Cisco Q3 2021 Earnings Update

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Summary: Cisco remains a good RELATIVE investment proposition. The numbers look good from a relative comparison to the market. Debt is going down further, growth is likely ahead and at some point they might put the hammer down on buybacks. Positive outlook on the stock price but keep in mind this is a relative investing opportunity, not an absolute as the long-term expected return is below 10%.

Q3 2021 Numbers

Cisco's numbers were really good last quarter.

Cisco Reports Third Quarter Earnings

SAN JOSE, Calif., May 19, 2021 /PRNewswire/ --

News Summary:

- Overall performance: $12.8 billion in revenue, up 7% year over year with broad-based strength across the business; GAAP EPS $0.68 and Non-GAAP EPS $0.83, each up 5% year over year
- 10% year-over-year total product order growth representing the strongest demand in nearly a decade
- Continued momentum in transforming business to software and subscriptions: 81% of software revenue sold as a subscription, up from 76% last quarter

Q3 Results:

- **Revenue:** $12.8 billion
  - Increase of 7% year over year
- **Earnings per Share:** GAAP: $0.68; Non-GAAP: $0.83
  - GAAP EPS increased 5% year over year
  - Non-GAAP EPS increased 5% year over year

Q4 Guidance:

- **Revenue:** 6% to 8% growth year over year
- **Earnings per Share:** GAAP: $0.64 to $0.69; Non-GAAP: $0.81 to $0.83

Cisco today reported third quarter results for the period ended May 1, 2021. Cisco reported third quarter revenue of $12.8 billion, net income on a generally accepted accounting principles (GAAP) basis of $2.9 billion or $0.68 per share, and non-GAAP net income of $3.5 billion or $0.83 per share.

Cisco Press Release

Cash is down, I have to check closely what is going on there: we have return to shareholders of around $2 billion, but also a few acquisitions.

Net Income and EPS -- On a GAAP basis, net income was $2.9 billion, an increase of 3%, and EPS was $0.68, an increase of 5%. On a non-GAAP basis, net income was $3.5 billion, an increase of 4%, and EPS was $0.83, an increase of 5%.

Cash Flow from Operating Activities -- $3.9 billion for the third quarter of fiscal 2021, a decrease of 8% compared with $4.2 billion for the third quarter of fiscal 2020.

Balance Sheet and Other Financial Highlights

Cash and Cash Equivalents and Investments -- $23.6 billion at the end of the third quarter of fiscal 2021, compared with $29.4 billion at the end of fiscal 2020.

Deferred Revenue -- $20.9 billion, up 12% in total, with deferred product revenue up 20%. Deferred service revenue was up 7%.

Remaining Performance Obligations -- $28.1 billion at the end of the third quarter of fiscal 2021, up 10%.

Capital Allocation -- In the third quarter of fiscal 2021, we returned $2.1 billion to stockholders through share buybacks and dividends. We declared and paid a cash dividend of $0.37 per common share, or $1.6 billion, and repurchased approximately 10 million shares of common stock under our stock repurchase program at an average price of $48.71 per share for an aggregate purchase price of $510 million. The remaining authorized amount for stock repurchases under the program is $8.7 billion with no termination date.

Acquisitions

In the third quarter of fiscal 2021, we closed the following acquisitions:

- Acacia Communications, Inc., a public fabless semiconductor company that develops, manufactures and sells high-speed coherent optical interconnect products that are designed to transform communications networks through improvements in performance, capacity and cost.
- IMImobile PLC, a United Kingdom-based publicly-traded cloud communications software and services company.
- Dashbase, Inc., an enterprise software company.

In the fourth quarter of fiscal 2021, we closed the acquisition of Slido s.r.o, a privately held company that provides an audience interaction platform.

Ok, they have increased working capital due to growth and also paid down $2 billion of debt which is getting very low.

CONDENSED CONSOLIDATED BALANCE SHEETS
(In millions)
(Unaudited)

	May 1, 2021	July 25, 2020
ASSETS		
Current assets:		
Cash and cash equivalents	$ 7,350	$ 11,809
Investments	16,229	17,610
Accounts receivable, net of allowance for doubtful accounts of $110 at May 1, 2021 and $143 at July 25, 2020	4,425	5,472
Inventories	1,579	1,282
Financing receivables, net	4,648	5,051
Other current assets	2,829	2,349
Total current assets	37,060	43,573
Property and equipment, net	2,367	2,453
Financing receivables, net	5,068	5,714
Goodwill	37,690	33,806
Purchased intangible assets, net	3,716	1,576
Deferred tax assets	4,070	3,990
Other assets	3,925	3,741
TOTAL ASSETS	$ 93,896	$ 94,853
LIABILITIES AND EQUITY		
Current liabilities:		
Short-term debt	$ 2,000	$ 3,005
Accounts payable	2,440	2,218
Income taxes payable	753	839
Accrued compensation	3,327	3,122
Deferred revenue	11,492	11,406
Other current liabilities	4,250	4,741
Total current liabilities	24,262	25,331
Long-term debt	9,532	11,578
Income taxes payable	8,247	8,837
Deferred revenue	9,397	9,040
Other long-term liabilities	2,253	2,147
Total liabilities	53,691	56,933
Total equity	40,205	37,920
TOTAL LIABILITIES AND EQUITY	$ 93,896	$ 94,853

Paying down debt, making acquisition and investing the money into long-term bonds – so they might be planning for something bigger in the M&A field.

Cash flows from operating activities:		
Net income	$ 7,582	$ 8,578
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation, amortization, and other	1,373	1,364
Share-based compensation expense	1,337	1,170
Provision (benefit) for receivables	(4)	60
Deferred income taxes	(89)	103
(Gains) losses on divestitures, investments and other, net	(201)	(185)
Change in operating assets and liabilities, net of effects of acquisitions and divestitures:		
Accounts receivable	1,250	774
Inventories	(260)	143
Financing receivables	1,160	380
Other assets	(233)	145
Accounts payable	24	324
Income taxes, net	(828)	(700)
Accrued compensation	145	(220)
Deferred revenue	263	333
Other liabilities	(569)	(645)
Net cash provided by operating activities	10,950	11,624
Cash flows from investing activities:		
Purchases of investments	(7,855)	(6,880)
Proceeds from sales of investments	2,724	4,737
Proceeds from maturities of investments	6,445	5,708
Acquisitions, net of cash and cash equivalents acquired and divestitures	(6,333)	(237)
Purchases of investments in privately held companies	(138)	(143)
Return of investments in privately held companies	96	213
Acquisition of property and equipment	(530)	(562)
Proceeds from sales of property and equipment	14	175
Other	(56)	(10)
Net cash (used in) provided by investing activities	(5,633)	3,001
Cash flows from financing activities:		
Issuances of common stock	307	335
Repurchases of common stock - repurchase program	(2,096)	(2,659)
Shares repurchased for tax withholdings on vesting of restricted stock units	(419)	(519)
Short-term borrowings, original maturities of 90 days or less, net	—	(3,470)
Repayments of debt	(3,000)	(5,220)
Dividends paid	(4,601)	(4,491)
Other	39	(3)
Net cash used in financing activities	(9,770)	(16,027)

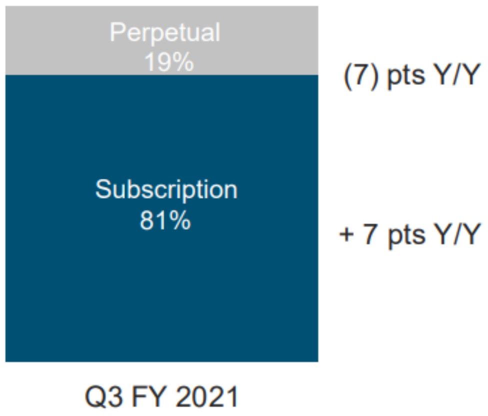
They are seeing early momentum in the key sectors there.

Q3 FY 2021 Highlights

- **Broad-based strength across business with product order growth of 10% y/y**
  - Return to growth y/y for Infrastructure Platforms, continued growth in WiFi6, Webscale, Security and Webex
  - Public Sector, Commercial, and Service Provider orders all growing double digits y/y, Enterprise continues to improve
- **Strong revenue growth of 7% y/y**
  - Extra week contributes ~3% of growth
- Seeing **early momentum** in the ramping of key technology cycles that are long-term growth drivers for our business such as **5G, 400G and edge**
- **Great progress on business model transformation**; achieved software revenue of $3.8B, +13% y/y, of which 81% is recurring
- **Double-digit growth y/y in Deferred Revenue and Remaining Performance Obligations (RPO)**
- Gross margin pressure driven by supply chain challenges

Subscription as a service is growing – which is the focus of the business now. But, Wall Street and tech people might be missing it as I get so many emails about Cisco and the old things they did.

Subscriptions as a % of Software Revenue



- Q3 software revenue of $3.8B, +13% y/y
- Annual run rate over $14B

Amounts may not sum and percentages may not recalculate due to rounding.

Source: [Presentation]

$2 billion per quarter in returns to shareholders equal to $8 billion per year.

Q3 FY 2021 Capital Allocation

Total Capital Allocation	
Share Repurchases ($M)	$510
Dividends Paid ($M)	1,560
Total ($M)	$2,070
Quarterly Dividends Per Share	$0.37
Share Repurchases	
Amount Purchased ($M)	$510
Number of Shares (M)	10
Avg. Price Per Share	$48.71

Approximately $8.7B remaining authorized funds in repurchase program as of the end of Q3 FY 2021.

Conference call notes

Turning to the quarter, we had impressive momentum in Q3, which gives me a great sense of optimism going forward. We returned to growth, with revenue up 7%, driven by an improving macro environment, the strongest product portfolio in our history and great execution by our teams. We saw broad-based demand across the business, led by our biggest growth opportunities: hybrid work, digital transformation, cloud and continued strong uptake of our subscription-based offerings. We are also seeing early momentum in the ramping of key technology cycles that are long-term growth drivers for our business, such as 5G, 400 gig and Edge.

Software

We continue to aggressively shift our business to more recurring revenue streams which we expect to grow over time as we expand our offerings. In Q3, we achieved $3.8 billion in software revenue, with 81% of our software revenue sold as a subscription, up from 76% last quarter. We also saw another quarter of double-digit growth in our deferred revenue and remaining performance obligations. Over the past six years, we have made significant progress and now have one of the largest software businesses in the industry with an annual run-rate well over $14 billion.

Acquisitions, buybacks and debt payment!

We ended Q3 with total cash, cash equivalents and investments of $23.6 billion, down $7 billion sequentially, driven by $5.5 billion in payments for acquisitions, as well as 3 billion in repayments of our long-term debt. From a capital allocation perspective, we returned $2.1 billion to shareholders during the quarter. It was comprised of $1.6 billion for our quarterly dividend and $510 million of share repurchases. Year-to-date, we returned $6.7 billion to shareholders, which represents 64% of our free cash flow, and we have $8.7 billion in capacity remaining under our current share repurchase program authorization.

Q&A

Margin inflation? Some inflation, segment, nothing to report!

Return to work planning? Economies coming back, first U.S., then likely other globally.

Acquisition impact on growth guidance? Not in guidance but 0.9%

Mostly margin, technology segment sales and supply chain issues questions.

Valuation update

If they keep returning $2 billion per quarter to shareholders, I can update a bit the valuation from $6 billion per year to $8 billion per year.

Cisco LINK

STOCK VALUE LIST'!A1

												Terminal Value	Growth rate	
Scenario 1	**Dividend in billions**	**2021**	**2022**	**2023**	**2024**	**2025**	**2026**	**2027**	**2028**	**2029**	**2030**	**2030**	6%	next 5 years
normal case	8.00	8.48	8.99	9.53	10.10	10.71	11.35	12.03	12.75	13.52	14.33	337.90	6%	5 to 10 years
in EUR	10%)	7.71	7.43	7.16	6.90	6.65	6.41	6.17	5.95	5.73	5.52	130.27	10%	Discount rate
	INTRINSIC VALUE	195.90											25.0	Terminal multiple

However, they should soon stop paying down debt as by the end of the year they could be done with that at the tempo they have now.

The current market cap is $223 and the stock is up from first purchase as planned. This is not really an absolute investment but more of a relative one. The stock will likely continue to go up all else equal and boom when they put the hammer down on buybacks. Plus, relatively the valuation is still below the market average, but that is just relative.