TRANSCRIPT

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PRESENTATION

Operator

Good afternoon, and welcome to the Fiscal Year 2022 Second Quarter Results Conference Call for Dell Technologies Inc. I'd like to inform all participants that 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. Mr. Williams, you may begin.

Robert L. Williams - Dell Technologies Inc. - SVP of IR

Thanks, Jermiria, and thanks, everyone, for joining us. With me today are Jeff Clarke, Chuck Whitten, Tom Sweet and 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. Also note that all growth percentages refer to year-over-year change unless otherwise specified.

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 could 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.

Now I'll turn it over to Jeff.

Jeffrey W. Clarke - Dell Technologies Inc. - Co-COO & Vice Chairman

Thanks, Rob. Hi, everyone. Thanks for joining us today. We made it through the first half of the year, and in this incredibly unpredictable environment, we delivered our best second quarter ever. That's because whether we are reopening or reclosing, eating in restaurants or ordering out, returning to the office or staying at home, the one constant has been an unprecedented demand for technology. Another constant is our ability to execute against our stated strategy and deliver consistent performance no matter the market dynamics.

In the last week of June, we released an investor presentation where we outlined our differentiated strategy to drive growth and value creation post the spin-off of VMware. As we've engaged with investors, there are a number of key points I want to reiterate today from that presentation. These can also be found on Slide 4 of today's earnings web deck.

First, we have leadership positions in large, stable and expanding markets with strong underlying fundamentals. Q2 was an exceptional example of how we've leveraged our leadership positions to seize the opportunities in these growing markets. In Q2, we set a second quarter record with revenue up 15% to $26.1 billion and record second quarter EPS of $2.24, up 17%. We have talked previously about our ability to quickly pivot the business where the demand is strongest, and that was evident in these results. The need for better technology connectivity and productivity in the new do-anything-from-anywhere economy has driven strong IT spending across multiple industries and customer sizes, from large enterprises to medium businesses to small business and consumers. And we're leaning in to capture our share of the strong IT spending.

Our Client Solutions Group delivered record revenue of $14.3 billion, up 27% as we leaned into commercial, along with solutions in the broader client ecosystem, including software and peripherals, where we are #1 in displays. And we believe we gained more than 100 basis points of share in calendar Q2. There are positive secular trends at play in client, especially in the areas we are most focused, notably the commercial market, premium price bands and gaming, that should enable stable growth over the next few years.

The Infrastructure Solutions Group continued growth with revenue up 3% to $8.4 billion, primarily driven by growth in servers and networking as customers modernize their IT infrastructure to enable data-driven AI and machine learning technologies. We are also encouraged by the strengthening of storage during the quarter and the overall demand for hyperconverged infrastructure and midrange storage. Tom will dive into more of the financial details of Q2 in just a moment.

The second point is that we have durable competitive advantages that uniquely position us to win in our core and adjacent markets. A few I would call out that drove our Q2 performance. We have built an end-to-end innovation engine that delivers engineered solutions and software enhancements based on our unparalleled market reach and ability to see across a customer's full set of IT needs. These include management and orchestration, embedded intelligence, automation, predictive analytics, proactive support, telemetry and intrinsic security.

A key example is PowerStore, our micro-services-based midrange storage solution, which is ramping faster than any new architecture we've released with double-digit increases in net new storage buyers for both Q1 and Q2. We are utilizing our industry-leading scale and differentiated supply chain to successfully navigate through the operational challenges caused by the unprecedented demand that is way ahead of supply right now. Despite industry supply shortages, we shipped a record number of PCs and displays in the second quarter.

The third point is that we're driving a differentiated strategy to seize the tremendous growth potential ahead. We are focused on winning the consolidation and modernizing our core businesses by driving ongoing share gains and improving margins through scale, engineering, innovation and product mix shift. We are the clear #1 in external storage, #1 in hyperconverged infrastructure, #1 in mainstream servers, #1 in data protection appliances, and our Client Solutions business is #1 in revenue.

We have demonstrated the ability to adapt to the market dynamics over time as evidenced by our commercial client share gains in 30 of the last 34 quarters, and we have gained more than 700 basis points of share over that period. Additionally, we have gained more than 700 basis points of share for mainstream servers and approximately 200 basis points of share for external storage over the last 5 years as of calendar Q1 2021 according to IDC data.

We are focused on the midrange segment of storage and are pleased with the momentum we are seeing, but we know we still have work to do. When server and storage calendar Q2 share data is released in September, we expect share gains in both markets. We are also prioritizing customer outcomes and modernizing our business model with APEX, which provides an incremental growth opportunity as we introduce more as-a-service solutions and gain traction with current offers.

For example, in July, we announced GE is using APEX data center utility to blend automation and software architecture to support its increasing workloads from traditional IT applications to data analytics. With APEX, GE can scale up or down its data center, storage and compute resources on demand as the company executes an approach that adapts to each business unit strategy. We are innovating, integrating and partnering to create the technology ecosystem of the future for our customers with our unique partnership with VMware as the centerpiece.

We continue to drive new product innovation and business opportunities with VMware. For instance, in Q2, we launched new VxRail systems with the latest PowerEdge servers and new software advancements that deliver faster performance as well as simplified deployment and management. Additionally, we introduced VxRail dynamic nodes that expand how customers can use existing Dell Technology storage resources to support new multi-cloud workloads. VxRail continues to be an area of growth and one of the fastest-growing segments in storage with orders up 34% in Q2.

We're also pursuing adjacent high-value growth opportunities where we are uniquely positioned to win, areas like multi-cloud, edge, telecom, data management that open up adjacent multibillion dollar markets. We are investing in these opportunities and expect meaningful contribution from them in years to come. And we're already seeing powerful customer use cases today.

For example, our disruptive bet in telecommunications has led to multiple flagship wins to build open radio access networks, or Open RAN. We are working with Vodafone to build Europe's first commercial Open RAN, bringing more broadband access to European businesses and communities; with Orange to launch Europe's first 5G stand-alone, fully end-to-end cloud network; and with Deutsche Telekom, whose multi-vendor Open RAN network in Neubrandenburg, Germany is now live. These are just a few examples, and we are excited about the progress we are making in this space.

With these leading market positions, durable competitive advantages and a differentiated strategy, I believe we can drive consistent growth and significant value creation. I'm really excited about the opportunities ahead, and I look forward to talking in more detail at our Virtual Securities Analyst Meeting on September 23.

Before we go to Tom and our financial performance, let me introduce Chuck Whitten. As most of you are aware, in June, we announced Chuck was joining me as Co-Chief Operating Officer. He and I have worked together for many years alongside of the rest of the leadership team to help shape Dell's strategy and growth initiatives. Welcome, Chuck.

Chuck Whitten - Dell Technologies Inc. - Co-COO

Thanks, Jeff, and hello, everyone. I'm thrilled to join the Dell Technologies leadership team and look forward to regularly engaging with investors. As Jeff said, I've worked for more than a decade with Michael, Jeff and the rest of Dell leadership on the company's strategy and positioning.

The company has tremendous opportunity ahead, and we're focused on executing the strategy laid out in the June investor presentation. And we have never been more optimistic about our ability to innovate, delight customers, deliver growth and create value for all shareholders in the coming years. We operate in large, growing markets with ample headroom. The markets we target total $1.3 trillion today with core markets growing in the low single digits and adjacent markets growing faster through 2024 as widespread digital transformation drives sustained technology investment.

But beyond sheer size, those markets are evolving in ways that play to our market positions and the durable competitive advantages Jeff mentioned. As technology becomes ever more essential, more distributed, more hybrid and more multi-cloud, customers need a scale, trusted and global partner who can help them simplify and create business value, from the PC to the core data center to the cloud to the edge.

In short, this company was built for this moment in technology, and there is substantial growth opportunity in both our core markets and in high-value adjacent markets where our competitive advantages matter. And the spin-off of VMware will unlock the opportunity for us to pursue a balanced capital allocation strategy and invest in sustained profitable growth for years to come.

Our strategy is good for customers, employees and shareholders, and our first half results are proof. It's clear to us that our strategy will drive sustained value creation post spin-off, and that's what we're focused on executing every day as a team.

I look forward to speaking with you in more detail at the analyst meeting. Let me now turn the call over to Tom.

Thomas W. Sweet - Dell Technologies Inc. - Executive VP & CFO

Thanks, Chuck, and glad you're with us. I am pleased with our performance and the execution of our strategy as we delivered another quarter of consistent growth for revenue and profitability. Over the last 4 fiscal years, we've grown operating income faster than or equal to revenue every year. Secular trends such as work and learn from anywhere, digitalization of businesses and governments and real-time decision-making with edge data leads us to be optimistic on our long-term growth prospects.

Revenue for the second quarter was a Q2 record at $26.1 billion, up 15%, driven by growth in all 3 business units, led by outstanding performance in CSG and growth in ISG. Demand was ahead of revenue growth as we manage supply constraints, which should not come as a surprise to anyone.

Gross margin was $8.3 billion, up 9% at 31.9% of revenue. Gross margin as a percentage of revenue was 160 basis points lower, primarily due to a 540 basis point revenue mix shift to CSG. We are navigating the inflationary cost environment and have adjusted prices for the higher input cost while being mindful of our competitive positioning.

Operating expense was $5.5 billion, up 10%, as we invest for long-term growth, and we have certain costs come back from the depressed levels we saw last year. Given our strong performance, our variable costs, such as sales compensation and bonus, are running ahead of prior year levels. We have been disciplined in our decisions and will continue to be prudently managing our expenses going forward.

Operating income was also a second quarter record at $2.8 billion, up 7% and 10.8% of revenue. Our interest expense was down approximately $134 million given the progress on debt reduction, contributing to the expansion of our consolidated net income to $1.9 billion and earnings per share of $2.24, up 17%.

Adjusted EBITDA was $3.3 billion, up 7% at 12.7% of revenue. For the trailing 12 months, adjusted EBITDA was $13.6 billion, up 16%. Our recurring revenue is approximately $6 billion a quarter, up 14%.

Our remaining performance obligations, or RPO, is approximately $46 billion, up 24% and includes deferred revenue plus committed contract value not included in deferred revenue. The growth was driven by an expanded backlog given that demand is ahead of supply in addition to solid performance in hardware and software maintenance. Excluding VMware, Dell's RPO is approximately $35 billion, up 30%.

Turning to the business units. We had another quarter of very strong performance by our Client Solutions Group despite industry-wide supply chain challenges. CSG revenue hit a new record at $14.3 billion, up 27%, on the strength and demand for devices and solutions that offer improved connectivity and productivity. We continue to see strength across notebooks, but we also saw strong double-digit growth in commercial and desktop orders. As Jeff mentioned, we leaned into commercial where more than 70% of our CSG revenue comes from, and commercial also contributed to our return to share gains per IDC's calendar Q2 results.

Commercial revenue was up 32% to a record $10.6 billion as businesses look to upgrade devices and productivity solutions for their long-term in-office, remote and hybrid workforce environments. Consumer revenue was a second quarter record at $3.7 billion, up 17% as digital entertainment and e-commerce are still driving strong demand for upgraded experiences.

CSG operating income was $995 million, up 39% and was 7% of revenue. We saw solid profitability primarily due to strong shipments, a mix shift to commercial and a balanced pricing environment.

Moving to ISG, where revenue was up 3% to $8.4 billion. We saw a strong demand environment for compute and positive momentum in storage. Customers across all regions are investing in IT infrastructure focused on multi-cloud solutions and accelerating digital transformation. Servers and networking reported its third consecutive quarter of positive growth, with revenue of $4.5 billion, up 6%, with strong demand across all customer segments and geographies.

Storage revenue was $4 billion, down 1%. On an orders basis, we were encouraged to see positive overall storage growth of 2%, with ongoing demand in high-growth areas like hyperconverged infrastructure, where VxRail's orders were up 34%, and in midrange storage, where orders were up 17%. PowerStore continues to ramp nicely, making up approximately 38% of our midrange storage portfolio. 23% of PowerStore customers in Q2 were net new to Dell storage.

ISG operating income was flat at $970 million and was 11.5% of revenue. The VMware business unit revenue was $3.1 billion, up 8%, and operating income was $849 million or 27% of revenue.

Dell Financial Services originations were $1.9 billion, down 27%, due to the tougher comparison last year as more customers leveraged financing during the early stages of the pandemic. DFS ended the quarter with $12.6 billion in total managed assets, flat year-over-year with global portfolio losses at historic lows.

Turning to our capital structure and balance sheet. We generated strong cash flow in Q2 and are making good progress on delevering. Cash flow from operations was $1.7 billion. Although cash flow was slightly lower sequentially, impacted partly by working capital dynamics, our cash flow from operations was $4 billion through the first half of the year, which was up 56% compared to the same period last year. On a trailing 12-month basis, cash flow from operations was $12.8 billion, and excluding VMware, it was $8.4 billion. Over the last 3 years, on a trailing 12-month basis, cash flow from operations grew at a 15% CAGR. Cash and investments ended the quarter at $13.6 billion and approximately $7.5 billion for Dell, excluding VMware.

During the second quarter, we paid down $3 billion of the $4 billion margin loan that was outstanding as of the beginning of the quarter, and we paid down the remaining $1 billion earlier this week. We have now paid down approximately $5.5 billion of debt year-to-date and expect to pay down at least $16 billion for the full fiscal year. Our core debt ended the quarter at $27.6 billion, and our core leverage ratio was approximately 2.2x versus our long-term core leverage target of 1.5x.

We expect to achieve an investment-grade corporate family rating once the VMware spin is finalized. Once we get to IG, there will be opportunity for a more balanced capital allocation policy, including shareholder capital return, investments to grow the business and value-enhancing M&A. We will provide more details on our post-spin capital allocation policy at our Analyst Meeting next month.

Now to our outlook. From a macro point of view, the global economic recovery is driving broad demand across multiple sectors, including IT. As a result, demand for integrated circuits and components that are fundamental building blocks of today's modern IT, automotive, industrial solutions and home appliances are in tight supply. One of our durable advantages is our industry-leading scale and supply chain expertise. This is serving us well in this environment, and we are actively managing demand that is ahead of the industry's ability to deliver ICs and components.

For Q3, we now expect an above-normal sequential revenue growth pattern and year-over-year growth up mid- to high teens. For CSG, we expect high single-digit growth sequentially. For ISG, we expect low single-digit growth sequentially. And for VMware, you should factor in their stand-alone revenue guidance, which is roughly flat sequentially. Given this, we expect Q3 revenue overall to be up mid-single digits sequentially versus a normal 2% decline.

For Q3 operating income, we expect a mix shift to CSG sequentially, ongoing component cost dynamics, a modest increase in OpEx as we invest for growth, and we are considering the impact of VMware stand-alone guidance. With all of these factors, in our view, operating income dollars will be up 1% to 2% sequentially. Below the operating income line, we will continue to benefit from lower interest expense as we reduce our debt. But do keep in mind, the majority of our $16 billion plus in targeted debt paydown will occur at the time of the VMware transaction, which we now estimate to be -- to close in early November.

For non-GAAP tax rate, you should assume 17% plus or minus 100 basis points. In the absence of share repurchase activity, diluted share count should also increase slightly sequentially.

In closing, we have a track record of consistent execution across any economic or IT spending cycle given our durable competitive advantages, and we are investing in innovation and software development to differentiate our solutions and appliances. We are optimistic about the long-term growth prospects for our businesses. I'm confident in our ability to deliver consistent and predictable financial performance.

From fiscal year '18 through fiscal year '21, we grew revenue at a 6% CAGR and grew adjusted EBITDA at a 12% CAGR, and we generated nearly $28 billion in operating cash flow. We are well positioned and have the right strategy to create long-term value for our stakeholders. We look forward to sharing more about our plans for core Dell with all of you on September 23.

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

Robert L. Williams - Dell Technologies Inc. - SVP of IR

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

QUESTIONS AND ANSWERS

Operator

We'll take our first question from Krish Sankar with Cowen and Company.

Krish Sankar - Cowen and Company, LLC, Research Division - MD & Senior Research Analyst

Jeff, I had a question on the PC side. It looks like your U.S. competitor had some operational misstep last quarter, and based on your above-seasonal October guidance for CSG, are you gaining market share in this environment? Or are component constraints limiting it? And also in regards to the industry shortages, can you share where exactly you're seeing those constraints? Is this like power management ICs and display drivers or any other components? Any color there would be helpful.

Jeffrey W. Clarke - Dell Technologies Inc. - Co-COO & Vice Chairman

Sure, Krish. I mean first to answer your question about share. In the most recent IDC-published share data, Dell was the top share gainer of the top 5 manufacturers in the marketplace. We took share in total PCs. We took share in commercial PCs, our focus. We took more share than any of our other competitors in those spaces. So to answer your question, yes, we're taking share. We took 120 basis points of share, for example, in the commercial PC market in calendar Q2.

Your specific question of where are the shortages in the industry, as we've, I think, mentioned through several of these calls now, it's semiconductors. The industry demand, and industry being IT, consumer electronics, automotive, industrials, for electronics, for semiconductor continues to be strong. That is the area that is challenged certainly for us. We continue to work through it. I think we are working through it reasonably well.

The execution of our supply chain team is, I think, quite impressive with record shipments for the quarter for PCs, record shipments for displays. But the types of devices would be scalers, TCONs, microcontrollers, power ICs, driver ICs. Those types of devices are the ones that we see consistently challenged at different times. I hope that helped.

Operator

Our next question is from Rod Hall with Goldman Sachs.

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

I guess I wanted to ask something on PCs as well. Your U.S. competitor has just signaled that they're reducing their promotional and marketing spend assumptions substantially, and that had a big impact on margins in the quarter. And we're assuming it will have a large impact on their PC margins looking forward. I'm just curious if you guys are seeing that kind of promotional and marketing spend reduction in the market today and what you're thinking in terms of your own expenditures in that respect in the back end of the year given the demand dynamics against the supply dynamics.

Jeffrey W. Clarke - Dell Technologies Inc. - Co-COO & Vice Chairman

We have not lowered our marketing or compensation for whether it's our direct sellers or our channel partners. We've seen the demand of the market continue to pick up. It's been pivoting or moving towards commercial, which generally has a lower marketing cost in it as well, but the selling costs are fairly consistent. And we don't have any planned changes.

We like where our business is. We think we are executing at a very high level. We saw a tremendous rebound in our premium products, whether that be our workstation products, our commercial desktop products. We continue to see strong demand for our commercial notebook products. Rod, I don't know any other way to say this other than demand was strong through the quarter. I think you probably saw that in our backlog growth that Tom alluded to before, and business is good.

Thomas W. Sweet - Dell Technologies Inc. - Executive VP & CFO

Rod, I would also add that I think Jeff and I have a lot of scar tissue over the years where one of the things that we believe is that you have to have a consistent presence in the market in terms of driving demand and driving your message. And when you pull back, you tend to see the impacts of that 1 to 2 quarters out.

So we like where we are. We like what we're doing. We're being disciplined in our spend. But we also want to make sure that we are positioned thoughtfully in the market relative to the demand signals that we're seeing.

Operator

Our next question is from Amit Daryanani with Evercore.

Amit Jawaharlaz Daryanani - Evercore ISI Institutional Equities, Research Division - Senior MD & Fundamental Research Analyst

I guess my question is on the storage side. And Jeff, I'd love to get your perspective here because overall sales on storage, I think, down 1%, compares were fairly easy. And I think a couple of your peers in that space actually had double-digit growth yesterday. So I'd love to understand, how do you think storage performed versus your own internal expectations this quarter? And then what do you think is fundamentally needed for Dell to start gaining share on the storage side over the next few quarters?

Jeffrey W. Clarke - Dell Technologies Inc. - Co-COO & Vice Chairman

Sure. Thanks for the question. Maybe sometimes I think we don't do a good job of describing our storage business. And let me start with, first, we have the broadest portfolio in the marketplace. Second to none. We're the leader in high-end storage, midrange storage, entry-level storage, unstructured storage, object storage, all-flash as well as modern storage, software-defined, HCI, the hyperconverged space. Our share position in calendar Q1 was 32.3%, which is larger than #2, 3, 4 and 5 combined.

Our business -- and Tom and I, I think, referenced it in our prepared comments. Our business grew in the midrange. Our business grew in HCI, and we believe we grew in unstructured as fast or faster than any of our competitors in those spaces. In the midrange, which is defined as the $25,000 to $255,000 price bands, which is about 60% of the marketplace, we grew 17%. That's very competitive against the numbers that you mentioned from yesterday against our pure-play competitors in the midrange market space. In Q1 -- or I should say, and this marks the third consecutive quarter with that 17% that we've grown in the midrange. So for the last 3 quarters, we grew 8% in Q4, 23% in Q1, 17% in Q2. Our midrange business is growing. Our midrange business is taking share.

We've recently added the PowerStore 500, which allows us to cover the entry-level price band. So we now cover all price bands in the midrange marketplace. We also added new performance upgrades to our product in a seamless upgrade that happened earlier this year. Our storage buyer base grew double digits, as we mentioned in our prepared comments. PowerStore remains the fastest-growing new storage product in the history of the company through its first 5 quarters. 23% of our PowerStore buyers are new to our storage business, and 20% of them are repeat buyers. So we think we are executing at a very high level degree of performance or execution in our midrange.

That said, you called out one of our challenges that our orders growth was 2%. Our P&L growth was negative 1%. And we have a very large high-end business. That large high-end business is cyclical in nature. It was down year-over-year, and that's down year-over-year after a very solid first half of last year.

So we like our hand. We like our execution today. We do have this broad portfolio that is subjected to the cyclical nature of some segments. But in the high-growth space of HCI, our VxRail product grew 34% and midrange at 17%. We are growing very competitively against our pure-play competitors there. And we like the momentum. As I've said, as a trained engineer 3 data points makes a trend. We now have a trend of 3 growth data points in midrange storage.

Thomas W. Sweet - Dell Technologies Inc. - Executive VP & CFO

Amit, I would also add that -- and Jeff mentioned it in his prepared remarks, that we have gained 200 basis points of storage share over the last 5 years. So would we like to gain more? Sure. But we do cover all segments of the storage market where there's pure plays that are more narrowly focused. And we're going to keep working on it. And our focus is how do we grow, grow profitably and make sure that we're satisfying our customer demands.

Operator

Our next question is from Aaron Rakers with Wells Fargo.

Aaron Christopher Rakers - Wells Fargo Securities, LLC, Research Division - MD of IT Hardware & Networking Equipment and Senior Equity Analyst

I wanted to ask about the RPO balance. And I think you guys noted that your RPO, excluding VMware, was up about 30%. If I put that in context, your deferred revenue, ex VMware, grew about 11% year-over-year. So clearly, the RPO balance is expanding much faster than core Dell deferred revenue. Can you help me appreciate how much of that is just this backlog build due to supply constraints relative to kind of software deferred -- software RPO growing or subscription growing? I'm just trying to understand the backlog build that you're seeing right now.

Thomas W. Sweet - Dell Technologies Inc. - Executive VP & CFO

Yes. Aaron, let me take that. So you saw quarter-on-quarter that overall RPO was up roughly about $3.9 billion. The vast majority of that principally related to backlog growth, right? So that's how you should think about the RPO growth Q1 to Q2.

Jeffrey W. Clarke - Dell Technologies Inc. - Co-COO & Vice Chairman

Maybe just an add to that. If you think about that backlog growth and the momentum that we saw in our business, at least from our seat, that indicates strong demand for our products and our services as that backlog build. Our cancellation rates didn't change over the quarter. Our ability to deliver for our customers or to our customer commitments, I think, is indicative of that cancellation rate not changing at all. Again, we shipped a record number of PCs and displays as we had the building backlog, and our supply chain team continues to be agile in this dynamic marketplace. We're maneuvering to maximize shipments for our customers. And probably just a little plug here, there are 200 PCs available today on dell.com with next-day ship ready to go.

Operator

Our next question is from Katy Huberty with Morgan Stanley.

Kathryn Lynn Huberty - Morgan Stanley, Research Division - MD and Research Analyst

The guidance for above-seasonal 3Q growth is particularly impressive given market concerns around slowing PC growth and the supply constraints that you've talked some about. So can you just give more specifics around the products or end markets within CSG and any notable trends in ISG that's driving the more bullish outlook?

Thomas W. Sweet - Dell Technologies Inc. - Executive VP & CFO

Yes, Katy. Look, I think as we step back, we like the demand environment that we're seeing right now. Yes, it's challenging from a supply team. They're -- clearly, we're constrained on certain parts, as Jeff and his team worked their way through that. But the demand signals that we see from our end customers, it looks promising. And so as we think about the business and our position within the -- what we're trying to drive, as Jeff mentioned, very strong client demand.

And we, as you know, are more heavily oriented towards commercial PCs, and that mix was up this quarter. And we've seen continued strength in commercial PC demand. So we're encouraged by that even as consumer demand was double digits this quarter. So we're pleased with how that's growing as well.

So look, I think from a parsing of the guidance, I would tell you, we're pleased with CSG, which is what I mentioned in my guidance comment. From an ISG perspective, strong compute opportunity. We're encouraged by the improving storage performance there. I don't want to oversell that. There's work to do in storage, but we're pleased with the environment and the spend we're seeing in the data center. So for us, the dynamic is going to be the supply chain framework around can Jeff get the appropriate -- Jeff and the team get the appropriate parts in and the configurations that we need to be able to ship, right?

And so -- but overall, I think the demand environment from our perspective for Q3 looks healthy. We've talked about the fact that we've got -- we've talked about the fact that we saw some component cost inflation beginning in Q2. Component costs are inflationary in Q3. And so we are working our way through that. We have adjusted pricing accordingly. And it does not, at this point, seem to have impacted any of the demand signals that we're seeing. So I think we're well positioned. We've got to go execute. But overall, I think we feel pretty good about where we are at this point.

Jeffrey W. Clarke - Dell Technologies Inc. - Co-COO & Vice Chairman

Yes. Katy, maybe just 2 points of color to emphasize what Tom said. We saw the movement in CSG towards commercial away from consumer and away from Chrome to commercial, and we believe we positioned our supply chain to capture that momentum.

And then secondly, I think we've talked about this with our growing server momentum now 3 quarters in a row of server growth that we're seeing a returned investment into the data center, that a couple of years of delayed investments in aging installed base, new product transitions with the new processors that are available in the marketplace, some of the supply uncertainty is having customers prioritize their projects to transform, modernize and protect their digital businesses. And we're seeing that momentum build.

Operator

Our next question is from Toni Sacconaghi with Bernstein.

A.M. Sacconaghi - Sanford C. Bernstein & Co., LLC., Research Division - Senior Analyst

I was wondering if you could help quantify either the book-to-bill or the magnitude of your prevailing backlog. I think in response to a prior question, you said RPO was up. Most of it was backlog growth, so $3-plus billion sequentially. That's about 1.5 weeks of backlog. I'm wondering if you can help to mention either book-to-bill or size of backlog exiting Q2 in terms of weeks of backlog by business.

And then secondly, when you -- related to that, when you talk about the above-seasonal guide, what are you assuming for backlog in Q3? Are you assuming you're drawing some down? And how much of the above-seasonal growth is driven by pricing and/or expected change in backlog?

Thomas W. Sweet - Dell Technologies Inc. - Executive VP & CFO

Well, Tony, there's like 3 questions in that question.

Jeffrey W. Clarke - Dell Technologies Inc. - Co-COO & Vice Chairman

I counted 5.

Thomas W. Sweet - Dell Technologies Inc. - Executive VP & CFO

Look, I don't really want to unpack backlog or parse backlog. I will tell you that it has expanded on us, as you might imagine, given the demand dynamics that we're working our way through and the supply constraints. Unlike some of our competitors, I'm not going to tell you how many weeks of backlog we have. I'll just tell you that it's extended and that -- or it's expanded, and we need to work our way through it.

As we think about Q3, I think what you should -- what you need to think about is that, look, we believe the demand environment remains healthy. We are -- we did adjust pricing for higher input costs. So there is obviously some translation to higher TRU. But the overall prevailing framework that we're going to have to work our way through for Q3 is around what our shipment mix -- what's our shipment mix look like, right? And that's the work that Jeff and his team are doing right now around what goes out, what mix of products goes out. But overall, we feel good about their ability to execute on that given -- and hence, the revenue guide that we provided to you.

Operator

Our next question is from Steven Fox with Fox Advisors.

Steven Bryant Fox - Fox Advisors LLC - Founder & CEO

I understand and it's well documented where we are with the component constraints. So I was curious how you would describe sort of the path out of this for the company. How much more can you control on your own destiny going forward? And just to be clear, what is the impact you're seeing like this quarter versus last quarter?

Jeffrey W. Clarke - Dell Technologies Inc. - Co-COO & Vice Chairman

Well, thanks for the question. Look, in aggregate, the semiconductor industry needs more capacity. I think we've talked about this before, but we're seeing the same thing. It's constrained. I think the constraints certainly last or go into next year. The most constrained nodes are the trailing nodes, most particularly the parts that come off the 8-inch network. Quite frankly, no one's investing in a lot of new 8-inch capacity, if any. There's wafer and substrate shortages. We have assembly and test. Wire bonding lead frame areas are challenged. So I think these are consistent things that we've talked about as we've got into the semiconductor challenge broadly across multiple industries.

The path out of this is ultimately more capacity. It takes a long time to build these different fabs anywhere from a couple of years to 3 years depending on the process technology we're talking about. And obviously, lots of capital is required to do that. Our job is that's the environment we're playing in. We've been directly managing our components for a very long time in this company. We have longstanding relationships and partnerships. We continue to let people know what our long-term demand is. It's how we plan this company. And what we have found is those partnerships over long periods of time and consistency in those partnerships and the agreements that we have in place certainly help us navigate these types of situations. That's what we're focused on.

You're not going to see us get into the semiconductor business. It's certainly not a core competence and something that we wouldn't touch. We're working with our partners to continue to understand what the demand characteristics long term look like for these marketplaces. I think as we've been consistent, we believe the PC market long term continues to grow. We believe the server industry continues to grow long term as we believe the same to be true of the storage business. And letting our partners know that there'll be long-term demand is the best thing we can do to ensure there will be capacity in the future.

Operator

Our next question is from Samik Chatterjee with JPMorgan.

Samik Chatterjee - JPMorgan Chase & Co, Research Division - Analyst

I guess I just wanted to follow up on the price increases that you've talked about previously, and you mentioned this today as well. Are we starting to see those kind of impact your guidance for the next quarter? And when do we kind of -- typically with the lag through the channel, when do we start to expect the full impact of that? And how are you thinking about like the magnitude in terms of that benefit between ISG and CSG?

Thomas W. Sweet - Dell Technologies Inc. - Executive VP & CFO

Yes. Samik, so the way I would think about it is we have adjusted our pricing given the higher costs we're seeing, and Jeff has mentioned some of the constraints we have in that space. We have -- I mentioned earlier that we expect Q3 is inflationary from a component cost perspective. We expect Q4 to be inflationary with what we know today.

We've talked a lot for a while now about the fact that with our broad, diverse portfolio, as we adjust pricing, it does take a little bit of time for that to flow through. I think we've been pretty proactive on it at this point. We expect that some of those price increases, a portion of those price increases will impact Q3 and then obviously on into Q4.

The challenge in the dynamic that we're working our way through -- or the mix dynamic, I should say, we're working our way through is the fact that I'm coming into -- I've got backlog that's priced at different price points given where we were in the cost curves at the time of the transaction. So there's some mixed dynamics within backlog that we'll work our way through. Hence, why I guided like I guided.

While we're bullish -- while we like our revenue guidance, the op inc guidance wasn't quite as expansive. In fact, our EPS -- you just think about our EPS, probably our guidance as being similar to how I guided on operating income. And that's just -- we've got some mixed dynamics there that we're working our way through. And obviously, the gating factor, again, comes back to what can we get shipped within the quarter.

So look, I think the teams reacted well. The encouraging news from -- encouraging perspective that I have is that even with the price increases, we have not seen demand signals change. And I think that's very encouraging. We watch our transactional velocity quite closely. That has not really moved on us even with the price increases.

So again, it comes back to, yes, we've got build in backlog. Cancellation rates are -- haven't changed at all. So we feel good about the overall environment. And look, customers have generally been accepting of the price increases given there's inflation in the environment broadly in many different commodities and areas. And so they're -- they've -- and quite frankly, with the lack of supply in the industry, there's not a lot of places that they can go.

Operator

Your next question comes from Shannon Cross with Cross Research.

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

I'm curious on the PC side. How are you thinking about Win11 and commercial demand, how long that will sort of last? I don't know. It's just -- it seems like we've had so many different Wins going at the PC market, predominantly tailwinds. I'm wondering how much of a benefit you think it will have.

Jeffrey W. Clarke - Dell Technologies Inc. - Co-COO & Vice Chairman

Shannon, Jeff, good to hear your voice again. Look, we're bullish on Windows 11. Our industry has a history of new operating systems driving an upgrade cycle. The upgrade cycle, when the product is formally released into the marketplace, we believe, is there. We think Windows 11 brings a lot to end users from anywhere, from a new user interface to the ability to see some productivity enhancements, run multiple desktops and such, drives a higher hardware specification, which is good for business.

We have a large installed base that will continue to need to be refreshed against that. We believe that this is really a replacement of a PC, not an upgrade of an OS on an old PC. So that generally drives demand in our industry. You couple that with what we believe is a general change in usage patterns that the PC has become more essential in this work-from-home, learn-from-home, game-from-home, buy-from-home, entertain-from-home world.

And we think that we're on the verge of new models where, a long time ago, we thought success was one PC per household, now we're seeing multiple PCs per household. We're seeing a more mobile PC base, which requires a more frequent upgrade or replacement cycle is the right word. We think the future is pretty bright for the PC. And a phrase that we've been kicking around the organization is all signs point to a stronger and longer demand cycle for PCs. And we think commercial PCs, in particular, will benefit from that.

Operator

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

Wamsi Mohan - BofA Securities, Research Division - Director

Congrats on the solid quarter and guide. Jeff, can you update us maybe on the specific milestones for the VMware spend that you're tracking? And any timing or milestones that you can share here at all outside of sort of the potential closing in November? And can you also tell us if you received [accelerating] the tax-free spin ruling from the IRS?

Thomas W. Sweet - Dell Technologies Inc. - Executive VP & CFO

Wamsi, it's Tom. Let me take that. There's -- as we track the -- track towards the potential VMware spin date of early November, we are still awaiting the private letter ruling from the IRS. So that is the one major milestone out there. And so we're continuing to work very closely with them, and it's tracking as expected. So that's the remaining major hurdle, if you will.

Everything else is moving as planned, right? The teams are working very closely together as they continue -- as we continue to sort of work through our workflows and work streams around post-spin work innovation targets, innovation areas. The go-to-market motions are all in place. So we feel good about where we are. But we do obviously need to close and get the successful ruling of the private -- from the IRS on the private letter ruling, and that remains on track as of this date.

Jeffrey W. Clarke - Dell Technologies Inc. - Co-COO & Vice Chairman

Yes. Thanks for the question, Wamsi. And I would also just say that we intend to continue to provide information. We've been pretty transparent to the best of our abilities as we move through this process, and we'll continue to do that along with VMware. And we've released some preliminary non-GAAP P&Ls in conjunction with the roadshow materials back at the end of June. And we hope to give you some additional information in conjunction with or just prior to the Analyst Meeting on September 23. So I look forward to continuing to provide additional insight as we move along here.

Operator

Our next question is from Sidney Ho with Deutsche Bank.

Shek Ming Ho - Deutsche Bank AG, Research Division - Director & Senior Analyst

My question is on the operating margins by segment. Your ISG margin has improved to now close to long-term trend. Conversely, CSG has come down a little bit, but still very good. How do you expect operating margins of both segments to trend for the next few quarters given the higher input cost? Maybe you can choose -- pick and choose which one to serve in the supply-constrained environment. It sounds like Q3 is a dip, but how about beyond Q3, especially when IT spending continues to improve?

Thomas W. Sweet - Dell Technologies Inc. - Executive VP & CFO

Yes. Sidney, I don't really want to get into long-term operating margin guidance on this call. But I would just tell you, look, we're pleased overall with the progress we made with our CSG performance and strong profitability. We have talked about in the past that we expect -- we think that, that business runs somewhere between 5 to 6 points of operating margin on a sort of a long-term basis. We're continuing to evaluate that, whether that's the appropriate model on a go-forward basis, and we'll share some of that at our Analyst Meeting on the 23rd of September.

I think from an ISG perspective, we're pleased with the performance -- the progress, but I think there's more work to do there, particularly as we continue to push on storage growth, which generally drives a higher operating margin. So look, good progress, but always more to do, and we'll update you guys on our long-term thinking as we -- at the Analyst Meeting here next month.

Operator

Our next question is from Simon Leopold with Raymond James.

Simon Matthew Leopold - Raymond James & Associates, Inc., Research Division - Research Analyst

You did talk earlier about price increases, but I'm assuming, particularly within the CSG segment, you're shifting your mix towards your higher-profit, higher-price products, and that's a tailwind. So just trying to understand how much of this good revenue trend, the revenue growth is driven by mix versus price increases. If you could just help us break this down in terms of kind of what's sustainable here and what are the key factors on the overall growth. I assume it's not just about more units.

Thomas W. Sweet - Dell Technologies Inc. - Executive VP & CFO

Simon, look, I think you got to think about it like this. So you know, having been around this business for a while, that some of the TRU dynamics within the business are going to be generated based upon what's the component cost environment. And so they will move as component costs move. Right now, with the higher input costs, we've raised prices. So yes, that does have a TRU impact. So we do expect some favorability coming through the -- from TRUs as we look into Q3 and probably into Q4 just given the component cost environment.

Having said that, we're also bullish on demand, right, with what we know today. So we do expect the demand environment to remain favorable absent some sudden change. And so again, I think it's going to come down to -- as you're trying to think your way through how do I think about revenue in the future, at least in the near term, it's going to come down to the shipment mix, right? And that's the thing that we're continuing to work through in all transparency as the supply chain team continues to work through component cost shortages and what they can get in into and what does that look like.

So I'm not -- that's about the most straightforward answer I can give you right now, which is, look, yes, TRU should be somewhat of a benefit, but the mix dynamics from the shipment is going to be what's going to really sort of move -- will decide how the P&L shake out. And we feel good about what we can get done in Q3, hence the guidance we gave you, and we'll update you on Q4 at the appropriate time.

Operator

We'll now take our final question from Jim Suva with Citigroup.

James Dickey Suva - Citigroup Inc., Research Division - MD & Research Analyst

A lot of my questions have been answered so I'll just ask one question, and that's a follow-up on the storage side. You talked about different end segments you feel pretty proud about and pleased about. But when you look at the overall numbers, they look pretty disappointing relative to your competitors out there. So the question is, are you guys like disengaging in quite a few markets and we should be aware at that? Or what you're talking about, the small slices that you're doing okay at, are those early green shoots of what's yet to come in the future?

Jeffrey W. Clarke - Dell Technologies Inc. - Co-COO & Vice Chairman

Well, let me work our way through that, Jim. So the 17% growth that I mentioned is in the biggest part of the storage market. It represents 60% of the revenue, the midrange, the price spends that cover $25,000 to $250,000. We grew that 17% in the quarter, the third consecutive quarter that we've had growth in the midrange on the back of our new product PowerStore, which we've talked about is our game changer in the midrange. And it's proven to be that to date. We're excited, fastest-growing product we've ever launched through its first 5 quarters. We have a growing customer base, and we have repeat buyers. Good signs.

Hyperconverged, the fastest-growing space in storage, where we have the privileged position of being the market leader. Our combined product with VMware, VxRail, grew 34%. So in the 2 most important marketplaces, midrange and the new 2-tier architecture, modern architecture, we're the leader and we're growing. And we're growing at or a faster rate than our competitors in those spaces.

What I mentioned before is in the high end where we have the privileged position of having a share position of in excess of 42%, that market is declining. It's cyclical in nature. Last first half, it grew. This first half, it's not growing. That business, we're obviously exposed to a large percentage of that business being the market share leader with 42-plus percent share, is declining and we're declining like the market is declining. I hope that helped put color to it.

Robert L. Williams - Dell Technologies Inc. - SVP of IR

All right. Appreciate it, Jim. Appreciate it, Jeff. Thanks to everyone for joining. Look forward to seeing you all at our Securities Analyst Meeting. It will be virtual. It will be on September 23 in the morning, and additional details will continue to head your way. So thanks again. Take care.

Operator

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