

These prepared remarks should be viewed solely in conjunction with the related quarter's conference call webcast and press release, which can be found [here](#). The webcast includes the prepared remarks as well as a question and answer session.

Please [click here](#) for complete GAAP reconciliation information between our GAAP financial results and our non-GAAP financial results.

Cisco Systems, Incorporated [CSCO]

Q4FY24 Earnings Results Conference Call

Wednesday, August 14, 2024

Introduction

This is Sami Badri, Cisco's Head, Investor Relations, and I'm joined by Chuck Robbins, Chair and CEO, and Scott Herren, our CFO. By now, you should have seen our earnings press release. A corresponding webcast with slides including supplemental information will be available on our website in the Investor Relations section following the call. Income statements, full GAAP to non-GAAP reconciliation information, balance sheets, cash flow statements, and other financial information can also be found in the Financial Information section of our Investor Relations website.

Throughout this conference call, we will be referencing both GAAP and non-GAAP financial results and will discuss product results in terms of revenue and geographic and customer results in terms of product orders, unless stated otherwise. All comparisons made throughout this call will be on a year-over-year basis.

The matters we will be discussing today include forward-looking statements, including the guidance we'll be providing for the first quarter and full year fiscal 2025. They are subject to the risks and uncertainties that we discuss in detail in our documents filed with the SEC, specifically with the most recent report on Forms 10-K and 10-Q, which identify important risk factors that could cause actual results to differ materially from those contained in the forward-looking statements.

With respect to guidance, please also see the slides and press release that accompany this call for further details. Cisco will not comment on its financial guidance during the quarter unless it is done through an explicit public disclosure.

I will now turn it over to Chuck.

Opening Remarks

Thanks, Sami, and thank you, all, for joining us today. We had a strong close to fiscal 2024, delivering \$13.6 billion in revenue for the fourth quarter, coming in above the high end of our guidance range, and \$53.8 billion in revenue for the year, coupled with growth in annualized recurring revenue, remaining performance obligations, and subscription revenue. We also generated excellent margins boosted by Splunk. Our gross margin of 67.5% was the highest for Cisco in 20 years.

We saw steady demand as we closed the year, with total product order growth of 14% and growth of 6% excluding Splunk, indicating that the period of inventory digestion by our customers is now

largely behind us, as we expected. We've also been investing to accelerate critical innovation in key areas, with Hypershield and HyperFabric for AI being two outstanding examples.

With Splunk now part of Cisco, we believe we have an unmatched capability to unlock the full power of the network with market-leading security and observability solutions to deliver even greater value for our customers. We have hit the ground running since we brought the Splunk and Cisco teams together, integrating powerful new customer solutions and beginning to realize early synergies.

We know that our biggest competitive differentiator is the power of our full portfolio. This is why earlier today, we announced that we will be bringing our Networking, Security, and Collaboration teams together as one organization with Jeetu Patel stepping into an expanded role as Chief Product Officer to lead this group effective immediately.

As we complete the full integration of Splunk into Cisco, the Splunk product line will also integrate into this new organization at the right time, bringing our entire product portfolio together as one team. With this new organization, our products will come together in a more integrated way than ever before, positioning us to deliver incredibly powerful outcomes for our customers.

Looking ahead, we remain laser-focused on growth and consistent execution as we invest to win in AI, cloud, and cybersecurity. To focus on these key priority areas, today we announced a restructuring plan to allow us to both invest in key growth opportunities, as well as drive more efficiency in our business.

Now let me share some details on our fourth quarter. We delivered solid performance in Q4, with revenue coming above the high end of our guidance range. Strong operating leverage across our business once again drove non-GAAP margins above the high end of our expectations, resulting in earnings per share also coming in above the high end of our guidance range. We continue to focus on growth in our recurring revenue streams. Annualized recurring revenue, remaining performance obligations, and subscription revenue all showed solid growth, and subscriptions made up 56% of our revenue in the quarter.

We also continued to deliver on our commitment to consistent capital returns. In Q4, we returned \$3.6 billion in value to our shareholders through share repurchases and cash dividends, bringing the total to \$12.1 billion in value returned in fiscal 2024 or 119% of free cash flow.

In terms of customer demand, as I mentioned earlier, we saw steady demand in Q4. This resulted in double digit product order growth across all geographies and strength in all customer markets despite persistent macro uncertainty. Public sector demand was particularly strong worldwide driven by Federal spending in the US and strength in APJC.

Enterprise demand returned to strength in the quarter with solid performance in the Americas and EMEA and even stronger results in APJC. We signed several \$100 million-plus transactions in the quarter with global enterprises who are leveraging the breadth of our technology platforms to modernize and automate their network operations and deploy next generation machine learning and AI applications.

I'd like to highlight one of the largest deals we signed in the quarter with a leading global logistics company to advance their efforts in creating the world's most flexible, efficient, and intelligent logistics network. Cisco's technology platforms across switching, routing, security, and observability will enable our customer to automate network operations with cutting-edge innovations like AI-powered robotics and unmatched supply chain visibility.

We also signed our first cross-portfolio agreement that includes Splunk with a major automotive company in this quarter. AI is transforming every aspect of our customers' IT environments. They need to modernize their infrastructure, harness the full power of AI and data, and improve their cybersecurity posture, all while building agility and resiliency across their entire digital footprint. Our customers continue to put their trust in Cisco, and we are very well-positioned to be their strategic partner for this era.

In Service Provider, while our telco and cable customer demand remained muted overall amid continued industry-wide pressure, we saw strength in EMEA, driven by investment in AI operations and autonomous networks by service providers to help them monetize their B2B offerings. We're also encouraged to see signs of stabilization and improved performance in webscale in terms of pipeline and demand, with double digit order growth.

To provide some incremental color, let me share some data on demand through the lens of our products. Excluding Splunk, Security product orders grew double digits. Collaboration product orders grew double digits. In our Networking portfolio, data center switching also saw double digit product order growth. In Enterprise routing, campus switching, and wireless orders were also strong, with wireless orders greater than \$1 million up more than 20% year-over-year, as customers look to enhance their office environments.

Across the breadth of our portfolio and global customer base, our product order results demonstrate strengthening demand as our customers focus on their next top priority, technology investments. While customers continue to ruthlessly prioritize their investments, our product order results demonstrate that our customers continue to look to Cisco as they focus on their most important technology initiatives.

Now turning to look at our product categories in more detail, we saw revenue growth in Security and double digit growth in Observability year-over-year excluding Splunk, as customers looked to enhance their digital resilience with Cisco's technologies. We've had extremely positive feedback from customers with early access to Hypershield, the first truly distributed AI-native cybersecurity solution built into the fabric of the network.

Hypershield furthers our vision for the Cisco Security Cloud which is expected to deliver the industry's most comprehensive, unified platform with end-to-end solutions making it easier for our customers to protect against evolving threats, and we look forward to making it available this fall.

Our new Security solutions, XDR and Secure Access, are continuing to gain strong traction. We added over 230 new XDR customers in Q4. Early in the quarter, we announced the integration of Cisco XDR with Splunk Enterprise Security, and at the Black Hat Security Conference earlier this month, we announced the availability of Talos Incident Response for Splunk customers, enabling

access to the full suite of proactive and emergency services to help prepare for, respond to, and recover from a breach.

We also continue to capitalize on the multibillion-dollar AI infrastructure opportunity. We have now crossed \$1 billion in AI orders with webscale customers to date, with three of the top four hyperscalers deploying our Ethernet AI fabric, leveraging Cisco-validated designs for AI infrastructure. We expect an additional \$1 billion of AI product orders in fiscal year 2025.

As I shared at our Investor Day in June, this momentum is being fueled by multiple use cases in production with the hyperscalers, several of which are in AI. In addition, we have multiple design wins with roughly two-thirds of these in AI.

Over and above the webscale AI opportunity, we believe we are well-positioned to be the key beneficiary of AI application proliferation in the enterprise. Our HyperFabric AI cluster solution created with NVIDIA helps our enterprise customers build infrastructure to run generative AI models and inference applications. The on-premise solution will guide users from design to validated deployment to monitoring and assurance when it becomes available later this fiscal year.

We're also enhancing our own productivity by using AI in our services and customer experience organization. We have a robust AI and automation framework that touches at least 50% of our service requests. In addition, we are incorporating AI assistants into our products so that our customer and partners have efficient options to access support. Before I hand it over to Scott, I want to take a moment to thank our teams for all their hard work to close out the year and their relentless focus on our customers.

In closing, while we're pleased with our performance in a dynamic environment, we know we have to drive strong execution to be successful in the growing markets we serve. We believe this will result in strong growth and profitability as we enter fiscal 2025.

I'll now turn it over to Scott to provide more detail on the quarter and our outlook.

Financial Overview

Thanks, Chuck. I'll start with a summary of our financial results for the quarter then cover the full fiscal year followed by our guidance.

Our Q4 results reflect solid execution with strong margins and strength in orders as customer buying patterns begin to return to normal. For the quarter, total revenue was above the high end of our guidance range at \$13.6 billion, down 10% year-over-year comparing against our strongest quarter ever in the fourth quarter of fiscal 2023. Splunk contributed approximately \$960 million in revenue for the quarter, in line with our expectations.

Non-GAAP net income was \$3.5 billion. Non-GAAP earnings per share was above the high end of our guidance range at \$0.87. The interest impact from financing the Splunk acquisition more than offset the positive operating impact of Splunk. The net effect was a negative impact of \$0.04 on non-GAAP earnings per share for the quarter.

Looking at our Q4 revenue in more detail, total product revenue was \$9.9 billion, down 15% as we move through the final quarter of customer inventory issues, and services revenue was \$3.8 billion, up 6%.

Networking, our largest product category, was down 28% when compared to our Q4 2023 Networking revenues, which benefited from near record shipments of excess backlog. Security was up 81% including the benefit from Splunk. Excluding Splunk, Security grew 6%, driven by competitive wins and growth in SASE and double-digit growth in network security.

Collaboration was flat, driven by growth in our cloud calling and CPaaS offerings, offset by declines in meetings and devices. Observability was up 41%, driven by growth in our Observability suite, our Splunk Observability offering, and ThousandEyes network services. Excluding Splunk, Observability grew 12% for the quarter.

Looking at our recurring metrics, ARR ended the quarter at \$29.6 billion, which increased 22% due to continued strong performance and contribution from Splunk. These factors also drove our product ARR growth of 43%. Without Splunk, ARR was \$25.3 billion, up 4%, and product ARR was up 9%.

Total subscription revenue increased 17% to \$7.7 billion, which now represents 56% of Cisco's total revenue. Without Splunk, total subscription revenue was up 2%, representing 53% of Cisco's total revenue. Total software revenue was up 15% at \$5.3 billion, with software subscription revenue up 25%. 92% of our total software revenue was subscription-based. Without Splunk, software revenue was down 5% due to declines in perpetual license software as we move to more subscription-based software arrangements. Software subscription revenue was up 2%.

Total RPO was \$41.0 billion, up 18% due to both strong organic performance and the addition of Splunk. Product RPO grew 27%. Total short-term RPO was up 17%. Without Splunk, RPO was \$37.5 billion, up 8%, with product RPO also grew at 8%.

As Chuck said, Q4 product orders were up 14% year-over-year. Excluding Splunk, product orders were up 6% year-over-year, indicating the period of inventory digestion by our customers is now largely behind us. Looking at our product orders across our geographic segments year-over-year, Americas was up 15%, EMEA was up 12%, and APJC was up 16%. In our customer markets, public sector was up 20%, enterprise was up 13%, and service provider and cloud was up 5%.

Total non-GAAP gross margin came in at 67.9%, up 200 basis points year-over-year and exceeding the high end of our guidance range. Product gross margin was 67.0%, up 150 basis points, largely driven by Splunk and favorable product mix offset by price. Services gross margin was 70.3%, up 280 basis points. Non-GAAP operating margin came in at the high end of our guidance range at 32.5%.

Shifting to the balance sheet, we ended Q4 with total cash, cash equivalents, and investments of \$17.9 billion. Operating cash flow was \$3.7 billion. Consistent with our capital allocation strategy, we returned \$3.6 billion to shareholders comprised of \$1.6 billion for our quarterly cash dividend and \$2.0 billion of share repurchases. We took advantage of market conditions to increase our share repurchases during the quarter.

Turning to the full fiscal year, we delivered strong margins and increased our operating leverage. Revenue at \$53.8 billion made fiscal 2024 Cisco's second strongest year on record as compared to the all-time high revenues of \$57 billion in fiscal 2023, which benefited from significant shipments of heightened backlog. Splunk contributed approximately \$1.4 billion in revenue after the close of the acquisition in March of this year.

Non-GAAP earnings per share was \$3.73, exceeding the high end of our guidance range, down 4% year-over-year. Splunk was \$0.04 dilutive to full year earnings, including the impact of financing costs.

In terms of our recurring metrics, total software revenue for the full year was up 9% at \$18.4 billion with the product portion also up 9%. Software subscription revenue was up 15%. 89% of total software revenue was subscription-based. Without Splunk, total software revenue was up 1%. Total subscription revenue was \$27.4 billion, an increase of 11%. Without Splunk, total subscription revenue was up 6%.

As Chuck mentioned, total non-GAAP gross margin was 67.5%, up 300 basis points and the highest in 20 years. On the bottom line, non-GAAP net income was \$15.2 billion. Operating cash flow was \$10.9 billion. As a reminder, cash flow was impacted by the timing of large tax payments in fiscal 2024 compared to fiscal 2023.

In the year, we returned \$12.1 billion in value to shareholders through cash dividends and share repurchases. This comprised of \$6.4 billion in quarterly cash dividends and \$5.8 billion of share repurchases. We increased our dividend for the 13th consecutive year in fiscal 2024, reinforcing our confidence in the strength and stability of our ongoing cash flows.

To summarize, we executed well in Q4 and the fiscal year. We exited the year with order levels improving as customers largely completed the implementation of record Cisco product shipments. Further, as Chuck mentioned, we are realigning our expenses to better capture the opportunities ahead. As part of our announced restructuring plan, we expect to impact approximately 7% of our global workforce with total estimated pre-tax charges of up to \$1 billion.

Turning to our financial guidance, for fiscal Q1 our guidance is as follows. We expect revenue to be in the range of \$13.65 billion to \$13.85 billion. We anticipate the non-GAAP gross margin to be in the range of 67% to 68%. Non-GAAP operating margin is expected to be in the range of 32% to 33%. Non-GAAP earnings per share is expected to range from \$0.86 to \$0.88 and in Q1, we're assuming a non-GAAP effective tax rate of approximately 19%.

For fiscal year 2025, our guidance is as follows. We expect revenue to be in the range of \$55 billion to \$56.2 billion. Non-GAAP earnings per share is expected to range from \$3.52 to \$3.58, and we're assuming a non-GAAP effective tax rate of approximately 19%.

Closing

Thank you, all, for joining us. Cisco's next quarterly call which will reflect our fiscal year 2025 first quarter results will be on Wednesday, November 13, 2024, at 1:30 p.m. Pacific Time, 4:30 p.m. Eastern Time.

The prepared remarks set forth above and the related conference call may be deemed to contain forward-looking statements, which are subject to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. These forward-looking statements include, among other things, statements regarding future events (such as our customers reliance on Cisco to connect and protect their organizations in the era of AI and our focus on growth and consistent execution as we invest in AI, cloud and cybersecurity, while maintaining capital returns) and the future financial performance of Cisco (including the guidance for Q1 FY 2025 and full year FY 2025) that involve risks and uncertainties. Readers are cautioned that these forward-looking statements are only predictions and may differ materially from actual future events or results due to a variety of factors, including: business and economic conditions and growth trends in the networking industry, our customer markets and various geographic regions; global economic conditions and uncertainties in the geopolitical environment; our development and use of artificial intelligence; overall information technology spending; the growth and evolution of the Internet and levels of capital spending on Internet-based systems; variations in customer demand for products and services, including sales to the service provider market, cloud, enterprise and other customer markets; the return on our investments in certain priorities, key growth areas, and in certain geographical locations, as well as maintaining leadership in Networking and services; the timing of orders and manufacturing and customer lead times; supply constraints; changes in customer order patterns or customer mix; insufficient, excess or obsolete inventory; variability of component costs; variations in sales channels, product costs or mix of products sold; our ability to successfully acquire businesses and technologies and to successfully integrate and operate these acquired businesses and technologies; our ability to achieve expected benefits of our partnerships; increased competition in our product and services markets, including the data center market; dependence on the introduction and market acceptance of new product offerings and standards; rapid technological and market change; manufacturing and sourcing risks; product defects and returns; litigation involving patents, other intellectual property, antitrust, stockholder and other matters, and governmental investigations; our ability to achieve the benefits of restructurings and possible changes in the size and timing of related charges; cyber attacks, data breaches or other incidents; vulnerabilities and critical security defects; our ability to protect personal data; evolving regulatory uncertainty; terrorism; natural catastrophic events (including as a result of global climate change); any pandemic or epidemic; our ability to achieve the benefits anticipated from our investments in sales, engineering, service, marketing and manufacturing activities; our ability to recruit and retain key personnel; our ability to manage financial risk, and to manage expenses during economic downturns; risks related to the global nature of our operations, including our operations in emerging markets; currency fluctuations and other international factors; changes in provision for income taxes, including changes in tax laws and regulations or adverse outcomes resulting from examinations of our income tax returns; potential volatility in operating results; and other factors listed in Cisco's most recent reports on Forms 10-Q and 10-K filed on May 21, 2024 and September 7, 2023, respectively. The financial information contained in the prepared remarks and the related conference call should be read in conjunction with the consolidated financial statements and notes thereto included in Cisco's most recent reports on Forms 10-Q and 10-K as each may be amended from time to time. Cisco's results of operations for the three months and the year ended July 27, 2024 are not necessarily indicative of Cisco's operating results for any future periods. Any projections in the prepared remarks and the related conference call are based on limited information currently available to Cisco, which is subject to change. Although any such projections and the factors influencing them will likely change, Cisco will not necessarily update the information, since Cisco will only provide guidance at certain points during the year. Such information speaks only as of the date of the prepared remarks and the related conference call.