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# EDITED TRANSCRIPT

PBI - Q4 2012 Pitney Bowes Inc. Earnings Conference Call

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**OVERVIEW:**

PBI announced 4Q12 revenue of $1.3b and 4Q12 GAAP diluted EPS of $0.55. 2012 GAAP EPS came in at $2.21. Management announced 2013 guidance including revenues flat to up 3% and GAAP EPS from continuing operations of $1.85-2.00.

## CORPORATE PARTICIPANTS

**Charles McBride** *Pitney Bowes Inc - VP, IR*

**Marc Lautenbach** *Pitney Bowes Inc - President & CEO*

**Michael Monahan** *Pitney Bowes Inc - EVP and CFO*

## CONFERENCE CALL PARTICIPANTS

**Blaine Marder** *Loeb Capital Management - Analyst*

**Ananda Baruah** *Brean Capital - Analyst*

**Scott Wipperman** *Goldman Sachs - Analyst*

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## PRESENTATION

**Operator**

Good morning and welcome to the Pitney Bowes, fourth quarter and year end 2012 results conference call. Your lines have been placed in a listen only mode during the conference, until the question-and-answer segment. Today's call is also being recorded. If you have any objections, please disconnect your lines at this time. I would now like to introduce your speakers for today's conference call; Mr. Marc Lautenbach, President and Chief Executive Officer; Mr. Michael Monahan, Executive Vice President and Chief Financial Officer; and Mr. Charles McBride, Vice President Investor Relations. Mr. McBride will now begin the call with a Safe Harbor overview, please go ahead.

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**Charles McBride** - *Pitney Bowes Inc - VP, IR*

Thank you, included in this presentation are forward-looking statements about our expected future business and financial performance. Forward-looking statements involve risks and uncertainties that could cause actual results to be materially different from our projections. More information about these risks and uncertainties can be found in our 2011 Form 10K annual report, and other reports filed with the SEC that are located on our website at www.PB.com, and by clicking on the investor relations section. Please keep in mind that we do not undertake any obligation to update any forward-looking statements as a result of new information or developments. Also for non-GAAP measures used in the press release, or discussed in this presentation, you can find reconciliations to the appropriate GAAP measures in the tables attached to our press release and also on our investor relations website. Additionally, we have provided slides that summarize most of the points we will discuss during the call, these slides can also be found on our investor relations website. Now our President and Chief Executive Officer, Marc Lautenbach will start with a few opening remarks. Marc?

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**Marc Lautenbach** - *Pitney Bowes Inc - President & CEO*

Thank you Charlie and good morning everyone. Let me start by thanking all of you for joining our discussion of the fourth-quarter and full-year earnings. I've been at Pitney Bowes a little less than 60 days now. In that time, I have learned a tremendous amount about our Company, about our capabilities, but as you would guess, it would be premature for me to declare a new strategy for our Company at this early date. I will, however help you begin to understand the way and through which I am working at the business, by telling you a little bit more about my background at IBM and what I've been doing since I've been here at Pitney Bowes.

Two thirds of my executive career at IBM was in small and medium business. I had pretty much every executive role there was inside that business. I had substantial rolls in our inside sales organization, which was responsible for the preponderance of our relationships in account management. I had substantial positions in marketing, and in 1998, I moved to Asia to run our small and medium business operation in Asia Pacific. And finally, in 2001 I was named General Manager of small and medium business for all of IBM, responsible for all of our operations.

In that time, we completely redesigned our strategy, we re-engineered the go to market, using telesales, third parties, and the web, dramatically increasing our reach into the market driving efficiencies and, ultimately better client service. We created the express product line, a product line designed specifically for the mid-market. And we moved substantial resources to growth. The net result was that the SMB business at IBM became a substantial contributor to IBM's top and bottom line.

More recently, I was the managing partner of IBM's consulting and systems integration business in North America. The focus of that organization was to help businesses become globally integrated enterprises. Said another way, helping organizations implement standard processes, standard systems, to take advantage of their global scale. In 2009, we shifted our focus, to help clients make their client facing functions, that is marketing, sales, client service, billing, more effective.

During my IBM career I had the privilege to work from two work class CEOs, Lou Gerstner and Sam Palmisano. From Lou I learned about the importance of strategy, and how to drive transformations from the client back into the Company. From Sam, it was all about execution, and from both of them, how to deliver substantial shareholder value.

I was attracted to Pitney Bowes because I believe it has all the necessary ingredients to be a great Company. It has a great financial model, a strong and dependable market position, a great brand name and perhaps most importantly, a wonderful client base. Pitney Bowes also has a set of challenges and opportunities that I understand well from my previous experiences. In a little less than two months here, I've spent substantial time with our clients, both small, medium and large. I have spent time with the US Postal Service, spent time with the Australian Post, and I've spent a lot of time getting to know our employees. As you also guess, I have spent a lot of time learning about our businesses through business reviews and learning about our businesses through our clients.

I have particularly enjoyed and quite frankly have been very impressed about learning about the Company's technologies. I will have a lot more to say about the Company, and our going forward plans at our investor briefing in mid-May. As Mike will discuss, there was movement in a positive direction in the fourth quarter, that said, we can and we must do more. I'm encouraged that there is a strong base to build off of, and I believe this Company can control its investing. Now let me turn it over to Mike to our discuss our 2012 results for the quarter, and for the year. Mike?

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**Michael Monahan** - *Pitney Bowes Inc - EVP and CFO*

Thanks, Marc, this morning we reported results for the fourth quarter and full year 2012, during the quarter we had growth in four of our business segments, and we expect some of these positive trends to continue into 2013. I will discuss those trends in more detail as I take you through the results of each of the business segments. Additionally, our Board of Directors approved a first quarter dividend of $0.375 per share for our common stock.

Before we get started though I want to remind everyone that as we announced last quarter, we intend to sell our international mail services business, which was part of our mail services segment. As a result, this business is now treated as a discontinued operation, and therefore our results for 2012, 2011 and 2010 have been restated to reflect this. Restated financials by quarter can be found on our investor relations website.

Now let me take you through the results. The fourth-quarter revenue totaled $1.3 billion, a decline of 1% compared to the prior year on both a reported and constant currency basis. This quarter's decline in revenue is the lowest year over year rate of decline in five quarters. Revenue benefited from growth in the international segment of our mailing business, our software business, management services and mail services. However, revenue was adversely impacted by the decline in recurring revenue streams in our mailing business, but at a lower rate of decline than in the prior year. Adjusted earnings per share from continuing operations for the quarter were $0.56, compared with $0.98 per share for the same period in 2011.

2011 adjusted EPS from continuing operations included a $0.37 per share benefit related to favorable tax settlements last year. GAAP earnings per diluted share for the quarter were $0.55, GAAP EPS included a $0.07 per share charge for restructuring. GAAP earnings per share also included income of $0.06 per share from discontinued operations. Which was the net of income from the resolution of certain tax matters this quarter of $0.07 per share, and a loss of less than $0.02 per share related to the international mail services business. GAAP EPS for the fourth quarter 2011 were $1.28, which included charges totaling $0.72 per share for goodwill, restructuring and asset impairments. It also included income of $1.03 per share in discontinued operations, which was primarily related to certain net tax settlements during the quarter. For the full year, revenue for the year declined 4% on a reported basis, and declined 3% when the impacts of currency are excluded.

Approximately 68% of the revenue came from the US, and 32% came from outside the US.

Adjusted earnings per share from continuing operations for the full year 2012 were $2.18, compared with $2.75 per share for the same period in 2011. 2012 adjusted EPS from continuing operations included an $0.11 per share benefit related to favorable tax settlements, while 2011 adjusted EPS from continuing operations included a $0.44 per share net tax benefit. Excluding these tax benefits, comparable adjusted EPS from continuing operations for 2012 were $2.07, compared with $2.31 in 2011.

GAAP earnings per share for 2012 were $2.21, GAAP EPS included a net charge of $0.08 per share for restructuring, as well as a net benefit of $0.06 per share from the sale of leveraged lease assets. GAAP earnings per share also included income of $0.05 per share from discontinued operations, which is the net of $0.17 per share of income from the resolution of certain tax matters, and a loss of $0.12 per share related to international mail services.

GAAP EPS for the full year 2011 were $3.05, which included charges totaling $0.89 per share for goodwill restructuring, and asset impairments. It also included income of $1.07 per share in discontinued operations, which is the net of a $1.31 per share of income related to certain net tax settlements during the year, and a $0.24 per share loss related to the international mail services business.

Adjusted results for this quarter, this year and the prior year exclude the impact of restructuring and asset impairment charges, goodwill charges, asset sales and tax settlements that may have occurred in those periods that are not usual occurrences when considering normal ongoing operating results. A reconciliation schedule of GAAP to non-GAAP measures is included in the earnings press release, and posted to the investor relations section of our website.

The remainder of my discussion will focus on the results for the fourth quarter. All income statement related references and net results are on an adjusted basis.

Looking at the income statement, adjusted earnings before interest and taxes or adjusted EBIT, was $216 million this quarter, and the adjusted EBIT margin was 16.7%. Adjusted EBIT this quarter included an incremental investment of $2 million for Volly versus last year, and approximately $2 million for infrastructure and related costs associated with our e-commerce growth initiative. Last year's EBIT margin benefited from a $9 million insurance reimbursement related to the Dallas facility fire.

Adding back depreciation and amortization, EBITDA for the quarter was $280 million, or $1.38 per share.

Selling, general and administrative expenses, or SG&A, for the quarter was $410 million, a decline of $15 million versus the prior year. As a percentage of revenue, SG&A was 31.9%, which was a 70 basis point improvement versus the prior year. SG&A continues to benefit from ongoing productivity initiatives and good credit experience, as well as lower employee benefit costs.

As we highlighted in the third quarter, we are building on the success of the strategic transformation program, and have identified further opportunities to reduce costs and streamline the business. As a result, during the quarter, we identified approximately $40 million in new restructuring initiatives that are expected to generate incremental savings in the range of $45 million to $55 million. We expect to realize most of these savings in the second half of 2013. And although we are investing $40 million in new restructuring initiatives this quarter, the net charge was $22 million. That was because we did not have to spend as much as originally anticipated to implement certain changes in our 2009 strategic transformation program. However we were still able to achieve more than our targeted savings goals.

Net interest expense which includes financing interest, declined by about $4 million, compared with the prior year. The average interest rate this quarter was 4.7%, which was 10 basis points higher than the prior year. However, our average outstanding borrowings during the quarter were $314 million lower than the prior year.

The effective tax rate on adjusted earnings for the quarter was 30.2%, versus a tax credit of 5% last year. The tax rate last year benefited from the resolution of certain tax matters.

Balance sheet and cash flow items on the balance sheet or cash flow during the year -- cash flow during the quarter was $253 million and it was $769 million for the year. On a GAAP basis, we generated $256 million in cash from operations for the quarter, and $660 million for the year. We continue to closely monitor our cash flow results and working capital requirements, and remain focused on maintaining a strong balance sheet. We returned $84 million of cash to our shareholders in the form of dividends, and had $14 million of restructuring payments related to our restructuring programs. We are committed to a prudent use of cash that will enhance long-term shareholder value.

We had $4 billion of debt on the balance sheet at the end of the quarter, which was $217 million less than the amount of debt at the end of 2011. Our debt is lower than 2011 even though we obtained $230 million of term bank loans during the quarter, and issued $110 million of retail debt. We expect to use the proceeds of both of these borrowings, to pay down debt that is maturing later this year.

Now I would like to discuss the fourth quarter results for each of our business segments. This information can also be found in our earnings press release, and the slides that are posted to the PB.com website, under the investor relations section.

North American mailing revenue for the quarter was $456 million and EBIT was $174 million. North American mailing revenue growth was impacted by lower recurring revenue streams, but we have seen a continuation of improvement in trend. Also, the decline in equipment sales of 3% versus the prior year is an ongoing improvement in the trend we have seen for the last six quarters. Equipment sales during the quarter benefited from increased placements of our SendSuiteLive shipping solutions.

EBIT margin was lower than the prior year due to our placing more new equipment at lower margins, rather than doing more lease extensions on existing equipment. Also, there was a decline in high-margin recurring revenue streams.

International mailing revenue for the quarter was $188 million and EBIT was $26 million. Year over year revenue growth was 4%, excluding currency and was driven primarily by equipment sales in the Nordics, and sales of our Connect+ mailing systems in France and Germany. EBIT margin improved year over year due to improved service margins and productivity initiatives.

Turning to the enterprise business solutions group...

Production mail revenue for the quarter was $152 million, and EBIT was $14 million. Production mail revenue declined by 6% year over year due to economic weakness around the world in prior periods, however the business finished the quarter with one of its best backlog of orders in recent years. It is expected that this backlog will help drive revenue in future periods. EBIT margin declined due to lower revenue mix of equipment sales, and an increased investment in Volly. Production mail margins would have been 510 basis points higher this quarter, if the investment in Volly was excluded.

Software revenues for the quarter was $105 million, and EBIT was $18 million. Revenue growth of 2% this quarter was attributable in part to an increase in the number large licensing deals for data quality and location intelligence products, such as Spectrum and GeoTAX. That was especially true in the Americas. However, the software business continued to experience challenges in Europe and Asia because of the ongoing economic uncertainty in these regions and the austerity measures in the public sector of many countries. EBIT margin improved significantly when compared to the prior year. EBIT margin benefited from revenue growth and productivity initiatives.

Management services revenue for the quarter was $242 million, and EBIT was $19 million. This was the first quarter of year over year revenue growth in Management Services since the third quarter of 2008. Revenue was helped by positive net new written business in previous quarters and a year-end increase in the volumes of documents process. The business continues to experience positive net new written business, and this is expected to help drive revenue in future periods. EBIT margin benefited from an increase in revenue, and continued expense management.

Mail services revenue was $113 million and EBIT was $20 million. Revenue in mail services again benefited from growth in the presort operations, driven by continued penetration in workshare discount categories, as well as increased co-transportation of mail for customers. While our ecommerce growth initiative is still in its early stages, it provided a small incremental contribution to revenue growth this quarter. Ecommerce is expected to continue to ramp-up throughout 2013. EBIT for mail services included a net incremental investment of $2 million in our ecommerce offering. Also, year over year EBIT comparisons are impacted by the $9 million insurance proceeds we received in the fourth quarter of 2011. Excluding the insurance proceeds in the fourth quarter of 2011, EBIT for the underlying presort business was in-line with the prior year.

Marketing services revenue was $32 million and EBIT was $6 million. Revenue declined in part due to lower household move volumes during the quarter, while the EBIT margin improved due to lower print production costs, and ongoing productivity initiatives.

That concludes my comments on our business performance this quarter. Now I would like to discuss our 2013 guidance.

For 2013, we assume that there will not be a significant improvement or deterioration in the economic or postal environments worldwide. We believe that the enterprise solutions group, in aggregate, will generate revenue growth, and there will be a moderation in the decline of revenue in the SMB solutions group. We expect revenue will benefit from our growth initiatives of ecommerce and print outsourcing, and also from increased placements of our Connect+ mailing systems, and our SendSuiteLive shipping solutions. However, revenue is expected to continue to be impacted by a decline in recurring revenue streams, albeit at a lesser rate of decline than in 2012. The Company also expects that free cash flow will be less in 2013 than it was in 2012 because deferred taxes, depreciation and amortization, and finance receivables will provide less benefit to cash flow than the year before.

Based on these assumptions, the Company expects revenue excluding the impacts of currency, to be in the range of flat to 3% growth, when compared to 2012. GAAP EPS from continuing operations to be in the range of $1.85 to $2.00, which excludes any unusual items that may occur during the year. And free cash flow to be in the range of $600 million to $700 million.

The Company also expects that it will make continued investments in its growth initiatives that will result in higher expenses in the first half of the year. However, these investments are anticipated to lead to greater revenue and margin contribution in the second half of the year. Additionally, it is expected that the decline in recurring revenue streams will continue to moderate and will have less of a negative impact on revenue and earnings in the second half of the year. That concludes my remarks, operator can you now open the line for questions?

## QUESTIONS AND ANSWERS

**Operator**

(Operator instructions)

Blaine Marder, Loeb Capital Management.

**Blaine Marder** - *Loeb Capital Management - Analyst*

Hi guys, congratulations Marc and congratulations, welcome. I look forward to meeting you in person. Marc, as you start with the clean sheet of paper, as you know, the stock is down over 55% in the last five years. Can you give us a sense of one, your timing, in terms of reaching certain strategic decisions, what work you have left to do before you can do that? And two, give us a window into your thinking and the Board in terms of strategically addressing certain issues of the Company, such as debt levels, the level of the dividend, asset or business sales, and restructuring. Implementing some restructuring? Can you give us a window into your and the Board at least initial thoughts and thinking? Thank you very much.

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**Marc Lautenbach** - *Pitney Bowes Inc - President & CEO*

Sure, so lots in that question, let me first state that the obvious point that strategies are evolving, and on-going, so you ought to expect that we continue to clarify our strategy, going forward. But I would caution you to not think that there is going to be an epiphany that will be delivered upon the market. We will have more to say about our strategy for the respective businesses and our financial strategy in the Investor Meeting in May.

In terms of the second part of your question about capital structure and dividend, divestitures, acquisitions, I will let Mike comment more detailed, but the prism that are working through -- all of those decisions is, how is it that we create the maximum shareholder value? It is not lost on anyone around here, the Board of Directors or the leadership team, what has happened to the stock price. So as we think about those decisions going forward, it is through the lens of how it is that we create more shareholder value going forward. So I will let Mike elaborate further.

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**Michael Monahan** - *Pitney Bowes Inc - EVP and CFO*

Blaine, in terms of capital allocation, obviously we look at the needs of the business. We look at the balance of returning cash to shareholders as well as looking at the debt ratings, and our access to capital markets, and have taken an approach there to balance those over time and use the different mix as appropriate for the opportunities and all in the business. So as Marc said, we will continue to evolve that as the strategy of the business evolves, and obviously keep people posted on that.

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**Blaine Marder** - *Loeb Capital Management - Analyst*

Finally, Mike, to what do you attribute this slowing decline in both recurring revenues and equipment sales? Is it economy driven or Company specific initiatives or a little of both? Thank you.

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**Michael Monahan** - *Pitney Bowes Inc - EVP and CFO*

Sure, I would say it is somewhat of both, we have a situation where we have taken, brought some new products to market in the form of Connect+ , we have rolled that out globally. We have obviously been very focused on customer retention in the business as well. And we are seeing a really maturing of the lease base in particular. Where we have really about four years now, elapsed from the time that we saw a real drop-off in the economy, to that moving through the base and that is why we expect to see some improvement -- continued improvement -- in the trend in the underlying recurring revenue streams. And then obviously, getting some growth on the Enterprise side has been a benefit as well.

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**Blaine Marder** - *Loeb Capital Management - Analyst*

Thanks guys.

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**Operator**

Ananda Baruah, Brean Capital.

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**Ananda Baruah** - *Brean Capital - Analyst*

Just to kick it off there, following up on the last question, what might be your basic or basic set of philosophies to running a business and what might be some of the things that for you after 60 days might seem like they might fit well with Pitney or be the most obvious for you to bring to bear on the business as you get started? And then I have a couple of follow-ups. Thanks.

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**Marc Lautenbach** - *Pitney Bowes Inc - President & CEO*

Sure, in terms of philosophy, I'm not sure it is anything that's terribly divine. I do look at the business through three different lens - the first is foundationally, how do our clients see our business, second how do our employees see our business and finally, how do our shareholders see the business? And you work to balance the interest of those three constituents to drive value. To drive value for the client and to drive value for the shareholders. So that is, that is the foundation of how I am looking at the business.

As I said at the outset, when I describe my experiences in small and medium business, in terms of how we re-engineered the go-to market, how it is that we created new products, how it is that we moved resources to growth areas -- are all experiences that I have had in my previous life that color how I think about the small and medium business inside of Pitney Bowes. In terms of the Enterprise business, obviously in my most recent responsibilities inside of IBM were in a GBS business -- our consulting and systems integration business, which is a services business. We had deep relationships with many software companies. So I understand those businesses from the client, as well as the development forward. We will move forward. Right now we're focused on executing the first quarter and we have got plenty to do in the next 90 days to drive value for our clients and for our shareholders.

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**Ananda Baruah** - *Brean Capital - Analyst*

Yes, just with regards to the guidance, can you and Mike maybe talk to what you see as the drivers of the revenue growth for next year? It would be -- growth would be a pleasant change, pleasant shift, and maybe talk about which segments you expect to grow and those drivers of that? And then it seems like if you do grow revenue next year, it seems like the EPS guidance would imply margins actually being softer, just for the higher level, and could you talk to that as well? Thanks.

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**Michael Monahan** - *Pitney Bowes Inc - EVP and CFO*

Sure, I will take that one and yes we would all appreciate revenue growth. The growth will likely come, as I noted on the Enterprise side. We have seen a continued improvement in the Management Services business and positive growth there. We see the Software business as being able to contribute to that growth as well. Our newer initiatives, particularly around e-commerce and print outsourcing, both have the potential to contribute to growth. As we noted on the SMB side, or the Mailing side of the business, while we will still have some impacts on the recurring revenue stream, with the natural migration of the lease base, we do expect that to moderate more and we do expect there to be less of an impact as we go out over the course of the year from both the level of CP or lease extensions that we do, as well as more moderation in the lease base. Those are the major drivers with respect to the margins. It is obviously more of a mix shift between the higher margin Mailing business versus growth in some of the Enterprise businesses like Management Services, as well as some of the investment we are doing to ramp up some of the new growth initiatives.

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**Ananda Baruah** - *Brean Capital - Analyst*

Got it, thanks, that helpful. Last one for me, you announced approval of the dividend, but you did not raise the dividend. I think this is the first time in a while. So does that signify any shift in the dividend policy or is that reading into it too much?

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**Michael Monahan** - *Pitney Bowes Inc - EVP and CFO*

As we of said in the past, the Board reviews and approves the dividend each quarter, and we kept it flat in the first quarter in part to allow Marc to complete his strategic review of the business. We expect to make capital allocation recommendations in-line with that strategy, and in-line with opportunities in business as we go forward.

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**Ananda Baruah** - *Brean Capital - Analyst*

Got it thanks a lot, guys.

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**Operator**

Scott Wipperman, Goldman Sachs.

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**Scott Wipperman** - *Goldman Sachs - Analyst*

Mike, I think you mentioned in your comments about some of the success of the Connect+ machines in your International Mailing business, first, is there a reason why you're seeing better success with that in the international markets versus North America? And then I have a couple of follow-ups.

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**Michael Monahan** - *Pitney Bowes Inc - EVP and CFO*

Sure, yes, there is a reason and that is a product that has to get approved, market by market, around the world. It was most recently approved in France, which has generally been one of the later markets to get the product approved in. It is a large Mailing market, it's second-largest actually in the world to the U.S. And so the launch of that in France has been well received. And Germany was the market just before France. So again, we have seen good pick up of that product there.

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**Scott Wipperman** - *Goldman Sachs - Analyst*

Thanks, Marc maybe just some initial thoughts from you just on how you view some of these Software investments, specifically, I'm wondering your views on the Volly initiative? I have one other follow-up after that.

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**Marc Lautenbach** - *Pitney Bowes Inc - President & CEO*

Yes, I think the -- and obviously, I'm 60 days into this, so I am still learning. I am very pleased, I'll say at the outset, to walk into a Company that has a set of software assets that I think can be the basis for our growth going forward. The interesting thing about the Software businesses to me is that as you grow those businesses, from a margin perspective, you actually mix up so you can increase your margins for the Company as you drive more and more Software growth. That is no easy feat given the great job that the Company has done on margins, life to date.

So I think that is a really interesting dynamic. I think the Software businesses going forward, should be a substantial part of our growth strategy. The part that is most intriguing to me is to look at the technologies, and the technology threads that run through our core business, you know you think of the meters, all the way through the Software business and how it is you drive synergies.

So I am excited, I think there is good opportunities there. We do have more to do in terms of concluding my strategic review of how we assemble those in a way that drives value for our clients, and importantly our shareholders. I think there are some things that are distinctive about Pitney Bowes that we can do that, with those assets. Volly, right now we are heads down completing our commitments to Australia Post. You will see that my focus can be very balanced between strategy and execution and right now on Volly, we are about execution in terms of delivering our commitments, and we will say more about how we go forward in the next 60 or 90 days.

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**Scott Wipperman** - *Goldman Sachs - Analyst*

Thanks. Just one last one, just Mike, we have seen some peers that have finance receivable portfolios look to right size those portfolios, divest them, divest some blocks of some assets, some receivables. Is that something that you guys are all looking at? And if you could just share with us how much cash generation came from the receivables in the quarter? Thanks.

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**Michael Monahan** - *Pitney Bowes Inc - EVP and CFO*

In terms of looking at the portfolio, we have looked at it periodically over time. In terms of ways or potentially securitizing or otherwise actually many years ago, we did some things like that. It is not terribly tax effective for us to do that today. And quite honestly, we find it valuable to have that linkage of the credit availability for our customers within our business model. So that is something we continue to evaluate but do not have an immediate plan around. In terms of the finance receivables, it was very minimal, only about a $3 million contribution to cash flow in the quarter, so relatively flat balances year-over-year.

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**Scott Wipperman** - *Goldman Sachs - Analyst*

Thanks for all the questions.

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**Operator**

Kartik Mehta, Northcoast Research.

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**Kartik Mehta** - *Northcoast Research - Analyst*

Thank you. Good morning. Marc could you, or maybe Mike, expound on the areas of investment you have going in 2013, what the three key areas are and how that compares to 2012? Are there areas where you may be investing more in 2013 or less, compared to 2012?

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**Michael Monahan** - *Pitney Bowes Inc - EVP and CFO*

Yes, there are a couple of key areas of investment, obviously we plan to continue to invest in Volly and we have assumed an investment level consistent with 2012. So, we do not expect that to be a variance year-over-year but we continue to make meaningful investment in that. As I mentioned, we have begun to implement our e-commerce program, and we are investing in building out both the technology and delivery platform around that business.

In terms of delivering with eBay, a very substantial product offering to their user base. And we began that rollout in the fourth quarter and will continue that throughout 2013. We are investing -- obviously we continue to invest in -- R&D across our business, and we expect R&D levels to be similar to what they were 2012. Those are some of the key investment areas.

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**Kartik Mehta** - *Northcoast Research - Analyst*

So Mike for, in the e-commerce, can you talk about maybe the level of investment, maybe the dollars, how that is impacting margins from right now until that product becomes something that is generating revenue in margins for you?

**Michael Monahan** - *Pitney Bowes Inc - EVP and CFO*

Sure, as I mentioned, there was about a $2 million incremental investment in the fourth quarter. Obviously as we build out that platform as the volumes scale, obviously we will see margin improvement in that business with the scaling of volumes. Part of the reason I talked about first half expenses being higher than second half expenses, is because we expect there to be an investment period in the first half of the year, and assuming that those volumes ramp as expected, then that could be a contributor in the second half of the year.

**Kartik Mehta** - *Northcoast Research - Analyst*

And then Mike, on the free cash flow side, as we move forward and Pitney hopefully continues to drive revenue. Will there be a period of time where you anticipate cash flow to be somewhat flat, and because of some of the drag or some of the lack of benefit from a finance receivables? Or should free cash flow, once again begin to improve as the revenue continues to improve?

**Michael Monahan** - *Pitney Bowes Inc - EVP and CFO*

Well, obviously the single most important variable in cash flow is earnings, so our focus is on getting back to earnings growth. That starts with getting the revenue growth, and getting the leverage from our infrastructure that Marc touched on and I touched on earlier in my comments. So that will be the most important piece. But we also think there is opportunities to continue to refine the working capital in the business and improve that. I expect finance receivables to be less of a contributor to cash as we go forward, and that is assumed in our guidance in 2013.

**Kartik Mehta** - *Northcoast Research - Analyst*

And then just a last question Marc, do you believe that it will be until May that you will wait to give your strategic vision or do you anticipate that you might talk about your strategy earlier than that?

**Marc Lautenbach** - *Pitney Bowes Inc - President & CEO*

May is the right expectation, so if you think about typical 100 days, that places you right into the middle of between now and then. So, we will have an Investor Day conversation in May and I think that will be a very natural time with the conclusion of my 100 days, Investor Day. We can talk about the first quarter. I think that gives me enough time to complete my understanding of the business and is a very natural time to communicate.

**Kartik Mehta** - *Northcoast Research - Analyst*

Thank you very much.

**Operator**

Shannon Cross, Cross Research.

**Shannon Cross** - *Cross Research - Analyst*

Thank you very much and Marc, welcome. My first question is on verticals and -- in terms of customers, verticals and what you heard geographically, Mike, from customers during the quarter. I am curious about where there were strengths and weaknesses and obviously with your products that we can see where that was? The other question I have, is do you see business getting better or worse as you went through the quarter? Obviously through the last first few weeks of the first quarter.

**Michael Monahan** - *Pitney Bowes Inc - EVP and CFO*

Sure, in terms of the verticals, obviously the one vertical that we probably saw the most impact from, I referenced in discussion of the Software business, was around government. Particularly in the European markets, where we have seen some impact of the cut back in budgets and all in some of the government agencies around the world. I do not think we have seen other verticals in particular that have had issues.

In terms of the second part of your question. The trend in the quarter, we did not see a big variation in the business. As you know, a significant portion of our revenue streams are recurring in nature. We did see some better print volumes in PBMS towards the end of the quarter, that contributed to their growth, but that was more project based. But generally speaking, did not see any unusual trends. Production Mail, we did see some better written business towards the end of the year which yielded the backlog that you see. That was driven by some large implementation -- or future implementations.

**Shannon Cross** - *Cross Research - Analyst*

With the strength in PBMS and the projects you talked about, is this something that you think could be recurring? Is it the strength that came in the quarter? Are you seeing maybe -- are you actually embracing more of a growth perspective on this business? I know for quite a while you were really focused on driving profitability, and obviously with services businesses, sometimes you end up having to invest before you see a big ramp. So I am curious as your thought process around PBMS since it did move into the growth category, which is nice to see.

**Michael Monahan** - *Pitney Bowes Inc - EVP and CFO*

Sure, there were really two parts that contributed to that. I would say that the team has worked aggressively over the last 12 plus months to really refine their offerings and take more of a vertical approach, sector approach, and have had success in getting new written business. As those new projects have come online that has driven an improvement in the revenue run-rate. And was a contributor to it going positive. And then as I mentioned, we did have some project work at the end of the year which is not unusual, but we did get a good level of project work at the end of the year, as well - that supplemented that. But we do see that that business has the potential for ongoing revenue growth.

**Shannon Cross** - *Cross Research - Analyst*

Okay great. Last question on cash flow. Just as we look to the guidance you provided, obviously finance receivables will be less of a contributor next year, or not providing much. So, what are the other puts and takes, if there are any, that we should keep in mind terms of your drivers of cash flow? Given net income is going to be flat to down depending on where you come in from an earnings standpoint?

**Michael Monahan** - *Pitney Bowes Inc - EVP and CFO*

Yes just on a straight up comparative basis, we did have a tax receipts come in, in 2012, that will not likely repeat themselves in 2013. But that is reflected in our guidance number. The other variables really are around working capital and earnings themselves, are the most variable of the lines. As I mentioned, we are focused on being more effective on the working capital side. And obviously, looking at driving earnings is a very important part of our goals going forward.

**Shannon Cross** - *Cross Research - Analyst*

Great, thank you very much.

**Operator**

Eric Carlson, AKO Capital.

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**Eric Carlson** - *AKO Capital - Analyst*

I just had a question on 2014, assuming and a more directly recovering economy, do you think the SMB business can grow in 2014?

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**Michael Monahan** - *Pitney Bowes Inc - EVP and CFO*

At this point, yes, we have looked ahead to 2013 and really are not in the position to make projections around 2014.

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**Eric Carlson** - *AKO Capital - Analyst*

Okay. And just on your International Mailing business, if you could, so we saw a marked improvement in this quarter. And it was a best growth rate we have seen for nine quarters, I think. To what extent was that you gaining market share and to what extent was that the underlying market improved for you?

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**Michael Monahan** - *Pitney Bowes Inc - EVP and CFO*

There really are a couple of key contributors, one, was the performance of our new Connect+ product as we noted particularly in France and Germany. In the Nordics, we do sell other products as well. And we had a very strong quarter in the Nordics business as well. So those were the key drivers and we think that was a solid performance across the geography. Obviously there were other markets in Europe that because of the overall economic situation did not do as well, but collectively, we were satisfied with the results.

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**Eric Carlson** - *AKO Capital - Analyst*

That is great, and do you think the International Mailing business can grow this year?

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**Michael Monahan** - *Pitney Bowes Inc - EVP and CFO*

We think that there is the opportunity for that business to grow. Obviously it is a matter of what happens in the overall marketplace, and then just our day-to-day performance in the market.

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**Eric Carlson** - *AKO Capital - Analyst*

Very helpful, thank you very much.

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**Operator**

Hale Holden, Barclays.

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**Hale Holden** - *Barclays Capital - Analyst*

Thanks for taking the question. I had just two, the first was would it be possible for you to give us a breakdown for the free cash flow guidance of what percentage is generated offshore for 2013?

**Michael Monahan** - *Pitney Bowes Inc - EVP and CFO*

Generally speaking, about 80% of our free cash flow is generated in the US, and about 20% outside the US, obviously that can vary a little bit. But generally that is a good rule of thumb.

**Hale Holden** - *Barclays Capital - Analyst*

Perfect. Marc I was hoping to pin you down a little bit further on capital allocation, your predecessor sort of gave the impression that a dividend cut was really unlikely or not something that was on the table. So, I was just curious if you could tell us for the May meeting, after your 100 days, if it was possible or a potential that you would actually cut the dividend?

**Marc Lautenbach** - *Pitney Bowes Inc - President & CEO*

I am not going to preview where I come out in May. Obviously as Mike said, the dividend is a decision that is the Board's decision. It's made on a quarter-by-quarter basis, and it is made in the context of delivering great shareholder value. And we will conclude the review, and we will talk more about it in May.

**Hale Holden** - *Barclays Capital - Analyst*

Okay, I appreciate it thank you.

**Operator**

Chris Whitmore, Deutsche Bank.

**Chris Whitmore** - *Deutsche Bank - Analyst*

Thanks very much. Mike I wanted to follow-up on your comments around the mail cycle and the meter cycle through 2013. You suggested it would improve due in part to a better renewal cycle or lease cycle runoffs from four years ago. But if I look at 2008 to 2009 equipment sales, equipment sales in 2009 versus 2008 were actually down 20% or so. Help me understand how the full year cycle is playing into a better outlook for 2013? Thanks.

**Michael Monahan** - *Pitney Bowes Inc - EVP and CFO*

Sure, in terms of the lease cycle, our average lease terms are actually probably in the 50 to 51 month timeframe. There are various periods of time that we can offer extensions for our customers on. There is a tail-end effect of that, it is a piece of the overall equation in terms of the timing of when we place equipment, and when that equipment runs off. So, that is one piece of it. The other piece of it that we touched on was due to the fact that we have less customer privilege which is the lease extension program in 2013. Then we had in the first half of 2012, which would have a leveling effect as we get into the second half of the year.

**Chris Whitmore** - *Deutsche Bank - Analyst*

Okay, so okay thanks that is very helpful. And then looking at margins in the equipment business, they look a little bit lower than I would have guessed for the typical current Q4 particularly in light of the restructuring. Have you seen any change in competitive environment or pricing or can you give us a little color on the margin performance there?

**Michael Monahan** - *Pitney Bowes Inc - EVP and CFO*

Yes, the overall equipment margin is probably more about mix than it is about margin in the individual businesses. There is a little bit of effect in their within the Mailing business related to doing less CP and more new equipment. But there is also a mix of non-mailing equipment in international, that is higher. And then there is a mix of equipment in DMT that had more print and less inserter than the normal average. So it is the combination of those three things that yield that margin relationship.

**Chris Whitmore** - *Deutsche Bank - Analyst*

Okay, so you have not seen much of a change in the competitive environment from Neopost for example given -? (multiple speakers)

**Michael Monahan** - *Pitney Bowes Inc - EVP and CFO*

No, I would not put it on an account-by-account basis, we do not see a big change in the competitive environment, it is much more about a mix of the revenue sources.

**Chris Whitmore** - *Deutsche Bank - Analyst*

Okay, great. And finally, Marc, I just wanted to come back to the strategy question, a capital allocation strategy one more time. Let me ask the question in a different way, it sounds to me like you want to [combine] the Software strategy to some extent. Do you think you have the right assets in place to take the Software business to where you want it to be today? Or do you think acquisitions may become a more significant part of the strategy going forward? Thanks a lot.

**Marc Lautenbach** - *Pitney Bowes Inc - President & CEO*

Yes, I will go back to my original answer that we will talk more about that in May. I will tell you I am very impressed with the base of what we have in this Company in terms of technology assets, and businesses and important capabilities. So I think there is a great base to build off of.

**Chris Whitmore** - *Deutsche Bank - Analyst*

Okay, thanks, I thought I would try. (laughter)

**Michael Monahan** - *Pitney Bowes Inc - EVP and CFO*

Good try, Chris.

**Operator**

Barbara Noverini, Morningstar.

**Barbara Noverini** - *Morningstar - Analyst*

Hello. Good morning. Regarding your global shipping solution with eBay, it appears to be quite scalable yet it also appears to be more labor intensive on your end than what you have offered through eBay in the past. However, I expect that you are leveraging existing facilities to provide the services. So, can you comment on the margin profile of this business, and what your expectations for growth will be for it?

**Michael Monahan** - *Pitney Bowes Inc - EVP and CFO*

Sure, there are really two components to that business. There is the technology piece, which is providing the fully landed cost capability. And the second piece of that is the enablement of the physical delivery of the goods on a cross-border basis. We are using a combination of our own capabilities, particularly the technology piece as our own. And also working with third parties, as well as leveraging our own capabilities in the delivery element of it. So it won't be all fixed cost in terms of facilities and labor to enable that delivery piece. We will do a combination of fixed and variable with partners in that. What we are focused on in particular is creating the value in the technology side of it.

**Barbara Noverini** - *Morningstar - Analyst*

Thanks for the additional detail.

**Operator**

(Operator instructions)

Ananda Baruah, Brean Capital.

**Ananda Baruah** - *Brean Capital - Analyst*

Thanks guys for taking the follow-up. Mike, Marc, just trying to go back to the revenue growth. What makes you have the confidence that this year is the year revenue gets back to growth? And can you talk to the drivers there? And then should we assume given that you are talking of that a little bit more investment in the first half of the year, that we actually see negative leverage in the first half of the year? And maybe a little better leverage in the second half of the year? Thanks.

**Michael Monahan** - *Pitney Bowes Inc - EVP and CFO*

Sure, yes, in terms of revenue growth, as I outlined. We are looking at the trends that we saw throughout 2012, I think manifest themselves again in the fourth quarter. As I mentioned, we expect that the contribution would come more from the Enterprise side of the business, and in particular contribution from the Software business and the growth initiatives that we outlined.

To the second part of your question, it is somewhat linked to those growth initiatives, some upfront investment, and then getting some leverage from the growth on the backend. And as I also mentioned, the relationship on the recurring revenue streams in the core Mailing business continuing to improve as we have seen over the last year or so. So, those are the key drivers, and that is why we identified the difference between the front and back halves of the year.

**Marc Lautenbach** - *Pitney Bowes Inc - President & CEO*

I have one additional point and I spent the last several years working for a company that was tremendously successful in terms of driving earnings growth, and revenue growth is clearly an important part of the equation. And there is no getting away from that. That said, and there is a lot that can be done in terms of productivity and mix that drives important shareholder value as well, so as I look at the business in our strategic review, we look at all the different levers that drive earnings. And I think there is plenty of great existence there out in the industry of how to drive great shareholder value using lots of the levers.

**Ananda Baruah** - *Brean Capital - Analyst*

Yes, I can appreciate that. Just on the revenue I was -- is there something that you guys see manifesting itself in a much more indicative way exiting this year coming into -- exiting '12 coming into '13 than it has in the past that gives you increased confidence in positive revenue growth this year? That is what I was wondering.

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**Michael Monahan** - *Pitney Bowes Inc - EVP and CFO*

Yes and I would point you to just the trends that we outlined relative to the fourth quarter as being the same as going into '13.

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**Ananda Baruah** - *Brean Capital - Analyst*

Yes, and then just my last one is, can you give us a sense of what the cash taxes and the cash interest were in 2012? You made some comments, I think Mike, about taxes being lower I think in '12 and '13?

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**Michael Monahan** - *Pitney Bowes Inc - EVP and CFO*

Yes, I would say that it is likely it would be more neutral in '13 where we had a tax refund in '12 that was in the $70 million range.

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**Ananda Baruah** - *Brean Capital - Analyst*

Yes, that was the cash tax, and how about cash interest?

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**Michael Monahan** - *Pitney Bowes Inc - EVP and CFO*

I do not expect it to be materially different.

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**Ananda Baruah** - *Brean Capital - Analyst*

Got it, can you give us a number the cash interest number?

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**Michael Monahan** - *Pitney Bowes Inc - EVP and CFO*

I do not have it off the top of my head.

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**Ananda Baruah** - *Brean Capital - Analyst*

Got it, thanks a lot.

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**Operator**

There are no further questions in the queue at this time, please continue.

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**Michael Monahan** - *Pitney Bowes Inc - EVP and CFO*

In closing, the progress reflected in the fourth quarter results were driven by year-over-year revenue growth in four businesses and continued improvement revenue trends throughout our SMB group. We will drive shareholder returns as Marc said, by continuing to take actions as necessary to reduce costs and make the appropriate investments in the profitable growth of the business. Thank you for joining us.

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**Operator**

Thank you and ladies and gentlemen, this conference will be available for replay after 10 AM this morning until February 28, 2013 at midnight. You may access the AT&T executive playback service at any time by dialing 1-800-475-6701 entering the access code 275683. International participants may dial 1-320-365-3844, using the same access code 275683.

Once again those numbers are 1-800-475-6701, international 1-320-365-3844, the access code is 275683. That does conclude our conference for today, thank you again for your participation, and for using AT&T executive teleconference service. You may now disconnect.

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