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DELL - Dell Inc. at Morgan Stanley Technology, Media & Telecom Conference

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PRESENTATION

Katy Huberty - *Morgan Stanley - Analyst*

Good morning, everyone. Welcome to the Dell presentation. It's my pleasure to welcome Paul Bell, the President of the Global Public and Large Enterprise business unit at Dell. Paul has spent 15 years at the Company across the consumer, commercial, enterprise, public segments, spent some time in Europe, so brings great knowledge to the stage today.

Thank you very much for spending the time with us, Paul, and we're just going to jump right into questions and we'll leave some time for yours at the end.

So, just to start high level, you obviously spend time with large enterprise and public-sector CIOs. What are your customers telling you about their IT spending plans for 2011?

Paul Bell - *Dell, Inc. - President Global Public and Large Enterprise*

They've generally, across the board, been moderately growing budgets, and that's what they've been describing as coming off a year where, in the commercial sector in particular, there was a very significant growth after stalling out the year before.

So, that's kind of behind us. People are back to levels of spend similar to right before the recession, and now they're kind of the long-term growth that you see. And of course, the interesting bit comes in where they are investing and where the growth comes, but on average we're up. And of course, commercial is a bit stronger than public sector, or at least the government part of public sector, which in western Europe and North America continues to be a bit soft.

Katy Huberty - *Morgan Stanley - Analyst*

You mentioned that the interesting point is where they are spending. What are the top priorities that you hear from customers?

Paul Bell - *Dell, Inc. - President Global Public and Large Enterprise*

There is clearly continuation in the growth around lifecycle management of data, storage, all the solutions there because everybody is, of course, on an explosive growth trajectory for the data, so how they solve that, how they invest in getting out in front of that, and getting the true benefits of lifecycle data management, rather than just sort of a static storage model, is right at the top of everybody's list.

They're spending on security, which shows up as a subset of lots of different projects or, in some cases, as a big project in and of itself. But that's right at the top of the priority list, anyway.

And there's all kinds of innovation and experimentation and early projects around mobility for their end users, whether it's the smartphone or tablet or other pocket device, or it's how they make full use of client virtualization across multiple devices. Those are very common new initiatives across the spectrum.

Katy Huberty - *Morgan Stanley - Analyst*

And you had mentioned that some of your commercial customers are back up to their prior peak spending levels. Are there still industry verticals or areas of government where they are underspending and you see some catch up over the next year or two?

Paul Bell - *Dell, Inc. - President Global Public and Large Enterprise*

Certainly in western Europe and North America, you see national and regional government decline, so here in the U.S. obviously -- so the federal government was the strongest sector for a number of years there, while the commercial sector was down, and now we are into continuing budget resolution. We are into some uncertainty about what the level of budget will actually be, and so that has put a pause on spending until that is sorted out.

Then you have, trickling down to state and local governments, actual budget cuts that are now being implemented pretty significantly.

Now I will tell you that some of that has created a big opportunity for us because -- you know, you've heard this line that's been reused a lot in the recession about it's a shame to waste a good crisis. I've had a lot of IT customers in various levels of government say, okay, all these ideas you had about how you have a fundamentally more efficient and lower-cost infrastructure in IT, I had a lot of resistance to change before but now I'm able to do it. Let's talk about how we can get you on a lower cost, more efficient architecture.

So in some cases, we are seeing pretty good growth despite the budget decline in the sector.

Katy Huberty - *Morgan Stanley - Analyst*

In the public sector, you say.

Paul Bell - *Dell, Inc. - President Global Public and Large Enterprise*

Yes, particularly state, local, and the K-12 school district world.

Katy Huberty - *Morgan Stanley - Analyst*

I know it's a little early, given the year-end is June for state and local and September for federal, but is there any talk as to whether, as we go into the following fiscal year, that budgets will stabilize or improve?

Paul Bell - *Dell, Inc. - President Global Public and Large Enterprise*

You know, they've been declining for about -- a good solid three years now, and what happened this year was more the scale of the deficits, and it's turning into actual cuts in spend or, in some cases, people had other contingencies or other things they did, so it's not a new topic for them. It's just degrees of magnitude.

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I don't see anybody feeling great yet about the next fiscal year as the state and local level.

Katy Huberty - *Morgan Stanley - Analyst*

Okay. I want to talk a little bit about Dell's go-to-market strategy, particularly in enterprise. A number of technology companies are increasingly discussing a solution-led selling process, and a lot of your peers are investing in new sales resources, so can you talk about how Dell, who purchased Perot and is selling more in a solutions-led way, how does Dell differentiate in a market where IBM has been doing that for a long time, HP, Cisco, Oracle are all investing incrementally? How does Dell differentiate?

Paul Bell - *Dell, Inc. - President Global Public and Large Enterprise*

The differentiation comes with the level of the solutions themselves, and our kind of internal rallying cry for this has been open, capable, affordable solutions.

It says that people expect Dell to help them get to the next level of technology sophistication, but in a way that leverages building blocks, modular architectures, gives them choice as they put that together. It's kind of an antidote to the lock in of the completely vertical stack.

So that's the differentiation, is to say, okay, if you want to get to an all-virtualized world, you want to get to this world of mobile apps that are creating new experiences for your end users, let us show you how we can get you there in a way that is far more cost effective and gives you flexibility. That's the differentiation.

The sales force to do that does require a lot more specialization. So, Dell has been differentiated from some of our large technology customers in that we've always had the unified account owner model, an account executive. Our customers like that because as Dell is broader and has many more different solutions to bring to bear, the fact that there is still one person whose job is to be expert in me, the customer, and can bring in a technology specialist as needed when I have the opportunity, that is a good relationship model. So we're keeping that, but we're adding thousands of specialists into our Company who are bringing the depth of domain knowledge we need.

Katy Huberty - *Morgan Stanley - Analyst*

And fair to say those specialists are focused on some of the higher-margin categories that you've entered, both organically and through acquisitions?

Paul Bell - *Dell, Inc. - President Global Public and Large Enterprise*

Correct. Almost all of our -- the nine acquisitions we did in the last 1.5 years and the organic investment we're making are in the higher-value, higher-margin end of the spectrum.

Katy Huberty - *Morgan Stanley - Analyst*

How happy is Dell with the efficiency metrics that you've seen with some of those new salespeople that have been added over the last six months or so?

Paul Bell - *Dell, Inc. - President Global Public and Large Enterprise*

We start by saying you have to look at margin productivity, right? Some of these areas, they're narrow specialization. It's not about a lot of volume. It's not about a lot of revenue. But it's that they are sophisticated projects with very high profit characteristics. And so if we did unit or revenue scaling, it wouldn't make sense, but as a margin lever, it's a very positive trend.

Katy Huberty - *Morgan Stanley - Analyst*

Dell acquired Perot, as we had mentioned earlier, which is a services company with some great specializations in certain markets. Can you talk about some of the successes and some of the challenges that Dell has run into as you've integrated and brought on board that asset?

Paul Bell - *Dell, Inc. - President Global Public and Large Enterprise*

It's going extremely well. We passed our one-year anniversary in the fourth quarter. And we beat all of our milestone objectives for the integration.

I'll start by saying that some of it is picking the right partner. We had done a whole lot of work with Perot. They were culturally the same. They were right up the road in their global headquarters in Dallas, and we are in Austin.

We came in on day one, we said, you know what, this isn't to buy you and then slash your personnel and do a big consolidation. We want all of you to stay and we want to grow the business with you. And so from day one, the two teams were coming together very nicely as a kind of entrepreneurial opportunity.

Secondly, we reverse-integrated Dell services into Perot. So this is a more sophisticated, more broadly capable service leadership because they've been doing a broader range of things. Let's have them run the entire service organization. And something we think is important in this market is that we put all of Dell IT and treat it as a customer of this service organization, so our IT people are in Dell services. They'll do it for Dell, a given project, and then they'll do it for a customer. And then they'll come back.

All of those things have been elements that made it a lot easier, I think, to bring the teams together.

Now the milestones that you asked about were very measurable in that we call them synergy wins. We said Dell had a relationship, Perot had a relationship. Where are we getting new wins that we wouldn't otherwise have been getting, and we had very strong progress on that.

One I don't think I can name yet because we haven't gotten through all the legal stuff, but just from last week a federal government one for about $250 million over five years that Dell had a relationship in, pro services and services capability. It's a long sales cycle. It took most of the year to close that, but we've had a number of wins like that that bode well for the future.

Katy Huberty - *Morgan Stanley - Analyst*

And can you just talk, for those not familiar with the Perot business, which industry verticals Perot focuses on, and what's Dell's strategy to take that business roadmap and replicate it into new industries? When could we start to see the benefit of that?

Paul Bell - *Dell, Inc. - President Global Public and Large Enterprise*

One of the real strengths of Perot is that they really did look at verticals and if people specialized in a vertical market.

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The biggest single one was healthcare, and with Dell being already big in healthcare and Perot being big in healthcare, we're now the world's largest IT service provider to healthcare. And that is a great position to be in because we have relationships that at all levels of that industry, and we are working with them on how do we weave all of it?

We made our first dedicated acquisition for one sector this year, buying a cloud service company for medical image archiving, and one of the reasons we were able to do that is because we have such a presence in that market, it makes sense to make additive investments.

A lot of strength in the federal government piece, which I already mentioned, and in some industrial verticals, including retail and manufacturing.

How we build from here is -- typically, the easiest synergy is where Dell has a deep presence in a market and a lot of knowledge internally, has been doing a lot of integrated solutions within our business, and Perot has a lot of capability but didn't have the vertical sectors. So I'll give you one example. Last -- two weeks ago, I guess it was, we won what is a very unusual deal in an early -- in the K-12 market in the United States, a complete outsourcing deal with the Keller Independent School District.

Now, Perot came to the healthcare business 15 years ago and said outsourcing and large services provision is common in some corporate sectors, and it's not happening in hospitals. And as they consolidate, this is going to be a big business. And they made it a big business.

We look at education now. So Dell has a tremendous strength in education. And some people already rank us the second biggest service provider to education in the world because it's fragmented. Nobody is big yet. And we look at that and say, okay, that's a big opportunity.

We expect to announce our first out -- complete outsourcing contract for a major U.S. university this quarter, too. That one's close to done. And that's an example.

We're working at another commercial and public sectors, but you take where Dell was strong and you bring the services, you figure out how to tailor it in a way that's actually going to add a lot of value to the customers, and it took about the past year to do the product development. What is that service that's going to be differentiated?

Katy Huberty - *Morgan Stanley - Analyst*

Over the last couple of years, Dell has really built out as enterprise solutions into higher-growth and higher-margin categories, and some of the focus areas are systems management, data management, security, and cloud. Can you just talk about, on those four in particular, how happy are you now with that portfolio? Are you done building that out or is there more work to do in those categories?

Paul Bell - *Dell, Inc. - President Global Public and Large Enterprise*

No, we're not done. It was very helpful for our Company, and hopefully for our investors, as we were able, going back a couple of years to our start, to brought a lot of clarity about the domains we were going to focus on and what we weren't, how open, capable, and affordable was really going to play out. It gave us a roadmap.

Then we, of course, built up an internal M&A capability, which is -- right now, I could give a number and size of deals similar to the other large technology companies. Those were very, very important starting points.

Now, we know that we need to continue to bring in best-in-class technologies so it doesn't stop at all. We have a lot of buildout to do, and we're very pleased with how quickly as a company we've built the capability that to find the right targets, do the due

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diligence, integrate the companies well, because if that weren't going well, we wouldn't have confidence in this strategy, but it is going well. And we've seen again and again if we can get a company that has really differentiated best-in-class technology our customers will value and then put it through the powerful distribution engine of having a global sales force of 8,000 people in just public and large enterprise, we can grow these.

But those four domains you mentioned are the focus areas.

Katy Huberty - *Morgan Stanley - Analyst*

The focus areas. How does -- just from a structure and a business process standpoint, how do you decide where to invest? We had breakfast this morning and we talked about how analytics is a big focus here. We talked about is 10 GigE going to be a big opportunity? Dell doesn't have a lot of exposure. I mean, there are 10, 20 opportunities like that. How does Dell decide where to use its firepower?

Paul Bell - *Dell, Inc. - President Global Public and Large Enterprise*

It starts with the domains that we -- you already articulated. So there are technology sectors where we have a lot of capability today, and we have a point of view that says that the architectures of the future that we can start to get to will be very disruptive, very differentiated, add a lot of value for customers, and so we're looking there as opposed to other areas we might look.

And then you say, okay, there is -- this is an industry that is always leaving its legacy behind and go doing its new thing, and that transition is always hard for people. How do we -- instead of build on bigger scale of the legacy stuff, how do we get to a future where people really want to go?

So, give you an example. We've been building up a very large security practice because it was top of CIOs' lists, and we did it out of services. We were architecting features into our products. The Perot Systems group did a lot of work on this across the federal government and healthcare, in particular.

We said, okay, but rather than just build that, what people really want is to leverage the best-in-class technologies, make it easy to adopt, and make sure that they get a great price performance. So we bought SecureWorks, which is a company that's about a decade old, and we said this is the model. It's a cloud service to do what we otherwise could have architected on premise.

That kind of thing -- great company with great financial performance and great customer loyalty, but I use that as an example of where you kind of shoot ahead of the duck, so to speak. So where is the industry going to go and how can we build the scale around the core technology?

Katy Huberty - *Morgan Stanley - Analyst*

So I guess from one angle, you could argue that Dell not having a lot of legacy on the enterprise side, coming from being a PC business, there's not a lot of legacy businesses where you have to eat your own young. You can actually just start fresh with the right -- the new technology and drive growth from there.

Paul Bell - *Dell, Inc. - President Global Public and Large Enterprise*

Yes, that's played out again and again, I mean, as Dell largely grew, or almost exclusively grew, organically through the first 24 years of our history.

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But if you think about the conversations I was having when I was running Europe 10 years ago, where we were saying, no, really, you can run a large enterprise all on x86 on Linux. We are doing it. We're a $30 billion-plus Company, and a lot of our customers were still kind of in a legacy architecture.

Now they think that's a quaint thing. They've sort of moved on. It's always finding that next thing, and saying, okay, there are disruptions in business model as well as technology that mean that you can find a much higher ROI than what you've been doing out of the legacy.

Katy Huberty - *Morgan Stanley - Analyst*

Some of the recent acquisitions, you know, Kace, EqualLogic, you could argue Compellent, their initial focus was smaller and medium-sized businesses or enterprises. Do you feel like you can take those technologies and scale them up into the customers that you address?

Paul Bell - *Dell, Inc. - President Global Public and Large Enterprise*

Absolutely. And keep in mind, my customer base starts at 500 employees. So we have -- we have that sweet spot as well.

We talk a lot about optimizing solutions for the middle market. And what we mean by that is not that they are not great for very large organizations, but it means if you are optimized for the middle market, they have to be extreme on ease of use. Because the thing about middle market is they just don't have the depth of specialized IT talent. They don't want a solution that works turnkey.

That's where EqualLogic was really good. That's where Kace as a systems management appliant was really good. So those companies as small startups were kind of focused on the smaller accounts that they kind of knew how to get to.

When we took it to our existing installed base of large accounts, we said this is what the technology can do. NASA, for instance, implemented Kace for something like 90,000 seats. And they said, well, we actually organized them 5,000 seats at a time, and so they kind of look like a collection of medium enterprises.

So we took EqualLogic into very large enterprises and said, I know you have a fiber channel network, but there's going to be some parts of your new storage architecture that you might as well reuse your ethernet network with iSCSI. And you're talking about an office that is not your headquarters. They don't have a huge storage staff. Let's implement this because it's very, very easy to operate. That message works in very large organizations. Everybody is looking for ease of use wherever they can find it.

Katy Huberty - *Morgan Stanley - Analyst*

As it relates to storage, and this is an area where you have invested, you recently closed the Compellent acquisition, but how should we think about EMC, one of your partners in storage, starting to focus more on non-Dell channel partners? How will that influence revenue growth in storage? And then, we can talk about how it influences margins.

Paul Bell - *Dell, Inc. - President Global Public and Large Enterprise*

Yes, this is a continuation, but an acceleration, of what's been going on since we bought EqualLogic. EqualLogic would go head to head with EMC, so we were competing, but in other areas we were selling other EMC technologies still, so it's a cooperate -- it's the co-opetition thing that we all know well in the IT space. That will accelerate now.

We think -- Compellent has actually migrated a lot of customers from other kind of legacy software architectures onto Compellent over time. We'll be going more head to head with EMC, offering choice to our customers. They have relationship with our customers. We do, too.

One of the things I would say that I appreciate from their leadership that we are committed to, too, is I think we really are looking at the customer first. We have a lot of existing customers who buy a lot of equipment and service from both accounts, and our first message to them is we're going to take care of you. Over time, you'll get some more choices for what you want to buy next, but for now, we are committed to making sure that it's a good transition for them.

Katy Huberty - *Morgan Stanley - Analyst*

And on the margin front, in the EMC partnership, you were essentially earning reseller-like margins, and now that you own more of your own technology, you enjoy the margin that other storage vendors do. How significant has that been in moving the margin needle? Can it continue to move the margin needle as we go into this year? And any quantification or general comments on how different the margins are between the old -- the EMC business versus your new business.

Paul Bell - *Dell, Inc. - President Global Public and Large Enterprise*

Yes, I can quantify it by saying extremely. You're absolutely right. There is reseller -- we are kind of higher end of that because we did some more joint development of solutions. But, kind of reseller margins, and now kind of think of the industry-standard margins on the -- for owning storage IP.

If you've watched the swapout we've been doing, which is EqualLogic growing at a very torrid rate, it was about $100 million company when we bought it. It's kind of done about $800 million now, since we -- actually, over $1 billion now, I guess, since we've bought it. So, it was very, very high rates of growth, and that was swapping out for what we had historically done with EMC. That will happen again.

So, for the last few years and probably for the next year, you'll see the revenues be relatively flat, but it's a dynamic shift in what it is we are selling and it's been one of the main margin engines for the Company for the last couple of years.

Katy Huberty - *Morgan Stanley - Analyst*

If you look at -- just on that point, if you look at Dell non-PC revenue, it's relatively flat as a percentage of revenue today versus a year ago, and so at face value you wouldn't really see a mix story, but as we discussed, within storage there is a margin mix or a composition mix of that revenue. Are there any other areas within Dell's business that maybe you won't see a big shift in the overall revenue size, but within that, the composition is changing?

Paul Bell - *Dell, Inc. - President Global Public and Large Enterprise*

Yes, all over the place. Servers, for one. There's a lot of just volume -- the low end of the server business is kind of like the PC business, but the real data center solutions and where we have been driving complete virtualization projects around people's server, storage, and networking architectures altogether, that type of work is typically bringing much higher end -- higher spec'ed servers, so the price per unit of our servers has gone up dramatically. So it's not just been a unit play so much.

Even in the client business, as we get more involved in delivering complete integrated solutions for people, we are less likely to take that kind of reverse auction bid on just a lot of units. We just don't do that as much anymore. An example would be in school districts, which people always thought of as people with the least money and they're going to be cheap and you're not going to make any money off them. As we have integrated and added more value, integrated what we call connected classroom

or connected campus solutions, which is everything from their data center out through their wireless network to what happens in the classroom, that client business can be profitable because we've earned it by adding a lot more value.

So even within the client business, we've been selling a lot more of the high-priced [band] product within our public and large enterprise organizations.

Katy Huberty - *Morgan Stanley - Analyst*

You talked about ASPs moving higher in servers. If you look at units, Dell did see some unit market share the last couple of quarters. Is that a function of a competitive change, or just a function of where you're choosing to do business?

Paul Bell - *Dell, Inc. - President Global Public and Large Enterprise*

The way we -- the best data we can get on revenue share, we're doing fine on revenue share, as we've continued to go to the higher value-added end, our margin growth is even faster than revenue, so I think on a profit pool share, we are probably doing fine.

And that's really the way we try to think about it. The unit charts are interesting, but it's, are we winning more of the kinds of engagement where we're the critical IT partner and we're driving the sort of high-value engagement that will pay out over a long period of time? That's -- so we really track account share and share of wallet as what really matters in the enterprise end.

Katy Huberty - *Morgan Stanley - Analyst*

And ASP has started to surprise upside. I think it was the fourth quarter of 2009, so this trend has occurred for many quarters now, and what seems to be driving it is more fully configured servers that are going into virtual environments needing more memory I/O performance. Is there -- where does that top out? Is there any line of sight into when, whether large enterprises adopting virtualization? Is there more opportunity for ASP lift in emerging markets and small/medium businesses? Essentially trying to get at, was this a 12-, 18-month phenomenon, or does it continue into the next year or two?

Paul Bell - *Dell, Inc. - President Global Public and Large Enterprise*

Yes, I think it can continue. But before long, when you watch what's really happening in the trends out there, it gets less and less about the standalone server device choice anyway.

What we are starting to see is sort of the beginning of the transition here, as it is indicative, that we sell a lot of our infrastructure and storage and servers as a combined pool. When we manage it with the infrastructure software we acquired when we bought Scalent earlier this year, and that is taking Dell storage, typically EqualLogic, Dell blades or other services, some of Dell networking capability, and it's really orchestrating across all of that. So the product is now that whole stack, including the services to implement and get it up and running.

That's still a small percentage of the business, but it is where it's clearly going and the direction, so you start to think more in terms of a modular data center -- it might just be a rack for some people -- but all the way up to these containerized data centers we built for a number of customers where they don't really talk so much about the individual ingredients. They talk about how that whole architecture works.

Katy Huberty - *Morgan Stanley - Analyst*

We talked a lot about the enterprise and more of the data center products. Just to spend a minute or two on the commercial PC business, do you have a sense for what inning we are in in the PC refresh, the corporate PC refresh that's been driving unit strength in the markets?

Paul Bell - *Dell, Inc. - President Global Public and Large Enterprise*

If we're thinking about it as sort of an ongoing cycle which lengthened in -- what basically happened in the big recession, everybody just said, well, I know it makes sense to migrate to the next OS or to upgrade to some of my apps and I'm going to need some new equipment, but I think we'll just take a pause on that.

So the cycle lengthened, and this year everybody did a lot of catch-up. We began to see Windows 7 migration, which still has a long way to go in the enterprise. It's still really just beginning.

I think what you see now is that this whole discussion is brought together around, okay, what is the future of end-user computing in my enterprise? What mix of devices do I want to have?

And one of the things I don't know that people understand real well is we reengineered our supply chain over the past three or four years to do a fundamental -- a couple of fundamental things. One was the major cost reductions, which are now starting to show up in our margins. The other thing was the speed and flexibility of development to be able to get purpose-built end-user devices to enterprises.

I'll give you an example, so you know what I'm talking about. We developed -- when the netbook craze hit, we developed a tailored netbook for the education market with a rubberized exterior and things that would make it tough and a bunch of education features on it that sold for the same margins or slightly higher as our corporate notebook. We were able to get it from conceptualization into the market in about six months.

That is increasingly important. As people think about refresh, they're really thinking about, okay, I'm not just necessarily going to upgrade to the faster speeds and feeds and I'm going to do the next migration of the OS and apps. They're really thinking, how am I going to rearchitect this, and it's creating in some cases client virtualization projects for us, in other cases service and architecting work out of our mobility and mobile apps practice that we've built.

Katy Huberty - *Morgan Stanley - Analyst*

A couple of companies at this conference, including Motorola, Salesforce.com, Ingram Micro, have talked about being surprised or expecting the market to be surprised by the uptake of tablets in the enterprise. It seems to be happening much faster than, for instance iPhone or Android smartphones penetrated the enterprise. What are you hearing from your customers as it relates to the demand of those solutions, but also what are the problems that they are turning to Dell to solve in order to get there?

Paul Bell - *Dell, Inc. - President Global Public and Large Enterprise*

Very high levels of interest in that. Just about everybody is toying with them, trying them, et cetera, et cetera. Whether that's a surprise in the volume or not depends on people's view of the volume.

We are pretty bullish that we think this is -- will have a real use case. I think -- here's the questions we hear from CIOs, and I talked to a lot of big bankers in New York last week about them, particularly, using this, so some of your firms probably, but they -- everything -- first of all, there is the security and manageability issues. We have been architecting more and more to this mode

where people can work from home on any device, and so we know that can work and that's a good thing and that provides flexibility.

At the same time, we've got to make sure as we move into a whole new class of devices that we thought through security and manageability, and we can, and a lot of our initial projects with people are on how to do that.

Second thing they get into is they're thinking about, okay, really what is the enterprise productivity use case? When I say, who are the first people who will use this in your company? They usually say, oh, you know, the CEO or the senior executives. I say, okay, fine, but what are you really going to do with it as opposed to it's the e-mail and scheduling and content device because that is as far as it's gone with a lot of people.

But some enterprises are really thinking through how to fundamentally rearchitect how certain productivity tools can use these sort of tablets. To give you an example, this device is (technical difficulty) small tablet. It's our Streak five-inch, which we've had out. We have the seven-inch version of it out, and we have an auto manufacturer that was using it -- that looked at it and said, this is so much more than what a PC was or what a smartphone was. You combine location awareness, with video, with voice.

What they did was create a solution for their maintenance workers. They put a little sleeve pocket to shove the thing in, and said if you see something on the line you don't know how to do, take a little video of it, send it back up to the headquarters, and they would send you, download you a little video to view on how to fix it, and with GPS they'd show you where on these massive campuses to go to get the spare part you need.

Okay, that's clever. That was pretty good. Until you had the combination of those features in the device, you weren't even thinking about that use case. So, is the tablet or the smartphone in the pocket going to be just sort of the way people are using in the consumer model, which is powerful enough, or will we do tailored applications?

We are working very heavily in the defense industry on specific applications for how that could work for the war fighter, for instance. And that is as much in what's on the back end as what's running on the device itself. But that's where you get the breakthroughs, when enterprise says I know this use case for that for that employee and it's going to be very productive for them. That's why I'm going to put real money behind it.

Katy Huberty - *Morgan Stanley - Analyst*

When you talk about adoption in financial services or defense categories where security is probably the most important -- or the thing that keeps those CIOs up at night, and you tie that back to the various platforms that are available, Android is open, which seems to be good for the consumer, at least up until this point. Others are more closed and controllable. What are you hearing from enterprises as it relates to how they view the various OS platforms based on their security concerns?

Paul Bell - *Dell, Inc. - President Global Public and Large Enterprise*

Yes, and it's one of the elements that come together. Our roadmap is going to give people a lot of options within Android and Windows Mobile.

And so, you've got -- people are saying, well, I understand how to manage and secure within a Windows architecture. This can be an extension to what I'm doing. That might lead them down one path.

Other people are saying, well, I really have valued what my early development of Android apps has created. I've got users that are creating great stuff that we can use in the enterprise, so I'm going to work with you, Dell, on a way to secure and manage that. So, our view at this point is to have choice and keep working on finding what those best integrated solutions are.

Katy Huberty - *Morgan Stanley - Analyst*

This has been a topic in the consumer market, less so in the enterprise market because I think most of the conversations are proof of concept and not yet big purchases, but in the consumer market what has happened is tablets are either delaying PC purchases or, in some cases, replacing them, but it's mostly a delay or you only have so much money to spend, and if you are buying these mobile devices you might not be buying a new computer this year. Have you heard any thoughts as to whether tablets are just an incremental device and all additive, or are they also influencing the spend on PCs, whether it's true cannibalization or thoughts about do we move to desktop virtualization and extend the lifecycle as all these devices are used more on a mobile basis?

Paul Bell - *Dell, Inc. - President Global Public and Large Enterprise*

Right now, the best I could tell you is sort of sentiment because so far there has not been a lot of purchase of these devices by the enterprise for the enterprise.

There is consumerization where people bring them to work, and as they look forward -- I will tell you something that might actually surprise you. We've seen remarkable growth in desktops this year. Okay, now if we were having this conversation a few years ago, we would have said, okay, you know, mobility grows forever, desktops are going to start shrinking, and at some point tablets will come in and they will go to the next level.

But sometimes these trends can surprise us because what happens is people get into that combination of devices, which is the way their worker is expected to be productive, and it really is a combination of devices. So is that going to mean that these are additive net or will they substitute for some notebooks? The kinds of people in this room and the kind of people we see on airplanes are actually the first group that would substitute because we're more the consumers of information, in many cases, and so you see a lot of that substitution to tablets.

A lot of these thousands and thousands of employees large enterprises have are working in some kind of producing data model, and so how that mix comes, we don't really know, but we are going to be providing both the devices for each one of those form factors and the solutions which typically are anchored in the data center, first, for how you run all of these options for your users.

Katy Huberty - *Morgan Stanley - Analyst*

Right. I'll ask one more question, then we'll open it up to the audience. This is a question that I've gotten from investors as it relates to betting on Dell's enterprise strategy, and it has to do with your R&D spend versus some of the peers that you are combating every day. Dell's R&D spend is in the $600 million, give or take, range. If you look at HP, Oracle, Cisco, IBM, they are spending $3 billion to $6 billion a year. And so, in that context, how do you explain your ability to really differentiate and compete while spending far less money on technology?

Paul Bell - *Dell, Inc. - President Global Public and Large Enterprise*

First of all, one of the fastest growth items in our spending is research and development, and so that is going to change dramatically.

Ultimately, though, the winning or losing is going to happen as to whether our solutions that we bring to market are really differentiated or not. One of the nice -- you already made the point earlier about the role of the legacy. This R&D is heavily focused on the kind of architectures that are driving the new growth in the industry that are maybe nascent technologies today, but could be quite a bit of scale in four or five years. Some of the large numbers in other companies are going to the big legacy

they've been doing for a long time. And there's no question, though, that we will continue and need to continue to develop more of our own IP, acquire more assets to bring it with them, so you'll expect to see R&D grow dramatically in Dell.

Katy Huberty - *Morgan Stanley - Analyst*

So on that front, I know you're not looking at the entire Company from a financial perspective, but just philosophically, do we see the investments in R&D and the incremental sales resources, do we see that bucket of OpEx grow faster than revenues, or do you make sure the Company is positioned well to succeed, or do you think you can still show operating leverage despite those investments?

Paul Bell - *Dell, Inc. - President Global Public and Large Enterprise*

I would expect to see, certainly in the enterprise business, for sure, operating expenses growing faster than revenue, but margins growing faster than that, so the idea is how we generate the cash and operating income growth as a higher-margin, higher up OpEx mix of product.

Katy Huberty - *Morgan Stanley - Analyst*

So it goes back to the composition of revenues driving higher gross margins, which allows you to invest in R&D and sales.

Paul Bell - *Dell, Inc. - President Global Public and Large Enterprise*

Exactly right. So if you see, last year -- each year will have its own combination of factors, but last year there was revenue for growth again. A lot of that was sort of the recovery growth, along with the market, but you had margins growing faster than revenue and operating income growing faster than that. That's our goal.

Katy Huberty - *Morgan Stanley - Analyst*

Let me stop there and see if there are any questions in the audience. Any questions back there?

QUESTIONS AND ANSWERS

Unidentified Audience Member

Earlier this week, Intel was talking about cloud [putouts] in their presentation, and I believe they said almost 50% of the cloud data centers are using white box servers. That's obviously the fastest growing part of the market, and I think they even mentioned that some of them may be -- lower than top three server vendors were growing faster than the market, so I guess my question to you is, are you seeing increased competition there? What is kind of the competitive dynamics in that market?

Paul Bell - *Dell, Inc. - President Global Public and Large Enterprise*

Yes, if you start by the most visible end of that market, which is the 25 largest Web 2.0, hyperscale data center companies, we are in 22 of the 25.

They are U.S. concentrated, but Baidu and [Tienchin] and China are on that list as well. And when we created a group in Dell called Data Center Solutions four years ago, we were finding it was mostly white box or small company. And we were doing

the kind of corporate infrastructure, and we found in this sector the big branded players, including us, weren't very relevant at all, and so we built that practice as a completely different business, which I've been told, I think this is right, that DCS within Dell would be the third-largest server provider in the United States now if it were an independent company. So, it's a huge business for us and has focused heavily on those top 25.

Our differentiation was really around engineering where we were driving some very innovative solutions all the way up to the containerized model that some are using and others are still developing, that we were able to differentiate. We put a lot of investment in having the A-Team in that.

Second was our supply chain. A lot of these companies are in very competitive high-growth situations. Time is of the essence, and our ability to do some complex projects for them has led to a lot of growth there.

So I don't doubt that the white box or smaller -- and it's not necessarily a fair characterization. There are some great companies in there that have great technology, but maybe they're not as globally known. That they've focused on this sector makes sense, but it's continued to be a really strong business for Dell that's still growing.

What you will -- we'll have to see, if you follow our server share, you might be -- it's really lumpy, so you'll have a huge quarter that will lift our entire server business, then it will go down because that is such a big part, and they might order -- we've had customers order 50,000 servers in one order. That's enough to shift the trajectory.

Katy Huberty - *Morgan Stanley - Analyst*

Great. We've actually run out of time, so we're going to wrap it up there. Paul, thank you very much for your time.