Q2 2022 Earnings Call

Company Participants

- Hock Tan, President and Chief Executive Officer
- Ji Yoo, Director of Investor Relations
- Kirsten Spears, Chief Financial Officer
- Tom Krause, President of Broadcom Software Group

Other Participants

- Ambrish Srivastava, Analyst
- Harsh Kumar, Analyst
- Ross Seymore, Analyst
- Stacy Rasgon, Analyst
- Toshiya Hari, Analyst
- Vivek Arya, Analyst

Presentation

Operator

Welcome to Broadcom Inc VMware transaction and Second Quarter Fiscal Year 2022 Financial Results Conference Call. At this time for opening remarks and introductions, I would like to turn the call over to Ji Yoo, Director of Investor Relations of Broadcom Inc.

Ji Yoo {BIO 21112206 <GO>}

Thank you, operator and good morning everyone. Joining me on today's call are Hock Tan, President and CEO; Kirsten Spears, Chief Financial Officer.; Tom Krause, President Broadcom Software Group; and Charlie Kawwas, Chief Operating Officer. This morning Broadcom issued a press release and presentation regarding our announced agreement to acquire VMware. We also distributed our fiscal second quarter '22 results and financial tables.

If you did not receive a copy, you may obtain the information from the investors section of Broadcom's website at broadcom.com. This conference call is being webcast live and a recording will be available via telephone playback for one week.

It will also be archived in the investors section of our website at broadcom.com. During the prepared remarks, Hock, Tom and Kirsten will be providing details regarding our announced acquisition of VMware and Broadcom's second quarter fiscal year '22 results, guidance for our third quarter, as well as commentary regarding the business environment.

We'll take questions after the end of our prepared comments.

Please refer to our press release and presentation today and our recent filings with the SEC for information on the specific risk factors that could cause our actual results to differ materially from the forward-looking statements made on this call. In addition to US GAAP reporting, Broadcom reports certain financial measures on a non-GAAP basis.

A reconciliation between GAAP and non-GAAP measures is included in the tables attached to today's press release. Comments made during today's call will primarily refer to our non-GAAP financial results. I'll now turn the call over to Hock.

Hock Tan {BIO 1460567 <GO>}

Thank you, Ji. And thank you everyone for joining today. If you could indulge me, let me start off by reviewing our fiscal Q2 results and outlook for -- on Q3 and the broader markets, of course, we play in.

So in fiscal Q2 '22, consolidated net revenue was a record $8.1 billion, up 23% year-on-year. Semiconductor solutions revenue growth accelerated to 29% year-on-year to $6.2 billion and infrastructure software revenue grew 5% year-on-year to $1.9 billion. Demand as referenced by consolidated bookings continue to be strong, even as our lead times remain unchanged, but extended.

In hardware, backlog at the end of Q2 was over $29 billion compared to $25 billion the preceding quarter and $21 billion a year ago.

In software, backlog grew as well and ended the quarter at over $15 billion compared to $14 billion a year ago.

Let me provide more color by end-markets. Starting with networking. Networking revenue was a record $2.2 billion, with growth accelerating to 44% year-on-year. There were two major drivers, we saw substantial deployment by hyperscalers of their AI engines and networks using our silicon during this quarter.

More importantly, we saw adoption of our next generation merchant[ph] switching and routing continuing to accelerate in hyperscale enterprises and service providers at the expense of proprietary solutions. These fundamental transition to merchant silicon based on Broadcom's platform will continue in Q3, and as a result, we expect in excess of 25% year-over-year growth in networking.

Next, our server storage connectivity revenue was $939 million, and as we guided, accelerated to 66% year-on-year growth. While service storage spending in enterprise was strong, our content increased in next generation MegaRAID drove a substantial portion of this growth.

Additionally, hyperscalers are aggressively adopting our next generation server storage solutions to scale their massive consumption of nearline hard disk drive race[ph]. So in Q3, we expect these same drivers to continue with revenue to grow over 60% year-on-year.

Now moving on to broadband. Q2 revenue of $1.1 billion grew 24% year-on-year. Deployment during the quarter on next generation PON and cable modem DOCSIS with high attach rate of WiFi 6 and 6E continue to be good among major service providers globally.

Just as a reminder however, expansion in broadband investments arising particularly from COVID-19 pandemic lockdowns is a multi-year phenomenon, Investments are measured and we are still in the early innings. Accordingly, in Q3, we do expect Broadcom broadband revenue to sustain a growth rate around 20% year-on-year.

On the wireless. Q2 revenue of $1.7 billion was up 6% from a year ago and as guided, decline a seasonal 14% quarter-on-quarter. In Q3, we expect wireless revenue to be flat to slightly down quarter-on-quarter, but up mid-teens[ph] percentage from a year ago, reflecting an increase in content.

Finally, in Industrial, Q2 resales of $254 million grew 14% year-over-year, driven by strong demand from electric vehicles, renewable energy, factory automation, and healthcare. Reflecting this -- such strong resales,our inventory in the channel continue to be very lean at around one month. And in Q3, we expect industrial resales to remain stable and inventory levels to continue to be lean.

So in summary, Q2 semiconductor solutions revenue was up 29% year-on-year, step up from the 20% year-on-year growth the preceding quarter.

As I highlighted above, content increase in service storage and the fundamental shift to merchant silicon in switching and routing drove this accelerated growth.

This will continue in Q3 and accordingly, we expect semiconductor revenue in Q3 to grow 31% year-on-year.

Now turning to software. In Q2, infrastructure software revenue of $1.9 billion grew 5% year-on-year and represented 23% of total revenue. Co-software[ph] revenue grew 5% year-on-year. In dollar terms, consolidated renewal rates average a 120% over expiring contracts. While in strategic accounts we average 136%. Within our strategic accounts, $641 million of -- represented renewals and expiring contracts, of which, $117 million represented cross selling including PLAs of our portfolio products to these same customers. Over 90% of the renewal value represented recurring subscription and maintenance. ARR at the end of Q2 was $5.4 billion, which was up 4% from a year ago. And in Q3, we expect our infrastructure software revenue to sustain a mid-single digit percent growth year-over-year.

In summary, our outlook for Q3, semiconductor revenue growth will continue to be strong, up 31% year-on-year, layering on our stable software business, we expect Q3 consolidated revenue growth of 24% year-on-year to $8.4 billion.

Well, that concludes my discussion of our second quarter results. I will now turn to what perhaps you all have been waiting to hear more about.

Now please refer to our accompanying slides regarding our agreement to acquire VMware.

As you know, we never embarked on an acquisition unless we feel our call is very strong and solid, irrespective of what you might think of where we are in the semiconductor cycle today. I do want to reassure you the fundamentals of our business, both in semiconductors and in software have never been stronger. We have just reviewed how solid -- solidly grounded these businesses are. So let me discuss now what we believe is a very unique opportunity to take our company and its business to the next level.

Starting with slide number 4, by adding VMware, we will bring significant scale to Broadcom's software business and reinforce our position as a premier provider of mission-critical platform solutions to enterprises globally. VMware is an iconic company providing call[ph] cloud infrastructure that powers more than enterprises. The company began as the virtualization pioneer, bringing revolutionary levels of efficiency to on-premise data centers. VMware extended its platform to the private cloud, giving enterprise customers unmatched levels of security, performance and control over their applications and underlying infrastructure.

And most exciting, today, VMware is now powering solutions for multi-cloud hybrid cloud future, where oneware[ph] it will be possible for enterprises to develop and run their apps anywhere, everywhere with no trade-offs in a truly cloud-neutral fashion.

One of the reasons we became very interested in VMware was because of its world-class team, engineering-centric culture and strong customer and partner relationships.

As shown in slide 5, VMware importantly aligns incredibly well with the Broadcom strategy and it has all the attributes we seek in the platforms we operate. VMware is the leader in big growing and global markets. The company's an indispensable provider of commission-critical platform technology with a blue-chip customer base and an incredible innovation engine.

As Tom will discuss next in more detail, together with Broadcom's existing software portfolio, we are positioned to create a uniquely powerful value proposition for enterprises. Enabling them to develop, deploy, and manage their applications securely seamlessly across every type of cloud and to accelerate the application lifecycle for their workloads.

And in addition to adding new dimensions of value for customers, VMware, also has an ideal profile that will enable us, Broadcom, to create compelling value for our shareholders. As part of Broadcom, our target is for VMware to contribute approximately $8.5 billion of EBITDA once we have fully integrated the company onto our platform.

Slide 6 shows that we have more than $40 billion of pro forma revenue and this is pro forma on our fiscal '21. We are creating one of the world's largest infrastructure technology companies.

Our semiconductor business is one of the largest semiconductor business globally. with 17 key franchises. It is highly profitable, and as I just reviewed, continues to post very strong organic growth. Revenues have grown from $15.6 billion 2017 following the acquisition of Classic Broadcom to $20.4 billion in fiscal '21.

All this growth being organic. With the addition of VMware, our software business will now represent close to half of our total pro forma revenue, with approximately $20 billion of software revenue for fiscal '21. With this type of scale and a continuing commitment to R&D and innovation, we will be able to significantly invest and fund new innovative solutions that will support our customer base.

To now dive deeper into the VMware market opportunity and products, I'll hand the call over to Tom.

Tom Krause {BIO 17978469 <GO>}

Thanks, Hock. Now turning to slide 7. As Hock previewed, VMware sits at the nexus of the largest opportunity in enterprise infrastructure today. In essence, VMware is a foundational platform that enables enterprises to drive competitive advantage with technology by leveraging two operational modes to develop and run their applications.

First, VMware serves many of the same types of customers that we have worked with at Broadcom, large multinational organizations with complex IT challenges. These enterprises want to move fast and innovate, but also mitigate risk by retaining control of their underlying infrastructure and data. To do this, enterprises are deploying applications in their own data centers, but need software to enable them to develop and run these applications in a flexible, agile and cost-effective fashion.

This private cloud market is very large and workload growth in the private cloud continues to grow. Beyond the private cloud, as we all know, public cloud workloads are growing rapidly. The public cloud brings unprecedented scalability and cost benefits and also enables enterprises to leverage cutting-edge technologies to drive their business forward. So we think it is clear that both of these modes private cloud and public cloud are going to be important for enterprises going forward.

Turning to slide 8, VMware is a truly foundational infrastructure software platform that is critical for enterprises to leverage the benefits of both the private and public clouds. We have tremendous respect for the leading platform VMware has built, supported by an incredible team of R&D talent. By bringing our teams together, we will deliver even more innovation to our customer.

As we think about it, VMware's platform really consists of three pillars: first, within the core private cloud infrastructure pillar, is the category-defining vSphere, server virtualization platform, vSAN, data storage virtualization solution, vRealize, cloud management platform that provides automation, analytics and lifecycle management for private cloud workloads, and NSX, which enables enterprises to manage their entire physical network as a single entity from a single pane of glass.

Next, VMware's Tanzu platform provides an end-to-end modern application management platform for building, deploying, securing, and operating applications in private, hybrid, or public cloud environments.

Finally, VMware has a robust portfolio of end-user and security solutions that enable employees to securely work from anywhere, anytime and with seamless employee experiences.

On slide 9, let me double click on the first pillar, as this makes up the bulk of VMware's revenue contribution today and is positioned to continue to grow well going forward. VMware pioneered the concept of virtualization and today, this technology is foundational to the development and computing operations of basically all enterprises in the world.

Over time, VMware has evolved its value proposition from core server virtualization to enabling one to virtualize the underlying compute resources of the entire data center, which is the private cloud. They further extended this value proposition with NSX and vSAN, by enabling software defined networks and storage. Then with vRealize, VMware made it extremely easy to manage and operate the entire data center infrastructure.

With these products, VMware offers a complete platform that delivers the scalability, flexibility, and cost benefits of virtualizing the underlying infrastructure across servers, networking, and storage.

In concert with this private cloud capability, VMware also offers a seamless way to evolve the enterprise infrastructure to embrace the benefits of the public cloud with VMware Cloud Foundation. VMware Cloud Foundation gives the same operating environment for developers, letting them write the code once and deploy it anywhere they want, whether it's in the private cloud, in AWS, Azure, GCP[ph] or even a cross clouds. This simplicity is unique to VMware in ushering in the coming age of mass cloud adoption.

Stepping back on slide 10 and thinking about our existing software portfolio, we are incredibly excited about the opportunity to marry our products with the VMware platform to deliver more end-to-end capabilities to our enterprise customers.

As we all know, enterprises need to manage a constantly changing portfolio of thousands of applications that reside on a wide variety of underlying infrastructure, from mainframe, to client server, to hybrid and public cloud. And all of these applications are operating in different stages of their life cycle.

And we think together, Broadcom software assets for the distributed enterprise can seamlessly complement and augment VMware's multi-cloud offerings in the areas of operation management, value stream and DevOps management, and Security to address the entire application lifecycle.

Starting with application development, we bring significant value to help accelerate the development of applications through VMware's Tanzu products and our value stream management products like Rally and Clarity.

Once developed, VMware's vSphere and Cloud Foundation can deploy these apps across a wide variety of environments. We can secure these applications with the combined capabilities of Symantec's leading security portfolio along with Carbon Black's cloud-native endpoint security products.

Now, given the hybrid working environment we are all in today, it's critical for enterprise to be able to enable seamless highly performant and ubiquitous access to these applications and VMware has a leading set of products to enable this.

Finally, to optimize and monitor these apps, Broadcom's existing portfolio of AIOps observability, enterprise automation and continuous delivery can ensure these applications are running well. Since these applications are constantly changing, it's exciting to be able to close the loop and feed any runtime operational issues right back into the application development step[ph].

So, what's exciting is that when you put the two portfolios together, we're delivering an end-to-end solution that enables enterprises to support the three major types of application paradigms, including applications that run critical business functions that will remain in private cloud data centers, applications that are being ported to run in the public cloud, and new generation applications that are written natively for one or several of the public cloud provider. We do this across the entire application lifecycle and we can support any underlying IT infrastructure.

That's unique to us and we think this adds massive value to enterprise customers.

Moving to the next slide. When I think about this deal, it reminds me of when as Avago, we acquired Classic Broadcom. This really transform the time and modernized our semiconductor business. And ultimately, this is why we renamed ourselves Broadcom.

As we come together with VMware, this represents the same level of transformation for our software business and we stand to benefit from VMware's unparalleled brand, trusted apps, its long-standing position as an iconic software platform within a robust, vibrant ecosystem of hyperscalers, solutions and cloud providers and channel partners among others.

We're excited to announce the following the closing of the transaction, Broadcom Software Group will rebrand and operate as VMware, incorporating Broadcom's existing infrastructure and security software solutions into the VMware platform. Together we will deliver the broadest range of platforms and tools to accelerate our combined customers' digital transformation.

Turning to slide 12. Together, Broadcom and VMware cover all major industry verticals and sell to all enterprises globally. And with this transaction, we are focused on serving all customers via a combination of our collective direct sales organizations as well as through our important channel partners.

When we look at the majority of our revenues, they are derived from the largest global multinationals, and they fit six key attributes. These customers are usually highly regulated and risk-averse, with large and expanding IT budgets. They also have complex and heterogeneous environments that are built around hybrid and multi-cloud strategies. While many of these companies want to explore moving more workloads to the public cloud, they are held back by many factors, including the number of applications that they have, the unfavorable economics of the public cloud for certain workload types, the sensitive data they handle and/or regulation.

As a result, these companies will have to keep complex operating environments containing a private cloud and over time, to increasingly leverage the benefits of the public cloud as well. The amount of operational complexity created here is a challenge that we are uniquely qualified to partner with our customers to solve. In summary, together with VMware, we are best positioned to help the world's largest enterprises to embrace a hybrid and multi-cloud environment. As shown on slide 13, we have a proven track record of creating shareholder value by applying Broadcom's disciplined business model built on significant R&D investment and customer focus.

Applying this same model to VMware, we are targeting to increase VMware's standalone EBITDA of approximately $4.7 billion to approximately $8.5 billion in pro forma run rate EBITDA within three years of closing. Driving this are some material tailwinds to revenue growth and multiple knobs that we can turn on profitability. Some of these opportunities include focusing on Research and Development, to support efforts, where we can uniquely deliver customer value, driving sales and marketing efficiency gains by focusing on our installed base and eliminating duplicative general and administrative functions.

We envision a long-term model for software, where we can grow our top line revenues at mid-single digits on a recurring basis, if not faster, while driving EBITDA margins in the mid-60s. Given our scale, this will allow us to reinvest very significant dollars back into the business both via R&D as well as sales and marketing.

Now on slide 14, let's talk about the deal structure. We are acquiring all of VMware's outstanding shares for approximately $61 billion in a 50% cash, 50% stock transaction. Additionally, we are assuming VMware's $8 billion of net debt. VMware shareholders will have the option to elect between receiving $142.50 in cash or 0.252 shares of Broadcom common stock for each of their shares. We expect VMware shareholders to own approximately 12% of the pro forma company at close.

The transaction will be financed with $32 billion in new fully committed debt financing from a consortium of banks. We are committed to a strong balance sheet and we remain steadfastly committed to our investment grade rating. The acquisition is subject to regulatory approvals and other customary closing conditions, including approval of VMware shareholders. Michael Dell and Silver Lake have agreed to vote in favor of the transaction and we expect the transaction to close in our fiscal 2023. The merger agreement does include a 40 day go-shop provision.

I'll hand it over to Kirsten who is going to go through the financial results of the quarter and provide an update on our capital allocation policy.

Kirsten Spears {BIO 19712531 <GO>}

Thank you, Tom. Let me now provide additional detail on our financial performance. Revenue was $8.1 billion for the quarter, up 23% from a year ago. Gross margin was 76% of revenue in the quarter and up 145 basis points year-on-year. Operating expenses were $1.2 billion, up 8% year-on-year driven by investment in R&D. Operating income for the quarter was $4.9 billion and was up 30% from a year ago. Operating margin was 61% of revenue, up approximately 345 basis points year-on-year. Adjusted EBITDA was $5.1 billion or 63.1% of revenue. This figure excludes $135 million of depreciation.

Now a review of the P&L for our two segments.

Revenue for our semiconductor solutions segment was $6.2 billion and represented 77% of total revenue. This was up 29% year-on-year. Gross margin for our semiconductor solutions segment was approximately 72%, up 290 basis points year-on-year, driven by favorable product mix and content growth in next generation products across our extensive product portfolio.

Operating expenses were $873 million in Q2, up 10% year-on-year. R&D was $772 million in the quarter, up 10% year-on-year. Q2 semiconductor operating margins increased to 58%, so while semiconductor revenue was up 29%, operating profit grew 42%.

Moving to the P&L for our infrastructure software segment. Revenue for infrastructure software was $1.9 billion and represented 23% of revenue. This was up 5% year-on-year. Gross margin for infrastructure software was 90% in the quarter, up 10 basis points year-over-year. Operating expenses were 374 million in the quarter, up 5% year-over-year. Infrastructure software operating margin was 70% in Q2 and operating profit grew 5%.

Moving to cash flow. Free cash flow in the quarter was $4.2 billion, representing 51% of revenue. We spent $85 million on capital expenditures. Day sales outstanding were 35 days in the second quarter and we ended the second quarter with inventory of $1.7 billion. We also ended the second quarter with $9 billion of cash and $39.5 billion of gross debt, of which $302 million is short-term. With liability management activities during the quarter, we were able to extend our weighted average debt maturity from 10.4 years to 10.9 years, with the weighted average interest rate relatively unchanged at 3.6%.

Turning to capital allocation. In the quarter, we paid stockholders $1.8 billion of cash dividends. Consistent with our commitment to return excess cash to shareholders, we repurchased $2.8 billion in common stock and eliminated $514 million of common stock for taxes due[ph] on vesting [ph] of employee equity, resulting in the elimination of approximately 6 million AVGO a shares. The non-GAAP diluted share count in Q2 was 441 million.

Based on current business trends and conditions, our guidance for the third quarter of fiscal 2022 is for consolidated revenues of $8.4 billion[ph] an adjusted EBITDA of approximately 63.5% of projected revenue. Note that we expect Q3 non-GAAP diluted share count to be 439 million.

With the acquisition of VMware, let me now share our thinking on capital allocation policy going forward. Historically, over the last six years, we have grown free cash flow to increase at a 41% CAGR organically, and through acquisition. With the acquisition of VMware, we expect to enhance our already strong organic earnings and free cash flow growth.

The Board of Directors has approved a third quarter cash dividend on our common stock of $4.10 per share. Following the acquisition of VMware, we remain committed to our dividend policy of returning 50% of prior year's free cash flows as dividends. We are also committed to maintaining our investment grade rating and plan to rapidly delever from a approximately 3.5 times gross debt to EBITDA at closing, to normalized leverage ratios of less than 2.5 times gross debt to EBITDA within approximately two years post deal close.

Between now and deal close, we expect to generate considerable free cash flow. As it relates to the buyback, we have $3 billion remaining under the current authorization to date. In addition, we are announcing today an incremental $10 billion authorization to buyback shares through the end of December of 2023.

That concludes my prepared remarks. Operator, please open up the call for questions.

Questions And Answers

Operator

Thank you. (Operator Instructions) And our first question comes from Ross Seymore from Deutsche Bank.Your line is open.

Q - Ross Seymore {BIO 20902787 <GO>}

Hey, everyone. Thanks for let me ask the question and congratulations on the deal and the results. Tom, I wanted to ask a question on the VMware side of things. You gave a bit of a long-term model, mid-single digit revenue growth and then mid-single or mid-60s

EBITDA, can you talk a little bit about the revenue growth side of that equation? It seems like the VMware asset according to the Street[ph] is growing a little bit faster than that. What are you doing and assuming as far as the growth rate of that piece?

And then on the EBITDA side of things, out of the levers you showed on -- I think it's slide 13, can you just give us an idea of how those all fall in to get you to that mid-60s level overall?

A - Tom Krause {BIO 17978469 <GO>}

Sure, Ross, and thanks for the question. Let me start and then I'll let Hock embellish[ph]. When we think about the top line, a number of things going on. But fundamentally, and this is actually back on slide 7 (inaudible) deck. It's all about workload growth. Maybe think about private cloud growing mid to high single digital, to public cloud growing high-double digits. That's what's really going to drive the topline fundamental and that's actually got what it got us comfortable with the business here.

I think, in addition to that, we are going to focus on going through a transition, and a rapid transition from perpetual licensing to subscription. As you know with the software business, we've been totally focused on pretty much 100% recurring revenue and we see ARR[ph] growth being able to sustain that 5% if not faster when we think about the combined business.

When you think about EBITDA, there are multiple knobs. We covered that. You can look at slide 13. In terms of R&D, we're going to reinvest back in the core business, the core franchises. If you think about the three different pillars of this business, and I went through it, but it's really the core infrastructure business, vSAN, vSphere, vRealize, these are the businesses that are core to driving the bulk of the revenues and that's where the reinvestment is going to occur. We are going to focus on our common customers. We have a significant go-to-market engine here, at Broadcom Software, obviously, so does VMware in their own regard, actually much more significant than ours.,

And so we have a direct sales force, and we're going to leverage the fact that we have common coverage in both of those areas and take advantage of getting synergies there. But beyond that, we also see a very valuable channel. I think there are some things we've learned relative to the CA and the Symantec acquisitions in terms of the value of the channel, and we want to continue to support that channel, that's going to allow us to support a lot more revenues in a cost effective way, so we see some real opportunity to leverage that. And then, of course, as you all know, we run G&A at 1% of revenue, we've been integrating companies for a long time, we have tremendous scale, it's going to give us even more significant scale going forward and we think there's a lot of opportunity there to drive synergies from the redundancies we see.

Hock anything you want to add to that?

A - Hock Tan {BIO 1460567 <GO>}

Thanks, Tom. No. Well done on that on explaining it, but Ross, to answer your question pointedly, directly, on the revenue side and you can hear two dynamics going on. One is how we make the investment, where do we do the spending. The other top line is you can see that VMware has a perpetual model a lot in a lot of their on-prem licenses. We have a substantial 3 billion perpetual and we are converting to over time -- over the next couple of years, to subscription; and that will likely take from a reporting point of view, a slight dip but within three years, a recovery and a recovery back to a run rate that probably as Tom[ph] indicated -- it's probably higher than mid-single digits and well, we are structuring ourselves to go through that.

Now, from an economics point of view, whether it's perpetual or subscription, frankly, it's the same, but we want to make it very consistent with the way we run the model and based on this, we are in a sense restructuring the contracts, perpetual to subscription and that's why you, depending a way you see it, you will see a slower growth at the beginning, if any, followed by a more rapid growth as we convert more to subscription.

Q - Ross Seymore {BIO 20902787 <GO>}

Great, thanks guys.

Operator

Thank you. Our next question comes from Ambrish Srivastava from BMO. Your line is open.

Q - Ambrish Srivastava {BIO 4109276 <GO>}

Hi, thank you very much. Excuse me. Just getting back to following up on what Ross was asking, this asset is very different than the other two in terms of growth rate, growth trajectory. It doesn't seem like you would need to divest pieces of the business that you had to in the other two, can you just talk us through the synergies that you see in combining these businesses and if these businesses, in parts, have had partnerships in the past and how would you change that on a go-forward basis, and getting back to the (inaudible) into longer-term, this could be a faster growing software business than what you're laying out today? Thank you.

A - Tom Krause {BIO 17978469 <GO>}

Yes, no, certainly. I mean if you think about it from a go-to-market standpoint, that's where software companies spend the bulk of their dollars. The fact that we're going to go from 5 plus billion of software revenue to much closer to $20 billion is a big deal and the fact that we can leverage the combined go-to market engine at that scale it gives us huge economies.

I think what we're going to be able to do is marry[ph] effectively, a direct sales force which covers the largest couple of thousand customers. These are large multinationals,it's across all the key verticals, primarily focused in North America and Europe, but also in parts of Asia, with a very significant channel partner arrangement. I think one thing we've learned is there is an opportunity to embrace the channel, the two-tier distribution model, with distribution partners and key value-added resellers.

There's also a big GSI opportunity, we work significantly GSIs on our side. So does VMware. And so when I look at that in its totality, what we can't do today, let given our scale, we can definitely take advantage of with the newfound scale between the two companies.

Beyond that, when you think about the R&D side of the equation, to dig deeper into it and follow up, when we talked about with Ross, when you think about what supports the development of software, there is a lot of what we refer to sometimes in the (inaudible) side Central Engineering.

So software business operations, this is the continuous delivery, continuous testing capability, the ability to continuously develop applications on a consistent basis, that's expensive. It requires having your own private data centers that are working with cloud providers and having the scale to be able to drive that kind of R&D investment over a much larger portfolio is also going to drive significant benefits.

So hopefully that helps answer your question. Hock, do you want to add anything to that?

A - Hock Tan {BIO 1460567 <GO>}

Well, again we're dancing around the central issue, which is we will keep -- we -- and we have seen is -- we invest in R&D and on the way, we do a lot of that if we have to. And it's all at the end of the day, is -- this is a great -- in terms of monetization, it's all about execution and that's in a nutshell what we are seeing here. We believe we will execute much, much different, hopefully better than what we have been seeing so far.

Q - Ambrish Srivastava {BIO 4109276 <GO>}

That's a good bottom line. Thank you.

Operator

Thank you. Our next question comes from Stacy Rasgon from Bernstein Research. Your line is open.

Q - Stacy Rasgon {BIO 16423886 <GO>}

Hi guys, thanks for taking my question. Tom, I found your comments on leveraging the new channel differently to be interesting, because I guess I'm going to oversimplify it, but your prior strategy was sort of the focus on the largest customers in kind of let the long tail sort of weather[ph]. Am I right in sort of thinking that you are sort of changing that now, you're going to be going after that long tail little harder because now you actually have the channel to do it?

And will that be like feeding into the other -- because it sounds like it'd be feeding into the other businesses as well. I guess maybe, could you talk a little bit more about how that business model is changing, especially in that like tail of smaller customers? What does that actually mean for the degree of cost synergies and everything that can come out of this relative to what you've seen before? And it doesn't sound like you're seeing that driving upside to the growth rate, you're still talking about mid-single digits, although, again, maybe there is some conservatism in that number.

Anything you can give us on maybe some of that change in the business model, especially around long tail of customers would be helpful.

A - Tom Krause {BIO 17978469 <GO>}

Yes. No, you're picking up on it, Stacy. I think a lot of it is because of the portfolio. (Technical Difficulty) -- Yes, Stacy, a lot of it's based on the portfolio and the breadth of capability that VMware has relative to where we sit today. You're right. When we bought CA, mainframe made up at least half the revenues, today's mainframe is still about 50% of the overall software business at Broadcom and that's very much levered toward about 500 accounts in what we call our strategic account area, which is a direct sales motion, and that's also where we sell a lot of opportunity to drive customer synergy with Symantec, and particularly around some of the Blue Coat and DLP activities that we were driving.

So that was the business model that made sense, that of course, meant we could drive operating margins and frankly, slightly north of 70%, because we didn't have to invest as much in our go-to-market motion. I think with VMware, when we look at it and we look at the fact that vSphere, going back to the core, serves over 300,000 customers and we look at the growth and that the company is driving with their more modern applications, whether it be for private cloud or public cloud, we see a much bigger opportunity. And so to support that opportunity, we need to invest in sales and marketing. So when you think about the 60s EBITDA margins that I was discussing and I think I said mid-60s, that's on a much bigger scale, but it's a lower EBITDA margin profile (inaudible) today. All of that variance is going back into the sales and marketing investment and we think from learning about how we experience VA and Symantec in frankly some of the revenues that we gave up, we think we can actually go back and reinvest in the channel and continue to drive revenue growth profitably. We don't want to walk away from the channel. We actually want to embrace it.

Q - Stacy Rasgon {BIO 16423886 <GO>}

That's helpful. Thank you.

Operator

Thank you. Our next question comes from Vivek Arya from Bank of America Securities. Your line is open.

Q - Vivek Arya {BIO 6781604 <GO>}

Thanks. I had a question on the process and then on the accretion side[ph]. On the process side, which jurisdictions will you need approvals from? Do you see any product overlap that any regulator could push back against and why is there a go-shop provision? And then on the accretion side, will this be accretive in year one, and I think Tom you said mid-60s EBITDA margin, is that for VMware only or is that for your entire software business? Because the rest of the software business is running closer to 70%, I believe. So just any thoughts on the process and the accretion would be very helpful. Thank you.

A - Tom Krause {BIO 17978469 <GO>}

Yes, sure. So this will be accretive out of the gates and it will get very accretive as we get through our integration process, as you look at the aggregate value here and then you look at the EBITDA expectations, we expect to drive double-digit cash on cash returns. That's always been our criteria and we think that's going to create a lot of value for shareholders.

In jurisdictions, we're going to file a number of areas. You'll see that in the filings when we're around the merger agreement, and everything else. But nothing -- ordinary there and then I won't comment much on go-shop or the sales and highly negotiated deal and there is a go-shop for 40 days.

A - Hock Tan {BIO 1460567 <GO>}

Clarifying, the mid-60s referred to VMware's standalone where we're driving in. And just to make it clear on handling where the long tail is, I think our strategy of focusing, as Tom indicated very clearly, on selling new products, on supporting the largest enterprises in the world, create their private cloud and beyond that, having a hybrid cloud structure will probably extend, as Tom indicated today, core 600 strategic accounts to a larger group of 1,500 accounts.

This is what is enabling us to do with VMware. And that will be direct focus and a lot of attention and support to get to drive revenue growth and adoption of the various new products and software stack that VMware has, especially in the realm of private cloud and software defined networks.

In terms of the longer tail of 300,000 customers, we do not -- as we perhaps had looked at before, we are looking at it very, very positively too -- in the sense that we will make sure these are well supported. This continues to be a business base that will grow, but we will go through it -- we will handle this, guys[ph] through partners as Tom indicated, distributors, resellers, GSI partners.

These will be handled, simplifying our business model, but we will not have a larger core group of global 1,500 and we call it that -- where VMware and its scale will now enable us to focus as we had focus on the last 600 before[ph].

Q - Vivek Arya {BIO 6781604 <GO>}

Thank you.

Operator

Thank you. Our next question comes from Harsh Kumar from Piper Sandler. Your line is open.

Q - Harsh Kumar {BIO 3235392 <GO>}

Yes. Hey, guys. First of all, congratulations on the deal. It sounds like an amazing deal. Hock, for a change, I've got a question on some of your business commentary related to organic Broadcom. You mentioned that in the networking business, you're seeing proprietary solutions from your customers losing out to Merchant Solutions and silicon that you guys sell.

I was curious, is there anything happened recently, which is driving this shift over to your solutions or was this just something in the making a long time and it's just now happening? And also if you can talk about supply concerns, you don't seem to be seeing any supply issues, whereas the other guys are, I'd be curious if you could provide color on that?

A - Hock Tan {BIO 1460567 <GO>}

Okay. Well, very interesting question on networking side. It's -- it has been a trend obviously, that has been happening for the last -- for over five years, which is in -- for us in networking, switching and routing, merchant silicon has been taking share over proprietary solutions, black box, so to speak. Merchant solutions enable disaggregation of hardware and software and then always offers more resiliency, more flexibility for customers, starts the hyperscale, we are now talking about service providers and enterprise. And what perhaps has -- may be triggering an acceleration which I indicated and may be --

Is probably related to the fact that -- where all, enterprises in particular, are now all in reinvesting upgrading after a hiatus, probably from 2019 cutting through to the pandemic timeframe. They are now investing in new data centers and they are now investing in -- basically modernizing their data centers and they are going for next generation and that, we figure, is what's triggering it.

We are seeing acceleration in our Tomahawk 3s and 4s. We are seeing a sell at the leading edge products, this and the Trident versions correspondingly. We are seeing acceleration in Jericho 2 series and the latest one on at the edge (inaudible) All these are the big drivers and it's almost a fast and more larger adoption and we would perceive under normal growth patterns.

I'll put it bluntly, we're gaining market share in merchant silicon over proprietary solution. And it's a -- it's an acceleration of a trend, there has been going on over five years. And we -- and that's grown fairly quick. And in terms of supply chain question, I always get this question and of course, I'll answer that point-blank for -- from over the past 12 months or so, we are challenged on making sure we meet demand. On a timely basis which is what they want and you look at it that way, we do not see a challenge necessarily in supply.

We rather -- we see as a demand -- constant demand challenge in the sense that we have to pass through our backlog carefully and as I indicated, in the last three months, we just (inaudible) our backlog substantially and it's -- and it doesn't -- we -- in spite of lead times being unchanged -- extended and unchanged. So there is demand out there and it keeps coming in for products, and now it's particularly slow in couple of areas. It's not necessarily across the board, it's in a couple of areas and we happen to be very lucky to be in those areas that are still strong, luxury[] related to infrastructure.ph

We are seeing in that in networking that includes both hyperscale, telcos, service providers, as well as in enterprise and particularly in enterprise, we are seeing that -- we are seeing an embellish a lot I might add, by content increase in server storage connectivity, where we're now selling in the newer generation, as I indicated, in the last earnings call, subsystems, where our customers prefer buying subsystems from us rather than just a chip and that step up content dramatically, and couple that with still continuing strong demand in these two space, we're seeing continuously, not just revenue accelerating, but bookings accelerating.

And there's a real demand and we have of course a supply to meet those critical needs as we see it.

Q - Harsh Kumar {BIO 3235392 <GO>}

Fantastic. Congratulations, guys. Thank you.

A - Hock Tan {BIO 1460567 <GO>}

Thank you.

Operator

Thank you. And we'll take our last question from Toshiya Hari from Goldman Sachs. Your line is open.

Q - Toshiya Hari {BIO 6770302 <GO>}

Hi, good morning. Thank you so much for squeezing me in. And, Hock so after the acquisition, your business is going to be roughly 50% semis and 50% software. I was hoping you could remind us some of the pros and cons for running these two businesses under one umbrella? And assuming the deal successfully closes, would you ever consider splitting up to two businesses, particularly if you feel like you're not getting the valuation that you deserve? Thank you.

A - Hock Tan {BIO 1460567 <GO>}

To answer, right to the bottom line, we see a lot of benefits in putting all this various franchises we have, hardware and software under one umbrella. Think of it this way,Toshiya, it's like one merchant silicon is driving that trend. It's -- you know -- the old model is -- you sell a black box, hardware and software system to a customer in the IT department -- to JP Morgan IT department. That's what you do in the past and something goes wrong, hell, you ask for support is, you scream from help, because you don't know what's going on inside the thing.

We are creating a model of disaggregation between hardware and software. We may still not know much about systems, but we sure know the technology that enables systems, whether they are switches, routers, compute storage and this is -- Broadcom is a model of disaggregating hardware and software and combined, I think we are stronger than[ph] divided. So I hope that answers your question.

Q - Toshiya Hari {BIO 6770302 <GO>}

Thank you.

Operator

Thank you. And that does conclude our question and answer session for today's conference. I'd now like to turn the call back over to Ji Yoo for any closing remarks.

A - Ji Yoo {BIO 21112206 <GO>}

Thank you, operator. As we have released the results of Broadcom Second Quarter of Fiscal '22 today, we will no longer hold the conference call previously scheduled for Thursday, June 2. Broadcom currently plans to report its earnings for the third quarter of fiscal '22 after close of market on Thursday, September 1, 2022. A public webcast of Broadcom's earnings conference call will follow at 2:00 PM Pacific Time. That will conclude our earnings call and -- call today. Thank you all for joining. Operator, you may end the call.

Operator

Thank you. This concludes today's conference call. Thank you for your participation and you may now disconnect. Everyone have a wonderful day.