**Dell Technologies Q4 FY'24 Earnings Call**

**Thursday, February 29th, 2024**

**Rob**

- Thanks everyone for joining us. With me today are Jeff Clarke, Yvonne McGill and Tyler Johnson.
- Our earnings materials are available on our IR website and I encourage you to review these materials and the presentation which includes additional content to complement our discussion this afternoon. Guidance will be covered on today's call.
- During this call, unless otherwise indicated, all references to financial measures refer to non-GAAP financial measures, including non-GAAP gross margin, operating expenses, operating income, net income, diluted earnings per share and adjusted free cash flow.
- A reconciliation of these measures to their most directly comparable GAAP measures can be found in our webdeck and our press release.
- Growth percentages refer to year-over-year change unless otherwise specified.
- Statements made during this call that relate to future results and events are forward-looking statements, based on current expectations.
- Actual results and events could differ materially from those projected due to a number of risks and uncertainties, which are discussed in our webdeck and our SEC filings. We assume no obligation to update our forward-looking statements.
- Now, I'll turn it over to Jeff.

**Jeff**

- Thanks Rob and thanks everyone for joining us.

**FY24 highlights**

- As I reflect back on this past year, it's increasingly clear that data and technology are central to everything our customers do, and Dell is well-positioned to thrive in this environment.
- Our FY24 revenue was $88.4 billion with operating income of $7.7 billion and EPS of $7.13.
- In a year where revenue declined, we maintained our focus on operational excellence delivering solid earnings per share and outstanding cash flow.
- FY 24 was one of those years that didn't go as planned, but I really like how we navigated it. We showed our grit and determination by quickly adapting to a dynamic market, focusing on what we can control, and extending our model into the high growth AI opportunity.
- Our operating margin rate improved as we delivered higher gross margins with disciplined operating expense management.
- We focused on cash and working capital improvements, generating $8.7 billion of cash flow from operations, and we improved our cash conversion cycle to negative 47 days exiting the year, a 15 day improvement.

- We delivered on our capital allocation commitments, and have returned $7 billion to shareholders since the initiation of our dividend.
- Earlier today, we announced an increase to our dividend which Yvonne will cover in more detail.
- We have positioned ourselves well in AI. We have already started to benefit from the momentum we're seeing.  We saw strong demand continue for our AI optimized server portfolio, including our flagship PowerEdge XE9680, which remains the fastest ramping solution in company history.
- We've just started to touch the AI opportunities ahead of us, including broader adoption of AI by enterprise customers and the projected growth in unstructured data where we are well positioned with industry leading storage solutions.
- We believe the long-term AI action is on-prem where customers can keep their data and intellectual property safe and secure.
- PCs will become even more essential as most day-to-day work with AI will be done on the PC. We remain excited about the long-term opportunity in our CSG business.
- Look for us to make a number of new product and solution announcements at Dell Technologies World in May that will help customers get started with AI and make it easy.

**Q4 highlights**

- Turning to Q4, we saw positive signs in the business as we exited the year, but enterprise and large customers remained cautious with their spend.

- Our Q4 execution was solid given the environment with ISG faring better than CSG.
- We delivered revenue of $22.3 billion with strong profitability and cash flow.
- Operating income was $2.1 billion, diluted EPS was $2.20, and cash flow from operations was $1.5 billion.

**ISG**

- In ISG, traditional server demand grew Y/Y, and a third consecutive quarter of sequential growth, and storage demand grew above normal seasonality though down Y/Y as expected. Storage recovery typically lags servers by a couple of quarters.
- Our strong momentum in the AI build out continues as we believe Dell is uniquely positioned with our broad portfolio to help customers build genAI solutions that meet their performance, cost and security requirements.
- In Q4, we saw strength across a wider range of customers and geographies with an expanding pipeline.
- AI optimized server orders increased by nearly 40% sequentially.
- We shipped $800 million of AI optimized servers, and our backlog nearly doubled sequentially, exiting the fiscal year at $2.9 billion.
- Demand continues to outpace GPU supply, though we are seeing H100 lead times improving.
- We are also seeing strong interest and orders for AI optimized servers equipped with the next generation of AI GPUs, including the H200 and MI300X.

- Most customers are still in the early stages of their AI journey, and they are very interested in what we are doing at Dell. We are helping them get started and work through their use cases, data preparation, training and infrastructure requirements.
- They appreciate our perspective, our collaborative approach, and the capabilities we can provide to help them create holistic AI solutions including our end-to-end portfolio, engagement with our engineering teams, consulting services and financing options.
- Progress in this space won't always be linear but we are excited about the opportunity ahead.

**<u>CSG</u>**

- In CSG, we remain optimistic about the coming PC refresh cycle as the PC install base continues to age, Windows 10 reaches end-of-life later next year, and the industry makes advances in AI-enabled architectures and software applications.
- In Q4, we maintained pricing discipline and managed our costs well in an increasingly competitive environment, delivering solid operating margins.
- In the near-term, the PC market is still soft and we expect recovery to push into the second half as enterprise and large customers remain cautious with their spend.
- We will continue to execute our CSG strategy which has served us well across various economic cycles, focusing on commercial and high-end consumer with a strong attach motion.

**<u>FY25 Optimism</u>**

- As we enter FY25, our strategy remains simple - we are leveraging our strengths to extend our leadership positions, and turning new opportunities into incremental growth.
- We are well positioned with our unique operating model and a number of tailwinds.
- We are driving a disproportionate level of AI server growth, fueled by our technology leadership, engineering expertise, services capabilities, and our traditional server business is gaining momentum.
- Our storage business will benefit from the exponential growth expected in unstructured data.
- And we are bullish on the coming PC refresh cycle where we are well-positioned.
- We are optimistic about FY25 and expect a return to growth above our long-term framework.
- Now over to Yvonne for more details about Q4.

**Yvonne**

- Thanks Jeff.
- In Q4, we delivered revenue of $22.3 billion, down 11%, with strong gross margins and lower operating expense.
- Gross margin was $5.5 billion and 24.5% of revenue, up 70 basis points with a mix shift to ISG.

- We saw increased pricing pressure in Q4 in PCs and servers, but remained focused on profitable opportunities, and we will continue to maintain that discipline and focus going forward.
- Operating expense was almost half a billion dollars lower than this time last year at $3.3 billion or 14.9% of revenue, down 12% as we actively manage our overall spend.
- Operating income was 9.6% of revenue and $2.1 billion, down 1%, with lower operating expense and an increase in our gross margin rate largely offsetting the revenue decline.
- Q4 net income was $1.6 billion, up 22% driven by a lower tax rate and lower I&O.
- Diluted EPS was $2.20, up 22%.

**ISG**

- ISG revenue was $9.3 billion, down 6% and up 10% sequentially.
- Servers and networking revenue was $4.9 billion, down 2% Y/Y and up 4% sequentially. Server order growth was strong with the majority of our AI optimized server orders going into backlog.
- Our AI mix of server demand increased again sequentially given strong customer interest in genAI.
- We delivered storage revenue of $4.5 billion, down 10% Y/Y and up 16% sequentially with better profitability as we increased our mix of proprietary storage software. Demand improved sequentially across the storage portfolio, above our normal seasonality.

- ISG operating income was 15.3% of revenue and $1.4 billion, down 7% driven by a decline in revenue and a lower gross margin rate given the higher AI optimized server mix, partially offset by lower operating expense.

**CSG**

- Our Q4 CSG revenue was $11.7 billion, down 12%, largely driven by a decline in units.
- Commercial and Consumer revenue were $9.6 billion and $2.2 billion respectively.
- CSG operating income was $0.7 billion, or 6.2% of revenue. Op Inc was up 8% driven by lower operating expense and higher gross margin rates partially offset by a decline in revenue.
- Earlier this week we announced that Dell will have the broadest portfolio of commercial AI PCs in the industry and new XPS systems, which feature built-in AI acceleration with an addition of the neural processing unit, or NPU, helping to improve performance, productivity and collaboration.
- While PC demand recovery has pushed out, we remain bullish on the coming PC refresh cycle and the longer-term impact of AI on the PC market.

**DFS**

- Our Dell Financial Services originations were $8.4 billion for the year and $2.5 billion in Q4, down 19% driven by the sale of our consumer revolving portfolio and lower VMware resell. DFS managed assets ended the year at $14.4 billion while the overall DFS portfolio quality remains strong with credit losses near historically low levels.

**Cash flow and B/S**

- Turning to cash flow and balance sheet.
- Our Q4 cash flow from operations was $1.5 billion, primarily driven by profitability.
- We ended the quarter with $9 billion in cash and investments, down $0.9 billion sequentially, driven by capital returns of $1.1 billion and debt paydown partially offset by free cash flow generation, and we reached our core leverage target of 1.5x exiting the year.
- During the quarter, we repurchased 11.2 million shares of stock at an average price of $74.67 and paid a 37 cent per share quarterly dividend, and earlier today we announced a 20% increase in our annual dividend to $1.78 per share, well above our long-term financial framework and a testament to our confidence in the business and our ability to generate strong cash flow.

**Guidance**

- Turning to guidance.
- There are several trends that give us confidence in our view of FY25.
- First the momentum around AI, second the improvement we're seeing in traditional servers and third, the aging PC installed base that is due for a refresh.
- The macro environment, however, is leading customers to be more thoughtful about their infrastructure budgets, particularly in the first half.

- Against that backdrop, we expect Dell Technologies FY25 revenue to be in the range of $91 and $95 billion with a midpoint of $93 billion and 5% growth, above our long-term value creation framework.
- We expect ISG to grow in the mid-teens fueled by AI, with a return to growth in traditional servers and storage, and our CSG business to grow in the low single digits for the year.
- We expect the combination of ISG and CSG to grow 8% at the midpoint, offset by a decline in other businesses.
- Given the higher mix of AI optimized servers, inflationary input costs and the current competitive environment, we do expect our gross margin rate to decline roughly 100 basis points.
- We'll maintain our cost discipline and expect opex to be roughly flat.
- We expect I&O of roughly $1.4 billion.
- Diluted non-GAAP EPS is expected to be $7.50 plus or minus 25 cents, up 5% at the midpoint assuming an annual non-GAAP tax rate of 18%.
- For Q1 of fiscal 25, we expect Dell Technologies revenue to be in the range of $21 and $22 billion with a midpoint of $21.5 billion, up 3%.
- We expect the combination of ISG and CSG to grow 5% at the midpoint, with ISG up in the mid to high teens.

- Gross margin rate will be lower sequentially given seasonally lower storage mix and a higher AI optimized server mix. Opex will be up slightly with typical seasonality.
- Q1 diluted share count should be between 723 and 727 million shares.
- Diluted non-GAAP EPS is expected to be $1.15, plus or minus $0.10.

**Close**

- In closing, we are optimistic and expect a return to growth in FY25 and beyond with a number of tailwinds.
- We have strong conviction in the growth of our TAM over the long-term, and we are committed to delivering against our long-term financial framework with average annual revenue growth of 3% to 4%, diluted EPS growth of at least 8% and a net income to adjusted free cash flow conversion of 100% or better over time.
- We are also committed to returning 80% or more of our adjusted free cash flow to shareholders over the long-term.
- We're excited about the future and confident in our ability to create meaningful long-term value for all our key stakeholders.
- Now I'll turn it back to Rob to begin Q&A.