Good day, ladies and gentlemen. Welcome to the Quarter 4 2011 Intel Corporation Earnings Conference Call. My name is Misty, and I will be your coordinator for today. [Operator Instructions] As a reminder, this conference is being recorded for replay purposes. I would now like to turn the presentation over to your host for today's call, Mark Henninger, Director of Investor Relations. Please proceed, sir.

Mark Henninger

Thank you, Misty, and welcome, everyone to Intel's Fourth Quarter 2011 Earnings Conference Call. By now, you should have received a copy of our earnings release and the CFO commentary that goes along with that. If you've not received both documents, they are currently available on our investor website, intc.com.

I'm joined today by Paul Otellini, our President and CEO; and Stacy Smith, our Chief Financial Officer. In a moment, we'll hear a brief remarks from both of them followed by Q&A.

By way of announcement, we'll be hosting our annual Investor Day at our headquarters in Santa Clara on Thursday, May 10, and we look forward to seeing many of you there.

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 this call, we use any non-GAAP financial measures or references, we will post the appropriate GAAP financial reconciliations to our website intc.com. So with that, let me hand it over to Paul.

Paul S. Otellini

Thanks, Mark, and good afternoon everyone. 2011 was a year of records, milestones and breakthroughs. I want to begin by highlighting a few of the most significant. We reinvented the transistor with our 3-D Tri-Gate technology. We unveiled a new generation of personal computers, the Ultrabook. We closed 2 large acquisitions: McAfee and Infineon Wireless Solutions. We broke ground on the world's first 14-nanometer fabs, D1X in Oregon and Fab 42 in Arizona. And our 2011 revenue and earnings were the best in Intel's history.

We surpassed $50 billion in revenue for the first time, after crossing $40 billion for the first time just last year. This was our second consecutive year of more than 20% revenue growth. Since 2009, we have added $19 billion to the top line. The investments we've made to innovate and to expand our capabilities are paying off. Let me highlight a few examples.

As the volume of traffic crossing the Internet continues to explode, this has left companies and individuals searching for simple ways to store, manage and access this flood of information. This mega trend led to a fantastic year for our Data Center Group, with revenue up 17% on record microprocessor units, exceeding $10 billion for the first time. But this wasn't just servers. Storage revenue was up 42% to a new record high, and our Embedded Communications Infrastructure business was up 18%, also to a new record high.

Volume shipments of our Sandy Bridge server product, code-named Romley, have begun. We also demonstrated Knights Corner, the first single-chip coprocessor capable of delivering a teraflop of computing power.

Turning now to our PC business. We saw record notebook microprocessor units in 2011, as the PC Client Group grew 17%, fueled by demand in the enterprise and emerging markets, and PC users' appetites for higher performance and more energy-efficient computing. The result was a second consecutive year of rising ASPs, as our mix of core CPUs increased to nearly 70%. Sandy Bridge microprocessors accounted for approximately 40% of the company's total revenue.

Emerging markets now account for 2 out of every 3 incremental units of PC demand, a shift that's rewarding Intel and the PC companies that have a long-standing, deep presence in these markets.

Looking back at the last 12 months of reported data, emerging markets like India and Indonesia grew 22% and 37%, respectively. China, now the largest PC market in the world, represents 20% of all PC demand, and grew a remarkable 15%. Even with that, China has a household penetration rate of just 35%, versus almost 90% in the U.S. China is the world's largest market for mobile phones with more than 950 million subscribers. It's also at the forefront of the smartphone boom and will be the home of the world's first 32-nanometer smartphone.

Last week at CES, Lenovo announced the K800 smartphone based on our Medfield SoC. The K800 will be available on the China Unicom network in Q2, and will showcase Intel architecture in a phone with very competitive battery life and outstanding performance.

2011 was also a year in which we completed several important acquisitions. In the first quarter, we completed the purchase of McAfee and Intel Mobile Communications, formerly the Infineon Wireless division. Together, McAfee and IMC added $3.6 billion in revenue and new strategic capabilities in security and connectivity that will allow us to extend our strategies across the continuum of computing. McAfee has already announced the Deep Safe platform, around which we are building a family of products to take advantage of the combination of McAfee software and Intel silicon to deliver first-of-its-kind protection against day 0 threats.

Lastly, in the fourth quarter, we announced the acquisition of Telmap, whose location-based search and navigation expertise will allow us to add differentiated services to Intel architecture-based devices from Ultrabooks to smartphones. As many of you know, we made several important announcements at CES last week. In addition to the Lenovo K800, we announced the Medfield-based smartphone reference design that boasts a sleek form factor, 8 hours of talk time, 6 hours of 1080p video playback and 14 days of standby power, clearly demonstrating the low-power, high-performance capabilities of Intel architecture. Yet as the performance of this device that really showcases what's possible when you combine advanced process technology and the world's most popular computer architecture. Though Medfield is our very first smartphone SoC, independent testers appointed to benchmarks to place Medfield reference design among the very best in the markets.

It was this differentiated performance and exceptional roadmap and exciting new usage models that led to our multiyear, multi-device strategic relationship with Motorola Mobility. The first of these Intel architecture-based devices will go through carrier certification this summer with commercial availability shortly thereafter. And while the Lenovo and Motorola designs are exciting first steps, we're not done making announcements in the smartphone space.

In the months ahead, we're looking forward to sharing with you a range of exciting new products. Let me highlight just a few. We'll launch Romley for servers in the first quarter. We'll launch Ivy Bridge, our first 22-nanometer product, in early spring. Ivy Bridge will improve on the graphics performance of Sandy Bridge by more than 70%. The industry will bring more than 70 new Ultrabook designs to market this year. And when Windows 8 launches, we'll be ready with both PCs and tablets.

In summary, 2011 was an outstanding year for Intel. As we look to 2012, we're excited about bringing more Intel innovations to the market. With that, let me turn the meeting over to Stacy.

Stacy J. Smith

Thanks, Paul. 2011 was our most profitable year and a year of record revenues. Revenue of $54 billion was up over $10 billion or 24% from a year ago and was our second year in a row with business growing greater than 20%. Our PC Client Group and our Data Center Group both grew at 17% year-on-year. In addition, we closed on the acquisitions of McAfee and the Infineon Wireless division in 2011 which contributed $3.6 billion to our revenue growth.

Gross margin of 62.5% in 2011 was at the high-end of our historical range, as our investments in industry-leading manufacturing process technology continued to enable leadership products, which drove a richer mix across client and server. Spending, as a percent of revenue, was approximately flat at 29.7%. Operating income, net income and earnings per share were all records.

Non-GAAP operating income of $18.4 billion was up 18% year-on-year, and non-GAAP earnings per share was up 25% from a year ago.

For the year, we generated a record $21 billion of cash from operations. We invested over $8 billion in research and development, $10.8 billion in capital assets, primarily building and equipping leading-edge factories; and spent $8.7 billion on acquisitions. Additionally, we paid $4.1 billion in dividends, increasing the annualized dividend per share by 33% and increasing our dividend payout ratio to 40% of free cash flow. Lastly, we used our stock repurchase program to return over $14 billion of cash to shareholders in 2011, reducing diluted shares outstanding from a year ago by roughly 450 million shares.

Total cash investments ended the year at $14.8 billion, down approximately $6.7 billion from a year ago. Fourth quarter revenue finished at $13.9 billion, up $2.4 billion and 21% from the fourth quarter of 2010.

As we announced in December, revenue in the fourth quarter was negatively impacted by the floods in Thailand and the resulting hard disk drive supply shortage. As a result of the hard disk drive shortage, we saw a reduction of orders for microprocessors as customers reduced inventories across the supply chain. Despite this reduction in inventory levels, it is our belief that the shortage did not impact the actual sales of personal computers in the fourth quarter, with demand trends playing out as expected.

Gross margin improved to 64.5% from the third quarter, with lower factory start-up costs as we qualified for sale our first product on 22-nanometer process technology and lower unit costs. Non-GAAP operating income of $4.8 billion was up 20% from a year ago and non-GAAP earnings per share of $0.68 was up 21% from a year ago.

As we look forward to the first quarter of 2012, we are forecasting the midpoint of the revenue range at $12.8 billion, down 8% from the fourth quarter. This decline is slightly more than the average seasonal decline as we expect the shortage of hard disk drives to continue to impact our business in the first quarter. We are forecasting the midpoint of the gross margin range for the first quarter to be down 1.5 points to 63%, but manufacturing costs going up as we begin to sell our first 22-nanometer product, Ivy Bridge, and ship lower volumes, when compared to the fourth quarter.

Turning to 2012. We are planning on another strong year, with revenue growth in the high single-digits and gross margin at the high end of our historical range, at 64%. Importantly, we will continue to invest in our business in 2012. We are forecasting an increase in capital spending to $12.5 billion as we build the world's first high-volume manufacturing factories for 14-nanometer process technology. We are also forecasting an increase in investment in research and development of $1.8 billion. We are making critical investments in R&D for Ultrabooks, data centers, phones and tablets. In addition, we are making R&D investments in core capabilities like security, SoCs and extending our process technology leadership.

The trends that we discussed in May drove our performance in 2011, and we expect will drive our financial performance in 2012. We expect continued strength in emerging markets as rising incomes increase the affordability of personal computers. We will continue to benefit from the explosion of devices that compute and connect to the Internet as they've drive the build-out of the cloud infrastructure and as we expect to generate more sales in storage, communications and networking products for this segment.

Our process technology and manufacturing advantage will continue to extend in 2012, enabling a leadership product portfolio, not just in PCs and servers, but also in low-power products for phones, tablets and embedded systems. With that, let me turn it back over to Mark.

Mark Henninger

All right. Thank you, Stacy and Paul. We'll now move to Q&A. [Operator Instructions] Misty, please go ahead and introduce our first questioner.

Question-and-Answer Session

Operator

Your first question comes from the line of Glen Yeung with Citi.

Glen Yeung - Citigroup Inc, Research Division

I guess, the first one is, Stacy, in your forecast for gross margins, I think you have 50 basis points in there for higher revenues. And I hear your point about higher -- high single-digit revenue growth for the year. What's your PC forecast assumption that underlies that?

Stacy J. Smith

You're talking for the year, Glen? Or are you talking...

Glen Yeung - Citigroup Inc, Research Division

Yes, for 2012.

Stacy J. Smith

For 2012. It will play out, we believe, pretty similar to this year. There'll be some unit growth, but I believe we'll also benefit from the fact that we have a very strong product portfolio and we'll benefit from a rich mix. You've seen that over the last couple of years. And if I can just take a second here, just to put the high single-digit revenue growth in perspective. If you go back to 2011 and you strip out the acquisitions and the fact that we had a 53rd week, you're left with an underlying growth rate for what I'll call the existing core business, of about 15%. You compare that to the high single-digit forecast for 2012, you see. We do expect it to come down some, that's because we expect GDP growth rates to come down a little bit and we do correlate to GDP growth rates. But still, the same kind of drivers in '12 that we saw in '11.

Glen Yeung - Citigroup Inc, Research Division

Okay. The other question I have is on unit costs. And again, in your written comments, it suggests that they'll be up for the quarter end for the year. And I wonder if you could just walk us through the puts and takes on unit costs in particular. And I guess, I'm kind of wondering if more Ivy Bridge ultimately results in reduced unit costs at some point.

Stacy J. Smith

Yes. The unit cost increase that we're seeing in Q1 and over the course of '12 is a normal phenomenon, as we're ramping new factories and new process technologies. If you go back 2 years, and you have to offset it for a different quarter, but if you go back and you look at the first 32-nanometer products, what you see is, as we're just starting to ramp those big factories, the first products are coming out, those tend to be pretty expensive products, and then the cost kind of comes down over the course of the year. It's a consistent phenomenon that we've seen before.

Operator

Your next question comes from the line of Mark Lipacis with Jefferies.

Mark Lipacis - Jefferies & Company, Inc., Research Division

In thinking about, as you guys get more success in the smartphone and tablet markets, comparing the strategy there to your PC market -- PC microprocessor market, in PCs, you're up and down the stack, you're everywhere. And I'm wondering if that's your intention in the handset and tablet market? And whether or not that necessarily means that there's a different business model for that business versus your core business.

Paul S. Otellini

Let me take that one, Mark. Our intention is to participate broadly in all 3 of those markets. In tablets, I think we'll be able to do that from day one, as you see the Android tablets coming out and Windows 8 tablets coming out. And you'll see us well-positioned in multiple price point on those. And who knows where those prices go over time, but our intention would be to use the advanced silicon integration capability we have to be able to drive the build material cost down, integration up in tablet space, which I think is going to be a sweet spot for Intel. On phones, our strategy is a little bit different. We're coming in at the top of the smartphone market. Our value proposition initially is aimed at best performance and very competitive feature sets and very good battery life. Over -- and then let me say on the other end of the market, the Infineon acquisition has given us a very strong position in basic phones and feature phones. They shipped 400 million modems this year into the cell phone business. So over time, what we'll want to do is grow that capability up by integrating the apps processor and the comm processors onto the same chip, while we drive our initial positions in apps processors from the top down.

Mark Lipacis - Jefferies & Company, Inc., Research Division

And does that mean that -- are those businesses -- are they -- do they inherently carry a different profitability than your core PC microprocessor business? Or is that too early to say?

Paul S. Otellini

Well, the pattern today of the vendors in that space is that the margin is -- their margins are lower than ours. Now if you remember, their margins only reflect half of the equation. Most of -- virtually all of them use a foundry. So as we enter this business, we intend to get paid twice. We get paid a foundry margin while optimizing our product on our silicon, and then the architectural margin.

Stacy J. Smith

If I can just add to that, Mark. As I look out over the next few years, we'll have success in these devices. I think they'll start to grow earnings for us out in time. It doesn't change my intermediate view of long-term gross margins. And if we end up in a situation where we're seeing a lot more success in those businesses and we're growing earnings but it causes gross margins to come down a little bit, that's a trade-off that we'll gladly make at that time.

Mark Lipacis - Jefferies & Company, Inc., Research Division

Fair enough, and if I could ask a follow-up on the...

Mark Henninger

Mark, I want to try and make sure we get as many callers as we can, so we'll move on.

Operator

Your next question comes from the line of Vivek Arya with Bank of America Merrill Lynch.

Vivek Arya - BofA Merrill Lynch, Research Division

My first question is on Ultrabooks. So a number of announcements at CES. Conceptually, do you expect this to expand the category? Or do you think it's just going to cannibalize notebook sales that you might have had anyway? How has the feedback been from your early customers?

Paul S. Otellini

Well, let me just say, I'm not seeing this level of excitement in our customer base since, even before Centrino, which is 2003. People are very excited about the feature set and having the PC reenergized. I think initially, what you're going to see is that this will be replacement of existing notebook sales and customers and so forth. People will trade up for it. It's a very exciting new product. As we go through the course of 2012, particularly as -- and into '13, as Windows 8 machines rollout, you have the possibility, and then as I look at our design wins, the probability of many of those machines incorporating touch. At that point, it's hard to tell what the market impact is going to be because the PC now has the characteristics of the best of all tablets and very high performance-capable machine -- notebooks. So I don't know that we know how that plays out. No one knows how that plays out. What I know is that we'll be well positioned for it in any direction.

Vivek Arya - BofA Merrill Lynch, Research Division

Got it. And one on -- follow-up on CapEx this time. So you obviously decided to raise the CapEx for this year. And -- Intel has always had a very strong lead versus competitors, 1 or 2-year lead. So I'm curious, what are the criteria that you use to decide to accelerate CapEx? Like what is the incremental benefit that this provides you? And I know that in the past year you said that you expect to get paid for it, but over what time frame? And I'm just curious as to how you make those decisions.

Stacy J. Smith

Yes, it's a good question. So I just want to come back and clarify something. The CapEx that we're spending doesn't increase our cadence of Moore's Law. We're still on a 2-year cadence, and as we have shown you in investor meetings, we would go faster if we could but we don't think the industry can keep up with us. Your point, though, is still valid and that based on everything we see from other people that are building factories, they're struggling to solve some of the same problems that the cadence that we solved. So I think our process technology lead is extending. The way we get paid for that is simple. We can put more features, more performance and bring power envelopes down faster than the competition can. I think if you look historically, we've gotten paid for that by driving cost down at a curve, and we're going to still use cost as one of the ways that we get paid here. But increasingly, if you look at the last 2-plus years, we've also gotten paid by bringing out these really capable products and driving a richer mix. And that's really been the story over the last couple of years, is by integrating the graphics transistors to end -- to our leading-edge process technology, we're creating much more capable products, we're putting other features on those products, things like WiDi and things that differentiate us from the market, and we get paid in a richer mix. And so that's where our strategy going forward is we'll have cost-reduced products, and we'll have then also a portfolio of really capable products where we drive a sell up.

Operator

Your next question comes from the line of Alex Gauna with JMP Securities.

Alex Gauna - JMP Securities LLC, Research Division

Paul, I know you don't guide by segment, but can you talk about what's in the down March quarter? What's happening on the Data Center side of things? And what's your sense on how market demand is holding up ahead of the Romley refresh? When do we really see those numbers coming through and how strong will they be?

Stacy J. Smith

Yes, let me do kind of a higher level of what we're seeing by segment and then Paul will pick up and talk about Romley in particular and where it’s heading. If you step back and look at the Data Center Group in 2011, it grew revenue 17%. And if you think back to the investor meeting, we told you our plan was to grow 15% at the top line and consistent on the bottom line. We did that in '11. Based on everything we see for '12, we have high confidence that we can continue to grow at that kind of a rate. We're not going to get into a quarter-by-quarter because remember, the service business can be pretty -- the Data Center business can be pretty lumpy if there's one big customer that's buying and a big buying pattern, you'll see a pop-up and it can come down the next quarter. But on the secular basis, we're pretty confident in the growth trends.

Paul S. Otellini

And let me address the Romley one, in particular, Alex. We're seeing right now, stronger demand for Romley than we did from the Nehalem at the same point of its life sort of 2 years ago. The product is in high-volume production now getting ready for our customers assistance launches later this quarter and into early Q2. It provides an outstanding value proposition and a good ROI for CIOs to evaluate. I think, though, that this is not -- initially it will not drive that kind of replacement cycle that we saw for Nehalem because it's still relatively new machines. On the other hand, I think people will embrace this machine for high-capacity needs. We talked earlier about the build-out of Internet data centers, about storage and other segments in this type of Data Center and I think this product is probably the most well-rounded product we've produced in this genre so far.

Alex Gauna - JMP Securities LLC, Research Division

And then as a follow-up, if could ask. If we think about...

Stacy J. Smith

Actually, Alex, I'm going to -- Alex, we want to make sure we get on to the next caller. Thank you.

Operator

Your next question comes from the line of Ross Seymore with Deutsche Bank.

Ross Seymore - Deutsche Bank AG, Research Division

Paul, congrats on a very strong year. Overall, as we look at the flood impact that you mentioned in your guidance, how should we think about that snapping back and maybe just within your guidance of being up 8% for the entire year of high single-digits, how should we think about seasonality considering the floods snapback, multiple discrete items like Ivy Bridge coming out, Romley, Windows 8, Ultrabook, et cetera?

Paul S. Otellini

You're absolutely right. There's probably more moving pieces as I look out over the next 11.5 months than I can recall for a long time, Ross. So let me start with the flood first. Our view and the view from our customers, and I talked to everybody at CES, from OEMs to OEMs, it's very consistent, is that the industry seems to be hitting the bottom of their output trough in the January, February time frame and then it starts recovering from there. Everything we've seen so far suggests that anyone on Earth who wanted to buy a PC has been able to buy a PC. There's not -- there may be some spot stockouts of a particular SKU at a particular store, but all of our channels are still showing pretty good sales outgrowth and that seems a strong indicator as we go through this underlying demand. I think that you will see -- we have seen a compression of the supply chain that hit us very dramatically in the fourth quarter and was the result of the driver for our pre-announcement. And it's also the driver, as Stacy said, for our being under seasonality in Q1. We think that there's likely to be some refilling of those pipes in the second quarter, early third quarter, as the supply lines come back in normalcy. On the other hand, it's very possible that people just learned to live with leaner inventories, which is always very good for us. As a result, we see a more nonlinear, more second half loaded year this year than we've seen for quite some time, in terms of CPU shipments, not necessarily for a PC shipments.

Ross Seymore - Deutsche Bank AG, Research Division

Great, and I guess as the one follow-up switching to Stacy on the gross margin line, ASP has been a lot of a tailwind for your goodness in the gross margin line over the last 2 years. What's the expectation for ASPs in 2012? And do they need to rise again for your gross margin guidance

of 64% to be attained?

Stacy J. Smith

I'm predicting growth of ASPs to be what I'll call pretty benign in 2012. We have a strong product line. We've generated a strong mix. I think maintaining that is probably a pretty likely case. And then what we're watching is with Ultrabooks, as they ramp into the -- a much higher percentage of the consumer market in the back half of the year, that could give us a little bit of an oomph, but I'm not counting on that -- my gross margin forecast, but it certainly one of the things we'd like to see happen. You also have to keep in mind that one of the less bright spots for us in 2011 was that netbooks were way down. And so I'm going to see kind of a natural mixing up as I go from '10 to '11 and '11 to '12 with less netbooks and a large percentage of the total being Core.

Operator

Your next question comes from the line of Jim Covello with Goldman Sachs.

James Covello - Goldman Sachs Group Inc., Research Division

I guess my main question is: What is the incremental growth in capacity as a result of last year's CapEx and this year's CapEx? And how does that capacity kind of layer on over the course of the year? And then the follow-up part and parcel of that, so that we can just kill everything at once, is what is the assumption around factory loadings as that capacity growth ramps over the course of the year?

Stacy J. Smith

I'll be -- I have to be a little long-winded I think, to get to both of those. So first, let's talk about what's driving the capital spending. And I'll be the first to admit when I see numbers like the $10.8 billion in 2011 and $12.5 billion for 2012, those are big numbers. I have to step back and look at it against the context of how much our business has grown. We were up 25% from '09 to '10, we're up 24% from '10 to '11, so it's more than 50% growth in 2 years. Put another way, it's almost $20 billion of incremental revenue over the course of that time period. When you look at that in that context, it makes sense. And just to give you one other data point that at least helps me be comfortable here, I think my depreciation as a percent of revenue in 2012 stays in a healthy range. So I think that gives me some comfort. In terms of the makeup of the specific capital in '12, it's more heavily weighted than what we've historically seen to building buildings. And Andy told you in the investor meeting that we've kind a -- it's a 2-year cycle and we're building buildings. So we're seeing that it's more than 1/3 of the total capital in '12. I think that piece starts to come down in '13. And remember, that piece has a much longer useful life which means we depreciated over a much longer period of time. The equipment piece actually comes down from '11 to '12, and that's a little more -- it's heavily weighted towards 14-nanometer equipment that we're putting in place. So that's kind of the makeup of the capital. In terms of utilizations, we're running full out today. We're just at the beginning edge of 22-nanometer. Every unit that we can get out there, we can sell. So we're running the new stuff full out. We did take a little bit of advantage in Q4 based on the hard disk drive shortage. We took some older generation capacity off-line to avoid putting some older generation product in inventory and we utilize that equipment, as you've seen us do before, to offset -- to go a little faster on 22-nanometer. So those are responsive things that we do. But I think we're running full out today, and I think will be nicely loaded over the course of 2012.

Operator

Your next question comes from the line of Uche Orji with UBS.

Uche X. Orji - UBS Investment Bank, Research Division

Stacy, can I just start off by asking you about gross margins? Your full year gross margin guidance is about 1 point higher than Q1. Is there any way for us to think about it typically not in Q4? How that should play out through the year?

Stacy J. Smith

It's a hard year to talk about normal seasonality. But you should, based on what Paul told you in terms of how we're viewing the impact of the hard disk drive shortage, it says we have a back-end-loaded year from a unit standpoint that will clearly give us a little bit of a tailwind. You also have to remember that those first wafers that come off the line for 22-nanometer, these are big factories, the very first products are coming off the line now. Those tend to be pretty expensive and that cost comes down over the course of the year as well. So those are things that give you a tailwind into the back half of the year -- give me tailwind over the back half of the year.

Uche X. Orji - UBS Investment Bank, Research Division

All right. Can I just go back to the question of channel inventory? I mean, you described it as historically lean. And Paul, you said people might just be willing to leave with -- they may choose to leave with these levels of inventory. But let's assume that we get to the hard disk drive issue and inventory were to go back to normal levels. Where are we now? Can you quantify where these historically low levels are? And if we went back to normal, how much more weeks of inventory do you think your distributors need to carry to sustain what should be a fairly robust second half of the year?

Paul S. Otellini

I think we're talking about less -- I mean, remember, we ship kind of a 1 million unit today as an industry. So we're talking about something – a correction, that's in the order of a week, Uche. It's not like this is a months' worth of inventory. And really, as much as that can get compensated for, in either direction, by the decisions of OEMs to put things on boats versus airplanes. And so I think while there's still a shortage of drives, you're going to see more use of planes, shipping things from Asia to the end markets. And depending on how things, how fast things recover, you may see people go back to boats, which puts a bit more buffer into the system. It's on the order of a week, not in the order of a month.

Stacy J. Smith

Yes, and it probably comes down a little bit more -- and it doesn't probably. It almost certainly comes down more in Q1 and our view is in that that's the level of inventory that they can live with. They just -- they may not go all the way back up to the previews inventory levels. We see that as these things play out. And as Paul said, over time, leaner inventory levels in the supply chain and then the kind of things we can do to be just in time, they actually make the supply chains much more efficient. They benefit our business over time.

Operator

Your next question comes from the line of John Pitzer with Crédit Suisse.

John Pitzer - Crédit Suisse AG, Research Division

I guess, Paul, my first question on Ultrabooks. Are there any sort of milestones that you can share with us as far as percent of notebooks exiting the year that you would expect to be on Ultrabook? And I guess, as you think about kind of ASP versus unit growth this year for you guys in PCG, how important is getting Ultrabook up in the curve as a percentage of notebooks to kind of the mix story this year?

Paul S. Otellini

Well, let me start with the mix and work backwards, John. I said that core is approximately 70% of our mix already and I don't know that that's going to go 90%, and there's no way it's going likely down to 50%. So I think we're sort of in -- it's historically high for our premium brand, but I think we're in the sweet spot for what we're going to see, certainly the bulk of 2012 because the Ultrabooks are going to be Core-centric. And what we can't yet predict is the mix between i3, i5 and i7. Right now, the stuff that's sold in Christmas and into January were a very good mix of i5s and i7s, but the price points were $8.99, $9.99. As we move towards the second half of the year, and price points come down maybe as low as $6.99, the mix may come down a bit to i3s. But I still think you're going to see people position this as a premium product. Their industry is enjoying a little sell-up around it. In terms of a target, what we said before is that our goal this year will be to exit the year at about 40% of consumer notebooks being Ultrabook.

John Pitzer - Crédit Suisse AG, Research Division

And then guys, as my follow-up, Stacy, just a follow-up to Uche's question on gross margins, the 63% for Q1 versus the 64% for the full year on a high 9 -- high single-digit revenue growth, I would have thought you would have seen more margin expansion. Is this conservatism? Or is this kind of the penalty you're paying as depreciation grows relative to the CapEx spending?

Stacy J. Smith

I don't think it's either. I don't think I'm being overly conservative, although I certainly hope so. And it's not a higher depreciation cost. Again, my depreciation as a percent of revenue, looks like it stays in a nice, healthy range. It's the unit cost penalty associated with the ramping 4 big 22-nanometer factories. Again, those are big factories and the first wafers off the line are pretty expensive. And so that will cause a little bit of an offset to the good news that I expect that we're going to see based on start-up costs and the higher platform revenue.

Operator

Your next question comes from the line of Chris Danely with JPMorgan.

Christopher B. Danely - JP Morgan Chase & Co, Research Division

Just one more question on revenues. So if I try and get to the high single-digit revenue growth that you guys have guided for this year, even assuming some of that inventory correction comes back into sales, it's still, I think, like several billion dollar jump above normal seasonality in the second half. So I mean do you -- how do we get there? Do you guys expect tablets and phones? Do you expect further price increases? Can you just maybe take us through that?

Stacy J. Smith

Yes, I know. So I think if you're pointing to that we have a nonseasonal unit forecasting, the answer is yes, for the reasons Paul said. And again, based on what we've seen so far, sales of PCs look to be pretty seasonal. We think what's going to happen is the industry is going have to go through some kind of extraordinary measures to make sure PCs are getting to the right place to be sold, with very low inventory levels out there, and that pipeline starts to refill in Q2 and causes us to have more of our units in the back half. This isn't predicated on us magically winning half of the phone market. We're super excited to get those first products in the market, as Paul said, they have critical acclaim, but they don't move the needle from the standpoint of revenue or profit this the year. This is a year where we're going to get on there and fight and win designs.

Christopher B. Danely - JP Morgan Chase & Co, Research Division

Great. And for my follow-up, just on spending, both R&D and CapEx, it is going up more than sales growth this year. Do you think that formalizes in 2013, i.e., it comes back in line? Or is this something that we should maybe get used to?

Stacy J. Smith

You're going to ask if Paul and I are going to spend like drunken sailors or not? We're above model in 2012. We'll come back down towards model over time...

Christopher B. Danely - JP Morgan Chase & Co, Research Division

On spending?

Christopher B. Danely - JP Morgan Chase & Co, Research Division

On spending, yes. So spending as a percent of revenue will come up in 2012 and we expect it'll come down over time. If you deconstruct what we're doing in 2012, my opinion is we're making some significant but prudent incremental investments in some critical areas. We made a lot of progress in terms of where we are with Ultrabooks, where we are with phones and tablets. We're going to make some investments there. In addition, we're making some investments in our Server business. You've seen us moving our product line from just focusing on servers to broader products in the Data Center that are focused on storage and communications and networking. You're going to see us continue to do that. And then underlying that, there's some core capabilities for the company around SoC integration, communications technology, security, process technology. We're going to make some investments there. So I think we'll come down from here. But this is an investment here for us in some areas where I think we got long-term shareholder return.

Operator

Your next question comes from the line of Romit Shah with Nomura.

Romit J. Shah - Nomura Securities Co. Ltd., Research Division

Stacy, the platform costs seem like they're increasing less than I would have expected for this year. Can you talk a little bit about 22-nanometer yields? And do you think it will be similar to 32?

Stacy J. Smith

No, I'm not going to get into that level of detail. What we're seeing from a cost standpoint, as I said before, is pretty normal, as we're seeing the first wafers coming off. We have a very fast ramp of Ivy Bridge, strong demand, so that should give you some comfort. And we'll talk more about some of the longer-term trends when we get to the investor meeting.

Romit J. Shah - Nomura Securities Co. Ltd., Research Division

Okay. And as follow up, Paul, Android tablets sales seems like they are a disappointment last year, relative to what some were thinking at the beginning of 2011. And I'm just curious what you think the issue was last year and if there's reasons to be more optimistic about tablet sell-through this year?

Paul S. Otellini

Well, actually, they were about where I thought they would be, but I was well below what many of you had. I think the thing is, tablets are a little bit about hardware and an awful lot about software. And I think that until you get to Ice Cream Sandwich, the offering isn't as powerful as what's out there with Apple. And as the Ice Cream Sandwich tablets start shipping, I think you'll start seeing a little bit better receptivity, Google just added the music store, the videos are better, everything got a little bit better bit ICS. And so I think the better test is year 2 here, in terms of is there anyone that can compete with the iPad? And then the other part of that test, of course, is the Windows 8 tablets that are being queued up for production. So I don't know that the whole tablet thing is settled down by any stretch, and I do have a lot of interest in, if you heard me at CES about these hybrid and convertible designs as they apply to clamshells, where there's a significant blurring between what people do with tablets and what people do with PCs. So the jury is out on I think the long-term segmentation by form factor. But I do think you'll see more progress on the Android side as a result of ICS.

Operator

Your next question comes from the line of CJ Muse with Barclays Capital.

Christopher J. Muse - Barclays Capital, Research Division

If I look at the incremental revenues you've guided to at high single-digits in your commentary about servers, I guess, made double-digit in PCs, I guess, low single-digit unit growth. It would suggest roughly $1 billion, $1.5 billion of incremental revenues from non-BCG, non-PCG. So curious if you could walk through what that the key contributors will be to that kind of growth.

Stacy J. Smith

No, CJ. We've given a lot in terms of annual revenue guidance and a lot in terms of what we expect from the standpoint of the different businesses. I'm not going to get more granular than that.

Christopher J. Muse - Barclays Capital, Research Division

All right. I guess, in terms of Server business, if you could walk through, I guess, linearity there. Are you seeing softness in Q1, given the Romley launch? And if so, how should we think about that through the year? Should that track similar to PCs in terms of back half loaded? Or should that see a nice bump up in Q2?

Stacy J. Smith

Again, I'm not going to get to that level of granularity on a prospective basis. We didn't see softness in the Server business in Q4. It may have jumped out at you that the year-over-year comp was down a little bit, it was 8% versus higher comps but if you go back to Q4 of last year, we had a Q4 of '10, we had an extraordinary strong quarter there. If I recall right, it was almost 30% growth from Q3 to Q4 of '10. So we're still seeing a nice, secular growth trend in servers and that's what we saw in Q4 and that's what we expect...

Paul S. Otellini

I would just add, CJ, that the Data Center business we have today is not your grandmother Server business that we had for many years, right? There's other elements in there around storage and networking equipment. And the other big element of that is the sales to the large Internet data centers that are being built up around the world. I think Stacy talked about that last quarter. Those sales were lumpy. They tend to be a function of when Facebook or Google or Amazon decides to turn on a new Data Center and they buy x 100,000 units. Or there's a new generation and they want to have a quick complete swap out. And as a result, we're seeing a change to the historical linearity that we saw in this -- in the enterprise Data Center business for many years. So I think you should probably get used to a little bit more lumpiness here and look at the overall year-on-year growth, which is what we've been trying to discuss at the last couple of analyst meetings.

Operator

Your next question comes from the line of Srini Pajjuri with CLSA Securities.

Srini Pajjuri - Credit Agricole Securities (USA) Inc., Research Division

Paul, couple of questions on the mobile side. You said as you enter the smartphone market more broadly, as you moved on to mid-end and low-end smartphones, you mentioned that it makes sense to integrate Medfield with the baseband that you had with Infineon. I'm just wondering what should we be thinking in terms of the timeframe for that solution. And also, as a follow-up, I'm just curious, given that all the smartphones also have Wi-Fi, Bluetooth and GPS and then [ph]. Do you have that capability today internally? If not, what's your strategy for those components?

Paul S. Otellini

Yes, we've got the multi-comm capability in-house. A lot of that came with the acquisition from the Infineon group. And that's got 2G, 3G, they have an LTE solution underway. We've had Wi-Fi forever, and we've had Bluetooth for many years. So all of those are being integrated into our comms capabilities. In fact, we've integrated those business units now into a single unit to be able to accelerate that. I did not say, I want to be very clear, I did not say that our intent would be to integrate Medfield to baseband. I said over time, you'll see us move from the low-end baseband-only business in the feature phones and value phones to having it a more integrated capability. I didn't say when and what generation. I'm really not at liberty to discuss that. But the major thrust over the next year or 2 is going to be to have very high-performance modems as a comps processor and the best-of-class apps processors for smartphones.

Operator

Your final question comes from the line of Craig Ellis with Caris & Company.

Craig A. Ellis - Caris & Company, Inc., Research Division

Stacy, if you have the high-class problem, better units this year than PC Client in last year. What are the implications for CapEx?

Stacy J. Smith

So I hinted at it I think in the previous answer. If you look at the spending of CapEx for 2012, and this is consistent with what we said last year. It's a big component of it, but historically large component of it, is actually building the facilities, these 4 factory model that we've been talking about. We've got big construction projects underway. They start to taper off. From here, our CapEx, really, will be a function of 2 things: it's the unit growth that we see going forward, and it's the speed at which we bring capabilities to that leading-edge process technology. And I think graphics has been the classic example of that. As we move that to the process edged to the leading-edge process technology, it did drive an increase in CapEx but it also drove a really capable product line that we got paid for. So we balance off those decisions as we go forward. A big increase in units would say that we'll continue to spend CapEx to support those units. If it's less than that, then CapEx is less. It becomes a pretty -- a more traditional relationship going forward.

Craig A. Ellis - Caris & Company, Inc., Research Division

Okay. That's helpful. And then secondly, as we look at the balance sheet and the capital structure, you've taken on some debt in the fourth quarter. Can you frame for us, is that about the right level, a comfortable level for you? Are you capable of taking on more debt? Did you look for potentially flexibility to buy back more stock, et cetera, in 2012?

Stacy J. Smith

Well, let me separate out those quarters. At the end of this, I'm not going to make a prospective statement on buybacks or debt. But our balance sheet certainly supports us taking on more debt. We have a relatively low amount of debt for a company of our size. So if we had a strategic need or decided that we wanted to take on more debt to buy back stock and recapitalize the company, we certainly have the capability of doing so. I'll come back to our capital structure philosophy. We've said in the past that our first priority is investing in our business. I think if you look at 2011, it's a perfect example of that, we've made some significant investments in research and development in CapEx. We bought it, we bought back and we bought the Infineon Wireless division that we believe bring really important capabilities, as well as nice business models into the company. Second priority is the dividend. We had a pretty significant increase in the dividend in 2011, and we've increased the amount of dividend as a percent of free cash flow in terms of our target. And we're kind of right in there now. And then third is buying back stock and you saw us do a pretty significant amount of stock buyback. We did take advantage in 2011 of fairly low interest rates and high dividend yields to accelerate that some, and it probably didn't escape you noticed that we bought back $4.1 billion in the fourth quarter, which I think is probably our largest quarter of buybacks ever. So all that's true. I'm not going to talk prospectively, though, about more debt or the size of the buyback. That's not how we do it.

Paul S. Otellini

Thank you, Misty, for hosting us. And thank you, all, for joining the call today. Have a good night.