

VMW Q3 FY18 Earnings Conference Call

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Pat Gelsinger, CEO

- Q3 results driven by broad-based strength across the product portfolio and in all three geographies
- Q3 FY18 total revenue grew 11% YoY⁽¹⁾
- Q3 FY18 non-GAAP earnings of \$1.34 per share⁽²⁾
- Welcomed over 77,000 customers, partners and influencers to VMworld and vForum events globally
- Announced, in partnership with Amazon Web Services, initial availability of VMware Cloud on AWS in the AWS U.S. west (Oregon) region
- Unveiled VMware Hybrid Cloud Extension service

(1) Year-over-Year comparisons are of VMware's fiscal 2018 third quarter (August 5, 2017 through November 3, 2017) to VMware's fiscal 2016 third quarter (July 1, 2016 through September 30, 2016)

(2) See Appendix for reconciliation to GAAP

Pat Gelsinger, CEO

- Introduced new VMware Cloud Services that enable end-to-end visibility into cloud usage, costs and networks
- Unveiled two new offerings: VMware AppDefense and Pivotal Container Service (PKS)
- According to IDC, VMware, based on sales of hyperconverged solutions running VMware vSAN, was the largest hyperconverged infrastructure software vendor during the first half of 2017 ⁽¹⁾
- Announced intent to acquire VeloCloud Networks, provider of industry-leading cloud-delivered software-defined wide-area network (SD-WAN) technology for enterprises and service providers

⁽¹⁾ IDC Worldwide Quarterly Converged Systems Tracker, 2Q2017

Overview of Results: Revenue Highlights

Q3 FY18		
	Actual (\$M)	YoY Growth
Total Revenue	1,976	11%
License Revenue	785	14%

Hybrid Cloud and SaaS

Q3 FY18

Over 8% of total revenue

Hybrid Cloud and SaaS Revenue contains:

VMware Cloud Provider Program - formerly known as vCloud Air Network

Portion of AirWatch revenue recognized as SaaS

Wavefront

Other "as a Service" offerings such as Desktop as a Service and VMware Cloud on AWS

Income Statement Highlights

	Q3 FY16	Q2 FY18	Q3 FY18
License Revenue (\$M)	691	732	785
Services Revenue (\$M)	1,087	1,168	1,191
Total Revenue (\$M)	1,778	1,900	1,976
Non-GAAP Operating Margin ⁽¹⁾	33.3%	30.8%	34.8%
Non-GAAP Net Income per Diluted Share (\$) ⁽¹⁾	1.14	1.19	1.34

Select Financial Measures

	Q3 FY16	Q3 FY18
Headcount	19,656	21,557
Cash & Short-Term Investments (\$M)	8,254	11,612
Operating Cash Flow (\$M)	620	970
CapEx (\$M)	30	59
Unearned Revenue Total (\$M)	5,094	5,647
Long-Term Unearned Revenue (\$M) ⁽¹⁾	1,815	2,147

(1) Non-current unearned revenue as reported on VMware's consolidated balance sheets

Zane Rowe, CFO & EVP

- YoY growth rate for total revenue plus the sequential change in total unearned revenue was 21%⁽¹⁾
- YoY growth rate for license revenue plus sequential change in unearned license revenue was 16%⁽¹⁾
- NSX license bookings grew over 100% YoY and vSAN license bookings grew over 150% YoY
- EUC license bookings for the quarter were up over 40% YoY

(1) See Appendix for calculation

Zane Rowe, CFO & EVP

- **Total Compute bookings were up 11%; Compute license bookings were up in the mid-single-digits YoY**
- **Total Cloud Management bookings were flat, with Cloud Management license bookings down in the low-single digits YoY**
- **Revenue for VMware Cloud on AWS will be recognized on a “net” basis upon adoption of the new accounting standard ASC 606 in Q1 FY19**
- **Completed a \$300M repurchase of VMware’s Class A common stock from Dell Technologies**
- **Completed \$555M of stock repurchases in the open market, finishing the quarter with just over \$1B remaining on our stock repurchase authorizations**

FY18 Guidance

FY18	
Total Revenue	\$7.875B
License Revenue	\$3.155B
Non-GAAP Operating Margin ⁽¹⁾	33%
Diluted Non-GAAP EPS ⁽¹⁾	\$5.13
Diluted Share Count	412M

(1) See Appendix for reconciliation to GAAP

FY18 Additional Guidance

	FY18
Non-GAAP Tax Rate	20.50%
GAAP Tax Rate	Approximately 4 to 5 points lower than non-GAAP tax rate
Cash Flow From Operations	\$3.10B
CapEx	\$260M
Free Cash Flow ⁽¹⁾	\$2.84B

(1) Free Cash Flow is a non-GAAP financial measure calculated by subtracting CapEx from Cash Flow From Operations. See table above.

Q4 FY18 Guidance

Q4 FY18	
Total Revenue	\$2.263B
License Revenue	\$1.028B
Non-GAAP Operating Margin ⁽¹⁾	36.9%
Diluted Non-GAAP EPS ⁽¹⁾	\$1.62
Diluted Share Count	409M

(1) See Appendix for reconciliation to GAAP

Q&A

Appendix

Enterprise Agreements

42% of total bookings

7 deals over \$10M

9 of the top 10 deals included EUC

9 of the top 10 deals included NSX

8 of the top 10 deals included vSAN

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RECONCILIATION OF GAAP TO NON-GAAP DATA For the Three Months Ended November 3, 2017 (amounts in millions, except per share amounts, and shares in thousands) (unaudited)

	GAAP	Stock-Based Compensation	Employer Payroll Taxes on Employee Stock Transactions	Intangible Amortization	Acquisition, Disposition and Other Related Items	Tax Adjustment ⁽¹⁾	Non-GAAP, as adjusted ⁽²⁾
Operating expenses:							
Cost of license revenue	\$ 38	—	—	(26)	—	—	\$ 11
Cost of services revenue	\$ 240	(13)	(1)	(1)	—	—	\$ 225
Research and development	\$ 449	(96)	—	—	(1)	—	\$ 352
Sales and marketing	\$ 607	(52)	(1)	(6)	(1)	—	\$ 550
General and administrative	\$ 175	(21)	—	—	(4)	—	\$ 149
Realignment and loss on disposition	\$ 2	—	—	—	(2)	—	\$ —
Operating income	\$ 465	182	2	33	8	—	\$ 689
Operating margin ⁽²⁾	23.5%	9.2%	0.1%	1.6%	0.4%	—	34.8%
Other income (expense), net	\$ (2)	—	—	—	3	—	\$ 2
Income before income tax	\$ 468	182	2	33	11	—	\$ 696
Income tax provision	\$ 25					118	\$ 143
Tax rate ⁽²⁾	5.4%						20.5%
Net income	\$ 443	182	2	33	11	(118)	\$ 553
Net income per weighted-average share, diluted for Classes A and B ⁽²⁾⁽³⁾	\$ 1.07	\$ 0.44	\$ —	\$ 0.08	\$ 0.03	\$ (0.28)	\$ 1.34

⁽¹⁾ Non-GAAP financial information for the quarter is adjusted for a tax rate equal to our annual estimated tax rate on non-GAAP income. This rate is based on our estimated annual GAAP income tax rate forecast, adjusted to account for items excluded from GAAP income in calculating the non-GAAP financial measures presented above as well as significant tax adjustments. Our estimated tax rate on non-GAAP income is determined annually and may be adjusted during the year to take into account events or trends that we believe materially impact the estimated annual rate including, but not limited to, significant changes resulting from tax legislation, material changes in the geographic mix of revenue and expenses and other significant events. Due to the differences in the tax treatment of items excluded from non-GAAP earnings, as well as the methodology applied to our estimated annual tax rates as described above, our estimated tax rate on non-GAAP income may differ from our GAAP tax rate and from our actual tax liabilities.

⁽²⁾ Totals may not sum, due to rounding. Operating margin, tax rate and net income per weighted average share information are calculated based upon the respective underlying, non-rounded data.

⁽³⁾ Calculated based upon 413,013 diluted weighted-average shares for Classes A and B.

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RECONCILIATION OF GAAP TO NON-GAAP DATA

For the Three Months Ended September 30, 2016

(amounts in millions, except per share amounts, and shares in thousands)

(unaudited)

	GAAP	Stock-Based Compensation	Employer Payroll Taxes on Employee Stock Transactions	Intangible Amortization	Acquisition, Disposition and Other Related Items	Tax Adjustment ⁽¹⁾	Non-GAAP, as adjusted ⁽²⁾
Operating expenses:							
Cost of license revenue	\$ 40	—	—	(26)	—	—	\$ 13
Cost of services revenue	\$ 226	(13)	—	(1)	—	—	\$ 212
Research and development	\$ 389	(80)	—	—	—	—	\$ 309
Sales and marketing	\$ 564	(51)	(2)	(5)	—	—	\$ 507
General and administrative	\$ 178	(26)	—	—	(6)	—	\$ 145
Operating income	\$ 381	170	2	32	6	—	\$ 592
<i>Operating margin⁽²⁾</i>	<i>21.4%</i>	<i>9.6%</i>	<i>0.1%</i>	<i>1.8%</i>	<i>0.4%</i>	—	<i>33.3%</i>
Other income (expense), net	\$ (8)	—	—	—	13	—	\$ 5
Income before income tax	\$ 387	170	2	32	19	—	\$ 611
Income tax provision	\$ 68					57	\$ 126
<i>Tax rate⁽²⁾</i>	<i>17.6%</i>						<i>20.5%</i>
Net income	\$ 319	170	2	32	19	(57)	\$ 485
Net income per weighted-average share, diluted for Classes A and B ^{(2) (3)}	\$ 0.75	\$ 0.40	\$ 0.01	\$ 0.08	\$ 0.04	\$ (0.13)	\$ 1.14

⁽¹⁾ Non-GAAP financial information for the quarter is adjusted for a tax rate equal to our annual estimated tax rate on non-GAAP income. This rate is based on our estimated annual GAAP income tax rate forecast, adjusted to account for items excluded from GAAP income in calculating the non-GAAP financial measures presented above as well as significant tax adjustments. Our estimated tax rate on non-GAAP income is determined annually and may be adjusted during the year to take into account events or trends that we believe materially impact the estimated annual rate including, but not limited to, significant changes resulting from tax legislation, material changes in the geographic mix of revenue and expenses and other significant events. Due to the differences in the tax treatment of items excluded from non-GAAP earnings, as well as the methodology applied to our estimated annual tax rates as described above, our estimated tax rate on non-GAAP income may differ from our GAAP tax rate and from our actual tax liabilities.

⁽²⁾ Totals may not sum, due to rounding. Operating margin, tax rate and net income per weighted average share information are calculated based upon the respective underlying, non-rounded data.

⁽³⁾ Calculated based upon 425,008 diluted weighted-average shares for Classes A and B.

Appendix

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RECONCILIATION OF GAAP TO NON-GAAP DATA

For the Three Months Ended August 4, 2017

(amounts in millions, except per share amounts, and shares in thousands)

(unaudited)

	GAAP	Stock-Based Compensation	Employer Payroll Taxes on Employee Stock Transactions	Intangible Amortization	Acquisition, Disposition and Other Related Items	Tax Adjustment ⁽¹⁾	Non-GAAP, as adjusted ⁽²⁾
Operating expenses:							
Cost of license revenue	\$ 39	—	—	(26)	—	—	\$ 12
Cost of services revenue	\$ 231	(12)	1	(1)	1	—	\$ 221
Research and development	\$ 428	(89)	(1)	—	(1)	—	\$ 338
Sales and marketing	\$ 668	(48)	(1)	(6)	(1)	—	\$ 612
General and administrative	\$ 160	(20)	—	—	(8)	—	\$ 132
Realignment and loss on disposition	\$ 36	—	—	—	(36)	—	\$ —
Operating income	\$ 338	169	1	33	45	—	\$ 585
Operating margin ⁽²⁾	17.8%	8.9%	0.1%	1.7%	2.4%	—	30.8%
Other income (expense), net	\$ 51	—	—	—	(38)	—	\$ 13
Income before income tax	\$ 407	169	1	33	7	—	\$ 616
Income tax provision	\$ 73					53	\$ 127
Tax rate ⁽²⁾	17.9%						20.5%
Net income	\$ 334	169	1	33	7	(53)	\$ 489
Net income per weighted-average share, diluted for Class A and Class B ⁽²⁾⁽³⁾	\$ 0.81	\$ 0.41	\$ —	\$ 0.08	\$ 0.02	\$ (0.13)	\$ 1.19

⁽¹⁾ Non-GAAP financial information for the quarter is adjusted for a tax rate equal to our annual estimated tax rate on non-GAAP income. This rate is based on our estimated annual GAAP income tax rate forecast, adjusted to account for items excluded from GAAP income in calculating the non-GAAP financial measures presented above as well as significant tax adjustments. Our estimated tax rate on non-GAAP income is determined annually and may be adjusted during the year to take into account events or trends that we believe materially impact the estimated annual rate including, but not limited to, significant changes resulting from tax legislation, material changes in the geographic mix of revenue and expenses and other significant events. Due to the differences in the tax treatment of items excluded from non-GAAP earnings, as well as the methodology applied to our estimated annual tax rates as described above, our estimated tax rate on non-GAAP income may differ from our GAAP tax rate and from our actual tax liabilities.

⁽²⁾ Totals may not sum, due to rounding. Operating margin, tax rate and net income per weighted average share information are calculated based upon the respective underlying, non-rounded data.

⁽³⁾ Calculated based upon 412,768 diluted weighted-average shares for Class A and Class B.

GROWTH IN REVENUE PLUS SEQUENTIAL CHANGE IN UNEARNED REVENUE
(in millions)
(unaudited)

Growth in Total Revenue Plus Sequential Change in Unearned Revenue

	Three Months Ended	
	November 3, 2017	September 30, 2016
Total revenue, as reported	\$ 1,976	\$ 1,778
Sequential change in unearned revenue ⁽¹⁾	143	(27)
Total revenue plus sequential change in unearned revenue	<u>\$ 2,119</u>	<u>\$ 1,751</u>
Change (%) over prior year, as reported	21%	

Growth in License Revenue Plus Sequential Change in Unearned License Revenue

	Three Months Ended	
	November 3, 2017	September 30, 2016
Total license revenue, as reported	\$ 785	\$ 691
Sequential change in unearned license revenue	(16)	(30)
Total license revenue plus sequential change in unearned license revenue	<u>\$ 769</u>	<u>\$ 661</u>
Change (%) over prior year, as reported	16%	

⁽¹⁾ Sequential change in unearned revenue consists of the change in total unearned revenue from the preceding quarter. Total unearned revenue consists of current and non-current unearned revenue amounts presented in the condensed consolidated balance sheets.

Appendix

Reconciliation of GAAP to Non-GAAP Operating Margin Guidance

	Fourth Quarter Fiscal 2018 (Projected)		Full Year Fiscal 2018 (Projected)	
GAAP Operating Margin	29.0% - 26.8% ⁽¹⁾	Projected	21.5% - 20.9% ⁽²⁾	Projected
Stock-based Compensation	7.1%	Estimated	8.6%	Estimated
Employer Payroll Tax on Employee Stock Transactions	0.1%	Estimated	0.1%	Estimated
Intangible Amortization	1.4%	Estimated	1.6%	Estimated
Acquisition, Disposition and Other Related Items	0.2%	Estimated	1.5%	Estimated
Non-GAAP Operating Margin	36.9%	Projected	33.0%	Projected

(1) Values of items excluded from GAAP operating margin are estimates. While the aggregate of estimates may not foot, in total we expect GAAP operating margin to be 8 to 10 percentage points less than non-GAAP operating margin.

(2) Values of items excluded from GAAP operating margin are estimates. While the aggregate of estimates may not foot, in total we expect GAAP operating margin to be 11 to 12 percentage points less than non-GAAP operating margin.

Appendix

Reconciliation of GAAP to Non-GAAP Net Income per Diluted Share Guidance

	Fourth Quarter Fiscal 2018 (Projected)		Full Year Fiscal 2018 (Projected)	
GAAP Net Income per Diluted Share	\$1.22 - \$1.12 ⁽¹⁾	Projected	\$3.66 - \$3.56 ⁽²⁾	Projected
Stock-based Compensation	0.39	Estimated	1.63	Estimated
Employer Payroll Tax on Employee Stock Transactions	0.00	Estimated	0.02	Estimated
Intangible Amortization	0.08	Estimated	0.31	Estimated
Acquisition, Disposition and Other Related Items	0.03	Estimated	0.23	Estimated
Tax Adjustment	(0.07)	Estimated	(0.68)	Estimated
Non-GAAP Net Income per Diluted Share	\$1.62	Projected	\$5.13	Projected

(1) Values of items excluded from GAAP net income per diluted share are estimates. While the aggregate of estimates may not foot, in total we expect GAAP net income per share to be \$0.40 to \$0.50 less than non-GAAP net income per share.

(2) Values of items excluded from GAAP net income per diluted share are estimates. While the aggregate of estimates may not foot, in total we expect GAAP net income per share to be \$1.47 to \$1.57 less than non-GAAP net income per share.

Revised Fiscal Calendar

YoY Comparisons of Quarterly Results and Sequential Change in Unearned Revenue Balances

VMware revised its fiscal calendar effective January 1, 2017. VMware's first fiscal year under its revised fiscal calendar began on February 4, 2017 and will end February 2, 2018. The period from January 1, 2017 through February 3, 2017 was recorded as a transition period and was reported as a separate period in VMware's Form 10-Q filing for the first quarter of fiscal 2018.

Year-over-year comparisons of quarterly financial results included in this earnings presentation compare results for VMware's fiscal 2018 third quarter (August 5, 2017 through November 3, 2017) to VMware's fiscal 2016 third quarter (July 1, 2016 through September 30, 2016). Sequential changes in total unearned revenue and unearned license revenue for the third quarter of fiscal 2018 compare VMware's total unearned revenue and unearned license revenue balances as of August 4, 2017, the last day of the second fiscal quarter, to the respective balances as of November 3, 2017, the last day of VMware's fiscal 2018 third quarter.

Forward-Looking Statements

This presentation contains forward-looking statements including expected benefits to customers of VMware products and services; VMware's intention to acquire VeloCloud Networks, Inc. and the expected advantages of combined offerings after the acquisition's close; expectations regarding total and license revenues growth, non-GAAP operating margin, diluted non-GAAP earnings per share and diluted share count for Q4 fiscal year 2018 (FY18) and FY18; expectations regarding FY18 GAAP and non-GAAP tax rates, cash flow from operations, capital expenditures and free cash flow; and expectations related to VMware's non-GAAP to GAAP reconciliations of free cash flow for Q4 FY18 and operating margin and diluted earnings per share for Q4 FY18 and FY18. These forward-looking statements are subject to the safe harbor provisions created by the Private Securities Litigation Reform Act of 1995. Actual results could differ materially from those projected in the forward-looking statements as a result of certain risk factors, including but not limited to: (i) adverse changes in general economic or market conditions; (ii) delays or reductions in consumer, government and information technology spending; (iii) competitive factors, including but not limited to pricing pressures, industry consolidation, entry of new competitors into the virtualization software and cloud, end user and mobile computing industries, and new product and marketing initiatives by VMware's competitors; (iv) VMware's customers' ability to transition to new products and computing strategies such as cloud computing, desktop virtualization and the software defined data center; (v) VMware's ability to enter into and maintain strategically effective partnerships and alliances; (vi) the uncertainty of customer acceptance of emerging technology; (vii) rapid technological changes in the virtualization software and cloud, end user and mobile computing industries; (viii) changes to product and service development timelines; (ix) VMware's relationship with Dell Technologies and Dell's ability to control matters requiring stockholder approval, including the election of VMware's board members and matters relating to Dell's investment in VMware; (x) VMware's ability to protect its proprietary technology; (xi) VMware's ability to attract and retain highly qualified employees; (xii) the ability of the parties to satisfy closing conditions to VMware's acquisition of VeloCloud Networks, Inc. on a timely basis or at all; (xiii) market conditions, regulatory requirements and other corporate considerations that could affect the timing and closing conditions to VMware's acquisition of VeloCloud Networks, Inc.; (xiv) the ability to successfully integrate into VMware acquired companies and assets and smoothly transition services related to divested assets from VMware; (xv) the ability of VMware to realize synergies from Dell; (xvi) disruptions resulting from key management changes; (xvii) fluctuating currency exchange rates; (xviii) changes in VMware's financial condition; and (xix) potential disruptions relating to the transition to Dell's fiscal year and further business integrations with Dell. These forward-looking statements are based on current expectations and are subject to uncertainties and changes in condition, significance, value and effect as well as other risks detailed in documents filed with the Securities and Exchange Commission, including VMware's most recent reports on Form 10-K and Form 10-Q and current reports on Form 8-K that VMware may file from time to time, which could cause actual results to vary from expectations. VMware assumes no obligation to, and does not currently intend to, update any such forward-looking statements after the date of this presentation.