

Good day ladies and gentlemen, and welcome to the Intel Q3 2012 earnings call. At this time, all participants are in a listen-only mode. Later, we will conduct a question-and-answer session and instructions will follow at that time. As a reminder, this conference call is being recorded.

I would now like to introduce your host for today's conference, Mark Henninger. Please go ahead.

Mark Henninger

Thank you, Patrick and welcome everyone to Intel's third quarter 2012 earnings conference call. By now you should have received a copy of our earnings release and the CFO commentary that goes along with it. If you've not received both documents, they're currently available on our investor website intc.com. I am joined today by Paul Otellini, our President and CEO and Stacy Smith, our Chief Financial Officer. In a moment, we'll hear brief remarks from both of them, followed by the Q&A.

Before we begin, let me remind everyone that today's discussion contains forward-looking statements based on the environment as we currently see it, and as such does include risks and uncertainties. Please refer to our press release for more information on the specific risk factors that could cause actual results to differ materially. Also, if during the call, we use any non-GAAP financial measures or references, we'll post the appropriate reconciliations to our website, intc.com.

With that, let me hand it over to Paul.

Paul Otellini

Thanks, Mark and good afternoon everyone. Our third quarter results came in slightly above our revised guidance as PC related billings improved in September over the July and August levels. We believe that Q3 PC sales grew approximately half of the seasonal norm and reflected flat enterprise sales. The billings upside we saw late in the quarter reflected our customers beginning their system production in advance of the Windows 8 launch later this month.

As we look into Q4, we believe that the overall PC business will grow at about half of what we would expect from normal seasonality. Our revenue forecast growth is below these levels as our customers are taking a cautious inventory approach in the face of market uncertainty and the timing of the Windows 8 launch. Our forecast assumes an incremental decrease in inventory at our customers going into year end.

Our Data Center business saw the Corporate Server segment softening over the course of the quarter, with the Cloud segment growing 50% over last year and storage revenue growing 27% to a new record. During the last month, I have met with all of our major customers and while the market remains tough, I have been encouraged to see a renewed appetite for innovation across the entire ecosystem.

Our customers are designing entirely new categories of PCs that will take advantage of our new microprocessors combined with Microsoft's new touch enabled Windows 8 operating system to bring dozens of beautiful new tablet, convertible and Ultrabook designs to the market.

In the coming months consumers will see tremendous form factor and industrial design innovation. There will be more than 140 Core based Ultrabooks, more than 40 of which will have touch. This will include more than a dozen convertibles that combine the productivity of the laptop with the convenience of a tablet.

Many of the Ultrabook SKUs will hit the mainstream \$699 price point with some Burst SKUs well below even that number. Q4 will see more than 20 Atom based tablets from six or more leading OEMs using Clover Trail. Clover Trail is a brand new SoC that will enable tablets as thin as 8.5 millimeters and as light as 1.5 pounds.

With three weeks of connected standby battery life and all of the compatibility that Windows users and Intel customers have come to expect, I am excited about these products and the capabilities they bring to consumers and the enterprise.

Last month at IDF, we shared details of our next-generation Core processor codenamed Haswell. Originally targeted at 15 watts, we have made significant advancements in micro-architecture and process technology that will allow us to move Haswell down into the 10 watt envelope fostering even more innovation in form factor as well as new usage models like gesture computing and voice recognition.

We continue to make progress in handhelds with Motorola's launch of the RAZR i, the world's only two gigahertz smartphone that delivers better battery life than similar computing devices. In general, I see the computing market in a period of transition, but also a period of breakthrough innovation and creativity.

Intel has a history of navigating the industry's transitions and emerging better and stronger. With the hardware and software roadmap that spans the smallest portable devices to the most powerful datacenter servers and

world leading silicon process technology, we are excited about the future and confident in our strategy and prospects in all the markets we serve.

With that, let me turn the call over to Stacy.

Stacy Smith

Thanks, Paul. Third quarter revenue came in at \$13.5 billion flat from the second quarter and slightly better than our revised expectations. For the fourth quarter of 2012, we are forecasting the midpoint of the revenue range of \$13.6 billion, up 1% from the third quarter. This slight increase in revenue in the fourth quarter reflects the caution we are seeing in the order patterns of our customers as a result of concerns about the global environment, ongoing consumer softness in mature markets and a slowing enterprise market segment.

As a result of weaker than expected demand environment, we are taking several actions. We significantly cut factory loadings at the end of the quarter and we will maintain low factory utilization rates throughout the fourth quarter. We expect these factory adjustments to help bring down our total inventory levels by approximately \$0.5 billion. Additionally, we are redirecting equipment and space to 14-nanometer from older generation technologies. The result of this is a \$1.2 billion decrease from our July forecast for capital spending with the midpoint of our capital spending forecast for the year now at \$11.3 billion.

Moving to gross margin; third quarter gross margin of 63% was slightly better than the midpoint of our revised guidance and flat to the second quarter. We are forecasting the midpoint of our fourth quarter gross margin range to be 57%, down 6 points from the third quarter. Two-thirds of the gross margin decline is a result of that excess capacity charges. In addition, we expect an increase in inventory reserves as we start production on our next-generation micro-architecture product codenamed Haswell which we expect to qualify for sale in the first quarter of 2013.

Taking a look at the balance sheet, total cash investments ended the quarter at \$10.5 billion, down approximately \$3 billion to the second quarter. We generated over \$5 billion in cash from operations; paid approximately \$1 billion in dividends; repurchased nearly \$3 billion in capital assets and had roughly \$1 billion of stock repurchases. In addition, we closed our \$3 billion strategic equity investment in ASML.

As a result of lower than expected sales in the third quarter inventory grew by approximately \$400 million. More than all of the increase in inventories came from the Ivy Bridge product ramp with an offset as we reduced inventory levels of older generation products.

We are taking aggressive tactical actions to reduce inventory levels and redirect space and equipment 14-nanometer and we are also seeing some important positive trends in the markets. In the client space, we are seeing innovative products coming to the market with Intel Inside, ranging from Ultrabooks, to smartphones to tablets.

In the Data Center, we expect to continue to benefit from the dole out of the Cloud and a substantial performance cost and power benefit that our enterprise customers get from our leadership products. Underlying all of this, our manufacturing advantage is extending over the rest of the industry as we start to ramp-up Haswell, our new micro-architecture on 22-nanometer and begin to build-out our 14-nanometer factory network. The combination of the tactical actions we are taking coupled with new products and design wins across all segments and our manufacturing leadership will all benefit our business over the coming quarters.

With that, let me turn it back over to Mark.

Mark Henninger

Alright, thank you Paul and Stacy. We'll now go ahead and move on to the Q&A. As is our normal practice, we'll ask each participant to ask one question and just one follow-up if you have one. Patrick please go ahead and introduce our first questioner.

Question-and-Answer Session

Operator

(Operator Instructions) Our first question comes from Ambrish Srivastava from BB&T [BMO Capital Markets]. Your line is open.

Ambrish Srivastava - BMO Capital Markets

Last I checked, I was from BMO, hi guys. First question is Stacy, just on the startup cost cadence, given that you are moderating the 14-nanometer a little bit. Typically, if I remember correctly, it's a two quarter cadence, how does that play-out this time around?

Stacy Smith

I am not seeing anything that would cause it to be off of historical patterns. So if you look at what's happened in odd number of years when we started the new process technology, you'll see a increase in startup costs that hits pretty significantly in Q1, goes up some more in Q2 and then it will start to

come down from there. So I am not seeing anything that would cause that to be different from historical patterns.

Ambrish Srivastava - BMO Capital Markets

And then my follow-up is on the CapEx Stacy, does that change from what you had given us during the 2012 Analyst Day for 2013?

Stacy Smith

Yeah, we're not putting out a forecast yet for 2013 CapEx yet; we're reducing '12 capital pretty significantly. 2013 will be a function of the unit growth that we see in '13 and our expectations for '14. Right now, we want to fight through the Q4 where we don't have a lot of visibility before we lock in on 2013 number.

Operator

Our next question comes from Doug Freedman from RBC Capital. Your line is open.

Doug Freedman - RBC Capital

Stacy, you gave a number at the Analyst Day regarding full year 2013 gross margin. Can you give us some idea what range you are looking at now that you are taking the actions you are presently communicating today?

Stacy Smith

Yeah, we will provide a forecast for 2013 when we get to January, so again similar to the prior question, I think it's premature to provide a forecast at this point across revenue or gross margin or CapEx for '13. We need to fight through Q4 first.

There is a couple of things that I think you can model for '13 though that are helpful, we've just talked about the startup costs. We are starting up 14-nanometer, so historically that's worth two to three points of gross margin.

In terms of excess capacity charges that we are taking, we are taking a lot in Q4. I think we'll see that significantly better in Q1 and by then by the time we get to Q2, I don't expect really any excess capacity charges. So yeah, you will see that play out.

And just to size those two things in Q1, I think the excess capacity charges and the startup costs are kind of roughly similar orders of magnitude; so those two things should offset. Beyond that, wait till we get to January because there are just many other moving parts for 2013.

Doug Freedman - RBC Capital

So as my follow-up, on the revenue side we did see some movement this quarter, probably not completely expected, PC Clients a little bit better than maybe you might have expected when you pre-announced. The Data Center, however, though has seen some ASP movement that caused that revenue to be soft. Can you communicate to us what your outlook is as far as the revenue mix for next quarter and maybe what that might do to our gross margin number?

Stacy Smith

Yeah, so just to come back to Q3 for a second and then I'll answer your question on Q4. What we saw specifically in the Client side, it played out roughly as we thought when we did the preannouncement and if you step back from that, what we saw was some growth in consumption. But our customers continuing to manage inventories very lean, and in fact we saw across the worldwide PC supply chain, we actually saw a reduction in overall inventory levels in Q3, and normally in Q3 you would see an increase, so you can kind of get a sense of how lean they are managing things.

In the Data Center, what we saw was strong growth in the internet IP datacenters, the Cloud, that was up actually 50% from a year ago. It was offset, but we started to see some weakness on enterprise side and that's where you are seeing the lower ASPs just because of the difference in ASP between those two segments.

As we go into Q4, in terms of the overall mix of our business, I'll direct you to the gross margin recon, there is an issues there with the excess capacity charges. We have some builds on Haswell; really ASP is not impact any gross margin and so you can take from that that we expect it to continue to be kind of similar mix in a roughly benign ASP environment.

Operator

Our next question comes from John Pitzer from Credit Suisse. Your line is open.

John Pitzer - Credit Suisse

Paul, how do you assess how much of what's going on in the PC market right now; is macro, timing of Windows 8 versus kind of the more structural bearish view that tablets and smartphones are just plain and simple eating into PC TAM. How do you think about those dynamics?

Paul Otellini

I think it's a bit of each and I would be reticent to quantify it John. Clearly, we saw a softening in the consumer segments. We talked about that when we did the pre-announcement about a month ago and the surprise there was that China which had been very strong in those current week on us on top of continuing weakness in the mature markets of U.S. and Western Europe.

However, having said that, we do believe that when the numbers are all in, the PC consumption did grow in Q3 at about half the normal seasonal rate and will also grow in Q4 about half the normal seasonal rate. How much of that happening is macroeconomic versus the timing of the Windows 8 builds and the share of wallet, war for tablets versus PCs is TBD, and we'll know a lot more about that 90 days from now after the Windows 8 launch, after we see Intel based tablets start shipping, when people start playing with the operating system and have all the touch based Ultrabooks out there. We'll know a lot more. So we'll try to quantify that a bit more for you in 90 days, but right now it's a bit of each.

John Pitzer - Credit Suisse

And then guys as my follow-up Stacy, I appreciate the fact that it's too early to talk about next year CapEx, but underutilization in Q4 is clearly helping you kind of lower this year's CapEx a bit and back in '09 off of about half the CapEx base, I think the underutilization is around the credit crisis saved you about \$1.5 billion in capital spending. Is this going to hold where as we go into '13, the lack of underutilization will allow you to save on CapEx and if you are twice the base then can we think about \$3 billion number in total?

Stacy Smith

I am not going to get to that level of granularity. You can see that 2012 capital spending is down \$1.2 billion from what we thought a quarter ago. Although, we have some indications that we were trending down a little bit and so you know that's a big chunk and we'll talk about '13 when we get to January.

Operator

Our next question comes from David Wong from Wells Fargo. Your line is open.

David Wong - Wells Fargo

Thanks very much. You commented on Clover Trail tablet; are you seeing many Ivy Bridge tablet designs in addition to the Microsoft Surface and can you give us some idea of how many tablet makers you are currently working with on Haswell tablets for the future?

Paul Otellini

I can help you on the former, not the latter. On Ivy Bridge, you know, there is, I would say, a handful, five to eight, something like that that I've seen off the top of my head. And for Haswell, it's too soon to tell, I mean we have, when you start seeing an Ultrabook with a detachable touch screen, is it a tablet and it's based on Haswell, so the tablet is an Ultrabook or is it a convertible, you know, I don't know; lots of inventive names for these things as we go along. What I can tell you is that the level of innovation there is really unbounded; I haven't seen this in a long time.

But, I think in terms of, just little bit near term selling season, there are some Ivy Bridge ones. They tend to be skewed more towards to the enterprise, where our customers believe that their customers, the CIOs of the world want a high performance tablet that is compatible, that is secure and that runs all their enterprise software. So I think that's where you'll see those migrate versus I think Clover Trail stuff which was going to be a bit more consumer centric.

David Wong - Wells Fargo

Great. And, you said you expect to qualify Haswell in the March quarter, will Haswell be appearing in systems in the March quarter or should we look for that a bit later in the year?

Paul Otellini

The first half.

Operator

Our next question comes from Christopher Danely from JPMorgan. Your line is open.

Christopher Danely - JPMorgan

Thanks guys. So Paul can you just give us maybe just your take on what you think is going to take to pull the PC industry out of this slunk? And do you think that with the advent of tablets cannibalizing notebooks that we're never going to see the growth in PCs we used to; is it going to be something lower than what we have been used to?

Paul Otellini

Again, since we don't know how much of the flatness that we're seeing this year in PCs as a function of which of those variables that we talked about earlier, it's pretty hard to say that in good economic cycles that we wouldn't

return to normal growth. But, what I get back to as I look out here, I don't think and I said this to you guys before, I don't think that the tablet as we've seen it evolve over the last several years is the end state of computing.

The innovation is going to start pouring in now that you have widely available SKUs on a widely distributed operating system that will come from multiple vendors that can unleash their creativity. And, what I can't predict is what form factor is going to win here, but I do think that some of these things that have sort of the best of both worlds, the performance and the capability of a laptop and the form factor and convenience of a tablet, are likely to be the things that are most high volume earners, but we honestly won't know for 12 months.

Christopher Danelly - JPMorgan

Thanks. And a follow-up question for Stacy, just a clarification on the Q1 gross margins Stacy, so you've given us what the utilization rates, underutilization cost look like. If we look at typical seasonality for Q1, you guys are probably down like a \$1 billion or something like that. So if sales are down \$1 billion and depreciation is up a little bit and startup costs are up, can the margins be flat with current utilization rates and what would inventory look like?

Stacy Smith

You are trying to back me into a forecast, a few lines and I hear that, I would maybe make a couple of comments though to your thesis. One is, based on what we are seeing in the back-half of this year I am less convinced that normal seasonality is a great guide. What we are seeing is that the customers are managing things very cautiously; depending on how sales go, you know I think yeah, multiple different outcomes for Q1 and we will get there in a quarter.

In terms of inventory levels, we are too high today, because the unit volume that we expected in September didn't materialize, we were under on what we thought from Q4, that's one of the reasons we're bringing that the utilization down; lowering inventory levels down significantly in Q4 back into a healthy range and our intent would be to keep them in that range.

Operator

Our next question comes from CJ Muse from Barclays. Your line is open.

CJ Muse - Barclays

Yeah, thank you for taking my question. I guess just as a follow-up on the inventory side. Can you discuss what you have seen downstream particularly in China and then also as part of the healthy days, my math suggest exiting December at roughly 75 days. Is that kind of the new normal we should think about for you guys in a lower PC growth rate environment or do you think that you need to be some thing lower?

Paul Otellini

Let me try the China one CJ, and Stacy will come to the inventory.

Stacy Smith

And I'll do the second. Yeah.

Paul Otellini

I was just in China a week and a half ago, so there is a fairly current view. I see the same situation. China as a manufacturing center is reflecting the comments that we had in our commentary which is that the OEMs are being very cautious with their inventory comments at this point in time for all the reasons we've discussed and it's as lean as we've seen it in normal times without the shortage of let's say their hard drives of last year.

In terms of the channel inventory, there really isn't very much. I went into Tier 3 city, you don't see things stocked up or sacked up on pallet and stuff. People are generally -- I think most of our customers worldwide spent a lot of Q3 thinning out their Windows 7 inventory, so they wouldn't have an overhang at the launch. And that accounts for a lot of this inventory shipped of our billings versus the consumption that we've been talking about. And now with the launch of Windows 8 coming in a week or so, you'll see a new round of build and hopefully consumption.

Stacy Smith

Yeah and in terms of the inventory targets, the number you threw out is in the 70s is where we're planning to get to in Q4. Just to put that in perspective maybe two other comments on what we're doing. One is we are taking down utilization in the factories down to sub 50%, again to take inventory out and free up the opportunity to move both space and equipment and redirect that to 14-nanometer. So it's a pretty significant series of actions. And I also want to point to the inventory that we have in place while it's in terms of units more than I want to hold. It's on the order of 70% Ivy Bridge, so it's our freshest stuff. I am not worried about the salability of the inventory, but I do want to bring the Ivy Bridge inventory levels down. It's just healthy for us to have less.

Operator

Our next question comes from Kevin Cassidy from Stifel Nicolaus. Your line is open.

Kevin Cassidy - Stifel Nicolaus

And maybe along those lines of the utilization or underutilization, in last year's Investor Meeting, Andy Bryant had presented and his presentations around the risk of too much capital spending and that Intel had one more fab building that needed what we would do; is this part of that plan; are you mothballing one building?

Stacy Smith

I would say it's more down the line of my presentation where I showed you that we're constantly trying to match our capacity that's in place to the demand. We are putting in capacity for bigger second half than we got. We are going to now make adjustments, so that we can move capacity to 14-nanometer and bring our inventory levels down.

It doesn't change the fact that our planning model, we're always looking to make sure we have the ability in terms of what we call white space to some unallocated factory space as well as some equipment to respond to upsides. The risk of being caught short and the cost of being caught short is much more than the cost of being long, because as you can see when we get a little long, we can take actions and within a six month period, we can get back aligned. If you are sure it can take you two years to get caught back up.

Kevin Cassidy - Stifel Nicolaus

And with the reuse of equipment, can you give an idea what percentage that is that can be reused from 22-nanometer to 14-nanometer?

Stacy Smith

It's not different than our historical pattern. So you could think of it in the range of 80% to 90% of the equipment that we buy and 22-nanometer is usable at the 14-nanometer nodes. And that's not by accident. It's one of the things that technologists spend a lot of time to make sure we have these forward reuse paths because it gives us great flexibility to respond to things like we're seeing today.

Operator

Our next question comes from Daniel Berenbaum from MKM Partners. Your line is open.

Daniel Berenbaum - MKM Partners

When you talk about clearing inventory, does pricing come into play in any fashion on the PC, just talk about pricing a little bit on the Data Center side, clearing inventory on either the consumer side or the enterprise side, is that helping? And then follow-up also a little bit on an earlier question, is there anything else that Intel can be doing to spur demand? We've already seen sort of Microsoft take matters a bit into their own hands with some of the designs that they are trying to sell; is pricing help you spur demand or is there something else that you can do?

Paul Otellini

The short answer to your question is no on pricing. We do forward pricing with our customers. It's priced I think aggressively to move into the mainstream price points in terms of the stuff I talked about. If you look at our PC group numbers quarter-over-quarter, the ASP was about flat year-over-year. It was down a bit, mobile was down a bit. What that reflects was really us going after some incremental share at the bottom of the market, so didn't really change pricing but it changed the mix, and we thought it was time we could do some of that and we did it opportunistically. That's more the driver on that side.

In terms of demand stimulation, a lot of what we are doing is really to make sure that the feature set of this season's Ultrabooks are really consistent with where the market is, that's why we've been so focused on working with our customers and the ecosystem just, for example, bring the touch SKUs in. So six to eight months ago that we did not have line of sight to 40 out of a 140 SKUs of Ultrabooks being touch enabled, it was probably five or 10; we are up to 40 now, and that's just going to get bigger as we go into 2013. So working with the vendors and the glass manufacturers to bring the cost of touch as an increment down has been one of the key things we think we can do to drive demand.

Daniel Berenbaum - MKM Partners

And related to pricing, you've obviously got a wounded competitor out there now. Are you seeing that competitor get aggressive on pricing, especially in this environment? Your competitor talked about a big inventory write-down in its negative preannouncement; are you seeing lower pricing there and is that in any way impacting you?

Paul Otellini

I think you would have to ask them their strategy for pricing. As Paul said, we had last quarter and this quarter, we believe, we've won some share at the lower end of the market; that's our strategy here. So you've got to ask them the question about their pricing strategy.

Operator

Our next question comes from Jim Covello from Goldman Sachs. Your line is opened.

Jim Covello - Goldman Sachs

Guys, kind of a question stand on the margins. In the context of cyclical history, what we are seeing here isn't too unique from the standpoint of the margins usually decline pretty significantly on the other side of the big CapEx cycles. I think the average margin decline is 700 basis points. The peak is 1,300 basis points. You are down about 1,000 basis points now from the peak gross margins, so pretty normal. Is there anything you see in that context that would cause this margin decline to be worse than some of the more dramatic declines you've seen historically?

Stacy Smith

Right; I think that when you go back and look across the long range of history, when we have seen a situation where the industry got a head on capacity, the time that it took to get things realign typically was much longer than two quarters. I think we have done a lot to improve the responsiveness, and I think that has been helpful and you saw that in 2009, but if you go back before that as opposed to a couple of quarters, you are sometimes starting at couple years to get capacity back in line. I think that's different.

And then the other thing I would point to that's different is while the decline is significant and we are taking some excess capacity charges, if you compare what we're going through now with 2009, in 2009 we were into the mid to high 40s; now we're in the mid to high 50s and I think that really points to the structural improvements we made in our business in terms of cost and mix and the competitiveness of our products, and so while it may have seem the same to you but actually I think it's faster and we are still maintaining a higher gross margin.

Jim Covello - Goldman Sachs

So my follow-up question stands specific to the Data Center Group, some of the ARM based server players are arguing that they can now address a significant part of the workload from the Google's and the Amazon's and

Facebook's data centers. Is that some competitive dynamic that you're seeing in that area or do you think that ARM still isn't competitive in that realm?

Paul Otellini

They need to add features sets like 64-bits and ECC and RAS features to be particularly in those environments to be considered, so that maybe a roadmap planning opportunity that they are pushing but the products that are being shipped today certainly don't have those feature sets.

You can look at some of the workloads, things like Hadoop, Jim that would be conducive to let me say in a ray of micro servers, and those can easily be run on Atom; we've got our second generation of the Atom micro server chips out now, the first one is on 32-nanometers. Now we're now sampling the 22-nanometer one and what we've decided that we are just going to push Atom as hard as possible in this space and have it be a better offering for our customers than having to switch all their software and worry about all the reliability features.

Operator

Our next question comes from JoAnne Feeney from Longbow Research. Your line is open.

JoAnne Feeney - Longbow Research

Yeah, I was hoping you can elaborate a little bit more on what you are seeing and what you saw last quarter and what you expect this quarter in terms of the mix of demand, both across consumer and enterprise geographically and then PC, you know, notebooks, desktops; just some more color if you would on what kind of mix you are seeing out there and where you expect it to go and what you're relying on to get those inventories clear say by the beginning of 2013?

Paul Otellini

Well, let me start with the last part. The inventory, I think is straight forward. The work-in-process and finished goods that we're expecting to come down over this quarter are our Ivy Bridge products which is the mainstream high-end product we have today. And as the market picks up, Windows 8 launches, Ultrabooks pick up and so forth then that just consumes that inventory. And as I said earlier, in my comments and Stacy's, our OEMs are running very lean right now. So any kind of demand blip would cause us to be able to reduce that even more perhaps.

In terms of the mix, there is really not much more to add than we put in our pre-release and in the comments today which is that the U.S. and Western Europe PC markets remained soft in terms of consumers. The change that we have seen and we talked about at the pre-announcement was that the enterprise PC market has gone relatively flat now and I think that's just a reflection of large corporations making hard decisions on CapEx versus people, and where they want to put their investments and now that seems to have spilled over from the client side of the enterprise also the data center server part of the enterprise. And you know I think we will see how that sorts out over the next quarter or so as CEOs and CIOs make their next round of decisions.

In terms of China, the slowdown there was – it's principally a notebook business and the slowdown there was in consumer notebooks.

Stacy Smith

And I'll just add in the DCG, we saw strength in the Cloud customers and over the course of the quarter weakening in the large enterprise purchases of server chips. So the mix there was more towards the Cloud.

Paul Otellini

Mix had been strong in the first half.

Stacy Smith

Mix had been strong in the first half, yeah.

JoAnne Feeney - Longbow Research

And then as a follow-up, Stacy could you let us know what happened with units versus ASPs in PCs versus servers last quarter?

Stacy Smith

Yeah, it's actually in the CFO commentary JoAnne, but in general we saw PC units up 1% versus the prior quarter and datacenter units were also up 1%. This is a quarter-on-quarter compare.

JoAnne Feeney - Longbow Research

Sorry, and the ASPs?

Stacy Smith

The PC ASPs were down 1% and the server ASPs were down 7% based on the mix kind of things that I have been talking about.

Operator

Our next question comes from Patrick Wang from Evercore Partners. Your line is open.

Patrick Wang - Evercore Partners

Great, thanks so much. First question, I want to see if we can go back to China and Paul may be kind of recap some of the feedback you are hearing from those meetings you did have, because it seems like the slowdown in China is really impacting global PC demand and weakness out there. So just curious what the latest you are hearing?

Paul Otellini

Well, what I don't know is how much of this is and China is in their own macroeconomic cycle slowing down, I mean the GDP forecast for the year have come down for next have come down. There is also a reasonable amount of anxiety around the change in government and that tends to put a little bit of nervousness into the system and what I don't know is how much of that clarifies after they change, because it's not so much they don't know who is coming in. The issue is what are the policies, in terms of stimulus and taxation and so forth. They have been pretty generous the last year or so, a year or two rather, in terms of stimulating domestic consumption and the question is will those policies continue or not.

Patrick Wang - Evercore Partners

I want to talk quickly about Data Center. The trend that we're seeing in ASPs right now are down since the last quarter; I am just kind of curious how you see that over the next couple of years, because when we take a look at your Cloud segment, you're forecasting pretty robust growth there. You talked about 50% growth last quarter. As that continues to really outstrip growth from your more traditional server customers, what kind of impact does that do to your blended ASPs?

Paul Otellini

Well, I think the better comparison for us the Data Center is year-on-year, for which the ASP was up a bit, up 1%. The down a bit was really a big shift in the mix between what would be normal enterprise growth and of slowing in the enterprise growth. In general, for storage, for networking and I think for some aspects of the internet data center the mix was actually quite good.

Sometimes they – two way machines versus four way machines, but they tend to be fairly high mix and one of the fastest growing elements of the business is high performance computing which buyers buy at the top of the line of our skews. As those product lines get flushed out more and more, I really don't see the mix shifting away from where it's been in the first half of this year; I see the current mix being a bit of an anomaly as a result of the softness of corporate datacenter server purchases.

Mark Henninger

Thanks Patrick and operator we have time for two more questions.

Operator

Our next question comes from Glen Yeung from Citi. Your line is open.

Glen Yeung - Citi

Stacy, maybe the first question for you. As you sort of think about your capacity for 2013 and you are obviously taking action now, what kind of PC environment are you notionally targeting and maybe just in up or down is sufficient unless you want to be more specific?

Stacy Smith

Yeah, I am going to be less specific. If you wanted the other, yeah either up or down; hold off on triangulating on a capital forecast or on a unit growth until we get to next quarter. The CapEx number as I said is going to be really be dependent on where we think unit growth is in '13 and '14 and right now we're fighting through Q4. There is a lack of visibility on the current quarter; I want to have the 90 days to really think about what we want to put in place.

Glen Yeung - Citi

And then Paul maybe next question for you. Notionally, we won't expect to see when we have an operating transition like we're seeing a spark to PC demand and yet we don't seem to be seeing that and I wonder if you could just give us your thoughts as to why you think this time that's not happening?

Paul Otellini

Yeah, I don't think, we know it's not happening yet. I am very excited about this new operating system. As I said earlier, it brings touch into the mainstream for the first time and we know that in the last couple of years the tablets have changed the paradigm for people to use computers, they

like touch, they like to make the photos get larger with their fingers and everything else is good about that. And so I think we haven't had a chance to really judge how the consumers will embrace this in the mainstream PC space or not.

I am very optimistic as we've been playing with these things and we see the products being built and we take them out for testing to consumer and we've now on test on Windows 8, touch enabled Ultrabooks in number of the major cities around the world, across multiple demographics. The feedback is universally positive. So I think we're just too soon to tell. The designs aren't even launched yet and we'll know a lot more about this 90 days from now.

Mark Henninger

Patrick, please go ahead and introduce our last questioner.

Operator

Our last question comes from Sumit Dhanda from ISI. Your line is open.

Sumit Dhanda - ISI

Yes hi, two questions. First question for you either Paul or Stacy, you know you noted that inventories are lean and you expect half the normal seasonal growth in PCs, but you're dialing down that number. If the set up is lean from an inventory perspective, why are customers choosing to take down inventories even further or is that just a cushion you are building into your forecast for the fourth quarter?

Stacy Smith

I think it's just caution. We're seeing a very cautious environment there. But I think it's a combination of what they are seeing from macro standpoint and a slowing enterprise and operating system transition and weak consumer mature market segment, I think all of that is just leading people to be cautious. Ultimately, I think leaner inventory levels are healthy, but that's what we're seeing right now.

Sumit Dhanda - ISI

My second question was actually a follow-up on the server ASP stuff that was talked about earlier on the call. I guess my question was I think you talked about the fact that you have twice as many SKUs with Romley with a sort of \$1,000 mark from a processor pricing perspective. Has the uptake on the higher SKUs stalled and I guess sort of in line with this question, I was a

little confused by why the Cloud mix would be so much poorer versus the enterprise mix, because I would have assumed that the uptake in Cloud would be a richer mix and that would actually help your ASPs relatively (inaudible)?

Paul Otellini

A lot of the cloud is two way versus enterprise at four way. That will add 50,000 (inaudible) that's the simple answer.

Sumit Dhanda - ISI

Okay. And then the uptake for Romley of sort of above the...

Paul Otellini

Romley has been quite good. All right, thanks everyone for joining us today. Patrick, please go ahead and wrap up the call for us.