the value this transaction will create for Xerox shareholders as two-fold. First, Xerox shareholders will receive a significant and certain value in the form of a $2.5 billion special dividend immediately at closing, which is more than 30% of Xerox's unaffected share price as of January 10. Second, and more importantly, shareholders will become owners of a stronger company with enhanced growth prospects, significant margin expansion opportunity and a balance sheet that provides financial flexibility to invest in future growth, while delivering attractive capital returns to shareholders. By combining, we're immediately increasing the value of our shareholders' investment.

Turning to Slide 15. We are excited to be creating this new company with our joint venture partner of 56 years, Fujifilm. We have had a great partnership over the years and look forward to leveraging that history to ensure our new company's success. Both Xerox and Fujifilm leadership teams have significant experience executing large-scale transformations, which will be highly valuable in executing the integration of the 2 companies and achieving our ambitious goals for the new Fuji Xerox.

Slide 16 provides a snapshot of the combined company. The new Fuji Xerox will have truly global scale with $18 billion in revenue, presence in over 180 countries and already established leadership positions in fast-growing markets. We will have a total market opportunity that is currently estimated at $120 billion, with an additional $100 billion future opportunity in adjacent markets in industrial print, leveraging our combined technologies.

Innovation is in the DNA of both companies. Bringing them together will create a global innovation powerhouse with world-class research and development capabilities and industry-leading IP. And the financial profile of the company will be enhanced with an accelerated path to growth, significant cost savings and margin expansion opportunity, leading to high-teens operating margin and free cash flows of approximately $1.5 billion by 2020.

Before I go into further detail about the combined company's long-term creation opportunity, I'll touch on a few details of this transaction on Slide 17. As I've mentioned, our shareholders will benefit from owning a part of a much stronger and more competitive company, with significantly enhanced prospects for revenue growth and margin expansion. This will be supported by an expected investment-grade credit profile at closing. The combined company's capital return policy will be aligned with Xerox's current plan, maintaining a $1 per share annual dividend and at least 50% of combined free cash flow return to shareholders.
As for the governance and leadership team of the combined company, I will have the honor to lead the combined company as CEO. I am pleased to announce that Shigetaka Komori, Chairman and CEO of Fujifilm, will serve as Chairman of the Board of the new Fuji Xerox. Mr. Komori has been a transformational leader at Fujifilm having successfully reinvented the company. We will build a world-class management team, pulling from a deep talent at both companies. The new company board will include 7 directors appointed by Fujifilm and 5 independent directors from the current Xerox Board. The combined company will be named Fuji Xerox and trade on the New York Stock Exchange under our current ticker. We believe it is important to retain our brand’s strengths in our operating regions, which is why we will continue to go to market as Xerox and Fuji Xerox in our respective regions. We expect to meet the conditions and obtain the necessary approvals to complete the transaction in the second half of 2018.

Turning to Slide 19 and the strategic rationale I outlined a minute ago, I’d like to take a few minutes to walk you through a bit more detail on the many reasons why this deal was so compelling to Xerox and our shareholders.

Turning to Slide 20. As I mentioned before, we’re excited to create an industry leader with approximately $18 billion in annual revenue, which puts the combined company in the top ranks of global print technology businesses. Establishing this leadership position is especially important in today’s competitive environment, which requires broad global reach and scale to be able to effectively and rapidly meet customers’ demands around the world. Bringing together the geographic, product and innovation profiles of these 2 companies will amplify our market leadership and enable us to more effectively compete for global deals and provide opportunities for future share gains.

Turning to Slide 21. This combination also creates significant cost saving and margin expansion opportunities. We expect to deliver our $1.7 billion in annual cost savings in total through 2022, with $1.2 billion of the total cost savings expected to be realized by the end of the second year post close. The total cost-saving target includes $1.25 billion in transaction synergies as well as a separate cost-reduction program that will be implemented at the existing Fuji Xerox joint venture and is expected to generate $450 million in annual savings. These amounts are all in addition to Xerox’s ongoing Strategic Transformation cost productivity program. Given our proven track record of driving operational excellence and efficiencies as well as our long history of working together with the Fuji Xerox team, we are very confident of our company’s ability to deliver these savings.

I will now go into more detail on the sources of these savings on the next slide. Of the $1.7 billion in total annual cost savings, a large portion of the reductions will come from cost of goods sold through supply chain optimization, such as manufacturing, sourcing, procurement and vendor consolidation. We also identified significant opportunities from the elimination of duplicative corporate functions and R&D spend. Finally, the Fuji Xerox joint venture is commencing a cost-reduction program immediately, which is expected to deliver approximately $450 million in annual cost savings by 2022. This program is specific to Fuji Xerox and is incremental to the synergy opportunities I just discussed. It will focus on driving efficiencies in manufacturing, R&D and SG&A as well as product portfolio optimization. We expect these efforts to be front loaded, with more than 70% of total savings being delivered by year 2 and 85% by year 3.

Moving to Slide 23. This transaction is extremely compelling from a revenue standpoint as well. The combined company will have an improved revenue profile, with a greater mix of revenues from fast-growing markets in Asia Pacific. As you can see, Fuji Xerox currently has a strong presence in growing markets such as China and the rest of Asia as well as #1 share in Japan.

As I noted earlier, the combined company will have a nearly $120 billion market opportunity compared to the approximately $85 billion we were able to target as a stand-alone company. Upon completion of the transaction, Xerox will have the opportunity to participate in these markets while benefiting from Fuji Xerox’s established leadership positions and market know-how. The combined company will also have an accelerated path to future revenue growth as we integrate, including the ability to leverage each company’s deep customer relationships, regional networks, shared IP, product portfolios and complementary distribution and service capabilities.

On Slide 24. With 6 world-class innovation labs globally and nearly 11,500 patents, the new Fuji Xerox will have world-class R&D capabilities. Fuji Xerox’s expertise in areas such as automation, security and analytics, will be highly complementary to Xerox’s hardware and materials technology. Combining these existing assets with a nearly $1 billion R&D annual spend will enable us to sharpen our focus on innovative print technologies and work solutions, with the aim of accelerating our participation in the more rapidly growing markets. Together, we will be well-positioned to lead the future of printing and enterprise technology and capture next-generation growth opportunities.

With that, I’ll pass it to Bill to provide more details on the financial profile of the new Xerox.
William F. Osbourn - Xerox Corporation - Executive VP & CFO

Thank you, Jeff, and good morning, everyone. I will start with an overview of the new company’s financial profile and long-term targets, which will help clarify the significant value we’re creating through this combination.

As Jeff explained, the transaction we announced today will create a stronger company with enhanced growth prospects and margin expansion opportunities. And as you can see on this slide, we are expecting a rapid acceleration of the combined company’s financial performance over the next 4 years. While we made significant progress toward improving our revenue trajectory over the last year, we continue to experience revenue declines. The combination with Fuji Xerox will allow us to accelerate our growth by providing access to key growth markets, unlocking synergy opportunities and leveraging each other’s competitive advantages.

We’re starting from a base of $18.2 billion in pro forma combined annual revenues, and we expect to return to revenue growth by 2020. From an operating margin perspective, the cost-savings opportunities we identified will drive significant margin expansion over the next 4 years, with the majority also being realized by 2020. As we begin realizing the benefits from the targeted cost savings, we expect to achieve industry-leading operating profit margin in the high-teens by 2022, which compares to a blended margin rate of 10% on an adjusted basis in 2017. It is important to note that the lower operating margin rate for the combined company versus the 12.8% for stand-alone Xerox in 2017 is primarily due to backing out equity income and royalty revenue from the Xerox margin and adding Fuji Xerox in at a lower margin.

We expect total restructuring charges of $1.4 billion related to the targeted transaction synergies and Fuji Xerox separate cost-reduction program, which will be incurred predominantly in the first 3 years, in line with the progression of cost savings that Jeff walked you through. These will impact cash flows in the first few years, but the new company will continue to generate robust free cash flow, which is expected to reach $1.5 billion by 2020. Additionally, we anticipate approximately $80 million in annual tax dis-synergies associated with the transaction.

Finally, we expect the transaction to be EPS accretive in 2020. Overall, this transaction clearly enhances the financial profile of both Xerox and Fuji Xerox. There is a very significant synergy opportunity over time, and this transaction allows us to go after both revenue growth and cost far beyond what we could do alone.

Turning to capital structure and balance sheet. A preliminary high-level view of the pro forma capital structure of the combined company results in $1.8 billion combined cash and $8.6 billion total debt on the balance sheet as of December 31, 2017. This includes the transaction-related cash outflows of $350 million needed to pay down a mandatory pension contribution triggered by the transaction and debt associated with the $2.5 billion special dividend to Xerox shareholders at the closing, which will be funded by bridge financing that has been secured. Following the announcement and before the close, the new Fuji Xerox plans to put in place permanent financing, including an amended revolver. All Fuji Xerox and Xerox debt is expected to be retained in the combined company’s balance sheet post transaction.

As mentioned, the combined company will have a robust cash flow generation capacity, particularly beyond 2020. This will further strengthen the balance sheet and provide more financial flexibility for the combined company for attractive capital deployment, which I will discuss on the next slide.

The new company is expected to have an investment-grade credit profile and is committed to maintaining this over time. And the new Fuji Xerox will uphold the principles that currently underpin Xerox’s disciplined return on investment approach. With an investment-grade credit profile, the combined company will have broader access to capital markets and the financial flexibility to support all its operations. We will remain committed to delivering an attractive capital returns to our shareholders. The new Xerox will maintain the current Xerox $1 annual dividend per share as well as the target to return at least 50% of free cash flow to shareholders.

Moreover, our increased cash flows will enable us to make M&A growth investments. Having the financial flexibility to seize value-creation opportunities is key to our strategy of returning to revenue growth. Over time, the new company is expected to have greater capital deployment opportunities toward targeted growth initiatives, increased dividend and share repurchases.

With that, I’ll turn it back to Jeff.
Thank you, Bill. To conclude, today is a significant moment in the next chapter for our company and shareholders as well as the industry. The strong fourth quarter and full year 2017 performance we announced not only show clear progress on our stand-alone strategic goal, but also provide positive momentum for the future and a solid foundation for the combination with Fuji Xerox.

We are energized by the opportunities inherent in taking our Fuji Xerox joint venture to the next level, combining 2 industry leaders in unlocking significant value while unleashing innovation for future revenue streams. The proposed transaction will create substantial value to Xerox shareholders through a combination of an immediate special cash dividend and the opportunity to realize value from the future growth of a significantly stronger combined company.

We are excited about the progress we have made at Xerox and the resulting performance improvement. While we work to finalize this transaction, we at Xerox remain committed to continuing our progress and further strengthening the company as we move into 2018.

With that, I will hand it over to Jennifer.

Jennifer Horsley - Xerox Corporation - VP Investor Relations

Thanks, Jeff. Before we get to your questions for Jeff and Bill, I will point out that we had posted on our Investor Relations website the full set of our normal earnings slides to provide you with the details around our fourth quarter results. (Operator Instructions) At the end of our Q&A session, I will turn it back to Jeff for a few closing comments.

Operator, please open the line for questions now.

Shannon Siemsen Cross - Cross Research LLC - Co-Founder, Principal and Analyst

Congratulations on the deal.

Jeffrey Jacobson - Xerox Corporation - CEO & Director

Thanks, Shannon.

Shannon Siemsen Cross - Cross Research LLC - Co-Founder, Principal and Analyst

Can -- I just want to walk through quickly so people -- so I make sure I'm correct on exactly what you're getting. So effectively, if you're a Xerox shareholder today, you're getting $10 a share in the dividend, you're getting $12 effective benefit from a synergy that you expect to receive in the next few years and then you get 50% share in a company that for fiscal -- or sorry, for 2017, generated about $2.6 billion in EBITDA and you expect will maintain an investment-grade balance sheet.
Jeffrey Jacobson - Xerox Corporation - CEO & Director

So Shannon, it’s Jeff. Thank you, and I think you’ve summarized it very well. So again, it’s a $2.5 billion dividend that we have said is about $9.80 per share. There will be $1.7 billion in total cost reductions. That’s the $1.25 billion in transaction cost synergies, plus the $450 million from Fuji Xerox. If you put a normal industrial multiple of 7 to 8x EBITDA on the $1.25 billion, I think we get to the numbers that you stated. And then they get 49.9% of a growing, thriving company that you mentioned. So I think you’ve nailed it pretty well.

Shannon Siemsen Cross - Cross Research LLC - Co-Founder, Principal and Analyst

Okay. I just want to make sure because I’m getting over $50 a share in value, so I just wanted to make sure that was correct. So with that then, can you talk a bit about, as we look at the company over the next couple of years, you’ve laid out synergies, but how should -- how are you thinking about, first, how the company is going to operate together? What are your first sort of focuses to make sure that go-to-market remains very consistent and then you can continue to see improvement, for instance, on the equipment sales side of things? And then can you talk a bit about like the goalpost we should look for? So again, we know synergies. But beyond that, are there things that we can look toward to see that this combined company is effectively executing?

Jeffrey Jacobson - Xerox Corporation - CEO & Director

Yes, sure. So Shannon, this is -- the most exciting part of this is, as you said, it’s the go-to-market and it’s the innovation aspects. The cost synergies drive tremendous value that you delineated in the question you gave. What I really like about this is when you go through integrations, people worry about the integration complexity. What we’re doing now is we get to participate in growing markets. So Xerox is participating in about an $85 billion market that was declining at about 3%. We now have access through Fuji Xerox to a $36 billion market that’s growing at 2%, with very large shares in China, Asia Pacific and Japan. And the beauty is we don’t have to worry too much about complexity of integration of go-to-markets because the go-to-markets for the most part will stay exactly as they are. What I get really excited about is when I look at the innovation and getting into the new markets by combining technologies. One of the things in unlocking the value is we tended to have duplicative R&D. And now, we’re going to be able to divide and conquer. We’ll be able to take the 6,500 engineers that this combined company has, that produces about 1,500 patents a year over the last few years and accelerate innovation in the areas of industrial print, which is a $100 billion market that is untapped for us today. You know the packaging market very well, flexographic corrugated labels, folding carton, that’s still very much an analog market that’s not digital. We can take our print technologies and move them into the area on non-paper substrates, printing on objects, virtual reality, Internet of Things, machine learning, voice activation for multifunction devices. So while the cost synergies will provide the value that you delineated, the future is all about the innovation and the growth and the access to the growing revenues.

Operator

Our next question will come from the line of Katy Huberty with Morgan Stanley.

Kathryn Lynn Huberty - Morgan Stanley, Research Division - MD and Research Analyst

My congrats as well both on the quarter and the deal.

Jeffrey Jacobson - Xerox Corporation - CEO & Director

Thank you, Katy.
Kathryn Lynn Huberty  -  Morgan Stanley, Research Division - MD and Research Analyst

I guess 2 questions. One, do you have a view yet as to whether Xerox’s largest shareholders would be supportive of this deal? And then secondly, you just did a good job walking through some of the innovation and revenue synergy opportunities. How quickly do you expect Xerox to take advantage of some of the IP end markets that Fuji plays in that Xerox does not? Is that something you see happening over the next couple of years? Or are those growth opportunities beyond 2020?

Jeffrey Jacobson  -  Xerox Corporation - CEO & Director

Yes. So let me take the two-part question, Katy. So first, regarding the largest shareholder, we have not spoken. Obviously, this is a transaction that’s been in the works for many months, so we have not spoken on that issue. So we just don’t know, and we only know what we read at this point. With regard to integration and access, one of the exciting areas, if you were to look at inkjet as an example, right now, we have separate strategies for Fuji Xerox on inkjet, Fujifilm on inkjet, Xerox on inkjet. And you definitely know very well, Fujifilm has tremendous IP in the areas of inkjet heads, certainly ink capabilities as well, and we’ll be able to leverage those. When we talked about it and through the conversations we’ve had through this negotiation with Fuji Xerox, but certainly with Mr. Komori and the team at Fujifilm, one of the things was about how do we divide and conquer, how do we take the best technologies of what was all 3 companies and unleash it so that we can apply people who are working on some of the things I talked about, like in Palo Alto Research Center, whether it’s augmented reality, Internet of Things, machine learning; and then we have people on our Yokohama facility in Japan working on the other things that we need to. Now we do need to be a little careful because this will be the integration phase. So there are certain things we’re allowed to discuss and work on, and there are certain things we cannot. So for the next few months, and we expect to close this transaction sometime in the second half, we can only do a lot of planning. And then hopefully, we’ll hit the ground running upon the close.

Operator

Our next question will come from the line of Ananda Baruah with Loop Capital.

Ananda Prosad Baruah  -  Loop Capital Markets LLC, Research Division - MD

Congratulations from me as well. Look, there’s a million questions. I’ll try to keep it short here, so I’ll bundle. So do the synergies include -- the cost synergies, do they include what were the existing synergies? Or are the existing synergies incremental? And then I guess why not, if I read this right or heard this right, why not non-GAAP accretive in 2019 if you’re closing in ’18? And I might try to squeeze a follow-up then.

William F. Osbourn  -  Xerox Corporation - Executive VP & CFO

Yes, a couple of things, Ananda. First of all, regarding the synergies. The $1.7 billion, the $1.25 billion combination synergies in addition to the $450 million cost-reduction program at Fuji Xerox, that $1.7 billion is in addition to our ongoing Strategic Transformation program, which we in our regular earnings document that Jeff went through briefly, upped to $1.7 billion over the 3 years, approximately about $475 million in 2018. So those are in addition to the $475 million that we were doing in Strategic Transformation on our own. As far as accretiveness in 2019, there are -- there’s a benefit the synergies will be coming through relatively quickly as we’re incurring cost upfront to obtain those. But our analysis is that we will be getting it in 2020.

Jeffrey Jacobson  -  Xerox Corporation - CEO & Director

Yes, Ananda, let me give you a little background on that as well. Because if you think about it, one is on the $2.5 billion we’re going to have interest on the dividend. The equity income, we will no longer get. And then in order to do this deal basically, we’re doubling the amount of shares, so if you think about it from that standpoint. So if you were to look at Xerox today, and let’s just use the round figure about $8 billion market cap, and we deduct the dividend of $2.5 billion, let’s value Xerox from that standpoint at $5.5 billion, we then double the share count; and that $5.5 billion,
by doubling the share count, buys us 75% of Fuji Xerox, implying the $7.3 billion value. Now knowing the company and having worked with them as long as we have, we certainly view the intrinsic value is much more than $7.3 billion. So -- but it's really -- there are 3 factors: we normally get the equity income, we're doubling the shares and interest on the dividend.

Ananda Prosad Baruah - Loop Capital Markets LLC, Research Division - MD
Got it. That's helpful. And then just last one real quick. The free cash flow generation, I think you guys mentioned $1.5 billion to start. And then I think there was a remark that, but it will be greater than that, and it would seem that it would have an opportunity much stronger than that. So could you just give us some context around that remark?

William F. Osbourn - Xerox Corporation - Executive VP & CFO
Yes. I don't want to give a specific guidance out beyond 2020. But looking at the significant cost of $1.4 billion that we'll be incurring to effect the synergies predominantly in the first 3 years, we don't expect those to be continuing on. And absent those costs, we would expect even significant free cash flow over and above the $1.5 billion we cited.

Operator
And our next question will come from the line of Matt Cabral with Goldman Sachs.

Matthew N. Cabral - Goldman Sachs Group Inc., Research Division - Equity Analyst
So on the $1.7 billion in savings for the combined company, Jeff, can you just talk a little bit more about just how you arrived at that number? And how we should think about the net amount of that dropping through versus what you think you'll have to reinvest in the business over time?

Jeffrey Jacobson - Xerox Corporation - CEO & Director
Yes. So we've actually done a lot of work on that, Matt. And we've had numerous meetings throughout this negotiation process, and we've done a lot of work with both Fuji Xerox and Fujifilm, outside advisers, et cetera, as we worked through this. So the way I would look at it is, first of all, the total $1.7 billion, and again, that will be an excess of what Xerox is already doing as part of our Strategic Transformation program, that $1.7 billion will be by the end of 2022. Of that $1.7 billion, about $1.2 billion will be by the end of the second year post close, so let's call it 2020, which will be 70%: and 85%, it would be by the end of 2021 or the third year. Most of that $1.25 billion will flow right to the bottom line, okay? So the vast majority of the -- so I'd say on the $1.7 billion, somewhere in the neighborhood of about 80% will flow through the bottom line.

Matthew N. Cabral - Goldman Sachs Group Inc., Research Division - Equity Analyst
Got it. And then just a clarification, a follow-up for Bill. So FX was a nice tailwind to revenue in Q4. The revenue guidance you gave was on a constant currency basis. Can you just help us understand how you're thinking about, as of today, the FX impact on both revenue and operating margins for 2018?

William F. Osbourn - Xerox Corporation - Executive VP & CFO
Yes. We have modeled that in, obviously, to our guidance. And we do see it, based upon recent rates being a tailwind both from a translation currency perspective in '18 and from a transaction currency as far as effect on profits, we're estimating that at least a $50 million tailwind and -- could be higher based upon recent rates for 2018.
Jim Suva - Citigroup Inc, Research Division - Director

First, a question about the fundamental Xerox relationship as it is today, just stand-alone; and then second, more about this new relationship. So first of all, this year and -- well, in 2017, you launched several new hardware products. Just can you update us on how they’re going? I believe they came out a little more staggered than what you thought. Are they completely all out the door now and into your retail distribution VAR channel? Or are they all trained? And when do we hit kind of the sweet spot of the most traction from those? And then I’ll ask a follow-up question on the Fuji Xerox after that.

Jeffrey Jacobson - Xerox Corporation - CEO & Director

Yes, thanks, Jim. No, for the most part, the products rolled out just as we thought they would. So as we discussed before during Q2, there were about 44 products that came out. So by the end of the first half, we had all 13 A3 products and 4 A4 products. And in the third quarter, we had the remainder of the A4 products come out. So if you remember at the last earnings call, we said we had some confidence, but we don’t want to get out too far ahead of ourselves. But based upon what we knew about our September equipment results, we had some confidence. The fact that, and I think the evidence is at constant currency, we grew our equipment sales revenue 1.5%, which was the first time since second quarter 2013 that the company has grown their equipment sale revenue line. So it’s been very well-received. Our channel partners are growing to the tune of about 65 last year. And we’re pleased with the trajectory and where things are moving.

Jim Suva - Citigroup Inc, Research Division - Director

Yes. But my question was, is the quarter that you just printed, is that the quarter where basically, they’re all in the channel, all your VARs are selling them and distributors are selling them, is that enough kind of the best of a [gift]? Or is that kind of the early ramp of it, and in 2018, they really hit with a lot more force than even what we saw in this quarter, Q4?

Jeffrey Jacobson - Xerox Corporation - CEO & Director

Yes. So Q4 was the first impact that you had seen. Admittedly, it was coming off of a Q4 2016, if I remember, was down about 10%, a little bit of an easier compare. When we get to Q1, what you’ll see is we were down about 5.7% at constant currency Q1 2017, compares now to these, we’ll get into some relatively easier compares in Q2 and Q3. Q2 2017, we’re down 14.6% at constant currency. And then Q3, we were down again double digit. So -- but the thing is people ask all the time, is this something we will get 4- or 5-quarter benefit out of the new products, but the multi-brand expansion strategy is the thing that will prolong this for a while. And the reason I say that is I keep coming back to this $15 billion multi-brand reseller market that we really never participated in. We only had about 1% market share. And as we can continue to grow the number of multi-brand reseller partners there, every share point is worth about $150 million. I’ll also mention that as a result of the transaction, as we’re going through best practices with Fuji Xerox, they have a similar, similar issue from the past where they haven’t focused on multi-brand resellers. And it’s an area that they’re going to explore, too, which is part of the beauty of bringing these 2 companies together is comparing the best practices. As I mentioned before, their market shares in Asia are much higher than our market shares. We’re going to adopt their best practices as well.

William F. Osbourn - Xerox Corporation - Executive VP & CFO

Just a follow-on to Jeff’s comments, Jim, just we gave full year guidance in the regular earnings materials that we believe is very strong full year guidance. But just we’ve historically given -- look, we don’t give quarterly guidance, but we give sort of expectations. And just from a revenues
perspective at constant currency, we said full year down 2% to 4%. We would expect, just given it is a more challenging compares, as Jeff said, Q4 was a good -- I mean, Q1 last year was a good quarter. We’d expect to be near the lower end of that 2% to 4% on the full year guidance in the first quarter. And as far as our adjusted operating profit margin, our 13% to 14% in the full year is due to seasonality that we expect to be slightly below the low end of that range, but are fully confident in being within the full year range of 13% to 14%. As far as adjusted EPS, historically, we gave -- well, we gave guidance for next year of $3.50 to $3.70, $3.60 being the midpoint. And historically, the first quarter has typically done about 18% to 20% of the total, just to give people some guidelines what we’re expecting in Q1.

Jim Suva - Citigroup Inc, Research Division - Director
Okay. And then my quick follow-up is, are there any governmental approvals or antitrust or just any type of government approvals aside from the shareholder approvals we need to just keep an eye on for this pending transaction?

Jeffrey Jacobson - Xerox Corporation - CEO & Director
Well, any transaction of this magnitude, Jim, always has to go through government regulatory review and then shareholder approval, as you said.

Jim Suva - Citigroup Inc, Research Division - Director
Right. But can you list now which ones those are specifically, if you happen to know? Or we can do that on a follow-up call.

Jeffrey Jacobson - Xerox Corporation - CEO & Director
(inaudible) would be the most notable.

Operator
Our next question will come from the line of Paul Coster with JPMorgan.

Paul Coster - J P Morgan Chase & Co, Research Division - Senior Analyst, Alternative Energy, and Applied and Emerging Technologies
Congratulations.

Jeffrey Jacobson - Xerox Corporation - CEO & Director
Thanks, Paul.

Paul Coster - J P Morgan Chase & Co, Research Division - Senior Analyst, Alternative Energy, and Applied and Emerging Technologies
To start, Bill, any view on where the debt will be issued and what kind of debt will be issued to support this? And Jeff, the most substantive question for you really is, is there any risk here of in-product harmonization near term of one or other of the regions being disrupted, the clients kind of not being clear on what the product strategy is and there’s some potential dislocation very short term?
William F. Osbourn - Xerox Corporation - Executive VP & CFO

Thanks, Paul. Just a couple of things on the debt. As we said in our prepared remarks, we'll be issued that investment grade where we're confident on that. We have a bridge financing that is committed to. We will, between now and the close, be looking to potentially issue a public debt associated with the $2.5 billion dividend. But details on that to come, but we are evaluating.

Jeffrey Jacobson - Xerox Corporation - CEO & Director

Yes. And Paul, on the second part of your question, actually, it's a very fair question and one that most people would think about. In this case, we actually have benefits of bringing the 2 together, and the reason is this. Our 2 companies, even though they were separate, we combine R&D, we combine manufacturing, we do it for each other, so we actually make the same products. So the beauty of it now is now we'll go to things like a common controller so we won't have separate front-ends. We'll have synchronized introduction of new products. So as an example in the past, Fuji Xerox might roll out a product, and we wouldn't see it in our territories [until a year] later. We're going to have opportunities of also synthesizing our supply chain. When I look at areas, the thing that really excites me because -- well, I've never run a manufacturing facility. I've run companies that have very -- been very intense in supply chain and manufacturing. When we look at gross margin percentages, what happens is people always focus on price, and that's very important. But if you go back to the last 3 years at Xerox, our gross profit percentage has been relatively flat at 40% in a market that has price decline. The way we do that is we really get a lot of absorption and sweat the assets in our factories. We will have an even greater ability now to fill our factories in both locations, to get right absorption, which is a real benefit of bringing that together. And again, as I mentioned before, the coordination between our R&D centers to unleash innovation, we'll be able to compete much more effectively on global Managed Print Services deals to increase our win rates, best practice in shares. And then also, we won't have what I'll call the sharing of margin between the 2 businesses, which will be able to make us much more competitive on a global basis because we're not splitting the margin any longer.

Jennifer Horsley - Xerox Corporation - VP Investor Relations

Do you have another question, Paul?


No, I'm good.

Jennifer Horsley - Xerox Corporation - VP Investor Relations

Great. Operator, I think we have time for one last question.

Operator

Our last question will come from the line of Steve Milunovich with UBS.

Steven Mark Milunovich - UBS Investment Bank, Research Division - MD and IT Hardware and EMS Analyst

So it looks like there's elimination of a lot of current inefficiencies. Are there going to be any issues in terms of integration, particularly in R&D culturally? You've got 2 headquarters. What are you thinking about organizationally in terms of dealing with that? It's been kind of an arm's-length relationship in the past. Now it's going to have to be much tighter.
Jeffrey Jacobson - Xerox Corporation - CEO & Director

Yes. Steve, actually, so first, I never want to minimize integration because integration is always complex. But again, this is a 56-year partnership, so everything we had done over the decade has been joint R&D, joint manufacturing, joint product development. Our people know each incredibly well, and they've been doing this together for a long, long time. So instead of there truly being 2 separate companies that have never worked together, this is a case where if we introduce a product that came from Fuji Xerox in the past, it was with great involvement from Xerox people and vice versa. If it was Xerox introducing the product, it was with great involvement from Fuji Xerox. So from that standpoint, I think it'll be relatively seamless compared to most integrations.

Steven Mark Milunovich - UBS Investment Bank, Research Division - MD and IT Hardware and EMS Analyst

Okay. And I just want to ask about the sales margin, which was down. Is that because you're moving into more A4-type equipment? And where do you expect that to be heading?

William F. Osbourn - Xerox Corporation - Executive VP & CFO

Yes. Clearly, we have a commitment to A4, which on the upfront has a lower margin than our A3 and high-end products. And -- but we do believe that, obviously, over the life of that equipment that it is a very attractive margin. But upfront, as we are committing and building up our A4, we see and feel there is some impact -- negative impact on margin.

Jennifer Horsley - Xerox Corporation - VP Investor Relations

Great. Thanks, Steve. That's all the time we have for questions today. If you have further questions, please contact me or anyone else from the Investor Relations team.

Operator

Ladies and gentlemen, thank you for your participation on today's conference. This does conclude our program, and you may all disconnect. Everybody, have a wonderful day.