



# Cisco Systems Inc. (CSCO)

Updated August 15<sup>th</sup>, 2019 by Nathan Parsh

## Key Metrics

<b>Current Price:</b>	\$46	<b>5 Year CAGR Estimate:</b>	11.1%	<b>Volatility Percentile:</b>	29.3%
<b>Fair Value Price:</b>	\$51	<b>5 Year Growth Estimate:</b>	6.0%	<b>Momentum Percentile:</b>	62.4%
<b>% Fair Value:</b>	90%	<b>5 Year Valuation Multiple Estimate:</b>	2.1%	<b>Growth Percentile:</b>	54.2%
<b>Dividend Yield:</b>	3.0%	<b>5 Year Price Target</b>	\$68	<b>Valuation Percentile:</b>	60.4%
<b>Dividend Risk Score:</b>	B	<b>Retirement Suitability Score:</b>	B	<b>Total Return Percentile:</b>	54.7%

## Overview & Current Events

Cisco Systems is the global leader in high performance computer networking systems. The company's routers and switches allow networks around the world to connect to each other through the internet. Cisco also offers data center, cloud, and security products. The company went public on 2/16/1990 at the split-adjusted price of \$0.06. Today, Cisco employs more than 72,000 people and has a market capitalization of more than \$197 billion. The company generates almost \$52 billion in annual revenues.

Cisco reported financial results for the fourth quarter of fiscal 2019 on 8/15/2019. The company earned \$0.83 per share in the quarter, which was \$0.01 above expectations and an 18.6% increase from the previous year. Accounting for the company's divested service provider video business, revenue increased 6% to \$13.4 billion, which was \$36 million above estimates. For the fiscal year, earnings-per-share grew 19% to \$3.09, \$0.02 above our estimates. Revenue increased 7% to \$51.7 billion.

Infrastructure Platforms grew 6% on the strength in demand for the company's Catalyst 9000 switch. Applications revenues were up 11% due in part to higher demand for artificial intelligence products. Security improved 14% due to increased sales for identity and access, advanced threat and united threat. Software subscriptions accounted for 70% of total software revenue, an increase of 12% from the previous year. For the quarter, product revenue increased 6% while service revenue grew 4%. The Americas region improved 9% while the Europe/Middle East/Africa region was up 7%. Asia/Pacific declined 4%.

Shares of Cisco closed the trading session down nearly 9%. Guidance for the upcoming quarter was the primary reason for the sizeable drop. For the first quarter of 2020, Cisco expects to earn \$0.81 per share, \$0.02 below consensus estimates. Revenue is expected to grow 0% to 2% to \$13.1 billion to \$13.36 billion, which was below estimates of \$13.4 billion. We expect Cisco to earn \$3.41 per share in fiscal 2020, which would be a 10.4% gain from the previous year.

## Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
<b>EPS</b>	\$1.33	\$1.62	\$1.85	\$2.02	\$2.06	\$2.21	\$2.36	\$2.39	\$2.60	\$3.09	<b>\$3.41</b>	<b>\$4.56</b>
<b>DPS</b>	---	\$0.12	\$0.28	\$0.62	\$0.72	\$0.80	\$0.94	\$1.10	\$1.32	\$1.40	<b>\$1.40</b>	<b>\$1.87</b>
<b>Shares<sup>1</sup></b>	5655	5435	5298	5389	5107	5085	5029	4983	4670	4307	<b>4250</b>	<b>4000</b>

Between 2009 and 2018, Cisco's earnings increased at a rate of 9.5% per year, above the 2008-2017 growth rate of 6%. We reaffirm our expected growth rate of 6% due to a combination of revenue growth and share repurchases.

Cisco is one of the younger dividend payers in our coverage universe, but shareholders have seen impressive dividend growth since the company instituted its dividend. The average increase over the past five years is 13%. The most recent raise was announced on 2/13/2019 and resulted in a 6.1% increase for the 4/24/2019 payment. Though the payout ratio is in good shape, we assume dividend growth will equal earnings growth going forward given that Cisco spends so heavily on share repurchases as well.

<sup>1</sup> Share count in millions

Disclosure: This analyst has a position in the security discussed in this research report.



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## Valuation Analysis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2025
Avg. P/E	17.9	11.9	9.7	10.3	11.3	12.3	11.5	13.3	16.9	15.0	13.5	15.0
Avg. Yld.	---	0.6%	1.6%	3.0%	3.1%	2.9%	3.5%	3.5%	3.0%	3.0%	3.0%	2.7%

Shares of Cisco have decreased \$11, or 19%, since our 5/17/2019 update. Much of this decline occurred during the market-wide selloff that occurred in August. The 2009-2010 time frame saw shares of Cisco trade with a well above average price-to-earnings multiple. Excluding 2009-2010, shares have an average P/E of 12.2. Given the company's growth in subscription services and large cash balance, we maintain our target price-to-earnings multiple of 15 for fiscal 2025. If Cisco's stock was to revert to our target multiple by 2025, then valuation would be a 2.1% tailwind to total returns over this time period.

## Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	---	7%	15%	30%	35%	36%	40%	46%	50%	45%	41%	41%

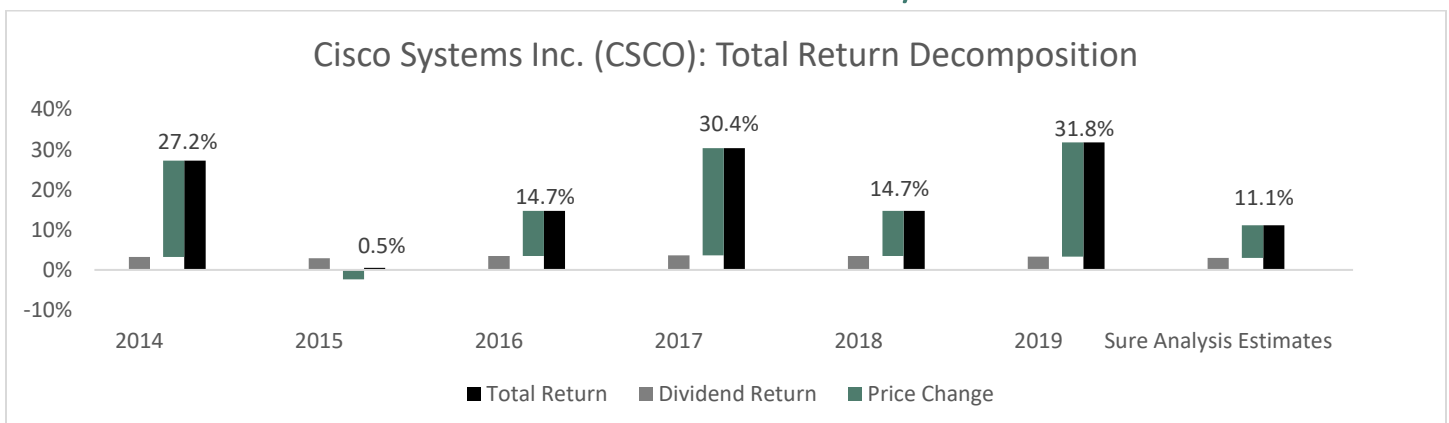
Cisco ended the fiscal year with \$33.4 billion in cash and equivalents. Given the cash on the company's balance sheet, it is likely that Cisco would be able to continue to pay a dividend even in the event of an extended recession.

With everything from computers to cell phones to buildings connected today, Cisco is in a prime position to capitalize on the Internet of Things. In fact, Cisco is responsible for 80% of all the data moved over the internet in the past 30 years. While Cisco continues to enjoy hardware dominance, the company is attempting to become more of a subscription services company. This should help create more predictable revenue streams. One such example of this effort is the Catalyst 9000 switch. This switch is twice as fast as competing products and protects data and cloud networks.

## Final Thoughts & Recommendation

Cisco posted solid top and bottom-line growth in both the fourth quarter and full fiscal year. However, that didn't stop the stock from dropping almost 9% following the results release. We think that this drop is due in large part to the guidance for the first quarter of fiscal 2020, but also because the stock had been up 22% through 8/13/2019. This selloff has raised our estimates for total annual returns over the next five years to 11.1% from 4.3% previously. As a result, Sure Dividend's rating for Cisco has been raised to buy from hold. We also raise our 2025 price target \$6 to \$68 due to earnings estimates for the current fiscal. Investors waiting for an opportunity to purchase shares of Cisco at a lower price are encouraged to use the recent share price weakness to purchase the stock.

## Total Return Breakdown by Year



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## Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
<b>Revenue</b>	40040	43218	46061	48607	47142	49161	49247	48005	49330	51904
<b>Gross Profit</b>	25643	26536	28209	29440	27769	29681	30960	30224	30606	32666
<b>Gross Margin</b>	64.0%	61.4%	61.2%	60.6%	58.9%	60.4%	62.9%	63.0%	62.0%	62.9%
<b>SG&amp;A Exp.</b>	10715	11720	11969	11802	11437	11861	11433	11177	11386	11398
<b>D&amp;A Exp.</b>	2030	2486	2208	2460	2439	2442	2150	2286	2192	1897
<b>Operating Profit</b>	9164	8473	10369	11301	9763	11254	12928	12729	12667	14541
<b>Op. Margin</b>	22.9%	19.6%	22.5%	23.2%	20.7%	22.9%	26.3%	26.5%	25.7%	28.0%
<b>Net Profit</b>	7767	6490	8041	9983	7853	8981	10739	9609	110	11621
<b>Net Margin</b>	19.4%	15.0%	17.5%	20.5%	16.7%	18.3%	21.8%	20.0%	0.2%	22.4%
<b>Free Cash Flow</b>	9165	8905	10365	11734	11057	11325	12424	12912	12832	14922
<b>Income Tax</b>	1648	1335	2118	1244	1862	2220	2181	2678	12929	2950

## Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
<b>Total Assets (\$B)</b>	81	87	92	101	105	113	122	130	109	98
<b>Cash &amp; Equivalents</b>	4581	7662	9799	7925	6726	6877	7631	11708	8934	11750
<b>Acc. Receivable</b>	4929	4698	4369	5470	5157	5344	5847	5146	5554	5491
<b>Inventories</b>	1327	1486	1663	1476	1591	1627	1217	1616	1846	1383
<b>Goodwill &amp; Int.</b>	19948	19359	18957	25322	27519	26845	29126	32305	34258	35730
<b>Total Liabilities</b>	36845	39836	40458	42063	48409	53666	58067	63681	65580	64222
<b>Accounts Payable</b>	895	876	859	1029	1032	1104	1056	1385	1904	2059
<b>Long-Term Debt</b>	15284	16822	16328	16211	20845	25354	28643	33717	25569	24666
<b>Total Equity</b>	44267	47226	51286	59120	56654	59698	63586	66137	43204	33571
<b>D/E Ratio</b>	0.35	0.36	0.32	0.27	0.37	0.42	0.45	0.51	0.59	0.73

## Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
<b>Return on Assets</b>	10.4%	7.7%	9.0%	10.3%	7.6%	8.2%	9.1%	7.6%	0.1%	11.3%
<b>Return on Equity</b>	18.7%	14.2%	16.3%	18.1%	13.6%	15.4%	17.4%	14.8%	0.2%	30.3%
<b>ROIC</b>	14.3%	10.5%	12.2%	14.0%	10.3%	11.0%	12.1%	10.0%	0.1%	18.3%
<b>Shares Out.</b>	5655	5435	5298	5389	5107	5085	5029	4983	4670	4307
<b>Revenue/Share</b>	6.85	7.77	8.52	9.03	8.93	9.55	9.68	9.51	10.11	11.66
<b>FCF/Share</b>	1.57	1.60	1.92	2.18	2.09	2.20	2.44	2.56	2.63	3.35

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.

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