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Good afternoon, and welcome to the Fiscal Year 2021 Third Quarter Results Conference Call for Dell Technologies Inc. I'd like to inform all participants: this call is being recorded at the request of Dell Technologies. This broadcast is the copyrighted property of Dell Technologies Inc. Any rebroadcast of this information in whole or part without the prior written permission of Dell Technologies is prohibited. (Operator Instructions)

I'd like to turn the call over to Rob Williams, Head of Investor Relations. Mr. Williams, you may begin.

Thanks, Erica, and thanks, everyone, for joining us. With me today are our Vice Chairman and COO, Jeff Clarke; and our CFO, Tom Sweet; along with our Treasurer, Tyler Johnson. Our press release, financial tables, web deck, prepared remarks and additional materials are available on our IR website. The guidance section will be covered on today's call.

During this call, unless we otherwise indicate, all references to financial measures refer to non-GAAP financial measures, including non-GAAP revenue, gross margin, operating expenses, operating income, net income, earnings per share, 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, and that VMware historical segment results have been recast to include pivotal results.

Additionally, 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 can differ materially from those projected due to a number of risks and uncertainties, which are discussed in our web deck and SEC filings. We assume no obligation to update our forward-looking statements.

Finally, before I turn it over to Jeff, I'd like to touch on the amended 13-D we filed in July regarding our exploration of potential alternatives with respect to our ownership interest in VMware. We believe the tax-free spend could drive significant shareholder value by simplifying our capital structures and enabling greater strategic flexibility while maintaining a strong commercial partnership between Dell and VMware. Both Dell and VMware have publicly highlighted mutual interest and the potential benefit of such a transaction and have engaged on key work streams, including mutually beneficial commercial arrangements and Dell's expectation of a substantial cash dividend to VMware stockholders in connection with such a transaction. As a reminder, the earliest the transaction could close would be September 2021, with an announcement coming between now and then, assuming we can come to an agreement. There is also the possibility that we will not do anything, and we would maintain our current ownership structure.

With that said, we will not address the discussions any further or take questions related to this topic on today's call.

Now I'd like to turn it over to Jeff.

Thanks, Rob. We have now been through 3 quarters of navigating an uncertain and, at times, difficult year. We have been tested across our global society, across industries and companies and as teams and as individuals like never before. I could not be prouder of how the Dell Technologies team has responded. We're growing, innovating and delivering for our customers in extraordinary ways when and how they need us most. Through it
all, one thing is clear, the mega technology trends that we have long called out are accelerating, and these trends are highly favorable to Dell Technologies. We are uniquely positioned to win in the growing markets of 2020, and we are making the right investments and innovating to capture the growing markets of tomorrow.

For the vast majority of companies, digital transformation is now a must-have and accelerating. We see it in our customers’ interactions. We see it in our data. In October, we released the third installment of our latest Digital Transformation Index, where we have been tracking digital transformation patterns of more than 4,000 customers since 2016.

Our 2020 index revealed that 80% of organizations globally have fast track digital transformation programs. And when compared to the 2018 study, nearly 25% of respondents have progressed from being digital laggards or followers to a more advanced stage in their digital journey. This is great news for our customers’ future and more broadly, for the global economy. And it’s also great news for us with major investments going towards edge, distributed work and modern consumption, cybersecurity, 5G infrastructure, digital experiences and data management.

Together, these trends are taking us to a future that is highly distributed, with distributed workforce, learning and health care enabled by distributed technology infrastructure, computing, analytics and real-time outcomes at the edge. Organizations investing today will have an advantage tomorrow and they are turning to Dell Technologies as their strategic partner.

Let me use a real customer example to talk about the edge. Fedex CIO, Rob Carter, was with me last month at Dell Technologies World, where we talked about how latency, decentralized computing and data-driven insights they need to lead in the Internet of everything.

FedEx uses an array of our hybrid cloud technology to bring simplicity and speed to the edge, including VxRail, VMware and pivotal and cloud-native environments, all to keep our world connected and moving. Now we are building on that relationship, working with FedEx and Switch, a leading exascale data center company, to develop technology hubs across the United States to bring IT resources closer to where the applications and data reside, enabling the benefits of 5G and AI technologies. This is a perfect example of how we take our deep IT experience and make it easy for customers to manage data and workloads across all of their operations.

We also had another exceptional quarter in CSG and what has become a multi-quarter trend as customers turn to Dell to enable the remote and hybrid workforce. Our wide range of PCs, including Chromebooks, are providing students everywhere with the essential learning tool they need. The pandemic has expanded consumers’ use of online purchasing, which is a big area of focus for us.

While we did lose share in calendar Q3, this is a result of a strategic decisions we made earlier in the year. We’ve moved from retail to our advantaged direct and online selling for consumers. Our strong financial performance reinforces that strategic decision, and we believe this is the right long-term balance for our business.

And finally, customers are looking for a choice in the way they consume and pay for IT. That’s why at Dell Technologies World, we announced Project APEX to unify our as-a-service and cloud capabilities. We have committed to providing all of our solutions as-a-service, and launched the Dell Technologies Cloud Console, enabling a consistent cloud operating model across a customer’s entire IT environment, from the edge to the core to the cloud.

In the past year, we’ve seen increased interest in our as-a-service and flexible consumption offerings. And this type of transformation expands recurring revenue, providing even more stability as we navigate industry seasonality, mix and demand. The accelerated digital transformation we are experiencing today plays directly to the thesis we had in creating Dell Technologies. We are #1 in everything, all in 1 place. We have the breadth and diversity to lean into pockets of growth when and where they happen, and we can deliver consistent long-term returns as a result.
Now let’s move into the third quarter performance and the team’s strong execution. Revenue was $23.5 billion, up 3%; and operating income was up 12% to $2.7 billion or 11.6% of revenue. As I mentioned earlier, our Client Solutions Group had an outstanding quarter, delivering record shipments, revenue and operating income. Revenue for Q3 was $12.3 billion, up 8%. The PC is the essential device for this remote-everything environment we’re living in today, as evidenced by the ongoing demand we are seeing for work and learn-from-home solutions, along with double-digit growth in education, government, particularly in our North America Federal business and the consumer vertical.

Demand for notebooks remained strong, with orders up 24%, driven by double-digit orders growth across the majority of our commercial and consumer notebook lines. In addition, orders for commercial Chromebooks more than doubled.

Our consumer business had another impressive quarter, primarily driven by our premium XPS and Alienware brands, which combined, were up 43% on an orders basis. The consumer direct business was up 40% -- was up 47% on orders, and our consumer direct online business was up 62% based on orders as we seize the opportunity what we believe is a long-term multiyear trend towards e-commerce.

Infrastructure Solutions Group revenue was $8 billion, down 4%. While the overall market for ISG has been soft this year, we are seeing improvement. Server demand improved and PowerEdge orders were up single digits sequentially. Large enterprise remain challenged, but we saw better velocity from our small business and medium business customers. Storage demand was mixed. We were pleased with our relative performance given current market dynamics. Bright spots included PowerMax and hyper converged infrastructure, each growing double digits in the third quarter on an orders basis.

PowerStore is gaining traction. We delivered nearly double the orders revenue achieved in the second quarter. Albeit on a small base, we are still early in the ramp. We’re pleased with the PowerStore -- we are pleased with PowerStore’s progress and are seeing early wins as customers transition from existing Unity, SC, VNX, Ecologic and XtremIO products. And more than 15% of the PowerStore customers are new storage buyers. We feel great about the future of PowerStore and our storage leadership.

Our VMware business segment had another strong quarter, delivering revenue of $2.9 billion, up 8%. The VMware partnership and teaming remains strong, and our cloud capabilities continue to build.

Year-to-date, performance has been amazingly consistent in the light of what has turned out to be an incredibly challenging macro environment. We have delivered $68.2 billion of revenue, flat year-on-year, as we executed against growth opportunities, and we delivered $7.5 billion of operating income and $8.9 billion of adjusted EBITDA.

In the first quarter, we saw a dramatic surge from large enterprise, health care and the financial sector for work from home and business continuity solutions. This drove strong growth in our commercial client and with our VMware solutions. Towards the end of that quarter, we started to see signs of a slowdown in small and medium businesses. Then in Q2, demand shifted to government, education and consumer as remote work continued and learn from home needs soared.

Similar to GDP, and given our third quarter results, our second quarter appears to be a trough for the year. In Q3, strength in government, education and consumer continued, and it was encouraging to see double-digit orders growth from our small and medium business customers, given the number of jobs this sector creates around the world.

And though some companies have moved to the public cloud for certain workloads or immediate business continuity needs, hybrid cloud momentum is building as the longer-term answer, a new operating model where workloads will be distributed between public and private clouds, traditional data centers and increasingly out to the edge. Like Australia’s largest retailer, Woolworths, where we recently announced a deal to enable their hybrid cloud strategy by bringing together their public and private clouds onto a single platform, utilizing as-a-service with Dell Technologies On Demand.
With our hybrid cloud capabilities, the depth and breadth of our portfolio, industry-leading global supply chain, go-to-market and services reach, we have a significant -- we have significant competitive advantages to be the partner of choice. Put this all together, and you get a track record of consistent execution, profitable growth, disciplined share gains, innovation and financial returns regardless of the environment.

Looking ahead, I see an extraordinary opportunity as technology continues to drive our society forward and Dell Technologies fulfills its role as the essential technology company for the data era. And with 5G, data-driven insights, automation and embedded intelligence, we will see an explosion of edge computing in smart cities and transportation, factories, hospitals and schools around the world.

We know how to get technology into the real world at scale, providing a consistent approach to infrastructure, data, applications and security across the entire environment from multiple clouds to the edge. What the last 9 months has shown is that Dell Technologies is resilient, ready to meet the needs of customers today and for what's to come.

According to IDC, the expected compound annual growth rate for IT, excluding telco, through 2024 is 4.7%. It's clear that digital future is bright. We're excited about the opportunities that lie ahead.

Now I'll turn it over to Tom to look at the financials.

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**Tom Sweet - Dell Technologies Inc. - Executive VP & CFO**

Thanks, Jeff. Overall, we have executed well this year, navigating through an uncertain macro environment. We've delivered stable and differentiated performance by leveraging our diversified IT platform and leaning into the current growth opportunities in a disciplined way. And we're driving value by expanding profitability faster than revenue and generating strong cash flow which has enabled significant debt paydown.

For the third quarter, revenue was better than expected and above our typical seasonality at $23.5 billion, up 3% both year-over-year and sequentially. FX this quarter did not have a meaningful impact on our financial results. Also, a reminder that we completed the sale of RSA in early September.

Gross margin was $7.8 billion or 33% of revenue. Gross margin dollars were flat, which I believe is a good result given the demand that we've seen from education, government and consumer customers typically tends to deliver less margin dollars. Operating expense was $5 billion, up slightly 1% sequentially and better than expected as we continue to benefit from the cost containment actions we instituted earlier this year. Operating income was up 12% to $2.7 billion or 11.6% of revenue driven primarily by our ongoing operating expense controls and strong profitability in CSG. Consolidated net income was $1.7 billion, up 18%, and EPS was $2.03 a share, up 16%. Adjusted EBITDA was $3.2 billion, up 13% at 13.7% of revenue. For the trailing 12 months, adjusted EBITDA was $12.1 billion. Total deferred revenue was $28.7 billion, up 11% year-over-year. Our recurring revenue, which includes deferred revenue amortization, utility and as-a-service models is now approximately $6 billion a quarter, up 13%.

As announced at Dell Technologies World, we will broaden our as-a-service solutions for our customers across our entire portfolio over the next year, giving them more flexibility to scale their IT to meet their business needs and budgets. We're seeing adoption of our portfolio delivered as a service through flexible consumption solutions and expect this to continue to grow over time.

Turning to the business units. Our Client Solutions Group results were above our expectations, driven by ongoing strong demand for work and learn from home solutions, along with gaming systems. CSG revenue was a record $12.3 billion, up 8% as we delivered record shipments in the quarter. Commercial revenue was up 5% to $8.8 billion as we saw strong growth in Latitude and Precision notebooks and commercial Chromebooks. Not
surprisingly, given the remote nature of this year’s working and learning environment, we continue to see reduced demand in commercial desktops.

Consumer revenue was $3.5 billion, up 14%, driven by strong growth across all of our consumer notebooks and gaming systems. Our premium consumer products, XPS and Alienware combined saw strong double-digit revenue growth for both notebooks and desktops. CSG operating income was also a record at $1 billion, up 36% and 8.2% of revenue. The strong profitability was driven by our record shipments, product mix and our operating expense discipline. This has been a great year for our Client Solutions business, and it’s clear that the PC is still the platform of choice. The revenue stability of this business has been beneficial and has consistently generated strong cash flow that has enabled us to weather different cycles and demand fluctuations. Over the past 5 fiscal years, CSG revenue has grown at a 3% CAGR, while the CAGR for operating income was nearly triple that rate.

ISG revenue was $8 billion, down 4%. Though disappointed in the decline, the overall server and storage market has been softer than we expected coming into this year. Given the dynamics in the macro environment, we executed against the growth opportunities within these markets while delivering solid profitability.

Storage revenue was $3.9 billion, down 7%. PowerMax and HCI, specifically VxRail, where highlights as both were up double digits based on orders. We continue to see softness in other areas of core storage, including mid-range. As Jeff described, PowerStore’s trending in the right direction, and we expect it to ramp through the rest of this year and into FY ‘22.

Servers and networking revenue was $4.2 billion, down 2%. Overall, server demand was softer than expected, but we did see improvement in orders with our mainstream servers growing sequentially. We also saw improved transactional demand for our mainstream servers as we move through the quarter. We continue to look for balanced growth, being disciplined and selectively leaning into opportunities that make economic sense. For instance, our high-value servers built for artificial intelligence and machine learning workloads had another quarter of positive growth, with orders up mid-single digits and is a growing piece of our server revenue mix.

ISG operating income was $882 million or 11% of revenue, which was down 90 basis points as higher component costs for servers and networking and product mix more than offset lower operating expense. The VMware business unit had another strong quarter, delivering revenue of $2.9 billion, up 8%, and operating income of $837 million or 28.9% of revenue. Based on VMware’s standalone results, subscription and software-as-a-service revenue grew 44%. The business saw better than expected growth in the VMware Cloud Provider Program, modern applications and VMware Cloud on AWS. VMware Cloud and AWS continued to show great traction in Q3, with triple-digit revenue growth.

Dell Financial Services growth continued in the third quarter with originations up 4% to $2.1 billion. DFS ended the quarter with $12.6 billion in total managed assets, up $1.9 billion year-on-year. DFS enables sales, drives profitable growth and retains customers through a number of traditional financing and innovative payment solutions, including consumption and as-a-service offerings.

Moving to our capital structure and balance sheet. Cash flow from operations was quite strong and above typical seasonality at approximately $3 billion, driven by improvement in net income and diligent working capital management. Adjusted free cash flow in Q3 was $2.7 billion, and on a trailing 12-month basis, adjusted free cash flow was $8.8 billion. We ended the quarter with $13 billion of cash and investments. Our liquidity position is strong, and we made excellent progress on deleveraging.

During the third quarter, we paid down approximately $4.6 billion of debt, including $3.1 billion of core debt and $1.5 billion of VMware debt. With the debt payments made in Q3, our total debt balance ended the quarter at $50.4 billion, and includes DFS-related debt of $10.1 billion and subsidiary debt of $4.8 billion. Our core debt ended the quarter at $31.4 billion. We are on track to reduce core debt by approximately $5.5 billion in FY ‘21 as we expect to pay down at least $2.4 billion in Q4.

With our continued debt paydown and strong profitability, our core leverage is now below 3x and at the top end of our target core leverage range of 2 to 3x. Recognizing leverage is only 1 metric used by the rating agencies,
based on our calculations, we believe this puts us inside the current investment-grade target range for S&P. We are pleased with the progress we've made against our delevering plan, and debt paydown will continue to be our capital allocation priority as we work toward investment-grade metrics.

Moving now to our outlook for the fourth quarter. Though the latest global GDP and industry data for infrastructure demand indicate gradual improvement into the next year, there continues to be a high degree of uncertainty as COVID-19 infections increased globally, and some geographies have implemented new restrictions. Given the macro backdrop and the trends that we've seen in our business, we expect Q4 revenue to be up 3% to 4% sequentially, which is slightly below typical seasonality of 5% to 6% sequentially. We expect strong CSG results with revenue expected to be slightly above normal seasonality of plus 2% to 3% sequentially. For ISG, we expect revenue to track slightly lower than last year's 4% sequential growth based on the continued softness in data center spending.

From an operating income standpoint, we expect CSG margins to remain strong and above historical averages but lower sequentially due to a higher mix of consumer PCs and commercial Chromebooks, along with holiday promotions. We are a bit more cautious on ISG margin dollars given the uncertainty in the macro, while VMware should benefit from typical seasonality in Q4. Taking all of this into account, we expect consolidated operating margin dollars to be slightly higher versus Q3.

Our breadth and diversity of portfolio has driven stability in our performance through the year, and we continue to adjust to opportunities we see in the business. Given the aforementioned risk, we believe it's still too early to talk about next year. That said, looking at the current global GDP and IDC forecast, we are cautiously optimistic about the potential for recovery post pandemic-related pressures. GDP expectations and IT spend, ex telco estimates from both IDC and Gartner, see 4% to 5% growth in 2021. We hope to have a better perspective on the global economy and our outlook after we close the current fiscal year.

In closing, we have a history of navigating through challenging environments, and this year has been a great example of our strong operating heritage. The steady execution in our core businesses and the ability to leverage our broad portfolio have enabled stability and generate a strong cash flow through these uncertain times. The teams are executing our strategy, and we're managing the business for long-term consistent growth. We're using our unique strengths to win in the consolidation of the markets in which we compete, running the business to outgrow the industry. And we're creating differentiated Dell Technologies solutions through innovation and integration across the entire family.

This year has also been a good example of maximizing value creation for all shareholders. We've outgrown our competitors, grown profitability faster than revenue and generated strong cash flow. We've made good progress on our delevering goal and are committed to getting back to investment grade. And we've taken the appropriate corporate structure steps as evidenced by the ongoing simplification of operations, the divestiture of RSA and the exploration of a potential tax-free spin of VMware. We're focused on what we can control and leaning into the areas of growth, which will continue to be the way we navigate through any environment or cycle.

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

Rob Williams - Dell Technologies Inc. - SVP of IR

Thanks, Tom. Let's get to Q&A. (Operator Instructions) Erica, can you introduce the first question?

**QUESTIONS AND ANSWERS**

**Operator**

Your first question is from Toni Sacconaghi with Bernstein.
I'm wondering if you can comment a little bit about the forces at work on margins in both your PC and your enterprise business. So specifically, how much is sort of cyclically lower OpEx spending, things like less travel, less promotion, helping both sides of the business? Secondly, what are you seeing on components? DRAM is essential to both, yet we're seeing record margins in PCs, and we're not really -- we're seeing kind of weak margins in enterprise. And then thirdly, what are you seeing in the pricing and competitive environment? Should we be reading into the weak margins and the sequential deterioration in margins in enterprise being a function of incremental price competition, given continued softness in the market?

Toni, it's Tom. Let me start, and then Jeff can jump in here as well. So look, as we think about sort of the margin dynamics, the operating margin dynamics across the various segments of the business, I'd characterize it like this. Obviously, the cost constraint actions that we did earlier in the year have been helpful from an operating margin perspective. I would remind everybody that those were put in at the time when there was significant uncertainty on the COVID impact. And obviously, we're still not through the navigation of that, but we will think our way to how do we think about the long-term sustainability or lack thereof of some of those OpEx actions as we get into next year.

But as we think about PCs, for instance, right? Clearly, component costs were inflationary for most of the year. The dynamic, though, Toni, has been that component -- some of the parts shorters and parts dynamics have, I would say, prevented a bit of -- or sort of encourage rational pricing in terms of the PC space. And so when some of the, for instance, screens are in short supply, you don't see extraordinarily aggressive pricing. It's still price competitive, but not as competitive.

And then on the enterprise mix, our enterprise side of the house, clearly, data center demand has been softer this year. And as a result of that, we have seen -- and we've talked about it in the past calls, pricing pressure, particularly on the large bid business, generally in the computer server space, storage is a little less sensitive to the pricing, just given the IP that's embedded in the solution capabilities. But net-net, it's -- those are the dynamics that we've been navigating our way through. And maybe, Jeff, you can jump in and add some color if you'd like?

Sure. Let me start with component pricing, Toni. It might be helpful. So we look at Q3. Q3 from our perspective was slightly inflationary, as Tom mentioned, driven by DRAM, NAND, and LCDs, offset by our structural commodity category. As we look in to Q4, it flips to be slightly deflationary driven by DRAM and NAND, offset by the shortages the industry is encountering around LCDs.

So I think that's the kind of component-driven cost environment. There are a couple of subcategories that are, I think, important for you to think about. One would be LCDs, and then particularly the components that go into the LCDs most notably T-Cons and drivers, ICs, those are in short supply, driving up the cost of LCDs. And then likely, there's going to be challenges in the freight network towards the very end of the year as airplanes get filled up with vaccines and we're all competing for a limited amount of space.

So that's how we look at the cost environment, Tom, and across pricing. If I went by specific product, notebook prices have generally firmed up around the industry. We have the demand/supply dynamic that Tom talked about. Desktop pricing is a little more competitive than normal, given that the demand for desktops has fallen considerably over the year. If I were to look at servers, servers, we still see the aggressiveness and the very big
deals. Although, as we mentioned in our prepared remarks, there is less of those, and we mentioned that in Q2 as well. But nothing out of the ordinary beyond that and the big deals and servers.

And the same is true in storage. We're not seeing anything out of the ordinary. Obviously, when we're doing competitive swap, those bids are fairly aggressive. Our discounting has been stable. We've not seen any major price move in the industry since July. So that's, in detail, how we look at the pricing environment that we're operating in today. I hope that was helpful.

Toni Sacconaghi - Bernstein & Co., LLC., Research Division - Senior Analyst

That was all helpful. If you could just comment on the cyclical OpEx reduction because of travel, et cetera. And does that become a headwind at some point?

Tom Sweet - Dell Technologies Inc. - Executive VP & CFO

Yes. Toni, it's Tom. Look, I mean, as I mentioned, we did do a number of cost containment actions. And as we think our way through next year, as we build the AOP for our operating plan for next year, obviously, there's a number of those cost containment actions that are not going to be sustainable long term. So we are going to have to work our way through how do we reset or rethink some of the OpEx framework, but that's no -- we're always having to do a bit of that. And so we'll have to work our way through the P&L framework for next year to make sure everything holds together the way we want it to, but we'll have to address it.

Jeff Clarke - Dell Technologies Inc. - Vice Chairman & COO

Yes. We recognized some of the costs moves we made this year are not sustainable as we head into next year's plan.

Operator

Your next question is from Wamsi Mohan with Bank of America.

Wamsi Mohan - BofA Merrill Lynch, Research Division – Director

Jeff or Tom, can you talk about the enterprise spend outlook? And Jeff, you opened the call talking about digital transformation and sort of this hybrid cloud transition. Over time, how that should help? Why is that not creating a better uplift in server revenues? If you could just talk about, is ISG potentially on a trajectory of growth as we look into the next fiscal year? And I have a quick follow-up.

Jeff Clarke - Dell Technologies Inc. - Vice Chairman & COO

Of course, Wamsi, I'll take a swing at and then Tom, I'm sure, will come over-the-top. And we step back and kind of look at this in the macro. FY '19 for us was an extraordinary enterprise year, specifically for servers. FY '20 was a year for digestion. And quite honestly, a year ago, when we were planning the business for FY '21, we thought there was a modest growth opportunity. Pandemic hits. We see companies respond to the pandemic by really pushing their budgets towards 3 specific areas: work from home, business continuity and strategic digital
transformation activities. Broad-based enterprise deployment or buys have been slowed, as we've mentioned over the previous calls, and we mentioned in our remarks.

So if I start there, that the pandemic has really changed the profile this year and really slowed down investments. And those budgets are under pressure, and those budgets are increasingly or have been increasingly been used over the year for things that certainly weren't contemplated, a work-from-home environment where large percentages of companies' workforces still remain at home, and that's where the investments have gone.

If you look at our business in our remarks, we talked about enterprise continues to be challenged. The very large businesses, the very large bids continues to be a challenged area for us. But we did see signs where our small and medium businesses did grow. We saw a sequential improvement in our server business, which we're encouraged by. We continue to keep the product line fresh. We keep the product line and price position.

And probably maybe to close on it before I turn it over to Tom. Look, we're optimistic about what IDC and the other industry pundits talk about for next year. So this year, we're weathering through a server marketplace that's down 6%, a storage marketplace that's down somewhere in the same ballpark, 7%, if I remember correctly. And we're looking into a calendar year '21, our fiscal '22 with servers being up nearly 4% and storage being up nearly 5%. We think the market response, companies can no longer defer their investments in infrastructure, and that's the rebound. I hope that helped. Tom?

Tom Sweet - Dell Technologies Inc. - Executive VP & CFO

Yes. Jeff, the only thing I would add is, obviously, part of our thinking around the ISG space is evidenced in our guidance that we just talked about and since we still expect Q4 to be relatively soft. And if you look at -- on a -- from an ISG perspective, if you look at storage, their forecast, IDC is forecasting storage at a minus 6% in Q4 and servers at a minus -- roughly a minus 4.5% mainstream servers, that is.

And so we do think that we've got to work our way through the remainder of the year. And then we are cautiously optimistic. Obviously, we'll have to see how the macro uncertainty plays out, but we do think that an investment cycle sets itself up next year given some of the indications we're seeing. And then, again, the IDC trends over the next 3 years or so are encouraging, but there's work to do clearly.

Wamsi Mohan - BofA Merrill Lynch, Research Division - Director

Jeff, if I could. In the prepared remarks, you guys noted the VMware spend could happen in September '21, if you came to an agreement. I know you're limited in what you can say around this, but any chance you can comment on the moving pieces that agreement hinges on in terms of perhaps debt levels or ownership structure or high voting share conversion? What are the pieces to think about that would make you either reach or not reach an agreement?

Rob Williams - Dell Technologies Inc. - SVP of IR

Wamsi, it's Rob. I appreciate the question. We're going to pass on that. We're just going to keep the comments specific to what I had in the lead-in. So well, if we have an update, we'll definitely let you know.

Operator

We'll take our next question from Amit Daryanani with Evercore.
Amit Daryanani - Evercore ISI Institutional Equities, Research Division – Senior MD

PI guess, Jeff, I was hoping you could talk a bit more on the storage side. I think it was down 7% this quarter, which is the largest decline we've seen in the last 2.5 years, I think. And that's despite PowerStore sounds like it's doing fairly well. So maybe just reconcile the storage declines versus the new product momentum? And then when I think about this 4% number that you talked about for infrastructure in [Jan.], how do you -- how does that stack up across storage and servers?

Jeff Clarke - Dell Technologies Inc. - Vice Chairman & COO

Sure. I think Tom and I will parse that, and I'll take the first part, talk about storage, what we're seeing and then maybe a few comments about PowerStore. And then Tom can link that to our guidance and look forward.

And clearly, we talked in our prepared remarks, and you'll see it in the web deck, our storage business was down 7% for the quarter. We were disappointed with that result. We talked about 2 areas where we have seen growth, in fact, strong double-digit growth with our PowerMax business and our VxRail business. And then we talked about its inability or -- it's implied its inability to offset what's happening in the midrange, which is why PowerStore is so important for us, getting our midrange trajectory on a take share trajectory, which, quite frankly, it's not with our performance. We're encouraged by the first 2 quarters of PowerStore. I think I mentioned in my remarks, it was up nearly twice the revenue in Q2 and Q3. 15% of the customers are new storage buyers to the company, and that makes us feel very good that we are on the right trajectory with PowerStore.

But remember, it's on a base of starting literally at 0 2 quarters ago. It has to build momentum. We expect it to continue to ramp in Q4 and all through next year, and that ramp is the key to our success in growing our storage business as we have strong success in the above $2,050 segments and have actually taken share there.

Tom Sweet - Dell Technologies Inc. - Executive VP & CFO

And then, Amit, why don't -- it's Tom. Why don't I just take a -- make a comment on your second part of that question, which I think was around the Q4 framework that we laid out, with the seasonality that we called out for ISG, which we said last year was 4%, and we expected it to be slightly lower than that on a sequential basis this year.

Look, I think the dynamics are pretty much what I just chatted about, which is we do continue to see softness in the data center space. Typically, Q4 is a larger storage quarter. And so we do expect some uplift in storage, although we are slightly cautious about how does data center spending play its way out through Q4. So it makes sense to us, given some of the dynamics that we're seeing that -- and by the way, that our Q3 results were for servers by -- we're sort of buoyed up by the federal mix in the government space. We won't have that in Q4. So we're just slightly cautious about what we see for Q4 ISG spend at this point.

Operator

We'll take our next question from Rod Hall with Goldman Sachs.
Yes. I wanted to start off, Tom, and go back to your comments on investment grade. You said that you're into that territory now. And I wonder if you could talk about what other pieces of data or evidence you think the rating agencies are waiting for to potentially make a change there? And also if you could give us any kind of idea on what the next chance for that timing-wise might look like? And then I have a follow-up.

Rod, it's Tom. And then I'll let Tyler jump in here as well as he's on the call. Look, the leverage ratio -- and we've made great progress on core leverage ratio. So as we highlighted, as I highlighted on the prepared remarks, we're down slightly below the 3x adjusted EBITDA sort of leverage ratio that we have been -- that we've talked about. Now the leverage ratio is only one element of what the rating agencies look at in terms of the totality of the credit, if you will. So they're obviously thoughtful about the macro environment, the pandemic. We've got some news out there around the potential VMware spend. So I'm assuming they're also trying to be -- trying to sift through what that looks like.

So we're holding regular conversations with them, and we continue to share our perspective, but we recognize that it's ultimately their call on when they might make that determination. And we'll continue to provide them our point of view, and we'll continue to stay focused on our capital allocation policy, which is centered around debt repayment at this point. Tyler, why don't you jump in and add some thoughts there, if you would, please?

Yes. I mean, look, I think you pretty much well covered it. I mean, look, we're happy with where we are. I mean if you go back and look at where we were really projecting when we were going to cross over, we were thinking it was going to be more at the end of the year, and that was really a pre-COVID projection. So I think the fact that we were able to do this in the face of COVID really speaks highly to the power of cash flow generation that the business throws off.

Look, I think the rating agencies and specifically S&P, which is the one that gives us credit for cash and the one that we mentioned in the talking points, they're going to want to see sustainability, so us staying under their targets for a reasonable period of time. And I think Tom called out, I mean, I think in the face of COVID, also the potential VMware transaction, that's something that's going to be top of their mind. So great progress. We'll keep doing what we're doing, and we'll go from there.

Okay. And then I wanted to -- on my follow-up, just ask Jeff about the PowerStore range and maybe some of the feature functionality there. Some of your competitors have called out things like clustering, storage efficiency technologies as lacking and needing development. But I know you guys rolled this thing out as -- in a containerized sort of solution so you can rapidly evolve it. I'm just wondering, do you think the ramp in that requires additional feature adds? Or do you think you've got everything you need and there's just more question and traction in the market and maybe COVID's slowing it down and so on?
Jeff Clarke - Dell Technologies Inc. - Vice Chairman & COO

Sure. Good question, Rod. Let me try to break that down. So if I think about what -- COVID is slowing it down, I think we last -- we talked last call about the things we're doing to ensure that the product is in front of our customers. We've clearly made a lot of progress in Q3 in doing that. We put a large number of seed units in front of our largest channel partners across the globe. They are 95% up and running in front of customers at all channel partners today. We put an active try-and-buy program in place. We have our team out delivering units to customers. We have an internal team that's out helping customers ramp their proof of concept, all with a desire to help drive assessment and the proof of concepts that go along with the new category and a new architecture that we put in the marketplace.

We've done, for example, 6,000 virtual demos and proof of concepts to help our customers through this. So we're very encouraged by that so much that it's ramping. You probably know our product line quite well, XtremIO, the groundbreaking all-flash architecture; VxRail, groundbreaking HCI architecture. PowerStore, at this point in time through its first 3 quarters, is ahead of both of their ramps.

So I don't know what competitors say. I know what customers say. Customers say we have a very competitive product. We have a product that is meeting their needs. It's revolutionary, and it is actually a modern storage product to the point that the number of competitive takeouts we had in Q3 over Q2 nearly doubled. So we like our momentum. We're impatient. We want it to be more. We want to grow faster, but we like what we've done.

When I look at architectural features, from my seat, it's the highest performance storage array in its price bands today in the mid range. It has the best data reduction in the marketplace today. It has features that are competitive today with more features coming. The fact that we can run an application on the array makes it a very differentiated architecture. And we're very pleased with its competitiveness from a feature performance and capability point of view, to the point that it's the first modern array in the marketplace.

So I like our hand. We just have to ramp it. Tom and I are impatient with the team. We want to see a more accelerated ramp. But again, its ramp today is faster than the 2 groundbreaking -- last 2 groundbreaking architectures in our company, XtremIO and VxRail. So the early signs remain good.

Operator

We'll take our next question from Katy Huberty with Morgan Stanley.

Katy Huberty - Morgan Stanley, Research Division - MD & Research Analyst

Can you just talk about the shape of demand recovery, if any, that you saw in the enterprise and the SMB market separately during the October quarter? And whether there were any material changes in these trends in the month of November as some of the countries rolled back their reopening plans.

Tom Sweet - Dell Technologies Inc. - Executive VP & CFO

Katy, it's Tom. So look, as we think about the ISG space, in particular in -- within the -- and within the SMB market, the small and medium business. We did see improved transactional velocity as we went through our quarter, started sort of soft and improved. I don't want to overstate it because it's still a bit of a tough slog but...
Jeff Clarke - Dell Technologies Inc. - Vice Chairman & COO

It's a smaller portion of the business.

Tom Sweet - Dell Technologies Inc. - Executive VP & CFO

Yes. And -- but it's a good indication of how we think about transactional velocity in the business. And in that case, what we saw was, I think, the demand velocity improving as we went through the quarter from something like a minus, say, mid-teens type of down to a much better performance as we got through month 3 of the quarter.

Now remember that -- I'm not going to comment on November, but -- which is our Q4, obviously. But we're encouraged by that, but we're also realistic as we think our way to how does ISG and infrastructure spending frame out in Q4. And our thinking is reflected in the results that -- or the guidance that we provided.

Jeff Clarke - Dell Technologies Inc. - Vice Chairman & COO

I think, Tom, it's spot on. Over the quarter, month-over-month, we saw improvement in the absolute demand profile, quite honestly, in both server and storage. The small and medium business comments you made are spot on. We saw more quote activity in that area. Conversion rates improved a little bit in that area. That's the trend, but again, we see budgets have tightened. They've been really redirected over the year to ensure the workforce is enabled to work from. That's certainly delayed or push bigger spend projects over the course of the year, and there's no reason to believe that doesn't continue into Q4.

Operator

We'll take our next question from Jim Suva with Citi Group Investment.

Jim Suva - Citigroup Inc., Research Division - MD & Research Analyst

My question is just on shares, like share losses or share gains. It sounds like your PC segment, you went through a shift to direct, and you lost some share. Are you now at a stabilization point or still some more to transition away? Then on the server side, was it -- not server, storage. On the storage side, was it missed execution? Was it not having the right product out at the right time? Was it COVID? You couldn't reach the end customer? It seems like on storage, you really are having some challenges there.

Jeff Clarke - Dell Technologies Inc. - Vice Chairman & COO

Well, I think there's certainly the devil's in the detail here. If you look at PC, we'll start there in Q3. We did lose absolute share. The market certainly shifted to consumer, and the consumer growth was extraordinary. Our consumer business, if I recall correctly, was up 14%, but that was certainly behind the marketplace. And I know I'm making a slight compare between the fiscal quarter and the calendar quarter, but you get the point.

You know, strategically, we have been working, particularly with the CPU shortages over the past 2-plus years, of prioritizing our business with commercial and premium consumer. And both of those businesses continue to respond well, but the commercial marketplace was soft in Q3. And consumer was significantly up in Q3, and our
share loss is largely on the consumer side. We did lose some share and timing in the commercial, but it's largely on the consumer side.

We made a strategic shift actually the end of last year of migrating to our heritage and advantage in the marketplace, which has been reinforced by the buying trends in the pandemic of our online direct business. That's serving us well. I think I made comments that our online business was up about 62%, and our consumer direct business was up 47%, if memory serves me right. That's encouraging.

We want to participate in the broad swath of the marketplace. For those who think we're only participating in the mid-range and above, we're not. I think I mentioned our Chromebooks doubled on a year-over-year basis. And we'll continue to participate and catch up to the marketplace. I think our fiscal results are very different than our calendar share results. Our fiscal results of being 8% revenue growth, I think, is pretty significant and different than our share results that ended in September. In other words, we had a very big October. We're encouraged though.

I look at the server side. The server side, we expect to take share. We think we've outperformed the market at a minus 2%. I think the market projection for Q3 in servers is minus 5%, 4%, something like that? If memory serves me right?

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**Tom Sweet - Dell Technologies Inc. - Executive VP & CFO**

It's minus 5.5%, Jeff (inaudible).

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**Jeff Clarke – Dell Technologies Inc. – Vice Chairman & COO**

Exactly. So we're in a share position there. And then on the storage side, it's not missed execution per se, Jim. We're taking share and consolidating in the high end. We continue to do that. Our PowerMax product continues to do well. We've taken share in the hyper-converged or software-defined space. It's back to the midrange. Our midrange is shrinking. I think we've mentioned that each of the previous 3 quarters this year, and it's why PowerStore is important. PowerStore is the catalyst. I think we've said this for the past couple of years in anticipation of the product, it is the catalyst for us to change our share trajectory in the midrange, which is the single largest segment in storage. That's why it's important. That's why doubling quarter-over-quarter is a good sign. That's why being ahead of our XtremIO and VxRail ramp is key. And again, we like our hand. We need to continue to ramp it, and we believe we can.

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**Operator**

We'll take our next question from Aaron Rakers with Wells Fargo.

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**Aaron Rakers - Wells Fargo Securities, LLC. - Research Division - MD of IT Hardware & Networking Equipment**

Yes. And I'll try and stick to this 1 question. It's on the storage business. And I guess my question is fairly simple in that we've seen the last couple of quarters, I think last quarter, you talked about triple-digit order growth in PowerStore. This quarter, it was double digits. So I'm just -- help us understand how we think about the growth of orders relative to when that kind of orders turns into revenue growth? I'm just trying to understand when maybe we could see that those businesses start to inflect? And appreciating that PowerStore is a big component of that.
Jeff Clarke - Dell Technologies Inc. - Vice Chairman & COO

Well, PowerStore would have been a small component in our (inaudible) last quarter.

Tom Sweet - Dell Technologies Inc. - Executive VP & CFO

Aaron, let me just -- from a materiality perspective, PowerStore is going to take a while to ramp to the point where it isn't going to move the needle on a business that's close to $4 billion on a revenue basis, right? So it will take a bit of time. That's why you heard me comment on the fact that we're optimistic about PowerStore, and we expect it to ramp Q4 on into next year. So when we referenced triple-digit or double-digit orders grow, obviously, it's starting from a base that's pretty small. And -- but clearly, we're optimistic, and we think as we work our way through the year, that you start to see that inflection point and particularly in the mid-range space. Jeff, I mean, I just wanted to set that comment.

Jeff Clarke - Dell Technologies Inc. - Vice Chairman & COO

No, I think you summed it up well. And then we continue to focus on our PowerMax performance and growth, in the high end, which we continue to be a consolidator in the high end, the most valuable portion of the storage marketplace. And we continue to see excellent performance there. But as I mentioned in the last question or the question before that, it's the midrange in changing that trajectory that's key to Tom's point. Our impatience, we want to continue to accelerate the ramp of PowerStore because it's the catalyst to change our share.

Operator

We'll take our final question from Shannon Cross with Cross Research.

Shannon Cross - Cross Research LLC - Co-Founder, Principal & Analyst

I was wondering if you could talk to, Jeff, about, from a macro standpoint, how you're thinking about the PC industry? And we heard from your competitor tonight, they're talking about 1 computer per person. I would assume at some point, we're going to start seeing lapping the initial Win10 computers that were put out there. So how are you kind of thinking about where this industry is going and the sustainability? Because it feels like we keep getting to the point where investors will say, "We're worried PCs are going to fall off a cliff in the next couple of quarters." And then obviously, the pandemic and everything seem to push that back. But I'm wondering [what] are you thinking?

Jeff Clarke - Dell Technologies Inc. - Vice Chairman & COO

Well, I suspect all of you who are working on a PC right now is taking notes. It is the essential device. It was pre-pandemic, and it's become even more of an essential device for productivity and for learning. And if you play that through, and you know our industry [of] about 1.7 billion units, give or take in the installed base, 700 million of those are 4 years or older, which is a refresh opportunity. The public sector, which has been a laggard in terms of its desktop and notebook mix has been 50-50, rapidly moving to 75% notebooks and up to the rest of the industry, which is a source of growth.

Education, the one-to-one initiative, the data I have would suggest there's still over 10 million children in the United States (inaudible) PC to turn on in this learn-from-home environment. There's 10 million in Japan. There's
over 40 million in Western Europe. There is a huge opportunity to get the necessary tools in our global students' hands so they can stay up and be educated along with everybody else. This notion of household rates going up, I think, is very real. I don't think you can get by having a PC for everyone in the home now. We have 2 parents likely working from home. You have multiple children working from home. That's a multi-PC environment in the home today, and I don't think that largely changes. As the industry moves towards the 75% or better in notebooks, you have a replacement cycle advantage. Notebooks are generally replaced about 1.5 years faster than desktops. So that will feed itself.

And you ultimately have, again, what I consider the essential device in the stay-at-home economy. And ultimately, we're bringing the world into the home through the PC.

Maybe that's a long-winded way of saying I'm bullish. I think if you look at the prospects from IDC and Gartner and look at low single-digit growth over the next 3-ish years, 4 years is realistic. Again, last quarter, I think the market was $82 million, give or take a few. That was the biggest quarter in 12 years. You've seen some of the forecasting for Q4. It's in the high teens. It will put the market roughly 300 million units in calendar '20. That will be the biggest year in 6 years. This thing is far from dead. It has become far more an essential device for all of us in this work-from-home, stay-from-home environment.

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**Shannon Cross - Cross Research LLC - Co-Founder, Principal & Analyst**

How material is gaming? And just quickly, how material do you see gaming being?

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**Jeff Clarke - Dell Technologies Inc. - Vice Chairman & COO**

Well, I think it's huge. Look at all the young people. That's what they do. I know I have one at home that is an active gamer. And I think, by the way, in the stay-in-home environment, entertainment is key, and gaming is a huge entertainment or outlet, and I think it is essential. And I think it's key. And certainly with our Alienware brand, the success we've had there, we're quite pleased and love to see more gaming. Got a few promos on the website today if you're interested in getting a great Alienware 17-inch notebook.

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**Rob Williams - Dell Technologies Inc. - SVP of IR**

All right. All right. Thanks, Jeff. Thanks, Shannon, and thanks, everyone, for joining us today. As a reminder, we'll be participating virtually in a couple of conferences next week. Tom will do a fireside chat on Tuesday at Wells Fargo, and Jeff will do a fireside chat on Thursday at Crédit Suisse -- or Suisse, sorry. Additionally, we will be attending several other virtual conferences in December and into January, so check the IR website for the latest updates. And finally, thank you for joining us today, and we wish everyone in the U.S. a safe and happy thanksgiving.

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**Operator**

This concludes today's conference call. We appreciate your participation. You may disconnect at this time.