

DELL, INCORPORATED
Moderator: Lynn Tyson
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Operator:

Good afternoon and welcome to the Dell, Incorporated First Quarter Fiscal Year 2009 Earnings Conference call. I'd like to inform all participants this call is being recorded at the request of Dell. This broadcast is the copyrighted property of Dell, Incorporated. Any rebroadcast of this information in whole or part without the prior written permission of Dell, Incorporated is prohibited. As a reminder, Dell is also simulcasting this presentation with slides at www.dell.com/investor.

Later we will conduct a question and answer session. If you would like to ask a question during this time, simply press star, then the number one on your telephone keypad. If you haven't already done so, please press the pound sign now, then press star, once again to ensure that your question is registered.

I'd like to turn the call over to Ms. Lynn A. Tyson, Vice President of Investor Relations. Ms. Tyson, you may begin.

Lynn Tyson:

Thank you. With me today are Chairman and CEO, Michael Dell and Vice Chairman and CFO Don Carty, and I'm very pleased to introduce Brian Gladden as SVP and our incoming CFO. Don will review our first quarter results. Brian will make a few comments and then he'll turn the call over to Michael, who will cover our strategy and progress on our long-term goals.

And then we'll move on to Q&A - and as the operator noted - there is a new procedure that's been implemented by our conference call provider and you will only be able to queue up for your questions at the end of the prepared comments.

Please make sure to review our web deck on dell.com/investor for additional information on our results. And as we mentioned last year, starting this quarter we now have four new external

reporting segments: America's commercial, EMEA commercial, APJ commercial and Global Consumer.

Prior to this quarter we had three segments: Americas, EMEA and APJ, and we broke out U.S. Consumer. So you can easily update your models, our earnings release and webdeck contain a table that has Fiscal 2008 quarterly revenue and operating income broken out by the new four external reporting segments.

Also, any references we make to Dell's unit growth as a multiple of the growth of the industry excludes Dell, and all growth rates are year over year unless otherwise noted. Please visit us at Dell Shares, our IR blog on dell.com, where you can ask questions and find timely information on our business and our strategies.

In late June we will post a V-log featuring Brad Anderson, our Senior Vice President and head of our enterprise business. Brad will take you through our virtualization strategy, and if there are any specific questions you'd like us to address in the V-log, please let me or my team know.

On July 18th we will host our Annual Meeting of Shareholders in Austin, Texas, and our Q2 earnings call is scheduled for August 28th at 4:00 P.M. Central Daylight.

Finally, I'd like to remind you that all statements made during this call that relate to future results and events are forward-looking statements that are based on our current expectations. Actual results could differ materially from those projected in the forward-looking statements. Because of a number of risks and uncertainties which are discussed in our annual and quarterly SEC filings, and in the cautionary statement contained in our press release and on our website.

I'd now like to turn the call over to Don.

Don Carty:

Thanks, Lynn, and good afternoon. A year ago almost to the day, we laid out for you the five actions that we were taking to transform the company and restore our competitiveness, reignite growth and build the solutions that we believe were critical to customer needs.

Those five actions were: restructuring the organization to move decision making closer to the customer; improving customer satisfaction; introducing new innovative products across our entire portfolio and across all our regions; globalizing services which at its core simplifies IT for our customers; and a comprehensive review of all costs with the goal of streamlining structure,

eliminating bureaucracy and better aligning expenses with the business environment and our growth opportunities.

I think our results this quarter demonstrate we've made some progress, although there's still a lot more to be done. Driven by a more robust and targeted product portfolio, we had unit share gain worldwide in all major product categories and, of course, in all major regions.

A couple of examples - worldwide consumer units were up 47 percent. In APJ and EMEA commercial units were up 31 percent and 30 percent, respectively. Pretty importantly for us in the key so-called BRIC countries, where over 40 percent of the industry growth will come from in the next five years, we outperformed all major competitors across all product categories. We had revenue up 58 percent on a 73 percent increase in units.

And for us, BRIC now stands at close to nine percent of our revenue mix. And I should add our revenue mix from outside the United States reached a record high of 50 percent.

On the OPEX front we had our best OPEX scaling versus revenue growth in over two years. And OPEX dollars actually declined sequentially against an increase in both units and revenue. Our headcount is now down year over year by 7,000 excluding the impact of acquisitions. I think now well within striking distance of the 8,900 target that we talked to you about a year ago. As we said in April, we believe we have opportunities to reduce our headcount even further.

We improved operating income margins sequentially and, importantly, we drove a 12 percent increase in earnings per share. Last year we said that the transformation of our company would take about 18 months to take hold. I think these results are evidence that our strategy of trying to reignite growth as a first step was the right one for us.

And now with our sights firmly on improving our competitiveness, we are really beginning to realize the benefits of some of the cost initiatives that we've talked to you about. As I take you through our results in more detail, you'll see that some aspects of our business have improved growth, some have improved profitability and some have both.

We're very confident as we continue to execute against our growth strategy that all aspects of our business will benefit and contribute to an optimized balance of liquidity, profitability and growth for the company as a whole.

Let me turn to our first quarter results in more detail and then I'll make a couple of comments about our outlook for the balance of the year.

In the first quarter we generated \$16 billion in revenue, a nine percent increase on a 22 percent increase in units. That's obviously our fastest growth in units in over two years. On a regional and channel basis, the growth in units was driven in large measure by emerging countries. It was also driven by our retail initiatives. On a product basis, the growth in units was driven by a 43 percent increase in mobility products.

Operating expenses were down 100 basis points sequentially to 12.9 percent of revenues. Operating income was \$899 million or five-and-a-half percent of revenue resulting in earnings per share of thirty-eight cents. Consistent with what we've talked to you about and what we did in the fourth quarter of last year, we have included in our earnings disclosure table some quantification of the impact of certain items that are in our GAAP results.

So let me just briefly just touch on those and give you an indication of what lines of our P&L you'll find the impact on. We had \$106 million in expense which amounts to four cents a share that related to our ongoing efforts to realign our business, and includes largely severance stocks and facility closures. By way of reference, \$82 million of that \$106 million shows up in our OPEX.

We had \$26 million or one cent per share in the amortization expenses of purchased intangible assets associated with the acquisitions we did. That \$26 million ends up getting split about evenly between COGS and OPEX. We had \$19 million in expense or one cent a share in investigative-related costs and all of that expense as it has in the past falls into the OPEX category.

We had a \$42 million increase in financing and other income, or two cents a share related to an error in currency exchange rates from prior periods. We had a \$46 million or two cent a share reversal in the provision for employee bonuses for Fiscal 2008. Most of that, although not all of it, is in OPEX.

And we had a reduction in a litigation reserve related to a favorable ruling in a patent case of \$55 million or two cents a share. All of that is in the COGS line. I should, I just mentioned by way of reference, we've been talking about investigative-related expenses kind of every quarter. To keep you up to date on that, that number is starting to drop to a smaller number, and I think we'll

probably drop a little further in the next quarter. I think it's small enough now that we will quit identifying it separately in future quarters.

Our cash flow from operations was \$143 million. Cash flow was impacted by slightly lower payables, but largely because the first quarter is the quarter when we have some significant outflows of cash associated with tax and associated with bonus payments.

Our ability to generate cash remains very robust. I think it's evidenced by our trailing four quarter cash flow from operations of \$4.2 billion. And we believe on an annualized basis, we can still easily generate cash flow from operations in excess of our net income.

We ended the quarter with \$9.8 billion in cash and investments. In the quarter we spent \$1 billion to buy back 52 million shares. That's driven our weighted average sharecount down to 2.04 billion; that's a 10 percent reduction versus Q1 of last year. Our share count actually finished the quarter at 2.02 billion, and this quarter we expect to spend at least \$1 billion on share repurchase.

During the quarter we raised one-and-a-half billion in private placement debt for general corporate purposes and we paid off \$200 million in debt. Relative to F&O, I do want to point out that we think our run rate F&O will be in the \$20 to \$30 million range per quarter, driven by the reduction in our cash balances, which of course are earning lower yields as well. And we have increased interest expense that's driven by that higher debt balance.

Our cash conversion cycle, which declined versus last year, was negative 30 days - driven by increases in DSO and DSI and a slight decrease in days payable outstanding. We expect our cash conversion cycle will remain significantly negative and we believe that for this year it will generally be in the 30 day range or better, reflecting in part our entry into the retail channel, and on the inventory side some strategic buys we've been making as we've moved through the year.

Our return on total capital for the quarter was 42 percent.

Let me turn to some regional and product highlights. In APJ commercial, our revenue is up 19 percent to two billion on a 31 percent increase in units. Operating income was up 52 percent on a very balanced country segment and product performance. In fact, revenue in India and China grew at 52 and 30 percent on a 68 percent and 43 percent increase in units, respectively.

This performance drove share gains in both countries, highlighted by India - where our commercial units grew at significant multiples of the market and we increased our share position by a full four points. And we also claimed the number two share position in servers.

Global consumer revenue was up 20 percent to \$2.9 billion on a 47 percent increase in units. And while off to an admittedly easily compare, profitability did improve and we did talk a little bit about that when we were on the call last quarter. It now stands at 1.2 percent of revenue. On a unit basis, we grew at over two times the industry and we increased our global share by 1.2 points, to 8.8 percent.

We expanded our global retail presence adding Suning in China and Costco in the United States. We now have over 13,000 points of presence. In addition, we continue to develop products that have more competitive features, more design, more cost points and while we still have a lot of work to do in the consumer business, I think we're all comfortable with their performance and their progress in Q1.

Turning to EMEA commercial, revenue was up 15 percent to \$3.8 billion on a 30 percent increase in units, with the fastest growth in the industry among vendors, server units were actually up 20 percent, two-and-a-half times the rate of the industry.

Growth in notebooks also outpaced the industry with a 59 percent increase in units. From a country perspective, units were up 20 percent in the U.K. and the region saw strong double-digit growth in several emerging countries like Russia and Turkey and the Ukraine.

Profitability in EMEA was adversely impacted by a favorable warranty change that actually helped Q1 of last year, but perhaps more importantly, a significant severance charge that was part of that \$106 million that I talked about earlier in Q1 of this year.

In our Americas commercial business, revenue increased one percent to \$7.3 billion on a three percent increase in units. Server shipments rose by 20 percent, more than four times the rate of the industry. Our mobility products were up 11 percent and desktops declined two percent.

Operating income declined as the business absorbed acquisitions and invested in sales capability, particularly in the emerging markets in Latin America and I might add in sales capability associated with our storage products.

Similar to Q4, we continue to see conservatism in the U.S., especially in the financial sector as well as state and local governments, and as well in the small and medium enterprise space. I just touched briefly on some product highlights - in client, mobility units up 43 percent as we grew at a premium to the industry and that drove a 22 percent increase in revenue. We also grew at a premium to the industry in desktops with a nine percent increase in units, which drove a five percent decline in revenue.

Growth in enterprise products and services accelerated very nicely in the quarter. Server revenues were up four percent but on a 21 percent increase in units, our fastest unit growth in over two years and three times the rate of the industry and that allowed us to gain one-and-a-half points a share in the quarter.

Our storage revenue jumped a very solid 15 percent, driven by strong growth from our Power Vault direct attached products and a full quarter now of EqualLogic. Our enhanced services revenue was up 13 percent, aided by the first full quarter of our new ProSupport offerings. Our services attach rates increased by 24 percent and a key leading indicator of services growth – our deferred services revenue balance grew 23 percent to \$5.4 billion.

Software and peripherals revenue increased 17 percent. As a result of our ASAP acquisition, S&P growth was aided by strength in software resale and in the licensing business associated with that acquisition.

During the fourth quarter we spent \$170 million net of cash, sorry during the first quarter we spent \$170 million net of cash acquired of acquisitions closing on two: MessageOne and The Networked Storage Company.

Lastly, our strategic assessment of our financing business, DFS, continues. We should have an update for you by the third quarter. As you will see when we file our 10Q in early June, this financing capability continues to be a key enabler of sales for our U.S. businesses, especially consumer direct. And we believe we are very nicely and adequately reserved against the backdrop of what's happening in the credit markets.

In sum, I'm really quite pleased with our performance in the quarter. I believe we're on the right trajectory to meet the long-term targets we set for you in April, which are to grow faster than the industry while generating sustainable EPS and cash flow growth.

Now before I turn it over to Brian, let me just make a couple of observations about our outlook.

There are a few items you should consider as you think about our performance over the balance of the year. First we will continue to incur costs as we realign our business to improve competitiveness, reduce headcount and invest in infrastructure and acquisitions.

Second, we are seeing conservatism in IT spending in the U.S. and that has extended modestly from global and large customers into public, small and medium business accounts. And we expect that to continue through the summer particularly, as many of these customer segments are seasonally slower.

Third, you will recall that we are overlapping a period of record cost declines in the same period as last year. Fourth, we will continue to benefit from improving performance in areas like emerging countries, notebooks, enterprise, and services which collectively are driving a more diversified portfolio of geographies and products.

Against this backdrop we recently shared with you our plans to improve our competitiveness and we are targeting three billion in annualized savings by fiscal 2011. Long term our focus remains on growing units faster than the industry, improved profitability and superior cash returns with a focus on making decisions that deliver the best long-term results for our shareholders.

Now I personally couldn't be happier to introduce Brian Gladden. All of us at Dell are delighted that we were able to attract to the team someone with Brian's operational and financial background. As you know, Brian joined Dell last week from SABIC Innovative Plastics Holding BV, formerly of course, GE Plastics. There Brian was President and CEO, and prior to that he spent nearly 20 years at GE where he held a variety of financial and leadership roles, including VP and GM of GE Plastics, CFO of GE Plastics, and CFO of GE Medical Systems, Healthcare IT business.

Brian will formerly take the reigns as CFO on June 13th, 2008 at which time I will happily move back to director-only status. Brian...

Brian Gladden:

Thanks, Don.

On behalf of the company and our shareholders I'd like to thank you for the outstanding contributions that you've made to the organization as CFO for the past 16 months, not to mention your board tenure of 16 years.

Your personal commitment to integrity, transparency and accountability has set the bar for the entire company. We look forward to your continued leadership on the board.

I'm now nine days into my new role here and I'm ramping up quickly on Dell and the industry. Don and I are meeting regularly to discuss the organizational priorities and challenges. And I'm quickly integrating into regular operating rhythmus and bi-costly – bi-weekly cost meetings. And I'm pleased with where we're headed.

I feel strongly that a world class finance organization is built around four key imperatives. First, controllership and integrity must be at the heart of everything that we do. Second, we must be operationally engaged in business partners that help drive growth and profitability.

Third, we must engage with and respond to you, the owners of our company. And finally, we must be good stewards of our company's capital. Making decisions that maximize cash returns and drive long-term value creation.

I look forward to meeting with you in the coming months. I'm very open to your ideas, concerns and feedback. This ensures that we, the Dell team, have the right priorities and plans to capture the incredible opportunities in front of us.

Let me now turn it over to Michael.

Michael Dell:

Thank you, Brian, and welcome.

In April, I laid out long-term goals to drive shareholder value, including unit growth at a Premium to the industry, executing on our \$3 billion cost opportunity, delivering sustained EPS growth, and executing on our five core initiatives; and also growing our retail end channel for scale and profit.

We grew significantly faster than the industry on a worldwide basis and this was despite a more conservative commercial IT spending environment in the United States. We targeted three billion in annualized cost savings and have started to make progress and are beginning to see positive results in our performance as cost savings begin to flow through the P&L during this quarter.

Let me go into a bit more detail. First, we grew faster than the industry worldwide in all major product categories and regions. And it's been three years since we had accomplished this. Worldwide, we grew units 22 percent while the industry was up 14 percent.

Looking at our major regions, we grew 11 percent in the United States while the industry was essentially flat. In APJ, we grew over 42 percent while the industry was up just 14 percent and in EMEA we grew 28 percent while the market was up 19 percent. This marks the first time in two years that we've outgrown the industry in all major regions.

On the product side, in notebooks we grew 43 percent while the industry was up 36 percent and in servers we outgrew all major competitors with a 21 percent increase in units while the industry grew seven percent. In desktops we were up nine percent, while the industry contracted in the quarter. And in storage our growth in revenues accelerated to 15 percent.

On the cost side, we've identified and are aggressively targeting COGS and OPEX savings and I continue to lead meetings every two weeks for each focus area. We have detailed road maps, targeted savings, actions, executive ownership with accountabilities, and specific timelines for the capturing of savings.

In the first quarter we made progress against our initial goal of reducing headcount by 8,900. Year over year we reduced our headcount before the impact of acquisitions by 7,000, which includes 3,700 just during this past quarter. In our first quarter we recognized \$106 million in severance and facilities related expenses and we'll see more benefits as we fully move throughout the year.

We also made adjustments to our compensation plans including evaluating and aligning our long-term incentive plans, both cash and equity, to current market conditions. Our total operating expenses were down seven percent sequentially and while we still have much to do, I'm encouraged by the progress we've made.

I believe you'll see additional productivity improvements in the form of OPEX scaling and some additional headcount reductions even as we invest significantly in growth areas.

Turning to products, we grew faster than the industry in every worldwide product category. In the enterprise, which is a core initiative for us, we had particularly strong results. In January we launched nine new servers, including the M600 and M605 two socket blades and the M1000E blade enclosure, the R805 and R905 virtualization optimized servers.

In addition, we're a leader in disruptive solutions for "The Cloud", powering about half the fastest growing Chinese internet companies, as well as the largest portal and largest search engine providers in China. These launches combined with our existing leading edge server lineup helped us grow more than eight percentage points faster than the industry and gain one-and-a-half share points worldwide.

In storage we grew revenues by 15 percent and based on our own estimates, we again took share worldwide in Q1 with the launch of the Dell EqualLogic PS5000 series IP SANs and our Dell/EMC AX4 and 5i SANs, we extended our position as the number one worldwide provider of iSCSI SAN solutions.

Finally, our emerging countries initiative had strong results. Recall that we define emerging countries as BRIC plus 10 and the combined 14 countries grew units at 62 percent and revenue accelerated to 47 percent, led by strong share gains in Brazil, India and China.

During the quarter we also launched the Dell 500 notebook, which was specifically designed for emerging countries. We're now shipping this in China and India, and will launch additional countries as well as we catch up with the phenomenal demand that we're seeing for this product.

We also launched our Partner Direct program in Europe and APJ this quarter. And since we launched the program in the United States in the fourth quarter we have added over 3,500 new global partners. And our channel business is now on a \$12 billion run rate.

While I'm encouraged with our progress, we still have much work to do to restore our competitive position. But over time, I am confident that our broad long-term goals – which include our growth initiatives - will drive growth in revenue, earnings, cash and ultimately shareholder value.

Let me turn it back over to Lynn.

Lynn Tyson:

Thanks, Michael. Before we begin the Q&A, please refrain from multi-part questions so everyone has an opportunity to ask a question. And as we said earlier, you should be queuing in right now and we will do our best to get to everyone.

Operator?

Operator:

Ladies and gentlemen, we will now begin the question and answer portion of today's call. If you have a question, please press star one on your telephone keypad. You will be announced prior to asking your question. If you would like to withdraw your question, press the pound key. One moment please for the first question.

We will take our first question from Richard Gardner from Citi.

Richard Gardner:

Thank you very much. You did a great job with headcount in the quarter you took out roughly three times as much as I think most of the Street was expecting in the quarter. Could you talk about where the reductions occurred in the quarter, what parts of the business in particular, and hopefully provide us with a new target since you've mentioned there are additional opportunities for headcount cuts in the core business? Thanks.

Don Carty:

Yes, Richard. I think if you look at where the headcount declined quarter over quarter it was really across the board and the reason I think all of you had lower expectations, we probably set that. I think I indicated at the Analyst Meeting that we would reduce at least 1,000 in the quarter.

We were successful in accelerating a fair bit of headcount reduction from the second quarter and even the third quarter into the first quarter. So we were able to move up some of our plans. A fair bit of it came in the consumer business. We talked to you about the fact that we were concerned about our level of OPEX; Consumer has been trying to execute on a lot of fronts - product, new distribution. But also at the same time execute on the cost side.

So a very substantial amount of the cut came in Consumer. It was headcount that we planned to cut but as I said, we were able to accelerate a fair bit of it. But I don't want you to walk away with the impression that it was just consumer. With the exception of some areas where we were investing very clearly in sales capacity - like APJ and the emerging markets of Eastern Europe, you saw headcount cuts virtually across the board, up through the management ranks to the most senior levels of the company. We thinned out the overhead pretty considerably in the quarter.

Richard Gardner:

And Don would you care to talk about a new target for headcount cuts?

Don Carty:

We're probably not going to reset the target. We told you we were heading toward 8,900 and we are. I think Michael even indicated that we had a line of sight beyond that. What you're going to find is the culture that we're building here is one that we are cutting costs everyday for the rest of the life of this company.

And this is going to stay a very cost conscious company. We do hope to drive headcount further in a number of areas. At the same time, of course, this is a growing company, you know. We're now growing very rapidly so sales capacity, service capacity; those are areas that we will have to invest in.

Michael do you want to add to that?

Michael Dell:

Yes. Yes, I think Don said it well. I mean we are, you know, embracing a new way of leading the company where there are areas as Don said, where we're cutting, we are finding productivity opportunities, consolidating, driving savings, at the same time making very significant investments in the new growth areas. In fact, we're doing one so we can do the other while, you know, certainly our intent is to grow the earnings of the company at the same time.

Lynn Tyson:

Next question, please.

Operator:

Our next question will come from Ben Reitzes with Lehman Brothers.

Ben Reitzes:

Thanks. Good afternoon. I'd like to ask you know kind of a devil's advocate question. I mean, if I calculate the gains in the quarter it's about five-and-a-half cents which puts us around thirty two to thirty-three cents, considering I had restructuring and some R&D in there as well, as well as the investigation I just always had that in there.

So, you know, versus consensus, it would look to me that we're pretty close to the thirty-three cents on a \$400 to \$500 million revenue beat and you crushed our headcount reduction number.

So I'm kind of wondering are the headcount – like why don't we have more leverage actually from real operating income from the headcount reductions and is that coming? Thank you.

Don Carty:

Yes, I think whenever headcount is reduced in a quarter particularly as you – as you accelerate headcount from the second quarter into the third quarter, some of this happened later in the quarter.

I think, Ben, we've said to you that we would hope to exit the year with OPEX closer to historical levels and we're not there yet. We're not growing about this OPEX level at this stage. Its progress, but both Michael and I said I think in our comments, more to be accomplished.

Ben Reitzes:

All right, thank you very much.

Operator:

Our next question will come from Katie Huberty with Morgan Stanley.

Katie Huberty:

What do you think the primary factors were behind such a meaningful inflection point in enterprise market share, especially in light of the cautiousness you mentioned in U.S. commercial IT spend and Dell's higher exposure domestically versus the competition?

Don Carty:

Let me make one observation and I'll turn it to Michael because he can talk an awful lot more about our product makeup. One of the interesting things in this downturn in the U.S., you know, we've referenced for you the financial services businesses as one of the pieces of the economy that has slowed their buying a little bit.

That has been true in all of our client products. But when it comes to enterprise, these customers still have vast amounts of data to manage and store. Data is growing, and that market has been a little more robust. I'll let Michael comment on our relative competitive position because I think that's been a big piece of it as well.

Michael Dell:

Yes, well a couple of things. If we did have almost 37 percent share of the U.S. server opportunity, which was a peak, you know, highest ever share for us. And, you know, I think Dell was one of the first companies to embrace virtualization on the server front, you know, a couple of years ago and its also fair to say that the, you know, the combination of virtualization

on the server plus the storage and the, you know, the addition of the EqualLogic offerings I think put a lot of focus with our sales organizations on driving enterprise success.

A lot of training, a lot of additional solution resources and then finally the last thing is, I think we've had great success in cloud computing both with the business software and service providers and a lot of the big internet companies that, you know, Dell I think has won a disproportionate percentage of the large web-driven opportunities and continue to be focused on that.

So we were the only server company in the quarter to gain both revenue and unit share.

Katie Huberty:

Great, thanks.

Operator:

Our next question will come from Brian Alexander with Raymond James.

Brian Alexander:

Thanks. On the consumer profitability it looked like it improved and you had, you know, the best margin performance. I know we're still at a low level, but best in five quarters based on your new reporting structure. Just talk about how much of the improvement on the consumer side was due to retail getting more efficient. Was that part of the business profitable and how confident are you that we'll continue to show some gradual improvement in consumer profitability versus retrenching to a loss situation in the next few quarters?

Don Carty:

Brian, good question. If you look at the consumer P&L you can see some pretty good improvement on the overhead cost side. And certainly that contributed in part to the improved profitability.

On the other hand, we are ramping volume very nicely. A lot of the COGS opportunity that we've talked about will benefit our consumer business. We still have too many products that we think are at a cost position on. We're successful in selling them but by definition if our costs were better our margins would be better.

So we've got a lot to accomplish. We don't break out retail and direct profitability but, suffice it to say, direct is a lot more profitable than retail. So we've got a ways to go in retail, there's absolutely no doubt about it. And Ron and his team are highly focused on it.

We're a long way from being ecstatic about our results. We like the progress but there's a lot more to follow here.

Michael Dell:

And we're seeing some very encouraging things. You know we have had a great reception from channel partners and retailers. If you take for example our business in China, we believe China is going to become the largest retail market in the world for PCs. We, at the end of the first quarter, had about 1,800 stores selling Dell products in China and the growth rate in units for the consumer business in China was about 140 percent.

We expect we'll have about 3,500 stores by the end of the second quarter, selling our products in China. So we are on an absolute, you know, rapid expansion in what we think is going to be the fastest growing country in the world. And the, you know, kind of acceptance of our brand inside those partners is very strong.

Brian Alexander:

So, just to follow up. It sounds like we're still very early in innings and a lot of the improvements you're making in this business such that there would be no good reason why you would regress from here. You should continue to improve in terms of overall profitability.

Michael Dell:

We think it's a multi-year opportunity. We're taking all the right steps to build, you know, this to be a substantial value creating part of our business.

Brian Alexander:

Thanks.

Operator:

Our next question is from David Bailey with Goldman Sachs.

David Bailey:

Thank you very much. It looks like you saw a mid-teens decline in both server and notebook ASP's this quarter on a year over year basis. Is that from mix or pricing or something else?

Michael Dell:

You know as I highlighted at the Analyst Meeting, a significant, you know, Dell has been kind of over-indexed to large commercial business around the world and our growth opportunities are substantially – are very significant in consumer and emerging countries wherever selling prices are in fact lower.

So that kind of explains the client side. On the server side, you know industry ASPs have been coming down and as I said earlier, we were the only company in the industry to grow revenue share or unit share.

Don Carty:

We did see some mix shift there as well. I mean we – our representation in the lower end of that product line – that product category increased during the quarter.

Lynn Tyson:

Next question, please.

Operator:

Our next question will come from Keith Bachman with Bank of Montreal.

Keith Bachman:

Hi, thanks for the question. Michael, I think this is for you. Both services and S&P had the best growth rate in well over a year. And I was just wondering if you could speak a little bit to you had some help from acquisitions. If you could pare it down in services and S&P on organic basis and related typically units is the best proxy for these two categories, unit growth. Is that still the case with the growth of the consumer businesses?

Michael Dell:

Well the consumer retail business doesn't have as much, you know, service attached to us for sure. But during the quarter we had, you know, continued progress of our new ProSupport offering. You know attach rates were up 24 percent on a year over year basis which is pretty staggering for an offering like this.

We're putting in a lot of resources into really solution selling. So as I mentioned earlier the focus on, you know, servers, storage and services, things that start with S is a big focus for the,

you know, tens of thousands of salespeople that we have out there, you know, talking to our customers.

And software too.

Don Carty:

Yes. The question about organic versus non-organic, as you know we required a number of very small companies to integrate into our service offering. We no longer kind of break that out. They become fully integrated into our service offerings so we're not able to answer the question.

But suffice it to say, at least at this early stage, the acquisitions would have had only a very trivial impact on the numbers Michael just talked about.

Keith Bachman:

Ok, that's very helpful. Thank you.

Operator:

Our next question is from Scott Craig with Bank of America.

Scott Craig:

Hey, good afternoon, thanks. Just quickly on the retail business, I think last quarter you mentioned the retail business specifically running at around a billion dollar run rate. Can you give us an update there and also in your short experience you know on the retail side of things, what are you seeing from a tax rate perspective in your retail partners. Thanks.

Michael Dell:

You know I'm not sure we have that to provide to you today, but I can tell you is that we have, you know, about 13,000 retail partners. We added about 2,000 during the first quarter. You know, Costco here in the United States, Suning who is the number two consumer electronics retailer in China, Gome and a variety of others in China as well. We added Best Buy in Canada. You know, don't have additional information for you.

Don Carty:

Obviously, most of our growth in the consumer space came from retail. So if you look year over year you can see virtually all of that growth is retail.

Operator:

Our next question is from Tony Sacconaghi with Sanford Bernstein.

Tony Sacconaghi:

Yes, thank you. You had mentioned at your Analyst Day that you thought that the biggest source of cost savings was in fact in the cost of goods line item rather than in SG&A and OPEX. You saw some improvement in OPEX this quarter; we did not see any in terms of cost of goods sold despite it was a very favorable component environment.

Understandably a lot of the cost savings initiatives on the COGS side are longer lead time. Can you give us a sense of when we should start to see some of the COGS initiatives which again maybe you can confirm are really the bigger lever in your eyes. When do we start to see them take hold, and given the mix shifts that you had talked about in terms of emerging market and consumer profitability, will they actually be evident in the income statement?

Don Carty:

You know, we are going through a pretty significant implementation here of, you know, changes in our product road map to capture the COGS opportunity that we've highlighted for you before. Its not just COGS, there's a lot in OPEX as well.

But you know, you can think about this somewhat tied to the product cycle. So as we introduced new products and those have been more tightly defined from a value standpoint based on customer features and you know we have to go through qualification cycles and that sort of thing. But I think you'll see this opportunity show up in a – but it certainly is going to ramp, you know, as we go through the year.

Operator:

Your next question is from Louis Miscioscia with Cowen and Company.

Louis Miscioscia:

OK, thank you. Can you actually give us some idea what you actually grew in constant currency and obviously with your comments about the environment out there, would you say that things have actually deteriorated as you went through the quarter and even as we stand here now into your next quarter. Or was it rather linear as you were experiencing the past quarter?

Don Carty:

You know, even though that was a two part question, I want to answer it. The COGS and currency question, you know, we don't publish details on that. But you can assume I think that

our currency effect obviously is somewhat less than the currency effect of some of our competitors, whose share in the international markets are somewhat larger than ours.

If you use a number between three and four percent you're pretty close on the cost and currency question.

The question on the economy, I don't think we've seen it deteriorate. I think we've seen a little bit spread, a little more hesitancy in the small and medium business. But we haven't seen anything falling off a cliff here. This is sort of the same currency we saw in the last quarter.

And you know from our perspective, the good news about this is these are purchases that can get deferred but they don't get eliminated as the cycle strengthens again, every time we've seen a cycle in the past, there's a backlog of demand for products.

So we're not at this stage terribly troubled by it. Like everybody else, we'd love to see the economy more robust than it appears to be, but we're not uncomfortable with it. Michael do you want...

Michael Dell:

Yes, the spending pattern we saw in the U.S. was about what we thought it would be. You know, we expected conservative spending and that is what we kind of saw. But it's also true that when you're selling a product enhancing device that has a defined life, you know, customers can delay the purchase of that for some period of time.

However, you know, at some point, it becomes counterproductive to have, you know, tools that are too old. And so we believe and have seen, you know, through any number of cycles that there's kind of a rebound effect. And so we're staying very close to these large customers.

We know that even the customers in sort of the most dire economic conditions have to upgrade their productivity tools. It's kind of the last thing that they will cut.

In fact, you know, the enterprise business was strong as this is a place if you look at data storage for example. Data storage is not stopping, in fact it continues to expand at a enormous rate and companies, you know, have to deal with that and we have great solutions for that.

Louis Miscioscia:

OK, so it wasn't a signal that things are changing drastically as we go here into the next quarter.

Don Carty:

No, not at all.

Louis Miscioscia:

Thank you.

Operator:

Our next question is from Jeff Ficadero with Merrill Lynch.

Jeff Ficadero:

Great. So I was wondering if you could just address sort of the component pricing and your outlook there. You know, just remind us how does Dell manage the component cost and how does that change really with the inclusion of retail and the ODM supply chain?

Michael Dell:

I don't think we're seeing anything dramatic in component trends. You know, in an overall basis. You know there's always things kind of moving around one way or another. But you know generally component trends have been, you know, following a fairly predictable pattern. The bigger thing for us is the efforts to really design in exactly the components we need and not kind of more or less.

I think that's going to be a bigger source of savings and improvement in our P&L.

Don Carty:

But to a point that was made earlier, this is not a period of really rapid component cost decreases. A year ago we were seeing kind of record cost component decreases. That's not the case today and in fact probably a little firming on the memory side, I think you're all familiar with that going on. That has been one area where we have held strategic inventory and it's served us very well.

But I agree with Michael, I don't think we see anything particularly unusual unfolding in this environment.

Operator:

Our next question is with Chris Whitmore with Deutsche Bank.

Chris Whitmore:

Thanks. I wanted to follow up on the consumer question. Specifically looking to disaggregate the growth related channel sale and channel inventory building versus sell through, if you could, maybe some color on channel inventory levels. And secondly, do you have a target for a number of retail outlets by year end. Thanks.

Michael Dell:

We're tracking channel inventory quite closely, very cautious here. Not to, you know, to make sure that our channel partners don't have too much inventory. You know, it's in our best interest and theirs as well. And you know we're pretty happy with the level of channel inventory that we have.

Don't really have a goal for you in terms of number of partners or number of stores. But I think you'll see us continue to add all over the world with a focus on kind of the leading and best partners and you know getting further penetration, you know, with those partners. You know, we don't want to be in – the opportunity universe is massively larger than 13,000 stores. So we're still at the very, you know, more at the beginning of this process.

Operator:

Our next question is with Bill Fearnley with FTN Midwest.

Bill Fearnley:

Yes, good afternoon. If I could ask a question about the pricing environment. A large distributor and others have made negative comments about the pricing environment especially in the U.S. business segments. Any additional color on what you saw last quarter on the pricing environment and near term thoughts on pricing environment and how it affects your margins near term?

Michael Dell:

I think the pricing environment has been pretty straight forward. I wouldn't say there's been, you know, dramatically different pricing environment. I mean, if anything, we might have tried some things in pricing that, you know, we wish we hadn't done. But, you know, I'd say that pricing is, you know, been pretty typical.

Bill Fearnley:

And when you say you hadn't done it, do you think you were too aggressive in some instances but it still helped you on the revenue line?

Michael Dell:

I think there were selected areas where we were probably, you know, more aggressive than what we should have been.

Don Carty:

I'd – let me just add to what Michael just said. In those areas, you know, sometimes when you see some softness you want to test the elasticity so you play with pricing a little bit. In this kind of economic environment, you don't see as much elasticity and hindsight I don't think it really helped our revenue line. I think to Michael's points, it probably – we probably had a little better profitability if we hadn't done it. But it wasn't extensive. There were just a few pockets where we experimented and in hindsight I think we would have done differently.

Operator:

Our next question is with David Wong with Wachovia.

David Wong:

Thanks so much. Given that you're continuing to focus on cost cutting, should we expect restructuring charges should continue at roughly the same level impacting EPS by two to four cents per quarter next few quarters?

Don Carty:

That gets a little more specific than I'm willing to get. But I did make a comment that we've still got cutting to go. We're not at our headcount target. We intend to get it.

I should also point out one accounting anomaly. I mentioned that our restructuring of EMEA resulted in a one-time charge. Under accounting rules we're only permitted to provide for the severance that is statutorily required. The way things work in Europe is you go from a decision to a discussion with works councils and what it finally costs you is usually significantly more than what's statutorily required. So we're likely to have another charge for that piece as we work through the details of those downsizings in EMEA which will impact the second and third quarter.

David Wong:

Great. Thanks.

Don Carty:

We also have some additional headcount cuts to come.

David Wong:

Great. Thanks.

Operator:

We'll now take our final question from Clay Sumner with FBR.

Clay Sumner:

Thank you. I just wanted to revisit the COGS question. On Analyst Day I believe you said you had 30 some odd new notebook models coming out that had been designed to be more cost optimized for the consumer segment. I was just wondering if you could give us an update on where you are and how many of those had been launched roughly.

Michael Dell:

We've introduced, you know, quite a number of notebooks so far this year. We have certainly much more to go. I think you'll see a very active back-to-school season for Dell in notebooks and we'll also be bringing out the Latitude E-Series. You know, Latitude is the best selling line of commercial notebooks in the developed world and you know we have our best ever, you know, notebooks – you know, best ever line of notebooks that we've ever produced, so very excited about those.

Clay Sumner:

All right. Congrats on the progress. Thanks.

Michael Dell:

Thank you.

Operator:

We'll now turn the call over to Mr. Dell for closing remarks.

Michael Dell:

So thank you for joining us today. I want to leave you with a few thoughts. First of all I'm encouraged by the acceleration in our growth. Second we continue to fill out our portfolio of products and services. And you'll see much more from us over the balance of the year.

And third, we continue to drive shareholder value by growing units that are at a premium to the industry, executing on our \$3 billion cost opportunity; delivering sustained EPS growth; and executing on our five core initiatives; and growing our retail channel for scale and profit.

Thanks for joining us today. We look forward to speaking to you again.

Operator:

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

END