Q4 2021 Earnings Call

Company Participants

- Chuck Robbins, Chair and Chief Executive Officer
- Marilyn Mora, Head of Investor Relations
- R. Scott Herren, Executive Vice President and Chief Financial Officer

Other Participants

- Aaron Rakers, Analyst
- Benjamin J Bollin, Analyst
- Fahad Najam, Analyst
- Jeff Kvaal, Analyst
- Jim Suva, Analyst
- Meta Marshall, Analyst
- Paul J Silverstein, Analyst
- Rod Hall, Analyst
- Sami Badri, Analyst
- Samik Chatterjee, Analyst
- Simon Leopold, Analyst
- Tim Long, Analyst

Presentation

Operator

Welcome to Cisco's Fourth Quarter and Fiscal Year 2021 Financial Results Conference Call. At the request of Cisco, today's conference is being recorded. If you have any objections, you may disconnect.

Now I would like to introduce Marilyn Mora, Head of Investor Relations. Ma'am, you may begin.

Marilyn Mora {BIO 19771101 <GO>}

Thanks, Michelle. Welcome everyone to Cisco's fourth quarter fiscal 2021 quarterly earnings conference call. This is Marilyn Mora, Head of Investor Relations and I'm joined by Chuck Robbins our 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 made 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 made on a year-over-year basis.

The matters we will be discussing today include forward-looking statements, including the guidance we will be providing for the first quarter and full year of fiscal 2022. They are subject to the risks and uncertainties, including COVID-19, that we discuss in detail in our documents filed with the SEC, specifically the most recent reports 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.

With that, I'll now turn it over to Chuck.

Chuck Robbins {BIO 17845882 <GO>}

Thank you, Marilyn and good afternoon everyone. I hope you're all remaining healthy and staying safe. Our team at Cisco ended fiscal 2021 with an incredibly strong finish. We had an outstanding Q4 performance and fiscal year revenue reflecting strength across our portfolio, customer segments and geographies. Our product order growth was the highest we've seen in over a decade and we're continuing to see strong customer reception to the accelerated investments in software and subscriptions. This great momentum is reaffirming our position as the worldwide leader in technology that powers the internet and the digital enterprise.

As I think about our achievements over the past year, three things stand out to me. First, the exceptional execution of our teams. We achieved these results through the extraordinary efforts of our leadership team, our partners and most importantly, our people around the world, who operated with incredible speed and at an unprecedented scale to deliver this growth. Second, our transformation and strategic investments are paying off. The benefits of our shift to software and subscriptions are clear and they are helping both Cisco and our customers move with greater speed and agility. And third, the power of our portfolio. The groundbreaking innovation we are investing in today will serve as the foundation for our customers' futures.

These three factors position us exceptionally well for growth, as we enter our next fiscal year, as evidenced by our results this quarter. We are more confident than ever that we are in a strong position to help our customers be successful. As we look forward, we are laser-focused on providing our customers the technologies they will need to successfully navigate highly dynamic environments at an incredibly rapid pace. With the rise of COVID variants and the inconsistent piece of vaccine deployment around the globe, organizations must be resilient and adaptable as we've seen how quickly the world around us can change.

While this may impact certain short-term plans like return to office for many, one thing is clear, there is tremendous demand for Cisco's technology. No matter how or when the global recovery takes shape, we are executing on our vision of rebuilding a better world, one that is digital, sustainable, inclusive and highly secure. I believe we're at a pivotal moment in our Company's history, as we have a massive opportunity to transform what has been the traditional office and define the future of hybrid work. As our customers look to create safer hybrid workplaces, as well as collaborative and engaging experiences for their customers and employees, we believe they are becoming increasingly reliant on Cisco technologies to help them with their transformation and resiliency.

Enterprises are increasingly seeking digital and cloud-enabled services, which is driving demand for our solutions and leading to new and expansive market opportunities for Cisco. We are in a unique leadership position to build and deliver innovative cloud to edge infrastructure platforms that our customers need. With the depth and breadth of our hardware, software, silicon and optics solutions, we are helping companies solve their biggest challenges. Whether it's adopting modern application architectures, shifting to hybrid work and hybrid cloud, securing their enterprise or meeting their ESG goals, Cisco is helping our customers thrive in a hybrid world.

These industry dynamics helped drive our strong fourth quarter performance. The momentum we saw in Q3 accelerated through Q4 as we delivered robust revenue growth, increased earnings, strong margins and record operating cash flow. We also generated strong double-digit growth in product deferred revenue, reflecting the success of our transformation around driving subscriptions and recurring revenues, which increases our visibility into future performance.

We are seeing IT budgets grow as companies begin to implement their critical future plans and business confidence increases. However, we do recognize that uncertainty remains around COVID-19 and we are closely monitoring the delta variant and its impact on customer spending. Right now, we are not seeing any additional impact to our business, aside from the components shortage we've been facing over the past several months.

Moving to the performance of our customer segments. As I mentioned, we delivered the highest product order growth in over a decade, with growth of 31% driven by strength across all of our end markets. This outstanding performance is also up over 17% from our pre-COVID Q4 levels in fiscal year 2019. We saw double-digit growth in every one of our customer segments. This strength is being driven by stronger customer investment in substantial network upgrades to help modernize and secure their environments to support the new way of working.

Specifically in our enterprise business, we had the best quarter in terms of product orders in over a decade and saw very strong order growth of 25%. We also had our third consecutive quarter of acceleration in our commercial, service provider and public sector businesses, with all of these segments showing growth in excess of 20%.

In our webscale business, we saw increased momentum, delivering record performance with over 160% order growth and on a trailing four quarter basis, orders grew over 80% due to customers adopting products across the portfolio and early traction of our 400-gig solutions, a huge testament to the investments we have made in accelerating innovation and the differentiated value we're bringing to these customers.

From a product portfolio perspective, we also had a very balanced performance. As customers prepare for office reopenings and hybrid work, they are increasing their investment across our networking, cloud security and unified communications portfolios. In Q4, we saw double-digit revenue growth in campus switching, Catalyst 9000, high-end routing, wireless and in our Zero Trust solutions, along with strength in our security endpoint portfolio.

We also had very strong adoption of our Acacia optical solutions, driven by increasing customer demand for leading-edge technology to address their growing bandwidth requirements. The transformation of our business to more software and subscriptions continues to show tremendous progress, as we achieved over $4 billion in software revenue in Q4, an increase of 7% sequentially and up 6% year-over-year. Within that, subscription revenue grew 9% in Q4 and 15% for the full fiscal year.

For perspective, software represented 31% of our business in Q4 and for the full year, when combined with our services business, they represent over 53% of revenue, clearly highlighting the success of our continued business transformation. In addition to delivering strong financial results, our innovation engine continues to accelerate. Over the last year, we introduced an impressive number of new capabilities across our entire portfolio, while also doubling down on more flexible consumption models, including our core networking capabilities as-a-service, highlighted by the recent launch of Cisco Plus.

Our new Cisco Plus solutions deliver cross portfolio technologies to help solve our customers' biggest needs, with faster time to value. Our initial network-as-a-service offerings deliver hybrid cloud technologies and will later expand to a broader catalog of services built and delivered with our partner ecosystem. Cisco Plus improved speed, agility and scale with on-demand solutions that intelligently adapt to our customers' business needs. While still early days in its launch, Cisco Plus directly aligns with our transformation goals around driving more subscription-based recurring revenue via the cloud.

Our unique strengths and proven strategy give us the confidence to move at a more accelerated pace. You will see us continue to invest in our key growth areas in technology shifts like hybrid cloud, hybrid work, 5G, Wi-Fi 6, edge, security and cloud native architectures to extend our technology leadership positions. You will also see us deliver even more strategic offers to enable our customers to thrive in a cloud-first digital world. These include full stack observability to improve their digital experiences by providing visibility and insights across their entire technology stack and Secure Access Services

Edge or SASE designed to enable seamless secure access to applications anywhere their users work.

Given the momentum we're seeing in our business, we have more conviction than ever that we are investing in the right areas and we'll continue to extend our competitive advantages and drive growth. Before I turn it over to Scott for more details on the quarter and our expectations for the next fiscal year, let me give you an update on the supply environment. While we are seeing increasing demand for our technology, we are also continuing to manage through the component shortage challenges that nearly every company is experiencing. Our world-class supply chain team as always, is doing an incredible job navigating this complex situation by working with our global suppliers to meet customer demand as quickly as possible. Looking ahead, we expect the supply challenges and cost impacts to continue through at least the first half of our fiscal year and potentially into the second half.

In summary, demand for our technology is very strong and our strategy is more relevant than ever. This allows us to deliver greater value to our customers, partners and communities, as we all adapt to new ways of living and working. I'm very encouraged by the recovery trajectory across the Board and with our momentum. I am confident in our strategy and investments. I feel great about the innovation we are driving in our portfolio and I'm incredibly proud of what our teams and partners have achieved. I look forward to building on these insights with a more comprehensive deep-dive on our multi-year vision and strategic growth drivers at our virtual Investor Day on September 15th and I hope you'll join us. Thank you again for your time.

And with that, I'll turn it over to Scott for additional detail.

R. Scott Herren {BIO 18902845 <GO>}

Thanks, Chuck. Our fourth quarter reflects a strong close to our fiscal year with significant momentum across our business. We saw a robust customer demand, demonstrating the third consecutive increase in product order growth and solid execution by our teams. I'll provide some detail on our financial results for the quarter, then cover the full fiscal year, followed by our guidance.

Q4 was a very strong quarter and a very dynamic environment. We executed exceptionally well with greater than 30% product order growth year-on-year, and more than 17% order growth versus our pre-COVID Q4 fiscal '19 product bookings, driven by strength across our portfolio. In fact, it was the strongest product order growth rate in over a decade. We also had strong results across revenue, net income, earnings per share and as Chuck said earlier, record operating cash flows.

Total revenue increased to $13.1 billion, up 8% year-over-year, coming in at the high end of our guidance range for the quarter. We saw strength in a number of product areas and across all geographies. Our business continue to recover well and build momentum with sequential revenue growth of 3%. Our non-GAAP operating margin was 33.5% up 50 basis points. Non-GAAP net income was $3.6 billion and non-GAAP earnings per share was $0.84, both up 5% year-over-year and exceeding the high end of our guidance range.

Now let me turn to provide more detail on our Q4 revenue. Total product revenue was $9.7 billion, up 10%, service revenue was $3.4 billion, up 3%. Infrastructure Platforms performed very well with revenues up 13%. All businesses saw double-digit growth with the exception of data center. Switching had strong growth driven by double-digit increase in campus switching, led by our Catalyst 9K and Meraki switching offerings. We also had solid growth in our data center switching portfolio with the Nexus 9K products.

Routing grew driven by both the service provider and enterprise markets, as we saw strong adoption across our portfolio including robust uptake of our Cisco 8000 platform. Wireless had strong growth, driven by the continued ramp of our Wi-Fi 6 products and our Meraki wireless offerings. Data center revenue declined driven primarily by servers, as we experienced continued market contraction. Applications were down 1% driven by a slight decline in our collaboration portfolio. However recurring subscription revenue within our Webex suite grew 9% in Q4.

We also saw solid growth in IoT software, AppDynamics, cloud contact center and our cloud calling platforms. Security was up 1%. Our cloud security and Zero Trust portfolios performed well with greater than 20% growth, as we had continued momentum in our Duo and Umbrella offerings. Our security recurring subscription revenue grew 13% in Q4 and 18% for the full fiscal year. In both applications and security, we are seeing strong revenue growth in the strategic areas that we and our customers are investing in. We continue to transform our business, delivering more software offerings and driving growth in subscriptions and recurring revenue.

Software revenue was $4 billion, an increase of 6%. Subscriptions were 81% of total software revenue, up 3 points year-over-year. Software subscription revenue grew 9% in Q4 and 15% for the full fiscal year. As we continue to increase our software subscriptions, we're driving higher levels of recurring revenue. Additionally, the strength of our portfolio and transition to more software and services, is driving growth in remaining performance obligations or RPO. At the end of Q4, RPO crossed the $30 billion mark at $30.9 billion, up 9%. RPO for product was up 18% and service was up 3%. Approximately 53% of the total RPO is short-term, meaning it will be recognized as revenue in the next 12 months.

As I mentioned, we had exceptionally strong order momentum in Q4, as total product orders were up 31%, with strength across the business. Looking at our geographies, the Americas was up 34%, EMEA was up 24% and APJC was up 29%. Total emerging markets were up 25%, with the BRICS plus Mexico up 37%. In our customer segments, commercial was up 41%, service provider was up 40%. The enterprise returned to growth and was up 25%, while public sector was up 22%.

Non-GAAP total gross margins came in at 65.6%, up 60 basis points year-over-year. Product gross margin was 65%, up 180 basis points and services gross margin was 67.4%, down 240 basis points, which was in line with our expectations, as we do see variability from quarter to quarter. The increase in product gross margin was driven by productivity improvements from lower freight and other costs, partially offset by relatively modest price erosion.

As we discussed last quarter, we continue to manage through the supply chain constraints seen industry-wide due to component shortages. We've closely partnered with our key suppliers, leveraging our volume purchasing and extended supply commitments, as we address the supply challenges and cost impacts, which we expect will continue at least through the first half of our fiscal year and potentially into the second half. Our number one ranked global supply chain team continues to perform at a world-class level.

When you look at the impact of acquisitions on our Q4 results year-over-year, there was a positive 210 basis point impact on revenue and no material impact on our non-GAAP earnings per share. From a cash perspective, operating cash flow for the quarter was a record $4.5 billion, up 18% year-over-year, driven by strong cash collections. We ended Q4 with total cash, cash equivalents and investments of $24.5 billion, up approximately $900 million sequentially. In terms of capital allocation, we returned $2.4 billion to shareholders during the quarter, that was comprised of $1.6 billion for our quarterly cash dividend and $791 million of share repurchases.

We continue to invest organically and inorganically in our innovation pipeline. During Q4, we closed five acquisitions, Kenna Security, Socio Labs, Slido, Sedona Systems and Involvio. These investments are consistent with our strategy of complementing our internal innovation and R&D, with targeted M&A to allow us to further strengthen and differentiate our market position in our key growth areas.

Turning to the full fiscal year results. Overall, our financial results were solid in a very challenging global pandemic environment, with strong operational execution. Revenue was $49.8 billion, up 1%, total non-GAAP gross margin was 66.1%, up 10 basis points and our non-GAAP operating margin was 33.5%, down 30 basis points. From a bottom line perspective, our non-GAAP net income was flat at $13.6 billion and non-GAAP earnings per share was $3.22. We delivered operating cash flow of $15.5 billion, flat compared to fiscal '20. From a cap allocation perspective, we returned $9.1 billion in value to shareholders over the fiscal year, which represents 61% of our free cash flow. That was comprised of $6.2 billion in quarterly cash dividends and $2.9 billion of share repurchases.

We also increased our dividend for the 10th consecutive year in fiscal 2021, reinforcing our commitment to return capital to our shareholders and our confidence in the strength and stability of our ongoing cash flows. We remain firmly committed to maintaining a strong balance sheet to fuel our organic and inorganic growth initiatives, as well as continuing our cap allocation strategy of returning a minimum of 50% of our free cash flow to shareholders annually.

To summarize, we had a great Q4 and a solid fiscal year, with strong operational execution. We're seeing returns on the investments we're making in innovation and driving the continued shift to more software and subscriptions, driving more recurring revenue, delivering growth and driving shareholder value.

Now let me provide our forward-looking guidance. We are pleased to initiate the additional practice of providing an annual outlook to complement our regular quarterly look-ahead for fiscal year 2022. As successful transformation we've been executing around driving a higher proportion of our revenues from subscriptions, recurring and deferred revenue is affording us additional visibility into our outlook for future growth. Please note, our guidance is subject to the disclaimer regarding forward-looking information that Marilyn referred to earlier.

Our financial guidance for Q1 is as follows. We expect revenue growth to be in the range of 7.5% to 9.5% year-on-year. We anticipate the non-GAAP gross margin to be in the range of 63.5% to 64.5%, reflecting the continuing increase in supply chain costs we are incurring, as we protect shipments to our customers. Our non-GAAP operating margin is expected to be in the range of 31.5% to 32.5%. Non-GAAP earnings per share is expected to range from $0.79 to $0.81.

Our financial guidance for the full year fiscal '22 is as follows. We expect revenue growth to be in the range of 5% to 7% year-on-year. Non-GAAP earnings per share is expected to range from $3.38 to $3.45, also up 5% to 7% year-on-year. In both our Q1 and full-year outlook, we are assuming a non-GAAP effective tax rate of 19%. Looking ahead, we're excited to host a Cisco virtual Investor Day on Wednesday, September 15th, 2021, which we will webcast live and hope you can join us.

I'll now turn it back to Marilyn, so we can move into the Q&A.

Marilyn Mora {BIO 19771101 <GO>}

Thanks, Scott. Michelle, let's go ahead and queue up the Q&A line.

Questions And Answers

Operator

Thank you. Samik Chatterjee from J.P. Morgan. You may go ahead

Q - Samik Chatterjee {BIO 15496543 <GO>}

Hi, thanks for taking my question. I guess, Chuck, Scott, just wanted to get your thoughts on getting in terms of the timing of getting a full-year guide out here. I would think most other companies would have said, this is with the supply chain uncertainty, this is probably not the right time to get a full year guide out. So, definitely appreciate the full year guide and I wanted to understand what's providing that higher visibility. You mentioned the transformation. But also, how are the orders feeding into that visibility and what are you kind of baking in, in terms of supply chain in that full year guide overall, how much of -- what are you baking in terms of headwinds into that full year guide from a supply chain perspective? Thank you.

A - R. Scott Herren {BIO 18902845 <GO>}

Yes. It's a great question, Samik. Thanks for that. It really is one of the benefits of the transformation we are making. As we move to more and more of a software and services and recurring revenue base, we have greater visibility. One of the stats that we just talked about is our remaining performance obligations of $30.9 billion, of which 53% of that will turn into revenue in the next 12 months. We also have a good feel for what other renewals are going to come up and what our renewal rate is, as we work our way through this. So we have a pretty good sense of a big chunk of our revenue and how it's going to grow. We also have a good view of our pipeline and what that looks like ahead and one of the things that I would say about that pipeline is, it's one of the -- its -- we've seen year-on-year growth in the pipeline for Q1, better than we've ever seen in the last several years. So if, we see good growth in the pipeline as well.

So it's when you add all that up, that's what gives us the confidence to give a full year guide. What I would say is the -- to your question about supply chain and what's the assumption on supply chain. The way to think about that is, that's the difference between the high end and the low end of the guide. We expect the supply chain to impact us through the first half of the year and then at the low end of the guide, we think we continue to have supply chain impacts through most of the second half as well, with some clear up at the end. At the high end of the guide, we think that we begin to clear up the supply chain issues, supply and demand comes back more into balance earlier in the second half.

So that's the -- that's why we gave the full year guide. I think it -- certainly we have the confidence with the visibility we have and what's baked into that, based on some of the uncertainties still out there with the supply chain.

Q - Samik Chatterjee {BIO 15496543 <GO>}

Great. Thank you.

A - Marilyn Mora {BIO 19771101 <GO>}

Thanks, Samik. We'll take the next question please.

Operator

Meta Marshall from Morgan Stanley Investment Research. You may go ahead.

Q - Meta Marshall {BIO 18728692 <GO>}

Great, thanks. Maybe coupling onto that question, just how should we think about kind of the incremental 150 basis point sequential gross margin decline in the guidance? And just how much of that is incremental supply chain impact and would you expect to abate that through either price changes or supply chain improvement to improve that throughout the year? Thanks.

A - R. Scott Herren {BIO 18902845 <GO>}

Yes, thanks Meta for that. What we -- when you look at the Q4, gross margin obviously came in better than what we had expected and what we had guided to. And there was really favorable product mix built into that, some of that being driven by a good quarter for software as you heard on the call earlier. Looking ahead, we've taken several steps to ensure that we can continue to have supply and deliver products to our customers. They're in the midst of their own transformations. They're all in the midst of doing the things they have to do, to adapt to a world that's not only a hybrid work world, but one with the rise of the delta variant that, it's added complexity. It's not a -- the world is going to go back to normal at some point, it's, I need to continue to have this kind of flexibility ahead.

We're trying to support that and at the same time, there is supply and demand imbalances in some of the key components around semiconductors and memory and some of the same things you hear from others of our peers. That turns into higher component costs as we buy from those suppliers. We are also to ensure even greater supply going to brokers to get additional supply versus what we can get directly from our suppliers. And in some cases qualifying second sources, where we have to. Each of those obviously drives cost and it takes a while for those costs -- we've been in that process through Q4 and will be in it through Q1. It takes a while for those cost to flow through our standard costing system and show up in the cost of goods sold.

There's a little bit of unfavorable product mix headwind as well in Q1, as we have a good sense of the products that don't have those same impacts that we will be able to ship that are sitting in backlog. So that's what's driving that sequential change. As you know, we did put in place a price increase, very selective, very targeted, only on the products where we were seeing the higher component costs. That went into effect August 7th, but we always honor quotes that are out there for 30 days, beyond that price, because many of those quotes were produced before the price increase was put in.

So, scroll 30 days ahead from August 7th before the first orders come in with those higher prices and then it takes a while for those orders to come in, get built and shipped back out to customers and for us to realize the benefit of that on the top line. So think of those price increases as being something that we'll feel more of the benefit of in Q2 and Q3 versus what we see in Q1.

Q - Meta Marshall {BIO 18728692 <GO>}

Great. Thanks.

A - Marilyn Mora {BIO 19771101 <GO>}

Thank you. Next question please.

Operator

Paul Silverstein from Cowen. You may go ahead

Q - Paul J Silverstein {BIO 1812254 <GO>}

I appreciate Scott's pick up on the previous two questions. If I looked at your annual guidance, its strong revenue, it's almost a $1 billion above the consensus number, the EPS is more in line. Its slightly like, but not meaningful. But the difference obviously is gross margin and your OpEx. I appreciate that COVID's elevated your cost structure as well as all of your peers. Can you give us any granular insight in terms of translating the revenue upside that you're looking at that, that you're expecting relative to the more modest EPS outlook for the year, in terms of gross margin versus OpEx?

A - R. Scott Herren {BIO 18902845 <GO>}

Yeah, Paul, it really is gross margin driven and there is still -- there continues to be uncertainty and when the supply and demand gets back into balance on many of those components, that's why you see the range that we put out there at 5% to 7%, and that ripples through to the bottom line as well. I think that the only other comment I'd add on that front, I don't want to get into parsing it down to the various elements at least at this point, but there is still uncertainty and given that uncertainty and this being the first time we've given you annual guide, it's prudent. We're trying to be prudent with the guide we put out there as well.

Q - Paul J Silverstein {BIO 1812254 <GO>}

Yes. With respect to OpEx, is it your plan to grow OpEx more modestly than revenue? You're going to -- you're looking at some pretty healthy revenue growth this year. Will you restrain your OpEx growth below revenue to try to drive some leverage?

A - R. Scott Herren {BIO 18902845 <GO>}

Yes. I'll start and Chuck, you may want to add on to this. The way that you see the guidance laid out 5% to 7% growth on the top line and 5% to 7% growth on the bottom line. We're looking at balanced profitable growth and I think that's the way you should expect us to run the business going forward, is balanced profitable growth. 5% to 7% on both the top and bottom line is a pretty strong performance, certainly relative to where we've been over the last few years. And so again, I don't want to get into, Paul, I know what you're poking at. I really don't want to get into parsing down the elements of that, but the core principle is balanced profitable growth.

A - Chuck Robbins {BIO 17845882 <GO>}

You know Paul, (multiple speakers). Go ahead Paul. Go ahead.

Q - Paul J Silverstein {BIO 1812254 <GO>}

Just one last question on this, is there any reason why your cost structure from a gross margin perspective -- we envision going back to the 21st century and getting beyond COVID. Is there any reason why your gross margin structure will not go back to where it was, if not better? I recognize, you've got mix and other factors that influence one way or the other from quarter to quarter, but as a general proposition, should we expect your gross margin structure return to what it was pre-COVID?

A - Chuck Robbins {BIO 17845882 <GO>}

That is our expectation, Paul over time. I mean again I don't want to predict that for this fiscal year, just given some of the uncertainties in the supply chain. But it is our expectation that it gets back there and over the longer term as we continue to build a bigger mix of software into our revenue stream, that should also provide a bit of a tailwind to our margins.

Q - Paul J Silverstein {BIO 1812254 <GO>}

I appreciate it.

A - Marilyn Mora {BIO 19771101 <GO>}

Thanks, Paul. Michelle, next question.

Operator

Aaron Rakers from Wells Fargo. You may go ahead.

Q - Aaron Rakers {BIO 6649630 <GO>}

Yes. Thanks for taking the question and congrats on the good quarter. I wanted to kind of ask the supply chain question a little bit differently. As you see the order momentum in the pipeline build commentary that you laid out, obviously is quite positive, how are you assessing kind of the perishability of demand? Are you seeing any signs where customers might be double ordering or how do you just think about that in the function of the guidance that you've laid out?

A - Chuck Robbins {BIO 17845882 <GO>}

Yes. Aaron, this is Chuck. Thank you for that. Look, we expected to be asked about pull ahead. I think there's a couple of things that I would say, we obviously can't calculate that directly, we've looked at several indicators. Our pipeline analysis, channel orderings, our sales force opportunity movement, order cancellation rates, future pipeline build and we don't see any signs of ordering well ahead of needs, other than lining up with what our lead times are. And we have customers at large carriers, large telcos, cloud players, who have 12 to 18 to 24-month capacity plans, and so they look at our lead times and they are going to order into that, based on what they have. But we would not say there was a significant amount of pull ahead, other than dealing with the lead times.

And the other thing that I would just highlight is, it -- Scott pointed out earlier, after the real strong order growth we saw in Q4, we're sitting with the best start from a forecast pipeline perspective that we've had in several years. So that would lead us to believe that this is a trend that we should see continue for a little while.

Q - Aaron Rakers {BIO 6649630 <GO>}

Great. Thank you.

A - Marilyn Mora {BIO 19771101 <GO>}

Alright, great. Next question please.

Operator

Thank you. Tim Long from Barclays. You may go ahead.

Q - Tim Long {BIO 21123922 <GO>}

Thank you. Could you just dig into the software and go a little bit, numbers seem pretty strong, yet the applications and security lines trailed a little bit on the product side. So, could you just parse that through for us?

And then second, just did want to follow up on that cloud piece that was so strong in the quarter. Chuck, any other color you can give that -- on that? It sounded pretty broad-based, but I'm assuming some of your peers also, to the last question, saw a little bit more advanced, more longer lead-time orders or is there anything else in that huge cloud number? Thank you.

A - Chuck Robbins {BIO 17845882 <GO>}

Yes. Thanks, Tim. So, on the applications front, we expected that you guys might want to ask about that, and there's a couple of things to keep in mind in both applications and security. The order rates were certainly higher than the revenue rates. So that's the first thing I would tell you. The recurring subscription portions within each of those businesses were also very positive. As Scott said, in security within web -- I mean in the collaboration within applications, Webex suite, the recurring subscriptions within Webex suite revenue was up 9% in Q4, 16% for the year. We had solid growth in IoT, FD, cloud contact center and cloud calling. What's also in there, if you will recall is, there is phones and handsets and there is some on-prem software that's associated with collaboration and some of those were impacted by supply chain. But the future growth area is actually for us, looked really good.

On the security front, cloud security Zero Trust over 20%. The security recurring subscription revenue up 13% in Q4, up 18% for the year. So that was solid as well. And again, our next generation firewall demand was really good, but some of the legacy products and the supply chain created a little bit of a revenue headwind there. But again, orders were stronger than the revenues. We would expect those to normalize over the next few quarters.

As we get to webscale, this is a -- I have to tell you that, preparing for this call, I reflected over the last five six years of having this discussion and I always said that we would start talking about webscale when it was meaningful and I guess I can now declare it meaningful. We made multi-year investments building the Cisco 8000 with new silicon, the optics and the software and we had phenomenal growth and it was 160% order growth this quarter over almost 30% order growth a year ago in the same quarter. And the customers are really adopting our entire portfolio, including the enterprise side. But over half of that business landed in their cloud infrastructure. We also see 400-gig taking off in the -- really in a meaningful way. I'll give you a couple of stats on that, because someone is probably going to ask it.

In Q4, 400-gig ports, our orders were up 668% and for the year, 400-gig port orders were up 831%. We have over 400 customers that have deployed and we've taken orders for almost 180,000 ports total. So it's really moving forward. And I think those are the things that -- and we won several franchises in the cloud webscale space. We continue to do proof of concepts. We're in validation and certification stages in others. So we always said that we missed the first transition with these players and that we wanted to be prepared for this next architectural transition and I think our teams have done a great job, putting us in a good position.

Q - Tim Long {BIO 21123922 <GO>}

Okay. Thank you very much for the color.

A - Marilyn Mora {BIO 19771101 <GO>}

Thanks, Tim. Next question.

Operator

Thank you. Rod Hall from Goldman Sachs. You may go ahead, sir.

Q - Rod Hall {BIO 20453923 <GO>}

Great. Thanks for the question. A lot of port, Chuck, lot of port. So, I had two questions for you. One is regarding the order growth. I'm curious about linearity there, that the last time we thought three handle on that was back in 2010 when you guys were exiting the GST, but it seems like those orders could accelerate from here, and I'm curious whether you think that's a possibility or how probable an acceleration is from that 31% growth rate?

And then I wanted to come back to this pricing commentary and I'm curious, what the durability of these prices is, what your intention would be once these component cost, these underlying costs go down, will you flex these prices right back down again? Or do you expect them to sustain themselves a little bit longer? Just curious what your plan on pricing would be as these underlying cost change. Thanks.

A - Chuck Robbins {BIO 17845882 <GO>}

Yes. Let me start and I'll let Scott comment on the pricing issue as well. You asked a couple of questions there, Rod. On linearity, just to give you the quarter, it started hot and ended hot, right. It was from day one to the end. So this was not like we were 5% growth till last month and then it accelerated, it was pretty consistent throughout the entire quarter.

You mentioned the ability to accelerate. I certainly wouldn't expect 31% order growth to be the new standard. But, I think that there are certainly going to be -- it just feels like our customers are dealing with -- they're coming out, they're making decisions about modernizing their infrastructure and their technology assets to deal with this new hybrid work and I think now, what they're seeing is, that with the delta variant, they are understanding that this may not be a one -- this may not be one move back to the office, right. This is -- they're going to have to be resilient. They're going to have to build adaptability in for future, because we could have the next variant six months from now and I think that's what customers are thinking through right now.

The comment I'd make on pricing, and then I'll let Scott talk about the durability of them is, one thing that, as we talk about gross margin in the quarter we just finished, the pricing element of gross margin was actually at the very low end of our normal range, which means we're holding pricing with our sales teams, which is a good sign, right now. So once these things start flowing through, if that trend (technical difficulty) cost increases we are seeing. Now, there is a lag effect, right. It's going to take time before we see those prices show up actually in our revenue stream, but they're really motivated by that. And so, we'll continue to assess as we always do, if we need to make another price adjustment up or down, we'll continue to make those assessments going forward.

So it's -- don't think about them as being motivated though by top line drivers, it's really motivated by offsetting some of the higher cost that we're seeing. So the other thing I would just close on this one is it -- we have a price increase methodology that we deploy on a regular basis for different portfolios. We just don't talk about on earnings calls every time, but we -- so this is a muscle we have, that we actually use on a fairly regular basis when the conditions warrant it.

Q - Rod Hall {BIO 20453923 <GO>}

Okay. Great. Thank you.

A - Marilyn Mora {BIO 19771101 <GO>}

Next question please.

Operator

Thank you. Sami Badri from Credit Suisse. You may go ahead

Q - Sami Badri {BIO 20178177 <GO>}

Thank you. My first question is on your gross margins and just the costs of products and the question really is just around, how much of these cost inputs can Cisco control versus how many of them are not controllable at all, right? So that's kind of the first question.

And then the second question is, going back to some of your wins with the Series 8000, how much of these wins are completely new deployments versus you going head-to-head with an incumbent or going head-to-head with other competing vendors for those deployments, right or existing replacement on new deployments and that would be great. Thank you.

A - R. Scott Herren {BIO 18902845 <GO>}

Sure, Sami. I'll start on the cost of goods sold. It's overwhelmingly driven by the component costs and the contract manufacturing cost to do the various levels of assembly inside there versus something that we have the ability to the flex up or down. So I would think of that as being significantly driven by some of the factors that we've talked about, with the imbalance of supply and demand.

A - Chuck Robbins {BIO 17845882 <GO>}

And Sami, on your second question, it's really difficult to say which ones are new, which ones that we compete with an incumbent. But I will tell you we're in -- we're competing with incumbents on every one of them. Because I mean, even if it's a new architecture they're building, they have incumbents who are certainly competing with us. These are all super competitive and our teams have built some great technology and so it's -- and the cloud providers, they like diversity in their supply chain, they like diversity from a supplier perspective. And one other data point I meant to give earlier when Tim asked about the cloud business that we gave on the call last time, I want to make sure we share with you again. Webscale comprised 30% of our service provider segment from an orders perspective for the quarter.

Q - Sami Badri {BIO 20178177 <GO>}

Got it. Thank you.

A - Marilyn Mora {BIO 19771101 <GO>}

Thanks, Chuck. Next question.

Operator

Simon Leopold from Raymond James. You may go ahead, sir.

Q - Simon Leopold {BIO 4081594 <GO>}

Thank you very much for taking the question. I think you sort of alluded to 31% order growth not being sustainable. Can you give us some idea of what you see as really the sustainable or more normalized level? And also if you could comment on your purchase order commitments, because I would assume that the substantial commitments you've made help you lock-in and secure pricing, when you made those commitments and represents, I guess a way of controlling the headwind as we think about the full-year model. I want to make sure I'm understanding that correctly. Thank you.

A - R. Scott Herren {BIO 18902845 <GO>}

I'll start on the second part of that and then I'll let Chuck weigh in on the order growth. We -- clearly as we locked in some of that -- some of the work that we did on supply and particularly going after components that are particularly at an imbalance between supply and demand, we locked in both, right. We looked at both the cost that would come in for that and what the committed delivery schedule was on those. So we have a good sense of that for a subset of our components.

There is still going to be fluctuation in some areas. Memory is a good example, where there is going to continue to be fluctuation in pricing and we'll continue to monitor that.

You saw us -- you've seen us in the past, make price adjustments based on memory cost increases. And I would expect that to be kind of an ongoing process there. But for the ones that we locked in, which we're the, I think the ones that are -- that have the greatest imbalance and are in the highest demand, both for us and for our competitors, we locked in both from that standpoint.

A - Chuck Robbins {BIO 17845882 <GO>}

Yes. And on the order side, that's a difficult question to answer. What I would say is that, this is the first time we've given long range guidance or annual guidance on both revenue and EPS. We have the Investor Day coming up on the 15th, where we're going to talk about the key growth drivers in our business and we're also going to begin to share new metrics that will give you a flavor of the business in a different way. So, I think that's what -- as we spend time on that day, I think the drivers of growth will be clear to you and I think the bookings will only be one metric that we'll look at relative to the future performance.

Q - Simon Leopold {BIO 4081594 <GO>}

Thank you.

A - Marilyn Mora {BIO 19771101 <GO>}

Next question please.

Operator

Fahad Najam from MKM Partners. You may go ahead, sir.

Q - Fahad Najam {BIO 18889220 <GO>}

Thank you very much for taking my question. In terms of the order strength, do you have any way of parsing out any kind of double ordering or forward pull in orders from your customers? And have you adjusted for that? And I have a follow-up.

A - Chuck Robbins {BIO 17845882 <GO>}

Fahad as I said earlier, what we've looked at is, we've compared a lot of the -- our pipeline pull ahead activity, we've looked at our future pipeline, we've looked at order cancellation rates and we just don't see anything. So based on what we know now, we certainly think customers are placing orders further in advance because of lead times, which is just logical. But that's basically when you see the order growth we saw in Q4 and then you see the forecast pipeline that we see going forward, it would suggest that there is still a fair amount of demand out there.

A - R. Scott Herren {BIO 18902845 <GO>}

Fahad we're staying on top of that as much as possible. As you can imagine and Chuck talked earlier about some of the data points we're looking at to try to get a feel for it. Order cancellations would be one indication of double ordering from us and another party, that's order cancellation rates have actually come down modestly, return rates, looking at the pipeline and the pipeline growth. So we're not seeing it at any material level. I think the other thing -- the other data point we gave, is the growth of commercial. So if you look at the orders, the overall order growth, commercial was up 41% and I think where you might expect to see some of what you're talking about is actually in the enterprise segment or in SP. And we saw significant growth in commercial and I don't think you'd expect to see as much of that kind of a double ordering process happen in that customer size.

Q - Fahad Najam {BIO 18889220 <GO>}

I appreciate that. Chuck, if I could ask you a big picture question. Before COVID-19 happened, I think you had mentioned that for the first time virtually every product line in Cisco's family of products had been repriced. To the extent, how much of the strength you have seen is a function of product refresh cycle that is taking place across all your product lines versus total new growth? For example like edge cloud, which I think is going to be a total new network growth architecture that's never been deployed before. So, it's kind of like the new phase of growth. So how much of the strength you're seeing is a function of this refresh versus and the new phase of growth in your end business?

A - Chuck Robbins {BIO 17845882 <GO>}

What I would say is, there are several transformations that are occurring or transitions that are occurring across our customer base that we're just well positioned for. I mean if you think about what's happened with 5G and Wi-Fi 6, this whole move now to hybrid work, the whole re-architecting of infrastructure to support hybrid cloud, this 400-gig transition that we spoke about earlier, I mean these are all things that we have been working on our portfolio. So I think the refreshed portfolio and the new innovation that has been brought forward is just timely, because we're on the front end of some of these big transitions that we've been talking about for several years.

So I think that's really what's driving it. The teams have -- at the Investor and Analyst Day on the 15th of September, we're going to have our engineering leaders talking about what all they've done and what the future looks like and what the innovation pipeline looks like and I feel really good about what they've built. But we have a lot of plans for new technology and new capabilities.

Q - Fahad Najam {BIO 18889220 <GO>}

I appreciate the answer. Thank you.

A - Marilyn Mora {BIO 19771101 <GO>}

Thank you. Next question please.

Operator

James Suva from Citigroup Global Markets. You may go ahead, sir.

Q - Jim Suva {BIO 6329522 <GO>}

Thanks very much. Its Jim Suva. I had one question. The long-term full year outlook, product sales and EPS is greatly appreciated. And I noticed that's a big difference and shows a lot of conviction. But on the EPS, normally you also have some stock buyback going in, but some companies include stock buyback in the EPS guide, some don't. So what I'm wondering is, on your EPS guide, does it include some normal stock buyback? I know this year was different when you bought Acacia for about $4.5 billion and COVID in such, but I was kind of wondering about how we should think about that EPS, does it include stock buyback or what are the components of the EPS growth that match sales?

A - Chuck Robbins {BIO 17845882 <GO>}

That's a great question, Jim. It only assumes that we -- our share buybacks offset dilution. So think of that as you do in your own modeling, think of the share count to be roughly flat to where it ends this year.

Q - Jim Suva {BIO 6329522 <GO>}

Got you. Thank you so much for the clarification. It's great to hear all the details.

A - Chuck Robbins {BIO 17845882 <GO>}

Thanks, Jim.

A - Marilyn Mora {BIO 19771101 <GO>}

Thanks, Jim. Next question.

Operator

Jeff Kvaal from Wolfe Research. You may go ahead.

Q - Jeff Kvaal {BIO 3233206 <GO>}

Thanks very much. I am hoping to get a little bit of clarification into the software growth trajectory. It sounds like it was a great year overall and the fourth quarter maybe didn't close as well as you'd like and if we could talk about, what's the trajectory we should expect for software growth in 2022, that would be splendid.

A - Chuck Robbins {BIO 17845882 <GO>}

I'll start with some color and then Scott, you can chime in. I think, look, we continue to add more software capabilities across the portfolio. We continue to transition -- we've transitioned a lot of our portfolio to subscription based even for the hardware side of the business. Most of the acquisitions that we do come in as subscription or SaaS software businesses. So we would expect to continue just this move towards it becoming a greater percentage of our portfolio. And in the next couple of years, we think we also will see some of the renewal volume will start kicking in on top of it as well, but it's already -- the transformation has already made a big difference.

Scott and I were looking at last quarter when we did guidance for Q4, having the software revenue that came off the balance sheet, significantly altered positively what we were able to guide from a revenue perspective in Q4 versus what we would have done five or six years ago. I mean it was meaningful. And so we're going to continue to invest in this capability. We're going to continue to drive software. It's a huge important part of the business. Teams have done a great job.

Scott?

A - R. Scott Herren {BIO 18902845 <GO>}

Yes. Jeff, what I'd say is at $4 billion of software revenue over the last 90 days, we are one of the biggest software companies in the world. I mean annualize that or look at the trailing 12 months, makes us certainly on somewhere in the top 10 in software companies in the world. We posted 6% overall growth and 9% growth in subscriptions even off that base. I think the software business is actually doing quite well for us.

If what's underneath your question is, that what you saw in applications, I'll go back to what we said earlier about what's happening in applications. Underneath that, you've got to remember, that includes the entire collaboration portfolio, so not just the software pieces and not just the recurring software pieces, there's hardware elements there, there is some legacy on-prem elements there, both of those were headwinds. In the subscription software revenue piece, of both applications and security, we saw double-digit growth. We had nice growth year-on-year for the full year in both of those. So I actually feel good about where we're headed on that.

Q - Jeff Kvaal {BIO 3233206 <GO>}

Great. And then a quick clarification. Do you all plan to update the annual guidance every quarter for us?

A - R. Scott Herren {BIO 18902845 <GO>}

We'll assess it every quarter and update as needed. The big variable in there of course is what happens with supply chain and when do we start to see a little more balance come to supply and demand across some of our key components. And I think that will dictate when we've got a good view for updating.

Q - Jeff Kvaal {BIO 3233206 <GO>}

Thank you both very much.

A - Chuck Robbins {BIO 17845882 <GO>}

Thanks, Jeff.

A - Marilyn Mora {BIO 19771101 <GO>}

Thanks, Jeff. And we've got time for one more question.

Operator

Thank you. Ben Bollin from Cleveland Research. You may go ahead, sir.

Q - Benjamin J Bollin

Thanks for getting me in at the end. I also wanted to focus a little bit on software, a few specific items. The first, I'm curious how you think about your average contract duration and what you're seeing on kind of average invoice duration, as you shift more to software, any high-level implications you see for cash flow over time?

The second item is, curious if you've seen any trends with early renewals from the early DNA customers, what's happened at those renewals?

And then the last piece, how do you think about longer-term, making sure you're driving good utilization and consumption of the software licenses within the customer base? Thank you.

A - Chuck Robbins {BIO 17845882 <GO>}

You want to take the first?

A - R. Scott Herren {BIO 18902845 <GO>}

Yes. Okay. You managed to get in three there -- there Ben on the -- on the one question limit. I'll talk a bit about duration first. You see in our remaining performance obligations, you see the nice growth, $30.9 billion in total RPO is a record for us. What I'd say is underneath there, the short term is about 53% of that, they're growing somewhat balanced, slightly more growth in long-term than in short term, but that's what you'd expect, given that many of the -- over the short term is just the next 12 months, so the first year. The long-term is anything beyond that. So it's not surprising to see long-term grow a little bit more. We're not seeing a big change in duration overall.

And maybe I'll go ahead and hit the last one, Chuck and then leave the DNA question for you. As we look at the renewal rates and the actions we have to take, our renewal base is obviously growing and becoming much more important to us ahead and obviously renewals are dependent on adoption. We put in place very specific processes to understand where our customers are on usage and on adoption and you've got a -- if you don't drive the adoption, you don't get the renewal and so we're attacking it at that level. I think the team has done a nice job getting some headlights on that, some early warning and getting ahead of ensuring that we actually get the adoption we need.

A - Chuck Robbins {BIO 17845882 <GO>}

Yes. That's connected to the DNA renewal thing, because we actually have customer service -- I mean customer success specialists that are in the field, that are working with customers every day. We've got a virtual teller inside organization also doing customer success. So the adoption piece is really important.

As it relates to DNA, we've had sort of a handful in the first half of this year, of those renewals that will come through. It's a little bit more in the second half and then fiscal '23 is where it's actually a much more meaningful number and our teams have been working on the underlying processes, the metrics, the process, the systems, measurements and the engineering teams have been working really hard on continuing to evolve the offer to ensure that there is enough innovation going forward, that will optimize our opportunity on the renewal side of it.

So it's a bit early and I would say maybe second half of next year or this fiscal year, we can give you a little more on that and then into fiscal '23 is when it's a decent sized number.

Q - Benjamin J Bollin

Thank you.

A - Marilyn Mora {BIO 19771101 <GO>}

Great. Thanks Ben for the questions. Chuck, do you want to comment some closing remarks or I can close it up?

A - Chuck Robbins {BIO 17845882 <GO>}

I'll close and I'll hand it to you. So, I'm really proud of our team. I'm really proud of the performance and we're certainly pleased with the demand that we've seen. I'm super happy with the transformation. We believe our investments are paying off, our software business, the work we're doing with the webscale and the cloud providers and across the portfolio. I think our technology will help our customers deal with this emerging focus on resiliency and agility and adaptability. And then most of all, I want to thank our teams for the incredible execution, not only in Q4, but over the last 12 to 18 months during a very complicated time. And I'd like to also just remind you and encourage you all to join us on September 15th for the Investor Day. Thank you.

A - Marilyn Mora {BIO 19771101 <GO>}

Thanks, Chuck. So Cisco's next quarterly earnings conference call which will reflect our fiscal 2022 first quarter results will be on Wednesday November 17th, 2021 at 1:30 PM Pacific Time, 4:30 PM Eastern Time. Again, I'd like to remind the audience that in light of Regulation FD, Cisco's policy is not to comment on its financial guidance during the quarter, unless it is done through an explicit public disclosure. We will now plan to close the call. If you have any further questions, feel free to contact the Cisco Investor Relations group, and we thank you all very much for joining today's call.

Operator

Thank you for participating on today's conference call. If you would like to listen to the call in its entirety, you may call 1-800-388-4923. For participants dialing from outside the US, please dial 1-203-369-3800. This concludes today's call. You may disconnect at this time.