



Cisco Systems Inc. (CSCO)

Updated August 13th, 2020 by Nathan Parsh

Key Metrics

Current Price:	\$43	5 Year CAGR Estimate:	10.8%	Market Cap:	\$203 billion
Fair Value Price:	\$47	5 Year Growth Estimate:	6.0%	Ex-Dividend Date:	10/3/2020 ¹
% Fair Value:	91%	5 Year Valuation Multiple Estimate:	2.0%	Dividend Payment Date:	10/23/2020 ²
Dividend Yield:	3.3%	5 Year Price Target	\$63	Years Of Dividend Growth:	10
Dividend Risk Score:	B	Retirement Suitability Score:	B	Last Dividend Increase:	2.9%

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 generates nearly \$50 billion in annual revenues.

Cisco reported earnings results for the fourth quarter and fiscal year 2020 on 8/12/2020. Revenue declined 9.5% to \$12.2 billion, but was \$60 million higher than expected. Adjusted earnings-per-share decreased \$0.03, or 3.6%, to \$0.80, which was \$0.06 higher than expected. For the year, revenue was down 5% to \$49.3 billion while adjusted earnings-per-share improved 4% to \$3.21. This was \$0.03 lower than we had expected.

Infrastructure Platforms, which is the largest segment within Cisco, had a revenue decrease of 16%. This segment felt the most impact from the COVID-19 pandemic. Switching, routing, data center and wireless were all weaker during the quarter. The Catalyst 9K switch, however, benefited from customer's employees working at home during the quarter. Services sales were flat year-over-year as software and support gains were offset by advisory services. Software subscriptions accounted for 78% of total software revenue, an increase of 8% from the prior year. Revenues for Applications declined 9% due to continued weakness in unified communication. AppDynamics and Internet of Things software had solid gains. Security sales increased 10% as demand for network security, identify and access, advanced threat and unified front management products remained strong. Total product orders were down by 10%, led by an 11.6% decrease in the Americas region. EMEA was lower by 6% while Asia-Pacific/Japan/China was down 7%. All customer categories declined from the previous year, led by a 23% drop in sales to commercial customers. Total gross margins decreased 120 basis points to 65.6%. Deferred revenue was up almost 11% to \$20.4 billion. Cisco did not repurchase any shares during the fourth quarter, but did distribute \$1.5 billion of dividends.

Cisco expects first quarter of fiscal year 2021 adjusted earnings-per-share of \$0.41 to \$0.47, which is significantly below consensus estimates of \$0.75. Revenue is expected to range from \$11.7 billion to \$11.98 billion, which represents a decline of 9% to 11% year-over-year and is below consensus estimates of \$12.2 billion. Analysts expect adjusted EPS of \$3.15 for fiscal year 2021.

Growth on a Per-Share Basis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
EPS	\$1.62	\$1.85	\$2.02	\$2.06	\$2.21	\$2.36	\$2.39	\$2.60	\$3.09	\$3.21	\$3.15	\$4.22
DPS	\$0.12	\$0.28	\$0.62	\$0.72	\$0.80	\$0.94	\$1.10	\$1.32	\$1.40	\$1.44	\$1.44	\$1.93
Shares³	5435	5298	5389	5107	5085	5029	4983	4670	4307	4243	4243	4000

Between 2010 and 2019, Cisco's earnings increased at a rate of 8.8% per year. We reaffirm our expected growth rate of 6% due to a combination of improving margins and share repurchases offset by revenue weakness.

¹ Estimated ex-dividend date

² Estimated dividend payment date

³ Share count in millions

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Cisco has increased its dividend for a decade and 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 2/12/2020 and resulted in a 2.9% increase for the 4/22/2020 payment. Though the payout ratio is in good shape, we assume dividend growth will equal earnings growth going forward.

Valuation Analysis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	Now	2026
Avg. P/E	11.9	9.7	10.3	11.3	12.3	11.5	13.3	16.9	15.0	14.7	13.7	15.0
Avg. Yld.	0.6%	1.6%	3.0%	3.1%	2.9%	3.5%	3.5%	3.0%	3.0%	3.1%	3.3%	3.0%

Shares of Cisco have decreased \$1, or 2.3%, since our 5/15/2020 update. 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 in recent quarters and large cash balance, we maintain our target P/E of 15 for fiscal 2025. If Cisco's stock was to revert to our target multiple by 2025, then valuation would add 1.9% to annual returns over this time period.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
Payout	7%	15%	30%	35%	36%	40%	46%	50%	45%	45%	46%	46%

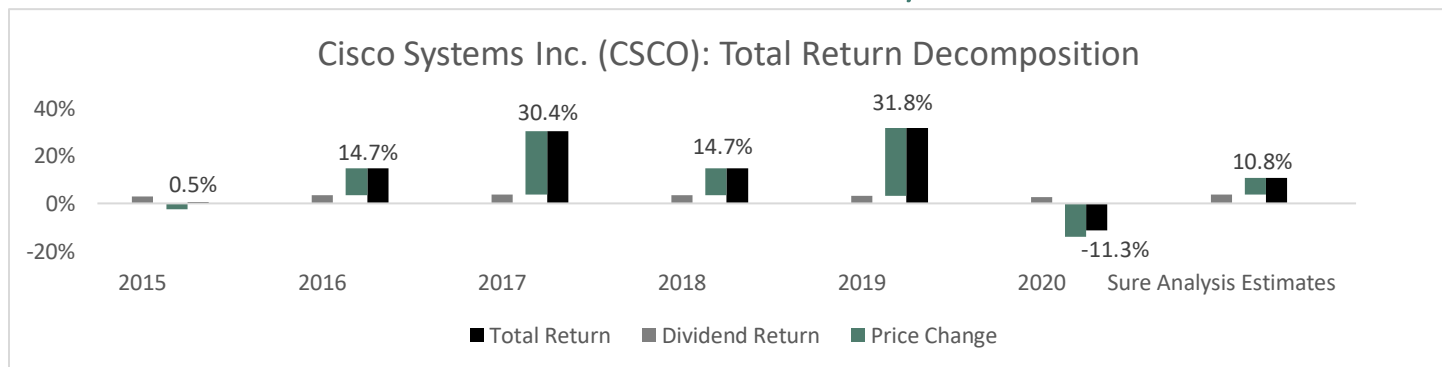
Cisco ended third quarter of fiscal 2020 with \$29.4 billion in cash and equivalents. Given the cash on the balance sheet, it is likely that Cisco would be able to continue to pay a dividend even in the event of an extended recession.

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 Systems is projected to return 10.8% annually over the next five years, matching our previous estimate. The fourth quarter did manage to top reduced estimates, but the company's guidance for the current quarter was well off what the market had anticipated. Every region and nearly every product category had declining sales during the quarter, though a large portion of this was due to the COVID-19 pandemic. We have decreased our five-year price target \$2 to \$63, but feel that Cisco offers enough potential return to warrant a buy rating.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Revenue	43218	46061	48607	47142	49161	49247	48005	49330	51904	49301
Gross Profit	26536	28209	29440	27769	29681	30960	30224	30606	32666	31683
Gross Margin	61.4%	61.2%	60.6%	58.9%	60.4%	62.9%	63.0%	62.0%	62.9%	64.3%
SG&A Exp.	11720	11969	11802	11437	11861	11433	11177	11386	11398	11094
D&A Exp.	2486	2208	2460	2439	2442	2150	2286	2192	1897	1808
Operating Profit	8473	10369	11301	9763	11254	12928	12729	12667	14541	14101
Op. Margin	19.6%	22.5%	23.2%	20.7%	22.9%	26.3%	26.5%	25.7%	28.0%	28.6%
Net Profit	6490	8041	9983	7853	8981	10739	9609	110	11621	11214
Net Margin	15.0%	17.5%	20.5%	16.7%	18.3%	21.8%	20.0%	0.2%	22.4%	22.7%
Free Cash Flow	8905	10365	11734	11057	11325	12424	12912	12832	14922	14656
Income Tax	1335	2118	1244	1862	2220	2181	2678	12929	2950	2756

Balance Sheet Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Total Assets (\$B)	87095	91759	101191	105070	113373	121652	129818	108784	97793	94853
Cash & Equivalents	7662	9799	7925	6726	6877	7631	11708	8934	11750	11809
Acc. Receivable	4698	4369	5470	5157	5344	5847	5146	5554	5491	5472
Inventories	1486	1663	1476	1591	1627	1217	1616	1846	1383	1282
Goodwill & Int.	19359	18957	25322	27519	26845	29126	32305	34258	35730	35382
Total Liabilities	39836	40458	42063	48409	53666	58067	63681	65580	64222	56933
Accounts Payable	876	859	1029	1032	1104	1056	1385	1904	2059	2218
Long-Term Debt	16822	16328	16211	20845	25354	28643	33717	25569	24666	14583
Total Equity	47226	51286	59120	56654	59698	63586	66137	43204	33571	37920
D/E Ratio	0.36	0.32	0.27	0.37	0.42	0.45	0.51	0.59	0.73	0.38

Profitability & Per Share Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Return on Assets	7.7%	9.0%	10.3%	7.6%	8.2%	9.1%	7.6%	0.1%	11.3%	11.6%
Return on Equity	14.2%	16.3%	18.1%	13.6%	15.4%	17.4%	14.8%	0.2%	30.3%	31.4%
ROIC	10.5%	12.2%	14.0%	10.3%	11.0%	12.1%	10.0%	0.1%	18.3%	20.3%
Shares Out.	5435	5298	5389	5107	5085	5029	4983	4670	4307	4243
Revenue/Share	7.77	8.52	9.03	8.93	9.55	9.68	9.51	10.11	11.66	11.59
FCF/Share	1.60	1.92	2.18	2.09	2.20	2.44	2.56	2.63	3.35	3.45

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

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