Dell Technologies Inc: UBS Global TMT Virtual Conference 2021

David Vogt: Good afternoon everyone and thank you for joining us on day two of the UBS Global TMT Conference. My name is David Vogt. I'm the US Enterprise Hardware and Networking Analyst here at UBS. I am pleased to have with us today, Chuck Whitten, Chief Operating Officer for Dell Technologies, who's responsible for running the day to day business operations of the company. Before we get started and jump into the presentation, Dell asked me to read the Safe Harbor statement. So just quickly.

David Vogt: Dell technology statements that relate to future results and events are forward looking statements and are based on Dell Technologies current expectations. Actual results and events in the future periods may differ materially from those expressed or implied by these forward looking statements because of a number of risks, uncertainties, and other factors, including those discussed in Dell Technologies periodic reports filed with the SEC. Dell technologies assumes no obligation to update its forward looking statements.

David Vogt: Non-gap financial measures. This presentation includes information about non-gap operating income, which is not a measurement of financial performance prepared in accordance with the US generally accepted accounting principles. Dell has provided reconciliation of non-gap measures to the most directly comparable gap measures in the slides, captions, supplemental non-gap measures, available on the company's fiscal year 2022 third quarter result event page at investors.delltechnologies.com. So with that out of the way. Chuck, thanks for joining today.

Chuck Whitten: No, well done, David. That's the fastest I've heard that read, so thank you.

David Vogt: I think Rob has his job safe. I'm never going to take that role over. I think since you're relatively new to the seat, a lot of people know you, but you're still relatively new. I thought it would make sense to maybe just spend a couple minutes going through your background and how you see your role at Dell and maybe touch on what you've worked on in the past that's applicable to what we're working on today at Dell in your role.

Chuck Whitten: Well first thanks for having me. I look forward to being able to do these in person soon, David. I thought I can do a quick introduction on me, as you said, and then share a little bit for investors that haven't taken a closer look at us recently, maybe some highlights of our strategy and vision, our recent performance and our long term shareholder return framework and then we can get the Q&A. Sound okay?

David Vogt: Sounds perfect.

Chuck Whitten: Well as you said, Chuck Whitten, you should in many ways think of me as a Dell insider, even though I'm just a little over a quarter with the company. I spent the last 22 years at Bain & Company, but about a decade of that, I spent working exclusively with Dell technologies and working alongside Michael, Jeff, Tom and the entire leadership team on their growth strategy and most critical strategic initiatives. So I'm very familiar with the company, spent the bulk of my time in technology and was excited to join this company at this critical point in its history, which is incredibly exciting as we'll talk about today. From a strategic perspective, maybe I would start by highlighting three things about our strategic position.

Chuck Whitten: The first thing I would call out to those that haven't looked at us recently, we are very uniquely positioned in the data and multi-cloud era. We have durable, competitive advantages. We have market leading positions. We have the financial flexibility to drive sustained profitable growth. We like to say in many ways, markets are coming our way as IT becomes more distributed, the edge, more multi-cloud and more data intensive. The second point I would make is that our ISG and CSG core businesses are very attractive. They set in large markets estimated about $670 billion in TAM. They're projected to grow in the low single digits over the next few years and that gives us ample head room for growth. We have a track record as a company of gaining share in these businesses behind what we think is a differentiated strategy to consolidate and modernize those core markets, which leads me to the third point.

Chuck Whitten: We have attractive new growth opportunities that surround that core business, about $650 billion in additional market, growing at an 8% CAGR through 2024 and these are markets where we have the ability to use the same advantages that we've developed in our core business and where we're driving real innovation today. Those are markets like Edge and Telco. Just to name a couple of examples. So with that is the sort of strategic backdrop. Maybe I'd highlight a few things about our recent performance. Look, we continue to see unprecedented demand for technology. It's clear that technology is more essential today than ever before and it's equally clear that Dell is at the center of customer's IT and digital agendas. The usage pattern for PCs has permanently changed and it's reset that market to new levels. Widespread digital transformation and the economic recovery has spurred growth in IT spending and IT infrastructure.

Chuck Whitten: And so against that backdrop, we delivered a fifth consecutive record quarter in Q3 delivering 21% revenue growth in that quarter and we saw growth in all business units, all regions and broad strength across our PCs, servers and notably an inflection point in storage as we grew that business year over year. I note we gained share in servers, storage and PCs, according to the latest reported IDC results as well. From a BU perspective, our CSG business delivered record revenue was up 35%. It was driven by ongoing strong demand across the board, commercial and consumer, notebooks and desktops and on a year to date basis, that business CSG is up 28%. ISG posted its third consecutive quarter of growth. That's up 5% on a year to date basis. ISG is up 4% and we continue to just generate exceptional cash flow. We had 13.5 trailing 12 months cash flow from operations. That's up 45%.

Chuck Whitten: And of course we delivered all of that performance in an incredibly challenging supply environment while managing through inflationary costs, and so we think that execution speaks to the strength of our position, our durable, competitive advantages and it adds another quarter to our track record of delivering consistent growth, profitability and cash flow in any environment. Maybe I'll just conclude quickly with long term value creation framework. We're firmly committed to creating shareholder value. We've simplified our corporate structure, selling Boomi and spinning off VMware. Our focus on debt paydown and achieving the investment grade rating has significantly simplified our capital structure, our business generates significant cash flow, as I said, and so over the past few years, we have used about 95% of our free cash load to pay down debt.

Chuck Whitten: Going forward, we're excited as we transition to a much more balanced capital allocation framework that will include return to shareholders and our financial framework is focused on growth. 3 to 4% over the long term with EPS growth of 6% or better. We're very optimistic about the future, the strength of our core businesses with number one market positions, the durable competitive advantages I mentioned, and our focus on new businesses and adjacent markets where we have a right to win. We think our strategy and financial flexibility will drive long term shareholder value and long term value creation. So with that, David, maybe we can go where you have questions?

David Vogt: Yeah, no, that's a great starting point and a great overview. We get a ton of questions on the durability of your business, the sustainability of some of the growth. Now, obviously I don't think anyone expects a growth to continue at such an unprecedented rate given where we're coming from, from a COVID perspective, but maybe let's just start with the CSG business for a second. Obviously, there's a range of expectations in the public domain. I think Dell's on the record, expecting that next fiscal year, the CSG business will grow. Maybe can you share with us kind of how you think about that business in the context of what we just went through from COVID? Maybe changes in consumer behavior and or commercial behavior, and what gives you some degree of confidence that maybe the next fiscal year, we're going to see growth.

David Vogt: Obviously we don't think it's going to be a linear growth environment. There'll be some peaks and some valleys, but there's to some debate whether the absolute level of PC demand remains relatively stable, as opposed to reverting back to a more normalized level that we saw pre-COVID. So just maybe start there and take it from there.

Chuck Whitten: Yeah. Happy to, again, I would start with the backdrop we're coming out of because I think the starting point matters as well, which is, look, CSG grew 35% in Q3. Our commercial business grew 40%. Our consumer business grew 21%, as I said, that's year to date up 28% and that healthy demand was across all geographies. So, let's start with the backdrop is very strong, but more directly to your question. Look, we believe we've seen a change in usage patterns that have fundamentally reset the market to a higher level. Why do I say that? You mentioned behavior. The do anything from anywhere economy, work from anywhere, shop from anywhere, entertain from anywhere, game from anywhere. It's created demand for a modern PC experience that's not going backwards. So pre-pandemic, the market averaged approximately 260 million units from 2016 to 2019. That jumped to 300 million last year.

Chuck Whitten: It's going to come in somewhere between 340 and 350 this year. That do anything from anywhere has increased the number of places that we need technology. That's what we mean by a reset, and then I think what's important is the texture underneath that top level demand, there are more notebooks. That drives a faster refresh cycle. There are approximately call it 700 million PCs greater than four years old. That means they can't deliver the modern experience that users have gotten used to in the last year. The modern experience that you and I are using right now to have this conversation, Windows 11 will add to that refresh cycle and requires modern hardware. If I turn to the consumer side of the business and education, we still have millions of children in schools without PCs. We remain pretty far from one PC per person.

Chuck Whitten: The benchmark long used to be one PC per household. That paradigm has obviously shifted. So look, all of those factors make us bullish on demand. I think IDC's latest forecast for next year is flat overall. So again, not the forward growth as you said of last year, we're more bullish than that. But the net is we expect growth next year, which me brings me probably to the final point I'd make on our business, which is not all units are created equal in the PC market and our business is positioned particularly advantageously.

Chuck Whitten: So our business and focus is centered on the higher value segments of the market, commercial PCs, premium consumer, gaming. We participate broadly, but that's our focus, and if you trace the arc from 260 to 270 million PCs in the TAM to the 340 to 350 I mentioned, those are the portions of the market that have proven to be the most stable. They're less susceptible to the fluctuations up and down that you may have seen in Chrome and lower end consumer units, so that gives us some that gives us some confidence as well, and look, the other thing I would leave you with is we're a structural share gainer and so in Q3 we gained 300 bips of share according to IDC. That was almost 400, approximately 400, excuse me, in commercial. The last five years, we've gained 140 bips overall

Chuck Whitten: And over 460 in commercials. So, we're poised to continue to grow against this backdrop of a sort of reset demand for PCs overall.

David Vogt: Got it. That's helpful. And maybe just from a behavior perspective, so there's a ton of discussion about work being just work. What I mean by that is work could be work from home to your point, work in the office. So does that change the sort of mix in terms of PCs going forward? What I mean by that, so your exposure is, 70, 75% commercial, but if I'm in the office and I want to have a better experience at home, is that machine going to skew more to the specs of a commercial PC, because I need it to have the greatest camera, the greatest video card, the best, experience I can actually work at home. And so to your point about IDC expecting flat overall PCs, maybe it skews a little bit better because of the mix is more commercial.

Chuck Whitten: I think there's, there's compelling elements of that argument. Let me tell you what we've seen. What we have seen is higher content rates in our PCs, right? In this environment, right. That because to deliver the modern experience you and I talking about it and that you get used to in a commercial environment, higher quality LCDs cameras, compute memory, and certainly in the high end of our business on the consumer side, we see that as well. And we see that overall. And so again, we think there are richer PCs out there to de to deliver the experience. The other thing I think you touched on in that question is the peripheral experience becomes very important as well, right? And as part of our secret sauce, if you will, to our profitability and growth, which is outside of the core PC, there's an almost equal, I think actually equal if not bigger, total addressable market for peripherals, we're the leader in one critical of those markets displays, but there's so much more that can go around the box, particularly if you want to deliver a modern experience.

Chuck Whitten: And so that's an opportunity for us as well. And again, in a market for PCs that that has to a higher level may not grow at the same rate, as you said, that we've seen over the last 12 to 18 months, but certainly plenty of opportunity.

David Vogt: Got it. And then maybe along those lines, without putting you on the spot, but all of these factors and the supply chain considerations would suggest to us in sort of intuitively that pricing should remain relatively healthy for of the foreseeable future. I mean, when you think about a relatively consolidated marketplace from a number of vendors perspective, I mean, is that a reasonable sort of leap going forward at this higher level where, there's only a handful of companies that can really satisfy the needs of both sort of the commercial and the high end consumer market, obviously your sales being one of them. So does that's suggest that we have a relatively stable pricing environment as we go forward, given that pricing has been relatively strong, you have some tough compares, but just generically is pricing not going to pull back to where we saw it pre COVID effectively.

Chuck Whitten: Well, maybe some observations on pricing historically, as you said, I'm not going to get into forecasting pricing. The only thing I know when I forecast is I'm going to be going to be wrong, but, in our segment, pricing tends to follow commodity costs and we have certainly seen higher input costs over the recent quarters, we're not immune to the broad dynamics across the industry. And as we've called out in Q3, the Q3 quarter over quarter cost increase in our environment was the largest the company has encountered in recent history. And in parallel with the part shortages, which I'm sure we'll get into at some point component cost, had an inflationary trend in Q3. And it was, it was memory. It was displays, it was SSD and by the way, logistics, as you read the papers, increasingly challenging air ocean freight remained at elevated levels.

Chuck Whitten: And so look, as we mentioned, with regard to pricing the last in our last two earnings Carls, look, we've taken pricing action to abate that higher input cost. And we've done that in both CSG and ISG and in general customers have been receptive to pricing moves due to the component cost inflation, but also because the dialogue has been about availability and look, we're mindful of our competitive position when it comes to pricing, we never want to dam and demand velocity. You know what the future of pricing holds, I'll leave that to you guys to speculate. But right now it is a benign environment given the overwhelming demand for PCs and supply challenges. And then as we just talked about, customers are pulling on higher content rates to deliver that modern experience. And that also is happening in our server business for running ML and AI workloads that require more CPU, GPU, memory and storage. And so again, it's been an attractive market for, for ASPs recently because of both of those polls, I'll leave it to you to forecast what happens in the future.

David Vogt: Yeah, that's fine. So maybe just going back to the pricing that you talked about, can you help us, can you remind us how the pricing flows through, let's say in CSG, right. So you've seen tremendous price increases from components over the last couple of months, given your inventory situation and the way your model works from a working capital perspective and the supply chain issues and elevated backlogs across the industry and what does that mean for pricing going forward? Are we going to see, a little bit of margin now and you'll see some pricing over the next, three to six months be a little bit more stable, or is it as close to real time as we can get given sort of the nature of your supply chain expertise?

Chuck Whitten: Well, you know, I think, I think as we mentioned in Q3, after I said that Q3 step up was the largest we'd fell quarter on quarter, as we go to Q4 cost remain inflationary and, but at a much less, step up than we saw in Q3. And we always endeavored a price ahead of that as best we can. We've also been transparent. We recover a portion of our pricing sort of in quarter and some the next quarter, I think that the other variable that's hard if commodities are sort of flattening a bit, if you will, David logistics continues to be very challenging. And so right now the pricing environment remain remains benign. And we do see sort of the inflationary pressures still in still inflationary, let me be clear, but at a less drastic clip than we saw in Q3.

Chuck Whitten: And we know that's how we sort of proceed with, with pricing, as we head into next year, what's going to happen is hard to say, we think it's going to continue to be a challenge. Some commodities will go through a period of decline. Others will offset it. I just think that's the environment we're we're in right now. And it's always of course dependent on the broader demand environment that we're in. So we'll obviously give much more clearer guidance on that as we get into Q4, but that's sort of where we stand right now. I think you're on mute, David.

David Vogt: Oh, sorry about that. I think... first day with the new camera. No, I'm kidding. I think people care tremendously about CSG, but obviously let's not forget the strength in your ISG business and maybe just pivoting that for a second. Obviously we're starting to see improvements in storage demand, server demand, and you touched on it in your prepared comments when you think about order growth that you've seen recently specifically in storage and what we think we're seeing from our supply chain checks in enterprise server demand as we move into calendar 2022, I'd love to get your thoughts on what you see driving sort of this improvement in demand. Maybe just in a little bit more detail starting, maybe on the server side and-

Chuck Whitten: Start on servers. I'll start on servers and we can discuss storage. So, you heard us say our recent history servers in networking revenue in Q3 was up for the fourth consecutive quarter. That was plus 9% mainstream server demand was up double digits here over year. And that's obviously, we're very pleased with that growth. I think to your direct question, as a reminder, we saw robust growth in FY 19, FY 20 was a period of digestion for compute in the server market and FY 21 or, or calendar 20 was supposed to be a year of again, infrastructure refresh. And then customers were focused on instead navigating the global pandemic and making targeted investments. And those investments often tilted, as you've seen in our financial is to the client side of the business and delivering for, for hybrid work.

Chuck Whitten: And so look what we've seen as the overall economy and IT spending is recovered, is a rebounded data center demand. And that's what we're feeling right now. You've seen the IDC forecast at server revenue this year of 6% and for the calendar, I think mid single digits moving for we're again, probably more bullish on that, given that we see widespread digital transformation not stopping, but regardless of the underlying market forecast, we, we see growth as the number one mainstream revenue leader in, in servers and a structural share gainer, we just feel really well positioned for this recovery phase, given our advantages and go to market our advantages and supply chain scale, our portfolio innovations and in DFS. And so net is it's a good market environment. We're well positioned. We're all optimistic storage.

Chuck Whitten: Storage is a more complicated story for us as you know, and it's been a working process for us for some time. But as I mentioned in my prepared remarks, look, we returned to growth in Q3. And that was an inflection point for us. I, because I know it's a broad group that, this, I always like to start with the most critical piece of context when you look at our storage business, which is, we're number one in all external storage categories, we're number one in high end, mid range, entry, unstructured object, all flash HCI, data protection, you name it, we lead in it. And that just means you have to look at our growth numbers with a little bit of a discerning eye, unlike some of our competitors, we cover the full market.

Chuck Whitten: And so that's some of the puts and takes that you feel in our business. And so while we don't disclose our full demand number every year, what we did or every quarter, what we did highlight was that we were very encouraged by our storage momentum in Q3. And as I call that it was an inflection point and we're particularly pleased with our performance in the largest and most strategically relevant portions of the market. So what are those mid range that represents roughly 60% of the storage market, where we grew 18% this quarter after growing 17% in Q2, 23% in Q on 8% in Q4 of last year. And as we've called out power store, which is our critical product in that, in that market, along with our unity offering, it's clearly winning, it's attracting new buyers, it's creating repeat buyers.

Chuck Whitten: It's the fastest growing storage architecture we've released through six quarter of sales. So we're very encouraged by mid-range. We always call at HCI, it's an important battleground. We're we're the market leader. We grew 47% in Q3. You know, we also highlighted our data protection business in growing 26% where again, an important in market leading segment for us. So with all of those data points, what, where, where are the challenges in our storage business? Again, with a broad business, the high end, continues to be a cyclical market. We're the leader in high end, over 40% market share. That's a business that's typically tied to the mainframe refresh cycle. And right now that's a down business year over year. And then, you know, there's two other primary dynamics that impact our sort of

Chuck Whitten: Walk, if you will, from our storage demand to our PnL revenue, where we posted 1% growth. And we called those out in Q3, but the two are, first, we had a lot of backloaded linearity, meaning storage orders came in late in the quarter. That's very typical for our storage business, but we would say Q3 was even more backloaded than normal and we built backlog in that business. And then second, and I think this is a really important part of the story, our storage business has high services and software content. And that typically is amortized over four to five years based on the life of the contract. That's obviously a great thing for the business. It creates happy and loyal customers, but that revenue is not realized in period. And those two impacts can create a separation between our orders momentum and all that optimism I just described and our PnL realization, which is what happened in Q3.

Chuck Whitten: So, look, the net from my chair is if we continue to deliver consistent quarterly growth in storage, particularly in those most strategically critical portions of the market, you'll see a steady build in our PnL as services are amortized. And broadly speaking, long term trends are favorable to us. In the data era, customers are going to need more external storage, and we're the leader there.

David Vogt: Yeah. I mean that's a great point. I just would mention that we've been doing a lot of survey work, and we do pretty regular checks. We picked up that it sounds like order momentum was late in the quarter as you articulated and it's been building. And so, expectations for, let's say, the quarter that was just reported were strong, but the expectations on a forward looking basis were even stronger. Would you characterize that as being directionally accurate in terms of what you're seeing here?

Chuck Whitten: Well, I mean, again, the challenge with linearity is it's all depends on how the linearity shapes in Q4 as well, David, right? And so, if we have a similarly backloaded quarter, you're always on the treadmill. I think, again, what I would tell you is from a demand standpoint and the resonance of our products and market, right now, we feel good. Obviously, we try very hard to not have the type of linearity that we saw in Q3, but it's a reality in our business, right. Well, have it in Q4 as well.

David Vogt: Got it. And then, when you think about the competitive landscape... You mentioned high end storage down year over year. Mainframes are the primary drivers of that business. There's some discussion that we may see a mainframe cycle at some point in the second half of next year maybe starting to pick up. Do you have any thoughts on maybe the compression of the cycles or the duration of the cycles from an IBM or a non-IBM-

Chuck Whitten: Yeah. That's a great question for IBM. I think I read and look at the same data you do on that, right, and say next year is the year to look at, right. And certainly, we try to proactively plan for that refresh cycle and do forward planning with our customers as well. But, in terms of the shrinking or lengthening of those cycles, that's a great question for one of my peer companies.

David Vogt: Yeah. They're not very forthcoming. So [inaudible]

Chuck Whitten: You've got to try. You've got to try. I know.

David Vogt: You've got to try somehow. Maybe just pivoting a little bit. I don't want to get into supply chain until later, and cashflow. But I'd be remiss if I didn't talk about VMware. The spin was incredibly successful. We think it created tremendous amount out of value. Obviously, it's early days, you have a commercial relationship. It's not effectively, my words, maybe not your words, profitable yet to where you want it to be. What if anything has changed in the early days post the spin if anything? And what are the steps that you can potentially take to work through sort of this lower profitability revenue stream?

Chuck Whitten: Lower profit?

David Vogt: Yeah. It'll take some time. We understand that. But maybe help investors understand kind of how you're thinking about it and what the relationship looks like today and what it could look like in the future.

Chuck Whitten: Yeah. Well, let me start at the strategic level and just say, I always like to categorize it as a capital structure change but not an operating model change. So, let me start there. The strength of our relationship with VMware has never been better. The first and best is the word we use all the time. Our first and best motions with VMware through our technical and commercial agreements that we've honed over five years plus, longer, dating back to EMC, are very hard for anyone else to replicate. And they run deep in our company. And so, our operational efforts don't change. And to our customers, we haven't heard noise. It's just been business as usual as we continue to innovate together and pursue joint market opportunities.

Chuck Whitten: We made a recent, relatively big announcement on our apex cloud services offering on VMware Cloud. That's a perfect example of us jointly going after the multi-cloud market together and a further example of our kind of technical alignment. So, look, that commercial agreement you described that formalizes our joint commitment to product innovation and go to market alignment means that we'll start reporting VMware revenue as reseller revenue in our other business segment. That's alongside our Secureworks business. And as you said, that today is, call it, neutral profitability, right, for us. Over time, we will work and revisit that. Within the frame of the agreement, we have an annual process around which we talk about our commercial agreement. So it's our intent to certainly improve that. But strategically speaking, we continue to be in lockstep with VMware driving technical innovation and serving our customers. And that's really our focus right now.

David Vogt: Got it. And just to be clear... You mentioned it, but I want to make sure I understood. So, you've been talking about the spinoff for 12 to 15 months before it actually happened. So, customers probably were well primed in terms of how to think about the two business as separate, effectively. Well, they were separate before, but financially you're separate. And so, other companies in the past might have had some disruptions in terms of relationships, revenue conversion. It sounds like you've seen none of it, right? And-

Chuck Whitten: No. And it is true because this isn't... It was not a carve-out of a business from inside of us where we had to separate a lot of... They were two businesses, right, that had a... It's almost like a strategic alliance or... It is a strategic alliance today, but it was like that before... That's why I think that it was it very, very seamless. Obviously, lots of lawyer work and banker work and all of that to get the spinoff to work correctly. But, no, from our technical teams and our go to market, limited changes other than getting used to this new reality of a more arms length arrangement.

David Vogt: Got it. You touched in your prepared remarks financials and cashflow, but before we get there, I told Rob... He put this late in the question, but we have to ask about supply chain. And I think most investors are comfortable with the headwinds that your company and other companies face today. But the question that we get over and over again is... You mentioned freight. You mentioned... A lot of companies talk about, specifically in the PC business, the lack of matched components, some older components. Maybe there is some shortages of PMICs or across the board, just random ad hoc shortages.

David Vogt: When you think about the expertise that Dell has put in place from a supply chain perspective, do you think longer term that more companies move in your direction and that your model is fine tuned when we come back to a normalized environment or do you think there's any sort of structural changes that need to be made in the supply chain to maybe mitigate these potential headwinds, right? So, maybe companies carry more inventory than normal, maybe just-in-time inventory isn't really the right way to go for the longer term. I know it's more a theoretical question. But I think companies have been spoiled for the better part of the last ten plus years.

Chuck Whitten: Yeah. I think you're asking sort of like let's get at the secret sauce of Dell's supply chain a little bit. Why are we performing the way we are? And we're getting that question a lot, right. And certainly, I'm sure the world is studying us because I think we're navigating well. I'll start with the environment and then let me go to what I think we're doing and how that might apply to other companies. I would say it's a difficult environment, but we're no different than anyone else in the industry. We see the same challenges, and you hit on a few of them. They're well documented and they fall under the broad header of integrated circuits, right? Overall, industry just remains constrained given global demand for electronic goods and components.

Chuck Whitten: And like the rest of the industry, we're therefore experiencing shortage of ICs, which are impacting PCs, displays, docking stations, and servers. As my co-chief operating officer, Jeff Clarke, has called out, older process nodes are the most challenged with multiple industries competing for that scarce capaciting supply. That's eight inch being the most constrained, 12 inch not much better. That's the 40, 55, 60 nanometer components. And it's truly day to day. And then add in logistics, as you said, which has proven very challenging as air and ocean freight remain at elevated levels. It's hard out there in day to day. So why are we performing well? What I would argue is it's not just one thing, it's our business model. And so, our supply chain is of course an advantage. And we've called it out as a durable, competitive advantage.

Chuck Whitten: It's the largest in the industry. But importantly, it's a multi decade, operational heritage of building direct relationships with the supply base. So these are intimate conversations with the supply chain on how to navigate this type of disruption. It allows us to flash demand forecasts to them well in advance so that then we can work our way through and navigate lead times on components. But there's other elements besides our supply chain, and this is what I think is tough for everyone to replicate. One is our product design flexibility. We have built in less complexity into our product line, more modularity, and the ability to qualify the parts that are available. Our direct sales engine is an enormous advantage in this environment because we get a very high quality demand signal. That's helpful to the supply base, for sure. But we're also able to shape demand based on that component availability.

Chuck Whitten: All of us at Dell are in regular conversations with customers that go something like, "Here is your spec and it's on extended lead time. Can I show you two or three other specs that are on shorter lead time?" That's a huge advantage for us right now. And so, that's why I think despite the shortages and the challenging environment, we shipped a record number of products globally in Q3. What can others learn from that? I would argue that's a really hard thing to replicate, right? If you don't have the ability to shape demand, if you don't have deep supply relationships that reach all the way down deep into not just the primary component, but the sub component, you can't build that on a dime. You have other solutions, but one of your solutions may be to hold more inventory. For us, I think this is just sort of part and parcel with what we do every quarter. It just happens to be in a sort of unprecedented time of complexity in supply chains.

David Vogt: Maybe can I ask you a devil's advocate question? So, if normal-

Chuck Whitten: Sure.

David Vogt: If demand normalizes and supply chain is normalized, does your ability to shape demand and steer demand sort of lose some

David Vogt: Some of its relevancy right where... Maybe it's a useless demand signal effect. Maybe not useless, that's too strong of a word, but less of a shared gaining opportunity for you, right? Where-

Chuck Whitten: Well, we're always able to... It's certainly a huge advantage now, but there are so many benefits to having a clean and advantage demand signal, whether that's our cost or continuity of supply, whether that's our access to technologies and transitions, whether that's the ability to shape a customer to a richer config for their workload or to say, "Hey, based on what you're trying to in your environment, here's the right tool for the job."

Chuck Whitten: So there's so many advantage to us. Right now, one of them happens to be I can shape the demand to the availability. But in times of normal supply, it's also an advantage for all those other reasons. And look at the end of the day, it's customer trust. We're a trusted partner in our customers' IT agendas. That has huge benefits, margin growth, and otherwise to our business.

David Vogt: I mean I would suggest... I would submit then it leads to better margins, which you've been able to generate relative to your peers. And I think a better ASP umbrella than your peers, at least.

Chuck Whitten: I would agree with both those. Yeah.

David Vogt: Got it. So just maybe in the interest of time, cashflow balance sheet seems to be a topic of debate. You've done a great job as a company deleveraging, as you mentioned in your prepared remarks. And I think Tom's talked about a little bit more incremental debt reduction to get that final upgrade from... I think it's Moody's has you on positive watch.

David Vogt: When you think about the cashflow and Tom's talked about this but would love to get your perspective. You know cashflow has been running almost 6 billion on average for the last couple of years, net income... Excuse me. Cashflow's going to be better than any net income. Can you give us a little bit more color on how we should think about the trajectory now that we're standalone and maybe, if possible, a little bit more color around maybe the delta between cashflow and net income, if possible, just to help investors?

Chuck Whitten: Well, yeah. Well, let me channel my inner CFO and friend, Tom Sweet and start by reminding you we're 35 days since the spinoff in investment grade rating. So I think a little patience is in order but look. As you said our business generates very strong cashflow. That's somewhat been overlooked, I think, given that much of our capital allocation for years is focused on debt paydown as you said. It's an advantage.

Chuck Whitten: You called out our negative working capital conversion cycle. It's just different. And when we grow with that negative working capital conversion cycle, we generate significant cashflow. As of our Q3 earnings, we paid down 15.9 billion in debt, as I said, and that brings us to a 1.9 core leverage ratio.

Chuck Whitten: And now that we're investment grade, you'll continue to see a bit more debt reduction as we manage our way to 1.5 core leverage target. I think more excitingly, it allows for that balanced capital allocation framework that I describe, which includes 40 to 60% adjusted free cashflow return to shareholders. We'll do this via dividend, subject of board approval, starting in Q1 and through share buybacks, which will be more programmatic managing dilution.

Chuck Whitten: And so, I'd continue to just point you back to our long-term value creation framework and how we've articulated that. It's a long-term framework. It's the starting point. Right now, we recognize that we do have considerable cash right now on the balance sheet. We've articulated many times it takes four to 5 billion dollars to run the business. We don't think we will adhere exactly to that four to five every minute of every quarter. But that's the framework I would point you to is the 40 to 60 adjusted free cashflow per term.

David Vogt: Got it. And in that context, when you put your COO hat back on when you look at the portfolio, you've divested Boom. You've obviously spun out VMware. You've done some other smaller deals. Right now, the portfolios seems to be hitting on all cylinders. Where do you look at the portfolio today and say in three to five years, we need to add some capability and if that's through internal R&D efforts or M&A, how do we get there? Besides that 40 to 60%, but what else is the cashflow going to be used for?

Chuck Whitten: Yeah, well, look. I think that flexible financial framework I gave you gives us the ability to invest in growth in the business and pursue M&A. And so maybe a few observations. M&A is going to certainly be part of our future. We think it's a core to any good growth strategy. Without giving shopping lists out, I'd say four things about our M&A strategy. We're strategic is the first thing I would say. M&A is clearly going to fit into our communicated strategic framework. And so don't expect a bunch of surprises from us. We're proactive on this, and the spaces that I've talked about as being interesting to us, Edge, Multi-cloud, Telco Data Management, they're those spaces I said that are in that big adjacent, total addressable market that sits next to our core business.

Chuck Whitten: So, first strategic, second targeted. I think Michael has been very clear. We've all been very clear. Don't expect large-scale M&A transactions. The circumstances that led to our combination with EMC were unique. And we're focused right now on what I would call scope acquisitions versus those large scale acquisitions. We're always looking but don't expect large-scale M&A.

Chuck Whitten: I would say third, look we're disciplined. Ultimately we're laser focused on value accretion to long-term shareholders. And many of the spaces I just described are, how would I say it, very, fairly valued right now. [crosstalk].

David Vogt: Lofty. [crosstalk].

Chuck Whitten: Yeah, lofty. So look, strategic targeted discipline, don't expect large transactions, but know that we have the financial fire power to invest in those growth markets. And that's what we tend to do, all in the context of a balanced capital allocation framework for investors.

David Vogt: Got it. [inaudible] So in the interest of time, I think we're running a little bit short. I always like to give the executive an opportunity to give the elevator pitch at the end. Maybe something that we didn't touch on at the very beginning, and just maybe leave it with you. If we didn't touch on anything other than what you said in your prepared remarks, anything you want to leave investors with, as the key takeaway?

Chuck Whitten: Well, no. I think in my prepared remarks, I tried to paint a vision of a business that has a lot of attractive characteristics right now, right? Our core businesses are in and of themselves attractive. And as we said, markets are coming our way. The PCs never been more critical to the world, whether it's in hybrid work or all of our lives. Infrastructure is rebounding. And we have leading positions everywhere. Number one, in external storage, number one in data protection, number one in x86, number one in HCI, number one in client revenue and profit, number one in displays.

Chuck Whitten: We're perfectly positioned for this moment in technology. When you couple that with adjacent growth opportunities where I think we have a right to win building off of the capabilities and customer access that we've built in our core business and a disciplined capital allocation process with the financial flexibility we've built through years of hard work and debt paydown, we think we're really well positioned right now to create long-term value. And I think you wrap all of that in what hopefully comes across every quarter as an incredibly high say-do ratio and a culture of execution, we think we're perfectly positioned.

David Vogt: Perfect. Well, Chuck, I think we'll just stop it there and end it. We appreciate you dedicating a lot of your time. Very generous. We appreciate it. And Rob, thanks for helping as well. And if anyone has any questions, please feel to reach out to me directly, or I'm sure many of you know Rob Williams, you can reach out to him. Chuck, thanks again. And everyone have a great evening.

Chuck Whitten: It was my pleasure. Thanks, David.