

TRANSCRIPT

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PRESENTATION

Roderick B. Hall - Goldman Sachs Group, Inc., Research Division - MD

All right. I think we're going to get going here. So it is my great pleasure to have Dell Technologies with us, Chuck Whitten, their co-CEO. Chuck, welcome. Thanks for coming.

Anthony Charles Whitten - Dell Technologies Inc. - Co-COO

Thanks for having me, Rod. Thrilled to be here.

Roderick B. Hall - Goldman Sachs Group, Inc., Research Division - MD

I think this is the first time I've interviewed you at a conference. So it's great to have you.

Anthony Charles Whitten - Dell Technologies Inc. - Co-COO

I see. Yes. I think it's the first time we've seen each other in 3 dimension. So it's great.

Roderick B. Hall - Goldman Sachs Group, Inc., Research Division - MD

Correct. Correct. Usually, I have a Hawaiian shirt on or something [wicked].

Anthony Charles Whitten - Dell Technologies Inc. - Co-COO

Yes. Is that's right?

Roderick B. Hall - Goldman Sachs Group, Inc., Research Division - MD

So welcome, everybody. I'm Rod Hall. I do all the infrastructure technology research at Goldman Sachs along with my team. So I hope everybody's had a good day. It's the first day at the conference here.

I need to read a safe harbor statement for Dell, and then we'll jump into questions. So Dell Technologies' statements that relate to future results and events are forward-looking statements that are based on Dell Technologies' current expectations. Actual results and events in future periods may differ materially from those expressed or implied by these forward-looking statements because of a number of risks, uncertainties and other factors, including those discussed in Dell Technologies' periodic reports filed with the SEC. Dell Technologies assumes no obligation to update its forward-looking statements.

Always exciting to do that right at the beginning.

Anthony Charles Whitten - Dell Technologies Inc. - Co-COO

Well done, Rod. [Thanks for that].

QUESTIONS AND ANSWERS

Roderick B. Hall - Goldman Sachs Group, Inc., Research Division - MD

All right. So you're approaching a year since your last Analyst Day when you laid out an updated strategy, capital allocation plan. So that was a very hotly anticipated Analyst Day actually as I recall. We were all looking forward to an update on that strategy. How would you describe the execution since then against that and the position looking forward?

Anthony Charles Whitten - Dell Technologies Inc. - Co-COO

Yes, sure. Maybe let me start by just recapping what we said a year ago and then we can kind of measure our progress against that. So a year ago, look, our argument was we are perfectly positioned in the data and multi-cloud era with a set of durable competitive advantages, leadership positions in a large and growing market that give us the opportunity to create significant profitable growth; and that after a couple of years of debt pay down, we have the ability to invest to extend those leadership positions and return capital to shareholders. And there's really 3 parts to that argument, I think, you should measure us against.

The first was our core business sits in about \$720 billion of total addressable market where we are the market leaders in those markets. We're the #1 player in client revenue. We're the #1 player in client units and revenue -- commercial client units and revenue, excuse me. We're #1 in x86 servers. We're #1 in external storage. We're #1 in data protection. We're #1 in hyper-converged infrastructure. And we've been a consistent share gainer in those markets. So \$720 billion of total addressable market, a history of share gain and leadership position. There's enormous headroom for us to grow just inside those core markets.

The second part of our argument was adjacent to those core markets is another \$720 billion of TAM, which we have the ability to address using the same capabilities and advantages that we've built inside our core business. These are places like telecom and Edge, multi-cloud or even the application of our APEX business, our as a service business to our existing TAM that further grows the market for us.

And then the third leg of our argument was we're committed to creating shareholder value. So at that point, we announced a balanced capital allocation strategy, including a commitment to return 40% to 60% of adjusted free cash flow to shareholders. And we reminded the world that we performed in multiple economic environments. And so how we've done against that in the last year, I think we've delivered against that framework pretty well.

If you sort of look at the trailing 12 months, \$105 billion in revenue. That's up almost 16%. If you zero in on our Q2, \$26.4 billion in revenue. That's up 9%. For the first half, \$52.5 billion. That's up 12%. And the balance in our business has been very good. So for the first half, both our CSG and our ISG business grew 13%. And it's not just our markets are buoyant. We're gaining share in those markets. So if you look at our Q2 results, we gained 200 basis points of share in the client business. We gained, importantly, 300 basis points of share in the commercial client business. We gained 188 basis points of share in servers, and we gained almost 300 basis points of share in external storage announced last week. So business is performing really well.

Outside our core business, we've continued to generate a lot of technical and commercial momentum in places like telco and the Edge. And during earnings in Q2, we announced our APEX business now crossed \$1 billion in ARR, growing 78% year-on-year and attracting new customers -- 200 new customers to the franchise in Q2. So again, we're building core -- new businesses outside our core.

And we followed through on our commitment to deliver capital to shareholders. So over the last years, we've paid down debt. We're now investment-grade by all 3 ratings agencies. We spun out VMware in a tax-efficient way to shareholders. We have returned \$3 billion in capital, 54 million shares purchased through Q2 since the inception of that program, \$500 million in dividends in the last 2 quarters. So stepping back, we're really proud of our execution against the framework we laid out a year ago. And as I think we'll talk about today, we're really optimistic about the future of the business.

Roderick B. Hall - Goldman Sachs Group, Inc., Research Division - MD

I don't think I've ever heard anybody start with so many numbers, so that's impressive. Let me jump into demand. I guess one of the things I like about the Dell team is it's a very seasoned team, and you guys are straight shooters. You're always very transparent with us about what's going on. I think that helps investors to feel more confident with the management team of the company, too, generally. You called out some weakness this last quarter. So could you dig a little deeper into when you started to see things slowing and how the trajectory of demand is progressing from your point of view? I guess maybe divide it into CSG and ISG, if you would.

Anthony Charles Whitten - Dell Technologies Inc. - Co-COO

Sure. Yes. And thank you for saying that. Again, we -- all we know how to do is communicate what we're seeing in our business. So we're halfway through the quarter, so I'll confine myself to kind of Q2 to give you a feel for the dynamics. But yes, starting on the CSG side, look, I would say in Q2, we saw a rather abrupt deceleration of demand in quarter. And it manifested itself sort of different ways inside our customer environment.

Look, in the commercial side of the business, we heard, "I'm having trouble hiring. I'm reevaluating my forward hiring. I'm distorting spend away from client to other IT priorities," or maybe in a backdrop where supply chains have improved and lead times have shrunk, "I'm focused only on my most pressing client needs." But the net was it was a rather abrupt shift in corporate sentiment. I think others saw that in the industry. Look, the consumer business, we knew -- smaller portion of our business, as you know, we knew it was going to be challenged in Q2, but it probably decelerated even more than we anticipated as inflation just sort of impacted household sentiment in all economies, frankly.

ISG dynamics were very different. So I think to be really clear, we had demand growth in both our server and storage business in Q2. But we saw that growth moderate coming into the quarter and over the course of the quarter. And where CSG dynamics were more of a pause and an abrupt shift, this was more like a slide. It just was more caution or more deliberate behavior kind of entering the customer environment. So deals took longer to close throughout the quarter. You felt more scrutiny of spending. Again, no one was canceling digital transformation investments. We didn't see a change in cancellation or orders rate or anything like that, but we did see caution kind of enter the environment.

What we did not hear on either business, Rod, was sort of a fundamental change in dynamics that would call into question the long-term health of our business. So in the commercial client business, 75% of companies are operating hybrid today. That's going to be a good thing for us as companies look to refresh all of those PCs that were bought in the early days of the pandemic. And as I said, nobody is saying, "I'm going to cancel digital transformation or automation investments in my business." That's core to company strategies. But we did hear caution kind of enter the environment.

Roderick B. Hall - Goldman Sachs Group, Inc., Research Division - MD

So the quarter ended in July. I'm sure everybody in the room knows that, maybe not. But did the linearity of that quarter -- in other words, you saw this sluggishness particularly in ISG I'm interested in. Could you tell a difference from one month to the next? Like did it develop more in July than it did in the prior 2 months? Or [how did you view it]?

Anthony Charles Whitten - Dell Technologies Inc. - Co-COO

I'm not sure I would parse it too much by month. I would just say over the course of the quarter, we saw caution kind of enter the environment. So what you saw was we had a much more backloaded ISG quarter than is typical for us, and backlog for us remained elevated kind of coming out of the quarter.

Roderick B. Hall - Goldman Sachs Group, Inc., Research Division - MD

Okay. And then the other thing that you guys talked about was large enterprises -- seeing it more in large enterprise than in SMBs. And you've been through -- it is a very seasoned team. It's been through downturns before. So can you talk a little bit about whether that's what you've seen in prior slowdowns and why you think it is the case that SMBs aren't as slow as the larger enterprises?

Anthony Charles Whitten - Dell Technologies Inc. - Co-COO

Yes. We dropped that tidbit into the earnings call. And you're right, it is unusual by historical standards. Typically, small businesses are the bellwether for us, a more pervasive slowdown in spending. And to be clear, small and medium business growth moderated for us, moderated kind of through the quarter a little bit, but it was much more resilient compared to the large enterprise business. What do we make of that? We're not quite sure, to be honest with you. It's -- for whatever reason, the caution that I described showed up in sort of the large corporations first or maybe only, we'll find out.

I think it's kind of a reminder to us, we're on a little bit of uncharted ground here. I had a lot of conversations over the last day here of teams trying to, I think, apply prior recessionary modeling to the current environment. I just don't think it's that simple anymore in this environment. But yes, for whatever reason, we saw more caution on the large enterprise side.

Roderick B. Hall - Goldman Sachs Group, Inc., Research Division - MD

Yes, this is -- if it turns into a recession, this would be my third that I've been through as an analyst. And I -- usually, you would see it bubbling up from the bottom: the consumer, the SMBs and so on. You don't really see that here, so it is a very confusing environment.

Anthony Charles Whitten - Dell Technologies Inc. - Co-COO

Yes. We don't have a huge consumer presence. I mean, obviously, consumer was really challenged. We knew it was going to be challenged. It was maybe moderately worse than we anticipated. But yes, SMB was relatively stronger.

Roderick B. Hall - Goldman Sachs Group, Inc., Research Division - MD

Yes. Okay. On the supplies, I guess, I'll maybe switch gears to that and ask a little bit about supply constraints. You said it's starting to ease. Could you say what areas are worst impacted and kind of what's going on with the supply chain for you right now? Another additional question that I'll add on the end of this is we've heard that companies in the PC supply chain are beginning to take parts out of inventory and sell them back out to brokers as production expectations come down, that kind of thing. So maybe you could set that one aside for a second and address it at the end, but...

Anthony Charles Whitten - Dell Technologies Inc. - Co-COO

Yes. Well, I think I would categorize the supply chain dynamics as improving, but we're not out of the woods yet by any stretch. And so, look, the prevalent challenge over the last couple of years stands, which is semiconductors and trailing node semiconductors, so the 40, 55, [60] nanometer

parts, I've heard investors here refer to them as the jellybean parts. Well, those jellybean parts can hold up a \$10,000 server shipment, and that's the reality of the environment we're in.

If I translate that kind of backdrop to our business, look, on the CSG side of the business, I would call our supply chain more or less back in normal profile. In Q1, we said we had elevated backlog, or maybe I think we categorized it at the higher end of normal. I would categorize our backlog as normal right now, and we're on standard lead times across the portfolio. So for purposes of this, there's always some amount of spot shortages, right, Rod. But for the purposes of this conversation, the PC supply chain is back in profile.

ISG continues to be challenged, and it continues to be challenged most principally in the server business. And that's where industry-wide shortages of NIC cards, network interface controllers, power supplies and other miscellaneous semiconductors, integrated circuits, that's what's causing the challenge. And so again, we had elevated backlog in our ISG business. Storage, there's always a little bit of shortages out there, but we're performing quite well and navigating. So the real pain point in the industry and for us is continue to be servers.

Roderick B. Hall - Goldman Sachs Group, Inc., Research Division - MD

Could you talk a little bit about this inventory situation? Do you find yourself now with excess component inventory? What are you doing with that excess inventory if you've got it?

Anthony Charles Whitten - Dell Technologies Inc. - Co-COO

Yes. Well, we've got -- we've gotten a lot of questions about -- because anyone who sort of has tracked us over time would say, "You're coming into this quarter with elevated inventory. Is that a permanent change in posture for you guys?" And it's truly not. It's a remnant of the challenges that we've just come through. And so where is there more inventory? The more inventory is in our infrastructure business as we wait to assemble that kit I just described, those jellybean parts, to show up so we can ship.

Again, it's not a permanent state of affairs for us. As supply gets better, we anticipate inventory coming more into our historic profile. As the consumer or Chrome business slows down, there's always portions of the market where you may sit on a little bit more finished goods inventory. But the reality of our business right now is that elevated inventory is materials and on the infrastructure.

Roderick B. Hall - Goldman Sachs Group, Inc., Research Division - MD

So it's not as if you're sitting on a bunch of power management chips that you could have used for PCs that somehow you would be either sending back out to brokers who are using it for other applications...

Anthony Charles Whitten - Dell Technologies Inc. - Co-COO

Not that fungible for us, no. And again, we're -- the investments that we've made in our supply chain over the years in digitization and simulation, we're pretty good about it. We sit on parts only that we need to sort of meet customer demand.

Roderick B. Hall - Goldman Sachs Group, Inc., Research Division - MD

Right. And that inventory management has likely been -- or I think it's been one of the reasons you've gained so much share in all these areas. I mean, clearly, it's been an advantage for you. Would you [agree with that]?

Anthony Charles Whitten - Dell Technologies Inc. - Co-COO

Look, our supply chain team is the best in the industry, period. And we -- it has been one of our most durable competitive advantages. I mentioned that phrase in my introductory remarks. And we have learned a lot, even against that backdrop, over the last years as we've sort of gotten stronger through this period of challenge. Look, we buy more than anybody in the industry, and that gives us an enormous advantage. But the reality what we found over the last 18 months for sure is it's our depth of supplier relationships that has been the differentiator for us.

So we didn't always used to be the biggest, and we found that trust and history with the supply base and the ability to go deeper into the supply base has been a real differentiator for access to the parts. You couple that with, as I said, smart continuity of supply strategies, things like multi-vendor strategies, the ability to use our balance sheet to take a long-term agreement when we need to, less complexity in our products, all of that contributes.

So our supply chain has been critical. But look, we also have a very different model on 2 other legs that has given us an advantage and let us gain share. One is our direct sales force is very different. We touch more customers than anybody, and that allows us to send a better demand signal back to the supply base. And importantly, it lets us shape demand to where there's available supply. So we've spent the last couple of years having a lot of conversation with customers that goes something like, "I know this is your spec. I know this is what you requested. Here's 2 to 3 alternatives on shorter lead time."

And then look, our product teams over the years, that's the third leg of the stool I would say, have worked to increase modularity and drive simplicity into the product line that lets us qualify parts faster and just be more responsive. So I'd like to say it's not one single thing, Rod. It's kind of our integrated business model that's been the differentiator.

Roderick B. Hall - Goldman Sachs Group, Inc., Research Division - MD

Okay. Sounds good, Chuck. Let's talk about costs a little bit. You've had logistics costs elevated. Other elements of costs that have been elevated through this thing. Can you just remind people here what the margin impact of this has been on Dell? And then when do you think margins return to some sort of a more normalized level?

Anthony Charles Whitten - Dell Technologies Inc. - Co-COO

Sure. Well, we've been in an inflationary environment for some time, as you know, and that is -- always puts pressure on margins because pricing in our business follows those cost increases. We obviously endeavor to take price as quickly as we can. But it takes time, usually a quarter, for us to sort of pass through the inflationary costs. The dynamics are shifting now. So as we said, in Q2, we saw commodity costs start to tip deflationary, principally because of memory and LCDs. And in Q3, we see, again, modest deflation year-over-year driven by SSDs, hard drives and LCDs.

Logistics has also been a challenging contributor to the margin dynamics. In Q2, they were elevated. We're starting now to see alleviation in Q3 principally on the ocean side. But also as the supply chain comes more back into profile, we are expediting fewer and fewer parts. And so this is when our model really is advantaged because we hold such low levels of inventory, we access deflationary components quicker than the rest of the industry, and that's good for our margin structure. So if you unpack our guide in Q3, I think what you'll see is we anticipate sequential margins improvement in Q3, and it's that dynamic. It's the deflationary environment coupled with our sort of low inventory model.

Roderick B. Hall - Goldman Sachs Group, Inc., Research Division - MD

Okay. Maybe talk a little bit about storage. That's been -- prior to us getting into the -- all the supply chain problems and demand and so on. One of the big stories is PowerStore in the midrange storage product and revitalization of that. And I think that's now on a -- or was on and still is on a pretty good track of momentum as that sells back into that preexisting base of midrange. But look, interested in an update on that and also kind of how you see the product portfolio in the higher end of storage as well and what other work needs to be done with that portfolio.

Anthony Charles Whitten - Dell Technologies Inc. - Co-COO

Sure. Yes. Well, look, we're incredibly pleased with the portfolio top to bottom. I think a reminder, we -- Dell EMC has been the leader in external storage -- in every external storage category for 20 years. So we're the leader in high end, midrange, unstructured data protection. You name it, we're sort of the leader in it. But as you said, look, we principally have been investing in that portfolio over the last couple of years with an acute eye on the midrange because that is the spot. First of all, it's the largest market with the fastest growth. It is also the place where we have given up the most share compared with our sort of historical high-water marks. And so that's our PowerStore product. But the investments that we've been making have been kind of top to bottom across the portfolio. So maybe a few observations.

PowerStore, you asked me to start with that. We've dropped in the last couple of years 3 different software updates to PowerStore. And the product just continues to perform really well. It grew double digits again in Q2. It's now representing 45% of our midrange SAN mix. And importantly, for us, it's attracting new customers and repeat buyers to the franchise. So in Q2, 21% of our customers were new to Dell, and 41% were repeat buyers. And we gained share in the midrange in Q2. So we're feeling really good about our midrange portfolio.

We also have refreshed PowerMax, which is our high-end product. We dropped a significant number of software upgrades to that, and it's got some features like the first mainframe compression, which positions us really well for the mainframe refresh that's underway. It's got a record now 65 million secure snapshots on the product. It's the leader in the market, and it sort of got better with that.

We also continue to invest in our PowerFlex product. 100 new features dropped this summer, including the ability to operate that in an AWS operating environment. We're making progress in our data protection business. I think we've shared, we now protect 12 petabytes of data in the public clouds with that. And so up and down the portfolio, we feel really, really, really good about the investments we've made and the strength of it.

Where do we need to invest going forward, I think, was the last part of your question. The first is in multi-cloud. I think we announced Project Alpine, which is our intent to bring our file, block and object storage to the public cloud. That's very important for a company like ours that views ourselves as essential to the future of sort of multi-cloud and customer environments. I would say DevOps continues to be a place that we focus. The DevOps community continues to be very influential in our customer environments. And so continuing to make our products easier to use and more relevant to DevOps is really important. And then just security. You can't have a conversation about infrastructure without talking about how you make your products more secure, how do you help people predict attacks and prevent attacks.

So I think those are the areas of focus. But look, 300 basis points of share in Q2. The breadth of our portfolio is our advantage because no matter the architectural discussion or the type of data -- file, block, object, data protection -- we are in the conversation with the customer. It's a really privileged position that we have.

Roderick B. Hall - Goldman Sachs Group, Inc., Research Division - MD

Do you -- storage is one of those things that -- it's a footprint game, and footprint doesn't seem to change all that much with storage. We talk about flow share a lot when we analyze it. So you'll see one day to the next, somebody is gaining share, somebody is losing share in the revenue flow of that particular quarter. But footprints don't seem to be all that malleable. But then I hear you talking about new customers coming on board. Do you feel you've gained footprint share particularly in the midrange or significant share?

Anthony Charles Whitten - Dell Technologies Inc. - Co-COO

For sure. I mean you can just see it in the quarter-after-quarter new customers that we're gaining. And look, even though footprints can be sticky in the short term, customers are always evaluating new storage architectures, new technologies, right? We have the ability to go into a customer environment and say, "We will make it attractive to you to swap out, right, to the latest and greatest technology." So I would agree with your premise, it is a stickier footprint, but it's not permanently stickier, right?

Roderick B. Hall - Goldman Sachs Group, Inc., Research Division - MD

And who do you think has been the major contributor to your share? Anybody to call out?

Anthony Charles Whitten - Dell Technologies Inc. - Co-COO

I'll let you guys go run your models on that versus -- (inaudible) quote for you to get public.

Roderick B. Hall - Goldman Sachs Group, Inc., Research Division - MD

Storage footprint is tough to model, I'll tell you that.

Anthony Charles Whitten - Dell Technologies Inc. - Co-COO

Yes, they are.

Roderick B. Hall - Goldman Sachs Group, Inc., Research Division - MD

Nobody throws storage away. So let's talk a little bit about your cloud offerings. Competitors like NetApp and Pure have been making some headway. It's hard to judge the sizing of it in some cases. NetApp's a little bit easier than Pure. Do you see that as a developing area of opportunity? So they've -- just to recap, NetApp is sold to some large cloud provider, pretty good size deal. They called out last quarter. Pure is selling into this [RCAI] installation of metas. We do seem to be seeing a little bit more branded storage coming in particularly for AI applications, and I'm curious how interesting do you think that is for Dell. Have you seen this kind of activity brewing out there?

Anthony Charles Whitten - Dell Technologies Inc. - Co-COO

Sure. Yes. Look, we think it's really interesting. And maybe taking a step back strategically, our -- the spinout of VMware was important for us on a couple of dimensions. One was, clearly, creating shareholder value and doing it in a tax-efficient way. And I think that part is clear. But the other was it was a reminder that we are not a VMware stack trying to compete against other cloud stacks, that our view of the world and, frankly, the hyperscalers' view of the world and our customers' view of the world is it is going to be a multi-cloud world.

And though we are first and best and we are the best choice in a VMware environment, ultimately, we have to operate in multi-cloud architectures. And that means us collaborating and working with all the major public clouds to make that happen given our position in infrastructure. And so we see it as an enormous opportunity to cooperate with the public clouds on multiple dimensions, and we're doing that. I mentioned Project Alpine, right, file, block, object storage, brought to the public cloud so that customers in a multi-cloud world can say, "I have the same tools and skill sets on-premises. I'm going to use them for public cloud storage and have the ability to train my team once without refactoring applications and all of that. So that's an important thrust for us.

We have other collaborations that are really important in a multi-cloud world. Our Azure Stack HCI solution is industry leading. I think we're responsible for 70% of Microsoft's Azure Stack HCI deployments out there. You can now apply EKS Anywhere and Anthos through Dell-validated designs on our PowerFlex product. And so the reality of it is -- and there's more to come. So I think, look, we see the opportunity to collaborate with hyperscalers and all types of clouds because that's what customers are demanding. It's very strategic for them in the future to be able to say, "I want to have a multi-cloud architecture where I access all of the innovation in the public clouds. But for security, latency, other reasons, I'm going to have on-premise infrastructure. I just want it to work better together."

Roderick B. Hall - Goldman Sachs Group, Inc., Research Division - MD

Okay. You can't go on to an earnings call lately for an enterprise IT company, particularly hardware companies, without hearing people ask whether backlog's cancelable or not. And server seems like a particular area where there may be some fungibility across different products, different companies. And I -- and you guys called out some slowdown in server last quarter. I'm not suggesting that's related to cancellation of orders, just that there was a little bit of demand slowdown. But I'm just curious whether you think there is more risk of cancellation there. Is the perception of that correct at least that we might have? Or is that really not true for reasons we don't maybe fully understand?

Anthony Charles Whitten - Dell Technologies Inc. - Co-COO

Yes, I can just speak for our company and say we feel very good about the stability of our backlog in server and in storage, but certainly in server since that's the premise of your question. Look, I'd start with industry backlog is high in servers. And so the world is not meeting the demand of customers right now, right? And so that's sort of the starting position.

But I think if you come to our business, you mentioned our supply chain earlier, we have -- to be direct, we have seen no evidence in the last 2 years of increases in cancellation rates or duplicate ordering or anything like that. And customers and partners have told us time and time again that an order with Dell has just been a more reliable order, right? And so -- because we've been able to meet lead times. We've been -- we've met our delivery commitments.

And so in many ways, again, given the backdrop of elevated backlog and we're still short of NICs and power supplies in the industry so the operating dynamic with customers, the most common conversation is about availability, not about anything else, provided our supply chain continues to out-execute everyone and have shorter lead times. We don't see a lot of risk in our -- in the sort of stability of our backlog, and we haven't.

Roderick B. Hall - Goldman Sachs Group, Inc., Research Division - MD

Do you think that as component prices -- let's assume that this thing continues to thaw out from a supply chain point of view, component prices. Some have already started coming down, but they come down more precipitously or at least a little bit more aggressively in the future. So the cost to make that marginal server is lower than the cost of the backlog order. Do you think that increases risk of cancellation?

Anthony Charles Whitten - Dell Technologies Inc. - Co-COO

Again, I would say, first of all, on pricing, there's a couple of dynamics going on. It's not all commodity dynamics, right? I mean one is -- there's sort of 2 things that have driven higher ASPs in servers. One is richer content rates. I mean I think we always have to remember that it's not all commodity costs that have driven up the price. But look, as long as there are shortages in the industry, I think the dynamic is going to be about availability and not cancellation rates.

And look, if I roll forward, as I said, modest deflation in sort of Q3. We're not anticipating, given higher content rates and that modest deflation, anything dramatic from an ASP standpoint. So again, at least the backdrop as it sits right now is much more about availability than I see the opportunity to cancel and book a cheaper server. That's just not -- it's not what we're seeing.

Roderick B. Hall - Goldman Sachs Group, Inc., Research Division - MD

I mean I guess if you guys saw that coming, there are a lot of detailed ways to get back into that backlog and manage it out as well. It's not necessarily just a binary situation.

Anthony Charles Whitten - Dell Technologies Inc. - Co-COO

Yes, I mean, look, and our customers need their compute, right? The higher backlog has been a pain point in the industry. So I mean we're endeavoring to burn through as fast as the supply chain will allow us to do it. It's the right thing to do for...

Roderick B. Hall - Goldman Sachs Group, Inc., Research Division - MD

We recognize these questions may sound ridiculous considering you can't really serve the demand right now here as we said.

Anthony Charles Whitten - Dell Technologies Inc. - Co-COO

Yes. But no, I get the premise of the question, which is look, this has been a unique time. And when and how will we see supply chains adjust and come back in a profile on what happens, those are the right questions to ask.

Roderick B. Hall - Goldman Sachs Group, Inc., Research Division - MD

Let me pause. We've got about 8 minutes left, but just see if anybody in the audience has any questions. I got one up here. Anybody else out there with a question for Chuck? Okay. Right here in the front. If you could say your name and where you're from before you ask, that would be great.

Chris Hanaway

Chris Hanaway, Allspring Global Investments. How important is dividend growth to your shareholder return policy?

Anthony Charles Whitten - Dell Technologies Inc. - Co-COO

Yes, so look, we're incredibly pleased to now finally have a balanced capital allocation strategy. So for those that haven't taken a look at us lately, in recent history, we were spending 95% of our available free cash flow to pay down debt. And as I mentioned at the outset, the achievement of investment-grade rating across all 3 rating agencies and right now, we're at about a 1.7 core leverage ratio -- our long-term aspiration is, call it, 1.5 -- it gives us the ability to return capital to shareholders. And so the few facets of the remaining capital allocation strategy, you mentioned dividend, \$1.32 per share this year, that's a billion dollar commitment. We paid 2 dividends last 2 quarters. We think that an annual cycle is the right time for us to start to evaluate that. And we certainly expect to have the opportunity to increase the dividend over time.

Share buybacks have been an important part of our equation in the last -- since inception. I think -- if you had gone back a year ago to our Analyst Day conversation, we said the principal objective of our capital allocation to do buybacks was to manage dilution. I think you've seen us use the words more now, "Hey, we're going to be opportunistic," and now maybe even stronger language, "We're intrinsic value buyers of our stock." So at the current share price level, it's -- we think it's an attractive thing to buy. And if it stays at that level or if it goes lower, we'll buy more. If it goes up, we'll buy less. And so I think that's part of our balanced allocation strategy.

And then look, we think M&A is part of any good growth strategy. We are -- the circumstances around which we did the transformational deal with EMC were pretty unique. And so what I would anticipate us doing is things that are much more smaller, technology focused, talent focused in those growth businesses I described. So nothing that would compromise our ability to return 40% to 60% to shareholders. So look, all of those levers are important to us on balance, and again, we're really happy. If I can [chat], I'm sure my CFO, Tom Sweet, is listening right now, we're only half a year into this new balanced capital allocation strategy. So give us time, but we're pleased with where we're headed.

Roderick B. Hall - Goldman Sachs Group, Inc., Research Division - MD

Great. Any other questions out there? Otherwise, I'll keep going. Okay. All right. Let's talk a little bit -- let me follow up on that real quick, and then I'll keep going. Interest rate environment. Clearly, it's changing. Does that have any impact on your thinking about dividend versus buyback? Or it's just sort of we just...

Anthony Charles Whitten - Dell Technologies Inc. - Co-COO

No, it doesn't. Yes.

Roderick B. Hall - Goldman Sachs Group, Inc., Research Division - MD

Okay. So let me talk a little bit about or ask you a little bit about the APEX, \$1 billion. That's seen some pretty good order growth you said, \$1 billion of ARR or over \$1 billion. Can you talk a little bit about the value proposition that, that brings to your customers here? And how does APEX attraction evolve over time for people, too, especially as interest rates go up? We always think about that with these kinds of offerings.

Anthony Charles Whitten - Dell Technologies Inc. - Co-COO

Yes, yes. So look, we're -- I mean, we were really excited to share the milestone of \$1 billion in ARR and 78% year-on-year growth and 200 new customers. Look, in some ways, what we're trying to do is really simple, which is provide our customers choice in how they can consume their infrastructure. So customers can buy our infrastructure. They can subscribe to our infrastructure. They can subscribe to our infrastructure with managed services on top of it. And APEX comes into play in the latter two. And certainly, in this environment, right, companies are increasingly interested in ratable, pay-as-you-go type offers. And where we've seen the most acceleration in the business has been in a couple of the offers.

One is our Flex on Demand offer. That's effectively any of our infrastructure: server, storage, hyperconverged infrastructure deployed at a customer with a fixed capacity and the ability to surge above it but managed by the customer. And then the data center utility offer which is, "Hey, Dell, would you manage a portion or all of my data center for me?" They -- so that's the value proposition. It's particularly attractive to this environment.

Interest rates aren't really an impact on it, except from a customer-backed perspective of, "Hey, I'm trying to stretch every dollar thoughtfully," and having a more ratable, pay-as-you-go framework is important. Increasingly, we expect that business to have more and more managed service type offerings on top of it. So you've heard us announce things like our APEX Cyber Recovery services. That's a, "We'll do cyber recovery for you," and I think that's the growth engine. But right now, the principal interest has been on our Flex on Demand and data center utility office, which is great. The reality is, is we're not trying to march customers down any specific path there because most customers are experimenting with multiple consumption models inside their environments. So that's the choice we just want to offer them.

Roderick B. Hall - Goldman Sachs Group, Inc., Research Division - MD

The reason I ask the interest rate question is if I'm leasing or if I'm taking as a service some hardware anyway, there must be an inherent financing cost built into that I'm going to have to pay...

Anthony Charles Whitten - Dell Technologies Inc. - Co-COO

Sure. Yes, no, that's our DFS business. I'd say we have a big leasing business as well. In Q2, that grew -- originations grew 24%. And that tends to be a very good business in times of economic turbulence, as you can imagine, for many of the reasons I just described there. Our DFS team would tell you, even at the current interest rate environment, it's not a deterrent for...

Roderick B. Hall - Goldman Sachs Group, Inc., Research Division - MD

Right. It is an initiation that actually increased in DFS.

Anthony Charles Whitten - Dell Technologies Inc. - Co-COO

There you go. Exactly.

Roderick B. Hall - Goldman Sachs Group, Inc., Research Division - MD

But -- okay. We've got a minute -- couple of minutes left. Let me ask you, I don't know if you'll have an answer on this, but what is your -- when you look at the economy next year, you look at all the information that you've got access to, what are Dell's thoughts? Or at least, how are you planning as you look into 2023? You've called out this weakness. Do you plan for a recession? Do you plan for a slowdown? What are some of your planning assumptions that you look into next year?

Anthony Charles Whitten - Dell Technologies Inc. - Co-COO

Well, I'm not an economist, so I'm not going to pontificate on the economy, but I know you have to ask. But I'll tell you what we're doing in our business, which is we focus maniacally on what we can control. So a few elements to that. And we have a playbook, by the way, that has been battle-tested over multiple cycles. But the first thing we did is we saw that demand signal. We see it better than anybody else given the reach of our direct sales force. And we immediately take action on the cost structure. And you saw that in our operating -- our OpEx, excuse me, in Q2 which was down 3% year-over-year and down 50 basis points sequentially. So we took immediate action.

But we did not do that in a peanut butter way across the business, right? We view these moments of turbulence as the opportunity for us to more quickly position because of our demand signal and go invest and gain share against the competition profitably. And so we protected our innovation investments. We protected investments in the new business, as I have described. And so we're being very thoughtful about how do we use this moment of time to accelerate the business long term.

And then we do what we do best, which is we get out and maniacally focus on customers. They're in the same economic environment we are. And technology is the solution to the challenges they're facing, whether it's inflation or labor challenges. And so if we can continue to be, as we are, good executors on the business, prudent in our cost management and customer centric, that's kind of our playbook.

Roderick B. Hall - Goldman Sachs Group, Inc., Research Division - MD

All right. I think that's a great place to end it. So thanks a lot, Chuck. (inaudible)

Anthony Charles Whitten - Dell Technologies Inc. - Co-COO

Thank you. I really enjoyed it. [Appreciate it]. Thanks.

Roderick B. Hall - Goldman Sachs Group, Inc., Research Division - MD

Yes, appreciate it.

Anthony Charles Whitten - Dell Technologies Inc. - Co-COO

Awesome.

