DELL TECHNOLOGIES INC.

Moderator: Robert Williams
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4:00 p.m. Central

Robert Williams

Thanks, Erica, and thanks for joining us. With me today are our vice-chairman, Jeff Clarke, our CFO, Tom Sweet and our Treasurer, Tyler Johnson.

During this call, we will reference non-GAAP financial measures, including non-GAAP revenue, gross margin, operating expenses, operating income, net income, EPS, EBITDA, adjusted EBITDA and adjusted free cash flow. A reconciliation of these measures to their most directly comparable GAAP measures can be found in our web deck and press release.

Please also note that all growth percentages refer to year-over-year change unless otherwise specified.

I want to mention that we will not be taking questions related to the Pivotal or Carbon Black transactions that VMware announced on August the 22nd.

Finally, I'd like to remind you that all statements made during this call that relate to future results and events are forward-looking statements based on current expectations. Actual results and events could differ materially from those projected due to a number of risks and uncertainties, which are discussed in our webdeck. We assume no obligation to update our forward-looking statements.

Now, I'll turn it over to Jeff.

Jeff Clarke

Thanks Rob, and thanks to all of you for joining us.

Since we launched Dell Technologies, we have been consistent about our long-term view on global technology investment and what we have to do to realize this unprecedented opportunity.

We have to innovate and integrate across the full Dell Technologies portfolio. Doing this creates the next generation of technology infrastructure that enables digital organizations operating in the data economy.

We have to continue innovating within our business units to win the consolidation and generate cash.

And of course, we have to do this with an eye towards the inevitable fluctuations in near-term demand.

Today, I would like to touch on each of these areas and share some of the progress we have made executing against our strategic priorities.

To begin, let me emphasize the long-term drivers for our business remain intact. We are in the early stages of a technology-led investment cycle that is accelerating digital transformation. That investment cycle is fueled by the exponential increase in data and data-centric workloads that drive better business outcomes, alongside an increasingly diverse and mobile workforce.

But to realize these outcomes, customers are grappling with increasing complexity across their operating environments and infrastructure including: data proliferation, multi-cloud management, security, new software architectures, applications, artificial intelligence and machine learning, all the while defining their approach to cloud and increasingly the edge and IoT.

Take hybrid cloud as an example. Companies deploying hybrid cloud strategies want seamless compatibility, consistent infrastructure and operations across private clouds, public clouds and the edge.

We are optimistic about IT spending, because customers need a partner to help them address these challenges, one who is innovating and delivering a comprehensive end-to-end IT strategy.

In fact, the latest IDC forecast for IT spending through 2023, excluding telco, backs up our optimistic view. IDC projects growth will be more than 2x real GDP or about 4.3 percent per year on average.

So, as I said, we believe the long-term drivers of our business are intact.
This brings me to my second point. Dell Technologies is uniquely positioned to capitalize on this enormous opportunity.

We have been hard at work innovating and integrating across the portfolio to deliver the future of technology infrastructure with solutions that dramatically simplify IT management. Last quarter, we made major progress with the announcement of Dell Technologies Cloud and Unified Workspace.

Interest remains high in our Dell Technologies Cloud platform, the easiest and fastest way to a consistent hybrid cloud experience. It brings together Dell EMC's VxRail hyperconverged infrastructure with VMware's Cloud Foundation software stack, offering customers a single, consistent platform for both traditional and cloud-native workloads, with full automation and integration for hybrid and multi-cloud environments, with consistent SLAs, tools, services and management from VMware and Dell EMC.

The customer pays subscription fees for as long as they use it, the same way they pay for public cloud infrastructure. CapEx becomes OpEx.

Earlier this week at VMworld, we announced several other enhancements to our Dell Technologies cloud offerings including: new Validated Designs for storage arrays and servers, initial availability of the industry's first fully managed on-premise Data Center-as-a-Service offering, and general availability of a new pay-for-what-you-use flexible consumption models. In addition, we announced Dell Technologies Cloud Platforms now support VMware Pivotal Container Service.

And with VMware's recent announcement of its intent to acquire Pivotal, our solutions and speed to market get even stronger. Pivotal further extends VMware's Kubernetes capabilities for building, running, managing modern applications on any cloud.

Another powerful example on how we are innovating across Dell Technologies is Unified Workspace. This solution integrates capabilities across Dell devices and services, VMware and SecureWorks, and now includes Dell ProManage, managed services that integrate Dell's highly skilled experts as part of the customers' IT teams.

Think about the IT investment cycle I mentioned earlier and the needs of the growing, diverse and mobile workforce. Unified Workspace is an intelligent solution that tells you the specific devices and applications your workforce needs on their specific usage. Then it delivers those personalized devices directly to the end user, preconfigured and preloaded with all the applications and security features they need. IT never has to touch the device.

With VMware's acquisition of CarbonBlack, Unified Workspace will only improve with a comprehensive, intrinsic security portfolio for the multi-cloud world and for modern applications and devices.

As you can see, we are delivering on our promise to innovate across Dell Technologies to create the future of technology infrastructure from the cloud to the edge while dramatically simplifying the customer experience.

And this brings me to our next strategic priority, which is all about what we are creating in our business units to drive and win in the consolidation, generate cash flow and fuel innovation. We have the strongest solutions set in our history with businesses that are consistently outperforming their competitors.

In the data center, we are seeing significant traction from our new Unity XT midrange storage solution, and the strong acceptance of XT in the market gives us confidence as we ramp the solution and prepare to bring our next-generation midrange storage offering to the market.

We are also seeing strong receptivity of our PowerProtect X400 and PowerProtect Software. The X400 delivers next-generation data management and protection in a software-defined, scale-out appliance.

It is highly complemented by our PowerProtect software offering that delivers data protection, deduplication, operation agility, self-service and IT governance.

In Q2, VxRail orders grew 77 percent as organizations continued to benefit from its simple integration with VMware Cloud Foundation to enable hybrid cloud environments. It's just another example of how we are collaborating with VMware to bring another first and best solution to the marketplace.

In Client Solutions, we introduced new XPS products with leading design and user experience, including more powerful processing and applications matched with thinner and lighter designs like our new XPS 13 2-in-1.

And, our Dell Latitude 7400 2-in-1 continues to receive incredible praise from the media and customers alike, with PC World deeming it "a nearly perfect combination of power and battery life." It is the first commercial laptop with built-in sensing technology.

Our teams are turning out the industry's best products and solutions, executing on our priority to win the consolidation and generate cash flow.

Which brings me to my final point. As we invest and innovate to capture the enormous opportunity, we must remain disciplined and mindful of the near-term environment in which we operate in.

So, before I turn it over to Tom, let me shift gears to the current demand environment and our view on component costs.

Our core Dell orders were up 4 percent, excluding China, and we are seeing a clear split between Enterprise Infrastructure and PC spending globally.

In Enterprise Infrastructure, the market is softer than we and the industry anticipated. We expect it to remain soft through the balance of the year, particularly in China.

We feel really good about our ISG execution in Q2, given the market context.

In the first half, we acquired approximately 21,000 ISG customers, up 11 percent from the prior year. And more of our ISG customers are purchasing multiple lines of businesses.

Our storage business remains healthy in Q2 with orders up 1 percent and first half orders up 4 percent. Our sales team remains optimistic about our portfolio and positioning as we head into the second half of the year.

Turning to servers, the industry saw unprecedented growth last year and many customers are still digesting their capex investments.

We are balancing revenue and profitability as we navigate through the current server dynamics. Our Q2 server revenue declined, but we realized higher margin dollars as we were consciously more selective on large, low margin deals in all geographies.

Outside of China, our server orders were up 1 percent and we expect to gain share this quarter in North America and EMEA when IDC publishes results next week.

Our server ASPs remain strong, up high single digits, as customers are increasingly buying higher-end systems to support their high value workloads.

In Q2, CSG delivered record performance driven by strong execution, the Win10 refresh and a declining component cost environment. Longer term, we expect to continue to drive share gains through innovation and execution as the industry continues to consolidate among the top vendors. We will continue to focus on commercial, high-end consumer and gaming as well as increasing our attach of services, financing, and software and peripherals.

In the supply chain, we expect the component cost environment to remain deflationary in aggregate through at least the end of the year. Though it is important to note we expect the decline to significantly slow down in the second half measured against the first half.

This quarter, we clearly benefited from the strength of our broad IT solutions portfolio, which helped us deliver strong results amid short-term market volatility. While we saw soft spending in pockets of the marketplace, our overall performance in our Q2 results reflect our competitive advantage.

In the second half, you should expect us to continue to balance growth and profitability, but with a slightly higher bias toward maintaining growth at the portfolio level.

We have built a business to be successful in any environment. We are differentiated by our broad portfolio in the industry, with leading solutions, our direct model, including services and financing, and our world-class supply chain with its size and scale. Whether the market expands or declines, we expect to outperform the industry.

So to recap, we believe strongly that our long term growth drivers are intact.

We are innovating across the portfolio to create the infrastructure for the digital future.

We are investing and innovating to win the consolidation.

And we are mindful of the near-term environment, and we are confident we can outperform.

Ultimately, it's all about the customer and no one is better positioned than Dell Technologies to be our customers' best, most trusted partner on their digital transformation journey.

With that I'll turn it over to Tom to talk about our Q2 results.

Tom Sweet

Thanks Jeff.

Our model is focused on long-term profitable growth, with the ability to adjust as needed based on market conditions. We are focused on growing faster than competitors and the industry; growing operating income and EPS faster than revenue; and generating strong cash flow over time.

We executed well against these priorities again in Q2, as we balanced revenue and profitability with market conditions. While we saw a softer Enterprise IT market this quarter, we continued to benefit from having the industry's broadest portfolio of solutions.

Revenue was $23.5 billion, up 1 percent, with core orders revenue up 4 percent, excluding China. And our deferred revenue balance increased to $25.3 billion, up 17 percent. FX remained a headwind this quarter, impacting year over year growth rates by approximately 150 basis points.

Gross margin was up 13 percent to $8 billion and was 34 percent of revenue, up 340 basis points, driven by lower component costs and pricing discipline.

Operating expenses were $5.2 billion, up 6 percent, due in part to investments we have made in sales coverage to expand our buyer base.

In the quarter, new Enterprise and Commercial customer acquisitions were up over 10 percent from the prior year. And over the last six quarters, approximately 80 percent of our top 30,000 customers have purchased four or more lines of business from us.

We are pleased with our operating income, which was up 30 percent to $2.7 billion, or 11.7 percent of revenue.

Our EPS was $2.15, benefiting from strong operating profitability and a lower tax rate in the quarter, due to revenue mix.

Adjusted EBITDA was $3.2 billion, or 13.5 percent of revenue, and $11.2 billion on a trailing twelve month basis.

We had a record cash flow quarter, generating $3.4 billion of adjusted free cash flow, driven by strong profitability and working capital discipline. Some of our working capital benefit came from reduced inventory as we are working through the supply chain dynamics that impacted cash flow last year.

We also saw deferred revenue increase 17 percent to $25.3 billion, with recurring revenue now making up 20 to 25 percent of our revenue each quarter. Our services and software businesses continue to grow as we expand the portfolios, adding revenue and cash flow stability and predictability.

We repaid approximately $2 billion of gross debt in the quarter, and $2.4 billion year to date, and we are well-positioned to repay approximately $5 billion of gross debt in total in FY20. We have now paid down $17 billion of gross debt since the EMC merger.

Shifting to our business unit results, ISG revenue was $8.6 billion, down 7 percent.

Storage revenue was flat at $4.2 billion. As Jeff mentioned, orders were up 1 percent, driven by strength in Isilon and our industry-leading HCI solutions. We are seeing strong receptivity for our new Unity XT solution in the midrange. And we continue to press on growth levers within the broadest and most diverse portfolio in the industry.

Servers and networking revenue was $4.4 billion, down 12 percent. The global server market remains softer than anticipated coming into the year and has affected our server growth. The impact to our business was most pronounced in China again this quarter where we were more selective on larger deals and focused on building sustainable long-term customer relationships.

ISG operating income was $1.1 billion or 12.2 percent of revenue. Operating income percentage was up 120 basis points, largely due to our business and geography mix, as well as pricing discipline.

Our VMware business unit had another good quarter, with revenue of $2.5 billion, up 12 percent. Operating income was $762 million, or 30.9 percent of revenue.

Based on VMware's standalone results reported last week, VMware's growth in total revenue, plus the sequential change in total unearned revenue, was 17 percent. Core Software-Defined Data Center license bookings grew in the high single digits. NSX license bookings were up over 30 percent and vSAN license bookings grew over 45 percent.

CSG delivered record revenue and units with strong profitability in Q2. Revenue was $11.7 billion, up 6 percent. Within CSG, Commercial revenue was $9.1 billion, up 12 percent, driven by double-digit growth in Commercial notebooks, desktops and workstations. Consumer revenue was $2.7 billion, down 12 percent, as we continue to prioritize Commercial mix and the higher end of Consumer PCs.

We saw strong profitability in CSG this quarter due to component cost declines, commercial/consumer mix and pricing discipline. CSG Operating Income was $982 million or 8.4 percent of revenue. Going forward, you'll continue to see us balance revenue and profitability against market dynamics.

Dell Financial Services originations were $2.0 billion, up 3 percent.

We did record a non-cash charge of $619 million, or $524 million net of tax benefits, after a strategic review of our Virtustream business. We remain committed to serving our customers as we reposition the business.

Turning to our balance sheet and capital structure, we grew cash and investments in the quarter to approximately $10 billion, even after the Q2 debt paydown of $2 billion.

Our core debt balance ended the quarter at $36.4 billion, down over $12 billion since the EMC acquisition. And net core debt ended Q2 at $30.5 billion. Please see slide 14 in our web deck for more detail.

We are focused on maximizing free cash flow and our capital allocation strategy remains unchanged. We are committed to reducing leverage and achieving investment-grade ratings. Given our recent debt paydown and refinancing activity, we have only $2.3 billion due in the next 18 months, excluding VMware. And we will continue to look for additional opportunities to smooth our debt maturity profile and optimize our capital structure.

We will maintain pricing discipline as we move into the back half of the year, while adjusting as appropriate, given market and competitive dynamics.

We are still monitoring the macroeconomic and IT spending environments, as well as ongoing trade discussions between the US and China.

Moving to guidance. Based on Q2 results and our current expectations for the balance of the year and excluding the impact of VMware's Pivotal and CarbonBlack acquisitions, we now expect fiscal year 20 GAAP revenue of $92.7 to $94.2 billion, operating income of $2.9 to $3.3 billion, and EPS of $5.45 to $5.90. We are narrowing our non-GAAP revenue range for the current fiscal year to $93 to $94.5 billion. Due to our strong profitability in the first half of the year, we are increasing our non-GAAP operating income guidance range to $9.8 to $10.2 billion, and increasing our non-GAAP EPS guidance range to $6.95 to $7.40. We expect our non-GAAP tax rate to be 16 percent plus or minus 100 basis points.

In closing, we are well-positioned, we are innovating to drive growth and future value, and we are driving the core for share gain and cash flow.

We have one of the industry's strongest and most comprehensive portfolios, its largest direct sales force, and a world-class supply chain with size and scale. And we are focused on enabling our customers' digital future.

With that, I'll turn it back to Rob to begin Q&A.

Robert Williams

Thanks Tom.

Let's get to Q&A.

We ask that each participant ask one question to allow us to get to as many of you as possible. Erica, could you please introduce the first participant?

[Q&A begins]

Operator: We'll take our first question from Katie Heberdy (ph.) with JP Morgan.

Katie Huberty: Thank you, good afternoon. You mentioned a bias toward growth in the second half of the year. Does that imply that you expect a pass-through, more of the lower memory prices into the next couple quarters? And if so, which segments of your business would you expect to see the most price elasticity?

Tom Sweet: Hi, Katie, it's Tom. So, look, I mean, what we were trying to signal there is that as we think about the business and the business velocity, which we like the ramp in business velocity during the quarter, we are starting to -- you know, as we think about cost trends and the deflationary cycle that we're seeing, which is slowing, we do expect that we'll pass -- particularly in some of the server space, probably have to pass more of those costs to clients through. And, in fact, we are seeing, you know, a little bit more aggressiveness in some of those large enterprise and large deals that we mentioned in the first quarter.

So, you know, the bias towards growth was really directed at trying to make sure -- we're a company that drives on scale. We're going to be balanced in the back half of the year, but I do think that from the dynamics that we're seeing right now, that I would expect that we're going to see a bit more pricing aggressiveness in the back half, and I would probably point towards servers.

I think we feel good about where the client business is and the storage business is from a pricing perspective, but I think servers may have some pressure points.

Katie Huberty: Thank you, that's very helpful.

Jeff Clarke: And I would add to that. We've certainly spent much of the first half of the year in servers keeping our product line in our traditional price position. And we're going to continue to price the product lines going forward to do that. And as Tom said, that's going to be our bias towards growth.

And I think the other thing that we're signaling, and we've mentioned a couple of times is the fuel of that, the commodity deflation substantially slows in the second half, so we have to watch that, but we're going to have a slight bias towards growth, keeping our eye on profitability, and both at the businesses.

Robert Williams: Thanks, Kate.

Operator: Our next question is from Rod Hall with Goldman Sachs.

Rod Hall: Yeah, hi, guys, thank you for the question. I wanted to ask about the trajectory of demand and where you guys have seen weakness, where you've seen strength. When we look at other companies that reported enterprise, we've seen a pattern of weakness in large enterprises that seems to have developed in, let's say, the June time frame. And so I'm wondering whether that has been the same for you and whether you've seen that continue to weaken, or you think it's stabilized. And then I'd also love to get a comment on small and medium businesses, those seem to have been more stable, and I'm wondering if you can just confirm that that's also what you're seeing. Thanks.

Jeff Clarke — Sure, Rod, Jeff here. When we look at the server business in particular, the softness that we have seen, and we actually talked about it last quarter as well, is in large bids and in China. So those large enterprise bids that you mentioned, we continue to see softness there as well as in China. In fact, if you were to look at our server business excluding China, we were actually at growth, our business was up 1% in orders.

We continue to see that pressure in the second half of the year. Tom alluded to just moments ago about the price aggressiveness that we think is turning up in the second half in those large orders, those large enterprise accounts. So I think that's consistent with what you've seen.

And then on MB and SB, we continue to see that business perform. We don't break out the segment performance of the businesses, but it's been an area of growth for us, and we'll continue I think to see that going forward.

Rod Hall — Great. Thanks, Jeff.

Jeff Clarke — Yeah.

Operator — Our next question is from Toni Sacconaghi with Alliance Bernstein.

Toni Sacconaghi — Yes, thank you. I'm wondering, given your significant overage in operating profit year to date why you wouldn't look to pay down more debt this year. I think your target was 4.8, you mentioned close to 5, which sounds pretty similar. But perhaps you can give us an updated view on what you think operating income will be for the year and why you wouldn't want to more aggressively pay down debt.

Tom Sweet — Hey, Toni, it's Tom. Let me start, and then I'll let Tyler talk a little bit about our debt plans. Look, I mean, the guidance we gave, clearly upped the range around our operating income given the overperformance in the first half. You know, we are -- we did end the quarter at $10 billion of cash, of which $6 billion of that you should think about as core.

So, look, I mean, I think we're going to have some possibility if all things flow like we think it does to take a look at that as we go through the year. Right now, as we look at the maturity stacks that we're planning on addressing, I think we'd feel good about the 5. We'll have to see where the rest of the year unfolds and whether we would commit to doing anything more than that. Tyler, I don't know if you would add anything.

Tyler Johnson — No, I think you said it. I mean, you know, the debt paydown remains a priority, so we'll continue to focus on that. We'll see how cash continues to come in for the remainder of the year but feel very confident about the $5 billion we talked about. So, making really good progress with that.

If you look at our leverage ratios, we improved about half a (turn?) going from the end of last year to where we are now, so making great progress.

Toni Sacconaghi — And if I could just sneak in another one, I missed a couple minutes because I got disconnected on the call, so I apologize if you addressed this during that period. But you seem to suggest that you see more incremental price aggression in servers, but you're pretty confident on the PC side. Are you suggesting that sort of the more normalized PC operating margin, which is you know more than 300 basis points currently above your prior indicated range, that we should be thinking, A, about sustainability in the mid- to high single digits, or high single digits for PC operating margins at least for a few more quarters? Or how much do you think the falling component prices has boosted PC op margins above a normalized rate?

Tom Sweet — Hey, Toni, it's Tom. Let me start and then Jeff can chime in here as well. As we think about our guidances we gave, which was 9.9-10.2, which was a raise of roughly about $700 million (inaudible) this point, as we think about the back half of the year, it's clear as we look at PC that that margin has benefited from a couple of things, one being the significant cost decline, of which we have probably (inaudible) still about 60% of that cost, and we've obviously let some of that cost fall through the bottom.

The other piece of the dynamic there has been the commercial client mix, and we're up about 4% year on year from 69% to 73% of mix. And so that's been beneficial as we navigated through the first half.

I think as we step through the back half, I think we're going to see PC margins gradually normalize back towards the historical norms. You know, we'll have to see how that unfolds, but the rate of cost decline is significantly less than it is in the second half than it was in the first half. You know, and as you think about pricing normalizing and the prices in the market beginning to capturing a lot of that cost decline already.

So, we are thinking that PC margins gradually come back to more historical norms, not in any sort of dramatic, cliff-like fashion, but I just think we're going to see those things gradually migrating back. Jeff, I don't know what you would add.

Jeff Clarke — A couple things. Part of our improvement or our performance in the first half, you talked about two of them being the commercial mix and pricing drew about 60% of the cost decline. Our direct commercial PC business grew double digits, which drives higher attach rates of services, peripherals, and financing that's helped. And we've seen an SRU improvement in there as well, and that's led to the performance that you just spoke about, Toni.

Conversely, when I look at the second half, the second half tilts towards consumer. And consumer has a lower margin structure than our commercial business. We certainly have the uncertainty with trade and the associated costs that go along with trade as we head into the second half. And then I would point to some of the publicly available data, which I know you know very, very well. But to make our point, DRAM -- if I look at DRAM exchange, if I look at where we started the first of the year to where we are today, DRAM has fallen 60% -- nearly 60%.

If I look at what they say the projection is for the remainder of the year, we see a 3% cost decline. So, the rate of deflation is changing, and we think the pricing environment will reflect that towards the end of the year. Does that help?

Toni Sacconaghi — Thanks, guys. Yes it does. Thank you.

Operator — Our next question is from Paul Coster with JP Morgan.

Paul Coster — Yeah, thanks for taking my question. I'll sneak in two quick ones, if I may. First off, to what extent do you think Windows 10 is kind of fueling the CSP growth this year? And does that set you up for tough comps next year? And on the China front, the business that you're kind of foregoing at the moment, is that business that you think you'll come back to at some future point or are you kind of moving on from that very competitive segment of the market? Thank you.

Tom Sweet — Hey, Jeff, why don't you take the Win10 and I'll take China?

Jeff Clarke — Sure. Yeah, Paul, I mean, the industry data varies, but we're roughly 60%-ish-plus through the Windows 10 migration. That has clearly been a source of growth for the commercial PC business for the past year and a half or so.

We see that continuing to be a source of growth for the remaining part of the year and probably into the very early part of next calendar year.

Tough comparison, of course, if you look at what the commercial PC business has performed at for the past six quarters and what's in front of us, it will be tougher compares next year. You see that in the industry forecast for PC growth next year, which is going to be down. The latest forecast, I believe, has PCs down 4% next year. This year, it's roughly flat, but heavily biased towards commercial, consumer being down. And that will be a headwind as we go into the business next year.

I would also tell you the things that we've done in the business to prepare us for that I think are pretty encouraging. We're going to focus on the consolidation that's underway, the PC industry continues to consolidate towards the top three manufacturers. We have made investments in coverage and capacity across all sorts of customers from the smallest businesses to the largest businesses in the world. We think that expansion of coverage and capacity helps us in the long term. And then we have new technologies that we think help us with our Unified Workspace, driving a different shade of solution into the marketplace that will be a source of growth for the business. And we are focused on our direct commercial business, and then the high-end consumer and gaming business are where you'll see our focus as we head into next year.

Tom Sweet — Paul, as it relates to China, you know, the business that we've essentially chosen to not participate in this year has generally been in the hyper-scale server space, where the pricing dynamics have not made a lot of sense to us. And the other thing that we look at when we look at and evaluate large bids or large opportunities is to what extent -- to what extent is that business strategic to us and sticky? Meaning, is it a long-term customer acquisition play where they're going to buy multiple LOBs and have the opportunity to sell multiple different types of solutions and service capabilities?

What we have generally seen with that -- the hyperscale business in China is that it tends to be very transactional where you're bidding -- that business is rebid every quarter or every past year. And so given that pattern in what we've seen, we've chosen not to participate in it. And if that's the pattern that continues, you'll see us continue to not participate in it.

Instead, we're very focused on growing the customer base in China and about building lasting, sustainable relationships. So we have shifted the focus of the China business to -- we'd much rather they go out and build the server buyer base into the mid and small enterprise and larger enterprise space absent the hyperscale, and not participate in that hyperscale space, just given the purchasing behavior and the buying behaviors that we're seeing.

So, I don't think that with what we know right now that that piece of that market -- well, it will still probably be there, it's not a lot of interest to us at this point in time.

Jeff Clarke — But it's the same characteristics we see globally are occurring in China. It's the second-largest market in the world, we're entering a data economy, there's a big opportunity. The role of hybrid cloud is important, data analytics, so the long-term attributes of the marketplace remain strong and we're very optimistic about that over the long term.

Tom Sweet — Which is why we want the business building the customer base, right?

Jeff Clarke — Correct.

Tom Sweet — We want them out, foundationally improving the scale.

Paul Coster — Thank you.

Operator — Our next question is from Aaron Rakers with Wells Fargo.

Aaron Rakers — Yeah, thanks for taking the questions. I wanted to ask about the storage business. As you look at storage demand being healthy, the revenue was only about flag this past quarter. And we (inaudible) growth or orders growth kind of playing into effect here, up 4% for the first half. But how do I think about the progression or flow as you kind of think about the product cycle, the dynamics, what's your expectation for the back half of the year in terms of the storage growth specifically?

Jeff Clarke — When I look at the storage performance through the quarter, I certainly point to areas that I think are positive. We see our HCI business continuing to grow. I think we made reference earlier than our HCI business specifically the VxRail component of that grew 77%. Our converged infrastructure business grew this past quarter. The broad category of unstructured data grew, and we saw actually good performance in our Unity and the new Unity XT midrange product had year-over-year growth as well.

In addition to the PowerMax 2000 that we introduced early last fall for the high price bands and the midrange all grew.

I think we've positioned the product line in a great way. You'll see some more announcements through the remainder of the year that will continue to refresh it and keep it competitive, and we expect to grow the marketplace. The marketplace is expected to grow -- the last forecast, I think just under 3%, I would expect us to outperform the market. The investments that we've made in capacity and coverage, the tenure of that salesforce continues to grow by the day -- literally -- pretty optimistic about our prospects to outperform the marketplace in the second half of the year.

Tom Sweet — And one thing I would add to that, and Jeff, obviously, highlighted a lot of how we're thinking about it. One of the things we've been very focused on with the investment we've made in the (inaudible) capacity has been around customer base expansion, which is why we highlighted the fact that in ISG, you know, year over year, 21,000 new buyers coming back into the ISG business.

Now, whether they're buying one LOB or two LOBs, but the point of it is that we're expanding the customer base, which gives us a broader field or broader base to sell into. We're encouraged by that. Obviously, we've got to go out and execute and make sure that the sales motion is right on the coverage model, but one of the investment paybacks we've been looking for from this go-to-market investment that we've made over the last two years has been around are we expanding the overall customer base itself? Encouraged by the trends we're seeing, but clearly (inaudible, distorted)

Operator — (Inaudible, distorted) -- we're certainly in the early stages (inaudible) there's more data being created, there will be more data created on the edge. We have a leadership position across HCI, CI, and external storage. And we've improved (inaudible, distorted) coverage that we talked about (inaudible, distorted) in the market.

Aaron Rakers — Thank you.

Operator — Our next question is from Shannon Cross with Cross Research.

Shannon Cross — Thank you very much. Jeff, can you talk a bit about what you're seeing from customers with initial response to Dell Technologies Cloud and maybe more in general, just commentary from clients about cloud adoption, both hybrid and public? Thank you.

Jeff Clarke — I'd be happy to. We had a good week this week. At VMWorld, we talked about our Dell Technologies Cloud platform. We actually made several announcements to extend that platform from what we announced at Dell Technologies World the last week of April, and the interest this week has been very high.

Specifically, we extended the platform of validated designs to support our PowerMax storage arrays and our Unity and Unity XT storage arrays, and our PowerEdge MX compute.

We also -- which is the thing I'm most I'm most excited about, and that patent team did a great job on stage earlier in the week, is we announced the initial availability of the first on-prem data center as a service, a managed services or a data center on prem. The initial availability of that product, which is pretty exciting for us.

And then on top of that, acknowledging or building upon what we announced back in that last week of April, we talked about new consumption models, and we've added our Dell Technology Cloud platform and our on-demand payment terms that we can pay in any form of consumption. So, very similar to how a pubic cloud operates today, we can actually bill the customer by usage, and that's been received quite well. So we're pretty excited about that capability. You think about we added VMware, Pivotal Container Service support on top of that, and we have a very comprehensive, multi-cloud, hybrid cloud in the marketplace. In fact, the only one that allows you to move data workloads across the edge to on-prem private data centers to the public clouds.

That's what our customers are asking for. The ability to do that in an automated way, to be able to manage it in a consistent way, and our Dell VMware Cloud allows us to do that. So, I'm pretty bullish on the opportunities going forward. Does that make sense?

Shannon Cross	Yes, thank you.
Operator	Our next question comes from Matt Cabral with Credit Suisse.
Matt Cabral	Yeah, thank you. On ISG margins, I'm wondering if you could bridge the strike you saw in the quarter between mix, the commodity tail winds, and maybe other factors. And in particular, just if you can touch a little bit on what margins for servers versus storage for you on a year-over-year basis.
Tom Sweet	Hey, Matt, it's Tom. We don't typically parse -- you know, we give you a revenue and a (inaudible) so let me sort of try and give you some -- because I'm feeling nice today, I'm going to give you some color around it, right? So, look, if we looked at our margin -- gross margin, our operating margin performance, let me start there. You know, what I would tell you is that it was up 190 basis points, I'm talking about Q on Q now. You know? So from 10.3 to 12.2, I think that from a -- if you were to think your way through that, most of that goodness was principally OPEX goodness. And the actual gross margins were actually flat to slightly down. And if you parse that margin, what you would see is storage margins were stable, and we saw some server -- we had server margins declining slightly. If you think about what's driving the server margin decline, it's really the thing that we previously talked about, which we saw some pricing aggressiveness and large enterprise deals, and we saw some mixed dynamics within China, which drove some margin pressure downward. So, that's sort of the environment we saw. That's also why we're essentially sort of flashing the headlights on the fact that we do think that we'll see a bit more server pricing aggressiveness in -- as we go through the back half. So that's sort of our current thinking. I don't know if, Jeff, if you would add anything, but I think that's how we've thought about it right now.
Jeff Clarke	Spot on.
Tom Sweet	Yeah.
Matt Cabral	That's very helpful, thank you.
Operator	Our next question is from Amit Daryanani with Evercore ISI.
Amit Daryanani	Thanks a lot, guys. I guess, you know, maybe I just going to have a broader question, but you know, when I think about getting into this earnings call, the expectation was Dell, and you guys would essentially miss revenues, miss EPS given what all your peers have talked about in terms of the negative commentary. Your numbers are actually much better than that fear was. So I'm curious, what do you think is driving the better performance at Dell versus what your peers have been talking about? And, importantly, do you think this performance is sustainable as you go forward?
Tom Sweet	Hey, Amit, it's Tom. Look, I won't comment on our peers. I mean, what I would tell you is that if you think about the broad set of capabilities or solutions and the comprehensive portfolio we have, we think we have more growth levers and more levers that we can address and build upon with our customers, right? And

so we have the most comprehensive portfolio in the IT infrastructure industry from our perspective.

You think about the work that we've done on go-to-market over the last two years with the building of the customer base as we've highlighted this quarter, whether it's around the 21,000 new buyers in ISG year over year, it's around the 11% -- or the 10% growth in customers, new acquisition customers.

And so we've been very focused on building our customer base as well. Now, look, you know, we've obviously -- if you think about the financial performance, we've clearly been aided by -- we've had some deflationary cost environment in the first half of the year. We are obviously signaling, through my guidance, and we have said that that cost decline -- or that cost deflation substantially slows in the second half of the year.

But, you know, our job and our model that we built is to grow at a premium to the market, take share, take relative share, and generate cash flow. And so that's the model we've built. We think that's the model that sustains in all the different types of economic environments.

And, you know, look, we're doing our best to execute the model. And, you know, I think we've had a pretty good execution quarter from my perspective. But, again, I get back to the broadness of the portfolio. If you look at the results, obviously, we're aided by a strong CSG business this quarter. You know? If we were solely an infrastructure data center business, it would have been a bit -- it would have been a little bit of a different story. But our broad portfolio allows us to play the growth levers that are available in the marketplace. And I think the team did a pretty good job on that.

Amit Daryanani: Thank you.

Operator: Our next question is from Wamsi Mohan with Bank of America.

Wamsi Mohan: Yes, thank you. Can you comment on the ability to absorb the higher tariffs coming here shortly, and particularly around notebook and displays? And your message is very clear around server pricing, but how should we think about pricing as a lever for share gains in stage and if you intend to use pricing as a lever there, can you be a little more specific around ATI and (inaudible)? Thank you.

Jeff Clarke: Sure, why don't I take the tariff question?

Tom Sweet: Yes.

Jeff Clarke: Wamsi, this is Jeff. Clearly, we have spent a lot of time planning and working through the very dynamic situation that we're living in today with tariffs. Our global supply chain with 25 manufacturing sites around the globe allows us to have the agility and flexibility we need to honestly move fast and to minimize the impact.

We're focused on continuity of supply, and continuity of supply and delivery to our customers and managing that. But, quite honestly, we're working through the challenges of list 4, which is what you're specifically talking about.

We've mentioned list 1-3 in the previous calls, we successfully mitigated that cost impact to the vast majority of our products. There have been cases where we have not and we've raised price. And we will continue to work to mitigate the impact to our customers with list 4, starting with all-in-ones on September the 1st, tablets December the 15th with flat panel monitors and notebooks.

In some cases, our costs are going to go up, and we will have to move price. It's one of the comments I made earlier. When you think about the second half and what's different in our client business, we have the uncertainty of tariffs and the uncertainty of the associated costs that go along with it.

We cannot absorb all of that cost, and we will pass that along to our customers in the form of price in various ways. How we do that, we're still working our way through. We spend a lot of time making sure that we have manufacturing capabilities in place, that the manufacturing sites are prepared, the manufacturing processes are prepared for the changes, sourcing operations for our notebooks, all-in-ones, and flat-panel monitors.

So that's where we are. I think that's the best answer I can give today. More to come. It is pretty dynamic. It has changed a couple of times. And will probably continue to change, but that's our guess.

Tom Sweet — Hey, Wamsi, your other comment around pricing. Obviously, we did signal or are signaling that we are seeing a bit more pricing aggressiveness in the server space. As it relates to our intention or strategy around pricing on storage and some of our other product lines, I mean, we're not -- we don't -- we're not driving any sort of significant change in our pricing strategy and our other LOBs. So we'll obviously react to ensure that we're price competitive relative to the environment and the market. But you know, at this point, there's no intention to use price as a lever in some of these other areas.

Wamsi Mohan — Okay, thanks a lot.

Operator — Our next question is from Simon Leopold with Raymond James.

Simon Leopold — Great. Thanks for taking the question. Wondering if maybe you could talk a little bit more about trending from a geography and market vertical beyond what you've -- you've mentioned China a number of times, but I guess I'd like to hear a little bit more detail maybe versus Europe. And then you also talked about sort of the large enterprise weakness. Could you maybe touch on some other verticals such a government markets and maybe some of the dynamics? Because it sounds to me that maybe Europe's a little bit better, government's a little bit better. I'd like some color beyond what we've talked about already. Thank you.

Tom Sweet — It's Tom. Let me start, and maybe Jeff can jump in. I'm going to try and keep this at a reasonably high level. But, you know, as we think about just geo-based right now, we would tell you that in general we've seen North American demand has generally been quite -- it's just been healthy and we're pleased with that. We're pleased with our Latin America demand.

I think we have seen some softening in Europe. And whether that's Brexit related or just sort of general economic dynamics, hard to parse that. But I think we've seen some softening there. I mean, you got Asia, clearly, we've talked about China being sort of a softer market for us this year.

Pleased with what we're seeing in Japan. We're starting to see better velocity coming out of Australia/New Zealand. So I think in general, I mean, that would be how I would frame it for you. On a vertical basis, a customer segment perspective, you know, Q2, which is the quarter we're reporting on is generally a strong education, state and local government market in the U.S. And I would tell you that that spending seems to be holding up fine.

We're optimistic about the federal business going into Q3 in the U.S. You know, so across the -- I think across the globe, government procurements continue to be on track. So, that's sort of what we're seeing right now. Jeff, I don't know if you would add anything to that.

Jeff Clarke — No, not at all. Very good.

Simon Leopold — Great, thank you.

Operator — Our next question is from (inaudible) with Deutsche Bank.

Deutsche Bank — Thanks, guys. Let me ask a question. I'm trying to reconcile the storage that you guys mentioned storage is going to grow more than 3% year on year, but yet enterprise IT spend is going to continue to be weak throughout the rest of the year. It seems like on your topline guidance that -- at least on a year-on-year basis, between 3Q and 4Q, I'm actually seeing that year-on-year's revenue should accelerate. Could you verify if that's true and kind of help me reconcile some of these statements and how that impacts your full-your guidance? Thanks.

Tom Sweet — It's Tim, Gerald. So, I'm not sure how you're modeling, and so maybe the team can help you with that offline. I would tell you that as we think about storage, I mean, the market is sort of, you know, low single digits and so that's the forecast from IDC. Jeff talked about the fact that we saw storage demand at 1% in Q2.

The broader ISG comment, which I think you're referring to is that we continue to see softness in servers. And so you've got to think about that mix dynamic. You know, IDC is forecasting negative growth in servers for mainstream servers for the rest of the year, and so there's some interplay between those two LOBs, as you model ISG.

So, you know, maybe the team can take that offline and take a look at how you're thinking about it. But as we look at the business, we expect to see server revenue -- you know, the server market to continue to be challenging for the remainder of the year with what we know today. We are more optimistic about the storage market.

Now, you know, it's not a double-digit growth market, but we are optimistic that given the improvements in the coverage model, all the work that Jeff has done with his team on product and product line positioning that we -- you know, we expect to see better results in storage. And so that's how we've thought about the year at this point.

Deutsche Bank — Appreciate it, thanks.

Operator — Our next question is from Andrew Binan (ph.) with Wolfe Research.

Andrew Binan — Hi thank you. So to start the year, you discussed the expectation that investments in sales capacity and coverage would add OPEX, and that you'd begin to see the benefit of these investments ramp as you moved into the second half of the year. But it seems like today's commentary was that the second half will balance growth and profitability, but maybe leaning towards growth. Can you just kind of level-set where we are with regards to sales productivity?

Tom Sweet: Well, look, hey, it's Tom. We don't sort of talk about those numbers publicly, but I would tell you that we are seeing the capacity that we've added sort of ramping on the -- sort of the normal productivity curves that we would expect. Right?

Now, you have to balance that against -- it is a bit tougher market than it was a year ago. And so there are macrodynamics that you're managing as you think about productivity, although they don't tend to give the sales orgs a lot of breaks on just asking them to drive to the productivity levels that they've committed to.

But to be fair, it's a bit choppier market out there, particularly on servers. So, but the productivity curves they're on. You know, and to your comment, we're biasing ourselves towards growth. What we're trying to signal is that we do want to make sure that the growth engine stays intact and that we have a bias towards customer-based expansion, revenue-based expansion, even in a tougher market. The benefits of scale for us are quite significant and we want to make sure that that scale advantage continues.

So, you know, as we think about the back half of the year, that was what we were trying to signal, and we're still investing in sales capacity, I might add, particularly as we think about some of the market opportunities as we set up for next year. So, you know, that's how we're thinking about it.

Andrew Binan: Thank you.

Robert Williams: Erica, one more question.

Operator: Yes, we'll take our final question from John Roy with UBS.

John Roy: Hey, maybe as a final, you've been talking a lot about enterprise weakness through now and through the back half of the year. Maybe if you could give us some color on why you think that the enterprises are doing that. Is it macro? Is it trade? Cloud? Is it really just digestion? Is it something else? Maybe if you could just kind of order what you're seeing out there and why the enterprises seem to be softer.

Operator: I think we've talked about it before, and I think even made reference in our talking points earlier. Coming off the best server year in time and the best storage year in times in 2018. If memory serves me, we roughly had the storage market growing 12% last year and the server market 30-ish percent, if memory serves me right.

There's been a digestion of that that's taken longer than I think all of us in the industry expected. And by and large, that's what we're dealing with. Combined with the softness that we talked about in what has been one of the fastest-growing markets in the world, China.

Tom Sweet: You know, I would also add that if you just -- and I'm not -- we don't have enough visibility to parse it I think in the way you're asking it, but most of us that are running large enterprises don't like uncertainty. And when you think about the macro environment, whether it's tariffs or Brexit or some of the other macrodynamics around interest rates and where GDP is trending, it does create an era of uncertainty. And so that also probably has some level of dampening effect on the market.

Having said that, though, right? I mean, we think that we're optimistic about the back half of the year. We think we're set up to continue to execute. And you know, companies are still spending. And companies are still in their digital transformation and they need to -- and they think about some of these IT investments as essential to their business model evolution. So, you know, we'll continue to press forward and drive the business.

John Roy: Great, thank you.

Robert Williams: Thank you, Tom. Thanks, John. As a reminder we'll be at the Citi Global Technology Conference in New York on September the 4th and 5th. We'll also be hosting our business update for the investment community in New York on September the 26th, so we look forward to continue the dialogue. Thanks for joining us today.

Operator: This concludes today's conference call, we appreciate your participation. You may now disconnect.

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