

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]

Q1FY24 Earnings Results Conference Call

Wednesday, November 14, 2024

Introduction

Good afternoon, everyone. This is Sami Badri, Cisco's Head of Investor Relations, joined by Chuck Robbins, our Chair and CEO; and Scott Herren, our CFO. Cisco's earnings press release and supplemental information, including GAAP to non-GAAP reconciliations, are available on our Investor Relations website. Following this call, we will also make the recorded webcast and slides available on the website.

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

Please note that our discussions today will include forward-looking statements, including our guidance for the second quarter and fiscal year 2025. These statements are subject to risks and uncertainties detailed in our SEC filings, particularly our most recent 10-K report, which identifies important risk factors that could cause actual results to differ materially from those contained in our 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.

Now, I'll turn it over to Chuck.

Opening Remarks

Thanks, Sami, and thank you all for joining us today. Cisco delivered a strong start to fiscal 2025, delivering \$13.8 billion in revenue for the first quarter, coming in at the high end of our guidance range. This was supported by solid growth in annualized recurring revenue, remaining performance obligations and subscription revenue, which now accounts for 57% of our total revenue. The strength of our recurring revenue streams is helping to fuel our profitability. Non-

GAAP EPS of \$0.91 exceeded the high end of our guidance range, driven by the highest non-GAAP gross margin we have seen in more than 20 years, which was further enhanced by Splunk.

The combination of Cisco and Splunk and our teams' great execution are both driving our strong operating leverage. The strength of our operating performance and free cash flow in Q1 fueled a return of \$3.6 billion in value to our shareholders through share repurchases and cash dividends, delivering on our commitment to consistent capital returns.

Building on the growing demand we saw at the end of fiscal year 2024, product orders grew 20% year-over-year in Q1 and were up 9% organically. This is an acceleration of the 14% product order growth we saw just three months ago, and is a clear sign of normalizing demand for Cisco's innovation.

Now, let me share some details on our first quarter, starting with the demand environment. Enterprise product orders were up 33%, driven by particularly strong performance in the Americas and EMEA across a broad range of customers. We saw continued strong momentum in service provider and cloud, with product orders up 28%, driven by triple-digit growth in webscale.

In Q1, our webscale customers placed AI infrastructure orders in excess of \$300 million. Our AI pipeline continued to be strong. We have earned more design wins and remain confident that we will exceed our target of \$1 billion of AI orders this fiscal year from webscale customers.

After a very strong Q4 last quarter, public sector orders were up 2% year-over-year in Q1. Federal spending in the US was lower year-over-year due to continuing resolutions discussions, the impact of the Fiscal Responsibility Act, and the diversion of funds within US federal. It's important to note that we believe the deals we are working on with US federal customers are simply delayed, not lost. In both EMEA and APJC, year-over-year public sector order growth was strong. Now, let me share some data on demand through the lens of our products to provide some incremental color.

Our Networking portfolio saw double-digit product order growth overall, driven by switching, wireless and Internet infrastructure. Looking at data center switching in particular, we have seen three consecutive quarters of double-digit order growth and an acceleration from Q4 into Q1. This shows our competitive strength in this key market and the power of our Nexus brand and the build out of private cloud infrastructure by our customers. We expect this momentum to continue, as customers are showing significant interest in our 400-gig and 800-gig switches based on Silicon One.

Security orders more than doubled year-over-year, driven by the advanced threat intelligence capabilities of Splunk. Excluding Splunk, growth in security product orders was driven by our renewed security strategy and new product pipeline, which continues to be well received by customers and analysts. We continue to see momentum around our new security products like XDR, Secure Access and Multicloud Defense, with now over 1,000 customers deploying these products thus far.

In Q1, we had a marquee win for over 75,000 cloud security seats, with a multinational IT services and consultancy company. The customer largely replaced an SSE competitor with our solution and moved from planning to implementation in 120 days, highlighting how fast our teams can implement our solutions at scale. We also booked our first seven-figure Hypershield deal in Q1.

Collaboration product orders grew double-digits again driven by demand for devices and our Cloud Webex Suite. Finally, in Observability, orders were up high-single digits driven by our Network Assurance solution, ThousandEyes and Splunk Observability.

I'd also like to highlight some of the progress we've made integrating Splunk. We now have a dozen updated data integrations between Cisco and Splunk across our Security and Networking portfolio, including Secure Firewall, Catalyst Center, SD-WAN and ICE. We continue our joint selling motions between Cisco and Splunk, including Cisco Secure Network Analytics and XDR alongside Splunk's SIEM offering enhanced capabilities to the security operations center. We also continue to build our market-leading observability solutions to accelerate full stack observability for the enterprise.

Overall, our Q1 results highlight continued strong demand for Cisco technologies, driven by the need for modern resilient networks as AI begins to scale. Findings from our new global AI partner study show that IT partners around the world are anticipating a transformative wave of AI technology demand, driven by infrastructure, cybersecurity and customer experience, which they expect to fuel the majority of their revenue over the next four to five years.

With the breadth of our portfolio, we are uniquely positioned to capitalize on this AI technology demand, as customers are investing in their critical infrastructure to prepare for AI. In fact, there are three distinct but connected pillars to the AI networking opportunity for Cisco, which we have outlined on a slide as part of our quarterly materials.

First, AI training infrastructure for webscale customers. AI networks demand scalable, programmable, low- power switches with advanced load balancing and observability. These characteristics in our products are driving hyperscalers to deploy the Cisco 8000 with Cisco Silicon One G200 for maximum power efficiency in their back-end AI training networks. As further proof, we also won a new super spine AI networking use case with one of our webscale customers this quarter.

Second, AI network connectivity. This quarter, we booked further platform sales with global enterprise customers, who are leveraging our technology platforms to modernize and automate their network operations to prepare for large-scale connectivity to AI applications. Our technology platforms across switching, routing, security, and observability will help enable our customers by leveraging cutting-edge innovations like AI-powered robotics and unmatched supply chain visibility.

Third, AI network inference and enterprise clouds. Most of the CIOs and technology leaders we talk to say that their organizations are planning full GenAI adoption within the next two years. Yet only 13% of organizations say their infrastructure is ready for AI today, according to the

Cisco AI Readiness Index. To help our customers prepare, we have announced two new additions to our data center infrastructure portfolio, a

new NVIDIA-based AI server and AI PODs, including NVIDIA's AI enterprise cloud native software platform and managed through Cisco Intersight to simplify and de-risk AI infrastructure deployment. Our new AI server is expected to begin shipping next month, and our AI PODs are orderable this month.

In addition, HyperFabric, our fabric-as-a-service solution, which is expected to be available in early calendar 2025, further simplifies infrastructure deployment and management, while providing real-time visibility into network performance. With these solutions, we are bringing the power of open hyperscale AI networking to the enterprise.

We also continue to fuse AI capabilities into our products. Hypershield, our first truly distributed AI-native cybersecurity solution built into the fabric of the network shows how we are delivering secured networking, making it easier for our customers to protect against evolving threats. Splunk's asset and risk intelligence solution is another example of how we are providing insights to help customers understand their security maturity and demonstrate compliance with evolving regulations.

In our Collaboration portfolio, we recently introduced the Webex AI Agent, AI Agent Studio and Cisco AI Assistant features for Webex Contact Center. These solutions use advanced conversational intelligence and automation to improve overall customer satisfaction. We have seen strong initial interest from customers and will continue to strengthen our Collaboration products, increasing AI capabilities.

We're also enhancing our own productivity by using AI in our services and customer experience organization. Over 60% of our technical assistance center support cases are now touched by AI-enabled automation backed by our expertise for faster resolutions, which is leading to higher customer satisfaction scores. In addition, our internal AI Assistant for TAC works alongside our engineers to improve quality and speed time to resolution, while allowing our people to work on more complex and creative problem solving.

To summarize, as we look at what's occurring with AI, there are three key things happening. First, there is significant investment in back-end AI networks with hyperscalers focused on training. Second, as enterprises look to adopt and deploy AI, they need to modernize and secure their infrastructure to prepare for pervasive deployment of AI applications. Finally, the combination of mature back-end models with enterprise AI application deployment will lead to increased capacity requirements on both private and public front-end cloud networks. Cisco is already playing a major role across all three of these significant opportunities and are uniquely positioned to win with the breadth of our product portfolio and our trusted customer relationships.

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

Financial Overview

Thanks, Chuck. We executed well in Q1 with strong order momentum, margins and operating cash flow. For the quarter, total revenue was at the high end of our guidance range at \$13.8 billion, down 6% year-over-year. As a reminder, Q1 of fiscal 2024 was the last quarter of significantly elevated backlog shipments.

Non-GAAP net income was \$3.7 billion and non-GAAP earnings per share were above the high end of our guidance range at \$0.91.

Looking at our Q1 revenue in more detail. Total product revenue was \$10.1 billion, down 9% and service revenue was \$3.7 billion, up 6%. Networking was down 23%, primarily driven by the elevated level of shipment we saw a year ago. As Chuck said, we saw strong order growth across our networking products as customers have worked down inventory and deployed the networking products we shipped them last year.

Security was up 100%, primarily driven by growth in our Threat Intelligence, Detection and Response offerings, which includes the offerings from Splunk, Network Security and SASE. Excluding Splunk, Security grew 2%, and our Security portfolio was particularly impacted by the delays in spending in US Fed.

Collaboration was down 3%, driven by declines in our on-prem Webex Suite and Collaboration Devices, partially offset by growth in our Contact Center and CPaaS offerings. Observability was up 36%, driven primarily by Observability Suite and growth in network assurance offerings. Excluding Splunk, Observability grew 1% for the quarter.

Looking at our recurring metrics, ARR ended the quarter at \$29.9 billion, which increased 22% with product ARR growth of 42%. Total subscription revenue increased 21% to \$7.8 billion, representing 57% of Cisco's total revenue. Total software revenue was up 24% at \$5.5 billion, with software subscription revenue up 35%. Total RPO was \$40 billion, up 15% year-over-year. Product RPO grew 24% and total short-term RPO was up 15% to \$20.3 billion.

Q1 product orders were up 20% year-over-year. Excluding Splunk, product orders were up 9% year-over-year. Looking at our product orders across our geographic segments, the Americas was up 17%, EMEA was up 26%, and APJC was up 25%. In our customer markets, enterprise is up 33%, service provider and cloud was up 28%, and public sector was up 2%.

Total non-GAAP gross margin came in at 69.3%, up 220 basis points year-over-year and exceeding the high end of our guidance range and reaching the highest level in more than 20 years. Product gross margin was 68.9%, up 240 basis points, driven by Splunk, favorable product mix, productivity improvements, and the one-time benefit of duty drawback, partially offset by price. Services gross margin was 70.3%, up 130 basis points.

We continued our focus on profitability and financial discipline with non-GAAP operating margin above the high end of our guidance range at 34.1%. On the bottom line, Q1 non-GAAP net income was \$3.7 billion and earnings per share were \$0.91.

Shifting to the balance sheet, we ended Q1 with total cash, cash equivalents and investments of \$18.7 billion. Operating cash flow was \$3.7 billion, up 54%. From a capital allocation perspective, we returned \$3.6 billion to shareholders during the quarter, comprised of \$1.6 billion for our quarterly cash dividend and \$2 billion of share repurchases.

We continue to invest organically and inorganically in our innovation pipeline. During Q1, we closed two software acquisitions, DeepFactor to accelerate innovation in the Cisco Security Cloud and augment our Secure Access offerings, and Robust Intelligence, which brings enhanced protection for AI models throughout their life cycle from development to production.

Additionally, we announced our intent to acquire Deeper Insights AI to expand our customer experience team's technology footprint and engineering talent, accelerating innovation and momentum of Cisco's CX AI capabilities and services. These investments are highly complementary to our internal R&D and align with our strategy to strengthen our position in security and AI with targeted strategic M&A.

To summarize, we started the fiscal year with a solid quarter, highlighted by strong order growth, margins and non-GAAP EPS. We remain focused on making strategic investments and accelerating innovation across our business to best capitalize on the significant growth opportunities we see ahead, all underpinned by disciplined expense management. It's this powerful combination that continues to fuel our strong cash flow generation as well as our ability to return significant value to shareholders.

Turning to our financial guidance. For fiscal quarter Q2, our guidance is as follows. We expect revenue to be in the range of \$13.75 billion to \$13.95 billion. We anticipate non-GAAP gross margins to be in the range of 68% to 69%. Non-GAAP operating margin is expected to be in the range of 33.5% to 34.5%. Non-GAAP earnings per share is expected to range from \$0.89 to \$0.91.

For fiscal year 2025, our guidance is we expect revenue to be in the range of \$55.3 billion to \$56.3 billion.

Non-GAAP earnings per share guidance is expected to range from \$3.60 to \$3.66. In both our Q2 and full year guidance, we're assuming a non-GAAP effective tax rate of approximately 19%.

Closing

Cisco's next quarterly call, which will reflect our FY 2025 second quarter results, will be on Wednesday, February 12, 2025, 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' investments in critical infrastructure to prepare for AI, our position to capitalize on that opportunity given the breadth of our portfolio, and our focus on solid execution and operating discipline while making strategic investments to drive innovation and growth) 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 key priority 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 report on Form 10-K filed on September 5, 2024. The financial information contained in this release should be read in conjunction with the consolidated financial statements and notes thereto included in Cisco's most recent report on Form 10-K as it may be amended from time to time. Cisco's results of operations for the three months ended October 26, 2024 are not necessarily indicative of Cisco's operating results for any future periods. Any projections in this release 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 this release.