



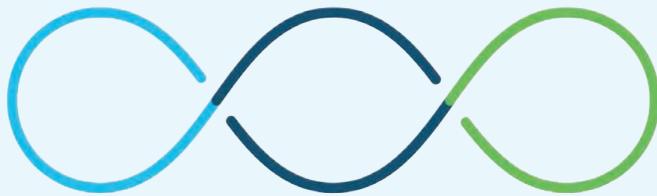
# 2018 Annual Report

# About Cisco

Cisco (NASDAQ: CSCO) is the worldwide technology leader that has been making the Internet work since 1984. Our people, products, and partners help society securely connect and seize tomorrow's digital opportunity today.

Discover more at [thenetwork.cisco.com](http://thenetwork.cisco.com) and follow us on Twitter at @Cisco.

## Our Culture



## Our People Deal

Our People Deal describes the culture Cisco wants and needs to lead in our industry. It is a deal because there are two sides—what our people can expect from Cisco and what we ask in return—and because every mature relationship needs both give and take.

These three pillars make up our unique experience at Cisco:

**connect**  
everything

innovate  
**everywhere**

**benefit**  
everyone

We **connect everything**—people, process, data, and things—and we use those connections to help change our world for the better. And we're doing it faster than ever before, in ways we believe no one else can.

We **innovate everywhere** to create fresh ideas and possibilities. We take bold risks to shape the future because we understand every failure is a success if we learn from it.

We support each other and work together to create shared success that will **benefit everyone**. The future of Cisco, the growth of our customers and partners, and the lives of people around the world—they're all connected.

# Introduction to Summary Report

This section provides an overview of Cisco. It does not contain all of the information you should consider. Please review our Annual Report on Form 10-K, our Proxy Statement for our 2018 Annual Meeting of Shareholders, and our Corporate Social Responsibility (CSR) Report, all available on our corporate website.

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## Online Report



To see our interactive online report visit our [Annual Reports](#) webpage. We welcome any [feedback](#) you may have.

## Forward-Looking Statements

This report contains projections and other forward-looking statements regarding future events or the future financial performance of Cisco, including future operating results. These projections and statements are only predictions. Actual events or results may differ materially from those in the projections or other forward-looking statements. See Cisco's filings with the Securities and Exchange Commission (SEC), including its most recent filings on Forms 10-K and 10-Q, for a discussion of important risk factors that could cause actual events or results to differ materially from those in the projections or other forward-looking statements.

# Letter to Shareholders

"With our commitment to providing a highly secure, intelligent platform for digital business, Cisco is firmly focused on being the most strategic partner for our customers."

## To our shareholders,

Fiscal 2018 was a great year for Cisco. As I look back, I am incredibly proud of the tremendous progress we have made. We returned to growth while transforming our business model, we executed well against our strategy, and our innovation pipeline has never been stronger. I could not be more excited about our future.

### Harnessing the power of connections

In today's complex, hyperconnected cloud world, agility, security, and speed are critical. To thrive, companies must be able to understand and securely harness the power of their connections, find patterns and intelligence in data, and anticipate and respond to shifting market conditions and stakeholders' needs. Our strategy is aligned with the changing needs of our customers. With our commitment to providing a highly secure, intelligent platform for digital business, Cisco is firmly focused on being the most strategic partner for our customers and helping them succeed in today's world.

The broad adoption of multicloud environments is changing the way our customers build and secure their IT infrastructure, and Cisco is at the center of this transition. Our highly secure, intelligent platform provides a critically important component: the ability to move workloads seamlessly across public and private clouds while ensuring that our customers' security policies are applied effectively. In fiscal 2018, we continued to innovate to manage complexity, deliver solutions, and enable applications for this environment. We have also extended our broad partnership ecosystem and have been working

closely with the major cloud providers. We are simplifying how our customers work by providing consistent experiences in on-premises and public-cloud environments for the development, deployment, and management of applications, and we believe Cisco is very well positioned to benefit from the increasing adoption of multicloud.

This past year we have also seen incredible momentum with our intent-based networking platform. Our customers are looking to have simplified, automated networks, and Cisco is delivering a fundamentally new, closed-loop system that is powered by intent and informed by context, constantly learning and adapting. The 2014 launch of our Application Centric Infrastructure (Cisco ACI)—policy-based automation for the data center—was our first step. We then brought intent-based networking to the access network with the launch of the Cisco Catalyst 9000 series of switches, Software-Defined Access (SD-Access), and DNA Center—a centralized management dashboard. Our Catalyst 9000 series of switches has become the fastest ramping product in Cisco's history—testament, we believe, to its ability to future-proof networks; to integrate automation, security and analytics; and to free up operating expenses and resources for our customers.

We have now extended SD-Access and DNA Center to the Internet of Things (IoT) environment, as well as extended Cisco ACI to the public cloud with Cisco ACI Anywhere. We have closed the loop with the addition of

network assurance capabilities, providing continuous verification of the network's intent, and offering insights and visibility into network policy and actions. We intend to extend open, programmable access across the entire network as we build an ecosystem around our intent-based networking portfolio.

Inevitably, as connections multiply, the threat landscape continues to grow and the concept of a security perimeter disappears. Security is fundamental across our portfolio and is foundational to all we do at Cisco. Our strategy is to simplify and increase security efficacy through an architectural approach, with products that work together and share analytics and actionable threat intelligence. We have been working hard to build an end-to-end security architecture from the endpoint to the network to the cloud, covering the entire attack continuum.

Shortly after the end of fiscal 2018, we announced our intention to acquire Duo Security to expand our cloud security capabilities. Duo's multifactor authentication solution verifies the identity of users and the health of their devices before granting them access to applications, helping prevent cybersecurity breaches. Duo's relevance within the context of our intent-based networking strategy spans the entire extended enterprise. Its portfolio of cloud-delivered solutions will help enable what our customers require in today's multicloud world: the ability to securely connect any user on any device to any application on any network.



## Key Milestones



**300+** projects completed or under way as part of Cisco's Country Digital Acceleration (CDA) program, encompassing economic development, entrepreneurship and innovation, research and education, and national infrastructures



**500,000+** registered users in DevNet, Cisco's developer program



**1.87 million** students in 180 countries participating in Cisco's Networking Academy in fiscal 2018



**"We are looking forward to fiscal 2019 with a clear focus on growth, execution, and innovation."**

With intent-based networking, we have not only changed the building blocks for networks but have created a platform for innovation across our entire portfolio. In fiscal 2018, we introduced new wide-area network (WAN) offerings through the integration of Viptela's SD-WAN capabilities with our core portfolio, as well as new access and data center offerings. With the integration of AppDynamics, we continued to develop our analytics capabilities, bringing end-to-end visibility and analytics from the end user to the network to the application. We also introduced new developer capabilities spanning all network domains through our DevNet program.

We are dedicated to creating better experiences for our customers and employees, and one way we do this is through our collaboration portfolio. In fiscal 2018, we created a new integrated meetings experience with Cisco Webex and added cloud calling and contact center solutions through the acquisition of Broadsoft and integration with Google. With the acquisition of Accompany, we are adding more intelligence and contextual information to meeting and team collaboration experiences.

#### Cultivating success

Our relationships with our customers are changing from transactional to lifecycle, so we have created a Customer Experience organization to help ensure their success at every stage of their digitization journey. Our commitment to our customers' success also drives our belief that it is essential to have a diversity of experiences and perspectives on our leadership team to yield the best results.

We are committed not only to our customers but also to making a difference in the world and solving some of the world's greatest challenges. Two years ago we set a goal to positively impact one billion people by 2025, and every day we come a step closer through our focus on educating the workforce of the future through the Cisco Networking Academy, building stronger communities, and applying our resources to the most pressing societal issues.

#### Transforming our business model

As we integrate our products and services into architectures, we are selling more software and subscription-based offerings. These are designed to provide our customers with flexibility and continuous value, and at the same time they help us to shift our business model to more recurring revenue streams.

In fiscal 2018, we delivered strong top-line growth and profitability, reporting our highest-ever revenue of \$49.3 billion. Recurring offers accounted for 32% of our total revenue in fiscal 2018, and revenue from subscriptions was 54% of our software revenue. Our intention is to continue to drive recurring revenues by applying a subscription-based model to many of the new products we launch and ultimately across our entire portfolio.

Our balance sheet remains strong, and we generated \$13.7 billion in operating cash flow in fiscal 2018. We returned \$23.6 billion to shareholders, comprising \$6.0 billion of dividends and \$17.7 billion of share repurchases.

#### Capitalizing on our opportunities

Our solid performance in fiscal 2018 demonstrates a combination of strong customer adoption of our latest solutions, the ongoing value customers see in our software and subscription offerings, and excellent execution. Our customers are looking for us to provide even greater value to them by redesigning their IT architecture; delivering security; and building, orchestrating, and managing applications. We are delivering solutions that matter to our customers, our strategy is working, and we believe we are well positioned to capture growth across our portfolio.

We are looking forward to fiscal 2019 with a clear focus on growth, execution, and innovation. We will continue to drive automation, security, and analytics across the entire network infrastructure. We will also leverage our assets and the power of connections across our portfolio and create an architecture designed to support our customers' success—all the way from IoT to multicloud—in a way that only Cisco can.

Thank you for your continued support.

**Charles H. Robbins**

Chairman and Chief Executive Officer  
October 17, 2018



**Partnership with Global Citizen**, whose mission is to eradicate poverty by 2030



**Five-year, \$50 million commitment** to "Destination: Home," a nonprofit organization, to help end homelessness in Silicon Valley



**440 million** people positively impacted by our cash grant investments



**\$383 million** Cisco and Cisco Foundation cash and in-kind contributions in fiscal 2018

# Financial Highlights for Fiscal 2018

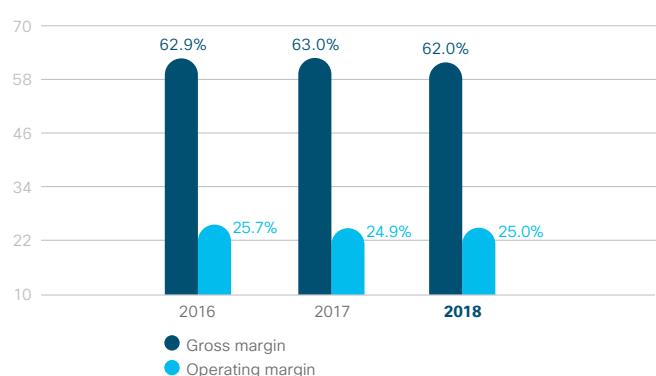
"We executed well, with strong top-line growth. We're seeing the returns on the investments we're making in innovation and driving the shift to more software and subscriptions, delivering long-term growth and shareholder value."

– Kelly Kramer, CFO

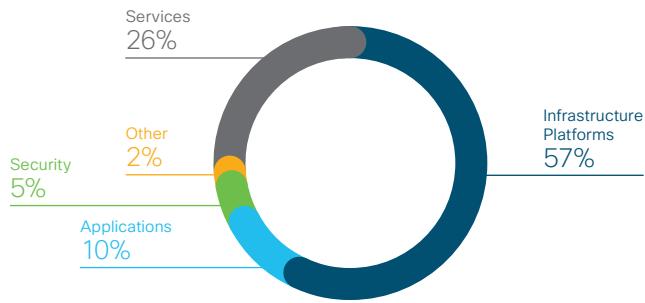
Revenue trend (\$B)



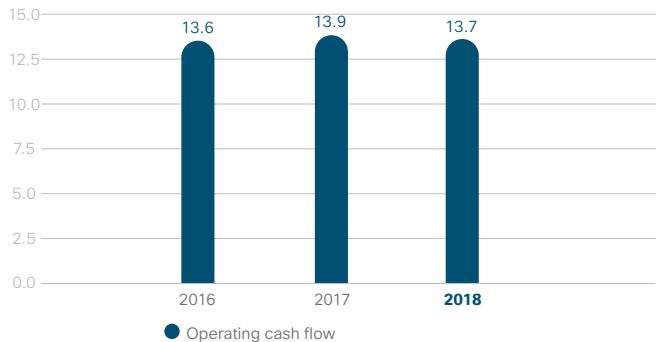
Margins (%)



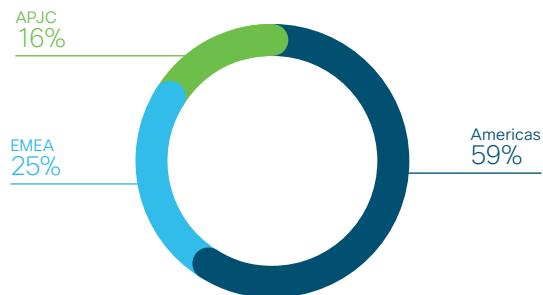
Revenue by product category and services



Operating cash flow (\$B)



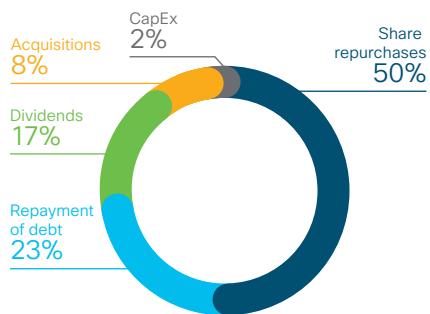
Revenue by geographical segment



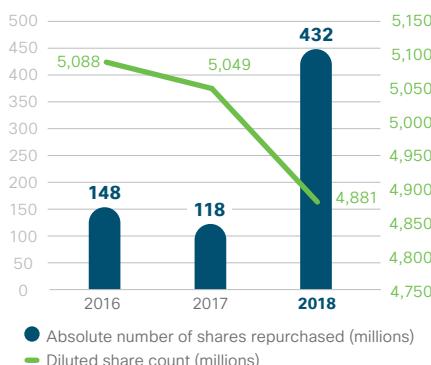
# Financial Highlights for Fiscal 2018

## Capital Allocation

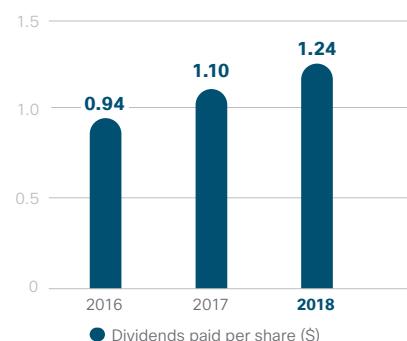
### Primary uses of cash



### Share repurchases and diluted share count (M)



### Dividends paid per share (\$)



### Acquisitions closed in fiscal 2018



July 2017

**Infrastructure Platforms–Routing and Switching**  
A software-defined wide area network (SD-WAN) solution that simplifies management, increases agility, and reduces costs of interconnecting dispersed enterprise networks



July 2017

**Security**  
Cloud-native network forensics security applications delivered as a service



September 2017

**Infrastructure Platforms–Data Center Computing**  
A distributed file system purpose-built for hyperconvergence that enables server-based storage systems



October 2017

**Applications–AppDynamics**  
Machine learning and data processing technology and expertise



December 2017

**Infrastructure Platforms–Cloud**  
A software solution that analyzes cloud-deployed workloads and consumption patterns and identifies cost-optimization strategies



February 2018

**Applications–Unified Communications**  
Cloud calling and contact center solutions



February 2018

**Infrastructure Platforms–Data Center Computing**  
Cloud-managed, hyperconverged systems that run and protect business-critical applications



May 2018

**Applications–Collaboration**  
An AI-driven relationship intelligence platform for finding new prospects, navigating the selling process, and strengthening relationships

# Our Strategy

As our customers add billions of new connections to their enterprises, and as more applications move to a multicloud environment, we believe the network continues to be extremely critical.

We believe that our customers are looking for intent-based networks that provide meaningful business value through automation, security, and analytics. Our vision is to deliver highly secure, software-defined, automated, and intelligent platforms for our customers. Our strategic priorities include accelerating our pace of innovation, increasing the value of the network, and transforming our business model.

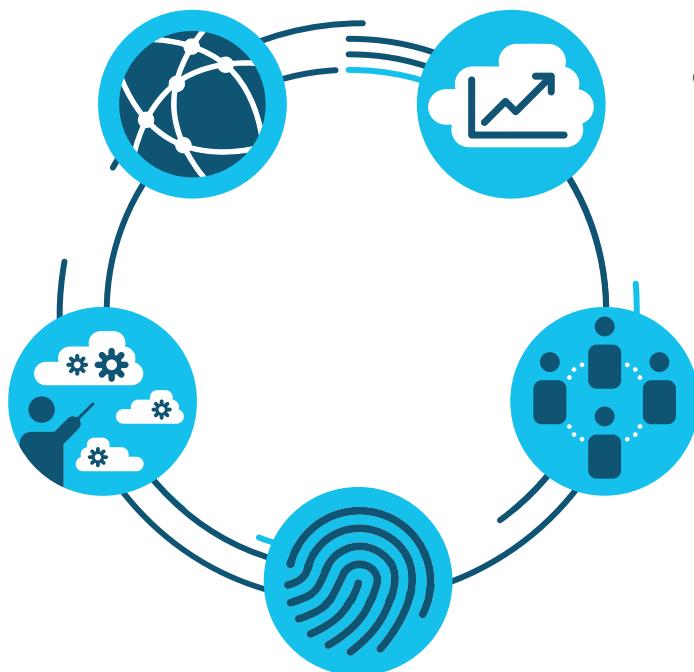
## Accelerating Our Pace of Innovation and Increasing the Value of the Network

### Reinvent the network

Our intent-based networking platform is designed to be intelligent, highly secure, powered by intent and informed by context—features aiming to constantly learn, adapt, automate, and protect to optimize network operations and defend against an evolving cyberthreat landscape.

### Power a multicloud world

Our cloud strategy is to deliver solutions designed to simplify, secure, and transform how customers work in this multicloud world to maximize business outcomes. We offer a solution for all cloud environments.



### Unlock the power of data

We believe the network will play an even more critical role in enabling customers to aggregate, automate, and draw actionable insights from highly distributed data, where there is a premium on security and speed.

### Create meaningful experiences

Our strategy is to make collaboration more effective and comprehensive and less complex by creating innovative solutions through combining the power of software, hardware, and the network.

### Security is foundational

Our security strategy is focused on delivering an effective cybersecurity architecture combining network, cloud, and endpoint solutions. Through our industry-leading Cisco Talos offering, we intend to protect against and provide security across the entire attack continuum—before, during, and after a cyberattack—and to help customers shorten the time between threat detection and response.

## Transforming Our Business Model

We are transforming our offerings to meet the evolving needs of customers. We are developing and selling more software and subscription-based offerings, which we expect will increase the amount of our recurring revenue. Historically, our various networking technology products have aligned with their respective product categories. However, increasingly our offerings are crossing multiple product categories. As our core networking evolves, we expect we will add more common software features across our core networking platforms.

# Cisco's Executive Leadership Team

Cisco's Executive Leadership Team brings a diverse set of experiences to identify and deliver strategic priorities, accelerate our innovation, enhance our execution, simplify how we do business, drive operational rigor, and inspire our employees to be the best that they can be.



**Chuck Robbins**

Chairman and  
Chief Executive Officer



**Mark Chandler**

Executive Vice President,  
Chief Legal Officer, and  
Chief Compliance Officer



**Amy Chang**

Senior Vice President,  
Collaboration  
Technology Group



**Gerri Elliott**

Executive Vice President  
and Chief Sales and  
Marketing Officer



**David Goeckeler**

Executive Vice President and  
General Manager, Networking  
and Security Business



**Anuj Kapur**

Senior Vice President and  
Chief Strategy Officer



**Francine Katsoudas**

Executive Vice President and  
Chief People Officer



**Kelly A. Kramer**

Executive Vice President and  
Chief Financial Officer



**Maria Martinez**

Executive Vice President  
and Chief Customer  
Experience Officer



**Mark Patterson**

Senior Vice President and  
Chief of Staff to the CEO



**Irving Tan**

Senior Vice President,  
Operations



**Michael Timmeny**

Senior Vice President  
and Chief Government  
Strategy Officer



## Executive Leadership Team diversity

We believe it is essential to have a diversity of experiences and perspectives on our Executive Leadership Team to yield the best results.

# Governance and Responsibility

Cisco is committed to shareholder-friendly corporate governance and the Board of Directors has adopted clear corporate policies that promote excellence in corporate governance.

## Shareholder Engagement

At Cisco, we recognize the importance of regular and transparent communication with our shareholders. Each year, we engage with a significant portion of shareholders that includes our top institutional investors. In fiscal 2018, we held meetings and conference calls with investors representing approximately 32% of our outstanding shares. We engaged with these shareholders on a variety of topics, including our corporate governance and risk management practices, board refreshment, sustainability initiatives, executive compensation program, and other matters of shareholder interest.



### Risk Management Approach

We believe that risk is inherent in innovation and the pursuit of long-term growth opportunities. Cisco's management is responsible for day-to-day risk management activities. The Board of Directors, acting directly and through its committees, is responsible for the oversight of risk management. With the oversight of the Board of Directors, Cisco has implemented practices and programs designed to help manage the risks to which we are exposed in our business and to align risk-taking with our efforts to increase shareholder value.

Cisco's management has implemented an enterprise risk management (ERM) program designed to work across the business to identify, assess, govern, and manage risks and Cisco's response to those risks. Cisco's internal audit function performs an annual risk assessment, which is utilized as part of the ERM program. The structure of the ERM program includes both an ERM operating committee that focuses on risk management-related topics, and an ERM executive committee consisting of members of senior management. The ERM operating committee conducts global risk reviews and generally provides biannual updates to the ERM executive committee.

The Audit Committee, which oversees financial and risk management policies including data protection (comprising both privacy and security), receives regular reports on ERM from the chair of the ERM operating committee and regular reports on cybersecurity from Cisco's Chief Security and Trust Officer. Other board committees oversee specific categories of risk associated with their respective areas of responsibility. The Board of Directors regularly discusses core subjects with senior management, including strategy, operations, information systems, finance, and legal and public policy matters, in which risk management is an inherent element.



### Policies and Practices

We have adopted these policies and practices consistent with our commitment to transparency and best-in-class practices, as well as to ensure compliance with the rules and regulations of the SEC, the listing requirements of NASDAQ, and applicable corporate governance requirements.

- ✓ Shareholder proxy access
- ✓ Annual election of all directors (since IPO)
- ✓ Majority voting (since 2007)
- ✓ Robust lead independent director role
- ✓ Shareholder right to call a special meeting (since IPO)
- ✓ No poison pill
- ✓ Recoupment policy (since 2008)
- ✓ Stock ownership guidelines for directors and executive officers
- ✓ Shareholder recommendations for director candidate to the board
- ✓ Shareholder right to act by written consent (since IPO)

# Governance and Responsibility

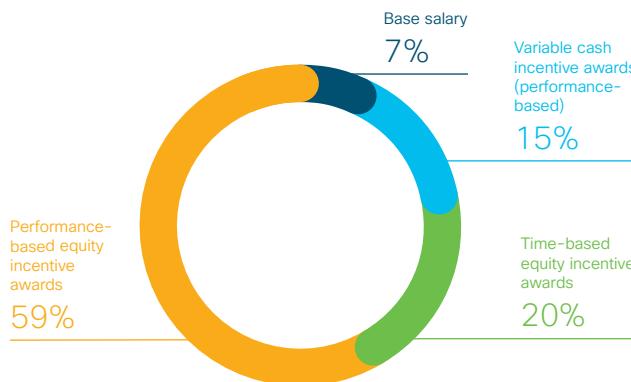
## Executive Compensation

Our pay practices align with our pay-for-performance philosophy and underscore our commitment to sound compensation and governance practices.

### Executive Compensation Highlights

These charts summarize the major elements of target total direct compensation for our CEO and our other named executive officers (NEOs<sup>1</sup>) as a group for fiscal 2018 and demonstrate our continued pay-for-performance philosophy.

#### CEO



#### NEOs other than CEO



Percentages may not total 100% due to rounding.

<sup>1</sup>As defined in our Proxy Statement for our 2018 Annual Meeting of Shareholders.



#### We apply leading executive compensation practices

- ✓ Independent compensation committee
- ✓ Independent compensation consultant
- ✓ Comprehensive annual compensation program risk assessment
- ✓ Caps on incentive compensation
- ✓ No employment or severance or change in control agreements
- ✓ Stock ownership guidelines
- ✓ Recoupment policy
- ✓ No single trigger vesting of equity award grants
- ✓ No stock option repricing or cash-out of underwater equity awards
- ✓ “No perks” policy with limited exceptions
- ✓ No supplemental executive retirement plan or executive-defined benefit pension plan
- ✓ No golden parachute tax gross-ups
- ✓ Broad anti-pledging and anti-hedging policies



#### Our executive compensation program rewards performance

- ✓ Compensation philosophy designed to attract and retain, motivate performance, and reward achievement
- ✓ Performance measures aligned with shareholder interests
- ✓ Majority of annual total direct compensation is performance-based
- ✓ No dividends on unvested awards

# Governance and Responsibility

## The Cisco Board of Directors

Cisco's Board of Directors believes strongly in the value of an independent board of directors. Independent board members have consistently comprised over 75% of the members of Cisco's Board of Directors. All members of the key board committees—the Audit Committee, the Compensation and Management Development Committee, and the Nomination and Governance Committee—are independent.



**Charles H. Robbins**

**Chairman and CEO**

Age **52**

Director since **2015**

Chairman since **2017**

Skills/Attributes



**Carol A. Bartz**

**Lead Independent Director**

Age **70**

Director since **1996**

Skills/Attributes



Committees



Mr. Robbins brings to the Board of Directors extensive industry, company and operational experience acquired from having served as Cisco's CEO since 2015, and prior to that from having led Cisco's global sales and partner teams. He has a thorough knowledge of Cisco's segments, technology areas, geographies, and competition. He has a proven track record of driving results and played a key role in leading and executing many of Cisco's investments and strategy shifts to meet its growth initiatives.

Ms. Bartz brings to the Board of Directors leadership experience, including service as the chief executive of two public technology companies. These roles have required technology industry expertise combined with marketing, operational, and global management expertise. Ms. Bartz also has experience as a public company outside director.

(Retiring from the Board in December 2018)



**M. Michele Burns**

**Independent Director**

Age **60**

Director since **2003**

Skills/Attributes



Committees



**Michael D. Capellas**

**Independent Director\***

Age **64**

Director since **2006**

Skills/Attributes



Committees



Ms. Burns provides to the Board of Directors expertise in corporate finance, accounting, and strategy, including experience gained as the chief financial officer of three public companies. Through her experience gained as chief executive officer of Mercer, she brings expertise in global and operational management, including a background in organizational leadership and human resources. Ms. Burns also has experience serving as a public company outside director.

Mr. Capellas brings to the Board of Directors experience in executive roles and a background of leading global organizations in the technology industry. Through this experience, he has developed expertise in several valued areas, including strategic product development, business development, sales, marketing, and finance.

\*The Board has appointed Michael Capellas as Lead Independent Director effective upon Mr. Capellas' re-election to the Board of Directors.



**Mark Garrett**

**Independent Director**

Age **60**

Director since **2018**

Skills/Attributes



Committees



**Dr. John L. Hennessy**

**Independent Director**

Age **66**

Director since **2002**

Skills/Attributes



Committees



Mr. Garrett brings to the Board of Directors extensive history of leadership in finance and accounting in the technology industry, including experience in the transformation and transition to the cloud. Mr. Garrett also has experience as a public company outside director.

Dr. Hennessy brings to the Board of Directors an engineering background as well as skill in the development of information technology businesses. In addition, he has leadership and management experience, both in an academic context at Stanford University and in a corporate context as a board member of public and private technology companies.

(Retiring from the Board in December 2018)

### Key to skills/attributes

Leadership

Technology

Financial experience

Global business

Gender/ethnic diversity

Sales and marketing

Academia

Public company board experience

# Board Snapshot

## Board governance structure



## Board diversity



## Balanced director tenure



**Dr. Kristina M. Johnson**  
**Independent Director**

Age **61**  
Director since **2012**

Dr. Johnson brings to the Board of Directors an engineering background as well as expertise in science, technology, business, education, and government. In addition, she has leadership and management experience, both in an academic context as chancellor, provost, and dean of nationally recognized academic institutions and in a corporate context as a board member of public technology companies.

### Skills/Attributes



### Committees



**Roderick C. McGeary**  
**Independent Director**

Age **68**  
Director since **2003**

Mr. McGeary brings to the Board of Directors a combination of executive experience in management and technology consulting. He also has expertise in leading talented teams, and skills in finance, accounting, and auditing with technology industry experience.



**Arun Sarin, KBE**  
**Independent Director**

Age **63**  
Director since **2009**

Mr. Sarin provides to the Board of Directors a telecommunications industry and technology background, as well as leadership skills, including through his global chief executive experience at Vodafone Group Plc. He also provides an international perspective as well as expertise in general management, finance, marketing, and operations. Mr. Sarin also has experience as a director, including service as an outside board member of companies in the information technology, banking, financial services, and retail industries.

### Skills/Attributes



### Committees



**Brenton L. Saunders**  
**Independent Director**

Age **48**  
Director since **2017**

Mr. Saunders brings to the Board of Directors his extensive leadership experience, including as chief executive officer of two global healthcare companies in addition to financial, strategic, and operational experience. He is a natural innovator and leader with a deep understanding of business transformation.



**Steven M. West**  
**Independent Director**

Age **63**  
Director since **1996**

Mr. West's experience in the information technology industry includes a variety of leadership and strategic positions, which have provided him with accumulated expertise in operational management, strategy, finance, and experience as an outside board member and audit committee member. Mr. West is a member of the National Association of Corporate Directors and was named to the NACD Directorship 100 in 2018. He is also a frequent speaker on audit committee and cybersecurity related issues. In addition, Mr. West has knowledge of Cisco acquired through more than 20 years of service on the Board of Directors.

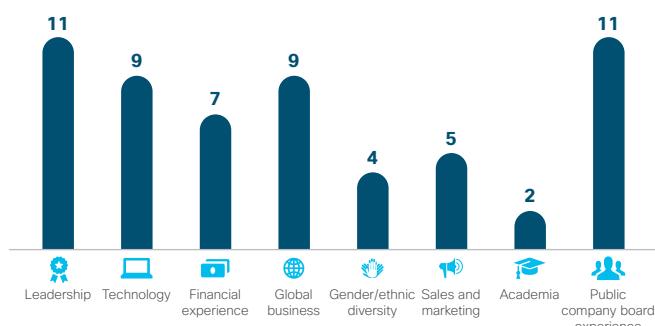
### Skills/Attributes



### Committees



## Board skills and attributes (number of Board members)



## Key to committees

**AU** Audit Committee

**N** Nomination and Governance Committee

**F** Finance Committee

**C** Compensation and Management Development Committee

**AQ** Acquisition Committee

**Committee Chair**

# Corporate Social Responsibility

Cisco pioneered the technology that connects everything and has now developed intent-based technologies that are constantly learning and adapting to provide customers with a highly secure, intelligent platform for their digital businesses. Through our technology, the passion and expertise of our people, and our network of partners, we are making connections to help accelerate global problem solving and advance positive social and environmental impact.

## Cisco Connects

We are taking action across our three focus areas of people, society, and planet that are aligned with Cisco's business strategy and where we believe we can make the greatest impact.



### People

- Attracting and retaining top talent
- Inclusion and collaboration
- Employee community impact



### Society

- Building skills and entrepreneurship
- Strategic social investments
- Human rights
- Responsible sourcing and manufacturing



### Planet

- Energy and greenhouse gas reduction
- Responsible resource use

## Culture of integrity

## Key Initiatives and Progress Toward Goals



**80%**

Achieve 80% employee engagement (through volunteering or making donations) by 2020

### People

Inclusion is the bridge that connects diverse perspectives, challenges the status quo, and unlocks the full potential of our people. In this age of digital transformation, we believe inclusion, diversity, and collaboration make us more innovative, more agile, and ultimately more successful.

At Cisco, our commitment to inclusion starts at the top. Women comprise 42% of our executive leadership team (ELT). Based on gender and ethnicity, our ELT is 58% diverse—making it one of the most diverse executive teams in our industry. We have driven broad improvements in representation across our global company that have resulted in the most diverse Cisco ever. In the past year, we have delivered innovative new solutions to some of our most business-critical challenges and opportunities to accelerate and develop diverse talent,

engage our employee community, advocate for a future of fairness, and impact society.

Our people are passionate about sharing their time and talents to help others in the community, and we want everyone to have time to participate in community-helping activities, so we offer full-time employees five days off per year to volunteer through a program we call Time2Give. Additionally, the Cisco Foundation matches volunteer time and employee donations up to \$10,000 per employee per year, which is one of the most generous matching gift policies in the industry.

During fiscal 2018, employee community engagement, measured by the proportion of employees volunteering or making donations, increased by approximately 2 percentage points compared to fiscal 2017, to 46%.

## Society



**1 billion**

Positively impact one billion people by 2025

**2 million**

Reach two million Cisco Networking Academy students per year by 2021

Cisco strives to accelerate global problem solving by creating exponential opportunity for social and business impact.

We are enabling social enterprises and nonprofits to accelerate early-stage, technology-based solutions addressing education, economic empowerment, and critical human needs. Our nonprofit partners report that our cash grant investments positively impacted 208 million people in fiscal 2018. This represents an increase of 54 million from the fiscal 2017 number of 154 million. The cumulative total since we announced the initiative in fiscal 2016 is 440 million, 44% of our goal of positively impacting one billion people by 2025.

Our strategic investment in the Cisco Networking Academy helps countries meet industry demand for a digitally skilled workforce by providing a

comprehensive learning experience. With 1.87 million students in 180 countries participating in the Cisco Networking Academy in fiscal 2018, we made tremendous progress toward our goal of reaching two million Cisco Networking Academy Students per year by 2021.

In fiscal 2018, cash and in-kind contributions from Cisco and the Cisco Foundation totaled \$383 million.

Ethical sourcing is an important facet of our ethical conduct strategy. Suppliers must acknowledge their commitment to our Supplier Code of Conduct, which is based on the Supplier Code of Conduct put forth by the Responsible Business Alliance (RBA). We have also expanded our Conflict Minerals Program to become a Raw Materials Sourcing Program, which now includes additional minerals such as cobalt.

## Planet



**60%**

Reduce Scope 1 and 2 GHG emissions worldwide by 60% absolute by fiscal 2022 (fiscal 2007 baseline)

**85%**

Use electricity generated from renewable sources for at least 85% of our global electricity by 2022

In fiscal 2017, Cisco met its five-year greenhouse gas (GHG) goal to reduce Cisco's worldwide Scope 1 and 2 GHG emissions by 40% in absolute terms compared to our fiscal 2007 baseline. Early in fiscal 2018, we announced new, five-year GHG and renewable electricity goals, continuing along the roadmap recommended by the Intergovernmental Panel on Climate Change in 2007.

Through the end of fiscal 2017, we had invested more than \$50 million—with a payback of less than four years—in 450 energy efficiency and renewable energy projects to meet our just completed, five-year 40% reduction goal. We are planning to invest \$45 million over the next five years to meet our fiscal 2022 goals.

As part of the Platform for Accelerating the Circular Economy (PACE), at the World Economic Forum in Davos in early 2018, Cisco Chairman and CEO Chuck Robbins pledged, as part of Cisco's sponsorship of the circular economy, the following: provide product return pickup and transport at no cost for any customer worldwide; return used product to Cisco; establish alternative commercial models to promote product return; offer comprehensive warranty, replacement, service, and repair for all products; and repurpose returned products and components, including closed-loop return to new product manufacturing.

# Governance and Responsibility

## CSR Governance and Recognition

### CSR Governance and Management

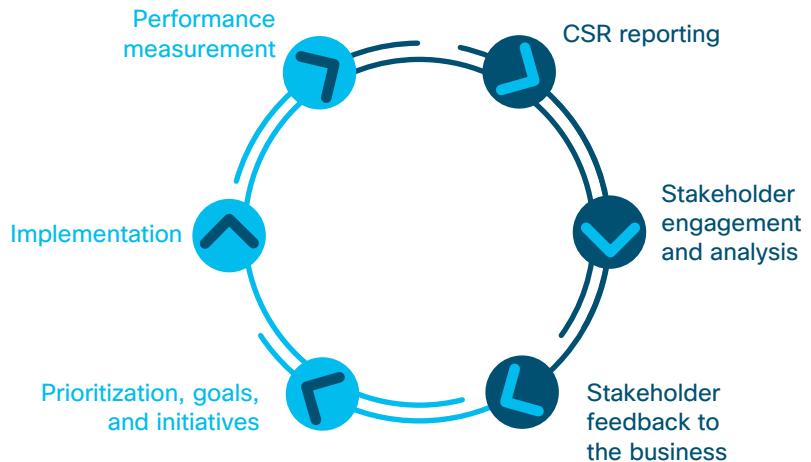
Cisco Corporate Affairs leads our social investment programs and champions our commitment to CSR performance and transparency. This team engages with internal and external stakeholders and leads CSR materiality assessment and reporting activities, which are aligned with standards set by the Global Reporting Initiative (GRI). The team assesses and monitors CSR priorities, establishes corporate CSR strategy, drives process for CSR management, and provides guidance and coordination across business functions.

CSR priorities are owned by business functions and are integrated into ongoing business strategy and planning. Business functions set CSR goals, implement plans, and measure performance. Where a cross-functional approach is needed, we establish teams to implement our commitments.

CSR is integrated into Cisco's business strategy and functions. It is foundational to our culture and a core value by which we do business.

### Cisco CSR Business Process

#### Business functions      Corporate Affairs



### Recognition

Earned the number one spot on **Barron's 100 Most Sustainable Companies** list (based on a review of 1000 publicly traded companies headquartered in the United States)

Earned **Newsweek's Green Ranking** – coming in fifth in its global list and ranking as the number one IT company worldwide

Named to **Corporate Knights' Global 100** list of the most sustainable corporations, coming in at number seven

Ranked third on **Fortune's 50 Best Workplaces for Giving Back**

Won a **Smart Energy Decisions Innovation Award** for Cisco's Global EnergyOps Program

Ranked in **Dow Jones Sustainability North America and World Index** for 2018

Made seventh appearance on the **CDP's Performance Leadership Index/Climate A List**. Fiscal 2018 represents our 14th year reporting to CDP (formerly Carbon Disclosure Project)



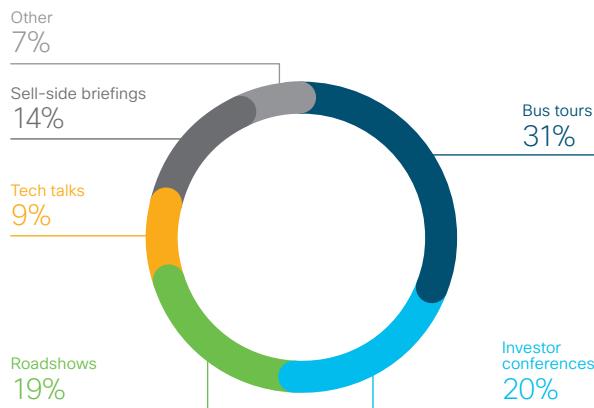
For more information about our performance, see our CSR website at [csr.cisco.com](http://csr.cisco.com). Our full fiscal 2018 CSR report will be published in December 2018.

# Investor Relations

The latest information about our earnings and stock performance, as well as presentations and webcasts, can be found on our Investor Relations website.

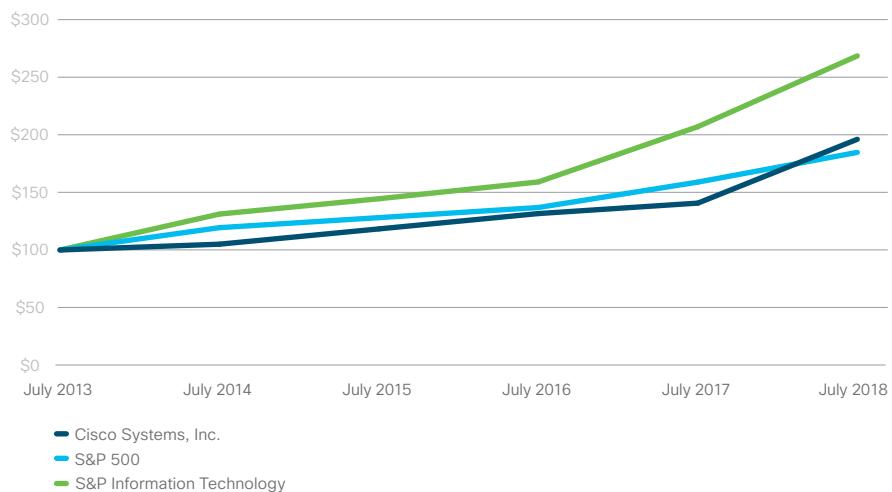
Learn more at [investor.cisco.com](http://investor.cisco.com).

## Our fiscal **2018** investor engagement by number of events



For webcasts and additional information, view our [events calendar](#).

## Comparison of five-year cumulative total return



This graph shows a five-year comparison of the cumulative total shareholder return on Cisco common stock with the cumulative total returns of the S&P 500 Index and the S&P Information Technology Index. The graph tracks the performance of a \$100 investment in Cisco's common stock and in each of the indexes (with the reinvestment of all dividends) on the date specified. Shareholder returns over the indicated period are based on historical data and should not be considered indicative of future shareholder returns.



## Investor contact

To contact Investor Relations:

### Investor Relations Department

Cisco Systems, Inc.  
170 West Tasman Drive  
San Jose, CA  
95134-1706 USA

Phone: 1 408 227 CSCO (2726)

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# UNITED STATES SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

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## FORM 10-K

(Mark one)

- ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934  
For the fiscal year ended July 28, 2018

or

- TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934  
For the transition period from \_\_\_\_\_ to \_\_\_\_\_  
Commission file number 0-18225



### CISCO SYSTEMS, INC.

(Exact name of Registrant as specified in its charter)

California  
(State or other jurisdiction of incorporation or organization)  
170 West Tasman Drive  
San Jose, California  
(Address of principal executive offices)

77-0059951  
(IRS Employer Identification No.)  
95134-1706

(Zip Code)

Registrant's telephone number, including area code: (408) 526-4000  
Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class:  
Common Stock, par value \$0.001 per share

Name of Each Exchange on which Registered  
The Nasdaq Stock Market LLC

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.  Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.  Yes  No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.  Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).  Yes  No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) is not contained herein, and will not be contained to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company" and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer

Accelerated filer

Non-accelerated filer  (Do not check if a smaller reporting company)

Smaller reporting company

Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).  Yes  No

Aggregate market value of registrant's common stock held by non-affiliates of the registrant, based upon the closing price of a share of the registrant's common stock on January 26, 2018 as reported by the Nasdaq Global Select Market on that date: \$207,120,318,133

Number of shares of the registrant's common stock outstanding as of August 31, 2018: 4,571,334,136

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### DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's Proxy Statement relating to the registrant's 2018 Annual Meeting of Shareholders, to be held on December 12, 2018, are incorporated by reference into Part III of this Annual Report on Form 10-K where indicated.

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*This Annual Report on Form 10-K, including the “Management’s Discussion and Analysis of Financial Condition and Results of Operations,” contains forward-looking statements regarding future events and our future results that are subject to the safe harbors created under the Securities Act of 1933 (the “Securities Act”) and the Securities Exchange Act of 1934 (the “Exchange Act”). All statements other than statements of historical facts are statements that could be deemed forward-looking statements. These statements are based on current expectations, estimates, forecasts, and projections about the industries in which we operate and the beliefs and assumptions of our management. Words such as “expects,” “anticipates,” “targets,” “goals,” “projects,” “intends,” “plans,” “believes,” “momentum,” “seeks,” “estimates,” “continues,” “endeavors,” “strives,” “may,” variations of such words, and similar expressions are intended to identify such forward-looking statements. In addition, any statements that refer to projections of our future financial performance, our anticipated growth and trends in our businesses, and other characterizations of future events or circumstances are forward-looking statements. Readers are cautioned that these forward-looking statements are only predictions and are subject to risks, uncertainties, and assumptions that are difficult to predict, including those identified below, under “Item 1A. Risk Factors,” and elsewhere herein. Therefore, actual results may differ materially and adversely from those expressed in any forward-looking statements. We undertake no obligation to revise or update any forward-looking statements for any reason.*

## PART I

### Item 1. Business

#### General

Cisco designs and sells a broad range of technologies that have been powering the Internet since 1984. Across networking, security, collaboration, applications and the cloud, our evolving intent-based technologies are constantly learning and adapting to provide customers with a highly secure, intelligent platform for their digital business.

We conduct our business globally, and manage our business by geography. Our business is organized into the following three geographic segments: Americas; Europe, Middle East, and Africa (EMEA); and Asia Pacific, Japan, and China (APJC). For revenue and other information regarding these segments, see Note 17 to the Consolidated Financial Statements.

Our products and technologies are grouped into the following categories: Infrastructure Platforms; Applications; Security and Other Products. In addition to our product offerings, we provide a broad range of service offerings, including technical support services and advanced services. Increasingly, we are delivering our technologies through software and services. Our customers include businesses of all sizes, public institutions, governments, and service providers. These customers often look to us as a strategic partner to help them use information technology (IT) to differentiate themselves and drive positive business outcomes.

We were incorporated in California in December 1984, and our headquarters are in San Jose, California. The mailing address of our headquarters is 170 West Tasman Drive, San Jose, California 95134-1706, and our telephone number at that location is (408) 526-4000. Our website is [www.cisco.com](http://www.cisco.com). Through a link on the Investor Relations section of our website, we make available the following filings as soon as reasonably practicable after they are electronically filed with or furnished to the Securities and Exchange Commission (SEC): our Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, and any amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act. All such filings are available free of charge. The information posted on our website is not incorporated into this report.

#### Strategy and Priorities

As our customers add billions of new connections to their enterprises, and as more applications move to a multi-cloud environment, we believe the network continues to be extremely critical. We believe that our customers are looking for intent-based networks that provide meaningful business value through automation, security, and analytics across private, hybrid, and multi-cloud environments. Our vision is to deliver highly secure, software-defined, automated and intelligent platforms for our customers. Our strategic priorities include the following: accelerating our pace of innovation, increasing the value of the network, and transforming our business model.

##### *Accelerating Pace of Innovation — Enabling Network Automation*

In fiscal 2017, we announced the initial development of new network product offerings that feature our intent-based networking technology. The intent-based networking platform is designed to be intelligent, highly secure, powered by “intent” and informed by “context”—features aiming to constantly learn, adapt, automate and protect in order to optimize network operations and defend against an evolving cyber threat landscape. To further our innovation in this area, we are applying the latest technologies such as machine learning and advanced analytics, to operate and define the network. From a security standpoint, these new network product offerings are designed to enable customers to detect threats, for instance, in encrypted traffic, and we have created what is in our view the only network that is designed for security while maintaining privacy.

Our Catalyst 9000 series of switches represent the initial build of our intent-based networking capabilities and provide highly differentiated advancements in security, programmability, and performance, while lowering operating costs by innovating at the hardware and software layers. Our intent-based network started with the Software-Defined Access (SD-Access) technology, one of our leading enterprise architectures. These offerings are designed to provide a single, highly secure network fabric that helps ensure policy consistency and network assurance; enables faster launches of new business services; and significantly improves issue resolution times while being open and extendable. SD-Access, built on the principles of Cisco Digital Networking Architecture (DNA), provides what we see as a transformational shift in the building and managing of networks.

For the data center, our Application Centric Infrastructure (ACI) solutions deliver centralized application-driven policy automation, management, and visibility of both physical and virtual environments as a single system.

### ***Increasing the Value of the Network***

Unlocking the Power of Data. Our customers are increasingly using technology, and specifically, networks to grow their businesses, drive efficiencies, and more effectively compete. We believe data is one of an organization's most strategic assets, and this data is increasingly distributed across every organization and ecosystem, on customer premises, at the edge of the network, and in the cloud. As the number of new devices connected to the Internet grows, we believe the network will play an even more critical role in enabling our customers to aggregate, automate, and draw actionable insights from this highly distributed data, where there is a premium on security and speed. We believe this is driving our customers to adopt entirely new IT architectures and organizational structures and, more specifically, to seek network deployment solutions that deliver greater agility, productivity, security, and other advanced network capabilities.

Security is Foundational. We believe that security is the top IT priority for many of our customers. Our security strategy is focused on delivering an effective cybersecurity architecture combining network, cloud and endpoint-based solutions. Through our industry-leading Cisco Talos offering, we intend to protect against and provide security across the entire attack continuum before, during, and after a cyberattack to help our customers shorten the time between threat detection and response.

Powering a Multi-Cloud World. Our customers are operating in multi-cloud environments with private, public, and hybrid clouds. Our cloud strategy is to deliver solutions designed to simplify, secure, and transform how customers work in this multi-cloud world to maximize business outcomes.

As our customers navigate the multi-cloud world, they need to connect new devices, protect their assets and monitor cloud consumption, and they also require advisory cloud services that are provided in a consistent manner. We are focused on enabling simple, intelligent, automated and highly secure clouds by delivering the infrastructure to navigate the complex IT environment through our software and subscription-based offerings including Webex, Meraki cloud networking, and certain other of our Security and Applications offerings. We believe that customers and partners view our approach to the cloud as differentiated and unique, recognizing that we offer a solution for all cloud environments, including private, hybrid, and public clouds.

In our view, over the next several years, customers will be increasingly writing modern applications that can run on any hybrid cloud, and will be adding billions of connections to their environment. We believe Cisco is uniquely positioned to enable successful business outcomes for customers in hybrid and multi-cloud environments. In our view, the network has never been more critical to business success and we believe our customers will benefit from the insights and intelligence that we are making accessible through our highly differentiated platforms.

### ***Transforming our Business Model***

We are transforming our offerings to meet the evolving needs of our customers. As part of the transformation of our business, we continued to make strides during fiscal 2018 to develop and sell more software and subscription-based offerings, which we expect will increase the amount of our recurring revenue. The Catalyst 9000 series of switches are an example of how we are beginning to shift more of our core business to a subscription-based model. Historically, our various networking technology products have aligned with their respective product categories. However, increasingly, our offerings are crossing multiple product categories. As our core networking evolves, we expect we will add more common software features across our core networking platforms. With respect to the disaggregation of hardware and software and how our customers want to consume our technology, we are increasing the amount of software offerings that we provide. We have various types of software arrangements including system software, on premise software, hybrid software and SaaS offerings. In terms of monetization, our software offerings fall into the broad categories of subscription arrangements and perpetual licenses.

For a discussion of the risks associated with our strategy, see "Item 1A. Risk Factors," including the risk factor entitled "We depend upon the development of new products and enhancements to existing products, and if we fail to predict and respond to emerging technological trends and customers' changing needs, our operating results and market share may suffer." For information regarding sales of our major products and services, see Note 17 to the Consolidated Financial Statements.

## **Products and Services**

Our products and services are grouped into the following categories:

### ***Infrastructure Platforms***

Infrastructure Platforms consist of our core networking technologies of switching, routing, data center products, and wireless that are designed to work together to deliver networking capabilities and transport and/or store data. These technologies consist of both hardware and software offerings that help our customers build networks, automate, orchestrate, integrate, and digitize data. We believe it is critical for us to continue to deliver continuous value to our customers. Over fiscal 2018, we made ongoing progress in shifting more of our business to software and subscriptions across our core networking portfolio, and in expanding our software offerings. Our objective is to continue moving to cloud-managed solutions across our entire enterprise networking portfolio. We continue to expand on our intent driven infrastructure, which focuses on simplicity, automation, and security, allowing enterprises to manage and govern the interactions of users, devices and applications across their IT environments. In fiscal 2017, we launched our Cisco Catalyst 9000 series of switches, which were developed for security, mobility, the Internet of Things (IoT), and the cloud. These switches form the foundation for our leading enterprise architectures, built on the principles of Cisco DNA. We continue to expand on this technology by extending SD-Access and Cisco DNA Center to the IoT environment and Application Centric Infrastructure (ACI) to the public cloud.

Our switching portfolio encompasses campus switching offerings as well as data center switching offerings. Our campus switching offerings provide the foundation for converged data, voice, video, and IoT services. These switches offer enhanced security and reliability and are designed to scale efficiently as our customers grow. Within campus switching are the recently launched Catalyst 9000 series of switches that include hardware with embedded software, along with, a software subscription referred to as Cisco DNA. Cisco DNA provides automation, analytics and security features and can be centrally monitored, managed, and configured. Our data center switching offerings provide the foundation for mission critical data centers with high availability, scalability, and security across traditional data centers and private and public cloud data centers.

Our routing portfolio interconnects public and private wireline and mobile networks and mobile networks, delivering highly secure and reliable service to campus, data center and branch networks. Our routing solutions are designed to meet the scale, reliability, and security needs of our customers. During fiscal 2018, we introduced the principles of Cisco DNA into our routing portfolio along with software-defined wide area network (SD-WAN), increasing flexibility and simplicity and delivery through the cloud.

Our Data Center portfolio incorporates various technologies and solutions including the Cisco Unified Computing System (Cisco UCS), HyperFlex (HX), and software management capabilities which combine computing, networking, and storage infrastructure management and virtualization to deliver agility, simplicity and scale. These products are designed to extend the power and simplicity of unified computing for data-intensive workloads, applications at the edge, and the next generation of distributed application architectures.

Our Wireless portfolio provides indoor and outdoor wireless coverage designed for seamless roaming use of voice, video, and data applications. These products include wireless access points that are standalone, controller appliance-based, switch-converged, and Meraki cloud-managed offerings. In fiscal 2018, we expanded our capabilities to include network assurance and automation through our Cisco DNA Center and location-based services.

### ***Applications***

The Applications product category consists primarily of software-related offerings that utilize the core networking and data center platforms to provide their functions. Our Applications offerings consist of both hardware and software-based solutions, including both software licenses and software-as-a-service. Applications include our collaboration offerings (unified communications, Cisco TelePresence and conferencing) as well as the IoT and analytics software offerings from Jasper and AppDynamics, respectively.

Our strategy is to make collaboration more effective, comprehensive, and less complex by creating innovative solutions through combining the power of software, hardware, and the network. We offer a portfolio of solutions which can be delivered from the cloud, premise or mixed environments, and which integrate voice, video, and messaging on fixed and mobile networks across a wide range of devices/endpoints such as mobile phones, tablets, desktop and laptop computers, video units and collaboration appliances. Growth in cloud-connected products and services was highlighted by the acquisition of BroadSoft, a leading provider of cloud-based unified communications. In addition, we announced innovative new cloud-connected products and services within our Collaboration portfolio including the Cisco WebexVirtual Assistant, AI driven voice assistance for workplace collaboration, and Webex Room telepresence endpoint devices. For on-premise collaboration markets, we launched multi-party Internet Protocol (IP) Phones to extend our reach into third-party call control platforms as well as a new series of telephony headsets which offer innovative integration with our market leading IP phone business.

Our analytics solutions seek to help businesses deliver consistently high quality digital experiences by connecting end-user experience and application performance to business outcomes. Our applications monitor, correlate, analyze, and act on application

performance and business performance data in real time. This automated, cross-stack intelligence enables developers, IT operations, and business owners to make mission critical and strategic improvements.

We continue to invest in IoT as the number of connected IoT devices continues to grow. Our Jasper Control Center Platform enables enterprises to automate the lifecycle of connected devices, including tools designed to automatically and remotely onboard, manage and monetize their IoT devices.

### ***Security***

The Security product category primarily includes our unified threat management products, advanced threat security products, and web security products that are designed to provide a highly secure environment for our customers. Security continues to be the top IT priority for many of our customers and we continue to believe that security solutions will help to protect the digital economy. We believe that security will be an enabler that helps safeguard our customers' business interests and can help create competitive advantage for them. Our approach is designed to provide protection across the entire attack continuum before, during, and after a cyber-attack and to help our customers shorten the time to threat detection and response. In our view, the escalation of ransomware and other malware events in the past year demonstrates that organizations are more critically exposed than ever.

Our security portfolio is designed to increase capability while reducing complexity by delivering simple, open, and automated solutions resulting in more effective security. Our security portfolio spans endpoints, the network, and the cloud. Our offerings cover the following network-related areas: network and data center security, advanced threat protection, web and email security, access and policy, unified threat management, and advisory, integration, and managed services. Our offerings are powered by Cisco Talos, our industry-leading, cloud delivered threat intelligence platform.

In fiscal 2018, we continued to invest in cloud security. These investments include introducing our Stealthwatch Cloud, behavioral threat detection for IaaS (infrastructure as a service) and PaaS (platform as a service) environments, extending our Umbrella Platform capabilities, and providing new functions such as shadow IT discovery in CloudLock, our CASB (Cloud Access Security Broker) solution. We significantly extended our endpoint security portfolio (Advanced Malware Protection for Endpoints) with new exploit prevention capabilities for fileless malware. We remain focused on delivering an integrated architecture across our Security products, highlighted by the introduction of Cisco Visibility, a unified threat management platform across many of our products.

### ***Other Products***

Our Other Products category primarily consists of Service Provider Video Software and Solutions and cloud and system management products. We announced a definitive agreement to sell our Service Provider Video Software and Solutions business in the fourth quarter of fiscal 2018. We expect this transaction to close in the first half of fiscal 2019 subject to regulatory approvals and customary closing conditions.

### ***Services***

In addition to our product offerings, we provide a broad range of service and support options for our customers, including technical support services and advanced services. In fiscal 2019, we introduced Customer Experience, combining our overall service and support offerings into one organization that is responsible for the end-to-end customer experience.

Technical support services help our customers ensure their products operate efficiently, remain available, and benefit from the most up-to-date system, and application software. These services help customers protect their network investments, manage risk, and minimize downtime for systems running mission-critical applications. A key example is Cisco Smart Services, which leverages the intelligence from the installed base of our products and customer connections to protect and optimize network investment for our customers and partners. We have expanded our Technical Services offerings from traditional hardware support to software, solutions, and premium support and outcome based offers.

Advanced services are part of a comprehensive program that is focused on providing responsive, preventive, and consultative support of our technologies for specific networking needs. We are investing in and expanding our advanced services in the areas of cloud, security, and analytics, which reflects our strategy of selling customer outcomes. We are focused on three priorities including, utilizing Technology Advisory Services to drive higher product and services pull-through; Assessment and Migration services providing the tools, expertise and methodologies to enable our customers to migrate to new technology platforms; and providing optimization services aligned with customers' measurable business outcomes.

We believe this strategy, along with our architectural approach and networking expertise, has the potential to further differentiate us from competitors.

## **Customers and Markets**

Many factors influence the IT, collaboration, and networking requirements of our customers. These include the size of the organization, number and types of technology systems, geographic location, and business applications deployed throughout the customer's network. Our customer base is not limited to any specific industry, geography, or market segment. In each of the past three fiscal years, no single customer accounted for 10% or more of revenue. Our customers primarily operate in the following markets: enterprise, commercial, service provider, and public sector.

### ***Enterprise***

Enterprise businesses are large regional, national, or global organizations with multiple locations or branch offices and typically employ 1,000 or more employees. Many enterprise businesses have unique IT, collaboration, and networking needs within a multivendor environment. We plan to take advantage of the network-as-a-platform strategy to integrate business processes with technology architectures to assist customer growth. We offer service and support packages, financing, and managed network services, primarily through our service provider partners. We sell these products through a network of third-party application and technology vendors and channel partners, as well as selling directly to these customers.

### ***Commercial***

We define commercial businesses as organizations which typically have fewer than 1,000 employees. We sell to the larger, or midmarket, customers within the commercial market through a combination of our direct sales force and channel partners. These customers typically require the latest advanced technologies that our enterprise customers demand, but with less complexity. Small businesses, or organizations with fewer than 100 employees, require information technologies and communication products that are easy to configure, install, and maintain. We sell to these smaller organizations within the commercial market primarily through channel partners.

### ***Service Providers***

Service providers offer data, voice, video, and mobile/wireless services to businesses, governments, utilities, and consumers worldwide. This customer market category includes regional, national, and international wireline carriers, as well as Internet, cable, and wireless providers. We also include media, broadcast, and content providers within our service provider market, as the lines in the telecommunications industry continue to blur between traditional network-based, content-based and application-based services. Service providers use a variety of our products and services for their own networks. In addition, many service providers use Cisco data center, virtualization, and collaboration technologies to offer managed or Internet-based services to their business customers. Compared with other customers, service providers are more likely to require network design, deployment, and support services because of the greater scale and higher complexity of their networks, whose requirements are addressed, we believe, by our architectural approach.

### ***Public Sector***

Public sector entities include federal governments, state and local governments, as well as educational institution customers. Many public sector entities have unique IT, collaboration, and networking needs within a multivendor environment. We sell to public sector entities through a network of third-party application and technology vendors and channel partners, as well as through direct sales.

## **Sales Overview**

As of the end of fiscal 2018, our worldwide sales and marketing departments consisted of approximately 25,200 employees, including managers, sales representatives, and technical support personnel. We have field sales offices in 96 countries, and we sell our products and services both directly and through a variety of channels with support from our salesforce. A substantial portion of our products and services is sold through channel partners, and the remainder is sold through direct sales. Channel partners include systems integrators, service providers, other resellers, and distributors.

Systems integrators and service providers typically sell directly to end users and often provide system installation, technical support, professional services, and other support services in addition to network equipment sales. Systems integrators also typically integrate our products into an overall solution. Some service providers are also systems integrators.

Distributors typically hold inventory and sell to systems integrators, service providers, and other resellers. We refer to sales through distributors as our two-tier system of sales to the end customer. Revenue from two-tier distributors is recognized based on a sell-through method using point of sales information provided by these distributors. Starting in fiscal 2019, in connection with the adoption of ASC 606, *Revenue from Contracts with Customers*, a new accounting standard related to revenue recognition, we will start recognizing revenue from two-tier distributors on a sell-in method. For further discussion of ASC 606, see Note 2 to the Consolidated Financial Statements. These distributors are generally given business terms that allow them to return a portion of inventory, receive credits for changes in selling prices, and participate in various cooperative marketing programs.

For information regarding risks related to our channels, see “Item 1A. Risk Factors,” including the risk factors entitled “Disruption of, or changes in, our distribution model could harm our sales and margins” and “Our inventory management relating to our sales to our two-tier distribution channel is complex, and excess inventory may harm our gross margins.”

For information regarding risks relating to our international operations, see “Item 1A. Risk Factors,” including the risk factors entitled “Our operating results may be adversely affected by unfavorable economic and market conditions and the uncertain geopolitical environment;” “Entrance into new or developing markets exposes us to additional competition and will likely increase demands on our service and support operations;” “Due to the global nature of our operations, political or economic changes or other factors in a specific country or region could harm our operating results and financial condition;” “We are exposed to fluctuations in currency exchange rates that could negatively impact our financial results and cash flows;” and “Man-made problems such as cyber-attacks, data protection breaches, malware or terrorism may disrupt our operations, harm our operating results and financial condition, and damage our reputation, and cyber-attacks or data protection breaches on our customers’ networks, in cloud-based services provided by or enabled by us, could result in claims of liability against us, damage our reputation or otherwise harm our business,” among others.

Our service offerings complement our products through a range of consulting, technical, project, quality, and software maintenance services, including 24-hour online and telephone support through technical assistance centers.

### **Financing Arrangements**

We provide financing arrangements for certain qualified customers to build, maintain, and upgrade their networks. We believe customer financing is a competitive advantage in obtaining business, particularly for those customers involved in significant infrastructure projects. Our financing arrangements include the following:

Leases:

- Sales-type
- Direct financing
- Operating

Loans

Financed service contracts

Channels financing arrangements

End-user financing arrangements

### **Product Backlog**

Our product backlog at July 28, 2018 was approximately \$6.6 billion, an increase of 38% year over year. The product backlog includes orders confirmed for products planned to be shipped within 90 days to customers with approved credit status. Subscription-based sales arrangements are not included in product backlog. Our cycle time between order and shipment is generally short and customers occasionally change delivery schedules. Additionally, orders can be canceled without significant penalties. As a result of these factors, we do not believe that our product backlog, as of any particular date, is necessarily indicative of actual product revenue for any future period.

### **Acquisitions, Investments, and Alliances**

The markets in which we compete require a wide variety of technologies, products, and capabilities. Our growth strategy is based on the components of innovation, which we sometimes refer to as “build, buy, partner, invest, and co-develop”. This five-prong approach to how we innovate can be summarized as follows:

<b>Build</b>	Working within Cisco, with the developer community, or with customers
<b>Buy</b>	Acquiring or divesting, depending on goals
<b>Partner</b>	Strategically partnering to further build out the business
<b>Invest</b>	Making investments in areas where technology is in its infancy or where there is no dominant technology
<b>Co-develop</b>	Developing new solutions with multi-party teams that may include customers, channel partners, startups, independent software vendors, and academics

## ***Acquisitions***

We have acquired many companies, and we expect to make future acquisitions. Mergers and acquisitions of high-technology companies are inherently risky, especially if the acquired company has yet to generate revenue. No assurance can be given that our previous or future acquisitions will be successful or will not materially adversely affect our financial condition or operating results. Prior acquisitions have resulted in a wide range of outcomes, from successful introduction of new products and technologies to an inability to do so. The risks associated with acquisitions are more fully discussed in “Item 1A. Risk Factors,” including the risk factor entitled “We have made and expect to continue to make acquisitions that could disrupt our operations and harm our operating results.”

## ***Investments in Privately Held Companies***

We make investments in privately held companies that develop technology or provide services that are complementary to our products or that provide strategic value. The risks associated with these investments are more fully discussed in “Item 1A. Risk Factors,” including the risk factor entitled “We are exposed to fluctuations in the market values of our portfolio investments and in interest rates; impairment of our investments could harm our earnings.”

## ***Strategic Alliances***

We pursue strategic alliances with other companies in areas where collaboration can produce industry advancement and acceleration of new markets. The objectives and goals of a strategic alliance can include one or more of the following: technology exchange, product development, joint sales and marketing, or new market creation. Companies with which we have added or expanded strategic alliances during fiscal 2018 and in recent years include Apple, Google, Salesforce.com and Ericsson, among others.

Companies with which we have strategic alliances in some areas may be competitors in other areas, and in our view this trend may increase. The risks associated with our strategic alliances are more fully discussed in “Item 1A. Risk Factors,” including the risk factor entitled “If we do not successfully manage our strategic alliances, we may not realize the expected benefits from such alliances, and we may experience increased competition or delays in product development.”

## ***Competition***

We compete in the networking and communications equipment markets, providing products and services for transporting data, voice, and video traffic across intranets, extranets, and the Internet. These markets are characterized by rapid change, converging technologies, and a migration to networking and communications solutions that offer relative advantages. These market factors represent both an opportunity, and a competitive threat to us. We compete with numerous vendors in each product category. The overall number of our competitors providing niche product solutions may increase. Also, the identity and composition of competitors may change as we increase our activity in our new product markets. As we continue to expand globally, we may see new competition in different geographic regions. In particular, we have experienced price-focused competition from competitors in Asia, especially from China, and we anticipate this will continue.

Our competitors include Amazon Web Services LLC; Arista Networks, Inc.; ARRIS Group, Inc.; Check Point Software Technologies Ltd.; Dell Technologies Inc.; Extreme Networks, Inc.; F5 Networks, Inc.; FireEye, Inc.; Fortinet, Inc.; Hewlett-Packard Enterprise Company; Huawei Technologies Co., Ltd.; Juniper Networks, Inc.; Lenovo Group Limited; Microsoft Corporation; New Relic, Inc.; Nokia Corporation; Nutanix, Inc.; Palo Alto Networks, Inc.; Symantec Corporation; Ubiquiti Networks and VMware, Inc.; among others.

Some of these companies compete across many of our product lines, while others are primarily focused in a specific product area. Barriers to entry are relatively low, and new ventures to create products that do or could compete with our products are regularly formed. In addition, some of our competitors may have greater resources, including technical and engineering resources, than we do. As we expand into new markets, we will face competition not only from our existing competitors but also from other competitors, including existing companies with strong technological, marketing, and sales positions in those markets. We also sometimes face competition from resellers and distributors of our products. Companies with which we have strategic alliances in some areas may be competitors in other areas, and in our view this trend may increase. For example, the enterprise data center is undergoing a fundamental transformation arising from the convergence of technologies, including computing, networking, storage, and software, that previously were segregated within the data center. Due to several factors, including the availability of highly scalable and general purpose microprocessors, application-specific integrated circuits offering advanced services, standards-based protocols, cloud computing, and virtualization, the convergence of technologies within the enterprise data center is spanning multiple, previously independent, technology segments. Also, some of our current and potential competitors for enterprise data center business have made acquisitions, or announced new strategic alliances, designed to position them to provide end-to-end technology solutions for the enterprise data center. As a result of all of these developments, we face greater competition in the development and sale of enterprise data center technologies, including competition from entities that are

among our long-term strategic alliance partners. Companies that are strategic alliance partners in some areas of our business may acquire or form alliances with our competitors, thereby reducing their business with us.

The principal competitive factors in the markets in which we presently compete and may compete in the future include:

- The ability to sell successful business outcomes
- The ability to provide a broad range of networking and communications products and services
- Product performance
- Price
- The ability to introduce new products, including providing continuous new customer value and products with price-performance advantages
- The ability to reduce production costs
- The ability to provide value-added features such as security, reliability, and investment protection
- Conformance to standards
- Market presence
- The ability to provide financing
- Disruptive technology shifts and new business models

We also face competition from customers to which we license or supply technology, and suppliers from which we transfer technology. The inherent nature of networking requires interoperability. Therefore, we must cooperate and at the same time compete with many companies. Any inability to effectively manage these complicated relationships with customers, suppliers, and strategic alliance partners could have a material adverse effect on our business, operating results, and financial condition and accordingly affect our chances of success.

### **Research and Development**

We regularly introduce new products and features to address the requirements of our markets. We allocate our research and development budget among our product categories, which consist of Infrastructure Platforms, Applications, Security, and Other Product technologies. Our research and development expenditures were \$6.3 billion, \$6.1 billion, and \$6.3 billion in fiscal 2018, 2017, and 2016, respectively. These expenditures are applied generally to all product areas, with specific areas of focus being identified from time to time. Recent areas of increased focus include our intent-based networking technologies (which encompasses switching, routing, and wireless technologies within Infrastructure Platforms), security, and analytics products. Our expenditures for research and development costs were expensed as incurred.

The industry in which we compete is subject to rapid technological developments, evolving standards, changes in customer requirements, and new product introductions and enhancements. As a result, our success depends in part upon our ability, on a cost-effective and timely basis, to continue to enhance our existing products and to develop and introduce new products that improve performance, and reduce total cost of ownership. To achieve these objectives, our management and engineering personnel work with customers to identify and respond to customer needs, as well as with other innovators of Internet working products, including universities, laboratories, and corporations. We also expect to continue to make acquisitions and investments, where appropriate, to provide us with access to new technologies. Nonetheless, there can be no assurance that we will be able to successfully develop products to address new customer requirements and technological changes or that those products will achieve market acceptance.

### **Manufacturing**

We rely on contract manufacturers for all of our manufacturing needs. We presently use a variety of independent third-party companies to provide services related to printed-circuit board assembly, in-circuit test, product repair, and product assembly. Proprietary software on electronically programmable memory chips is used to configure products that meet customer requirements and to maintain quality control and security. The manufacturing process enables us to configure the hardware and software in unique combinations to meet a wide variety of individual customer requirements. The manufacturing process uses automated testing equipment and burn-in procedures, as well as comprehensive inspection, testing, and statistical process controls, which are designed to help ensure the quality and reliability of our products. The manufacturing processes and procedures are generally certified to International Organization for Standardization (ISO) 9001 or ISO 9003 standards.

Our arrangements with contract manufacturers generally provide for quality, cost, and delivery requirements, as well as manufacturing process terms, such as continuity of supply; inventory management; flexibility regarding capacity, quality, and

cost management; oversight of manufacturing; and conditions for use of our intellectual property. We have not entered into any significant long-term contracts with any manufacturing service provider. We generally have the option to renew arrangements on an as-needed basis. These arrangements generally do not commit us to purchase any particular amount or any quantities beyond certain amounts covered by orders or forecasts that we submit covering discrete periods of time, defined as less than one year.

### **Patents, Intellectual Property, and Licensing**

We seek to establish and maintain our proprietary rights in our technology and products through the use of patents, copyrights, trademarks, and trade secret laws. We have a program to file applications for and obtain patents, copyrights, and trademarks in the United States and in selected foreign countries where we believe filing for such protection is appropriate. We also seek to maintain our trade secrets and confidential information by nondisclosure policies and through the use of appropriate confidentiality agreements. We have obtained a substantial number of patents and trademarks in the United States and in other countries. There can be no assurance, however, that the rights obtained can be successfully enforced against infringing products in every jurisdiction. Although we believe the protection afforded by our patents, copyrights, trademarks, and trade secrets has value, the rapidly changing technology in the networking industry and uncertainties in the legal process make our future success dependent primarily on the innovative skills, technological expertise, and management abilities of our employees rather than on the protection afforded by patent, copyright, trademark, and trade secret laws.

Many of our products are designed to include software or other intellectual property licensed from third parties. While it may be necessary in the future to seek or renew licenses relating to various aspects of our products, we believe, based upon past experience and standard industry practice that such licenses generally could be obtained on commercially reasonable terms. Nonetheless, there can be no assurance that the necessary licenses would be available on acceptable terms, if at all. Our inability to obtain certain licenses or other rights or to obtain such licenses or rights on favorable terms, or the need to engage in litigation regarding these matters, could have a material adverse effect on our business, operating results, and financial condition. Moreover, inclusion in our products of software or other intellectual property licensed from third parties on a nonexclusive basis can limit our ability to protect our proprietary rights in our products.

The industry in which we compete is characterized by rapidly changing technology, a large number of patents, and frequent claims and related litigation regarding patent and other intellectual property rights. There can be no assurance that our patents and other proprietary rights will not be challenged, invalidated, or circumvented; that others will not assert intellectual property rights to technologies that are relevant to us; or that our rights will give us a competitive advantage. In addition, the laws of some foreign countries may not protect our proprietary rights to the same extent as the laws of the United States. The risks associated with patents and intellectual property are more fully discussed in "Item 1A. Risk Factors," including the risk factors entitled "Our proprietary rights may prove difficult to enforce," "We may be found to infringe on intellectual property rights of others," and "We rely on the availability of third-party licenses."

### **Employees**

Employees are summarized as follows (approximate numbers):

July 28, 2018

#### Employees by geography:

United States.....	37,800
Rest of world.....	36,400
Total .....	74,200

#### Employees by line item on the Consolidated Statements of Operations:

Cost of sales <sup>(1)</sup> .....	20,200
Research and development.....	21,400
Sales and marketing .....	25,200
General and administrative .....	7,400
Total .....	74,200

<sup>(1)</sup> Cost of sales includes manufacturing support, services, and training.

## **Executive Officers of the Registrant**

The following table shows the name, age, and position as of August 31, 2018 of each of our executive officers:

<u>Name</u>	<u>Age</u>	<u>Position with the Company</u>
Charles H. Robbins .....	52	Chairman and Chief Executive Officer
Mark Chandler .....	62	Executive Vice President, Chief Legal Officer and Chief Compliance Officer
Gerri Elliott .....	62	Executive Vice President and Chief Sales and Marketing Officer
David Goeckeler .....	56	Executive Vice President and General Manager, Security and Networking Business
Kelly A. Kramer .....	51	Executive Vice President and Chief Financial Officer
Maria Martinez .....	60	Executive Vice President and Chief Customer Experience Officer
Irving Tan .....	48	Senior Vice President, Operations

**Mr. Robbins** has served as Chief Executive Officer since July 2015, as a member of the Board of Directors since May 2015 and as Chairman of the Board since December 2017. He joined Cisco in December 1997, from which time until March 2002 he held a number of managerial positions within Cisco's sales organization. Mr. Robbins was promoted to Vice President in March 2002, assuming leadership of Cisco's U.S. channel sales organization. Additionally, in July 2005 he assumed leadership of Cisco's Canada channel sales organization. In December 2007, Mr. Robbins was promoted to Senior Vice President, U.S. Commercial, and in August 2009 he was appointed Senior Vice President, U.S. Enterprise, Commercial and Canada. In July 2011, Mr. Robbins was named Senior Vice President, Americas. In October 2012, Mr. Robbins was promoted to Senior Vice President, Worldwide Field Operations, in which position he served until assuming the role of Chief Executive Officer. He is a member of the board of directors of BlackRock, Inc.

**Mr. Chandler** joined Cisco in July 1996, upon Cisco's acquisition of StrataCom, Inc., where he served as General Counsel. He served as Cisco's Managing Attorney for Europe, the Middle East, and Africa from December 1996 until June 1999; as Director, Worldwide Legal Operations from June 1999 until February 2001; and was promoted to Vice President, Worldwide Legal Services in February 2001. In October 2001, Mr. Chandler was promoted to Vice President, Legal Services and General Counsel, and in May 2003 he additionally was appointed Secretary, a position he held through November 2015. In February 2006, Mr. Chandler was promoted to Senior Vice President, and in May 2012 he was appointed Chief Compliance Officer. In June 2018, Mr. Chandler was promoted to Executive Vice President and Chief Legal Officer. Before joining StrataCom, Mr. Chandler had served as Vice President, Corporate Development and General Counsel of Maxtor Corporation.

**Ms. Elliott** joined Cisco in April 2018. Ms. Elliott is a former Executive Vice President of Juniper Networks, Inc., where she served as EVP and Chief Customer Officer from March 2013 to February 2014, EVP and Chief Sales Officer from July 2011 to March 2013 and EVP, Strategic Alliances from June 2009 to July 2011. Before joining Juniper, Ms. Elliott held a series of senior executive positions with Microsoft Corporation from 2001-2008 including Corporate Vice President of Microsoft's Industry Solutions Group, Worldwide Public Sector and North American Enterprise Sales organizations. Prior to joining Microsoft Corporation, Ms. Elliott spent 22 years at IBM Corporation, where she held several senior executive positions both in the U.S. and internationally. Since 2014 Ms. Elliott has served as a director on several public company boards including Whirlpool Corporation (since 2014), Bed Bath & Beyond, Inc. (2014-17), Imperva, Inc. (2015-18), Marvell Technology Group Ltd. (2017-18) and Mimecast Ltd. (2017-18), and during this period she also founded and led the development of Broadrooms.com, an informational resource for executive women who serve or want to serve on corporate boards in the U.S.

**Mr. Goeckeler** joined Cisco in May 2000, from which time until December 2010 he held a variety of leadership positions within Cisco's engineering organization, covering such technology focus areas as voice over IP, mobility, video infrastructure and networking. In December 2010, Mr. Goeckeler was promoted to Vice President, Engineering, in which his responsibilities included leading various product and platform-related initiatives within Cisco's Service Provider Business group. In October 2012, Mr. Goeckeler assumed leadership of engineering in Cisco's Security Business, and in November 2014 was promoted to Senior Vice President. In March 2016 he was elevated to Senior Vice President and General Manager of the Security Business. In May 2016, Mr. Goeckeler added networking to his oversight responsibilities, assuming the role of Senior Vice President, Networking and Security Business, and was promoted to Executive Vice President in July 2017. In March 2018, Mr. Goeckeler assumed the added responsibility for Cisco's IoT and analytics businesses.

**Ms. Kramer** joined Cisco in January 2012 as Senior Vice President, Corporate Finance. She served in that position until October 2014 and served as Cisco's Senior Vice President, Business Technology and Operations Finance from October 2013 until December 2014. She was appointed to her current position effective January 2015. From January 2009 until she joined Cisco, Ms. Kramer served as Vice President and Chief Financial Officer of GE Healthcare Systems. Ms. Kramer served as Vice President and Chief Financial Officer of GE Healthcare Diagnostic Imaging from August 2007 to January 2009 and as Chief Financial Officer of GE Healthcare Biosciences from January 2006 to July 2007. Prior to that, Ms. Kramer held various leadership positions with GE corporate and other GE businesses. She is a member of the board of directors of Gilead Sciences, Inc.

**Ms. Martinez** joined Cisco in April 2018. Prior to joining Cisco, she served in a variety of senior executive roles at Salesforce.com, inc. including President, Global Customer Success and Latin America from March 2016 to April 2018; President, Sales and Customer Success from February 2013 to March 2016; Executive Vice President and Chief Growth Officer from February 2012 to February 2013; and Executive Vice President, Customers for Life from February 2010 to February 2012. Ms. Martinez's experience prior to Salesforce includes Corporate Vice President of Worldwide Services at Microsoft Corporation, President and Chief Executive Officer of Embrace Networks, Inc. and various senior leadership roles at Motorola, Inc. and AT&T Inc./Bell Laboratories. Ms. Martinez was a member of the board of directors of Plantronics, Inc. from September 2015 to April 2018.

**Mr. Tan** joined Cisco in December 2005, serving in manager-level and director-level positions within Cisco's Sales and Managed Services functions until March 2008, at which time he joined Hewlett Packard Corporation as General Manager of its Communications and Media Solutions Group in Asia Pacific and Japan. In April 2009, Mr. Tan rejoined Cisco, serving as Sales Director in charge of Malaysia and Singapore, and in February 2013 he was promoted to Vice President, Sales with responsibility for the Southeast Asia region. In April 2014, Mr. Tan was promoted to Senior Vice President, Sales with responsibility for Cisco's APJ geography. In January 2018, he was promoted to his current position.

#### **Item 1A. Risk Factors**

Set forth below and elsewhere in this report and in other documents we file with the SEC are descriptions of the risks and uncertainties that could cause our actual results to differ materially from the results contemplated by the forward-looking statements contained in this report.

#### **OUR OPERATING RESULTS MAY FLUCTUATE IN FUTURE PERIODS, WHICH MAY ADVERSELY AFFECT OUR STOCK PRICE**

Our operating results have been in the past, and will continue to be, subject to quarterly and annual fluctuations as a result of numerous factors, some of which may contribute to more pronounced fluctuations in an uncertain global economic environment. These factors include:

- Fluctuations in demand for our products and services, especially with respect to service providers and Internet businesses, in part due to changes in the global economic environment
- Changes in sales and implementation cycles for our products and reduced visibility into our customers' spending plans and associated revenue
- Our ability to maintain appropriate inventory levels and purchase commitments
- Price and product competition in the communications and networking industries, which can change rapidly due to technological innovation and different business models from various geographic regions
- The overall movement toward industry consolidation among both our competitors and our customers
- The introduction and market acceptance of new technologies and products, and our success in new and evolving markets, and in emerging technologies, as well as the adoption of new standards
- The transformation of our business to deliver more software and subscription offerings where revenue is recognized over time
- Variations in sales channels, product costs, mix of products sold, or mix of direct sales and indirect sales
- The timing, size, and mix of orders from customers

- Manufacturing and customer lead times
- Fluctuations in our gross margins, and the factors that contribute to such fluctuations, as described below
- The ability of our customers, channel partners, contract manufacturers and suppliers to obtain financing or to fund capital expenditures, especially during a period of global credit market disruption or in the event of customer, channel partner, contract manufacturer or supplier financial problems
- Actual events, circumstances, outcomes, and amounts differing from judgments, assumptions, and estimates used in determining the values of certain assets (including the amounts of related valuation allowances), liabilities, and other items reflected in our Consolidated Financial Statements
- How well we execute on our strategy and operating plans and the impact of changes in our business model that could result in significant restructuring charges
- Our ability to achieve targeted cost reductions
- Benefits anticipated from our investments in engineering, sales, service, and marketing
- Changes in tax laws or accounting rules, or interpretations thereof

As a consequence, operating results for a particular future period are difficult to predict, and, therefore, prior results are not necessarily indicative of results to be expected in future periods. Any of the foregoing factors, or any other factors discussed elsewhere herein, could have a material adverse effect on our business, results of operations, and financial condition that could adversely affect our stock price.

#### **OUR OPERATING RESULTS MAY BE ADVERSELY AFFECTED BY UNFAVORABLE ECONOMIC AND MARKET CONDITIONS AND THE UNCERTAIN GEOPOLITICAL ENVIRONMENT**

Challenging economic conditions worldwide have from time to time contributed, and may continue to contribute, to slowdowns in the communications and networking industries at large, as well as in specific segments and markets in which we operate, resulting in:

- Reduced demand for our products as a result of continued constraints on IT-related capital spending by our customers, particularly service providers, and other customer markets as well
- Increased price competition for our products, not only from our competitors but also as a consequence of customers disposing of unutilized products
- Risk of excess and obsolete inventories
- Risk of supply constraints
- Risk of excess facilities and manufacturing capacity
- Higher overhead costs as a percentage of revenue and higher interest expense

The global macroeconomic environment has been challenging and inconsistent. Instability in the global credit markets, the impact of uncertainty regarding global central bank monetary policy, the instability in the geopolitical environment in many parts of the world including as a result of the recent United Kingdom “Brexit” referendum to withdraw from the European Union, the current economic challenges in China, including global economic ramifications of Chinese economic difficulties, and other disruptions may continue to put pressure on global economic conditions. If global economic and market conditions, or economic conditions in key markets, remain uncertain or deteriorate further, we may experience material impacts on our business, operating results, and financial condition.

Our operating results in one or more segments may also be affected by uncertain or changing economic conditions particularly germane to that segment or to particular customer markets within that segment. For example, emerging countries in the aggregate experienced a decline in product orders in the first quarter of fiscal 2018, in fiscal 2017 and in certain prior periods.

In addition, reports of certain intelligence gathering methods of the U.S. government could affect customers’ perception of the products of IT companies which design and manufacture products in the United States. Trust and confidence in us as an

IT supplier is critical to the development and growth of our markets. Impairment of that trust, or foreign regulatory actions taken in response to reports of certain intelligence gathering methods of the U.S. government, could affect the demand for our products from customers outside of the United States and could have an adverse effect on our operating results.

**WE HAVE BEEN INVESTING AND EXPECT TO CONTINUE TO INVEST IN KEY PRIORITY AND GROWTH AREAS AS WELL AS MAINTAINING LEADERSHIP IN INFRASTRUCTURE PLATFORMS AND IN SERVICES, AND IF THE RETURN ON THESE INVESTMENTS IS LOWER OR DEVELOPS MORE SLOWLY THAN WE EXPECT, OUR OPERATING RESULTS MAY BE HARMED**

We expect to realign and dedicate resources into key priority and growth areas, such as Security and Applications, while also focusing on maintaining leadership in Infrastructure Platforms and in Services. However, the return on our investments may be lower, or may develop more slowly, than we expect. If we do not achieve the benefits anticipated from these investments (including if our selection of areas for investment does not play out as we expect), or if the achievement of these benefits is delayed, our operating results may be adversely affected.

**OUR REVENUE FOR A PARTICULAR PERIOD IS DIFFICULT TO PREDICT, AND A SHORTFALL IN REVENUE MAY HARM OUR OPERATING RESULTS**

As a result of a variety of factors discussed in this report, our revenue for a particular quarter is difficult to predict, especially in light of a challenging and inconsistent global macroeconomic environment and related market uncertainty.

Our revenue may grow at a slower rate than in past periods or decline as it did in the first quarter of fiscal 2018 and in fiscal 2017 on a year-over-year basis. Our ability to meet financial expectations could also be adversely affected if the nonlinear sales pattern seen in some of our past quarters recurs in future periods. We have experienced periods of time during which shipments have exceeded net bookings or manufacturing issues have delayed shipments, leading to nonlinearity in shipping patterns. In addition to making it difficult to predict revenue for a particular period, nonlinearity in shipping can increase costs, because irregular shipment patterns result in periods of underutilized capacity and periods in which overtime expenses may be incurred, as well as in potential additional inventory management-related costs. In addition, to the extent that manufacturing issues and any related component shortages result in delayed shipments in the future, and particularly in periods in which our contract manufacturers are operating at higher levels of capacity, it is possible that revenue for a quarter could be adversely affected if such matters occur and are not remediated within the same quarter.

The timing of large orders can also have a significant effect on our business and operating results from quarter to quarter, primarily in the United States and in emerging countries. From time to time, we receive large orders that have a significant effect on our operating results in the period in which the order is recognized as revenue. The timing of such orders is difficult to predict, and the timing of revenue recognition from such orders may affect period to period changes in revenue. As a result, our operating results could vary materially from quarter to quarter based on the receipt of such orders and their ultimate recognition as revenue.

Inventory management remains an area of focus. We have experienced longer than normal manufacturing lead times in the past which have caused some customers to place the same order multiple times within our various sales channels and to cancel the duplicative orders upon receipt of the product, or to place orders with other vendors with shorter manufacturing lead times. Such multiple ordering (along with other factors) or risk of order cancellation may cause difficulty in predicting our revenue and, as a result, could impair our ability to manage parts inventory effectively. In addition, our efforts to improve manufacturing lead-time performance may result in corresponding reductions in order backlog. A decline in backlog levels could result in more variability and less predictability in our quarter-to-quarter revenue and operating results. In addition, when facing component supply-related challenges we have increased our efforts in procuring components in order to meet customer expectations, which in turn contribute to an increase in purchase commitments. Increases in our purchase commitments to shorten lead times could also lead to excess and obsolete inventory charges if the demand for our products is less than our expectations.

We plan our operating expense levels based primarily on forecasted revenue levels. These expenses and the impact of long-term commitments are relatively fixed in the short term. A shortfall in revenue could lead to operating results being below expectations because we may not be able to quickly reduce these fixed expenses in response to short-term business changes.

Any of the above factors could have a material adverse impact on our operations and financial results.

**WE EXPECT GROSS MARGIN TO VARY OVER TIME, AND OUR LEVEL OF PRODUCT GROSS MARGIN MAY NOT BE SUSTAINABLE**

Our product gross margins declined on a year-over-year basis and could decline in future quarters due to adverse impacts from various factors, including:

- Changes in customer, geographic, or product mix, including mix of configurations within each product group

- Introduction of new products, including products with price-performance advantages, and new business models including the transformation of our business to deliver more software and subscription offerings
- Our ability to reduce production costs
- Entry into new markets or growth in lower margin markets, including markets with different pricing and cost structures, through acquisitions or internal development
- Sales discounts
- Increases in material, labor or other manufacturing-related costs, which could be significant especially during periods of supply constraints such as those impacting the market for memory components
- Excess inventory and inventory holding charges
- Obsolescence charges
- Changes in shipment volume
- The timing of revenue recognition and revenue deferrals
- Increased cost (including those caused by tariffs), loss of cost savings or dilution of savings due to changes in component pricing or charges incurred due to inventory holding periods if parts ordering does not correctly anticipate product demand or if the financial health of either contract manufacturers or suppliers deteriorates
- Lower than expected benefits from value engineering
- Increased price competition, including competitors from Asia, especially from China
- Changes in distribution channels
- Increased warranty costs
- Increased amortization of purchased intangible assets, especially from acquisitions
- How well we execute on our strategy and operating plans

Changes in service gross margin may result from various factors such as changes in the mix between technical support services and advanced services, as well as the timing of technical support service contract initiations and renewals and the addition of personnel and other resources to support higher levels of service business in future periods.

#### **SALES TO THE SERVICE PROVIDER MARKET ARE ESPECIALLY VOLATILE, AND WEAKNESS IN ORDERS FROM THIS INDUSTRY MAY HARM OUR OPERATING RESULTS AND FINANCIAL CONDITION**

Sales to the service provider market have been characterized by large and sporadic purchases, especially relating to our router sales and sales of certain other Infrastructure Platforms and Applications products, in addition to longer sales cycles. Although product orders from the service provider market increased in the fourth quarter of fiscal 2018, service provider product orders decreased in the first nine months of fiscal 2018 and in fiscal 2017, and at various times in the past we have experienced significant weakness in product orders from service providers. Product orders from the service provider market could continue to decline and, as has been the case in the past, such weakness could persist over extended periods of time given fluctuating market conditions. Sales activity in this industry depends upon the stage of completion of expanding network infrastructures; the availability of funding; and the extent to which service providers are affected by regulatory, economic, and business conditions in the country of operations. Weakness in orders from this industry, including as a result of any slowdown in capital expenditures by service providers (which may be more prevalent during a global economic downturn, or periods of economic, political or regulatory uncertainty), could have a material adverse effect on our business, operating results, and financial condition. Such slowdowns may continue or recur in future periods. Orders from this industry could decline for many reasons other than the competitiveness of our products and services within their respective markets. For example, in the past, many of our service provider customers have been materially and adversely affected by slowdowns in the general economy, by overcapacity, by changes in the service provider market, by regulatory developments, and by constraints on capital availability, resulting in business failures and substantial reductions in spending and expansion plans. These conditions have materially harmed our business and operating results in the past, and some of these or other conditions in the service provider market could affect our

business and operating results in any future period. Finally, service provider customers typically have longer implementation cycles; require a broader range of services, including design services; demand that vendors take on a larger share of risks; often require acceptance provisions, which can lead to a delay in revenue recognition; and expect financing from vendors. All these factors can add further risk to business conducted with service providers.

## **DISRUPTION OF OR CHANGES IN OUR DISTRIBUTION MODEL COULD HARM OUR SALES AND MARGINS**

If we fail to manage distribution of our products and services properly, or if our distributors' financial condition or operations weaken, our revenue and gross margins could be adversely affected.

A substantial portion of our products and services is sold through our channel partners, and the remainder is sold through direct sales. Our channel partners include systems integrators, service providers, other resellers, and distributors. Systems integrators and service providers typically sell directly to end users and often provide system installation, technical support, professional services, and other support services in addition to network equipment sales. Systems integrators also typically integrate our products into an overall solution, and a number of service providers are also systems integrators. Distributors stock inventory and typically sell to systems integrators, service providers, and other resellers. We refer to sales through distributors as our two-tier system of sales to the end customer. Revenue from distributors is generally recognized based on a sell-through method using information provided by them. These distributors are generally given business terms that allow them to return a portion of inventory, receive credits for changes in selling prices, and participate in various cooperative marketing programs. If sales through indirect channels increase, this may lead to greater difficulty in forecasting the mix of our products and, to a degree, the timing of orders from our customers.

Historically, we have seen fluctuations in our gross margins based on changes in the balance of our distribution channels. Although variability to date has not been significant, there can be no assurance that changes in the balance of our distribution model in future periods would not have an adverse effect on our gross margins and profitability.

Some factors could result in disruption of or changes in our distribution model, which could harm our sales and margins, including the following:

- We compete with some of our channel partners, including through our direct sales, which may lead these channel partners to use other suppliers that do not directly sell their own products or otherwise compete with them
- Some of our channel partners may demand that we absorb a greater share of the risks that their customers may ask them to bear
- Some of our channel partners may have insufficient financial resources and may not be able to withstand changes and challenges in business conditions
- Revenue from indirect sales could suffer if our distributors' financial condition or operations weaken

In addition, we depend on our channel partners globally to comply with applicable regulatory requirements. To the extent that they fail to do so, that could have a material adverse effect on our business, operating results, and financial condition. Further, sales of our products outside of agreed territories can result in disruption to our distribution channels.

## **THE MARKETS IN WHICH WE COMPETE ARE INTENSELY COMPETITIVE, WHICH COULD ADVERSELY AFFECT OUR ACHIEVEMENT OF REVENUE GROWTH**

The markets in which we compete are characterized by rapid change, converging technologies, and a migration to networking and communications solutions that offer relative advantages. These market factors represent a competitive threat to us. We compete with numerous vendors in each product category. The overall number of our competitors providing niche product solutions may increase. Also, the identity and composition of competitors may change as we increase our activity in newer product areas, and in key priority and growth areas. For example, as products related to network programmability, such as SDN products, become more prevalent, we expect to face increased competition from companies that develop networking products based on commoditized hardware, referred to as "white box" hardware, to the extent customers decide to purchase those product offerings instead of ours. In addition, the growth in demand for technology delivered as a service enables new competitors to enter the market.

As we continue to expand globally, we may see new competition in different geographic regions. In particular, we have experienced price-focused competition from competitors in Asia, especially from China, and we anticipate this will continue. For information regarding our competitors, see the section entitled "Competition" contained in *Item 1. Business* of this report.

Some of our competitors compete across many of our product lines, while others are primarily focused in a specific product area. Barriers to entry are relatively low, and new ventures to create products that do or could compete with our products are regularly formed. In addition, some of our competitors may have greater resources, including technical and engineering resources, than we do. As we expand into new markets, we will face competition not only from our existing competitors but also from other competitors, including existing companies with strong technological, marketing, and sales positions in those markets. We also sometimes face competition from resellers and distributors of our products. Companies with which we have strategic alliances in some areas may be competitors in other areas, and in our view this trend may increase.

For example, the enterprise data center is undergoing a fundamental transformation arising from the convergence of technologies, including computing, networking, storage, and software, that previously were segregated. Due to several factors, including the availability of highly scalable and general purpose microprocessors, ASICs offering advanced services, standards based protocols, cloud computing and virtualization, the convergence of technologies within the enterprise data center is spanning multiple, previously independent, technology segments. Also, some of our current and potential competitors for enterprise data center business have made acquisitions, or announced new strategic alliances, designed to position them to provide end-to-end technology solutions for the enterprise data center. As a result of all of these developments, we face greater competition in the development and sale of enterprise data center technologies, including competition from entities that are among our long-term strategic alliance partners. Companies that are strategic alliance partners in some areas of our business may acquire or form alliances with our competitors, thereby reducing their business with us.

The principal competitive factors in the markets in which we presently compete and may compete in the future include:

- The ability to sell successful business outcomes
- The ability to provide a broad range of networking and communications products and services
- Product performance
- Price
- The ability to introduce new products, including providing continuous new customer value and products with price-performance advantages
- The ability to reduce production costs
- The ability to provide value-added features such as security, reliability, and investment protection
- Conformance to standards
- Market presence
- The ability to provide financing
- Disruptive technology shifts and new business models

We also face competition from customers to which we license or supply technology and suppliers from which we transfer technology. The inherent nature of networking requires interoperability. As such, we must cooperate and at the same time compete with many companies. Any inability to effectively manage these complicated relationships with customers, suppliers, and strategic alliance partners could have a material adverse effect on our business, operating results, and financial condition and accordingly affect our chances of success.

#### **OUR INVENTORY MANAGEMENT RELATING TO OUR SALES TO OUR TWO-TIER DISTRIBUTION CHANNEL IS COMPLEX, AND EXCESS INVENTORY MAY HARM OUR GROSS MARGINS**

We must manage our inventory relating to sales to our distributors effectively, because inventory held by them could affect our results of operations. Our distributors may increase orders during periods of product shortages, cancel orders if their inventory is too high, or delay orders in anticipation of new products. They also may adjust their orders in response to the supply of our products and the products of our competitors that are available to them, and in response to seasonal fluctuations in end-user demand. Revenue to our distributors generally is recognized based on a sell-through method using information provided by them, and they are generally given business terms that allow them to return a portion of inventory, receive credits for changes in selling price, and participate in various cooperative marketing programs. Inventory management remains an area of focus as we balance the need to maintain strategic inventory levels to ensure competitive lead times against the risk of inventory

obsolescence because of rapidly changing technology and customer requirements. When facing component supply-related challenges, we have increased our efforts in procuring components in order to meet customer expectations. If we ultimately determine that we have excess inventory, we may have to reduce our prices and write down inventory, which in turn could result in lower gross margins.

**SUPPLY CHAIN ISSUES, INCLUDING FINANCIAL PROBLEMS OF CONTRACT MANUFACTURERS OR COMPONENT SUPPLIERS, OR A SHORTAGE OF ADEQUATE COMPONENT SUPPLY OR MANUFACTURING CAPACITY THAT INCREASED OUR COSTS OR CAUSED A DELAY IN OUR ABILITY TO FULFILL ORDERS, COULD HAVE AN ADVERSE IMPACT ON OUR BUSINESS AND OPERATING RESULTS, AND OUR FAILURE TO ESTIMATE CUSTOMER DEMAND PROPERLY MAY RESULT IN EXCESS OR OBSOLETE COMPONENT SUPPLY, WHICH COULD ADVERSELY AFFECT OUR GROSS MARGINS**

The fact that we do not own or operate the bulk of our manufacturing facilities and that we are reliant on our extended supply chain could have an adverse impact on the supply of our products and on our business and operating results:

- Any financial problems of either contract manufacturers or component suppliers could either limit supply or increase costs
- Reservation of manufacturing capacity at our contract manufacturers by other companies, inside or outside of our industry, could either limit supply or increase costs
- Industry consolidation occurring within one or more component supplier markets, such as the semiconductor market, could either limit supply or increase costs

A reduction or interruption in supply; a significant increase in the price of one or more components; a failure to adequately authorize procurement of inventory by our contract manufacturers; a failure to appropriately cancel, reschedule, or adjust our requirements based on our business needs; or a decrease in demand for our products could materially adversely affect our business, operating results, and financial condition and could materially damage customer relationships. Furthermore, as a result of binding price or purchase commitments with suppliers, we may be obligated to purchase components at prices that are higher than those available in the current market. In the event that we become committed to purchase components at prices in excess of the current market price when the components are actually used, our gross margins could decrease. We have experienced longer than normal lead times in the past. Although we have generally secured additional supply or taken other mitigation actions when significant disruptions have occurred, if similar situations occur in the future, they could have a material adverse effect on our business, results of operations, and financial condition. See the risk factor above entitled “Our revenue for a particular period is difficult to predict, and a shortfall in revenue may harm our operating results.”

Our growth and ability to meet customer demands depend in part on our ability to obtain timely deliveries of parts from our suppliers and contract manufacturers. We have experienced component shortages in the past, including shortages caused by manufacturing process issues, that have affected our operations. We may in the future experience a shortage of certain component parts as a result of our own manufacturing issues, manufacturing issues at our suppliers or contract manufacturers, capacity problems experienced by our suppliers or contract manufacturers including capacity or cost problems resulting from industry consolidation, or strong demand in the industry for those parts. Growth in the economy is likely to create greater pressures on us and our suppliers to accurately project overall component demand and component demands within specific product categories and to establish optimal component levels and manufacturing capacity, especially for labor-intensive components, components for which we purchase a substantial portion of the supply, or the re-ramping of manufacturing capacity for highly complex products. During periods of shortages or delays the price of components may increase, or the components may not be available at all, and we may also encounter shortages if we do not accurately anticipate our needs. We may not be able to secure enough components at reasonable prices or of acceptable quality to build new products in a timely manner in the quantities or configurations needed. Accordingly, our revenue and gross margins could suffer until other sources can be developed. Our operating results would also be adversely affected if, anticipating greater demand than actually develops, we commit to the purchase of more components than we need, which is more likely to occur in a period of demand uncertainties such as we are currently experiencing. There can be no assurance that we will not encounter these problems in the future. Although in many cases we use standard parts and components for our products, certain components are presently available only from a single source or limited sources, and a global economic downturn and related market uncertainty could negatively impact the availability of components from one or more of these sources, especially during times such as we have recently seen when there are supplier constraints based on labor and other actions taken during economic downturns. We may not be able to diversify sources in a timely manner, which could harm our ability to deliver products to customers and seriously impact present and future sales.

We believe that we may be faced with the following challenges in the future:

- New markets in which we participate may grow quickly, which may make it difficult to quickly obtain significant component capacity
- As we acquire companies and new technologies, we may be dependent, at least initially, on unfamiliar supply chains or relatively small supply partners
- We face competition for certain components that are supply-constrained, from existing competitors, and companies in other markets

Manufacturing capacity and component supply constraints could continue to be significant issues for us. We purchase components from a variety of suppliers and use several contract manufacturers to provide manufacturing services for our products. During the normal course of business, in order to improve manufacturing lead-time performance and to help ensure adequate component supply, we enter into agreements with contract manufacturers and suppliers that either allow them to procure inventory based upon criteria as defined by us or that establish the parameters defining our requirements. In certain instances, these agreements allow us the option to cancel, reschedule, and adjust our requirements based on our business needs prior to firm orders being placed. When facing component supply-related challenges we have increased our efforts in procuring components in order to meet customer expectations, which in turn contributes to an increase in purchase commitments. Increases in our purchase commitments to shorten lead times could also lead to excess and obsolete inventory charges if the demand for our products is less than our expectations. If we fail to anticipate customer demand properly, an oversupply of parts could result in excess or obsolete components that could adversely affect our gross margins. For additional information regarding our purchase commitments with contract manufacturers and suppliers, see Note 12 to the Consolidated Financial Statements.

**WE DEPEND UPON THE DEVELOPMENT OF NEW PRODUCTS AND ENHANCEMENTS TO EXISTING PRODUCTS, AND IF WE FAIL TO PREDICT AND RESPOND TO EMERGING TECHNOLOGICAL TRENDS AND CUSTOMERS' CHANGING NEEDS, OUR OPERATING RESULTS AND MARKET SHARE MAY SUFFER**

The markets for our products are characterized by rapidly changing technology, evolving industry standards, new product introductions, and evolving methods of building and operating networks. Our operating results depend on our ability to develop and introduce new products into existing and emerging markets and to reduce the production costs of existing products. Many of our strategic initiatives and investments we have made, and our architectural approach, are designed to enable the increased use of the network as the platform for automating, orchestrating, integrating, and delivering an ever-increasing array of IT-based products and services. For example, in June 2017 we announced our Catalyst 9000 series of switches which represent the initial foundation of our intent-based networking capabilities. Other current initiatives include our focus on security; the market transition related to digital transformation and IoT; the transition in cloud; and the move towards more programmable, flexible and virtual networks.

The process of developing new technology, including intent-based networking, more programmable, flexible and virtual networks, and technology related to other market transitions—such as security, digital transformation and IoT, and cloud—is complex and uncertain, and if we fail to accurately predict customers' changing needs and emerging technological trends our business could be harmed. We must commit significant resources, including the investments we have been making in our priorities to developing new products before knowing whether our investments will result in products the market will accept. In particular, if our model of the evolution of networking does not emerge as we believe it will, or if the industry does not evolve as we believe it will, or if our strategy for addressing this evolution is not successful, many of our strategic initiatives and investments may be of no or limited value. For example, if we do not introduce products related to network programmability, such as software-defined-networking products, in a timely fashion, or if product offerings in this market that ultimately succeed are based on technology, or an approach to technology, that differs from ours, such as, for example, networking products based on "white box" hardware, our business could be harmed. Similarly, our business could be harmed if we fail to develop, or fail to develop in a timely fashion, offerings to address other transitions, or if the offerings addressing these other transitions that ultimately succeed are based on technology, or an approach to technology, different from ours. In addition, our business could be adversely affected in periods surrounding our new product introductions if customers delay purchasing decisions to qualify or otherwise evaluate the new product offerings.

Our strategy is to lead our customers in their digital transition with solutions that deliver greater agility, productivity, security and other advanced network capabilities, and that intelligently connect nearly everything that can be connected. Over the last few years, we have been transforming our business to move from selling individual products and services to selling products and services integrated into architectures and solutions, and we are seeking to meet the evolving needs of customers which include offering our products and solutions in the manner in which customers wish to consume them. As a part of this transformation, we continue to make changes to how we are organized and how we build and deliver our technology, including changes in our business models with customers. If our strategy for addressing our customer needs, or the architectures and solutions we develop

do not meet those needs, or the changes we are making in how we are organized and how we build and deliver our technology is incorrect or ineffective, our business could be harmed.

Furthermore, we may not execute successfully on our vision or strategy because of challenges with regard to product planning and timing, technical hurdles that we fail to overcome in a timely fashion, or a lack of appropriate resources. This could result in competitors, some of which may also be our strategic alliance partners, providing those solutions before we do and loss of market share, revenue, and earnings. In addition, the growth in demand for technology delivered as a service enables new competitors to enter the market. The success of new products depends on several factors, including proper new product definition, component costs, timely completion and introduction of these products, differentiation of new products from those of our competitors, and market acceptance of these products. There can be no assurance that we will successfully identify new product opportunities, develop and bring new products to market in a timely manner, or achieve market acceptance of our products or that products and technologies developed by others will not render our products or technologies obsolete or noncompetitive. The products and technologies in our other product categories and key priority and growth areas may not prove to have the market success we anticipate, and we may not successfully identify and invest in other emerging or new products.

**CHANGES IN INDUSTRY STRUCTURE AND MARKET CONDITIONS COULD LEAD TO CHARGES RELATED TO DISCONTINUANCES OF CERTAIN OF OUR PRODUCTS OR BUSINESSES, ASSET IMPAIRMENTS AND WORKFORCE REDUCTIONS OR RESTRUCTURINGS**

In response to changes in industry and market conditions, we may be required to strategically realign our resources and to consider restructuring, disposing of, or otherwise exiting businesses. Any resource realignment, or decision to limit investment in or dispose of or otherwise exit businesses, may result in the recording of special charges, such as inventory and technology-related write-offs, workforce reduction or restructuring costs, charges relating to consolidation of excess facilities, or claims from third parties who were resellers or users of discontinued products. Our estimates with respect to the useful life or ultimate recoverability of our carrying basis of assets, including purchased intangible assets, could change as a result of such assessments and decisions. Although in certain instances our supply agreements allow us the option to cancel, reschedule, and adjust our requirements based on our business needs prior to firm orders being placed, our loss contingencies may include liabilities for contracts that we cannot cancel with contract manufacturers and suppliers. Further, our estimates relating to the liabilities for excess facilities are affected by changes in real estate market conditions. Additionally, we are required to perform goodwill impairment tests on an annual basis and between annual tests in certain circumstances, and future goodwill impairment tests may result in a charge to earnings.

We initiated a restructuring plan in the third quarter of fiscal 2018. The implementation of this restructuring plan may be disruptive to our business, and following completion of the restructuring plan our business may not be more efficient or effective than prior to implementation of the plan. Our restructuring activities, including any related charges and the impact of the related headcount restructurings, could have a material adverse effect on our business, operating results, and financial condition.

**OVER THE LONG TERM WE INTEND TO INVEST IN ENGINEERING, SALES, SERVICE AND MARKETING ACTIVITIES, AND THESE INVESTMENTS MAY ACHIEVE DELAYED, OR LOWER THAN EXPECTED, BENEFITS WHICH COULD HARM OUR OPERATING RESULTS**

While we intend to focus on managing our costs and expenses, over the long term, we also intend to invest in personnel and other resources related to our engineering, sales, service and marketing functions as we realign and dedicate resources on key priority and growth areas, such as Security and Applications, and we also intend to focus on maintaining leadership in Infrastructure Platforms and in Services. We are likely to recognize the costs associated with these investments earlier than some of the anticipated benefits, and the return on these investments may be lower, or may develop more slowly, than we expect. If we do not achieve the benefits anticipated from these investments, or if the achievement of these benefits is delayed, our operating results may be adversely affected.

**OUR BUSINESS SUBSTANTIALLY DEPENDS UPON THE CONTINUED GROWTH OF THE INTERNET AND INTERNET-BASED SYSTEMS**

A substantial portion of our business and revenue depends on growth and evolution of the Internet, including the continued development of the Internet and the anticipated market transitions, and on the deployment of our products by customers who depend on such continued growth and evolution. To the extent that an economic slowdown or uncertainty and related reduction in capital spending adversely affect spending on Internet infrastructure, including spending or investment related to anticipated market transitions, we could experience material harm to our business, operating results, and financial condition.

Because of the rapid introduction of new products and changing customer requirements related to matters such as cost-effectiveness and security, we believe that there could be performance problems with Internet communications in the future, which could receive a high degree of publicity and visibility. Because we are a large supplier of networking products, our

business, operating results, and financial condition may be materially adversely affected, regardless of whether or not these problems are due to the performance of our own products. Such an event could also result in a material adverse effect on the market price of our common stock independent of direct effects on our business.

## **WE HAVE MADE AND EXPECT TO CONTINUE TO MAKE ACQUISITIONS THAT COULD DISRUPT OUR OPERATIONS AND HARM OUR OPERATING RESULTS**

Our growth depends upon market growth, our ability to enhance our existing products, and our ability to introduce new products on a timely basis. We intend to continue to address the need to develop new products and enhance existing products through acquisitions of other companies, product lines, technologies, and personnel. Acquisitions involve numerous risks, including the following:

- Difficulties in integrating the operations, systems, technologies, products, and personnel of the acquired companies, particularly companies with large and widespread operations and/or complex products
- Diversion of management's attention from normal daily operations of the business and the challenges of managing larger and more widespread operations resulting from acquisitions
- Potential difficulties in completing projects associated with in-process research and development intangibles
- Difficulties in entering markets in which we have no or limited direct prior experience and where competitors in such markets have stronger market positions
- Initial dependence on unfamiliar supply chains or relatively small supply partners
- Insufficient revenue to offset increased expenses associated with acquisitions
- The potential loss of key employees, customers, distributors, vendors and other business partners of the companies we acquire following and continuing after announcement of acquisition plans

Acquisitions may also cause us to:

- Issue common stock that would dilute our current shareholders' percentage ownership
- Use a substantial portion of our cash resources, or incur debt
- Significantly increase our interest expense, leverage and debt service requirements if we incur additional debt to pay for an acquisition
- Assume liabilities
- Record goodwill and intangible assets that are subject to impairment testing on a regular basis and potential periodic impairment charges
- Incur amortization expenses related to certain intangible assets
- Incur tax expenses related to the effect of acquisitions on our legal structure
- Incur large and immediate write-offs and restructuring and other related expenses
- Become subject to intellectual property or other litigation

Mergers and acquisitions of high-technology companies are inherently risky and subject to many factors outside of our control, and no assurance can be given that our previous or future acquisitions will be successful and will not materially adversely affect our business, operating results, or financial condition. Failure to manage and successfully integrate acquisitions could materially harm our business and operating results. Prior acquisitions have resulted in a wide range of outcomes, from successful introduction of new products and technologies to a failure to do so. Even when an acquired company has already developed and marketed products, there can be no assurance that product enhancements will be made in a timely fashion or that pre-acquisition due diligence will have identified all possible issues that might arise with respect to such products.

From time to time, we have made acquisitions that resulted in charges in an individual quarter. These charges may occur in any particular quarter, resulting in variability in our quarterly earnings. In addition, our effective tax rate for future periods is uncertain and could be impacted by mergers and acquisitions. Risks related to new product development also apply to acquisitions. See the risk factors above, including the risk factor entitled "We depend upon the development of new products

and enhancements to existing products, and if we fail to predict and respond to emerging technological trends and customers' changing needs, our operating results and market share may suffer" for additional information.

## **ENTRANCE INTO NEW OR DEVELOPING MARKETS EXPOSES US TO ADDITIONAL COMPETITION AND WILL LIKELY INCREASE DEMANDS ON OUR SERVICE AND SUPPORT OPERATIONS**

As we focus on new market opportunities and key priority and growth areas, we will increasingly compete with large telecommunications equipment suppliers as well as startup companies. Several of our competitors may have greater resources, including technical and engineering resources, than we do. Additionally, as customers in these markets complete infrastructure deployments, they may require greater levels of service, support, and financing than we have provided in the past, especially in emerging countries. Demand for these types of service, support, or financing contracts may increase in the future. There can be no assurance that we can provide products, service, support, and financing to effectively compete for these market opportunities.

Further, provision of greater levels of services, support and financing by us may result in a delay in the timing of revenue recognition. In addition, entry into other markets has subjected and will subject us to additional risks, particularly to those markets, including the effects of general market conditions and reduced consumer confidence. For example, as we add direct selling capabilities globally to meet changing customer demands, we will face increased legal and regulatory requirements.

## **INDUSTRY CONSOLIDATION MAY LEAD TO INCREASED COMPETITION AND MAY HARM OUR OPERATING RESULTS**

There has been a trend toward industry consolidation in our markets for several years. We expect this trend to continue as companies attempt to strengthen or hold their market positions in an evolving industry and as companies are acquired or are unable to continue operations. For example, some of our current and potential competitors for enterprise data center business have made acquisitions, or announced new strategic alliances, designed to position them with the ability to provide end-to-end technology solutions for the enterprise data center. Companies that are strategic alliance partners in some areas of our business may acquire or form alliances with our competitors, thereby reducing their business with us. We believe that industry consolidation may result in stronger competitors that are better able to compete as sole-source vendors for customers. This could lead to more variability in our operating results and could have a material adverse effect on our business, operating results, and financial condition. Furthermore, particularly in the service provider market, rapid consolidation will lead to fewer customers, with the effect that loss of a major customer could have a material impact on results not anticipated in a customer marketplace composed of more numerous participants.

## **PRODUCT QUALITY PROBLEMS COULD LEAD TO REDUCED REVENUE, GROSS MARGINS, AND NET INCOME**

We produce highly complex products that incorporate leading-edge technology, including both hardware and software. Software typically contains bugs that can unexpectedly interfere with expected operations. There can be no assurance that our pre-shipment testing programs will be adequate to detect all defects, either ones in individual products or ones that could affect numerous shipments, which might interfere with customer satisfaction, reduce sales opportunities, or affect gross margins. From time to time, we have had to replace certain components and provide remediation in response to the discovery of defects or bugs in products that we had shipped. There can be no assurance that such remediation, depending on the product involved, would not have a material impact. An inability to cure a product defect could result in the failure of a product line, temporary or permanent withdrawal from a product or market, damage to our reputation, inventory costs, or product reengineering expenses, any of which could have a material impact on our revenue, margins, and net income. For example, in the second quarter of fiscal 2017 we recorded a charge to product cost of sales of \$125 million related to the expected remediation costs for anticipated failures in future periods of a widely-used component sourced from a third party which is included in several of our products, and in the second quarter of fiscal 2014 we recorded a pre-tax charge of \$655 million related to the expected remediation costs for certain products sold in prior fiscal years containing memory components manufactured by a single supplier between 2005 and 2010.

## **DUE TO THE GLOBAL NATURE OF OUR OPERATIONS, POLITICAL OR ECONOMIC CHANGES OR OTHER FACTORS IN A SPECIFIC COUNTRY OR REGION COULD HARM OUR OPERATING RESULTS AND FINANCIAL CONDITION**

We conduct significant sales and customer support operations in countries around the world. As such, our growth depends in part on our increasing sales into emerging countries. We also depend on non-U.S. operations of our contract manufacturers, component suppliers and distribution partners. Emerging countries in the aggregate experienced a decline in orders in the first quarter of fiscal 2018, in fiscal 2017 and in certain prior periods. We continue to assess the sustainability of any improvements in these countries and there can be no assurance that our investments in these countries will be successful. Our future results could be materially adversely affected by a variety of political, economic or other factors relating to our operations inside and outside the United States, including impacts from global central bank monetary policy; issues related to the political relationship between the United States and other countries that can affect the willingness of customers in those countries to purchase

products from companies headquartered in the United States; and the challenging and inconsistent global macroeconomic environment, any or all of which could have a material adverse effect on our operating results and financial condition, including, among others, the following:

- Foreign currency exchange rates
- Political or social unrest
- Economic instability or weakness or natural disasters in a specific country or region, including the current economic challenges in China and global economic ramifications of Chinese economic difficulties; instability as a result of Brexit; environmental protection measures, trade protection measures such as tariffs, and other legal and regulatory requirements, some of which may affect our ability to import our products, to export our products from, or sell our products in various countries
- Political considerations that affect service provider and government spending patterns
- Health or similar issues, such as a pandemic or epidemic
- Difficulties in staffing and managing international operations
- Adverse tax consequences, including imposition of withholding or other taxes on our global operations

#### **WE ARE EXPOSED TO THE CREDIT RISK OF SOME OF OUR CUSTOMERS AND TO CREDIT EXPOSURES IN WEAKENED MARKETS, WHICH COULD RESULT IN MATERIAL LOSSES**

Most of our sales are on an open credit basis, with typical payment terms of 30 days in the United States and, because of local customs or conditions, longer in some markets outside the United States. We monitor individual customer payment capability in granting such open credit arrangements, seek to limit such open credit to amounts we believe the customers can pay, and maintain reserves we believe are adequate to cover exposure for doubtful accounts. Beyond our open credit arrangements, we have also experienced demands for customer financing and facilitation of leasing arrangements. We expect demand for customer financing to continue, and recently we have been experiencing an increase in this demand as the credit markets have been impacted by the challenging and inconsistent global macroeconomic environment, including increased demand from customers in certain emerging countries.

We believe customer financing is a competitive factor in obtaining business, particularly in serving customers involved in significant infrastructure projects. Our loan financing arrangements may include not only financing the acquisition of our products and services but also providing additional funds for other costs associated with network installation and integration of our products and services.

Our exposure to the credit risks relating to our financing activities described above may increase if our customers are adversely affected by a global economic downturn or periods of economic uncertainty. Although we have programs in place that are designed to monitor and mitigate the associated risk, including monitoring of particular risks in certain geographic areas, there can be no assurance that such programs will be effective in reducing our credit risks.

In the past, there have been significant bankruptcies among customers both on open credit and with loan or lease financing arrangements, particularly among Internet businesses and service providers, causing us to incur economic or financial losses. There can be no assurance that additional losses will not be incurred. Although these losses have not been material to date, future losses, if incurred, could harm our business and have a material adverse effect on our operating results and financial condition. A portion of our sales is derived through our distributors. These distributors are generally given business terms that allow them to return a portion of inventory, receive credits for changes in selling prices, and participate in various cooperative marketing programs. We maintain estimated accruals and allowances for such business terms. However, distributors tend to have more limited financial resources than other resellers and end-user customers and therefore represent potential sources of increased credit risk, because they may be more likely to lack the reserve resources to meet payment obligations. Additionally, to the degree that turmoil in the credit markets makes it more difficult for some customers to obtain financing, those customers' ability to pay could be adversely impacted, which in turn could have a material adverse impact on our business, operating results, and financial condition.

#### **WE ARE EXPOSED TO FLUCTUATIONS IN THE MARKET VALUES OF OUR PORTFOLIO INVESTMENTS AND IN INTEREST RATES; IMPAIRMENT OF OUR INVESTMENTS COULD HARM OUR EARNINGS**

We maintain an investment portfolio of various holdings, types, and maturities. These securities are generally classified as available-for-sale and, consequently, are recorded on our Consolidated Balance Sheets at fair value with unrealized gains or losses reported as a component of accumulated other comprehensive income (loss), net of tax. Our portfolio includes fixed income securities and equity investments in publicly traded companies, the values of which are subject to market price volatility to the extent unhedged. If such investments suffer market price declines, as we experienced with some of our investments in

the past, we may recognize in earnings the decline in the fair value of our investments below their cost basis when the decline is judged to be other than temporary. For information regarding the sensitivity of and risks associated with the market value of portfolio investments and interest rates, refer to the section titled “Quantitative and Qualitative Disclosures About Market Risk.” Our investments in private companies are subject to risk of loss of investment capital. These investments are inherently risky because the markets for the technologies or products they have under development are typically in the early stages and may never materialize. We could lose our entire investment in these companies.

### **WE ARE EXPOSED TO FLUCTUATIONS IN CURRENCY EXCHANGE RATES THAT COULD NEGATIVELY IMPACT OUR FINANCIAL RESULTS AND CASH FLOWS**

Because a significant portion of our business is conducted outside the United States, we face exposure to adverse movements in foreign currency exchange rates. These exposures may change over time as business practices evolve, and they could have a material adverse impact on our financial results and cash flows. Historically, our primary exposures have related to nondollar-denominated sales in Japan, Canada, and Australia and certain nondollar-denominated operating expenses and service cost of sales in Europe, Latin America, and Asia, where we sell primarily in U.S. dollars. Additionally, we have exposures to emerging market currencies, which can have extreme currency volatility. An increase in the value of the dollar could increase the real cost to our customers of our products in those markets outside the United States where we sell in dollars and a weakened dollar could increase the cost of local operating expenses and procurement of raw materials to the extent that we must purchase components in foreign currencies.

Currently, we enter into foreign exchange forward contracts and options to reduce the short-term impact of foreign currency fluctuations on certain foreign currency receivables, investments, and payables. In addition, we periodically hedge anticipated foreign currency cash flows. Our attempts to hedge against these risks may result in an adverse impact on our net income.

### **OUR PROPRIETARY RIGHTS MAY PROVE DIFFICULT TO ENFORCE**

We generally rely on patents, copyrights, trademarks, and trade secret laws to establish and maintain proprietary rights in our technology and products. Although we have been issued numerous patents and other patent applications are currently pending, there can be no assurance that any of these patents or other proprietary rights will not be challenged, invalidated, or circumvented or that our rights will, in fact, provide competitive advantages to us. Furthermore, many key aspects of networking technology are governed by industrywide standards, which are usable by all market entrants. In addition, there can be no assurance that patents will be issued from pending applications or that claims allowed on any patents will be sufficiently broad to protect our technology. In addition, the laws of some foreign countries may not protect our proprietary rights to the same extent as do the laws of the United States. The outcome of any actions taken in these foreign countries may be different than if such actions were determined under the laws of the United States. Although we are not dependent on any individual patents or group of patents for particular segments of the business for which we compete, if we are unable to protect our proprietary rights to the totality of the features (including aspects of products protected other than by patent rights) in a market, we may find ourselves at a competitive disadvantage to others who need not incur the substantial expense, time, and effort required to create innovative products that have enabled us to be successful.

### **WE MAY BE FOUND TO INFRINGE ON INTELLECTUAL PROPERTY RIGHTS OF OTHERS**

Third parties, including customers, have in the past and may in the future assert claims or initiate litigation related to exclusive patent, copyright, trademark, and other intellectual property rights to technologies and related standards that are relevant to us. These assertions have increased over time as a result of our growth and the general increase in the pace of patent claims assertions, particularly in the United States. Because of the existence of a large number of patents in the networking field, the secrecy of some pending patents, and the rapid rate of issuance of new patents, it is not economically practical or even possible to determine in advance whether a product or any of its components infringes or will infringe on the patent rights of others. The asserted claims and/or initiated litigation can include claims against us or our manufacturers, suppliers, or customers, alleging infringement of their proprietary rights with respect to our existing or future products or components of those products. Regardless of the merit of these claims, they can be time-consuming, result in costly litigation and diversion of technical and management personnel, or require us to develop a non-infringing technology or enter into license agreements. Where claims are made by customers, resistance even to unmeritorious claims could damage customer relationships. There can be no assurance that licenses will be available on acceptable terms and conditions, if at all, or that our indemnification by our suppliers will be adequate to cover our costs if a claim were brought directly against us or our customers. Furthermore, because of the potential for high court awards that are not necessarily predictable, it is not unusual to find even arguably unmeritorious claims settled for significant amounts. If any infringement or other intellectual property claim made against us by any third party is successful, if we are required to indemnify a customer with respect to a claim against the customer, or if we fail to develop non-infringing technology or license the proprietary rights on commercially reasonable terms and conditions, our business, operating results, and financial condition could be materially and adversely affected. For additional information regarding our indemnification obligations, see Note 12(g) to the Consolidated Financial Statements contained in this report.

Our exposure to risks associated with the use of intellectual property may be increased as a result of acquisitions, as we have a lower level of visibility into the development process with respect to such technology or the care taken to safeguard against infringement risks. Further, in the past, third parties have made infringement and similar claims after we have acquired technology that had not been asserted prior to our acquisition.

### **WE RELY ON THE AVAILABILITY OF THIRD-PARTY LICENSES**

Many of our products are designed to include software or other intellectual property licensed from third parties. It may be necessary in the future to seek or renew licenses relating to various aspects of these products. There can be no assurance that the necessary licenses would be available on acceptable terms, if at all. The inability to obtain certain licenses or other rights or to obtain such licenses or rights on favorable terms, or the need to engage in litigation regarding these matters, could have a material adverse effect on our business, operating results, and financial condition. Moreover, the inclusion in our products of software or other intellectual property licensed from third parties on a nonexclusive basis could limit our ability to protect our proprietary rights in our products.

### **OUR OPERATING RESULTS MAY BE ADVERSELY AFFECTED AND DAMAGE TO OUR REPUTATION MAY OCCUR DUE TO PRODUCTION AND SALE OF COUNTERFEIT VERSIONS OF OUR PRODUCTS**

As is the case with leading products around the world, our products are subject to efforts by third parties to produce counterfeit versions of our products. While we work diligently with law enforcement authorities in various countries to block the manufacture of counterfeit goods and to interdict their sale, and to detect counterfeit products in customer networks, and have succeeded in prosecuting counterfeiters and their distributors, resulting in fines, imprisonment and restitution to us, there can be no guarantee that such efforts will succeed. While counterfeiters often aim their sales at customers who might not have otherwise purchased our products due to lack of verifiability of origin and service, such counterfeit sales, to the extent they replace otherwise legitimate sales, could adversely affect our operating results.

### **OUR OPERATING RESULTS AND FUTURE PROSPECTS COULD BE MATERIALLY HARMED BY UNCERTAINTIES OF REGULATION OF THE INTERNET**

Currently, few laws or regulations apply directly to access or commerce on the Internet. We could be materially adversely affected by regulation of the Internet and Internet commerce in any country where we operate. Such regulations could include matters such as voice over the Internet or using IP, encryption technology, sales or other taxes on Internet product or service sales, and access charges for Internet service providers. The adoption of regulation of the Internet and Internet commerce could decrease demand for our products and, at the same time, increase the cost of selling our products, which could have a material adverse effect on our business, operating results, and financial condition.

### **CHANGES IN TELECOMMUNICATIONS REGULATION AND TARIFFS COULD HARM OUR PROSPECTS AND FUTURE SALES**

Changes in telecommunications requirements, or regulatory requirements in other industries in which we operate, in the United States or other countries could affect the sales of our products. In particular, we believe that there may be future changes in U.S. telecommunications regulations that could slow the expansion of the service providers' network infrastructures and materially adversely affect our business, operating results, and financial condition, including "net neutrality" rules to the extent they impact decisions on investment in network infrastructure.

Future changes in tariffs by regulatory agencies or application of tariff requirements to currently untariffed services could affect the sales of our products for certain classes of customers. Additionally, in the United States, our products must comply with various requirements and regulations of the Federal Communications Commission and other regulatory authorities. In countries outside of the United States, our products must meet various requirements of local telecommunications and other industry authorities. Changes in tariffs or failure by us to obtain timely approval of products could have a material adverse effect on our business, operating results, and financial condition.

### **FAILURE TO RETAIN AND RECRUIT KEY PERSONNEL WOULD HARM OUR ABILITY TO MEET KEY OBJECTIVES**

Our success has always depended in large part on our ability to attract and retain highly skilled technical, managerial, sales, and marketing personnel. Competition for these personnel is intense, especially in the Silicon Valley area of Northern California. Stock incentive plans are designed to reward employees for their long-term contributions and provide incentives for them to remain with us. Volatility or lack of positive performance in our stock price or equity incentive awards, or changes to our overall compensation program, including our stock incentive program, resulting from the management of share dilution and share-based compensation expense or otherwise, may also adversely affect our ability to retain key employees. As a result of one or more of these factors, we may increase our hiring in geographic areas outside the United States, which could subject us to additional geopolitical and exchange rate risk. The loss of services of any of our key personnel; the inability to retain and

attract qualified personnel in the future; or delays in hiring required personnel, particularly engineering and sales personnel, could make it difficult to meet key objectives, such as timely and effective product introductions. In addition, companies in our industry whose employees accept positions with competitors frequently claim that competitors have engaged in improper hiring practices. We have received these claims in the past and may receive additional claims to this effect in the future.

#### **ADVERSE RESOLUTION OF LITIGATION OR GOVERNMENTAL INVESTIGATIONS MAY HARM OUR OPERATING RESULTS OR FINANCIAL CONDITION**

We are a party to lawsuits in the normal course of our business. Litigation can be expensive, lengthy, and disruptive to normal business operations. Moreover, the results of complex legal proceedings are difficult to predict. For example, Brazilian authorities have investigated our Brazilian subsidiary and certain of its former employees, as well as a Brazilian importer of our products, and its affiliates and employees, relating to alleged evasion of import taxes and alleged improper transactions involving the subsidiary and the importer. Brazilian tax authorities have assessed claims against our Brazilian subsidiary based on a theory of joint liability with the Brazilian importer for import taxes, interest, and penalties. The asserted claims by Brazilian federal tax authorities which remain are for calendar years 2003 through 2007, and the asserted claims by the tax authorities from the state of Sao Paulo are for calendar years 2005 through 2007. The total asserted claims by Brazilian state and federal tax authorities aggregate to \$218 million for the alleged evasion of import and other taxes, \$1.4 billion for interest, and \$1.0 billion for various penalties, all determined using an exchange rate as of July 28, 2018. We have completed a thorough review of the matters and believe the asserted claims against our Brazilian subsidiary are without merit, and we are defending the claims vigorously. While we believe there is no legal basis for the alleged liability, due to the complexities and uncertainty surrounding the judicial process in Brazil and the nature of the claims asserting joint liability with the importer, we are unable to determine the likelihood of an unfavorable outcome against our Brazilian subsidiary and are unable to reasonably estimate a range of loss, if any. We do not expect a final judicial determination for several years. An unfavorable resolution of lawsuits or governmental investigations could have a material adverse effect on our business, operating results, or financial condition. For additional information regarding certain of the matters in which we are involved, see Note 12 to the Consolidated Financial Statements, subsection (h) "Legal Proceedings."

#### **CHANGES IN OUR PROVISION FOR INCOME TAXES OR ADVERSE OUTCOMES RESULTING FROM EXAMINATION OF OUR INCOME TAX RETURNS COULD ADVERSELY AFFECT OUR RESULTS**

Our provision for income taxes is subject to volatility and could be adversely affected by earnings being lower than anticipated in countries that have lower tax rates and higher than anticipated in countries that have higher tax rates; by changes in the valuation of our deferred tax assets and liabilities; by changes to domestic manufacturing deduction laws, regulations, or interpretations thereof; by expiration of or lapses in tax incentives; by transfer pricing adjustments, including the effect of acquisitions on our legal structure; by tax effects of nondeductible compensation; by tax costs related to intercompany realignments; by changes in accounting principles; or by changes in tax laws and regulations, treaties, or interpretations thereof, including changes to the taxation of earnings of our foreign subsidiaries, the deductibility of expenses attributable to foreign income, and the foreign tax credit rules. Significant judgment is required to determine the recognition and measurement attribute prescribed in the accounting guidance for uncertainty in income taxes. The Organisation for Economic Co-operation and Development (OECD), an international association comprised of 36 countries, including the United States, has made changes to numerous long-standing tax principles. There can be no assurance that these changes, once adopted by countries, will not have an adverse impact on our provision for income taxes. Further, as a result of certain of our ongoing employment and capital investment actions and commitments, our income in certain countries is subject to reduced tax rates. Our failure to meet these commitments could adversely impact our provision for income taxes. In addition, we are subject to the continuous examination of our income tax returns by the Internal Revenue Service and other tax authorities. We regularly assess the likelihood of adverse outcomes resulting from these examinations to determine the adequacy of our provision for income taxes. There can be no assurance that the outcomes from these continuous examinations will not have an adverse effect on our operating results and financial condition.

#### **OUR BUSINESS AND OPERATIONS ARE ESPECIALLY SUBJECT TO THE RISKS OF EARTHQUAKES, FLOODS, AND OTHER NATURAL CATASTROPHIC EVENTS**

Our corporate headquarters, including certain of our research and development operations are located in the Silicon Valley area of Northern California, a region known for seismic activity. Additionally, a certain number of our facilities are located near rivers that have experienced flooding in the past. Also certain of our suppliers and logistics centers are located in regions that have been or may be affected by earthquake, tsunami and flooding activity which in the past has disrupted, and in the future could disrupt, the flow of components and delivery of products. A significant natural disaster, such as an earthquake, a hurricane, volcano, or a flood, could have a material adverse impact on our business, operating results, and financial condition.

**MAN-MADE PROBLEMS SUCH AS CYBER-ATTACKS, DATA PROTECTION BREACHES, MALWARE OR TERRORISM MAY DISRUPT OUR OPERATIONS, HARM OUR OPERATING RESULTS AND FINANCIAL CONDITION, AND DAMAGE OUR REPUTATION, AND CYBER-ATTACKS OR DATA PROTECTION BREACHES ON OUR CUSTOMERS' NETWORKS, OR IN CLOUD-BASED SERVICES PROVIDED BY OR ENABLED BY US, COULD RESULT IN CLAIMS OF LIABILITY AGAINST US, DAMAGE OUR REPUTATION OR OTHERWISE HARM OUR BUSINESS**

Despite our implementation of network security measures, the products and services we sell to customers, and our servers, data centers and the cloud-based solutions on which our data, and data of our customers, suppliers and business partners are stored, are vulnerable to cyber-attacks, data protection breaches, malware, and similar disruptions from unauthorized tampering or human error. Any such event could compromise our networks or those of our customers, and the information stored on our networks or those of our customers could be accessed, publicly disclosed, lost or stolen, which could subject us to liability to our customers, suppliers, business partners and others, and could have a material adverse effect on our business, operating results, and financial condition and may cause damage to our reputation. Efforts to limit the ability of malicious third parties to disrupt the operations of the Internet or undermine our own security efforts may be costly to implement and meet with resistance, and may not be successful. Breaches of network security in our customers' networks, or in cloud-based services provided by or enabled by us, regardless of whether the breach is attributable to a vulnerability in our products or services, could result in claims of liability against us, damage our reputation or otherwise harm our business.

In addition, the continued threat of terrorism and heightened security and military action in response to this threat, or any future acts of terrorism, may cause further disruptions to the economies of the United States and other countries and create further uncertainties or otherwise materially harm our business, operating results, and financial condition. Likewise, events such as loss of infrastructure and utilities services such as energy, transportation, or telecommunications could have similar negative impacts. To the extent that such disruptions or uncertainties result in delays or cancellations of customer orders or the manufacture or shipment of our products, our business, operating results, and financial condition could be materially and adversely affected.

**VULNERABILITIES AND CRITICAL SECURITY DEFECTS, PRIORITIZATION DECISIONS REGARDING REMEDYING VULNERABILITIES OR SECURITY DEFECTS, FAILURE OF THIRD PARTY PROVIDERS TO REMEDY VULNERABILITIES OR SECURITY DEFECTS, OR CUSTOMERS NOT DEPLOYING SECURITY RELEASES OR DECIDING NOT TO UPGRADE PRODUCTS, SERVICES OR SOLUTIONS COULD RESULT IN CLAIMS OF LIABILITY AGAINST US, DAMAGE OUR REPUTATION OR OTHERWISE HARM OUR BUSINESS**

The products and services we sell to customers, and our cloud-based solutions, inevitably contain vulnerabilities or critical security defects which have not been remedied and cannot be disclosed without compromising security. We may also make prioritization decisions in determining which vulnerabilities or security defects to fix, and the timing of these fixes, which could result in an exploit which compromises security. Customers also need to test security releases before they can be deployed which can delay implementation. In addition, we rely on third-party providers of software and cloud-based service and we cannot control the rate at which they remedy vulnerabilities. Customers may also not deploy a security release, or decide not to upgrade to the latest versions of our products, services or cloud-based solutions containing the release, leaving them vulnerable. Vulnerabilities and critical security defects, prioritization errors in remedying vulnerabilities or security defects, failure of third-party providers to remedy vulnerabilities or security defects, or customers not deploying security releases or deciding not to upgrade products, services or solutions could result in claims of liability against us, damage our reputation or otherwise harm our business.

**IF WE DO NOT SUCCESSFULLY MANAGE OUR STRATEGIC ALLIANCES, WE MAY NOT REALIZE THE EXPECTED BENEFITS FROM SUCH ALLIANCES AND WE MAY EXPERIENCE INCREASED COMPETITION OR DELAYS IN PRODUCT DEVELOPMENT**

We have several strategic alliances with large and complex organizations and other companies with which we work to offer complementary products and services and in the past have established a joint venture to market services associated with our Cisco Unified Computing System products. These arrangements are generally limited to specific projects, the goal of which is generally to facilitate product compatibility and adoption of industry standards. There can be no assurance we will realize the expected benefits from these strategic alliances or from the joint venture. If successful, these relationships may be mutually beneficial and result in industry growth. However, alliances carry an element of risk because, in most cases, we must compete in some business areas with a company with which we have a strategic alliance and, at the same time, cooperate with that company in other business areas. Also, if these companies fail to perform or if these relationships fail to materialize as expected, we could suffer delays in product development or other operational difficulties. Joint ventures can be difficult to manage, given the potentially different interests of joint venture partners.

**OUR STOCK PRICE MAY BE VOLATILE**

Historically, our common stock has experienced substantial price volatility, particularly as a result of variations between our actual financial results and the published expectations of analysts and as a result of announcements by our competitors and

us. Furthermore, speculation in the press or investment community about our strategic position, financial condition, results of operations, business, security of our products, or significant transactions can cause changes in our stock price. In addition, the stock market has experienced extreme price and volume fluctuations that have affected the market price of many technology companies, in particular, and that have often been unrelated to the operating performance of these companies. These factors, as well as general economic and political conditions and the announcement of proposed and completed acquisitions or other significant transactions, or any difficulties associated with such transactions, by us or our current or potential competitors, may materially adversely affect the market price of our common stock in the future. Additionally, volatility, lack of positive performance in our stock price or changes to our overall compensation program, including our stock incentive program, may adversely affect our ability to retain key employees, virtually all of whom are compensated, in part, based on the performance of our stock price.

**THERE CAN BE NO ASSURANCE THAT OUR OPERATING RESULTS AND FINANCIAL CONDITION WILL NOT BE ADVERSELY AFFECTED BY OUR INCURRENCE OF DEBT**

As of the end of fiscal 2018, we have senior unsecured notes outstanding in an aggregate principal amount of \$25.8 billion that mature at specific dates from calendar year 2019 through 2040. We have also established a commercial paper program under which we may issue short-term, unsecured commercial paper notes on a private placement basis up to a maximum aggregate amount outstanding at any time of \$10.0 billion, and we had no commercial paper notes outstanding under this program as of July 28, 2018. The outstanding senior unsecured notes bear fixed-rate interest payable semiannually, except \$1.0 billion of the notes which bears interest at a floating rate payable quarterly. The fair value of the long-term debt is subject to market interest rate volatility. The instruments governing the senior unsecured notes contain certain covenants applicable to us and our wholly-owned subsidiaries that may adversely affect our ability to incur certain liens or engage in certain types of sale and leaseback transactions. In addition, we will be required to have available in the United States sufficient cash to service the interest on our debt and repay all of our notes on maturity. There can be no assurance that our incurrence of this debt or any future debt will be a better means of providing liquidity to us than would our use of our existing cash resources. Further, we cannot be assured that our maintenance of this indebtedness or incurrence of future indebtedness will not adversely affect our operating results or financial condition. In addition, changes by any rating agency to our credit rating can negatively impact the value and liquidity of both our debt and equity securities, as well as the terms upon which we may borrow under our commercial paper program or future debt issuances.

**Item 1B. Unresolved Staff Comments**

Not applicable.

**Item 2. Properties**

Our corporate headquarters are located at an owned site in San Jose, California, in the United States of America. The locations of our headquarters by geographic segment are as follows:

<u>Americas</u>	<u>EMEA</u>	<u>APJC</u>
San Jose, California, USA	Amsterdam, Netherlands	Singapore

In addition to our headquarters site, we own additional sites in the United States, which include facilities in the surrounding areas of San Jose, California; Research Triangle Park, North Carolina; Richardson, Texas; Lawrenceville, Georgia; and Boxborough, Massachusetts. We also own land for expansion in some of these locations. In addition, we lease office space in many U.S. locations.

Outside the United States our operations are conducted primarily in leased sites. Other significant sites (in addition to the two non-U.S. headquarters locations) are located in Belgium, Canada, China, Germany, India, Israel, Japan, Mexico, Poland, and the United Kingdom.

We believe that our existing facilities, including both owned and leased, are in good condition and suitable for the conduct of our business. For additional information regarding obligations under operating leases, see Note 12 to the Consolidated Financial Statements.

**Item 3. Legal Proceedings**

For a description of our material pending legal proceedings, see Note 12 “Commitments and Contingencies - (h) Legal Proceedings” of the Notes to Consolidated Financial Statements included in Item 8 of this Annual Report on Form 10-K, which is incorporated herein by reference.

**Item 4. Mine Safety Disclosures**

Not applicable.

**PART II****Item 5. Market for Registrant’s Common Equity, Related Stockholder Matters, and Issuer Purchases of Equity Securities**

- (a) Cisco common stock is traded on the Nasdaq Global Select Market under the symbol CSCO. Information regarding quarterly cash dividends declared on Cisco’s common stock during fiscal 2018 and 2017 may be found in Supplementary Financial Data on page 114 of this report. There were 40,817 registered shareholders as of August 31, 2018. The high and low common stock sales prices per share for each period were as follows:

Fiscal Quarter	FISCAL 2018		FISCAL 2017	
	High	Low	High	Low
First quarter .....	\$ 34.73	\$ 30.36	\$ 31.95	\$ 29.86
Second quarter .....	\$ 42.69	\$ 33.67	\$ 31.89	\$ 29.12
Third quarter.....	\$ 46.16	\$ 37.35	\$ 34.53	\$ 30.42
Fourth quarter.....	\$ 46.37	\$ 40.94	\$ 34.60	\$ 30.37

- (b) Not applicable.

- (c) Issuer purchases of equity securities (in millions, except per-share amounts):

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Approximate Dollar Value of Shares That May Yet Be Purchased Under the Plans or Programs	
				Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Approximate Dollar Value of Shares That May Yet Be Purchased Under the Plans or Programs
April 29, 2018 to May 26, 2018.....	44	\$ 44.63	44	\$ 23,076	
May 27, 2018 to June 23, 2018 .....	41	\$ 43.65	41	\$ 21,271	
June 24, 2018 to July 28, 2018 .....	53	\$ 42.65	53	\$ 19,036	
Total .....	138	\$ 43.58	138		

On September 13, 2001, we announced that our Board of Directors had authorized a stock repurchase program. On February 14, 2018, our Board of Directors authorized a \$25 billion increase to the stock repurchase program. As of July 28, 2018, the remaining authorized amount for stock repurchases under this program, including the additional authorization, is approximately \$19.0 billion with no termination date.

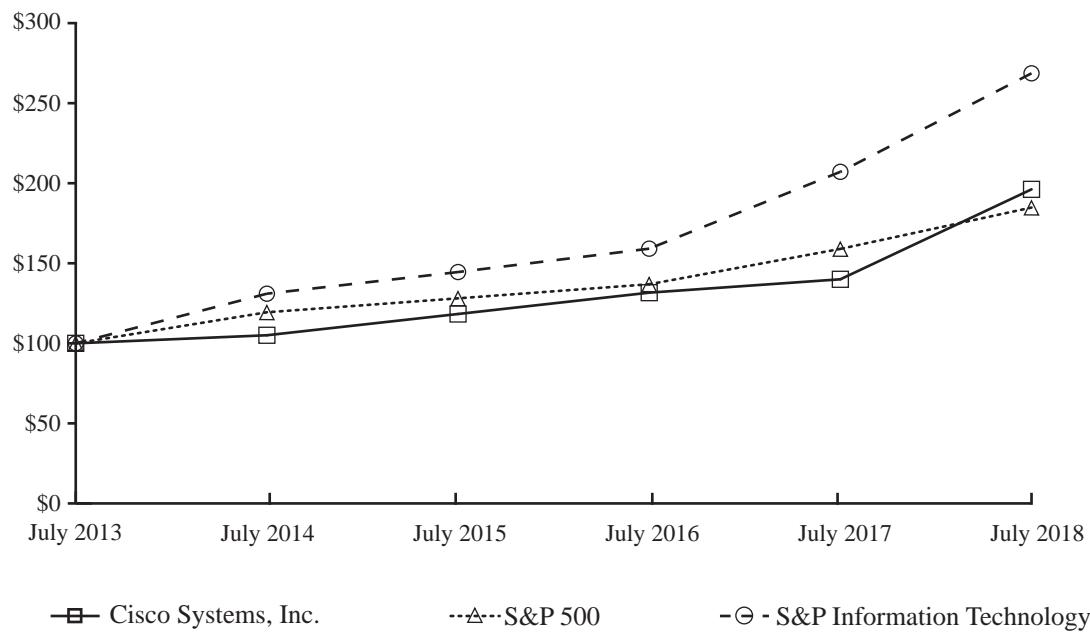
For the majority of restricted stock units granted, the number of shares issued on the date the restricted stock units vest is net of shares withheld to meet applicable tax withholding requirements. Although these withheld shares are not issued or considered common stock repurchases under our stock repurchase program and therefore are not included in the preceding table, they are treated as common stock repurchases in our financial statements as they reduce the number of shares that would have been issued upon vesting (see Note 13 to the Consolidated Financial Statements).

## Stock Performance Graph

The information contained in this Stock Performance Graph section shall not be deemed to be “soliciting material” or “filed” or incorporated by reference in future filings with the SEC, or subject to the liabilities of Section 18 of the Securities Exchange Act of 1934, except to the extent that Cisco specifically incorporates it by reference into a document filed under the Securities Act of 1933 or the Securities Exchange Act of 1934.

The following graph shows a five-year comparison of the cumulative total shareholder return on Cisco common stock with the cumulative total returns of the S&P 500 Index, and the S&P Information Technology Index. The graph tracks the performance of a \$100 investment in the Company’s common stock and in each of the indexes (with the reinvestment of all dividends) on the date specified. Shareholder returns over the indicated period are based on historical data and should not be considered indicative of future shareholder returns.

**Comparison of 5-Year Cumulative Total Return Among Cisco Systems, Inc.,  
the S&P 500 Index, and the S&P Information Technology Index**



	July 2013	July 2014	July 2015	July 2016	July 2017	July 2018
Cisco Systems, Inc.....	\$ 100.00	\$ 105.04	\$ 118.32	\$ 131.64	\$ 140.72	\$ 196.18
S&P 500 .....	\$ 100.00	\$ 119.40	\$ 128.10	\$ 136.90	\$ 158.98	\$ 184.80
S&P Information Technology.....	\$ 100.00	\$ 131.22	\$ 144.52	\$ 159.12	\$ 207.12	\$ 268.65

**Item 6. Selected Financial Data**

Five Years Ended July 28, 2018 (in millions, except per-share amounts)

<u>Years Ended</u>	<u>July 28, 2018 <sup>(1)</sup></u>	<u>July 29, 2017</u>	<u>July 30, 2016 <sup>(2)(3)</sup></u>	<u>July 25, 2015 <sup>(2)</sup></u>	<u>July 26, 2014 <sup>(4)</sup></u>
Revenue.....	\$ 49,330	\$ 48,005	\$ 49,247	\$ 49,161	\$ 47,142
Net income .....	\$ 110	\$ 9,609	\$ 10,739	\$ 8,981	\$ 7,853
Net income per share—basic .....	\$ 0.02	\$ 1.92	\$ 2.13	\$ 1.76	\$ 1.50
Net income per share—diluted.....	\$ 0.02	\$ 1.90	\$ 2.11	\$ 1.75	\$ 1.49
Shares used in per-share calculation—basic ...	4,837	5,010	5,053	5,104	5,234
Shares used in per-share calculation—diluted...	4,881	5,049	5,088	5,146	5,281
Cash dividends declared per common share ...	\$ 1.24	\$ 1.10	\$ 0.94	\$ 0.80	\$ 0.72
Net cash provided by operating activities .....	\$ 13,666	\$ 13,876	\$ 13,570	\$ 12,552	\$ 12,332
	<u>July 28, 2018</u>	<u>July 29, 2017</u>	<u>July 30, 2016</u>	<u>July 25, 2015</u>	<u>July 26, 2014</u>
Cash and cash equivalents and investments....	\$ 46,548	\$ 70,492	\$ 65,756	\$ 60,416	\$ 52,074
Total assets .....	\$ 108,784	\$ 129,818	\$ 121,652	\$ 113,373	\$ 105,070
Debt.....	\$ 25,569	\$ 33,717	\$ 28,643	\$ 25,354	\$ 20,845
Deferred revenue .....	\$ 19,685	\$ 18,494	\$ 16,472	\$ 15,183	\$ 14,142

<sup>(1)</sup> In fiscal 2018, Cisco recorded a provisional tax expense of \$10.4 billion related to the enactment of the Tax Cuts and Job Act (“the Tax Act”) comprised of \$8.1 billion of U.S. transition tax, \$1.2 billion of foreign withholding tax, and \$1.1 billion re-measurement of net deferred tax assets and liabilities (DTA).

<sup>(2)</sup> In the second quarter of fiscal 2016, Cisco completed the sale of the SP Video CPE Business. As a result, revenue from this portion of the Service Provider Video product category will not recur in future periods. The sale resulted in a pre-tax gain of \$253 million net of certain transaction costs. The years ended July 30, 2016 and July 25, 2015 include SP Video CPE Business revenue of \$504 million and \$1,846 million, respectively.

<sup>(3)</sup> In fiscal 2016 Cisco recognized total tax benefits of \$593 million for the following: i) the Internal Revenue Service (IRS) and Cisco settled all outstanding items related to Cisco’s federal income tax returns for fiscal 2008 through fiscal 2010, as a result of which Cisco recorded a net tax benefit of \$367 million; and ii) the Protecting Americans from Tax Hikes Act of 2015 reinstated the U.S. federal research and development (R&D) tax credit permanently, as a result of which Cisco recognized tax benefits of \$226 million, of which \$81 million related to fiscal 2015 R&D expenses.

<sup>(4)</sup> In the second quarter of fiscal 2014, Cisco recorded a pre-tax charge of \$655 million to product cost of sales, which corresponds to \$526 million, net of tax, for the expected remediation cost for certain products sold in prior fiscal years containing memory components manufactured by a single supplier between 2005 and 2010. See Note 12(f) to the Consolidated Financial Statements.

No other factors materially affected the comparability of the information presented above.

## Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

### Forward-Looking Statements

This Annual Report on Form 10-K, including this Management's Discussion and Analysis of Financial Condition and Results of Operations, contains forward-looking statements regarding future events and our future results that are subject to the safe harbors created under the Securities Act of 1933 (the "Securities Act") and the Securities Exchange Act of 1934 (the "Exchange Act"). All statements other than statements of historical facts are statements that could be deemed forward-looking statements. These statements are based on current expectations, estimates, forecasts, and projections about the industries in which we operate and the beliefs and assumptions of our management. Words such as "expects," "anticipates," "targets," "goals," "projects," "intends," "plans," "believes," "momentum," "seeks," "estimates," "continues," "endeavors," "strives," "may," variations of such words, and similar expressions are intended to identify such forward-looking statements. In addition, any statements that refer to projections of our future financial performance, our anticipated growth and trends in our businesses, and other characterizations of future events or circumstances are forward-looking statements. Readers are cautioned that these forward-looking statements are only predictions and are subject to risks, uncertainties, and assumptions that are difficult to predict, including those under "Part I, Item 1A. Risk Factors," and elsewhere herein. Therefore, actual results may differ materially and adversely from those expressed in any forward-looking statements. We undertake no obligation to revise or update any forward-looking statements for any reason.

### OVERVIEW

Cisco designs and sells a broad range of technologies that have been powering the Internet since 1984. Across networking, security, collaboration, applications and the cloud, our evolving intent-based technologies are constantly learning and adapting to provide customers with a highly secure, intelligent platform for their digital business.

A summary of our results is as follows (in millions, except percentages and per-share amounts):

	Three Months Ended			Years Ended		
	July 28, 2018	July 29, 2017	Variance	July 28, 2018	July 29, 2017	Variance
Revenue. ....	\$ 12,844	\$ 12,133	6%	\$ 49,330	\$ 48,005	3%
Gross margin percentage .....	61.7%	62.2%	(0.5) pts	62.0%	63.0%	(1.0) pts
Research and development.....	\$ 1,626	\$ 1,499	8%	\$ 6,332	\$ 6,059	5%
Sales and marketing .....	\$ 2,348	\$ 2,318	1%	\$ 9,242	\$ 9,184	1%
General and administrative .....	\$ 543	\$ 495	10%	\$ 2,144	\$ 1,993	8%
Total R&D, sales and marketing, general and administrative .....	\$ 4,517	\$ 4,312	5%	\$ 17,718	\$ 17,236	3%
Total as a percentage of revenue.....	35.2%	35.5%	(0.3) pts	35.9%	35.9%	— pts
Amortization of purchased intangible assets included in operating expenses .....	\$ 33	\$ 58	(43)%	\$ 221	\$ 259	(15)%
Restructuring and other charges included in operating expenses .....	\$ 26	\$ 142	(82)%	\$ 358	\$ 756	(53)%
Operating income as a percentage of revenue .....	26.1%	25.0%	1.1 pts	25.0%	24.9%	0.1 pts
Income tax percentage <sup>(1)</sup> .....	(5.9)%	23.8%	(29.7) pts	99.2%	21.8%	77.4 pts
Net income <sup>(1)</sup> .....	\$ 3,803	\$ 2,424	57%	\$ 110	\$ 9,609	(99)%
Net income as a percentage of revenue .....	29.6%	20.0%	9.6 pts	0.2%	20.0%	(19.8) pts
Earnings per share—diluted <sup>(1)</sup> .....	\$ 0.81	\$ 0.48	69%	\$ 0.02	\$ 1.90	(99)%

<sup>(1)</sup> Fourth quarter and fiscal year 2018 results include an \$863 million benefit and a \$10.4 billion charge, respectively, related to the enactment of the Tax Act.

## **Fiscal 2018 Compared with Fiscal 2017**

In fiscal 2018, we saw broad strength across the business and delivered solid revenue growth, margins, cash flow and returns for our shareholders. We remain focused on accelerating innovation across our portfolio, and we believe that we have made continued progress on our strategic priorities. Our product revenue reflected growth in Infrastructure Platforms, Applications and Security, and we continued to make progress in the transition of our business model to increased software and subscriptions. We continue to operate in a challenging and highly competitive environment. We experienced some weakness in the service provider market and we expect ongoing uncertainty in that area. While the overall environment remains uncertain, we continue to aggressively invest in priority areas with the objective of driving profitable growth over the long term.

Total revenue increased by 3% compared with fiscal 2017. Within total revenue, product and service revenue each increased by 3%. Total gross margin decreased by 1.0 percentage points, driven primarily by unfavorable impacts from pricing, a \$127 million legal and indemnification settlement charge, and unfavorable product mix, partially offset by productivity benefits. While productivity was positive to overall product gross margin, the benefit was lower than in the prior year as these improvements were adversely impacted by an increase in the cost of certain components which are currently constrained. As a percentage of revenue, research and development, sales and marketing, and general and administrative expenses, collectively, were flat. Operating income as a percentage of revenue increased by 0.1 percentage points. Diluted earnings per share and net income each decreased by 99% due to the \$10.4 billion provisional tax expense related to the Tax Act, comprised of \$8.1 billion U.S. transition tax, \$1.2 billion of foreign withholding tax, and \$1.1 billion of net deferred tax assets re-measurement.

In terms of our geographic segments, revenue from the Americas increased by \$0.7 billion, EMEA revenue increased by \$0.4 billion, and revenue in our APJC segment increased by \$0.2 billion. These increases reflect broad strength across several countries within these segments. The “BRICM” countries experienced product revenue growth of 2% in the aggregate, driven by increased product revenue in the emerging countries of Brazil, Russia, India and China of 17%, 10%, 3% and 3%, respectively, partially offset by a product revenue decline of 16% in Mexico.

From a customer market standpoint, we experienced solid product revenue growth in the commercial market and, to a lesser extent, in the enterprise and public sector markets. Product revenue in the service provider market declined with ongoing uncertainty in that area.

From a product category perspective, the product revenue increase of 3% was driven by a 2% product revenue increase in Infrastructure Platforms and solid product revenue growth in Applications and Security of 10% and 9%, respectively. We saw broad strength across the portfolio, with the exception of routing related to the weakness in the service provider market.

## **Fourth Quarter Snapshot**

For the fourth quarter of fiscal 2018, as compared with the fourth quarter of fiscal 2017, total revenue increased by 6%. Within total revenue, product revenue increased by 7% and service revenue increased by 3%. With regard to our geographic segment performance, on a year-over-year basis, revenue in the Americas, EMEA and APJC increased by 5%, 8% and 6%, respectively. From a product category perspective, we experienced broad strength across the portfolio. Total gross margin decreased by 0.5 percentage points, driven by some specific transactions with service providers in our APJC segment. Our gross margin also decreased due to unfavorable pricing, product mix and higher component costs, partially offset by improved productivity benefits. As a percentage of revenue, research and development, sales and marketing, and general and administrative expenses collectively decreased by 0.3 percentage points. Operating income as a percentage of revenue increased by 1.1 percentage points. Diluted earnings per share increased by 69% and net income increased by 57%, due in part to an \$863 million tax benefit related to the Tax Act.

## **Strategy and Priorities**

As our customers add billions of new connections to their enterprises, and as more applications move to a multi-cloud environment, we believe the network continues to be extremely critical. We believe that our customers are looking for intent-based networks that provide meaningful business value through automation, security, and analytics across private, hybrid, and multi-cloud environments. Our vision is to deliver highly secure, software-defined, automated and intelligent platforms for our customers. Our strategic priorities include the following: accelerating our pace of innovation, increasing the value of the network, and transforming our business model.

For a full discussion of our strategy and priorities, see Item 1. Business.

## **Other Key Financial Measures**

The following is a summary of our other key financial measures for fiscal 2018 compared with fiscal 2017 (in millions):

	<b>Fiscal 2018</b>	<b>Fiscal 2017</b>
Cash and cash equivalents and investments.....	\$ 46,548	\$ 70,492
Cash provided by operating activities .....	\$ 13,666	\$ 13,876
Deferred revenue .....	\$ 19,685	\$ 18,494
Repurchases of common stock—stock repurchase program.....	\$ 17,661	\$ 3,706
Dividends .....	\$ 5,968	\$ 5,511
Inventories .....	\$ 1,846	\$ 1,616

## **CRITICAL ACCOUNTING ESTIMATES**

The preparation of financial statements and related disclosures in conformity with accounting principles generally accepted in the United States requires us to make judgments, assumptions, and estimates that affect the amounts reported in the Consolidated Financial Statements and accompanying notes. Note 2 to the Consolidated Financial Statements describes the significant accounting policies and methods used in the preparation of the Consolidated Financial Statements. The accounting policies described below are significantly affected by critical accounting estimates. Such accounting policies require significant judgments, assumptions, and estimates used in the preparation of the Consolidated Financial Statements, and actual results could differ materially from the amounts reported based on these policies.

### **Revenue Recognition**

Revenue is recognized when all of the following criteria have been met:

- *Persuasive evidence of an arrangement exists.* Contracts, Internet commerce agreements, and customer purchase orders are generally used to determine the existence of an arrangement.
- *Delivery has occurred.* Shipping documents and customer acceptance, when applicable, are used to verify delivery. For software, delivery is considered to have occurred upon unrestricted license access and license term commencement, when applicable.
- *The fee is fixed or determinable.* We assess whether the fee is fixed or determinable based on the payment terms associated with the transaction and whether the sales price is subject to refund or adjustment.
- *Collectibility is reasonably assured.* We assess collectibility based primarily on the creditworthiness of the customer as determined by credit checks and analysis, as well as the customer's payment history.

In instances where final acceptance of the product, system, or solution is specified by the customer, revenue is deferred until all acceptance criteria have been met. When a sale involves multiple deliverables, such as sales of products that include services, the multiple deliverables are evaluated to determine the unit of accounting, and the entire fee from the arrangement is allocated to each unit of accounting based on the relative selling price. Revenue is recognized when the revenue recognition criteria for each unit of accounting are met. For hosting arrangements, we recognize revenue ratably over the hosting period, while usage revenue is recognized based on utilization. Software subscription revenue is deferred and recognized ratably over the subscription term upon delivery of the first product and commencement of the term.

The amount of revenue recognized in a given period is affected by our judgment as to whether an arrangement includes multiple deliverables and, if so, our valuation of the units of accounting. Our multiple element arrangements may contain only deliverables within the scope of Accounting Standards Codification (ASC) 605, *Revenue Recognition*, deliverables within the scope of ASC 985-605, *Software-Revenue Recognition*, or a combination of both. According to the accounting guidance prescribed in ASC 605, we use vendor-specific objective evidence of selling price (VSOE) for each of those units, when available. We determine VSOE based on our normal pricing and discounting practices for the specific product or service when sold separately. In determining VSOE, we require that a substantial majority of the historical standalone transactions have the selling prices for a product or service fall within a reasonably narrow pricing range, generally evidenced by approximately 80% of such historical standalone transactions falling within plus or minus 15% of the median rates. When VSOE does not exist, we apply the selling price hierarchy to applicable multiple-deliverable arrangements. Under the selling price hierarchy, third-party evidence of selling price (TPE) will be considered if VSOE does not exist, and estimated selling price (ESP) will be used if neither VSOE nor TPE is available. Generally, we are not able to determine TPE because our go-to-market strategy differs from that of others in our markets, and the extent of our proprietary technology varies among comparable products or services from those of our peers. In determining ESP, we apply significant judgment as we weigh a variety of factors, based on the characteristics of the deliverable. We typically arrive at an ESP for a product or service that is not sold separately by considering company-specific factors such as geographies, competitive landscape, internal costs, profitability objectives, pricing practices used to establish bundled pricing, and existing portfolio pricing and discounting.

As our business and offerings evolve over time, our pricing practices may be required to be modified accordingly, which could result in changes in selling prices, including both VSOE and ESP, in subsequent periods. There were no material impacts during fiscal 2018 from changes in VSOE, TPE, or ESP.

We make sales to distributors which we refer to as two-tier sales to the end customer. Revenue from two-tier distributors is recognized based on a sell-through method using point-of-sale information provided by these distributors. Distributors participate in various cooperative marketing and other incentive programs, and we maintain estimated accruals and allowances for these programs. If actual credits received by distributors under these programs were to deviate significantly from our estimates, which are based on historical experience, our revenue could be adversely affected.

In May 2014, the Financial Accounting Standards Board (FASB) issued ASC 606, *Revenue from Contracts with Customers*, a new accounting standard related to revenue recognition. ASC 606 will supersede nearly all U.S. GAAP on revenue recognition and eliminate industry-specific guidance. The underlying principle of the new standard is to recognize revenue when a customer obtains control of promised goods or services at an amount that reflects the consideration that is expected to be received in exchange for those goods or services. It also requires increased disclosures including the nature, amount, timing, and uncertainty of revenues and cash flows related to contracts with customers.

ASC 606 allows two methods of adoption: i) retrospectively to each prior period presented (“full retrospective method”), or ii) retrospectively with the cumulative effect recognized in retained earnings as of the date of adoption (“modified retrospective method”). We will adopt the new standard using the modified retrospective method at the beginning of our first quarter of fiscal 2019.

We do not expect that ASC 606 will have a material impact on total revenue for fiscal 2019 based on two factors: i) revenue will be accelerated consistent with the changes in timing as indicated in the table in Note 2 to the Consolidated Financial Statements, largely offset by ii) the reduction of revenue from software arrangements where revenue was previously deferred in prior periods and recognized ratably over time as required under the current standard. This preliminary assessment is based on the types and number of revenue arrangements currently in place. The exact impact of ASC 606 will be dependent on facts and circumstances at adoption and could vary from quarter to quarter.

For the first quarter of fiscal 2019, we expect that the adoption of ASC 606 may increase total revenue by about 1% on a year-over-year basis. For further discussion of ASC 606, including the estimated impacts on transition date, see Note 2 to the Consolidated Financial Statements.

### **Allowances for Receivables and Sales Returns**

The allowances for receivables were as follows (in millions, except percentages):

	<b>July 28, 2018</b>	<b>July 29, 2017</b>
Allowance for doubtful accounts .....	\$ 129	\$ 211
<i>Percentage of gross accounts receivable</i> .....	<i>2.3%</i>	<i>3.9%</i>
Allowance for credit loss—lease receivables .....	\$ 135	\$ 162
<i>Percentage of gross lease receivables</i> <sup>(1)</sup> .....	<i>4.7%</i>	<i>5.5%</i>
Allowance for credit loss—loan receivables .....	\$ 60	\$ 103
<i>Percentage of gross loan receivables</i> .....	<i>1.2%</i>	<i>2.3%</i>

<sup>(1)</sup> Calculated as allowance for credit loss on lease receivables as a percentage of gross lease receivables and residual value before unearned income.

The allowance for doubtful accounts is based on our assessment of the collectibility of customer accounts. We regularly review the adequacy of these allowances by considering internal factors such as historical experience, credit quality and age of the receivable balances as well as external factors such as economic conditions that may affect a customer’s ability to pay as well as historical and expected default frequency rates, which are published by major third-party credit-rating agencies and are updated on a quarterly basis. We also consider the concentration of receivables outstanding with a particular customer in assessing the adequacy of our allowances for doubtful accounts. If a major customer’s creditworthiness deteriorates, if actual defaults are higher than our historical experience, or if other circumstances arise, our estimates of the recoverability of amounts due to us could be overstated, and additional allowances could be required, which could have an adverse impact on our operating results.

The allowance for credit loss on financing receivables is also based on the assessment of collectibility of customer accounts. We regularly review the adequacy of the credit allowances determined either on an individual or a collective basis. When evaluating the financing receivables on an individual basis, we consider historical experience, credit quality and age of receivable balances, and economic conditions that may affect a customer’s ability to pay. When evaluating financing receivables on a collective basis, we use expected default frequency rates published by a major third-party credit-rating agency as well as our own historical loss rate in the event of default, while also systematically giving effect to economic conditions, concentration of risk and correlation. Determining expected default frequency rates and loss factors associated with internal credit risk ratings, as well as assessing factors such as economic conditions, concentration of risk, and correlation, are complex and subjective. Our ongoing consideration of all these factors could result in an increase in our allowance for credit loss in the future, which could adversely affect our operating results. Both accounts receivable and financing receivables are charged off at the point when they are considered uncollectible.

A reserve for future sales returns is established based on historical trends in product return rates. The reserve for future sales returns as of July 28, 2018 and July 29, 2017 was \$123 million and \$122 million, respectively, and was recorded as a reduction of our accounts receivable and revenue. If the actual future returns were to deviate from the historical data on which the reserve had been established, our revenue could be adversely affected.

### **Inventory Valuation and Liability for Purchase Commitments with Contract Manufacturers and Suppliers**

Inventory is written down based on excess and obsolete inventories, determined primarily by future demand forecasts. Inventory write-downs are measured as the difference between the cost of the inventory and market, based upon assumptions about future demand, and are charged to the provision for inventory, which is a component of our cost of sales. At the point of the loss recognition, a new, lower cost basis for that inventory is established, and subsequent changes in facts and circumstances do not result in the restoration or increase in that newly established cost basis.

We record a liability for firm, noncancelable, and unconditional purchase commitments with contract manufacturers and suppliers for quantities in excess of our future demand forecasts consistent with the valuation of our excess and obsolete inventory.

Our provision for inventory was \$63 million, \$74 million, and \$65 million in fiscal 2018, 2017, and 2016, respectively. The provision for the liability related to purchase commitments with contract manufacturers and suppliers was \$105 million, \$124 million, and \$134 million in fiscal 2018, 2017, and 2016, respectively. If there were to be a sudden and significant decrease in demand for our products, or if there were a higher incidence of inventory obsolescence because of rapidly changing technology and customer requirements, we could be required to increase our inventory write-downs, and our liability for purchase commitments with contract manufacturers and suppliers, and accordingly our profitability, could be adversely affected. We regularly evaluate our exposure for inventory write-downs and the adequacy of our liability for purchase commitments.

### **Loss Contingencies and Product Warranties**

We are subject to the possibility of various losses arising in the ordinary course of business. We consider the likelihood of impairment of an asset or the incurrence of a liability, as well as our ability to reasonably estimate the amount of loss, in determining loss contingencies. An estimated loss contingency is accrued when it is probable that an asset has been impaired or a liability has been incurred and the amount of loss can be reasonably estimated. We regularly evaluate information available to us to determine whether such accruals should be made or adjusted and whether new accruals are required.

Third parties, including customers, have in the past and may in the future assert claims or initiate litigation related to exclusive patent, copyright, trademark, and other intellectual property rights to technologies and related standards that are relevant to us. These assertions have increased over time as a result of our growth and the general increase in the pace of patent claims assertions, particularly in the United States. If any infringement or other intellectual property claim made against us by any third party is successful, or if we fail to develop non-infringing technology or license the proprietary rights on commercially reasonable terms and conditions, our business, operating results, and financial condition could be materially and adversely affected.

Our products are generally covered by a warranty for periods ranging from 90 days to five years, and for some products we provide a limited lifetime warranty. We accrue for warranty costs as part of our cost of sales based on associated material costs, technical support labor costs, and associated overhead. Material cost is estimated based primarily upon historical trends in the volume of product returns within the warranty period and the cost to repair or replace the equipment. Technical support labor cost is estimated based primarily upon historical trends in the rate of customer cases and the cost to support the customer cases within the warranty period. Overhead cost is applied based on estimated time to support warranty activities.

If we experience an increase in warranty claims compared with our historical experience, or if the cost of servicing warranty claims is greater than expected, our profitability could be adversely affected.

### **Fair Value Measurements**

Our fixed income and publicly traded equity securities, collectively, are reflected in the Consolidated Balance Sheets at a fair value of \$37.6 billion as of July 28, 2018, compared with \$58.8 billion as of July 29, 2017. Our fixed income investment portfolio, as of July 28, 2018, consisted primarily of high quality investment-grade securities. See Note 8 to the Consolidated Financial Statements.

As described more fully in Note 2 to the Consolidated Financial Statements, a valuation hierarchy is based on the level of independent, objective evidence available regarding the value of the investments. It encompasses three classes of investments: Level 1 consists of securities for which there are quoted prices in active markets for identical securities; Level 2 consists of securities for which observable inputs other than Level 1 inputs are used, such as quoted prices for similar securities in active markets or quoted prices for identical securities in less active markets and model-derived valuations for which the variables are derived from, or corroborated by, observable market data; and Level 3 consists of securities for which there are unobservable inputs to the valuation methodology that are significant to the measurement of the fair value.

Our Level 2 securities are valued using quoted market prices for similar instruments or nonbinding market prices that are corroborated by observable market data. We use inputs such as actual trade data, benchmark yields, broker/dealer quotes, and other similar data, which are obtained from independent pricing vendors, quoted market prices, or other sources to determine the ultimate fair value of our assets and liabilities. We use such pricing data as the primary input, to which we have not made any material adjustments during fiscal 2018 and 2017, to make our assessments and determinations as to the ultimate valuation of our investment portfolio. We are ultimately responsible for the financial statements and underlying estimates.

The inputs and fair value are reviewed for reasonableness, may be further validated by comparison to publicly available information, and could be adjusted based on market indices or other information that management deems material to its estimate of fair value. The assessment of fair value can be difficult and subjective. However, given the relative reliability of the inputs we use to value our investment portfolio, and because substantially all of our valuation inputs are obtained using quoted market prices for similar or identical assets, we do not believe that the nature of estimates and assumptions affected by levels of subjectivity and judgment was material to the valuation of the investment portfolio as of July 28, 2018.

### **Other-than-Temporary Impairments**

We recognize an impairment charge when the declines in the fair values of our fixed income or publicly traded equity securities below their cost basis are judged to be other than temporary. The ultimate value realized on these securities, to the extent unhedged, is subject to market price volatility until they are sold.

If the fair value of a debt security is less than its amortized cost, we assess whether the impairment is other than temporary. An impairment is considered other than temporary if (i) we have the intent to sell the security, (ii) it is more likely than not that we will be required to sell the security before recovery of its entire amortized cost basis, or (iii) we do not expect to recover the entire amortized cost of the security. If an impairment is considered other than temporary based on (i) or (ii) described in the prior sentence, the entire difference between the amortized cost and the fair value of the security is recognized in earnings. If an impairment is considered other than temporary based on condition (iii), the amount representing credit loss, defined as the difference between the present value of the cash flows expected to be collected and the amortized cost basis of the debt security, will be recognized in earnings, and the amount relating to all other factors will be recognized in other comprehensive income (OCI). In estimating the amount and timing of cash flows expected to be collected, we consider all available information, including past events, current conditions, the remaining payment terms of the security, the financial condition of the issuer, expected defaults, and the value of underlying collateral.

For publicly traded equity securities, we consider various factors in determining whether we should recognize an impairment charge, including the length of time and extent to which the fair value has been less than our cost basis, the financial condition and near-term prospects of the issuer, and our intent and ability to hold the investment for a period of time sufficient to allow for any anticipated recovery in market value.

We also have investments in privately held companies, some of which are in the startup or development stages. As of July 28, 2018, our investments in privately held companies were \$1,096 million, compared with \$983 million as of July 29, 2017, and were included in other assets. We monitor these investments for events or circumstances indicative of potential impairment, and we make appropriate reductions in carrying values if we determine that an impairment charge is required, based primarily on the financial condition and near-term prospects of these companies. These investments are inherently risky because the markets for the technologies or products these companies are developing are typically in the early stages and may never materialize.

### **Goodwill and Purchased Intangible Asset Impairments**

Our methodology for allocating the purchase price relating to purchase acquisitions is determined through established valuation techniques. Goodwill represents a residual value as of the acquisition date, which in most cases results in measuring goodwill as an excess of the purchase consideration transferred plus the fair value of any noncontrolling interest in the acquired company over the fair value of net assets acquired, including contingent consideration. We perform goodwill impairment tests on an annual basis in the fourth fiscal quarter and between annual tests in certain circumstances for each reporting unit. The assessment of fair value for goodwill and purchased intangible assets is based on factors that market participants would use in an orderly transaction in accordance with the new accounting guidance for the fair value measurement of nonfinancial assets.

The goodwill recorded in the Consolidated Balance Sheets as of July 28, 2018 and July 29, 2017 was \$31.7 billion and \$29.8 billion, respectively. The increase in goodwill during fiscal 2018 was due in large part to our acquisition of BroadSoft. In response to changes in industry and market conditions, we could be required to strategically realign our resources and consider restructuring, disposing of, or otherwise exiting businesses, which could result in an impairment of goodwill. There was no impairment of goodwill in fiscal 2018, 2017, and 2016. For the annual impairment testing in fiscal 2018, the excess of the fair value over the carrying value for each of our reporting units was \$73.0 billion for the Americas, \$53.0 billion for EMEA, and \$35.5 billion for APJC.

During the fourth quarter of fiscal 2018, we performed a sensitivity analysis for goodwill impairment with respect to each of our respective reporting units and determined that a hypothetical 10% decline in the fair value of each reporting unit would not result in an impairment of goodwill for any reporting unit.

The fair value of acquired technology and patents, as well as acquired technology under development, is determined at acquisition date primarily using the income approach, which discounts expected future cash flows to present value. The discount rates used in the present value calculations are typically derived from a weighted-average cost of capital analysis and then adjusted to reflect risks inherent in the development lifecycle as appropriate. We consider the pricing model for products related to these acquisitions to be standard within the high-technology communications industry, and the applicable discount rates represent the rates that market participants would use for valuation of such intangible assets.

We make judgments about the recoverability of purchased intangible assets with finite lives whenever events or changes in circumstances indicate that an impairment may exist. Recoverability of purchased intangible assets with finite lives is measured by comparing the carrying amount of the asset to the future undiscounted cash flows the asset is expected to generate. We review indefinite-lived intangible assets for impairment annually or whenever events or changes in circumstances indicate that the asset might be impaired. If the asset is considered to be impaired, the amount of any impairment is measured as the difference between the carrying value and the fair value of the impaired asset. Assumptions and estimates about future values and remaining useful lives of our purchased intangible assets are complex and subjective. They can be affected by a variety of factors, including external factors such as industry and economic trends, and internal factors such as changes in our business strategy and our internal forecasts. Our impairment charges related to purchased intangible assets were \$1 million, \$47 million, and \$74 million during fiscal 2018, 2017, and 2016, respectively. Our ongoing consideration of all the factors described previously could result in additional impairment charges in the future, which could adversely affect our net income.

### **Income Taxes**

We are subject to income taxes in the United States and numerous foreign jurisdictions. Our effective tax rates differ from the statutory rate, primarily due to the tax impact of state taxes, foreign operations, R&D tax credits, domestic manufacturing deductions, tax audit settlements, nondeductible compensation, international realignments, and transfer pricing adjustments. Our effective tax rate was 99.2%, 21.8%, and 16.9% in fiscal 2018, 2017, and 2016, respectively.

On December 22, 2017, the Tax Act was enacted. The Tax Act significantly revises the U.S. corporate income tax by, among other things, lowering the statutory corporate income tax rate (“federal tax rate”) from 35% to 21% effective January 1, 2018, implementing a modified territorial tax system, and imposing a mandatory one-time transition tax on accumulated earnings of foreign subsidiaries. As a fiscal-year taxpayer, certain provisions of the Tax Act impact us in fiscal 2018, including the change in the federal tax rate and the one-time transition tax, while other provisions will be effective at the beginning of fiscal 2019 including the implementation of a modified territorial tax system and other changes to how foreign earnings are subject to U.S. tax, and elimination of the domestic manufacturing deduction.

As a result of the decrease in the federal tax rate from 35% to 21% effective January 1, 2018, we have computed our income tax expense for the July 28, 2018 fiscal year using a blended federal tax rate of 27%. The 21% federal tax rate will apply to our fiscal year ending July 27, 2019 and each year thereafter. We must remeasure our DTA using the federal tax rate that will apply when the related temporary differences are expected to reverse.

In December 2017, the Securities and Exchange Commission staff issued Staff Accounting Bulletin No. 118, which addresses how a company recognizes provisional estimates when it does not have the necessary information available, prepared or analyzed (including computations) in reasonable detail to complete its accounting for the effect of the changes in the Tax Act. The measurement period ends when a company has obtained, prepared, and analyzed the information necessary to finalize its accounting, but cannot extend beyond one year. The final impact of the Tax Act may differ from the provisional estimates due to changes in interpretations of the Tax Act, any legislative action to address questions that arise because of the Tax Act, by changes in accounting standard for income taxes and related interpretations in response to the Tax Act, and any updates or changes to estimates used in the provisional amounts. We have determined that the \$8.1 billion of tax expense for the U.S. transition tax on accumulated earnings of foreign subsidiaries, the \$1.2 billion of foreign withholding tax, and the \$1.1 billion of tax expense for DTA re-measurement were each provisional amounts and reasonable estimates for fiscal 2018. Estimates used in the provisional amounts include: the anticipated reversal pattern of the gross DTAs; and earnings, cash positions, foreign taxes and withholding taxes attributable to foreign subsidiaries.

Significant judgment is required in evaluating our uncertain tax positions and determining our provision for income taxes. Although we believe our reserves are reasonable, no assurance can be given that the final tax outcome of these matters will not be different from that which is reflected in our historical income tax provisions and accruals. We adjust these reserves in light of changing facts and circumstances, such as the closing of a tax audit or the refinement of an estimate. To the extent that the final tax outcome of these matters is different than the amounts recorded, such differences will impact the provision for income taxes in the period in which such determination is made. The provision for income taxes includes the impact of reserve provisions and changes to reserves that are considered appropriate, as well as the related net interest and penalties.

Significant judgment is also required in determining any valuation allowance recorded against deferred tax assets. In assessing the need for a valuation allowance, we consider all available evidence, including past operating results, estimates of future taxable income, and the feasibility of tax planning strategies. In the event that we change our determination as to the amount of deferred tax assets that can be realized, we will adjust our valuation allowance with a corresponding impact to the provision for income taxes in the period in which such determination is made.

Our provision for income taxes is subject to volatility and could be adversely impacted by earnings being lower than anticipated in countries that have lower tax rates and higher than anticipated in countries that have higher tax rates; by changes in the valuation of our deferred tax assets and liabilities; by changes to domestic manufacturing deduction laws, regulations, or interpretations thereof; by expiration of or lapses in tax incentives; by transfer pricing adjustments, including the effect of acquisitions on our legal structure; by tax effects of nondeductible compensation; by tax costs related to intercompany realignments; by changes in accounting principles; or by changes in tax laws and regulations, treaties, or interpretations thereof, including changes to the taxation of earnings of our foreign subsidiaries, the deductibility of expenses attributable to foreign income, and the foreign tax credit rules. Significant judgment is required to determine the recognition and measurement attributes prescribed in the accounting guidance for uncertainty in income taxes. The Organisation for Economic Co-operation and Development (OECD), an international association comprised of 36 countries, including the United States, has made changes to numerous long-standing tax principles. There can be no assurance that these changes, once adopted by countries, will not have an adverse impact on our provision for income taxes. As a result of certain of our ongoing employment and capital investment actions and commitments, our income in certain countries is subject to reduced tax rates. Our failure to meet these commitments could adversely impact our provision for income taxes. In addition, we are subject to the continuous examination of our income tax returns by the Internal Revenue Service (IRS) and other tax authorities. We regularly assess the likelihood of adverse outcomes resulting from these examinations to determine the adequacy of our provision for income taxes. There can be no assurance that the outcomes from these continuous examinations will not have an adverse impact on our operating results and financial condition.

## RESULTS OF OPERATIONS

### Revenue

The following table presents the breakdown of revenue between product and service (in millions, except percentages):

	Years Ended			2018 vs. 2017		2017 vs. 2016	
	July 28, 2018	July 29, 2017	July 30, 2016	Variance in Dollars	Variance in Percent	Variance in Dollars	Variance in Percent
<b>Revenue:</b>							
Product.....	\$ 36,709	\$ 35,705	\$ 37,254	\$ 1,004	3%	\$ (1,549)	(4)%
<i>Percentage of revenue .....</i>	<i>74.4%</i>	<i>74.4%</i>	<i>75.6%</i>				
Service.....	<b>12,621</b>	12,300	11,993	321	3%	307	3%
<i>Percentage of revenue .....</i>	<i>25.6%</i>	<i>25.6%</i>	<i>24.4%</i>				
Total .....	<b><u>\$ 49,330</u></b>	<u>\$ 48,005</u>	<u>\$ 49,247</u>	<u>\$ 1,325</u>	3%	<u>\$ (1,242)</u>	(3)%

We manage our business primarily on a geographic basis, organized into three geographic segments. Our revenue, which includes product and service for each segment, is summarized in the following table (in millions, except percentages):

	Years Ended			2018 vs. 2017		2017 vs. 2016	
	July 28, 2018	July 29, 2017	July 30, 2016	Variance in Dollars	Variance in Percent	Variance in Dollars	Variance in Percent
<b>Revenue:</b>							
Americas .....	\$ 29,070	\$ 28,351	\$ 29,392	\$ 719	3%	\$ (1,041)	(4)%
<i>Percentage of revenue .....</i>	<i>58.9%</i>	<i>59.1%</i>	<i>59.7%</i>				
EMEA .....	<b>12,425</b>	12,004	12,302	421	4%	(298)	(2)%
<i>Percentage of revenue .....</i>	<i>25.2%</i>	<i>25.0%</i>	<i>25.0%</i>				
APJC.....	<b>7,834</b>	7,650	7,553	184	2%	97	1%
<i>Percentage of revenue .....</i>	<i>15.9%</i>	<i>15.9%</i>	<i>15.3%</i>				
Total .....	<b><u>\$ 49,330</u></b>	<u>\$ 48,005</u>	<u>\$ 49,247</u>	<u>\$ 1,325</u>	3%	<u>\$ (1,242)</u>	(3)%

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

During the second quarter of fiscal 2016, we completed the sale of the Customer Premises Equipment portion of our Service Provider Video Connected Devices business (“SP Video CPE Business”). SP Video CPE Business revenue was \$504 million for fiscal 2016.

### Fiscal 2018 Compared with Fiscal 2017

Total revenue increased by 3%. Product and service revenue each increased by 3%. Our total revenue reflected growth across each of our geographic segments. Product revenue for the emerging countries of BRICM, in the aggregate, experienced 2% product revenue growth, with increases in Brazil, Russia, India and China partially offset by a decrease in Mexico.

In addition to the impact of macroeconomic factors, including a reduced IT spending environment and reductions in spending by government entities, revenue by segment in a particular period may be significantly impacted by several factors related to revenue recognition, including the complexity of transactions such as multiple-element arrangements; the mix of financing arrangements provided to channel partners and customers; and final acceptance of the product, system, or solution, among other factors. In addition, certain customers tend to make large and sporadic purchases, and the revenue related to these transactions may also be affected by the timing of revenue recognition, which in turn would impact the revenue of the relevant segment. As has been the case in certain emerging countries from time to time, customers require greater levels of financing arrangements, service, and support, and these activities may occur in future periods, which may also impact the timing of the recognition of revenue.

### Fiscal 2017 Compared with Fiscal 2016

Total revenue decreased by 3%. Total company revenue not including SP Video CPE products decreased 2%. Product revenue decreased by 4% while service revenue increased by 3%. Fiscal 2017 had 52 weeks, compared with 53 weeks in fiscal 2016, thus our results for fiscal 2017 reflect one less extra week. We estimate that the additional revenue associated with the extra week was approximately \$265 million, \$200 million of which was from our services subscriptions, and \$65 million from our SaaS offerings such as WebEx, and a small amount from product distribution. Our total revenue declined in the Americas and EMEA geographic segments, while revenue grew in our APJC geographic segment. The emerging countries of BRICM, in the aggregate, experienced a 7% product revenue decline, with revenue declines in Mexico, China, and Brazil partially offset by increases in the other two BRICM countries.

### **Product Revenue by Segment**

The following table presents the breakdown of product revenue by segment (in millions, except percentages):

	Years Ended			2018 vs. 2017		2017 vs. 2016	
	July 28, 2018	July 29, 2017	July 30, 2016	Variance in Dollars	Variance in Percent	Variance in Dollars	Variance in Percent
<b>Product revenue:</b>							
Americas .....	\$ 21,088	\$ 20,487	\$ 21,663	\$ 601	3%	\$ (1,176)	(5)%
<i>Percentage of product revenue</i> .....	<i>57.5%</i>	<i>57.4%</i>	<i>58.1%</i>				
EMEA .....	9,671	9,369	9,682	302	3%	(313)	(3)%
<i>Percentage of product revenue</i> .....	<i>26.3%</i>	<i>26.2%</i>	<i>26.0%</i>				
APJC .....	5,950	5,849	5,909	101	2%	(60)	(1)%
<i>Percentage of product revenue</i> .....	<i>16.2%</i>	<i>16.4%</i>	<i>15.9%</i>				
<b>Total</b> .....	<b>\$ 36,709</b>	<b>\$ 35,705</b>	<b>\$ 37,254</b>	<b>\$ 1,004</b>	<b>3%</b>	<b>\$ (1,549)</b>	<b>(4)%</b>

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

### Americas

#### Fiscal 2018 Compared with Fiscal 2017

Product revenue in the Americas segment increased by 3%, driven by solid growth in the commercial and enterprise markets and, to a lesser extent, growth in the public sector market. Product revenue in the service provider market was flat. From a country perspective, product revenue increased by 3% in the United States, 9% in Canada and 17% in Brazil, partially offset by a decrease of 16% in Mexico.

#### Fiscal 2017 Compared with Fiscal 2016

The 5% decrease in product revenue in the Americas segment was driven by declines in the service provider, public sector and commercial markets. Product revenue in the enterprise market was flat. The product revenue decrease in the service provider market was driven in large part by the absence of product sales related to our SP Video CPE Business in fiscal 2017. We had \$378 million in product sales related to our SP Video CPE Business in fiscal 2016 in this segment. The product revenue decline in the public sector market was due primarily to lower sales to state and local governments and to the U.S. federal government. From a country perspective, product revenue decreased by 5% in the United States, 28% in Mexico and 7% in Brazil, partially offset by an increase of 2% in Canada.

### EMEA

#### Fiscal 2018 Compared with Fiscal 2017

The increase in product revenue in the EMEA segment of 3% was driven by solid growth in the commercial and public sector markets and, to a lesser extent, growth in the enterprise market. These increases were partially offset by a product revenue decline in the service provider market. Product revenue from emerging countries within EMEA and the remainder of the EMEA segment, which primarily consists of countries in Western Europe, each increased by 3%.

### Fiscal 2017 Compared with Fiscal 2016

Product revenue in the EMEA segment decreased by 3%, driven by a decline in the service provider market and, to a lesser extent, declines in the public sector and enterprise markets. Product revenue in the commercial market was flat. The product revenue decrease in the service provider market was driven in part by the absence of product sales related to our SP Video CPE Business in fiscal 2017. We had \$108 million in product sales related to our SP Video CPE Business in fiscal 2016 in this segment. Product revenue from emerging countries within EMEA and product revenue for the remainder of the EMEA segment each decreased by 3%.

### APJC

#### Fiscal 2018 Compared with Fiscal 2017

Product revenue in the APJC segment increased by 2%. The product revenue increase was led by solid growth in the commercial and enterprise markets. These increases were partially offset by product revenue declines in the service provider and public sector markets. From a country perspective, product revenue increased by 3% in China and 3% in India, partially offset by a decrease of 3% in Japan.

#### Fiscal 2017 Compared with Fiscal 2016

Product revenue in the APJC segment decreased by 1%. The product revenue decrease was led by declines in the service provider and public sector markets, partially offset by product revenue growth in the commercial market. Product revenue in the enterprise market was flat. From a country perspective, product revenue decreased by 12% in China, driven by a decrease in sales of Service Provider Video Software and Solutions products, while product revenue increased by 11% in India, 9% in Australia and 2% in Japan. Product sales for this geographic segment were adversely impacted by an \$18 million decrease in product sales related to the absence of our SP Video CPE Business.

### **Product Revenue by Groups of Similar Products**

In addition to the primary view on a geographic basis, we also prepare financial information related to groups of similar products and customer markets for various purposes. Effective in the first quarter of fiscal 2018, we began reporting our product revenue in the following categories: Infrastructure Platforms, Applications, Security, and Other Products. This change better aligns our product categories with our evolving business model. Prior period amounts have been reclassified to conform to the current period's presentation.

The following table presents revenue for groups of similar products (in millions, except percentages):

	Years Ended			2018 vs. 2017		2017 vs. 2016	
	July 28, 2018	July 29, 2017	July 30, 2016	Variance in Dollars	Variance in Percent	Variance in Dollars	Variance in Percent
<b>Product revenue:</b>							
Infrastructure Platforms . . . . .	\$ 28,270	\$ 27,779	\$ 28,851	\$ 491	2%	\$ (1,072)	(4)%
Applications . . . . .	5,035	4,568	4,438	467	10%	130	3%
Security . . . . .	2,353	2,153	1,969	200	9%	184	9%
Other Products . . . . .	1,050	1,205	1,996	(155)	(13)%	(791)	(40)%
	<b>\$ 36,709</b>	<b>\$ 35,705</b>	<b>\$ 37,254</b>	<b>\$ 1,004</b>	<b>3%</b>	<b>\$ (1,549)</b>	<b>(4)%</b>

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

### Infrastructure Platforms

#### Fiscal 2018 Compared with Fiscal 2017

The Infrastructure Platforms product category represents our core networking offerings related to switching, routing, wireless, and the data center. Infrastructure Platforms revenue increased by 2%, or \$491 million, with strength across the portfolio with the exception of routing. Switching experienced growth, with solid revenue growth in data center switching driven by an increase in sales of Cisco Nexus 9000 Series products, and with revenue growth in campus switching driven by our intent-based networking Cisco Catalyst 9000 Series. Data center had strong double digit growth driven by higher sales of server products and our hyperconverged data center offering, HyperFlex. We also experienced solid revenue growth from wireless products driven by Meraki as well as our Wave 2 offerings. We had a decrease in sales of routing products, driven by continued weakness in the service provider market.

### Fiscal 2017 Compared with Fiscal 2016

Revenue from the Infrastructure Platforms product category decreased by 4% or \$1,072 million, driven primarily by lower revenue from switching products. Within switching, we experienced a decrease in sales of switching products used in campus environments, which we believe was driven both by the uncertainty in the macro environment which led to a slowdown in customer spending, as well as by a highly competitive landscape. These impacts were partially offset by an increase in sales of our ACI portfolio which is included in our data center switching portfolio. We also experienced a decrease in revenue from routing products driven by weakness in enterprise access and a decrease in revenue from data center due to lower sales of server products. We had revenue growth from wireless products driven by Meraki.

### Applications

#### Fiscal 2018 Compared with Fiscal 2017

The Applications product category includes our collaboration offerings (unified communications, Cisco TelePresence and conferencing) as well as the Internet of Things (IoT) and analytics software offerings from Jasper and AppDynamics, respectively. Revenue in our Applications product category increased by 10%, or \$467 million, with growth across all of the businesses. We experienced solid growth in the Telepresence, unified communications, conferencing and analytics from our fiscal 2017 acquisition of AppDynamics. We continued to increase the amount of deferred revenue and the proportion of recurring revenue related to our Applications product category.

#### Fiscal 2017 Compared with Fiscal 2016

The increase in revenue in our Applications product category by 3%, or \$130 million, was in large part due to increased revenue from our IoT software offerings, driven by our fiscal 2016 Jasper acquisition. The growth in Conferencing revenue and the acquisition of AppDynamics in the third quarter of fiscal 2017 also contributed to the revenue increase in this product category. These increases in revenue were partially offset by decreased revenue from unified communications and Telepresence.

### Security

#### Fiscal 2018 Compared with Fiscal 2017

Revenue in our Security product category increased 9%, or \$200 million, driven by higher sales of unified threat management, web security, policy and access and advanced threat products. We continued to increase the amount of deferred revenue and the proportion of recurring revenue related to our Security product category.

#### Fiscal 2017 Compared with Fiscal 2016

Revenue in our Security product category increased 9%, or \$184 million, driven by higher sales of unified threat management, advanced threat security, and web security products.

### Other Products

#### Fiscal 2018 Compared with Fiscal 2017

The decrease in revenue from our Other Products category was primarily driven by a decrease in revenue from Service Provider Video Software and Solutions (“SPVSS”).

On May 1, 2018, we announced a definitive agreement to sell the SPVSS business. We expect this transaction to close in the first half of fiscal 2019 subject to regulatory approvals and customary closing conditions.

#### Fiscal 2017 Compared with Fiscal 2016

The decrease in revenue in our Other Products category was in large part due to a decrease in product sales of \$504 million related to our SP Video CPE Business and a decrease in revenue from SPVSS products.

## Service Revenue by Segment

The following table presents the breakdown of service revenue by segment (in millions, except percentages):

Years Ended	Years Ended			2018 vs. 2017		2017 vs. 2016	
	July 28, 2018	July 29, 2017	July 30, 2016	Variance in Dollars	Variance in Percent	Variance in Dollars	Variance in Percent
<b>Service revenue:</b>							
Americas .....	\$ 7,982	\$ 7,864	\$ 7,729	\$ 118	2%	\$ 135	2%
Percentage of service revenue...	63.3%	63.9%	64.4%				
EMEA .....	2,754	2,635	2,620	119	5%	15	1%
Percentage of service revenue...	21.8%	21.4%	21.9%				
APJC.....	1,885	1,801	1,644	84	5%	157	10%
Percentage of service revenue...	14.9%	14.7%	13.7%				
Total .....	<u>\$ 12,621</u>	<u>\$ 12,300</u>	<u>\$ 11,993</u>	<u>\$ 321</u>	3%	<u>\$ 307</u>	3%

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

### Fiscal 2018 Compared with Fiscal 2017

Service revenue increased across all geographic segments. Technical support services revenue increased by 2% and advanced services revenue increased by 4%. Technical support services revenue increased across all geographic segments. The increase in technical support services revenue was driven by an increase in software and solution support offerings. Advanced services revenue, which relates to professional services for specific customer network needs, had solid growth in the EMEA segment and, to a lesser extent, increased in our Americas and APJC segments.

### Fiscal 2017 Compared with Fiscal 2016

Service revenue grew 3%. Excluding the \$200 million of additional revenue as a result of the extra week in fiscal 2016, service revenue grew 4%. Service revenue grew across all of our geographic segments. Technical support services revenue increased by 3% and advanced services revenue increased by 1%. Technical support services revenue increased across all geographic segments. The increase in technical support services revenue was driven by contract initiations and renewals associated with product sales and an increase in software support offerings. Advanced services revenue had solid revenue growth in our APJC segment, declined slightly in our EMEA segment and was flat in our Americas segment.

## Gross Margin

The following table presents the gross margin for products and services (in millions, except percentages):

Years Ended	AMOUNT			PERCENTAGE		
	July 28, 2018	July 29, 2017	July 30, 2016	July 28, 2018	July 29, 2017	July 30, 2016
<b>Gross margin:</b>						
Product.....	\$ 22,282	\$ 22,006	\$ 23,093	60.7%	61.6%	62.0%
Service .....	8,324	8,218	7,867	66.0%	66.8%	65.6%
Total .....	<u>\$ 30,606</u>	<u>\$ 30,224</u>	<u>\$ 30,960</u>	<u>62.0%</u>	63.0%	62.9%

## Product Gross Margin

### Fiscal 2018 Compared with Fiscal 2017

The following table summarizes the key factors that contributed to the change in product gross margin percentage from fiscal 2017 to fiscal 2018:

	Product Gross Margin Percentage
<b>Fiscal 2017</b> .....	<b>61.6%</b>
<b>Product pricing</b> .....	<b>(1.4)%</b>
<b>Legal and indemnification settlements</b> .....	<b>(0.3)%</b>
<b>Mix of products sold</b> .....	<b>(0.2)%</b>
<b>Amortization of purchased intangible assets</b> .....	<b>(0.2)%</b>
<b>Productivity <sup>(1)</sup></b> .....	<b>1.2%</b>
<b>Fiscal 2018</b> .....	<b>60.7%</b>

<sup>(1)</sup> Productivity includes overall manufacturing-related costs, such as component costs, warranty expense, provision for inventory, freight, logistics, shipment volume, and other items not categorized elsewhere.

Product gross margin decreased by 0.9 percentage points due largely to unfavorable impacts from product pricing, a charge of \$127 million to product cost of sales recorded in fiscal 2018 related to legal and indemnification settlements, and unfavorable product mix, partially offset by productivity benefits.

The negative pricing impact, which was lower than the year-over-year impact we experienced in fiscal 2017, was driven by typical market factors and impacted each of our geographic segments and customer markets. While productivity was positive to overall product gross margin, the benefit was lower than the prior year as these improvements were adversely impacted by an increase in the costs of certain components which are currently constrained. We expect the higher component costs to continue to impact productivity in the near term. Productivity improvements were driven by cost reductions including value engineering efforts (e.g. component redesign, board configuration, test processes, and transformation processes), lower warranty expenses and continued operational efficiency in manufacturing operations. The decrease in product gross margin was also due to an unfavorable mix of products sold driven by negative mix impacts from our Infrastructure Platforms products, partially offset by favorability from Security, Applications and Other Products. Our product gross margin in fiscal 2018 was also negatively impacted by higher amortization expense from purchased intangible assets.

### Fiscal 2017 Compared with Fiscal 2016

The following table summarizes the key factors that contributed to the change in product gross margin percentage from fiscal 2016 to fiscal 2017:

	Product Gross Margin Percentage
<b>Fiscal 2016</b> .....	<b>62.0%</b>
<b>Product pricing</b> .....	<b>(2.1)%</b>
<b>Mix of products sold</b> .....	<b>(0.3)%</b>
<b>Supplier component remediation adjustment</b> .....	<b>(0.1)%</b>
<b>Other</b> .....	<b>(0.1)%</b>
<b>Productivity <sup>(1)</sup></b> .....	<b>1.4%</b>
<b>SP Video CPE Business impact</b> .....	<b>0.8%</b>
<b>Fiscal 2017</b> .....	<b>61.6%</b>

Product gross margin decreased by 0.4 percentage points as compared with fiscal 2016. The decrease in product gross margin was largely due to unfavorable impacts from product pricing, lower productivity benefits, and unfavorable product mix, partially offset by a benefit from the divestiture of the lower margin SP Video CPE business in fiscal 2016.

The negative pricing impact was driven by typical market factors and impacted each of our geographic segments and customer markets. While productivity was positive to overall product gross margin, the benefit was lower than the prior year as these improvements were adversely impacted by an increase in the cost of certain memory components. In addition, productivity was negatively impacted by decreases in core routing and switching revenue which limited our ability to generate cost savings. Productivity improvements were driven by value engineering efforts (e.g. component redesign, board configuration, test processes, and transformation processes), lower warranty expenses and continued operational efficiency in manufacturing operations. The decrease in product gross margin was also due to an unfavorable mix of products sold driven by negative mix impacts from our Infrastructure platform products.

## **Service Gross Margin**

### *Fiscal 2018 Compared with Fiscal 2017*

Our service gross margin percentage decreased by 0.8 percentage points due to increased headcount-related costs and, to a lesser extent, unfavorable mix and increased delivery costs. These cost impacts were partially offset by the resulting benefit to gross margin of higher sales volume in both advanced services and technical support services.

Our service gross margin normally experiences some fluctuations due to various factors such as the timing of contract initiations in our renewals, our strategic investments in headcount, and the resources we deploy to support the overall service business. Other factors include the mix of service offerings, as the gross margin from our advanced services is typically lower than the gross margin from technical support services.

### *Fiscal 2017 Compared with Fiscal 2016*

Our service gross margin percentage increased by 1.2 percentage points due to higher sales volume, decreased delivery costs, favorable mix and, to a lesser extent, lower share-based compensation expense. These benefits to service gross margin were partially offset by increased headcount-related costs.

## **Gross Margin by Segment**

The following table presents the total gross margin for each segment (in millions, except percentages):

Years Ended	AMOUNT			PERCENTAGE		
	July 28, 2018	July 29, 2017	July 30, 2016	July 28, 2018	July 29, 2017	July 30, 2016
<b>Gross margin:</b>						
Americas .....	\$ 18,792	\$ 18,284	\$ 18,986	64.6%	64.5%	64.6%
EMEA .....	7,945	7,855	7,998	63.9%	65.4%	65.0%
APJC .....	4,726	4,741	4,620	60.3%	62.0%	61.2%
Segment total .....	<b>31,463</b>	30,880	31,604	<b>63.8%</b>	64.3%	64.2%
Unallocated corporate items <sup>(1)</sup> .....	(857)	(656)	(644)			
Total .....	<b>\$ 30,606</b>	<b>\$ 30,224</b>	<b>\$ 30,960</b>	<b>62.0%</b>	63.0%	62.9%

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

<sup>(1)</sup> The unallocated corporate items include the effects of amortization and impairments of acquisition-related intangible assets, share-based compensation expense, significant litigation settlements and other contingencies, charges related to asset impairments and restructurings, and certain other charges. We do not allocate these items to the gross margin for each segment because management does not include such information in measuring the performance of the operating segments.

### *Fiscal 2018 Compared with Fiscal 2017*

We experienced a slight gross margin percentage increase in our Americas segment due to productivity improvements, partially offset by unfavorable impacts from pricing and product mix. The unfavorable mix of products sold in this segment was driven by negative mix impacts from our Infrastructure Platforms products, partially offset by favorability from Security, Applications and Other products.

The gross margin percentage decrease in our EMEA segment was due primarily to negative impacts from pricing and, to a lesser extent, an unfavorable product mix, partially offset by productivity improvements. Lower service gross margin also contributed to the decrease in the gross margin in this geographic segment.

The APJC segment gross margin percentage decreased due primarily to the negative impacts from pricing and an unfavorable product mix, partially offset by productivity improvements. Lower service gross margin also contributed to the decrease in the gross margin in this geographic segment. Our gross margin in this segment was also negatively impacted by specific transactions with service providers.

The gross margin percentage for a particular segment may fluctuate, and period-to-period changes in such percentages may or may not be indicative of a trend for that segment.

#### Fiscal 2017 Compared with Fiscal 2016

The Americas segment experienced a slight gross margin percentage decrease due to negative impacts from pricing and product mix, partially offset by productivity improvements and the sale of the lower margin SP Video CPE Business. The unfavorable mix impact was driven by Infrastructure Platforms products.

The gross margin percentage increase in our EMEA segment was due primarily to higher service gross margin. Product gross margin in this segment also increased slightly due to the impact of productivity improvements, the sale of the lower margin SP Video CPE Business and a favorable product mix, partially offset by unfavorable impacts from pricing.

The APJC segment gross margin percentage increased due primarily to higher service gross margin. Product gross margin in this segment decreased due to negative impacts from pricing and product mix, partially offset by productivity improvements. The unfavorable mix impact was driven by Infrastructure Platforms products.

#### **Research and Development (“R&D”), Sales and Marketing, and General and Administrative (“G&A”) Expenses**

R&D, sales and marketing, and G&A expenses are summarized in the following table (in millions, except percentages):

	Years Ended			2018 vs. 2017		2017 vs. 2016	
	July 28, 2018	July 29, 2017	July 30, 2016	Variance in Dollars	Variance in Percent	Variance in Dollars	Variance in Percent
Research and development . . .	\$ 6,332	\$ 6,059	\$ 6,296	\$ 273	5%	\$ (237)	(4)%
<i>Percentage of revenue . . . . .</i>	<i>12.8%</i>	<i>12.6%</i>	<i>12.8%</i>				
Sales and marketing. . . . .	9,242	9,184	9,619	58	1%	(435)	(5)%
<i>Percentage of revenue . . . . .</i>	<i>18.7%</i>	<i>19.1%</i>	<i>19.5%</i>				
General and administrative. . . . .	2,144	1,993	1,814	151	8%	179	10%
<i>Percentage of revenue . . . . .</i>	<i>4.3%</i>	<i>4.2%</i>	<i>3.7%</i>				
Total . . . . .	\$ 17,718	\$ 17,236	\$ 17,729	\$ 482	3%	\$ (493)	(3)%
<i>Percentage of revenue . . . . .</i>	<i>35.9%</i>	<i>35.9%</i>	<i>36.0%</i>				

Our fiscal 2016 had an extra week compared with fiscal 2017. We estimate that the extra week in fiscal 2016 contributed approximately \$116 million of the year-over-year decrease in total operating expenses (not including share-based compensation expense).

#### R&D Expenses

##### Fiscal 2018 Compared with Fiscal 2017

R&D expenses increased primarily due to higher headcount-related expenses, higher discretionary spending and, to a lesser extent, higher acquisition-related costs and higher share-based compensation expense, partially offset by lower contracted services.

We continue to invest in R&D in order to bring a broad range of products to market in a timely fashion. If we believe that we are unable to enter a particular market in a timely manner with internally developed products, we may purchase or license technology from other businesses, or we may partner with or acquire businesses as an alternative to internal R&D.

##### Fiscal 2017 Compared with Fiscal 2016

R&D expenses decreased primarily due to lower contracted services, lower headcount-related expenses, lower discretionary spending and lower acquisition-related costs, partially offset by higher share-based compensation expense. Lower headcount-related expenses were due to efficiencies related to our restructuring actions and the extra week in fiscal 2016.

## Sales and Marketing Expenses

### Fiscal 2018 Compared with Fiscal 2017

Sales and marketing expenses increased due to increases in headcount-related expenses, discretionary spending, share-based compensation expense and acquisition-related costs, partially offset by a decrease in contracted services.

### Fiscal 2017 Compared with Fiscal 2016

Sales and marketing expenses decreased due to lower headcount-related expenses, lower contracted services, lower discretionary spending, lower acquisition-related costs and, to a lesser extent, lower share-based compensation expense. Lower headcount-related expenses were due to efficiencies related to our restructuring actions. The extra week in fiscal 2016 also contributed to the decrease in headcount-related expenses.

## G&A Expenses

### Fiscal 2018 Compared with Fiscal 2017

G&A expenses increased due to increases in contracted services, headcount-related expenses, discretionary spending, acquisition-related/divestiture costs and share-based compensation expense, partially offset by gains on divestitures.

### Fiscal 2017 Compared with Fiscal 2016

G&A expenses increased primarily due to the \$253 million pre-tax gain from the sale of our SP Video CPE Business recorded during fiscal 2016 and, to a lesser extent, higher share-based compensation expense. These increases were partially offset by lower headcount-related expenses and lower contracted services. The extra week in fiscal 2016 contributed to the decreased headcount-related expense.

## Effect of Foreign Currency

In fiscal 2018, foreign currency fluctuations, net of hedging, increased the combined R&D, sales and marketing, and G&A expenses by approximately \$93 million, or 0.5%, compared with fiscal 2017. In fiscal 2017, foreign currency fluctuations, net of hedging, decreased the combined R&D, sales and marketing, and G&A expenses by approximately \$77 million, or 0.4%, compared with fiscal 2016.

## **Share-Based Compensation Expense**

The following table presents share-based compensation expense (in millions):

<u>Years Ended</u>	<u>July 28, 2018</u>	<u>July 29, 2017</u>	<u>July 30, 2016</u>
Cost of sales—product .....	\$ 94	\$ 85	\$ 70
Cost of sales—service .....	<u>133</u>	<u>134</u>	<u>142</u>
Share-based compensation expense in cost of sales .....	<u>227</u>	<u>219</u>	<u>212</u>
Research and development .....	<u>538</u>	<u>529</u>	<u>470</u>
Sales and marketing .....	<u>555</u>	<u>542</u>	<u>545</u>
General and administrative .....	<u>246</u>	<u>236</u>	<u>205</u>
Restructuring and other charges .....	<u>33</u>	<u>3</u>	<u>26</u>
Share-based compensation expense in operating expenses.....	<u>1,372</u>	<u>1,310</u>	<u>1,246</u>
Total share-based compensation expense.....	<u><u>\$ 1,599</u></u>	<u><u>\$ 1,529</u></u>	<u><u>\$ 1,458</u></u>

### Fiscal 2018 Compared with Fiscal 2017

The increase in share-based compensation expense was due primarily to higher expense related to equity awards assumed with respect to our recent acquisitions.

### Fiscal 2017 Compared with Fiscal 2016

The increase in share-based compensation expense was due primarily to higher expense related to equity awards assumed with respect to our recent acquisitions.

## **Amortization of Purchased Intangible Assets**

The following table presents the amortization of purchased intangible assets (in millions):

Years Ended	<u>July 28, 2018</u>	<u>July 29, 2017</u>	<u>July 30, 2016</u>
Amortization of purchased intangible assets:			
Cost of sales .....	\$ 640	\$ 556	\$ 577
Operating expenses			
Amortization of purchased intangible assets.....	221	259	303
Restructuring and other charges .....	—	38	—
Total .....	<u>\$ 861</u>	<u>\$ 853</u>	<u>\$ 880</u>

### Fiscal 2018 Compared with Fiscal 2017

Amortization of purchased intangible assets increased slightly as amortization from our recent acquisitions was partially offset by decreases related to SPVSS purchased intangibles which were held for sale and lower impairment charges in fiscal 2018.

### Fiscal 2017 Compared with Fiscal 2016

Amortization of purchased intangible assets decreased due to certain purchased intangible assets having become fully amortized and lower impairment charges in fiscal 2017, partially offset by amortization of purchased intangible assets from our recent acquisitions.

## **Restructuring and Other Charges**

The following table presents the restructuring and other charges (in millions):

Years Ended	<u>July 28, 2018</u>	<u>July 29, 2017</u>	<u>July 30, 2016</u>
Restructuring and other charges:			
Cost of sales .....	\$ —	\$ —	\$ (2)
Operating expenses			
Restructuring and other charges .....	358	756	268
Total .....	<u>\$ 358</u>	<u>\$ 756</u>	<u>\$ 266</u>

We initiated a restructuring plan during fiscal 2018 in order to realign our organization and enable further investment in key priority areas, with estimated pretax charges of approximately \$300 million. We expect this restructuring plan to be substantially completed in fiscal 2019. See Note 5 to the Consolidated Financial Statements.

We incurred restructuring and other charges of \$358 million during fiscal 2018, \$108 million of which was related to the restructuring plan initiated during fiscal 2018 and the remainder of which was related to the restructuring plan announced in August 2016.

We incurred restructuring and other charges of \$756 million and \$266 million during fiscal 2017 and 2016, respectively, in connection with the restructuring plans announced in August 2016 and August 2014.

These charges were primarily cash-based and consisted of employee severance and other one-time termination benefits, and other associated costs. We expect to reinvest substantially all of the cost savings from these restructuring actions in our key priority areas. As a result, the overall cost savings from these restructuring actions are not expected to be material for future periods.

## **Operating Income**

The following table presents our operating income and our operating income as a percentage of revenue (in millions, except percentages):

Years Ended	<u>July 28, 2018</u>	<u>July 29, 2017</u>	<u>July 30, 2016</u>
Operating income .....	\$ 12,309	\$ 11,973	\$ 12,660
Operating income as a percentage of revenue .....	25.0%	24.9%	25.7%

### Fiscal 2018 Compared with Fiscal 2017

Operating income increased by 3%, and as a percentage of revenue operating income increased by 0.1 percentage points. These increases resulted primarily from an increase in revenue and a decrease in restructuring and other charges.

### Fiscal 2017 Compared with Fiscal 2016

Operating income decreased by 5%, and as a percentage of revenue operating income decreased by 0.8 percentage points. These decreases resulted primarily from an increase in restructuring and other charges related to the restructuring action announced in August 2016 and the \$253 million pre-tax gain from the sale of our SP Video CPE Business recorded in fiscal 2016.

### **Interest and Other Income (Loss), Net**

Interest Income (Expense), Net The following table summarizes interest income and interest expense (in millions):

	Years Ended			2018 vs. 2017	2017 vs. 2016
	July 28, 2018	July 29, 2017	July 30, 2016	Variance in Dollars	Variance in Dollars
Interest income .....	\$ 1,508	\$ 1,338	\$ 1,005	\$ 170	\$ 333
Interest expense .....	(943)	(861)	(676)	(82)	(185)
Interest income (expense), net .....	<u>\$ 565</u>	<u>\$ 477</u>	<u>\$ 329</u>	<u>\$ 88</u>	<u>\$ 148</u>

### Fiscal 2018 Compared with Fiscal 2017

Interest income increased driven by higher yields on our portfolio. The increase in interest expense was driven by the impact of higher effective interest rates.

### Fiscal 2017 Compared with Fiscal 2016

Interest income increased driven by an increase in our portfolio of cash, cash equivalents, and fixed income investments as well as higher yields on our portfolio. The increase in interest expense was driven by higher average debt balances, which includes commercial paper notes, and the impact of higher effective interest rates on floating-rate senior notes and interest rate swaps associated with fixed-rate senior notes.

Other Income (Loss), Net The components of other income (loss), net, are summarized as follows (in millions):

	Years Ended			2018 vs. 2017	2017 vs. 2016
	July 28, 2018	July 29, 2017	July 30, 2016	Variance in Dollars	Variance in Dollars
<b>Gains (losses) on investments, net:</b>					
Publicly traded equity securities .....	\$ 529	\$ (45)	\$ 33	\$ 574	\$ (78)
Fixed income securities .....	(242)	(42)	(34)	(200)	(8)
Total available-for-sale investments.....	<u>287</u>	<u>(87)</u>	<u>(1)</u>	<u>374</u>	<u>(86)</u>
Privately held companies .....	<u>11</u>	<u>(46)</u>	<u>(35)</u>	<u>57</u>	<u>(11)</u>
Net gains (losses) on investments .....	<u>298</u>	<u>(133)</u>	<u>(36)</u>	<u>431</u>	<u>(97)</u>
Other gains (losses), net.....	<u>(133)</u>	<u>(30)</u>	<u>(33)</u>	<u>(103)</u>	<u>3</u>
Other income (loss), net .....	<u>\$ 165</u>	<u>\$ (163)</u>	<u>\$ (69)</u>	<u>\$ 328</u>	<u>\$ (94)</u>

### Fiscal 2018 Compared with Fiscal 2017

The change in total net gains (losses) on available-for-sale investments was primarily attributable to higher realized gains on publicly traded equity securities and lower impairment charges on publicly traded equity securities, partially offset by higher realized losses on fixed income securities as a result of market conditions and the timing of sales of these securities.

The change in net gains (losses) on investments in privately held companies was primarily due to lower impairment charges partially offset by lower realized gains on investments in privately held companies.

The change in other gains (losses), net was primarily driven by higher donation expense, net unfavorable foreign exchange impacts and impacts from equity derivatives.

#### Fiscal 2017 Compared with Fiscal 2016

The change in total net gains (losses) on available-for-sale investments was driven by \$74 million of impairment charges on publicly traded equity securities.

The change in net gains (losses) on investments in privately held companies was primarily due to higher impairment charges on investments in privately held companies, partially offset by higher realized gains on investments in privately held companies.

The change in other gains (losses), net was driven by lower donation expense partially offset by impacts from customer lease terminations, foreign exchange and equity derivatives.

#### **Provision for Income Taxes**

##### Fiscal 2018 Compared with Fiscal 2017

The provision for income taxes resulted in an effective tax rate of 99.2% for fiscal 2018, compared with 21.8% for fiscal 2017. The net 77.4 percentage point increase in the effective tax rate was primarily due to the mandatory one-time transition tax on accumulated earnings of foreign subsidiaries, foreign withholding tax, and DTA re-measurement during fiscal 2018.

During fiscal 2018, we recorded a provisional tax expense of \$10.4 billion related to the Tax Act, comprised of \$8.1 billion of U.S. transition tax, \$1.2 billion of foreign withholding tax, and \$1.1 billion re-measurement of net DTA. We plan to pay the transition tax in installments over eight years in accordance with the Tax Act. The Tax Act is discussed more fully in Note 16 to the Consolidated Financial Statements.

As a result of the adoption of the new accounting standard on share-based compensation in fiscal 2018, our effective tax rate will increase or decrease based upon the tax effect of the difference between the share-based compensation expenses and the benefits taken on the company's tax returns. We recognize excess tax benefits on a discrete basis and therefore anticipate the effective tax rate to vary from quarter to quarter depending on our share price in each period.

For a full reconciliation of our effective tax rate to the U.S. federal statutory rate of 27% and for further explanation of our provision for income taxes, see Note 16 to the Consolidated Financial Statements.

##### Fiscal 2017 Compared with Fiscal 2016

The provision for income taxes resulted in an effective tax rate of 21.8% for fiscal 2017, compared with 16.9% for fiscal 2016. The net 4.9 percentage point increase in the effective tax rate was primarily due to the recognition of a net benefit to the provision for income taxes in fiscal 2016 related to our settlement with the IRS of all outstanding items covering fiscal 2008 through fiscal 2010 and reinstatement of the U.S. federal R&D tax credit on December 18, 2015.

## LIQUIDITY AND CAPITAL RESOURCES

The following sections discuss the effects of changes in our balance sheet, our capital allocation strategy including stock repurchase program and dividends, our contractual obligations, and certain other commitments and activities on our liquidity and capital resources.

### Balance Sheet and Cash Flows

Cash and Cash Equivalents and Investments The following table summarizes our cash and cash equivalents and investments (in millions):

	July 28, 2018	July 29, 2017	Increase (Decrease)
Cash and cash equivalents . . . . .	\$ 8,934	\$ 11,708	\$ (2,774)
Fixed income securities . . . . .	37,009	57,077	(20,068)
Publicly traded equity securities . . . . .	605	1,707	(1,102)
Total . . . . .	<u>\$ 46,548</u>	<u>\$ 70,492</u>	<u>\$ (23,944)</u>

The net decrease in cash and cash equivalents and investments from fiscal 2017 to fiscal 2018 was primarily driven by cash returned to shareholders in the form of repurchases of common stock of \$17.5 billion under the stock repurchase program and cash dividends of \$6.0 billion, net decrease in debt of \$8.0 billion, net cash paid for acquisitions of \$3.0 billion, the timing of settlements of investments and other of \$2.0 billion, and capital expenditures of \$0.8 billion. These uses of cash were partially offset by cash provided by operating activities of \$13.7 billion.

In fiscal 2018, we repatriated \$70 billion of foreign subsidiary earnings to the U.S. (in the form of cash, cash equivalents, or investments), and paid foreign withholding tax of \$1.2 billion. We also paid approximately \$125 million of other one-time foreign taxes as a result of the Tax Act. Future repatriation of cash and other property held by our foreign subsidiaries will generally not be subject to U.S. federal tax. As we evaluate the impact of the Tax Act and the future cash needs of our global operations, we may revise the amount of foreign earnings considered to be permanently reinvested in our foreign subsidiaries.

In addition to cash requirements in the normal course of business, on August 2, 2018 we announced our intent to acquire Duo Security, Inc. for a purchase consideration of approximately \$2.35 billion in cash and assumed equity awards. See further discussion of liquidity and future payments under “Contractual Obligations” and “Liquidity and Capital Resource Requirements” below.

We maintain an investment portfolio of various holdings, types, and maturities. We classify our investments as short-term investments based on their nature and their availability for use in current operations. We believe the overall credit quality of our portfolio is strong, with our cash equivalents and our fixed income investment portfolio consisting primarily of high quality investment-grade securities. We believe that our strong cash and cash equivalents and investments position allows us to use our cash resources for strategic investments to gain access to new technologies, for acquisitions, for customer financing activities, for working capital needs, and for the repurchase of shares of common stock and payment of dividends as discussed below.

Free Cash Flow and Capital Allocation As part of our capital allocation strategy, we intend to return a minimum of 50% of our free cash flow annually to our shareholders through cash dividends and repurchases of common stock.

We define free cash flow as net cash provided by operating activities less cash used to acquire property and equipment. The following table reconciles our net cash provided by operating activities to free cash flow (in millions):

Years Ended	July 28, 2018	July 29, 2017	July 30, 2016
Net cash provided by operating activities . . . . .	\$ 13,666	\$ 13,876	\$ 13,570
Acquisition of property and equipment . . . . .	(834)	(964)	(1,146)
Free cash flow . . . . .	<u>\$ 12,832</u>	<u>\$ 12,912</u>	<u>\$ 12,424</u>

We expect that cash provided by operating activities may fluctuate in future periods as a result of a number of factors, including fluctuations in our operating results, the rate at which products are shipped during the quarter (which we refer to as shipment linearity), the timing and collection of accounts receivable and financing receivables, inventory and supply chain management, deferred revenue and the timing and amount of tax and other payments. For additional discussion, see “Part I, Item 1A. Risk Factors” in this report.

We consider free cash flow to be a liquidity measure that provides useful information to management and investors because of our intent to return a stated percentage of free cash flow to shareholders in the form of dividends and stock repurchases. We further regard free cash flow as a useful measure because it reflects cash that can be used to, among other things, invest in our business, make strategic acquisitions, repurchase common stock, and pay dividends on our common stock, after deducting capital investments. A limitation of the utility of free cash flow as a measure of financial performance and liquidity is that the free cash flow does not represent the total increase or decrease in our cash balance for the period. In addition, we have other required uses of cash, including repaying the principal of our outstanding indebtedness. Free cash flow is not a measure calculated in accordance with U.S. generally accepted accounting principles and should not be regarded in isolation or as an alternative for net income provided by operating activities or any other measure calculated in accordance with such principles, and other companies may calculate free cash flow in a different manner than we do.

The following table summarizes the dividends paid and stock repurchases (in millions, except per-share amounts):

Years Ended	DIVIDENDS		STOCK REPURCHASE PROGRAM			TOTAL
	Per Share	Amount	Shares	Weighted-Average Price per Share	Amount	
<b>July 28, 2018</b>	<b>\$ 1.24</b>	<b>\$ 5,968</b>	<b>432</b>	<b>\$ 40.88</b>	<b>\$ 17,661</b>	<b>\$ 23,629</b>
July 29, 2017	\$ 1.10	\$ 5,511	118	\$ 31.38	\$ 3,706	\$ 9,217
July 30, 2016	\$ 0.94	\$ 4,750	148	\$ 26.45	\$ 3,918	\$ 8,668

Any future dividends are subject to the approval of our Board of Directors.

On February 14, 2018, our Board of Directors authorized a \$25 billion increase to the stock repurchase program. The remaining authorized amount for stock repurchases under this program, including the additional authorization, is approximately \$19.0 billion, with no termination date. We expect to utilize this remaining authorized amount for stock repurchases over the next 12 to 18 months.

The purchase price for the shares of our stock repurchased is reflected as a reduction to shareholders' equity. We are required to allocate the purchase price of the repurchased shares as (i) a reduction to retained earnings and (ii) a reduction of common stock and additional paid-in capital. As a result of future stock repurchases, we may report an accumulated deficit in future periods in shareholders' equity.

Accounts Receivable, Net The following table summarizes our accounts receivable, net (in millions):

	July 28, 2018	July 29, 2017	Increase (Decrease)
Accounts receivable, net	\$ 5,554	\$ 5,146	\$ 408

Our accounts receivable net, as of July 28, 2018 increased by approximately 8% compared with the end of fiscal 2017, primarily due to higher product billings in the fourth quarter of fiscal 2018 compared with the fourth quarter of fiscal 2017.

Inventory Supply Chain The following table summarizes our inventories and purchase commitments with contract manufacturers and suppliers (in millions):

	July 28, 2018	July 29, 2017	Increase (Decrease)
Inventories	\$ 1,846	\$ 1,616	\$ 230

Inventory as of July 28, 2018 increased by 14% from our inventory balance at the end of fiscal 2017. The increase in inventory was due to an increase in raw materials due to securing memory supply which is currently constrained and also higher levels of manufactured finished goods in support of current order activity.

Our finished goods consist of distributor inventory and deferred cost of sales and manufactured finished goods. Distributor inventory and deferred cost of sales are related to unrecognized revenue on shipments to distributors and retail partners as well as shipments to customers. Manufactured finished goods consist primarily of build-to-order and build-to-stock products.

We purchase components from a variety of suppliers and use several contract manufacturers to provide manufacturing services for our products. During the normal course of business, in order to manage manufacturing lead times and help ensure adequate component supply, we enter into agreements with contract manufacturers and suppliers that allow them to procure inventory based upon criteria as defined by us or that establish the parameters defining our requirements and our commitment to securing manufacturing capacity.

Our purchase commitments are for short-term product manufacturing requirements as well as for commitments to suppliers to secure manufacturing capacity. Certain of our purchase commitments with contract manufacturers and suppliers relate to arrangements to secure long-term pricing for certain product components for multi-year periods. A significant portion of our reported purchase commitments arising from these agreements are firm, noncancelable, and unconditional commitments. In certain instances, these agreements allow us the option to cancel, reschedule, and adjust our requirements based on our business needs prior to firm orders being placed. We believe our inventory and purchase commitments levels are in line with our current demand forecasts. The following table summarizes our purchase commitments with contract manufacturers and suppliers as of the respective period ends (in millions):

<u>Commitments by Period</u>	<u>July 28, 2018</u>	<u>July 29, 2017</u>
Less than 1 year . . . . .	\$ 5,407	\$ 4,620
1 to 3 years . . . . .	710	20
3 to 5 years . . . . .	360	—
Total . . . . .	<u>\$ 6,477</u>	<u>\$ 4,640</u>

Purchase commitments with contract manufacturers and suppliers increased by approximately 40% compared to the end of fiscal 2017. On a combined basis, inventories and purchase commitments with contract manufacturers and suppliers increased by 33% compared with the end of fiscal 2017.

Inventory and supply chain management remain areas of focus as we balance the need to maintain supply chain flexibility to help ensure competitive lead times with the risk of inventory obsolescence because of rapidly changing technology and customer requirements. We believe the amount of our inventory and purchase commitments is appropriate for our revenue levels.

Financing Receivables and Guarantees The following table summarizes our financing receivables (in millions):

	July 28, 2018	July 29, 2017	Increase (Decrease)
Lease receivables, net . . . . .	\$ 2,576	\$ 2,650	\$ (74)
Loan receivables, net . . . . .	4,939	4,457	482
Financed service contracts, net . . . . .	2,316	2,487	(171)
Total, net . . . . .	<u>\$ 9,831</u>	<u>\$ 9,594</u>	<u>\$ 237</u>

Financing Receivables Our financing arrangements include leases, loans, and financed service contracts. Lease receivables include sales-type and direct-financing leases. Arrangements related to leases are generally collateralized by a security interest in the underlying assets. Our loan receivables include customer financing for purchases of our hardware, software and services and also may include additional funds for other costs associated with network installation and integration of our products and services. We also provide financing to certain qualified customers for long-term service contracts, which primarily relate to technical support services. The majority of the revenue from these financed service contracts is deferred and is recognized ratably over the period during which the services are performed. Financing receivables increased by 2%. We expect to continue to expand the use of our financing programs in the near term.

Financing Guarantees In the normal course of business, third parties may provide financing arrangements to our customers and channel partners under financing programs. The financing arrangements to customers provided by third parties are related to leases and loans and typically have terms of up to three years. In some cases, we provide guarantees to third parties for these lease and loan arrangements. The financing arrangements to channel partners consist of revolving short-term financing provided by third parties, generally with payment terms ranging from 60 to 90 days. In certain instances, these financing arrangements result in a transfer of our receivables to the third party. The receivables are derecognized upon transfer, as these transfers qualify as true sales, and we receive payments for the receivables from the third party based on our standard payment terms.

The volume of channel partner financing was \$28.2 billion, \$27.0 billion, and \$26.9 billion in fiscal 2018, 2017, and 2016, respectively. These financing arrangements facilitate the working capital requirements of the channel partners, and in some cases, we guarantee a portion of these arrangements. The balance of the channel partner financing subject to guarantees was \$953 million and \$1.0 billion as of July 28, 2018 and July 29, 2017, respectively. We could be called upon to make payments under these guarantees in the event of nonpayment by the channel partners or end-user customers. Historically, our payments under these arrangements have been immaterial. Where we provide a guarantee, we defer the revenue associated with the channel partner and end-user financing arrangement in accordance with revenue recognition policies, or we record a liability for the fair value of the guarantees. In either case, the deferred revenue is recognized as revenue when the guarantee is removed. As of July 28, 2018, the total maximum potential future payments related to these guarantees was approximately \$308 million, of which approximately \$122 million was recorded as deferred revenue.

#### Borrowings

Senior Notes The following table summarizes the principal amount of our senior notes (in millions):

	Maturity Date	July 28, 2018	July 29, 2017
<b>Senior notes:</b>			
Floating-rate notes:			
Three-month LIBOR plus 0.60% .....	February 21, 2018	\$ —	\$ 1,000
Three-month LIBOR plus 0.31% .....	June 15, 2018	—	900
Three-month LIBOR plus 0.50% .....	March 1, 2019	<b>500</b>	500
Three-month LIBOR plus 0.34% .....	September 20, 2019	<b>500</b>	500
Fixed-rate notes:			
1.40% .....	February 28, 2018	—	1,250
1.65% .....	June 15, 2018	—	1,600
4.95% .....	February 15, 2019	<b>2,000</b>	2,000
1.60% .....	February 28, 2019	<b>1,000</b>	1,000
2.125% .....	March 1, 2019	<b>1,750</b>	1,750
1.40% .....	September 20, 2019	<b>1,500</b>	1,500
4.45% .....	January 15, 2020	<b>2,500</b>	2,500
2.45% .....	June 15, 2020	<b>1,500</b>	1,500
2.20% .....	February 28, 2021	<b>2,500</b>	2,500
2.90% .....	March 4, 2021	<b>500</b>	500
1.85% .....	September 20, 2021	<b>2,000</b>	2,000
3.00% .....	June 15, 2022	<b>500</b>	500
2.60% .....	February 28, 2023	<b>500</b>	500
2.20% .....	September 20, 2023	<b>750</b>	750
3.625% .....	March 4, 2024	<b>1,000</b>	1,000
3.50% .....	June 15, 2025	<b>500</b>	500
2.95% .....	February 28, 2026	<b>750</b>	750
2.50% .....	September 20, 2026	<b>1,500</b>	1,500
5.90% .....	February 15, 2039	<b>2,000</b>	2,000
5.50% .....	January 15, 2040	<b>2,000</b>	2,000
Total .....		<b>\$ 25,750</b>	<b>\$ 30,500</b>

Interest is payable semiannually on each class of the senior fixed-rate notes, each of which is redeemable by us at any time, subject to a make-whole premium. Interest is payable quarterly on the floating-rate notes. We were in compliance with all debt covenants as of July 28, 2018.

Commercial Paper We have a short-term debt financing program in which up to \$10.0 billion is available through the issuance of commercial paper notes. We use the proceeds from the issuance of commercial paper notes for general corporate purposes. We had no commercial paper notes and \$3.2 billion in commercial paper notes outstanding as of July 28, 2018 and July 29, 2017, respectively.

**Credit Facility** On May 15, 2015, we entered into a credit agreement with certain institutional lenders that provides for a \$3.0 billion unsecured revolving credit facility that is scheduled to expire on May 15, 2020. Any advances under the credit agreement will accrue interest at rates that are equal to, based on certain conditions, either (i) the highest of (a) the Federal Funds rate plus 0.50%, (b) Bank of America's "prime rate" as announced from time to time, or (c) LIBOR, or a comparable or successor rate that is approved by the Administrative Agent ("Eurocurrency Rate"), for an interest period of one month plus 1.00%, or (ii) the Eurocurrency Rate, plus a margin that is based on our senior debt credit ratings as published by Standard & Poor's Financial Services, LLC and Moody's Investors Service, Inc., provided that in no event will the Eurocurrency Rate be less than zero. We may also, upon the agreement of either the then-existing lenders or additional lenders not currently parties to the agreement, increase the commitments under the credit facility by up to an additional \$2.0 billion and/or extend the expiration date of the credit facility up to May 15, 2022. This credit agreement requires that we comply with certain covenants, including that we maintain an interest coverage ratio as defined in the agreement. As of July 28, 2018, we were in compliance with the required interest coverage ratio and the other covenants, and we had not borrowed any funds under the credit facility.

**Deferred Revenue** The following table presents the breakdown of deferred revenue (in millions):

	<b>July 28, 2018</b>	July 29, 2017	Increase (Decrease)
Service . . . . .	<b>\$ 11,431</b>	\$ 11,302	\$ 129
Product:			
Deferred revenue related to recurring software and subscription offers . . . . .	<b>6,120</b>	4,971	1,149
Other product deferred revenue . . . . .	<b>2,134</b>	2,221	(87)
Total product deferred revenue . . . . .	<b>8,254</b>	7,192	1,062
Total . . . . .	<b>\$ 19,685</b>	\$ 18,494	\$ 1,191
Reported as:			
Current . . . . .	<b>\$ 11,490</b>	\$ 10,821	\$ 669
Noncurrent . . . . .	<b>8,195</b>	7,673	522
Total . . . . .	<b>\$ 19,685</b>	\$ 18,494	\$ 1,191

Total deferred revenue increased 6% in fiscal 2018. Deferred product revenue increased 15% primarily due to product deferred revenue related to recurring software and subscription offers, which grew 23% on a year-over-year basis to \$6.1 billion. Deferred service revenue increased 1%, driven by the impact of contract renewals, partially offset by amortization of deferred service revenue.

### Contractual Obligations

The impact of contractual obligations on our liquidity and capital resources in future periods should be analyzed in conjunction with the factors that impact our cash flows from operations discussed previously. In addition, we plan for and measure our liquidity and capital resources through an annual budgeting process. The following table summarizes our contractual obligations at July 28, 2018 (in millions):

July 28, 2018	PAYMENTS DUE BY PERIOD				
	Total	Less than 1 Year	1 to 3 Years	3 to 5 Years	More than 5 Years
Operating leases . . . . .	\$ 1,220	\$ 392	\$ 483	\$ 234	\$ 111
Purchase commitments with contract manufacturers and suppliers . . . . .	6,477	5,407	710	360	—
Other purchase obligations . . . . .	2,192	956	976	125	135
Senior notes . . . . .	25,750	5,250	9,000	3,000	8,500
Transition tax payable . . . . .	8,094	787	1,302	1,302	4,703
Other long-term liabilities . . . . .	1,293	—	264	168	861
Total by period . . . . .	<b>\$ 45,026</b>	<b>\$ 12,792</b>	<b>\$ 12,735</b>	<b>\$ 5,189</b>	<b>\$ 14,310</b>
Other long-term liabilities (uncertainty in the timing of future payments) . . . . .	1,419				
Total . . . . .	<b><u>\$ 46,445</u></b>				

**Operating Leases** For more information on our operating leases, see Note 12 to the Consolidated Financial Statements.

Purchase Commitments with Contract Manufacturers and Suppliers We purchase components from a variety of suppliers and use several contract manufacturers to provide manufacturing services for our products. Our purchase commitments are for short-term product manufacturing requirements as well as for commitments to suppliers to secure manufacturing capacity. Certain of our purchase commitments with contract manufacturers and suppliers relate to arrangements to secure long-term pricing for certain product components for multi-year periods. A significant portion of our reported estimated purchase commitments arising from these agreements are firm, noncancelable, and unconditional commitments. We record a liability for firm, noncancelable, and unconditional purchase commitments for quantities in excess of our future demand forecasts consistent with the valuation of our excess and obsolete inventory. See further discussion in “Inventory Supply Chain.” As of July 28, 2018, the liability for these purchase commitments was \$159 million and is recorded in other current liabilities and is not included in the preceding table.

Other Purchase Obligations Other purchase obligations represent an estimate of all contractual obligations in the ordinary course of business, other than operating leases and commitments with contract manufacturers and suppliers, for which we have not received the goods or services. Purchase orders are not included in the preceding table as they typically represent our authorization to purchase rather than binding contractual purchase obligations.

Long-Term Debt The amount of long-term debt in the preceding table represents the principal amount of the respective debt instruments. See Note 10 to the Consolidated Financial Statements.

Transition Tax Payable In connection with the Tax Act, we recorded an income tax payable of \$8.1 billion for the U.S. transition tax on accumulated earnings of foreign subsidiaries. Amounts associated with the Tax Act are considered provisional and may be subject to further adjustment during the measurement period. See Note 16 to the Consolidated Financial Statements.

Other Long-Term Liabilities Other long-term liabilities primarily include noncurrent income taxes payable, accrued liabilities for deferred compensation, deferred tax liabilities, and certain other long-term liabilities. Due to the uncertainty in the timing of future payments, our noncurrent income taxes payable of approximately \$1,278 million and deferred tax liabilities of \$141 million were presented as one aggregated amount in the total column on a separate line in the preceding table. Noncurrent income taxes payable include uncertain tax positions. See Note 16 to the Consolidated Financial Statements.

## **Other Commitments**

In connection with our acquisitions, we have agreed to pay certain additional amounts contingent upon the achievement of certain agreed-upon technology, development, product, or other milestones or the continued employment with us of certain employees of the acquired entities. See Note 12 to the Consolidated Financial Statements.

We also have certain funding commitments primarily related to our investments in privately held companies and venture funds, some of which are based on the achievement of certain agreed-upon milestones, and some of which are required to be funded on demand. The funding commitments were \$223 million as of July 28, 2018, compared with \$216 million as of July 29, 2017.

## **Off-Balance Sheet Arrangements**

We consider our investments in unconsolidated variable interest entities to be off-balance sheet arrangements. In the ordinary course of business, we have investments in privately held companies including venture funds and provide financing to certain customers. Certain of these investments are considered to be variable interest entities. We evaluate on an ongoing basis our investments in these privately held companies and customer financings, and we have determined that as of July 28, 2018 there were no material unconsolidated variable interest entities.

On an ongoing basis, we reassess our investments in privately held companies and customer financings to determine if they are variable interest entities and if we would be regarded as the primary beneficiary pursuant to the applicable accounting guidance. As a result of this ongoing assessment, we may be required to make additional disclosures or consolidate these entities. Because we may not control these entities, we may not have the ability to influence these events.

We provide financing guarantees, which are generally for various third-party financing arrangements extended to our channel partners and end-user customers. We could be called upon to make payments under these guarantees in the event of nonpayment by the channel partners or end-user customers. See the previous discussion of these financing guarantees under “Financing Receivables and Guarantees.”

## **Liquidity and Capital Resource Requirements**

Based on past performance and current expectations, we believe our cash and cash equivalents, investments, cash generated from operations, and ability to access capital markets and committed credit lines will satisfy, through at least the next 12 months, our liquidity requirements, both in total and domestically, including the following: working capital needs, capital expenditures, investment requirements, stock repurchases, cash dividends, contractual obligations, commitments, principal and interest payments on debt, pending acquisitions, future customer financings, and other liquidity requirements associated with our operations. There are no other transactions, arrangements, or relationships with unconsolidated entities or other persons that are reasonably likely to materially affect the liquidity and the availability of, as well as our requirements for, capital resources.

## **Item 7A. Quantitative and Qualitative Disclosures About Market Risk**

Our financial position is exposed to a variety of risks, including interest rate risk, equity price risk, and foreign currency exchange risk.

### **Interest Rate Risk**

**Fixed Income Securities** We maintain an investment portfolio of various holdings, types, and maturities. Our primary objective for holding fixed income securities is to achieve an appropriate investment return consistent with preserving principal and managing risk. At any time, a sharp rise in market interest rates could have a material adverse impact on the fair value of our fixed income investment portfolio. Conversely, declines in interest rates, including the impact from lower credit spreads, could have a material adverse impact on interest income for our investment portfolio. We may utilize derivative instruments designated as hedging instruments to achieve our investment objectives. We had no outstanding hedging instruments for our fixed income securities as of July 28, 2018. Our fixed income investments are held for purposes other than trading. Our fixed income investments are not leveraged as of July 28, 2018. We monitor our interest rate and credit risks, including our credit exposures to specific rating categories and to individual issuers. We believe the overall credit quality of our portfolio is strong.

The following tables present the hypothetical fair values of our fixed income securities, including the hedging effects when applicable, as a result of selected potential market decreases and increases in interest rates. The market changes reflect immediate hypothetical parallel shifts in the yield curve of plus or minus 50 basis points ("BPS"), plus 100 BPS, and plus 150 BPS. The hypothetical fair values as of July 28, 2018 and July 29, 2017 are as follows (in millions):

	VALUATION OF SECURITIES GIVEN AN INTEREST RATE DECREASE OF X BASIS POINTS			FAIR VALUE AS OF <b>JULY 28, 2018</b>	VALUATION OF SECURITIES GIVEN AN INTEREST RATE INCREASE OF X BASIS POINTS		
	(150 BPS)	(100 BPS)	(50 BPS)		50 BPS	100 BPS	150 BPS
	\$37,786	\$37,527	\$37,268		\$36,750	\$36,491	\$36,231
Fixed income securities . . . . .							
	VALUATION OF SECURITIES GIVEN AN INTEREST RATE DECREASE OF X BASIS POINTS			FAIR VALUE AS OF <b>JULY 29, 2017</b>	VALUATION OF SECURITIES GIVEN AN INTEREST RATE INCREASE OF X BASIS POINTS		
	(150 BPS)	(100 BPS)	(50 BPS)		50 BPS	100 BPS	150 BPS
	\$58,728	\$58,177	\$57,627		\$57,077	\$56,527	\$55,977
Fixed income securities . . . . .							

**Financing Receivables** As of July 28, 2018, our financing receivables had a carrying value of \$9.8 billion, compared with \$9.6 billion as of July 29, 2017. As of July 28, 2018, a hypothetical 50 BPS increase or decrease in market interest rates would change the fair value of our financing receivables by a decrease or increase of approximately \$0.1 billion, respectively.

**Debt** As of July 28, 2018, we had \$25.8 billion in principal amount of senior notes outstanding, which consisted of \$1.0 billion in floating-rate notes and \$24.8 billion in fixed-rate notes. The carrying amount of the senior notes was \$25.6 billion, and the related fair value based on market prices was \$26.4 billion. As of July 28, 2018, a hypothetical 50 BPS increase or decrease in market interest rates would change the fair value of the fixed-rate debt, excluding the \$6.8 billion of hedged debt, by a decrease or increase of approximately \$0.5 billion, respectively. However, this hypothetical change in interest rates would not impact the interest expense on the fixed-rate debt that is not hedged.

### **Equity Price Risk**

The fair value of our equity investments in publicly traded companies is subject to market price volatility. We may hold equity securities for strategic purposes or to diversify our overall investment portfolio. Our equity portfolio consists of securities with characteristics that most closely match the Standard & Poor's 500 Index or Nasdaq Composite Index. These equity securities are held for purposes other than trading. To manage our exposure to changes in the fair value of certain equity securities, we may enter into equity derivatives designated as hedging instruments.

**Publicly Traded Equity Securities** The following tables present the hypothetical fair values of publicly traded equity securities as a result of selected potential decreases and increases in the price of each equity security in the portfolio, excluding hedged equity securities, if any. Potential fluctuations in the price of each equity security in the portfolio of plus or minus 10%, 20%, and 30% were selected based on potential near-term changes in those security prices.

The hypothetical fair values as of July 28, 2018 and July 29, 2017 are as follows (in millions):

	VALUATION OF SECURITIES GIVEN AN X% DECREASE IN EACH STOCK'S PRICE			FAIR VALUE AS OF <b>JULY 28, 2018</b>	VALUATION OF SECURITIES GIVEN AN X% INCREASE IN EACH STOCK'S PRICE		
	(30)%	(20)%	(10)%		10%	20%	30%
	\$424	\$484	\$545		\$605	\$666	\$726
Publicly traded equity securities . . . . .							
	VALUATION OF SECURITIES GIVEN AN X% DECREASE IN EACH STOCK'S PRICE			FAIR VALUE AS OF <b>JULY 29, 2017</b>	VALUATION OF SECURITIES GIVEN AN X% INCREASE IN EACH STOCK'S PRICE		
	(30)%	(20)%	(10)%		10%	20%	30%
	\$1,195	\$1,366	\$1,536		\$1,707	\$1,878	\$2,048
Publicly traded equity securities . . . . .							

**Investments in Privately Held Companies** We have also invested in privately held companies. These investments are recorded in other assets in our Consolidated Balance Sheets and are accounted for using primarily either the cost or the equity method. As of July 28, 2018, the total carrying amount of our investments in privately held companies was \$1,096 million, compared with \$983 million at July 29, 2017. Some of the privately held companies in which we invested are in the startup or development stages. These investments are inherently risky because the markets for the technologies or products these companies are developing are typically in the early stages and may never materialize. We could lose our entire investment in these companies. Our evaluation of investments in privately held companies is based on the fundamentals of the businesses invested in, including, among other factors, the nature of their technologies and potential for financial return.

### Foreign Currency Exchange Risk

Our foreign exchange forward and option contracts outstanding at fiscal year-end are summarized in U.S. dollar equivalents as follows (in millions):

	July 28, 2018		July 29, 2017	
	Notional Amount	Fair Value	Notional Amount	Fair Value
<b>Forward contracts:</b>				
Purchased . . . . .	\$ 1,850	\$ (2)	\$ 2,562	\$ 39
Sold . . . . .	\$ 845	\$ 2	\$ 729	\$ (2)
<b>Option contracts:</b>				
Purchased . . . . .	\$ —	\$ —	\$ 528	\$ 7
Sold . . . . .	\$ —	\$ —	\$ 486	\$ (1)

We conduct business globally in numerous currencies. The direct effect of foreign currency fluctuations on revenue has not been material because our revenue is primarily denominated in U.S. dollars. However, if the U.S. dollar strengthens relative to other currencies, such strengthening could have an indirect effect on our revenue to the extent it raises the cost of our products to non-U.S. customers and thereby reduces demand. A weaker U.S. dollar could have the opposite effect. However, the precise indirect effect of currency fluctuations is difficult to measure or predict because our revenue is influenced by many factors in addition to the impact of such currency fluctuations.

Approximately 70% of our operating expenses are U.S.-dollar denominated. In fiscal 2018, foreign currency fluctuations, net of hedging, increased our combined R&D, sales and marketing, and G&A expenses by approximately \$93 million, or 0.5%, as compared with fiscal 2017. In fiscal 2017, foreign currency fluctuations, net of hedging, decreased our combined R&D, sales and marketing, and G&A expenses by approximately \$77 million, or 0.4%, as compared with fiscal 2016. To reduce variability in operating expenses and service cost of sales caused by non-U.S.-dollar denominated operating expenses and costs, we may hedge certain forecasted foreign currency transactions with currency options and forward contracts. These hedging programs are not designed to provide foreign currency protection over long time horizons. In designing a specific hedging approach, we consider several factors, including offsetting exposures, significance of exposures, costs associated with entering into a particular hedge instrument, and potential effectiveness of the hedge. The gains and losses on foreign exchange contracts mitigate the effect of currency movements on our operating expenses and service cost of sales.

We also enter into foreign exchange forward and option contracts to reduce the short-term effects of foreign currency fluctuations on receivables and payables that are denominated in currencies other than the functional currencies of the entities. The market risks associated with these foreign currency receivables, investments, and payables relate primarily to variances from our forecasted foreign currency transactions and balances. We do not enter into foreign exchange forward or option contracts for speculative purposes.

**Item 8. Financial Statements and Supplementary Data****Index to Consolidated Financial Statements**

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## **Report of Independent Registered Public Accounting Firm**

To the Board of Directors and Shareholders of Cisco Systems, Inc.

### ***Opinions on the Financial Statements and Internal Control over Financial Reporting***

We have audited the accompanying consolidated balance sheets of Cisco Systems, Inc. and its subsidiaries ("the Company") as of July 28, 2018 and July 29, 2017, and the related consolidated statements of operations, comprehensive income (loss), cash flows and equity for each of the three years in the period ended July 28, 2018, including the related notes and schedule of valuation and qualifying accounts for each of the three years in the period ended July 28, 2018 appearing under Item 15(a)(2) (collectively referred to as the "consolidated financial statements"). We also have audited the Company's internal control over financial reporting as of July 28, 2018, based on criteria established in *Internal Control - Integrated Framework* (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Company as of July 28, 2018 and July 29, 2017, and the results of its operations and its cash flows for each of the three years in the period ended July 28, 2018 in conformity with accounting principles generally accepted in the United States of America. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of July 28, 2018, based on criteria established in *Internal Control - Integrated Framework* (2013) issued by the COSO.

### ***Basis for Opinions***

The Company's management is responsible for these consolidated financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express opinions on the Company's consolidated financial statements and on the Company's internal control over financial reporting based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) ("PCAOB") and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement, whether due to error or fraud, and whether effective internal control over financial reporting was maintained in all material respects.

Our audits of the consolidated financial statements included performing procedures to assess the risks of material misstatement of the consolidated financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the consolidated financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

### ***Definition and Limitations of Internal Control over Financial Reporting***

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

*PricewaterhouseCoopers LLP*

San Jose, California  
September 6, 2018

We have served as the Company's auditor since 1988.

## **Reports of Management**

### **Statement of Management's Responsibility**

Cisco's management has always assumed full accountability for maintaining compliance with our established financial accounting policies and for reporting our results with objectivity and the highest degree of integrity. It is critical for investors and other users of the Consolidated Financial Statements to have confidence that the financial information that we provide is timely, complete, relevant, and accurate. Management is responsible for the fair presentation of Cisco's Consolidated Financial Statements, prepared in accordance with accounting principles generally accepted in the United States of America, and has full responsibility for their integrity and accuracy.

Management, with oversight by Cisco's Board of Directors, has established and maintains a strong ethical climate so that our affairs are conducted to the highest standards of personal and corporate conduct. Management also has established an effective system of internal controls. Cisco's policies and practices reflect corporate governance initiatives that are compliant with the listing requirements of Nasdaq and the corporate governance requirements of the Sarbanes-Oxley Act of 2002.

We are committed to enhancing shareholder value and fully understand and embrace our fiduciary oversight responsibilities. We are dedicated to ensuring that our high standards of financial accounting and reporting, as well as our underlying system of internal controls, are maintained. Our culture demands integrity, and we have the highest confidence in our processes, our internal controls and our people, who are objective in their responsibilities and who operate under the highest level of ethical standards.

### **Management's Report on Internal Control over Financial Reporting**

Management is responsible for establishing and maintaining adequate internal control over financial reporting for Cisco. Internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. Internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of the assets of the Company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles and that receipts and expenditures of the Company are being made only in accordance with authorizations of management and directors of the Company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the Company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions or that the degree of compliance with the policies or procedures may deteriorate.

Management (with the participation of the principal executive officer and principal financial officer) conducted an evaluation of the effectiveness of Cisco's internal control over financial reporting based on the framework in *Internal Control—Integrated Framework* (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this evaluation, management concluded that Cisco's internal control over financial reporting was effective as of July 28, 2018. PricewaterhouseCoopers LLP, an independent registered public accounting firm, has audited the effectiveness of Cisco's internal control over financial reporting and has issued a report on Cisco's internal control over financial reporting, which is included in their report on the preceding page.



Charles H. Robbins  
Chairman and Chief Executive Officer  
September 6, 2018



Kelly A. Kramer  
Executive Vice President and Chief Financial Officer  
September 6, 2018

**CISCO SYSTEMS, INC.**  
**Consolidated Balance Sheets**  
(in millions, except par value)

	<u>July 28, 2018</u>	<u>July 29, 2017</u>
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents .....	\$ 8,934	\$ 11,708
Investments .....	<u>37,614</u>	58,784
Accounts receivable, net of allowance for doubtful accounts of \$129 at July 28, 2018 and \$211 at July 29, 2017 .....	5,554	5,146
Inventories .....	1,846	1,616
Financing receivables, net .....	4,949	4,856
Other current assets .....	<u>2,940</u>	1,593
Total current assets.....	<u>61,837</u>	83,703
Property and equipment, net .....	3,006	3,322
Financing receivables, net .....	4,882	4,738
Goodwill .....	<u>31,706</u>	29,766
Purchased intangible assets, net .....	2,552	2,539
Deferred tax assets .....	3,219	4,239
Other assets .....	<u>1,582</u>	1,511
<b>TOTAL ASSETS</b> .....	<u><u>\$ 108,784</u></u>	<u><u>\$ 129,818</u></u>
<b>LIABILITIES AND EQUITY</b>		
Current liabilities:		
Short-term debt .....	\$ 5,238	\$ 7,992
Accounts payable .....	1,904	1,385
Income taxes payable .....	1,004	98
Accrued compensation .....	2,986	2,895
Deferred revenue .....	<u>11,490</u>	10,821
Other current liabilities .....	<u>4,413</u>	4,392
Total current liabilities.....	<u>27,035</u>	27,583
Long-term debt .....	<u>20,331</u>	25,725
Income taxes payable .....	8,585	1,250
Deferred revenue .....	<u>8,195</u>	7,673
Other long-term liabilities .....	<u>1,434</u>	1,450
Total liabilities .....	<u><u>65,580</u></u>	<u><u>63,681</u></u>
Commitments and contingencies (Note 12)		
Equity:		
Cisco shareholders' equity:		
Preferred stock, no par value: 5 shares authorized; none issued and outstanding .....	—	—
Common stock and additional paid-in capital, \$0.001 par value: 20,000 shares authorized; 4,614 and 4,983 shares issued and outstanding at July 28, 2018 and July 29, 2017, respectively .....	<u>42,820</u>	45,253
Retained earnings .....	<u>1,233</u>	20,838
Accumulated other comprehensive income (loss) .....	<u>(849)</u>	46
Total Cisco shareholders' equity .....	<u><u>43,204</u></u>	66,137
Noncontrolling interests .....	—	—
Total equity .....	<u><u>43,204</u></u>	66,137
<b>TOTAL LIABILITIES AND EQUITY</b> .....	<u><u>\$ 108,784</u></u>	<u><u>\$ 129,818</u></u>

See Notes to Consolidated Financial Statements.

**CISCO SYSTEMS, INC.**  
**Consolidated Statements of Operations**  
(in millions, except per-share amounts)

Years Ended	<u>July 28, 2018</u>	<u>July 29, 2017</u>	<u>July 30, 2016</u>
<b>REVENUE:</b>			
Product .....	\$ 36,709	\$ 35,705	\$ 37,254
Service .....	<u>12,621</u>	<u>12,300</u>	<u>11,993</u>
Total revenue .....	<u><b>49,330</b></u>	<u><b>48,005</b></u>	<u><b>49,247</b></u>
<b>COST OF SALES:</b>			
Product .....	<u>14,427</u>	13,699	14,161
Service .....	<u>4,297</u>	<u>4,082</u>	<u>4,126</u>
Total cost of sales .....	<u><b>18,724</b></u>	<u><b>17,781</b></u>	<u><b>18,287</b></u>
<b>GROSS MARGIN</b> .....			
	<u><b>30,606</b></u>	<u><b>30,224</b></u>	<u><b>30,960</b></u>
<b>OPERATING EXPENSES:</b>			
Research and development .....	<u>6,332</u>	6,059	6,296
Sales and marketing .....	<u>9,242</u>	9,184	9,619
General and administrative .....	<u>2,144</u>	1,993	1,814
Amortization of purchased intangible assets .....	<u>221</u>	259	303
Restructuring and other charges .....	<u>358</u>	<u>756</u>	<u>268</u>
Total operating expenses .....	<u><b>18,297</b></u>	<u><b>18,251</b></u>	<u><b>18,300</b></u>
<b>OPERATING INCOME</b> .....			
Interest income .....	<u>1,508</u>	1,338	1,005
Interest expense .....	<u>(943)</u>	<u>(861)</u>	<u>(676)</u>
Other income (loss), net .....	<u>165</u>	<u>(163)</u>	<u>(69)</u>
Interest and other income (loss), net .....	<u><b>730</b></u>	<u><b>314</b></u>	<u><b>260</b></u>
<b>INCOME BEFORE PROVISION FOR INCOME TAXES</b> .....			
Provision for income taxes .....	<u><b>13,039</b></u>	<u><b>12,287</b></u>	<u><b>12,920</b></u>
<b>NET INCOME</b> .....			
	<u><b>\$ 110</b></u>	<u><b>\$ 9,609</b></u>	<u><b>\$ 10,739</b></u>
Net income per share:			
Basic .....	<u><b>\$ 0.02</b></u>	<u><b>\$ 1.92</b></u>	<u><b>\$ 2.13</b></u>
Diluted .....	<u><b>\$ 0.02</b></u>	<u><b>\$ 1.90</b></u>	<u><b>\$ 2.11</b></u>
Shares used in per-share calculation:			
Basic .....	<u><b>4,837</b></u>	<u><b>5,010</b></u>	<u><b>5,053</b></u>
Diluted .....	<u><b>4,881</b></u>	<u><b>5,049</b></u>	<u><b>5,088</b></u>
Cash dividends declared per common share .....	<u><b>\$ 1.24</b></u>	<u><b>\$ 1.10</b></u>	<u><b>\$ 0.94</b></u>

See Notes to Consolidated Financial Statements.

**CISCO SYSTEMS, INC.**  
**Consolidated Statements of Comprehensive Income (Loss)**  
(in millions)

Years Ended	<b>July 28, 2018</b>	<b>July 29, 2017</b>	<b>July 30, 2016</b>
Net income.....	<b>\$ 110</b>	<b>\$ 9,609</b>	<b>\$ 10,739</b>
Available-for-sale investments:			
Change in net unrealized gains and losses, net of tax benefit (expense) of \$(11), \$74, and \$(49) for fiscal 2018, 2017, and 2016, respectively .....	<b>(554)</b>	(89)	92
Net (gains) losses reclassified into earnings, net of tax expense (benefit) of \$104, \$(37), and \$0 for fiscal 2018, 2017, and 2016, respectively .....	<b>(183)</b>	50	1
	<b>(737)</b>	(39)	93
Cash flow hedging instruments:			
Change in unrealized gains and losses, net of tax benefit (expense) of \$(3), \$(5), and \$7 for fiscal 2018, 2017, and 2016, respectively .....	<b>18</b>	17	(59)
Net (gains) losses reclassified into earnings, net of tax (benefit) expense of \$7, \$(5), and \$(4) for fiscal 2018, 2017, and 2016, respectively .....	<b>(61)</b>	74	16
	<b>(43)</b>	91	(43)
Net change in cumulative translation adjustment and actuarial gains and losses, net of tax benefit (expense) of \$(8), \$(13), and \$(42) for fiscal 2018, 2017, and 2016, respectively .....	<b>(160)</b>	321	(447)
Other comprehensive income (loss) .....	<b>(940)</b>	373	(397)
Comprehensive income (loss) .....	<b>(830)</b>	9,982	10,342
Comprehensive (income) loss attributable to noncontrolling interests.....	—	(1)	10
Comprehensive income (loss) attributable to Cisco Systems, Inc.....	<b>\$ (830)</b>	<b>\$ 9,981</b>	<b>\$ 10,352</b>

See Notes to Consolidated Financial Statements.

**CISCO SYSTEMS, INC.**  
**Consolidated Statements of Cash Flows**  
(in millions)

Years Ended		July 28, 2018	July 29, 2017	July 30, 2016
Cash flows from operating activities:				
Net income .....	\$ 110	\$ 9,609	\$ 10,739	
Adjustments to reconcile net income to net cash provided by operating activities:				
Depreciation, amortization, and other .....	2,192	2,286	2,150	
Share-based compensation expense.....	1,576	1,526	1,458	
Provision (benefit) for receivables .....	(134)	(8)	(9)	
Deferred income taxes .....	900	(124)	(194)	
Excess tax benefits from share-based compensation .....	—	(153)	(129)	
(Gains) losses on divestitures, investments and other, net.....	(322)	154	(317)	
Change in operating assets and liabilities, net of effects of acquisitions and divestitures:				
Accounts receivable .....	(269)	756	(404)	
Inventories .....	(244)	(394)	315	
Financing receivables.....	(219)	(1,038)	(150)	
Other assets .....	66	15	(37)	
Accounts payable .....	504	311	(65)	
Income taxes, net .....	8,118	60	(300)	
Accrued compensation.....	100	(110)	(101)	
Deferred revenue .....	1,205	1,683	1,219	
Other liabilities.....	83	(697)	(605)	
Net cash provided by operating activities .....	<u>13,666</u>	<u>13,876</u>	<u>13,570</u>	
Cash flows from investing activities:				
Purchases of investments.....	(14,285)	(42,702)	(46,760)	
Proceeds from sales of investments.....	17,706	28,827	28,778	
Proceeds from maturities of investments .....	15,769	12,143	14,115	
Acquisition of businesses, net of cash and cash equivalents acquired .....	(3,006)	(3,324)	(3,161)	
Proceeds from business divestitures .....	27	—	372	
Purchases of investments in privately held companies.....	(267)	(222)	(256)	
Return of investments in privately held companies .....	168	203	91	
Acquisition of property and equipment.....	(834)	(964)	(1,146)	
Proceeds from sales of property and equipment.....	59	7	41	
Other.....	(13)	39	(191)	
Net cash provided by (used in) investing activities .....	<u>15,324</u>	<u>(5,993)</u>	<u>(8,117)</u>	
Cash flows from financing activities:				
Issuances of common stock .....	623	708	1,127	
Repurchases of common stock - repurchase program.....	(17,547)	(3,685)	(3,909)	
Shares repurchased for tax withholdings on vesting of restricted stock units .....	(703)	(619)	(557)	
Short-term borrowings, original maturities of 90 days or less, net .....	(2,502)	2,497	(4)	
Issuances of debt .....	6,877	6,980	6,978	
Repayments of debt .....	(12,375)	(4,151)	(3,863)	
Excess tax benefits from share-based compensation .....	—	153	129	
Dividends paid .....	(5,968)	(5,511)	(4,750)	
Other.....	(169)	(178)	150	
Net cash used in financing activities .....	<u>(31,764)</u>	<u>(3,806)</u>	<u>(4,699)</u>	
Net (decrease) increase in cash and cash equivalents .....	<u>(2,774)</u>	<u>4,077</u>	<u>754</u>	
Cash and cash equivalents, beginning of fiscal year .....	<u>11,708</u>	<u>7,631</u>	<u>6,877</u>	
Cash and cash equivalents, end of fiscal year.....	<u>\$ 8,934</u>	<u>\$ 11,708</u>	<u>\$ 7,631</u>	
Supplemental cash flow information:				
Cash paid for interest .....	\$ 910	\$ 897	\$ 859	
Cash paid for income taxes, net .....	\$ 3,911	\$ 2,742	\$ 2,675	

See Notes to Consolidated Financial Statements.

**CISCO SYSTEMS, INC.**  
**Consolidated Statements of Equity**  
(in millions, except per-share amounts)

	Common Stock		Accumulated Other Comprehensive Income (Loss)		Total Cisco Shareholders' Equity	Non-controlling Interests	Total Equity
	Shares of Common Stock	and Additional Paid-In Capital	Retained Earnings	Income (Loss)			
BALANCE AT JULY 25, 2015 .....	5,085	\$ 43,592	\$ 16,045	\$ 61	\$ 59,698	\$ 9	\$ 59,707
Net income .....			10,739		10,739		10,739
Other comprehensive income (loss) .....				(387)	(387)	(10)	(397)
Issuance of common stock .....	113	1,127			1,127		1,127
Repurchase of common stock .....	(148)	(1,280)	(2,638)		(3,918)		(3,918)
Shares repurchased for tax withholdings on vesting of restricted stock units .....	(21)	(557)			(557)		(557)
Cash dividends declared (\$0.94 per common share) .....			(4,750)		(4,750)		(4,750)
Tax effects from employee stock incentive plans .....		30			30		30
Share-based compensation .....		1,458			1,458		1,458
Purchase acquisitions and other .....		146			146		146
BALANCE AT JULY 30, 2016 .....	5,029	\$ 44,516	\$ 19,396	\$ (326)	\$ 63,586	\$ (1)	\$ 63,585
Net income .....			9,609		9,609		9,609
Other comprehensive income (loss) .....				372	372	1	373
Issuance of common stock .....	92	708			708		708
Repurchase of common stock .....	(118)	(1,050)	(2,656)		(3,706)		(3,706)
Shares repurchased for tax withholdings on vesting of restricted stock units .....	(20)	(619)			(619)		(619)
Cash dividends declared (\$1.10 per common share) .....			(5,511)		(5,511)		(5,511)
Tax effects from employee stock incentive plans .....		(10)			(10)		(10)
Share-based compensation .....		1,540			1,540		1,540
Purchase acquisitions and other .....		168			168		168
BALANCE AT JULY 29, 2017 .....	4,983	\$ 45,253	\$ 20,838	\$ 46	\$ 66,137	\$ —	\$ 66,137
Net income .....			110		110		110
Other comprehensive income (loss) .....				(940)	(940)		(940)
Issuance of common stock .....	83	623			623		623
Repurchase of common stock .....	(432)	(3,950)	(13,711)		(17,661)		(17,661)
Shares repurchased for tax withholdings on vesting of restricted stock units .....	(20)	(703)			(703)		(703)
Cash dividends declared (\$1.24 per common share) .....			(5,968)		(5,968)		(5,968)
Effect of adoption of accounting standards .....			(36)	45	9		9
Share-based compensation .....		1,576			1,576		1,576
Purchase acquisitions and other .....		21			21		21
BALANCE AT JULY 28, 2018 .....	4,614	\$ 42,820	\$ 1,233	\$ (849)	\$ 43,204	\$ —	\$ 43,204

See Notes to Consolidated Financial Statements.

**CISCO SYSTEMS, INC.**  
**Notes to Consolidated Financial Statements**

## **1. Basis of Presentation**

The fiscal year for Cisco Systems, Inc. (the “Company,” “Cisco,” “we,” “us,” or “our”) is the 52 or 53 weeks ending on the last Saturday in July. Fiscal 2018 and fiscal 2017 were each 52-week fiscal years, while fiscal 2016 was a 53-week fiscal year. The Consolidated Financial Statements include the accounts of ours and those of our subsidiaries. All intercompany accounts and transactions have been eliminated. We conduct business globally and are primarily managed on a geographic basis in the following three geographic segments: the Americas; Europe, Middle East, and Africa (EMEA); and Asia Pacific, Japan, and China (APJC).

We consolidate our investments in a venture fund managed by SOFTBANK Corp. and its affiliates (“SOFTBANK”) as this is a variable interest entity and we are the primary beneficiary. The noncontrolling interests attributed to SOFTBANK are presented as a separate component from our equity in the equity section of the Consolidated Balance Sheets. SOFTBANK's share of the earnings in the venture fund are not presented separately in the Consolidated Statements of Operations as these amounts are not material for any of the fiscal periods presented.

Certain reclassifications have been made to the amounts for prior years in order to conform to the current year’s presentation. We have evaluated subsequent events through the date that the financial statements were issued.

## **2. Summary of Significant Accounting Policies**

**(a) Cash and Cash Equivalents** We consider all highly liquid investments purchased with an original or remaining maturity of three months or less at the date of purchase to be cash equivalents. Cash and cash equivalents are maintained with various financial institutions.

**(b) Available-for-Sale Investments** We classify our investments in both fixed income securities and publicly traded equity securities as available-for-sale investments. Fixed income securities primarily consist of U.S. government securities, U.S. government agency securities, non-U.S. government and agency securities, corporate debt securities, and U.S. agency mortgage-backed securities. These available-for-sale investments are primarily held in the custody of a major financial institution. A specific identification method is used to determine the cost basis of fixed income and public equity securities sold. These investments are recorded in the Consolidated Balance Sheets at fair value. Unrealized gains and losses on these investments, to the extent the investments are unhedged, are included as a separate component of accumulated other comprehensive income (AOCI), net of tax. We classify our investments as current based on the nature of the investments and their availability for use in current operations.

**(c) Other-than-Temporary Impairments on Investments** When the fair value of a debt security is less than its amortized cost, it is deemed impaired, and we will assess whether the impairment is other than temporary. An impairment is considered other than temporary if (i) we have the intent to sell the security, (ii) it is more likely than not that we will be required to sell the security before recovery of the entire amortized cost basis, or (iii) we do not expect to recover the entire amortized cost basis of the security. If impairment is considered other than temporary based on condition (i) or (ii) described earlier, the entire difference between the amortized cost and the fair value of the debt security is recognized in earnings. If an impairment is considered other than temporary based on condition (iii), the amount representing credit losses (defined as the difference between the present value of the cash flows expected to be collected and the amortized cost basis of the debt security) will be recognized in earnings, and the amount relating to all other factors will be recognized in other comprehensive income (OCI).

We recognize an impairment charge on publicly traded equity securities when a decline in the fair value of a security below the respective cost basis is judged to be other than temporary. We consider various factors in determining whether a decline in the fair value of these investments is other than temporary, including the length of time and extent to which the fair value of the security has been less than our cost basis, the financial condition and near-term prospects of the issuer, and our intent and ability to hold the investment for a period of time sufficient to allow for any anticipated recovery in market value.

Investments in privately held companies are included in other assets in the Consolidated Balance Sheets and are accounted for using either the cost or equity method. We monitor these investments for impairments and make reductions in carrying values if we determine that an impairment charge is required based primarily on the financial condition and near-term prospects of these companies.

**(d) Inventories** Inventories are stated at the lower of cost or market. Cost is computed using standard cost, which approximates actual cost, on a first-in, first-out basis. We provide inventory write-downs based on excess and obsolete inventories determined primarily by future demand forecasts. The write-down is measured as the difference between the cost of the inventory and market based upon assumptions about future demand and charged to the provision for inventory, which is a component of cost of sales. At the point of the loss recognition, a new, lower cost basis for that inventory is established, and subsequent changes in facts and circumstances do not result in the restoration or increase in that newly established cost basis. In addition, we record a liability for firm, noncancelable, and unconditional purchase commitments with contract manufacturers and suppliers for quantities in excess of our future demand forecasts consistent with our valuation of excess and obsolete inventory.

**(e) Allowance for Doubtful Accounts** The allowance for doubtful accounts is based on our assessment of the collectibility of customer accounts. We regularly review the allowance by considering factors such as historical experience, credit quality, age of the accounts receivable balances, economic conditions that may affect a customer's ability to pay, and expected default frequency rates. Trade receivables are written off at the point when they are considered uncollectible.

**(f) Financing Receivables and Guarantees** We provide financing arrangements, including leases, financed service contracts, and loans, for certain qualified end-user customers to build, maintain, and upgrade their networks. Lease receivables primarily represent sales-type and direct-financing leases. Leases have on average a four-year term and are usually collateralized by a security interest in the underlying assets. Loan receivables include customers financing purchases of our hardware, software and services and also may include additional funds for other costs associated with network installation and integration of our products and services. Loan receivables generally have terms of up to three years. Financed service contracts typically have terms of one to three years and primarily relate to technical support services.

We determine the adequacy of our allowance for credit loss by assessing the risks and losses inherent in our financing receivables by portfolio segment. The portfolio segment is based on the types of financing offered by us to our customers: lease receivables, loan receivables, and financed service contracts.

We assess the allowance for credit loss related to financing receivables on either an individual or a collective basis. We consider various factors in evaluating lease and loan receivables and the earned portion of financed service contracts for possible impairment on an individual basis. These factors include our historical experience, credit quality and age of the receivable balances, and economic conditions that may affect a customer's ability to pay. When the evaluation indicates that it is probable that all amounts due pursuant to the contractual terms of the financing agreement, including scheduled interest payments, are unable to be collected, the financing receivable is considered impaired. All such outstanding amounts, including any accrued interest, are assessed and reserved at the customer level. Our internal credit risk ratings are categorized as 1 through 10, with the lowest credit risk rating representing the highest quality financing receivables. Typically, we also consider financing receivables with a risk rating of 8 or higher to be impaired and will include them in the individual assessment for allowance. We evaluate the remainder of our financing receivables portfolio for impairment on a collective basis and record an allowance for credit loss at the portfolio segment level. When evaluating the financing receivables on a collective basis, we use historical default rates and expected default frequency rates published by major third-party credit-rating agencies as well as our own historical loss rate in the event of default, while also systematically giving effect to economic conditions, concentration of risk, and correlation.

Expected default frequency rates and historical default rates are published quarterly by major third-party credit-rating agencies, and the internal credit risk rating is derived by taking into consideration various customer-specific factors and macroeconomic conditions. These factors, which include the strength of the customer's business and financial performance, the quality of the customer's banking relationships, our specific historical experience with the customer, the performance and outlook of the customer's industry, the customer's legal and regulatory environment, the potential sovereign risk of the geographic locations in which the customer is operating, and independent third-party evaluations, are updated regularly or when facts and circumstances indicate that an update is deemed necessary.

Financing receivables are written off at the point when they are considered uncollectible, and all outstanding balances, including any previously earned but uncollected interest income, will be reversed and charged against the allowance for credit loss. We do not typically have any partially written-off financing receivables.

Outstanding financing receivables that are aged 31 days or more from the contractual payment date are considered past due. We do not accrue interest on financing receivables that are considered impaired or more than 90 days past due unless either the receivable has not been collected due to administrative reasons or the receivable is well secured and in the process of collection. Financing receivables may be placed on nonaccrual status earlier if, in management's opinion, a timely collection of the full principal and interest becomes uncertain. After a financing receivable has been categorized as nonaccrual, interest will be recognized when cash is received. A financing receivable may be returned to accrual status after all of the customer's delinquent balances of principal and interest have been settled, and the customer remains current for an appropriate period.

We facilitate arrangements for third-party financing extended to channel partners, consisting of revolving short-term financing, generally with payment terms ranging from 60 to 90 days. In certain instances, these financing arrangements result in a transfer of our receivables to the third party. The receivables are derecognized upon transfer, as these transfers qualify as true sales, and we receive a payment for the receivables from the third party based on our standard payment terms. These financing arrangements facilitate the working capital requirements of the channel partners, and, in some cases, we guarantee a portion of these arrangements. We also provide financing guarantees for third-party financing arrangements extended to end-user customers related to leases and loans, which typically have terms of up to three years. We could be called upon to make payments under these guarantees in the event of nonpayment by the channel partners or end-user customers. Deferred revenue relating to these financing arrangements is recorded in accordance with revenue recognition policies or for the fair value of the financing guarantees.

**(g) Depreciation and Amortization** Property and equipment are stated at cost, less accumulated depreciation or amortization, whenever applicable. Depreciation and amortization expenses for property and equipment were approximately \$1.1 billion, \$1.1 billion, and \$1.0 billion for fiscal 2018, 2017, and 2016, respectively. Depreciation and amortization are computed using the straight-line method, generally over the following periods:

Asset Category	Period
Buildings.....	25 years
Building improvements .....	10 years
Leasehold improvements .....	Shorter of remaining lease term or up to 10 years
Computer equipment and related software.....	30 to 36 months
Production, engineering, and other equipment .....	Up to 5 years
Operating lease assets.....	Based on lease term
Furniture and fixtures .....	5 years

**(h) Business Combinations** We allocate the fair value of the purchase consideration of our acquisitions to the tangible assets, liabilities, and intangible assets acquired, including in-process research and development (IPR&D), based on their estimated fair values. The excess of the fair value of purchase consideration over the fair values of these identifiable assets and liabilities is recorded as goodwill. IPR&D is initially capitalized at fair value as an intangible asset with an indefinite life and assessed for impairment thereafter. When an IPR&D project is completed, the IPR&D is reclassified as an amortizable purchased intangible asset and amortized over the asset's estimated useful life. Acquisition-related expenses and related restructuring costs are recognized separately from the business combination and are expensed as incurred.

**(i) Goodwill and Purchased Intangible Assets** Goodwill is tested for impairment on an annual basis in the fourth fiscal quarter and, when specific circumstances dictate, between annual tests. When impaired, the carrying value of goodwill is written down to fair value. The goodwill impairment test involves a two-step process. The first step, identifying a potential impairment, compares the fair value of a reporting unit with its carrying amount, including goodwill. If the carrying value of the reporting unit exceeds its fair value, the second step would need to be conducted; otherwise, no further steps are necessary as no potential impairment exists. If necessary, the second step to measure the impairment loss would be to compare the implied fair value of the reporting unit goodwill with the carrying amount of that goodwill. Any excess of the reporting unit goodwill carrying value over the respective implied fair value is recognized as an impairment loss. Purchased intangible assets with finite lives are carried at cost, less accumulated amortization. Amortization is computed over the estimated useful lives of the respective assets. See "Long-Lived Assets" for our policy regarding impairment testing of purchased intangible assets with finite lives. Purchased intangible assets with indefinite lives are assessed for potential impairment annually or when events or circumstances indicate that their carrying amounts might be impaired.

**(j) Long-Lived Assets** Long-lived assets that are held and used by us are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of such assets may not be recoverable. Determination of recoverability of long-lived assets is based on an estimate of the undiscounted future cash flows resulting from the use of the asset and its eventual disposition. Measurement of an impairment loss for long-lived assets that management expects to hold and use is based on the difference between the fair value of the asset and its carrying value. Long-lived assets to be disposed of are reported at the lower of carrying amount or fair value less costs to sell.

**(k) Fair Value** Fair value is defined as the price that would be received from selling an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. When determining the fair value measurements for assets and liabilities required or permitted to be either recorded or disclosed at fair value, we consider the principal or most advantageous market in which we would transact, and we also consider assumptions that market participants would use when pricing the asset or liability.

The accounting guidance for fair value measurement requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The standard establishes a fair value hierarchy based on the level of independent, objective evidence surrounding the inputs used to measure fair value. A financial instrument's categorization within the fair value hierarchy is based upon the lowest level of input that is significant to the fair value measurement. The fair value hierarchy is as follows:

Level 1 applies to assets or liabilities for which there are quoted prices in active markets for identical assets or liabilities.

Level 2 applies to assets or liabilities for which there are inputs other than quoted prices that are observable for the asset or liability such as quoted prices for similar assets or liabilities in active markets; quoted prices for identical assets or liabilities in markets with insufficient volume or infrequent transactions (less active markets); or model-derived valuations in which significant inputs are observable or can be derived principally from, or corroborated by, observable market data. We use inputs such as actual trade data, benchmark yields, broker/dealer quotes, and other similar data, which are obtained from quoted market prices, independent pricing vendors, or other sources, to determine the ultimate fair value of assets or liabilities.

Level 3 applies to assets or liabilities for which there are unobservable inputs to the valuation methodology that are significant to the measurement of the fair value of the assets or liabilities. The fair values are determined based on model-based techniques such as discounted cash flow models using inputs that we could not corroborate with market data.

**(l) Derivative Instruments** We recognize derivative instruments as either assets or liabilities and measure those instruments at fair value. The accounting for changes in the fair value of a derivative depends on the intended use of the derivative and the resulting designation. For a derivative instrument designated as a fair value hedge, the gain or loss is recognized in earnings in the period of change together with the offsetting loss or gain on the hedged item attributed to the risk being hedged. For a derivative instrument designated as a cash flow hedge, the effective portion of the derivative's gain or loss is initially reported as a component of AOCI and subsequently reclassified into earnings when the hedged exposure affects earnings. The ineffective portion of the gain or loss is reported in earnings immediately. For a derivative instrument designated as a net investment hedge of our foreign operations, the gain or loss is recorded in the cumulative translation adjustment within AOCI together with the offsetting loss or gain of the hedged exposure of the underlying foreign operations. Any ineffective portion of the net investment hedges is reported in earnings during the period of change. For derivative instruments that are not designated as accounting hedges, changes in fair value are recognized in earnings in the period of change. We record derivative instruments in the statements of cash flows to operating, investing, or financing activities consistent with the cash flows of the hedged item.

Hedge effectiveness for foreign exchange forward contracts used as cash flow hedges is assessed by comparing the change in the fair value of the hedge contract with the change in the fair value of the forecasted cash flows of the hedged item. Hedge effectiveness for equity forward contracts and foreign exchange net investment hedge forward contracts is assessed by comparing changes in fair value due to changes in spot rates for both the derivative and the hedged item. For foreign exchange option contracts, hedge effectiveness is assessed based on the hedging instrument's entire change in fair value. Hedge effectiveness for interest rate swaps is assessed by comparing the change in fair value of the swap with the change in the fair value of the hedged item due to changes in the benchmark interest rate.

**(m) Foreign Currency Translation** Assets and liabilities of non-U.S. subsidiaries that operate in a local currency environment, where that local currency is the functional currency, are translated to U.S. dollars at exchange rates in effect at the balance sheet date, with the resulting translation adjustments directly recorded to a separate component of AOCI. Income and expense accounts are translated at average exchange rates during the year. Remeasurement adjustments are recorded in other income (loss), net. The effect of foreign currency exchange rates on cash and cash equivalents was not material for any of the fiscal years presented.

**(n) Concentrations of Risk** Cash and cash equivalents are maintained with several financial institutions. Deposits held with banks may exceed the amount of insurance provided on such deposits. Generally, these deposits may be redeemed upon demand and are maintained with financial institutions with reputable credit and therefore bear minimal credit risk. We seek to mitigate our credit risks by spreading such risks across multiple counterparties and monitoring the risk profiles of these counterparties.

We perform ongoing credit evaluations of our customers and, with the exception of certain financing transactions, do not require collateral from our customers. We receive certain of our components from sole suppliers. Additionally, we rely on a limited number of contract manufacturers and suppliers to provide manufacturing services for our products. The inability of a contract manufacturer or supplier to fulfill our supply requirements could materially impact future operating results.

**(o) Revenue Recognition** We recognize revenue when persuasive evidence of an arrangement exists, delivery has occurred, the fee is fixed or determinable, and collectibility is reasonably assured. In instances where final acceptance of the product, system, or solution is specified by the customer, revenue is deferred until all acceptance criteria have been met. For hosting arrangements, we recognize revenue ratably over the hosting period, while usage revenue is recognized based on utilization. Software subscription revenue is deferred and recognized ratably over the subscription term upon delivery of the first product

and commencement of the term. Technical support and consulting services revenue is deferred and recognized ratably over the period during which the services are to be performed, which is typically from one to three years. Transactional advanced services revenue is recognized upon delivery or completion of performance milestones.

We use distributors that typically stock inventory and sell to systems integrators, service providers, and other resellers. We refer to this as our two-tier sales to the end customer. Revenue from distributors is recognized based on a sell-through method using point-of-sale information provided by the distributors. Distributors and other partners participate in various rebate, cooperative marketing, and other incentive programs, and we maintain estimated accruals and allowances for these programs. The ending liability for these programs was included in other current liabilities, and the balance was \$1.0 billion as of each of July 28, 2018 and July 29, 2017. We accrue for warranty costs, sales returns, and other allowances based on our historical experience. Shipping and handling fees billed to customers are included in revenue, with the associated costs included in cost of sales.

Many of our products have both software and non-software components that function together to deliver the products' essential functionality. We also provide technical support and advanced services. We have a broad customer base that encompasses virtually all types of public and private entities, including enterprise businesses, service providers, and commercial customers. Cisco and our salesforce are not organized by product divisions, and our products and services can be sold standalone or together in various combinations across our geographic segments or customer markets. For example, service provider arrangements are typically larger in scale with longer deployment schedules and involve the delivery of a variety of product technologies, including high-end routing, video and network management software, and other product technologies along with technical support and advanced services. Our enterprise and commercial arrangements are unique for each customer and smaller in scale and may include network infrastructure products such as routers and switches or collaboration technologies such as Unified Communications and Cisco TelePresence systems products along with technical support services.

We enter into revenue arrangements that may consist of multiple deliverables of our product and service offerings due to the needs of our customers. For example, a customer may purchase routing products along with a contract for technical support services. This arrangement would consist of multiple elements, with the products delivered in one reporting period and the technical support services delivered across multiple reporting periods. Another customer may purchase networking products along with advanced service offerings, in which all the elements are delivered within the same reporting period. In addition, distributors purchase products or technical support services on a standalone basis for resale to an end user or for purposes of stocking certain products, and these transactions would not result in a multiple-element arrangement. We consider several factors when reviewing multiple purchases made by the same customer within a short time frame in order to identify multiple-element arrangements, including whether the deliverables are closely interrelated, whether the deliverables are essential to each other's functionality, whether payment terms are linked, whether the customer is entitled to a refund or concession if another purchase is not completed satisfactorily, and/or whether the purchases were negotiated together as one overall arrangement.

In many instances, products are sold separately in standalone arrangements as customers may support the products themselves or purchase support on a time-and-materials basis. Advanced services are sometimes sold in standalone engagements such as general consulting, network management, or security advisory projects, and technical support services are sold separately through renewals of annual contracts. We determine our vendor-specific objective evidence (VSOE) based on our normal pricing and discounting practices for products or services when sold separately. VSOE determination requires that a substantial majority of the historical standalone transactions has the selling prices for a product or service that fall within a reasonably narrow pricing range, generally evidenced by approximately 80% of such historical standalone transactions falling within plus or minus 15% of the median rates. In addition, we consider the geographies in which the products or services are sold, major product and service groups and customer classifications, and other environmental or marketing variables in determining VSOE.

When we are not able to establish VSOE for all deliverables in an arrangement with multiple elements, which may be due to us infrequently selling each element separately, not pricing products within a narrow range, or only having a limited sales history, such as in the case of certain newly introduced product categories, we attempt to determine the selling price of each element based on third-party evidence of selling price (TPE). TPE is determined based on competitor prices for similar deliverables when sold separately. Generally, our go-to-market strategy differs from that of our peers, and our offerings contain a significant level of differentiation such that the comparable pricing of products with similar functionality cannot be obtained. Furthermore, we are unable to reliably determine what similar competitor products' selling prices are on a standalone basis. Therefore, we are typically not able to determine TPE.

When we are unable to establish fair value using VSOE or TPE, we use estimated selling prices (ESP) in our allocation of arrangement consideration. The objective of ESP is to determine the price at which we would transact a sale if the product or service were regularly sold on a standalone basis. ESP is generally used for new or highly proprietary offerings and solutions or for offerings not priced within a reasonably narrow range. We determine ESP for a product or service by considering multiple factors, including, but not limited to, geographies, market conditions, competitive landscape, internal costs, gross margin objectives, and pricing practices. The determination of ESP is made through consultation with and formal approval by our management, taking into consideration the go-to-market strategy.

We regularly review VSOE, TPE, and ESP and maintains internal controls over the establishment and updates of these estimates. There were no material impacts during fiscal 2018 from changes in VSOE, TPE, or ESP.

Our arrangements with multiple deliverables may include one or more software deliverables that are subject to the software revenue recognition guidance. In these cases, revenue for the software is generally recognized upon shipment or electronic delivery and granting of the license. The revenue for these multiple-element arrangements is allocated to the software deliverables and the non-software deliverables based on the relative selling prices of all of the deliverables in the arrangement using the hierarchy in the applicable accounting guidance. In the circumstances where we cannot determine VSOE or TPE of the selling price for all of the deliverables in the arrangement, including the software deliverables, ESP is used for the purposes of performing this allocation. VSOE is required to allocate the revenue between multiple software deliverables. If VSOE is available for the undelivered software elements, we apply the residual method; where VSOE is not available, software revenue is either recognized when all software elements have been delivered or recognized ratably when post-contract support is the only undelivered software element remaining.

(p) Advertising Costs We expense all advertising costs as incurred. Advertising costs included within sales and marketing expenses were approximately \$166 million, \$209 million, and \$186 million for fiscal 2018, 2017, and 2016, respectively.

(q) Share-Based Compensation Expense We measure and recognize the compensation expense for all share-based awards made to employees and directors, including employee stock options, restricted stock units (RSUs), performance-based restricted stock units (PRSUs), and employee stock purchases related to the Employee Stock Purchase Plan (Employee Stock Purchase Rights) based on estimated fair values. The fair value of employee stock options is estimated on the date of grant using a lattice-binomial option-pricing model (Lattice-Binomial Model) or the Black-Scholes model, and for employee stock purchase rights we estimate the fair value using the Black-Scholes model. The fair value for time-based stock awards and stock awards that are contingent upon the achievement of financial performance metrics is based on the grant date share price reduced by the present value of the expected dividend yield prior to vesting. The fair value of market-based stock awards is estimated using an option-pricing model on the date of grant. Share-based compensation expense is reduced for forfeitures.

(r) Software Development Costs Software development costs, including costs to develop software sold, leased, or otherwise marketed, that are incurred subsequent to the establishment of technological feasibility are capitalized if significant. Costs incurred during the application development stage for internal-use software are capitalized if significant. Capitalized software development costs are amortized using the straight-line amortization method over the estimated useful life of the applicable software. Such software development costs required to be capitalized have not been material to date.

(s) Income Taxes Income tax expense is based on pretax financial accounting income. Deferred tax assets and liabilities are recognized for the expected tax consequences of temporary differences between the tax bases of assets and liabilities and their reported amounts. Valuation allowances are recorded to reduce deferred tax assets to the amount that will more likely than not be realized.

We account for uncertainty in income taxes using a two-step approach to recognizing and measuring uncertain tax positions. The first step is to evaluate the tax position for recognition by determining if the weight of available evidence indicates that it is more likely than not that the position will be sustained on audit, including resolution of related appeals or litigation processes, if any. The second step is to measure the tax benefit as the largest amount that is more than 50% likely of being realized upon settlement. We classify the liability for unrecognized tax benefits as current to the extent that we anticipate payment (or receipt) of cash within one year. Interest and penalties related to uncertain tax positions are recognized in the provision for income taxes.

(t) Computation of Net Income per Share Basic net income per share is computed using the weighted-average number of common shares outstanding during the period. Diluted net income per share is computed using the weighted-average number of common shares and dilutive potential common shares outstanding during the period. Diluted shares outstanding includes the dilutive effect of in-the-money options, unvested restricted stock, and restricted stock units. The dilutive effect of such equity awards is calculated based on the average share price for each fiscal period using the treasury stock method. Under the treasury stock method, the amount the employee must pay for exercising stock options and the amount of compensation cost for future service that we have not yet recognized are collectively assumed to be used to repurchase shares.

(u) Consolidation of Variable Interest Entities We use a qualitative approach in assessing the consolidation requirement for variable interest entities. The approach focuses on identifying which enterprise has the power to direct the activities that most significantly impact the variable interest entity's economic performance and which enterprise has the obligation to absorb losses or the right to receive benefits from the variable interest entity. In the event that we are the primary beneficiary of a variable interest entity, the assets, liabilities, and results of operations of the variable interest entity will be included in our Consolidated Financial Statements.

**(v) Use of Estimates** The preparation of financial statements and related disclosures in conformity with accounting principles generally accepted in the United States requires management to make estimates and judgments that affect the amounts reported in the Consolidated Financial Statements and accompanying notes. Estimates are used for the following, among others:

- Revenue recognition
- Allowances for accounts receivable, sales returns, and financing receivables
- Inventory valuation and liability for purchase commitments with contract manufacturers and suppliers
- Loss contingencies and product warranties
- Fair value measurements and other-than-temporary impairments
- Goodwill and purchased intangible asset impairments
- Income taxes

The actual results experienced by us may differ materially from management's estimates.

**(w) New Accounting Updates Recently Adopted**

*Share-Based Compensation* In March 2016, the FASB issued an accounting standard update that impacts the accounting for share-based payment transactions, including income tax consequences, classification of awards as either equity or liabilities, and classification on the Consolidated Statements of Cash Flows. We adopted this accounting standard update beginning the first quarter of fiscal 2018 on a prospective basis. This resulted in an overall decrease in the effective tax rate for fiscal 2018 due to recognition of excess tax benefits from share-based compensation. The application of this accounting standard update did not have a material impact on our Consolidated Financial Statements.

*Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income* In February 2018, the FASB issued an accounting standard update that allows companies to reclassify from AOCI to retained earnings stranded tax effects resulting from the enactment of the Tax Cuts and Jobs Act (the "Tax Act"). The guidance is effective January 1, 2019 with early adoption permitted. We early adopted this accounting standard update in the third quarter of fiscal 2018 and elected not to reclassify prior periods. Adoption of this standard resulted in a decrease of \$45 million to retained earnings due to the reclassification from AOCI to retained earnings.

**(x) Recent Accounting Standards or Updates Not Yet Effective as of Fiscal Year End**

*Revenue Recognition* In May 2014, the FASB issued ASC 606, a new accounting standard related to revenue recognition. ASC 606 will supersede nearly all U.S. GAAP on revenue recognition and eliminate industry-specific guidance. The underlying principle of ASC 606 is to recognize revenue when a customer obtains control of promised goods or services at an amount that reflects the consideration that is expected to be received in exchange for those goods or services. It also requires increased disclosures including the nature, amount, timing, and uncertainty of revenues and cash flows related to contracts with customers.

ASC 606 allows two methods of adoption: i) retrospectively to each prior period presented ("full retrospective method"), or ii) retrospectively with the cumulative effect recognized in retained earnings as of the date of adoption ("modified retrospective method"). We will adopt ASC 606 using the modified retrospective method at the beginning of our first quarter of fiscal 2019.

We are in process of finalizing our new accounting policies, systems, processes, and internal controls necessary to support the requirements of ASC 606. We have substantially completed our assessment of the financial statement impact of ASC 606, the impacts of which are as discussed below.

ASC 606 will primarily impact our revenue recognition for software arrangements and sales to two-tier distributors. In both areas, the new standard will accelerate the recognition of revenue. The table below details the timing of when revenue is typically recognized under the current revenue standard compared to the timing of when revenue will typically be recognized under ASC 606 for these major areas:

	Current Revenue Standard	New Revenue Standard
Software arrangements:		
Perpetual software licenses .....	Upfront	Upfront
Term software licenses .....	Ratable	Upfront
Security software licenses .....	Ratable	Ratable
Enterprise license agreements .....	Ratable	Upfront
Software support services .....	Ratable	Ratable
Software-as-a-service .....	Ratable	Ratable
Two-tier distribution .....	Sell-Through	Sell-In

In addition to the above revenue recognition timing impacts, ASC 606 requires incremental contract acquisition costs (such as sales commissions) for customer contracts to be capitalized and amortized over the contract term. Currently, these costs are expensed as incurred.

Upon adopting ASC 606 at the beginning of fiscal 2019, our cumulative effect adjustment will increase retained earnings by approximately \$2.3 billion. This cumulative effect adjustment is primarily driven by a reduction to our deferred product revenue of approximately \$2.8 billion, of which \$1.3 billion relates to our recurring software and subscription offers, \$0.6 billion relates to two-tier distribution, and the remainder relates to non-recurring software, services and other adjustments. In addition to the adjustment to deferred product revenue, other adjustments at transition include adjustments to accounts receivable, inventories, other current and noncurrent assets, and other liabilities. The adjustment to other current and noncurrent assets is primarily for capitalized incremental contract acquisitions costs and the establishment of contract assets. The cumulative effect adjustment is recorded net of tax with the direct tax effect recorded primarily as a reduction of deferred tax assets. We also expect to record in the first quarter of fiscal 2019 a net indirect tax benefit to our provision for income taxes related to intercompany adjustments associated with the new standard. See Critical Accounting Estimates, “Revenue Recognition” for further discussion on the fiscal 2019 revenue impacts of ASC 606.

**Financial Instruments** In January 2016, the FASB issued an accounting standard update that changes the accounting for equity investments, financial liabilities under the fair value option, and the presentation and disclosure requirements for financial instruments. We will adopt this accounting standard update in the first quarter of fiscal 2019. The most significant impact of this accounting standard update for us is that it will require the remeasurement of investments that are not accounted for under the equity method at fair value at the end of each reporting period with the changes recorded to the income statement. We estimate an increase to retained earnings of approximately \$0.3 billion upon adoption of the accounting standard at the beginning of fiscal 2019. The adjustment is primarily driven by a reclassification of net unrealized gains (losses), net of tax on available-for-sale equity investments from accumulated other comprehensive income, and an increase related to our privately held investments. We expect that this accounting standard update will increase the variability of other income (loss), net in future periods.

**Income Taxes on Intra-Entity Transfers of Assets** In October 2016, the FASB issued an accounting standard update that requires recognition of the income tax consequences of intra-entity transfers of assets (other than inventory) at the transaction date. We will adopt this accounting standard update in the first quarter of fiscal 2019 on a modified retrospective basis. We estimate an increase to retained earnings of approximately \$1.3 billion upon adoption of the accounting standard at the beginning of fiscal 2019. The increase to retained earnings reflects estimated changes to deferred tax assets and other assets related to the recognition of income tax effects of intra-entity asset transfers (other than inventory) that occurred prior to the adoption date. The ongoing impact of this standard will be facts and circumstances dependent on any transactions within its scope.

**Classification of Cash Flow Elements** In August 2016, the FASB issued an accounting standard update related to the classification of certain cash receipts and cash payments on the statement of cash flows. We will adopt this accounting standard update in the first quarter of fiscal 2019 on a retrospective basis. We do not expect that this accounting standard update will have a material impact on our Consolidated Statements of Cash Flows.

**Restricted Cash in Statement of Cash Flow** In November 2016, the FASB issued an accounting standard update that provides guidance on the classification and presentation of changes in restricted cash and cash equivalents in the statement of cash flows. We will adopt this accounting standard update in the first quarter of fiscal 2019 using a retrospective transition method for each period presented. We do not expect this accounting update will have a material impact, though it will change the presentation of the Consolidated Statements of Cash Flows.

**Definition of a Business** In January 2017, the FASB issued an accounting standard update that clarifies the definition of a business to help companies evaluate whether acquisition or disposal transactions should be accounted for as asset groups or as businesses. We will adopt this accounting standard update beginning in the first quarter of fiscal 2019 on a prospective basis. The impact of this accounting standard update will be fact dependent, but we expect that some transactions that were previously accounted for as business combinations or disposal transactions will be accounted for as asset purchases or asset sales under the accounting standard update.

**Simplifying the Test for Goodwill Impairment** In January 2017, the FASB issued an accounting standard update that removes Step 2 of the goodwill impairment test, which requires the assessment of fair value of individual assets and liabilities of a reporting unit to measure goodwill impairments. Goodwill impairment will now be the amount by which a reporting unit's carrying value exceeds its fair value. We will early adopt this standard in the first quarter of fiscal 2019 on a prospective basis. We do not expect this accounting standard update will have a material impact on our Consolidated Financial Statements.

**Leases** In February 2016, the FASB issued an accounting standard update, as well as subsequent amendments, related to leases requiring lessees to recognize operating and financing lease liabilities on the balance sheet, as well as corresponding right-of-use assets. The new lease standard also makes some changes to lessor accounting and aligns key aspects of the lessor accounting model with the revenue recognition standard. In addition, disclosures will be required to enable users of financial statements to assess the amount, timing, and uncertainty of cash flows arising from leases. The accounting standard update will be effective for us beginning in the first quarter of fiscal 2020 on a modified retrospective basis, and early adoption is permitted. We are currently evaluating the impact of this accounting standard update on our Consolidated Financial Statements.

**Credit Losses of Financial Instruments** In June 2016, the FASB issued an accounting standard update that requires measurement and recognition of expected credit losses for financial assets held based on historical experience, current conditions, and reasonable and supportable forecasts that affect the collectibility of the reported amount. The accounting standard update will be effective for us beginning in the first quarter of fiscal 2021 on a modified retrospective basis, and early adoption in fiscal 2020 is permitted. We are currently evaluating the impact of this accounting standard update on our Consolidated Financial Statements.

### 3. Acquisitions and Divestitures

#### (a) Acquisition Summary

We completed eight acquisitions during fiscal 2018. A summary of the allocation of the total purchase consideration is presented as follows (in millions):

<b>Fiscal 2018</b>	<b>Net Tangible Assets</b>			
	<b>Purchase Consideration</b>	<b>Acquired Liabilities Assumed</b>	<b>Purchased Intangible Assets</b>	<b>Goodwill</b>
Viptela . . . . .	\$ 497	\$ (18)	\$ 180	\$ 335
Springpath . . . . .	248	(11)	160	99
BroadSoft . . . . .	2,179	353	430	1,396
Accompany . . . . .	222	6	55	161
<b>Others (four in total) . . . . .</b>	<b>72</b>	<b>4</b>	<b>42</b>	<b>26</b>
<b>Total . . . . .</b>	<b>\$ 3,218</b>	<b>\$ 334</b>	<b>\$ 867</b>	<b>\$ 2,017</b>

On July 31, 2017, we completed our acquisition of privately held Viptela Inc. (“Viptela”), a provider of software-defined wide area networking products. Revenue from the Viptela acquisition has been included in our Infrastructure Platforms product category.

On September 22, 2017, we completed our acquisition of privately held Springpath, Inc. (“Springpath”), a hyperconvergence software company. Revenue from the Springpath acquisition has been included in our Infrastructure Platforms product category.

On February 1, 2018, we completed our acquisition of publicly held BroadSoft, Inc. (“BroadSoft”), a cloud calling and contact center solutions company. Revenue from the BroadSoft acquisition has been included in our Applications product category.

On May 10, 2018, we completed our acquisition of privately held Accompany, a provider of an AI-driven relationship intelligence platform. Results from the Accompany acquisition will be included in our Applications product category.

The total purchase consideration related to our acquisitions completed during fiscal 2018 consisted of cash consideration and vested share-based awards assumed. The total cash and cash equivalents acquired from these acquisitions was approximately \$187 million.

#### Fiscal 2017 Acquisitions

Allocation of the purchase consideration for acquisitions completed in fiscal 2017 is summarized as follows (in millions):

	Purchase Consideration	Net Tangible Assets			Purchased Intangible Assets	Goodwill
		Acquired (Liabilities Assumed)	Purchased Intangible Assets	Goodwill		
Fiscal 2017						
CloudLock . . . . .	\$ 249	\$ —	\$ 36	\$ 213		
AppDynamics . . . . .	3,258	(175)	785	2,648		
MindMeld . . . . .	104	(11)	51	64		
Others (four in total) . . . . .	26	—	6	20		
Total . . . . .	<u>\$ 3,637</u>	<u>\$ (186)</u>	<u>\$ 878</u>	<u>\$ 2,945</u>		

On August 1, 2016, we acquired privately held CloudLock Inc. (“CloudLock”), a provider of cloud security that specializes in cloud access security broker technology that provides enterprises with visibility and analytics around user behavior and sensitive data in cloud services. Revenue from the CloudLock acquisition has been included in our Security product category.

On March 17, 2017, we acquired privately held AppDynamics, Inc. (“AppDynamics”), an application intelligence software company. AppDynamics’s cloud application and business monitoring platform is designed to enable companies to improve application and business performance. With the AppDynamics acquisition, we seek to provide end-to-end visibility and intelligence from the customer’s network through to the application. Product revenue from the AppDynamics acquisition has been included in our Other product category.

On May 26, 2017, we acquired privately held MindMeld, Inc. (“MindMeld”), an artificial intelligence (AI) company. MindMeld’s unique AI platform enables customers to build intelligent and human-like conversational interfaces for any application or device. Revenue from the MindMeld acquisition has been included in our Collaboration product category.

The total purchase consideration related to our acquisitions completed during fiscal 2017 consisted of cash consideration and vested share-based awards assumed. The total cash and cash equivalents acquired from these acquisitions was approximately \$138 million.

#### Fiscal 2016 Acquisitions

In fiscal 2016, we completed 12 acquisitions for total purchase consideration of \$3.4 billion.

##### **(b) Pending Divestiture of Service Provider Video Software Solutions Business**

In the fourth quarter of fiscal 2018, we announced a definitive agreement to sell our Service Provider Video Software Solutions (“SPVSS”) business. As of July 28, 2018, this business had tangible assets of approximately \$175 million (primarily comprised of accounts receivables, inventories and various other current and long-term assets) and net intangible assets and goodwill (based on relative fair value) of \$300 million. In addition, the business had total liabilities of approximately \$320 million (primarily comprised of deferred revenue and various other current and long-term liabilities). These assets and liabilities were held for sale and were not presented separately as the amounts were not material to the Consolidated Balance Sheet. We expect to have an immaterial financial statement impact from this transaction upon closing. The transaction is expected to close in the first half of fiscal 2019, subject to customary closing conditions and regulatory approvals.

##### **(c) Pending Acquisition of Duo Security**

On August 2, 2018, we announced our intent to acquire Duo Security, Inc., the leading provider of unified access security and multi-factor authentication delivered through the cloud. Integrating our network, device and cloud security platforms with Duo Security’s zero-trust authentication and access products is designed to enable customers to easily and securely connect users to any application on any networked device.

Under the terms of the agreement, we have agreed to pay approximately \$2.35 billion in cash and assumed equity awards to acquire Duo Security. The acquisition is expected to close during the first quarter of fiscal 2019 subject to customary closing conditions and regulatory approvals. Upon close of the acquisition, revenue from Duo Security will be included in our Security product category.

**(d) Other Acquisition and Divestiture Information**

Total transaction costs related to our acquisition and divestiture activities during fiscal 2018, 2017, and 2016 were \$41 million, \$10 million, and \$32 million, respectively. These transaction costs were expensed as incurred in G&A expenses in the Consolidated Statements of Operations.

Our purchase price allocation for acquisitions completed during recent periods is preliminary and subject to revision as additional information about fair value of assets and liabilities becomes available. Additional information that existed as of the acquisition date but at that time was unknown to us, may become known to us during the remainder of the measurement period, a period not to exceed 12 months from the acquisition date. Adjustments in the purchase price allocation may require a recasting of the amounts allocated to goodwill retroactive to the period in which the acquisition occurred.

The goodwill generated from our acquisitions completed during fiscal 2018 is primarily related to expected synergies. The goodwill is generally not deductible for income tax purposes.

The Consolidated Financial Statements include the operating results of each acquisition from the date of acquisition. Pro forma results of operations for the acquisitions completed during fiscal 2018, 2017, and 2016 have not been presented because the effects of the acquisitions, individually and in the aggregate, were not material to our financial results.

We completed two divestitures during fiscal 2018. The financial statement impact of these divestitures was not material for fiscal 2018.

**4. Goodwill and Purchased Intangible Assets**

**(a) Goodwill**

The following tables present the goodwill allocated to our reportable segments as of July 28, 2018 and July 29, 2017, as well as the changes to goodwill during fiscal 2018 and 2017 (in millions):

	Balance at July 29, 2017	Acquisitions	Other	Balance at July 28, 2018
<b>Americas</b> .....	\$ 18,691	\$ 1,355	\$ (48)	\$ 19,998
<b>EMEA</b> .....	7,057	491	(19)	7,529
<b>APJC</b> .....	4,018	171	(10)	4,179
<b>Total</b> .....	<b>\$ 29,766</b>	<b>\$ 2,017</b>	<b>\$ (77)</b>	<b>\$ 31,706</b>

	Balance at July 30, 2016	Acquisitions	Other	Balance at July 29, 2017
<b>Americas</b> .....	\$ 16,529	\$ 2,042	\$ 120	\$ 18,691
<b>EMEA</b> .....	6,269	740	48	7,057
<b>APJC</b> .....	3,827	163	28	4,018
<b>Total</b> .....	<b>\$ 26,625</b>	<b>\$ 2,945</b>	<b>\$ 196</b>	<b>\$ 29,766</b>

“Other” in the tables above primarily consists of divestitures, foreign currency translation, as well as immaterial purchase accounting adjustments.

**(b) Purchased Intangible Assets**

The following tables present details of our intangible assets acquired through acquisitions completed during fiscal 2018 and 2017 (in millions, except years):

	FINITE LIVES						INDEFINITE LIVES	
	TECHNOLOGY		CUSTOMER RELATIONSHIPS		OTHER		IPR&D	TOTAL
	Weighted-Average Useful Life (in Years)	Amount	Weighted-Average Useful Life (in Years)	Amount	Weighted-Average Useful Life (in Years)	Amount	Amount	Amount
Fiscal 2018								
Viptela.....	5.0	\$ 144	6.0	\$ 35	1.0	\$ 1	\$ —	\$ 180
Springpath.....	4.0	157	—	—	—	—	3	160
BroadSoft.....	4.0	255	6.0	169	2.0	6	—	430
Accompany.....	4.0	55	—	—	—	—	—	55
Others (four in total)....	3.9	39	4.0	3	—	—	—	42
Total.....		<u>\$ 650</u>		<u>\$ 207</u>		<u>\$ 7</u>	<u>\$ 3</u>	<u>\$ 867</u>

	FINITE LIVES						INDEFINITE LIVES	
	TECHNOLOGY		CUSTOMER RELATIONSHIPS		OTHER		IPR&D	TOTAL
	Weighted-Average Useful Life (in Years)	Amount	Weighted-Average Useful Life (in Years)	Amount	Weighted-Average Useful Life (in Years)	Amount	Amount	Amount
Fiscal 2017								
CloudLock.....	6.0	\$ 32	4.0	\$ 3	1.5	\$ 1	\$ —	\$ 36
AppDynamics.....	4.0	525	7.0	235	2.3	25	—	785
MindMeld.....	4.0	51	1.0	—	—	—	—	51
Others (four in total)....	3.0	6	—	—	—	—	—	6
Total.....		<u>\$ 614</u>		<u>\$ 238</u>		<u>\$ 26</u>	<u>\$ —</u>	<u>\$ 878</u>

The following tables present details of our purchased intangible assets (in millions):

July 28, 2018		Gross	Accumulated Amortization		Net			
<b>Purchased intangible assets with finite lives:</b>								
Technology .....								
Technology .....		\$ 3,711	\$ (1,888)	\$ 1,823				
Customer relationships .....		1,538	(937)	601				
Other .....		63	(38)	25				
<b>Total purchased intangible assets with finite lives</b> .....		<b>5,312</b>	<b>(2,863)</b>	<b>2,449</b>				
<b>In-process research and development, with indefinite lives</b> .....								
In-process research and development, with indefinite lives .....		103	—	103				
<b>Total</b> .....		<b>\$ 5,415</b>	<b>\$ (2,863)</b>	<b>\$ 2,552</b>				

July 29, 2017		Gross	Accumulated Amortization		Net			
<b>Purchased intangible assets with finite lives:</b>								
Technology .....								
Technology .....		\$ 3,182	\$ (1,386)	\$ 1,796				
Customer relationships .....		1,353	(765)	588				
Other .....		82	(38)	44				
<b>Total purchased intangible assets with finite lives</b> .....		<b>4,617</b>	<b>(2,189)</b>	<b>2,428</b>				
<b>In-process research and development, with indefinite lives</b> .....								
In-process research and development, with indefinite lives .....		111	—	111				
<b>Total</b> .....		<b>\$ 4,728</b>	<b>\$ (2,189)</b>	<b>\$ 2,539</b>				

Purchased intangible assets include intangible assets acquired through acquisitions as well as through direct purchases or licenses.

Impairment charges related to purchased intangible assets were approximately \$1 million, \$47 million, and \$74 million for fiscal 2018, fiscal 2017, and fiscal 2016, respectively. Impairment charges were as a result of declines in estimated fair value resulting from the reduction or elimination of expected future cash flows associated with certain of our technology and IPR&D intangible assets.

The following table presents the amortization of purchased intangible assets (in millions):

<u>Years Ended</u>	<u>July 28, 2018</u>	<u>July 29, 2017</u>	<u>July 30, 2016</u>
Amortization of purchased intangible assets:			
Cost of sales .....	\$ 640	\$ 556	\$ 577
Operating expenses			
Amortization of purchased intangible assets .....	221	259	303
Restructuring and other charges .....	—	38	—
Total .....	<u>\$ 861</u>	<u>\$ 853</u>	<u>\$ 880</u>

The estimated future amortization expense of purchased intangible assets with finite lives as of July 28, 2018 is as follows (in millions):

<u>Fiscal Year</u>	<u>Amount</u>
2019.....	\$ 714
2020 .....	\$ 667
2021.....	\$ 475
2022 .....	\$ 222
2023 .....	\$ 82
Thereafter.....	\$ 37

## 5. Restructuring and Other Charges

We initiated a restructuring plan during fiscal 2018 (the “Fiscal 2018 Plan”), in order to realign our organization and enable further investment in key priority areas. The total pretax charges are estimated to be approximately \$300 million. In connection with the Fiscal 2018 Plan, we incurred charges of \$108 million during fiscal 2018. These aggregate pretax charges are primarily cash-based and consist of employee severance and other one-time termination benefits, and other associated costs. We expect the Fiscal 2018 Plan to be substantially completed in fiscal 2019.

We announced a restructuring plan in August 2016 (the “Fiscal 2017 Plan”), in order to reinvest in our key priority areas. In connection with the Fiscal 2017 Plan, we incurred cumulative charges of \$1.0 billion, which were primarily cash-based and consisted of employee severance and other one-time termination benefits, and other associated costs. We completed the Fiscal 2017 Plan in fiscal 2018.

We announced a restructuring action in August 2014 (the “Fiscal 2015 Plan”), in order to realign our workforce towards key growth areas of our business such as data center, software, security, and cloud. In connection with this plan, we incurred cumulative charges of approximately \$756 million. We completed the Fiscal 2015 Plan at the end of fiscal 2016.

The following table summarizes the activities related to the restructuring and other charges, as discussed above (in millions):

	FISCAL 2017 AND PRIOR YEAR PLANS		FISCAL 2018 PLAN			Total
	Employee Severance	Other	Employee Severance	Other		
<b>Liability as of July 25, 2015</b>	\$ 60	\$ 29	\$ —	\$ —	\$ 89	
Charges	225	43	—	—	—	268
Cash payments	(264)	(15)	—	—	—	(279)
Non-cash items	—	(33)	—	—	—	(33)
<b>Liability as of July 30, 2016</b>	21	24	—	—	—	45
Charges	625	131	—	—	—	756
Cash payments	(569)	(37)	—	—	—	(606)
Non-cash items	(3)	(75)	—	—	—	(78)
<b>Liability as of July 29, 2017</b>	<b>74</b>	<b>43</b>	—	—	—	<b>117</b>
Charges	227	23	92	16	—	358
Cash payments	(262)	(35)	(73)	(2)	—	(372)
Non-cash items	2	(18)	—	(14)	—	(30)
<b>Liability as of July 28, 2018</b>	<b>\$ 41</b>	<b>\$ 13</b>	<b>\$ 19</b>	<b>\$ —</b>	<b>\$ 73</b>	

In addition to the above amounts, we incurred \$2 million credit of restructuring and other charges within cost of sales during fiscal 2016.

## 6. Balance Sheet Details

The following tables provide details of selected balance sheet items (in millions):

	<u>July 28, 2018</u>	<u>July 29, 2017</u>
Inventories:		
Raw materials . . . . .	\$    423	\$    289
Work in process . . . . .	—	1
Finished goods:		
Distributor inventory and deferred cost of sales . . . . .	443	451
Manufactured finished goods . . . . .	689	552
Total finished goods . . . . .	<u>1,132</u>	<u>1,003</u>
Service-related spares . . . . .	258	300
Demonstration systems . . . . .	33	23
Total . . . . .	<u>\$ 1,846</u>	<u>\$ 1,616</u>
Property and equipment, net:		
Gross property and equipment:		
Land, buildings, and building and leasehold improvements . . . . .	\$    4,710	\$    4,926
Computer equipment and related software . . . . .	1,085	1,258
Production, engineering, and other equipment . . . . .	5,734	5,707
Operating lease assets . . . . .	356	356
Furniture and fixtures . . . . .	358	572
Total gross property and equipment . . . . .	<u>12,243</u>	<u>12,819</u>
Less: accumulated depreciation and amortization . . . . .	(9,237)	(9,497)
Total . . . . .	<u>\$ 3,006</u>	<u>\$ 3,322</u>
Deferred revenue:		
Service . . . . .	\$    11,431	\$    11,302
Product:		
Deferred revenue related to recurring software and subscription offers . . . . .	6,120	4,971
Other product deferred revenue . . . . .	2,134	2,221
Total product deferred revenue . . . . .	<u>8,254</u>	<u>7,192</u>
Total . . . . .	<u>\$ 19,685</u>	<u>\$ 18,494</u>
Reported as:		
Current . . . . .	\$    11,490	\$    10,821
Noncurrent . . . . .	8,195	7,673
Total . . . . .	<u>\$ 19,685</u>	<u>\$ 18,494</u>

## 7. Financing Receivables and Operating Leases

### (a) Financing Receivables

Financing receivables primarily consist of lease receivables, loan receivables, and financed service contracts. Lease receivables represent sales-type and direct-financing leases resulting from the sale of Cisco's and complementary third-party products and are typically collateralized by a security interest in the underlying assets. Lease receivables consist of arrangements with terms of four years on average. Loan receivables represent financing arrangements related to the sale of our hardware, software, and services, which may include additional funding for other costs associated with network installation and integration of our products and services. Loan receivables generally have terms of up to three years. Financed service contracts include financing receivables related to technical support and advanced services. Revenue related to the technical support services is typically deferred and included in deferred service revenue and is recognized ratably over the period during which the related services are to be performed, which typically ranges from one to three years.

A summary of our financing receivables is presented as follows (in millions):

	Lease Receivables	Loan Receivables	Financed Service Contracts	Total
<b>July 28, 2018</b>				
Gross .....	\$ 2,688	\$ 4,999	\$ 2,326	\$ 10,013
Residual value .....	164	—	—	164
Unearned income .....	(141)	—	—	(141)
Allowance for credit loss .....	(135)	(60)	(10)	(205)
<b>Total, net .....</b>	<b>\$ 2,576</b>	<b>\$ 4,939</b>	<b>\$ 2,316</b>	<b>\$ 9,831</b>
<b>Reported as:</b>				
<b>Current .....</b>	<b>\$ 1,249</b>	<b>\$ 2,376</b>	<b>\$ 1,324</b>	<b>\$ 4,949</b>
<b>Noncurrent .....</b>	<b>1,327</b>	<b>2,563</b>	<b>992</b>	<b>4,882</b>
<b>Total, net .....</b>	<b>\$ 2,576</b>	<b>\$ 4,939</b>	<b>\$ 2,316</b>	<b>\$ 9,831</b>
<b>July 29, 2017</b>				
Gross .....	\$ 2,784	\$ 4,560	\$ 2,517	\$ 9,861
Residual value .....	173	—	—	173
Unearned income .....	(145)	—	—	(145)
Allowance for credit loss .....	(162)	(103)	(30)	(295)
<b>Total, net .....</b>	<b>\$ 2,650</b>	<b>\$ 4,457</b>	<b>\$ 2,487</b>	<b>\$ 9,594</b>
<b>Reported as:</b>				
<b>Current .....</b>	<b>\$ 1,301</b>	<b>\$ 2,104</b>	<b>\$ 1,451</b>	<b>\$ 4,856</b>
<b>Noncurrent .....</b>	<b>1,349</b>	<b>2,353</b>	<b>1,036</b>	<b>4,738</b>
<b>Total, net .....</b>	<b>\$ 2,650</b>	<b>\$ 4,457</b>	<b>\$ 2,487</b>	<b>\$ 9,594</b>

Future minimum lease payments to Cisco on lease receivables as of July 28, 2018 are summarized as follows (in millions):

Fiscal Year	Amount
2019 .....	\$ 1,311
2020 .....	745
2021 .....	415
2022 .....	177
2023 .....	12
Thereafter .....	28
<b>Total .....</b>	<b>\$ 2,688</b>

Actual cash collections may differ from the contractual maturities due to early customer buyouts, refinancings, or defaults.

**(b) Credit Quality of Financing Receivables**

Gross receivables, excluding residual value, less unearned income categorized by our internal credit risk rating as of July 28, 2018 and July 29, 2017 are summarized as follows (in millions):

	INTERNAL CREDIT RISK RATING			
	1 to 4	5 to 6	7 and Higher	Total
<u>July 28, 2018</u>				
Lease receivables . . . . .	\$ 1,294	\$ 1,199	\$ 54	\$ 2,547
Loan receivables . . . . .	3,184	1,752	63	4,999
Financed service contracts . . . . .	1,468	835	23	2,326
<b>Total . . . . .</b>	<b>\$ 5,946</b>	<b>\$ 3,786</b>	<b>\$ 140</b>	<b>\$ 9,872</b>

	INTERNAL CREDIT RISK RATING			
	1 to 4	5 to 6	7 and Higher	Total
<u>July 29, 2017</u>				
Lease receivables . . . . .	\$ 1,408	\$ 1,181	\$ 50	\$ 2,639
Loan receivables . . . . .	2,865	1,516	179	4,560
Financed service contracts . . . . .	1,593	902	22	2,517
<b>Total . . . . .</b>	<b>\$ 5,866</b>	<b>\$ 3,599</b>	<b>\$ 251</b>	<b>\$ 9,716</b>

We determine the adequacy of our allowance for credit loss by assessing the risks and losses inherent in our financing receivables by portfolio segment. The portfolio segment is based on the types of financing offered by us to our customers, which consist of the following: lease receivables, loan receivables, and financed service contracts.

Our internal credit risk ratings of 1 through 4 correspond to investment-grade ratings, while credit risk ratings of 5 and 6 correspond to non-investment grade ratings. Credit risk ratings of 7 and higher correspond to substandard ratings.

In circumstances when collectibility is not deemed reasonably assured, the associated revenue is deferred in accordance with our revenue recognition policies, and the related allowance for credit loss, if any, is included in deferred revenue. We also record deferred revenue associated with financing receivables when there are remaining performance obligations, as we do for financed service contracts.

The following tables present the aging analysis of gross receivables, excluding residual value and less unearned income as of July 28, 2018 and July 29, 2017 (in millions):

	DAYS PAST DUE (INCLUDES BILLED AND UNBILLED)						Nonaccrual Financing Receivables	Impaired Financing Receivables		
				Total	Current	Total				
	31 - 60	61 - 90	91+	Past Due						
<u>July 28, 2018</u>										
Lease receivables . . . . .	\$ 72	\$ 27	\$ 155	\$ 254	\$ 2,293	\$ 2,547	\$ 9	\$ 9		
Loan receivables . . . . .	104	55	252	411	4,588	4,999	30	30		
Financed service contracts . . . . .	138	78	304	520	1,806	2,326	3	3		
<b>Total . . . . .</b>	<b>\$ 314</b>	<b>\$ 160</b>	<b>\$ 711</b>	<b>\$ 1,185</b>	<b>\$ 8,687</b>	<b>\$ 9,872</b>	<b>\$ 42</b>	<b>\$ 42</b>		

	DAYS PAST DUE (INCLUDES BILLED AND UNBILLED)						Nonaccrual Financing Receivables	Impaired Financing Receivables		
				Total	Current	Total				
	31 - 60	61 - 90	91+	Past Due						
<u>July 29, 2017</u>										
Lease receivables . . . . .	\$ 160	\$ 60	\$ 216	\$ 436	\$ 2,203	\$ 2,639	\$ 14	\$ 14		
Loan receivables . . . . .	230	48	259	537	4,023	4,560	43	43		
Financed service contracts . . . . .	160	77	523	760	1,757	2,517	18	2		
<b>Total . . . . .</b>	<b>\$ 550</b>	<b>\$ 185</b>	<b>\$ 998</b>	<b>\$ 1,733</b>	<b>\$ 7,983</b>	<b>\$ 9,716</b>	<b>\$ 75</b>	<b>\$ 59</b>		

Past due financing receivables are those that are 31 days or more past due according to their contractual payment terms. The data in the preceding tables is presented by contract, and the aging classification of each contract is based on the oldest outstanding receivable, and therefore past due amounts also include unbilled and current receivables within the same contract. The balances of either unbilled or current financing receivables included in the category of 91 days plus past due for financing receivables were \$503 million and \$666 million as of July 28, 2018 and July 29, 2017, respectively.

As of July 28, 2018, we had financing receivables of \$182 million, net of unbilled or current receivables, that were in the category of 91 days plus past due but remained on accrual status as they are well secured and in the process of collection. Such balance was \$315 million as of July 29, 2017.

#### (c) Allowance for Credit Loss Rollforward

The allowances for credit loss and the related financing receivables are summarized as follows (in millions):

	CREDIT LOSS ALLOWANCES			
	Lease Receivables	Loan Receivables	Financed Service Contracts	Total
<b>Allowance for credit loss as of July 29, 2017 .....</b>	\$ 162	\$ 103	\$ 30	\$ 295
Provisions (benefits) .....	(26)	(43)	(20)	(89)
Recoveries (write-offs), net .....	(1)	(5)	—	(6)
Foreign exchange and other .....	—	5	—	5
<b>Allowance for credit loss as of July 28, 2018 .....</b>	<b>\$ 135</b>	<b>\$ 60</b>	<b>\$ 10</b>	<b>\$ 205</b>

	CREDIT LOSS ALLOWANCES			
	Lease Receivables	Loan Receivables	Financed Service Contracts	Total
Allowance for credit loss as of July 30, 2016 .....	\$ 230	\$ 97	\$ 48	\$ 375
Provisions (benefits) .....	(25)	7	(17)	(35)
Recoveries (write-offs), net .....	(37)	(11)	(1)	(49)
Foreign exchange and other .....	(6)	10	—	4
<b>Allowance for credit loss as of July 29, 2017 .....</b>	<b>\$ 162</b>	<b>\$ 103</b>	<b>\$ 30</b>	<b>\$ 295</b>

	CREDIT LOSS ALLOWANCES			
	Lease Receivables	Loan Receivables	Financed Service Contracts	Total
Allowance for credit loss as of July 25, 2015 .....	\$ 259	\$ 87	\$ 36	\$ 382
Provisions (benefits) .....	(13)	13	17	17
Recoveries (write-offs), net .....	(10)	—	(5)	(15)
Foreign exchange and other .....	(6)	(3)	—	(9)
<b>Allowance for credit loss as of July 30, 2016 .....</b>	<b>\$ 230</b>	<b>\$ 97</b>	<b>\$ 48</b>	<b>\$ 375</b>

#### (d) Operating Leases

We provide financing of certain equipment through operating leases, and the amounts are included in property and equipment in the Consolidated Balance Sheets. Amounts relating to equipment on operating lease assets and the associated accumulated depreciation are summarized as follows (in millions):

	July 28, 2018	July 29, 2017
Operating lease assets .....	\$ 356	\$ 356
Accumulated depreciation .....	(238)	(212)
<b>Operating lease assets, net .....</b>	<b>\$ 118</b>	<b>\$ 144</b>

Minimum future rentals on noncancelable operating leases as of July 28, 2018 are summarized as follows (in millions):

Fiscal Year	Amount
2019 .....	\$ 166
2020 .....	97
2021 .....	34
2022 .....	2
Thereafter .....	1
<b>Total .....</b>	<b>\$ 300</b>

## 8. Investments

### (a) Summary of Available-for-Sale Investments

The following tables summarize our available-for-sale investments (in millions):

<u>July 28, 2018</u>	<u>Amortized Cost</u>	<u>Gross Unrealized Gains</u>	<u>Gross Unrealized Losses</u>	<u>Fair Value</u>
<b>Fixed income securities:</b>				
U.S. government securities .....	\$ 7,318	\$ —	\$ (43)	\$ 7,275
U.S. government agency securities .....	732	—	(5)	727
Non-U.S. government and agency securities .....	209	—	(1)	208
Corporate debt securities .....	27,765	44	(445)	27,364
U.S. agency mortgage-backed securities .....	1,488	—	(53)	1,435
<b>Total fixed income securities.....</b>	<b>37,512</b>	<b>44</b>	<b>(547)</b>	<b>37,009</b>
<b>Publicly traded equity securities .....</b>				
<b>Total .....</b>	<b>\$ 37,884</b>	<b>\$ 277</b>	<b>\$ (547)</b>	<b>\$ 37,614</b>

<u>July 29, 2017</u>	<u>Amortized Cost</u>	<u>Gross Unrealized Gains</u>	<u>Gross Unrealized Losses</u>	<u>Fair Value</u>
<b>Fixed income securities:</b>				
U.S. government securities .....	\$ 19,880	\$ 3	\$ (60)	\$ 19,823
U.S. government agency securities .....	2,057	—	(5)	2,052
Non-U.S. government and agency securities .....	389	—	(1)	388
Corporate debt securities .....	31,626	202	(93)	31,735
U.S. agency mortgage-backed securities .....	2,037	3	(17)	2,023
Commercial paper .....	996	—	—	996
Certificates of deposit .....	60	—	—	60
<b>Total fixed income securities.....</b>	<b>57,045</b>	<b>208</b>	<b>(176)</b>	<b>57,077</b>
<b>Publicly traded equity securities .....</b>				
<b>Total .....</b>	<b>\$ 58,225</b>	<b>\$ 762</b>	<b>\$ (203)</b>	<b>\$ 58,784</b>

Net unsettled investment sales as of July 28, 2018 and July 29, 2017 were \$1.5 billion and \$30 million, respectively and were included in other current assets and other current liabilities.

Non-U.S. government and agency securities include agency and corporate debt securities that are guaranteed by non-U.S. governments.

### (b) Gains and Losses on Available-for-Sale Investments

The following table presents the gross realized gains and gross realized losses related to our available-for-sale investments (in millions):

<u>Years Ended</u>	<u>July 28, 2018</u>	<u>July 29, 2017</u>	<u>July 30, 2016</u>
Gross realized gains .....	\$ 628	\$ 114	\$ 152
Gross realized losses .....	(341)	(201)	(153)
<b>Total .....</b>	<b>\$ 287</b>	<b>\$ (87)</b>	<b>\$ (1)</b>

The following table presents the realized net gains and losses related to our available-for-sale investments by security type (in millions):

<u>Years Ended</u>	<u>July 28, 2018</u>	<u>July 29, 2017</u>	<u>July 30, 2016</u>
Net gains/(losses) on investments in publicly traded equity securities .....	\$ 529	\$ (45)	\$ 33
Net gains/(losses) on investments in fixed income securities .....	(242)	(42)	(34)
<b>Total .....</b>	<b>\$ 287</b>	<b>\$ (87)</b>	<b>\$ (1)</b>

The following tables present the breakdown of the available-for-sale investments with gross unrealized losses and the duration that those losses had been unrealized at July 28, 2018 and July 29, 2017 (in millions):

July 28, 2018	UNREALIZED LOSSES LESS THAN 12 MONTHS		UNREALIZED LOSSES 12 MONTHS OR GREATER		TOTAL	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
Fixed income securities:						
U.S. government securities .....	\$ 2,966	\$ (20)	\$ 4,303	\$ (23)	\$ 7,269	\$ (43)
U.S. government agency securities .....	206	(2)	521	(3)	727	(5)
Non-U.S. government and agency securities .....	105	(1)	103	—	208	(1)
Corporate debt securities .....	16,990	(344)	3,511	(101)	20,501	(445)
U.S. agency mortgage-backed securities...	826	(24)	581	(29)	1,407	(53)
Total fixed income securities .....	21,093	(391)	9,019	(156)	30,112	(547)
Publicly traded equity securities .....	—	—	—	—	—	—
Total .....	<u>\$ 21,093</u>	<u>\$ (391)</u>	<u>\$ 9,019</u>	<u>\$ (156)</u>	<u>\$ 30,112</u>	<u>\$ (547)</u>
July 29, 2017	UNREALIZED LOSSES LESS THAN 12 MONTHS		UNREALIZED LOSSES 12 MONTHS OR GREATER		TOTAL	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
Fixed income securities:						
U.S. government securities .....	\$ 14,962	\$ (55)	\$ 771	\$ (5)	\$ 15,733	\$ (60)
U.S. government agency securities .....	1,791	(4)	130	(1)	1,921	(5)
Non-U.S. government and agency securities .....	368	(1)	—	—	368	(1)
Corporate debt securities .....	9,487	(92)	101	(1)	9,588	(93)
U.S. agency mortgage-backed securities...	1,485	(16)	38	(1)	1,523	(17)
Total fixed income securities .....	28,093	(168)	1,040	(8)	29,133	(176)
Publicly traded equity securities .....	122	(27)	—	—	122	(27)
Total .....	<u>\$ 28,215</u>	<u>\$ (195)</u>	<u>\$ 1,040</u>	<u>\$ (8)</u>	<u>\$ 29,255</u>	<u>\$ (203)</u>

For fiscal 2018, the realized net losses for available-for-sale investments included impairment charges of \$52 million. These impairment charges related primarily to publicly traded equity securities and were due to a decline in the fair value of those securities below their cost basis that were determined to be other than temporary. For fiscal 2017, the realized net losses related to available-for-sale investments included impairment charges of \$74 million, primarily related to publicly traded equity securities. These impairment charges were due to a decline in the fair value of those securities below their cost basis that were determined to be other than temporary. For fiscal 2016, the realized net losses related to available-for-sale investments included impairment charges of \$3 million for fixed income securities.

As of July 28, 2018, for available-for-sale investments that were in unrealized loss positions, we have determined that no additional other-than-temporary impairments were required to be recognized.

**(c) Maturities of Fixed Income Securities**

The following table summarizes the maturities of our fixed income securities at July 28, 2018 (in millions):

	Amortized Cost	Fair Value
Less than 1 year . . . . .	\$ 12,361	\$ 12,316
Due in 1 to 2 years . . . . .	7,573	7,514
Due in 2 to 5 years . . . . .	14,290	14,012
Due after 5 years . . . . .	1,800	1,732
Mortgage-backed securities with no single maturity . . . . .	1,488	1,435
Total . . . . .	<u>\$ 37,512</u>	<u>\$ 37,009</u>

Actual maturities may differ from the contractual maturities because borrowers may have the right to call or prepay certain obligations. The remaining contractual principal maturities for mortgage-backed securities were allocated assuming no prepayments.

**(d) Securities Lending**

We periodically engage in securities lending activities with certain of our available-for-sale investments. These transactions are accounted for as a secured lending of the securities, and the securities are typically loaned only on an overnight basis. The average daily balance of securities lending for fiscal 2018 and 2017 was \$0.3 billion and \$0.7 billion, respectively. We require collateral equal to at least 102% of the fair market value of the loaned security and that the collateral be in the form of cash or liquid, high-quality assets. We engage in these secured lending transactions only with highly creditworthy counterparties, and the associated portfolio custodian has agreed to indemnify us against collateral losses. We did not experience any losses in connection with the secured lending of securities during the periods presented. As of July 28, 2018 and July 29, 2017, we had no outstanding securities lending transactions.

**(e) Investments in Privately Held Companies**

The carrying value of our investments in privately held companies was included in other assets. For such investments that were accounted for under the equity and cost method as of July 28, 2018 and July 29, 2017, the amounts are summarized in the following table (in millions):

	July 28, 2018	July 29, 2017
Equity method investments . . . . .	\$ 118	\$ 124
Cost method investments . . . . .	978	859
Total . . . . .	<u>\$ 1,096</u>	<u>\$ 983</u>

For additional information on impairment charges related to investments in privately held companies, see Note 9.

***Variable Interest Entities*** In the ordinary course of business, we have investments in privately held companies and provide financing to certain customers. These privately held companies and customers may be considered to be variable interest entities. We evaluate on an ongoing basis our investments in these privately held companies and our customer financings and have determined that as of July 28, 2018, except as disclosed herein, there were no variable interest entities required to be consolidated in our Consolidated Financial Statements.

As of July 28, 2018, the carrying value of our investments in privately held companies was \$1.1 billion, of which \$531 million of such investments are considered to be in variable interest entities which are unconsolidated. In addition, we have additional funding commitments of \$223 million related to these investments, some of which are based on the achievement of certain agreed-upon milestones, and some of which are required to be funded on demand. The carrying value of these investments and the additional funding commitments collectively represent our maximum exposure related to these variable interest entities.

## 9. Fair Value

### (a) Assets and Liabilities Measured at Fair Value on a Recurring Basis

Assets and liabilities measured at fair value on a recurring basis were as follows (in millions):

	JULY 28, 2018			JULY 29, 2017		
	FAIR VALUE MEASUREMENTS			FAIR VALUE MEASUREMENTS		
	Level 1	Level 2	Total Balance	Level 1	Level 2	Total Balance
<b>Assets:</b>						
Cash equivalents:						
Money market funds .....	\$ 6,890	\$ —	\$ 6,890	\$ 9,567	\$ —	\$ 9,567
U.S. government securities .....	—	—	—	—	139	139
Commercial paper .....	—	—	—	—	160	160
Certificates of deposit .....	—	—	—	—	25	25
Available-for-sale investments:						
U.S. government securities .....	—	7,275	7,275	—	19,823	19,823
U.S. government agency securities .....	—	727	727	—	2,052	2,052
Non-U.S. government and agency securities.....	—	208	208	—	388	388
Corporate debt securities.....	—	27,364	27,364	—	31,735	31,735
U.S. agency mortgage-backed securities.....	—	1,435	1,435	—	2,023	2,023
Commercial paper .....	—	—	—	—	996	996
Certificates of deposit .....	—	—	—	—	60	60
Publicly traded equity securities .....	605	—	605	1,707	—	1,707
Derivative assets .....	—	2	2	—	149	149
Total .....	\$ 7,495	\$ 37,011	\$ 44,506	\$ 11,274	\$ 57,550	\$ 68,824
<b>Liabilities:</b>						
Derivative liabilities.....	\$ —	\$ 74	\$ 74	\$ —	\$ 4	\$ 4
Total .....	\$ —	\$ 74	\$ 74	\$ —	\$ 4	\$ 4

We classify our cash equivalents and available-for-sale investments within Level 1 or Level 2 in the fair value hierarchy because we use quoted prices in active markets or alternative pricing sources and models using market observable inputs to determine their fair value. Our derivative instruments are classified as Level 2, as they are not actively traded and are valued using pricing models that use observable market inputs. We did not have any transfers between Level 1 and Level 2 fair value measurements during the periods presented.

**(b) Assets Measured at Fair Value on a Nonrecurring Basis**

The following table presents gains and losses on assets that were measured at fair value on a nonrecurring basis(in millions):

	TOTAL GAINS (LOSSES) FOR THE YEARS ENDED		
	July 28, 2018	July 29, 2017	July 30, 2016
Investments in privately held companies (impaired).....	\$ (56)	\$ (175)	\$ (57)
Purchased intangible assets (impaired) .....	(1)	(47)	(74)
Property held for sale - land and buildings .....	20	(30)	—
Gains (losses) on assets no longer held at end of fiscal year .....	(6)	(2)	(10)
Total gains (losses) for nonrecurring measurements .....	<u>\$ (43)</u>	<u>\$ (254)</u>	<u>\$ (141)</u>

These assets were measured at fair value due to events or circumstances we identified as having significant impact on their fair value during the respective periods. To arrive at the valuation of these assets, we consider any significant changes in the financial metrics and economic variables and also use third-party valuation reports to assist in the valuation as necessary.

The fair value measurement of the impaired investments was classified as Level 3 because significant unobservable inputs were used in the valuation due to the absence of quoted market prices and inherent lack of liquidity. Significant unobservable inputs, which included financial metrics of comparable private and public companies, financial condition and near-term prospects of the investees, recent financing activities of the investees, and the investees' capital structure as well as other economic variables, reflected the assumptions market participants would use in pricing these assets. The impairment charges, representing the difference between the net book value and the fair value as a result of the evaluation, were recorded to other income (loss), net. The remaining carrying value of the investments that were impaired was \$57 million and \$81 million as of July 28, 2018 and July 29, 2017, respectively.

The fair value for purchased intangibles assets measured at fair value on a nonrecurring basis was categorized as Level 3 due to the use of significant unobservable inputs in the valuation. Significant unobservable inputs that were used included expected revenues and net income related to the assets and the expected life of the assets. The difference between the estimated fair value and the carrying value of the assets was recorded as an impairment charge, which was included in product cost of sales and operating expenses as applicable. See Note 4. The remaining carrying value of the specific purchased intangible assets that were impaired was zero and \$63 million as of July 28, 2018 and July 29, 2017, respectively.

The fair value of property held for sale was measured with the assistance of third-party valuation models, which used discounted cash flow techniques as part of their analysis. The fair value measurement was categorized as Level 3, as significant unobservable inputs were used in the valuation report. The impairment charges as a result of the valuations, which represented the difference between the fair value less cost to sell and the carrying amount of the assets held for sale, was included in restructuring and other charges. The remaining carrying value of the property held for sale that was impaired was zero and \$5 million as of July 28, 2018 and July 29, 2017, respectively.

**(c) Other Fair Value Disclosures**

The carrying value of our investments in privately held companies that were accounted for under the cost method was \$978 million and \$859 million as of July 28, 2018 and July 29, 2017, respectively. It was not practicable to estimate the fair value of this portfolio.

The fair value of our short-term loan receivables and financed service contracts approximates their carrying value due to their short duration. The aggregate carrying value of our long-term loan receivables and financed service contracts as of July 28, 2018 and July 29, 2017 was \$3.6 billion and \$3.4 billion, respectively. The estimated fair value of our long-term loan receivables and financed service contracts approximates their carrying value. We use significant unobservable inputs in determining discounted cash flows to estimate the fair value of our long-term loan receivables and financed service contracts, and therefore they are categorized as Level 3.

As of July 28, 2018 and July 29, 2017, the estimated fair value of our short-term debt approximates its carrying value due to the short maturities. As of July 28, 2018, the fair value of our senior notes and other long-term debt was \$26.4 billion, with a carrying amount of \$25.6 billion. This compares to a fair value of \$32.1 billion and a carrying amount of \$30.5 billion as of July 29, 2017. The fair value of the senior notes and other long-term debt was determined based on observable market prices in a less active market and was categorized as Level 2 in the fair value hierarchy.

## **10. Borrowings**

### **(a) Short-Term Debt**

The following table summarizes our short-term debt (in millions, except percentages):

	July 28, 2018		July 29, 2017	
	Amount	Effective Rate	Amount	Effective Rate
Current portion of long-term debt .....	\$ 5,238	3.46%	\$ 4,747	1.66%
Commercial paper .....	—	—	3,245	1.16%
Total short-term debt .....	<u>\$ 5,238</u>		<u>\$ 7,992</u>	

We have a short-term debt financing program of up to \$10.0 billion through the issuance of commercial paper notes. We use the proceeds from the issuance of commercial paper notes for general corporate purposes.

The effective rates for the short- and long-term debt include the interest on the notes, the accretion of the discount, the issuance costs, and, if applicable, adjustments related to hedging.

**(b) Long-Term Debt**

The following table summarizes our long-term debt (in millions, except percentages):

	Maturity Date	July 28, 2018		July 29, 2017		
		Amount	Effective Rate	Amount	Effective Rate	
<b>Senior notes:</b>						
<b>Floating-rate notes:</b>						
Three-month LIBOR plus 0.60% .....	February 21, 2018	\$ —	—	\$ 1,000	1.84%	
Three-month LIBOR plus 0.31% .....	June 15, 2018	—	—	900	1.62%	
Three-month LIBOR plus 0.50% .....	March 1, 2019	<b>500</b>	<b>2.86%</b>	500	1.76%	
Three-month LIBOR plus 0.34% .....	September 20, 2019	<b>500</b>	<b>2.71%</b>	500	1.66%	
<b>Fixed-rate notes:</b>						
1.40% .....	February 28, 2018	—	—	1,250	1.47%	
1.65% .....	June 15, 2018	—	—	1,600	1.72%	
4.95% .....	February 15, 2019	<b>2,000</b>	<b>5.17%</b>	2,000	4.96%	
1.60% .....	February 28, 2019	<b>1,000</b>	<b>1.67%</b>	1,000	1.67%	
2.125% .....	March 1, 2019	<b>1,750</b>	<b>2.71%</b>	1,750	1.84%	
1.40% .....	September 20, 2019	<b>1,500</b>	<b>1.48%</b>	1,500	1.48%	
4.45% .....	January 15, 2020	<b>2,500</b>	<b>4.52%</b>	2,500	3.84%	
2.45% .....	June 15, 2020	<b>1,500</b>	<b>2.54%</b>	1,500	2.54%	
2.20% .....	February 28, 2021	<b>2,500</b>	<b>2.30%</b>	2,500	2.30%	
2.90% .....	March 4, 2021	<b>500</b>	<b>2.86%</b>	500	2.00%	
1.85% .....	September 20, 2021	<b>2,000</b>	<b>1.90%</b>	2,000	1.90%	
3.00% .....	June 15, 2022	<b>500</b>	<b>3.11%</b>	500	2.26%	
2.60% .....	February 28, 2023	<b>500</b>	<b>2.68%</b>	500	2.68%	
2.20% .....	September 20, 2023	<b>750</b>	<b>2.27%</b>	750	2.27%	
3.625% .....	March 4, 2024	<b>1,000</b>	<b>2.98%</b>	1,000	2.12%	
3.50% .....	June 15, 2025	<b>500</b>	<b>3.27%</b>	500	2.43%	
2.95% .....	February 28, 2026	<b>750</b>	<b>3.01%</b>	750	3.01%	
2.50% .....	September 20, 2026	<b>1,500</b>	<b>2.55%</b>	1,500	2.55%	
5.90% .....	February 15, 2039	<b>2,000</b>	<b>6.11%</b>	2,000	6.11%	
5.50% .....	January 15, 2040	<b>2,000</b>	<b>5.67%</b>	2,000	5.67%	
Total .....		<b>25,750</b>		30,500		
Unaccrued discount/issuance costs .....		<b>(116)</b>		(136)		
Hedge accounting fair value adjustments .....		<b>(65)</b>		108		
Total .....		<b>\$ 25,569</b>		<b>\$ 30,472</b>		
<b>Reported as:</b>						
Short-term debt .....		<b>\$ 5,238</b>		\$ 4,747		
Long-term debt .....		<b>20,331</b>		25,725		
Total .....		<b>\$ 25,569</b>		<b>\$ 30,472</b>		

We entered into interest rate swaps in prior periods with an aggregate notional amount of \$6.75 billion designated as fair value hedges of certain of our fixed-rate senior notes. These swaps convert the fixed interest rates of the fixed-rate notes to floating interest rates based on the London InterBank Offered Rate (LIBOR). The gains and losses related to changes in the fair value of the interest rate swaps substantially offset changes in the fair value of the hedged portion of the underlying debt that are attributable to the changes in market interest rates. For additional information, see Note 11.

Interest is payable semiannually on each class of the senior fixed-rate notes and payable quarterly on the floating-rate notes. Each of the senior fixed-rate notes is redeemable by us at any time, subject to a make-whole premium. The senior notes rank at par with the commercial paper notes that have been issued in the future pursuant to our short-term debt financing program, as discussed above under “(a) Short-Term Debt.” As of July 28, 2018, we were in compliance with all debt covenants.

As of July 28, 2018, future principal payments for long-term debt, including the current portion, are summarized as follows (in millions):

Fiscal Year	Amount
2019 .....	\$ 5,250
2020 .....	6,000
2021 .....	3,000
2022 .....	2,500
2023 .....	500
Thereafter .....	8,500
Total .....	<u>\$ 25,750</u>

### (c) Credit Facility

On May 15, 2015, we entered into a credit agreement with certain institutional lenders that provides for a \$3.0 billion unsecured revolving credit facility that is scheduled to expire on May 15, 2020. Any advances under the credit agreement will accrue interest at rates that are equal to, based on certain conditions, either (i) the highest of (a) the Federal Funds rate plus 0.50%, (b) Bank of America's "prime rate" as announced from time to time, or (c) LIBOR, or a comparable or successor rate that is approved by the Administrative Agent ("Eurocurrency Rate"), for an interest period of one-month plus 1.00%, or (ii) the Eurocurrency Rate, plus a margin that is based on our senior debt credit ratings as published by Standard & Poor's Financial Services, LLC and Moody's Investors Service, Inc., provided that in no event will the Eurocurrency Rate be less than zero. We may also, upon agreement of either the then-existing lenders or additional lenders not currently parties to the agreement, increase the commitments under the credit facility by up to an additional \$2.0 billion and/or extend the expiration date of the credit facility up to May 15, 2022.

This credit agreement requires that we comply with certain covenants, including that we maintain an interest coverage ratio as defined in the agreement. As of July 28, 2018, we were in compliance with the required interest coverage ratio and the other covenants, and we had not borrowed any funds under the credit facility.

## 11. Derivative Instruments

### (a) Summary of Derivative Instruments

We use derivative instruments primarily to manage exposures to foreign currency exchange rate, interest rate, and equity price risks. Our primary objective in holding derivatives is to reduce the volatility of earnings and cash flows associated with changes in foreign currency exchange rates, interest rates, and equity prices. Our derivatives expose us to credit risk to the extent that the counterparties may be unable to meet the terms of the agreement. We do, however, seek to mitigate such risks by limiting our counterparties to major financial institutions. In addition, the potential risk of loss with any one counterparty resulting from this type of credit risk is monitored. Management does not expect material losses as a result of defaults by counterparties.

The fair values of our derivative instruments and the line items on the Consolidated Balance Sheets to which they were recorded are summarized as follows (in millions):

	DERIVATIVE ASSETS		DERIVATIVE LIABILITIES			
	Balance Sheet Line Item	July 28, 2018	July 29, 2017	Balance Sheet Line Item	July 28, 2018	July 29, 2017
<b>Derivatives designated as hedging instruments:</b>						
Foreign currency derivatives .....	Other current assets	\$ 1	\$ 46	Other current liabilities	\$ —	\$ 1
Interest rate derivatives .....	Other current assets	—	—	Other current liabilities	10	—
Interest rate derivatives .....	Other assets	—	102	Other long-term liabilities	62	—
Total .....		1	148		72	1
<b>Derivatives not designated as hedging instruments:</b>						
Foreign currency derivatives .....	Other current assets	1	1	Other current liabilities	2	3
Total .....		1	1		2	3
Total.....		<u>\$ 2</u>	<u>\$ 149</u>		<u>\$ 74</u>	<u>\$ 4</u>

The effects of our cash flow and net investment hedging instruments on other comprehensive income (OCI) and the Consolidated Statements of Operations are summarized as follows (in millions):

	GAINS (LOSSES) RECOGNIZED IN OCI ON DERIVATIVES FOR THE YEARS ENDED (EFFECTIVE PORTION)			Line Item in Statements of Operations	GAINS (LOSSES) RECLASSIFIED FROM AOCI INTO INCOME FOR THE YEARS ENDED (EFFECTIVE PORTION)		
	July 28, 2018	July 29, 2017	July 30, 2016		July 28, 2018	July 29, 2017	July 30, 2016
<b>Derivatives designated as cash flow hedging instruments:</b>							
Foreign currency derivatives . . . . .	\$ 20	\$ 22	\$ (66)	Operating expenses . . . . .	\$ 52	\$ (59)	\$ (15)
				Cost of sales — service . . . . .	16	(20)	(5)
Total . . . . .	<u>\$ 20</u>	<u>\$ 22</u>	<u>\$ (66)</u>	Total . . . . .	<u>\$ 68</u>	<u>\$ (79)</u>	<u>\$ (20)</u>
<b>Derivatives designated as net investment hedging instruments:</b>							
Foreign currency derivatives . . . . .	<u>\$ (1)</u>	<u>\$ (15)</u>	<u>\$ 16</u>	Other income (loss), net . . . . .	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>

As of July 28, 2018, we estimate that approximately \$1 million of net derivative gains related to our cash flow hedges included in AOCI will be reclassified into earnings within the next 12 months when the underlying hedged item impacts earnings.

The effect on the Consolidated Statements of Operations of derivative instruments designated as fair value hedges and the underlying hedged items is summarized as follows (in millions):

	Line Item in Statements of Operations	GAINS (LOSSES) ON DERIVATIVE INSTRUMENTS FOR THE YEARS ENDED			GAINS (LOSSES) RELATED TO HEDGED ITEMS FOR THE YEARS ENDED		
		July 28, 2018	July 29, 2017	July 30, 2016	July 28, 2018	July 29, 2017	July 30, 2016
Derivatives Designated as Fair Value Hedging Instruments							
Interest rate derivatives . . . . .	Interest expense	\$ (174)	\$ (275)	\$ 175	\$ 173	\$ 271	\$ (169)

The effect on the Consolidated Statements of Operations of derivative instruments not designated as hedges is summarized as follows (in millions):

	Line Item in Statements of Operations	GAINS (LOSSES) FOR THE YEARS ENDED		
		July 28, 2018	July 29, 2017	July 30, 2016
Derivatives Not Designated as Hedging Instruments				
Foreign currency derivatives . . . . .	Other income (loss), net	\$ (24)	\$ 13	\$ (19)
Total return swaps—deferred compensation . . . . .	Operating expenses	50	53	6
	Cost of sales — product	1	2	—
	Cost of sales — service	3	3	1
	Other income (loss), net	(11)	—	—
Equity derivatives . . . . .	Other income (loss), net	(4)	11	13
Total . . . . .		<u>\$ 15</u>	<u>\$ 82</u>	<u>\$ 1</u>

The notional amounts of our outstanding derivatives are summarized as follows (in millions):

		July 28, 2018	July 29, 2017
Derivatives designated as hedging instruments:			
Foreign currency derivatives—cash flow hedges . . . . .		\$ 147	\$ 1,696
Interest rate derivatives . . . . .		6,750	6,750
Net investment hedging instruments . . . . .		250	351
Derivatives not designated as hedging instruments:			
Foreign currency derivatives . . . . .		2,298	2,258
Total return swaps—deferred compensation . . . . .		566	535
Total . . . . .		<u>\$ 10,011</u>	<u>\$ 11,590</u>

## (b) Offsetting of Derivative Instruments

We present our derivative instruments at gross fair values in the Consolidated Balance Sheets. However, our master netting and other similar arrangements with the respective counterparties allow for net settlement under certain conditions, which are designed to reduce credit risk by permitting net settlement with the same counterparty. To further limit credit risk, we also enter into collateral security arrangements related to certain derivative instruments whereby cash is posted as collateral between the counterparties based on the fair market value of the derivative instrument. Information related to these offsetting arrangements is summarized as follows (in millions):

	GROSS AMOUNTS OFFSET IN THE CONSOLIDATED BALANCE SHEET			GROSS AMOUNTS NOT OFFSET IN THE CONSOLIDATED BALANCE SHEET BUT WITH LEGAL RIGHTS TO OFFSET		
	Gross Amounts Recognized	Gross Amounts Offset	Net Amounts Presented	Gross Derivative Amounts	Cash Collateral	Net Amount
<u>July 28, 2018</u>						
Derivatives assets .....	\$ 2	\$ —	\$ 2	\$ (2)	\$ —	\$ —
Derivatives liabilities .....	\$ 74	\$ —	\$ 74	\$ (2)	\$ (53)	\$ 19

	GROSS AMOUNTS OFFSET IN THE CONSOLIDATED BALANCE SHEET			GROSS AMOUNTS NOT OFFSET IN THE CONSOLIDATED BALANCE SHEET BUT WITH LEGAL RIGHTS TO OFFSET		
	Gross Amounts Recognized	Gross Amounts Offset	Net Amounts Presented	Gross Derivative Amounts	Cash Collateral	Net Amount
<u>July 29, 2017</u>						
Derivatives assets .....	\$ 149	\$ —	\$ 149	\$ (4)	\$ (81)	\$ 64
Derivatives liabilities .....	\$ 4	\$ —	\$ 4	\$ (4)	\$ —	\$ —

## (c) Foreign Currency Exchange Risk

We conduct business globally in numerous currencies. Therefore, we are exposed to adverse movements in foreign currency exchange rates. To limit the exposure related to foreign currency changes, we enter into foreign currency contracts. We do not enter into such contracts for speculative purposes.

We may hedge forecasted foreign currency transactions related to certain revenues, operating expenses and service cost of sales with currency options and forward contracts. These currency options and forward contracts, designated as cash flow hedges, generally have maturities of less than 24 months. We assess effectiveness based on changes in total fair value of the derivatives. The effective portion of the derivative instrument's gain or loss is initially reported as a component of AOCI and subsequently reclassified into earnings when the hedged exposure affects earnings. The ineffective portion, if any, of the gain or loss is reported in earnings immediately. During the fiscal years presented, we did not discontinue any cash flow hedges for which it was probable that a forecasted transaction would not occur.

We enter into foreign exchange forward and option contracts to reduce the short-term effects of foreign currency fluctuations on assets and liabilities such as foreign currency receivables, including long-term customer financings, investments, and payables. These derivatives are not designated as hedging instruments. Gains and losses on the contracts are included in other income (loss), net, and substantially offset foreign exchange gains and losses from the remeasurement of intercompany balances or other current assets, investments, or liabilities denominated in currencies other than the functional currency of the reporting entity.

We hedge certain net investments in our foreign operations with forward contracts to reduce the effects of foreign currency fluctuations on our net investment in those foreign subsidiaries. These derivative instruments generally have maturities of up to six months.

## (d) Interest Rate Risk

Interest Rate Derivatives, Investments Our primary objective for holding fixed income securities is to achieve an appropriate investment return consistent with preserving principal and managing risk. To realize these objectives, we may utilize interest rate swaps or other derivatives designated as fair value or cash flow hedges. As of July 28, 2018 and July 29, 2017, we did not have any outstanding interest rate derivatives related to our fixed income securities.

Interest Rate Derivatives Designated as Fair Value Hedges, Long-Term Debt In fiscal 2018, we did not enter into any interest rate swaps. In prior fiscal years, we entered into interest rate swaps designated as fair value hedges related to fixed-rate senior notes that are due in fiscal 2019 through 2025. Under these interest rate swaps, we receive fixed-rate interest payments and make interest payments based on LIBOR plus a fixed number of basis points. The effect of such swaps is to convert the fixed interest rates of the senior fixed-rate notes to floating interest rates based on LIBOR. The gains and losses related to changes in the fair value of the interest rate swaps are included in interest expense and substantially offset changes in the fair value of the hedged portion of the underlying debt that are attributable to the changes in market interest rates. The fair value of the interest rate swaps were reflected in other assets and other current and long-term liabilities.

**(e) Equity Price Risk**

We may hold equity securities for strategic purposes or to diversify our overall investment portfolio. The publicly traded equity securities in our portfolio are subject to price risk. To manage our exposure to changes in the fair value of certain equity securities, we have periodically entered into equity derivatives that are designated as fair value hedges. The changes in the value of the hedging instruments are included in other income (loss), net, and offset the change in the fair value of the underlying hedged investment. In addition, we periodically enter into equity derivatives that are not designated as accounting hedges. The changes in the fair value of these derivatives are also included in other income (loss), net.

We are also exposed to variability in compensation charges related to certain deferred compensation obligations to employees. Although not designated as accounting hedges, we utilize derivatives such as total return swaps to economically hedge this exposure.

**(f) Hedge Effectiveness**

For the fiscal years presented, amounts excluded from the assessment of hedge effectiveness were not material for fair value, cash flow, and net investment hedges. In addition, hedge ineffectiveness for fair value, cash flow, and net investment hedges was not material for any of the fiscal years presented.

**12. Commitments and Contingencies**

**(a) Operating Leases**

We lease office space in many U.S. locations. Outside the United States, larger leased sites include sites in Belgium, Canada, China, Germany, India, Israel, Japan, Mexico, Poland, and the United Kingdom. We also lease equipment and vehicles. Future minimum lease payments under all noncancelable operating leases with an initial term in excess of one year as of July 28, 2018 are as follows (in millions):

Fiscal Year	Amount
2019 .....	\$ 392
2020 .....	293
2021 .....	190
2022 .....	138
2023 .....	96
Thereafter .....	111
Total .....	<u>\$ 1,220</u>

Rent expense for office space and equipment totaled \$442 million, \$403 million, and \$385 million in fiscal 2018, 2017, and 2016, respectively.

**(b) Purchase Commitments with Contract Manufacturers and Suppliers**

We purchase components from a variety of suppliers and use several contract manufacturers to provide manufacturing services for our products. During the normal course of business, in order to manage manufacturing lead times and help ensure adequate component supply, we enter into agreements with contract manufacturers and suppliers that either allow them to procure inventory based upon criteria as defined by us or establish the parameters defining our requirements. A significant portion of our reported purchase commitments arising from these agreements consists of firm, noncancelable, and unconditional commitments. Certain of these purchase commitments with contract manufacturers and suppliers relate to arrangements to secure long-term pricing for certain product components for multi-year periods. In certain instances, these agreements allow us the option to cancel, reschedule, and adjust our requirements based on our business needs prior to firm orders being placed.

The following table summarizes our purchase commitments with contract manufacturers and suppliers (in millions):

<u>Commitments by Period</u>	<u>July 28, 2018</u>	<u>July 29, 2017</u>
Less than 1 year . . . . .	\$ 5,407	\$ 4,620
1 to 3 years . . . . .	710	20
3 to 5 years . . . . .	360	—
Total . . . . .	<u>\$ 6,477</u>	<u>\$ 4,640</u>

We record a liability for firm, noncancelable, and unconditional purchase commitments for quantities in excess of our future demand forecasts consistent with the valuation of our excess and obsolete inventory. As of July 28, 2018 and July 29, 2017, the liability for these purchase commitments was \$159 million and \$162 million, respectively, and was included in other current liabilities.

#### (c) Other Commitments

In connection with our acquisitions, we have agreed to pay certain additional amounts contingent upon the achievement of certain agreed-upon technology, development, product, or other milestones or upon the continued employment with Cisco of certain employees of the acquired entities.

The following table summarizes the compensation expense related to acquisitions (in millions):

	<u>July 28, 2018</u>	<u>July 29, 2017</u>	<u>July 30, 2016</u>
Compensation expense related to acquisitions . . . . .	\$ 203	\$ 212	\$ 282

As of July 28, 2018, we estimated that future cash compensation expense of up to \$352 million may be required to be recognized pursuant to the applicable business combination agreements.

In fiscal 2012, we made an investment in Insieme, an early stage company focused on research and development in the data center market. This investment included \$100 million of funding and a license to certain of our technology. During fiscal 2014, we acquired the remaining interests in Insieme, at which time the former noncontrolling interest holders became eligible to receive up to two milestone payments, which were determined using agreed-upon formulas based primarily on revenue for certain of Insieme's products. The former noncontrolling interest holders earned the maximum amount related to these two milestone payments and were paid approximately \$441 million during fiscal 2017. We recorded compensation expense of \$47 million and \$160 million during fiscal 2017 and fiscal 2016, respectively, related to these milestone payments.

We also have certain funding commitments, primarily related to our investments in privately held companies and venture funds, some of which are based on the achievement of certain agreed-upon milestones, and some of which are required to be funded on demand. The funding commitments were \$223 million and \$216 million as of July 28, 2018 and July 29, 2017, respectively.

#### (d) Product Warranties

The following table summarizes the activity related to the product warranty liability (in millions):

	<u>July 28, 2018</u>	<u>July 29, 2017</u>	<u>July 30, 2016</u>
Balance at beginning of fiscal year . . . . .	\$ 407	\$ 414	\$ 449
Provisions for warranties issued . . . . .	582	691	715
Adjustments for pre-existing warranties . . . . .	(38)	(21)	(8)
Settlements . . . . .	(592)	(677)	(714)
Divestiture . . . . .	—	—	(28)
Balance at end of fiscal year . . . . .	<u>\$ 359</u>	<u>\$ 407</u>	<u>\$ 414</u>

We accrue for warranty costs as part of our cost of sales based on associated material product costs, labor costs for technical support staff, and associated overhead. Our products are generally covered by a warranty for periods ranging from 90 days to five years, and for some products we provide a limited lifetime warranty.

#### (e) Financing and Other Guarantees

In the ordinary course of business, we provide financing guarantees for various third-party financing arrangements extended to channel partners and end-user customers. Payments under these financing guarantee arrangements were not material for the periods presented.

**Channel Partner Financing Guarantees** We facilitate arrangements for third-party financing extended to channel partners, consisting of revolving short-term financing, generally with payment terms ranging from 60 to 90 days. These financing arrangements facilitate the working capital requirements of the channel partners, and, in some cases, we guarantee a portion of these arrangements. The volume of channel partner financing was \$28.2 billion, \$27.0 billion, and \$26.9 billion in fiscal 2018, 2017, and 2016, respectively. The balance of the channel partner financing subject to guarantees was \$953 million and \$1.0 billion as of July 28, 2018 and July 29, 2017, respectively.

**End-User Financing Guarantees** We also provide financing guarantees for third-party financing arrangements extended to end-user customers related to leases and loans, which typically have terms of up to three years. The volume of financing provided by third parties for leases and loans as to which we had provided guarantees was \$35 million, \$51 million, and \$63 million in fiscal 2018, 2017, and 2016, respectively.

**Financing Guarantee Summary** The aggregate amounts of financing guarantees outstanding at July 28, 2018 and July 29, 2017, representing the total maximum potential future payments under financing arrangements with third parties along with the related deferred revenue, are summarized in the following table (in millions):

	<u>July 28, 2018</u>	<u>July 29, 2017</u>
Maximum potential future payments relating to financing guarantees:		
Channel partner .....	\$   277	\$   240
End user .....	<u>31</u>	<u>74</u>
Total .....	<u>\$   308</u>	<u>\$   314</u>
Deferred revenue associated with financing guarantees:		
Channel partner .....	\$   (94)	\$   (82)
End user .....	<u>(28)</u>	<u>(52)</u>
Total .....	<u>\$   (122)</u>	<u>\$   (134)</u>
Maximum potential future payments relating to financing guarantees, net of associated deferred revenue .....	<u>\$   186</u>	<u>\$   180</u>

**Other Guarantees** Our other guarantee arrangements as of July 28, 2018 and July 29, 2017 that were subject to recognition and disclosure requirements were not material.

#### **(f) Supplier Component Remediation Liability**

In fiscal 2014, we recorded a charge to product cost of sales of \$655 million resulting from failures related to products containing memory components manufactured by a single supplier between 2005 and 2010. We perform regular assessments of the sufficiency of this liability and reduced the amount by \$164 million and \$74 million in fiscal 2015 and fiscal 2016, respectively, based on updated analyses. We further reduced the liability by \$141 million and \$58 million in fiscal 2017 and fiscal 2018, respectively, to reflect lower than expected defects, actual usage history, and estimated lower future remediation costs as more of the impacted products age and near the end of the support period covered by the remediation program.

During the second quarter of fiscal 2017, we recorded a charge to product cost of sales of \$125 million related to the expected remediation costs for anticipated failures in future periods of a widely-used component sourced from a third party which is included in several of our products.

The liabilities related to the supplier component remediation matters were \$44 million and \$174 million as of July 28, 2018 and July 29, 2017, respectively.

#### **(g) Indemnifications**

In the normal course of business, we indemnify other parties, including customers, lessors, and parties to other transactions with us, with respect to certain matters. We have agreed to hold such parties harmless against losses arising from a breach of representations or covenants or out of intellectual property infringement or other claims made against certain parties. These agreements may limit the time within which an indemnification claim can be made and the amount of the claim.

We have been asked to indemnify certain of our service provider customers that have been subject to patent infringement claims asserted by Sprint Communications Company, L.P. in federal court in Kansas and Delaware. Sprint alleges that the service provider customers infringed Sprint's patents by offering VoIP telephone services utilizing products provided by us generally in combination with those of other manufacturers. Sprint seeks monetary damages. Following a trial on March 3, 2017 against Time Warner Inc., a jury in Kansas found that Time Warner Cable willfully infringed five Sprint patents and awarded Sprint \$139.8 million in damages. On March 14, 2017, the Kansas court declined Sprint's request for enhanced damages and entered judgment in favor of Sprint for \$139.8 million plus 1.06% in post-judgment interest. On May 30, 2017, the Court awarded Sprint

\$20.3 million in pre-judgment interest and denied Time Warner Cable's post-trial motions. Time Warner Cable has appealed. On October 16, 2017, Sprint and Comcast Cable Communications, LLC reached resolution of the claims in Sprint's lawsuit against Comcast and, on October 19, 2017, the Kansas court dismissed Sprint's lawsuit. On December 6, 2017, Sprint and Cox Communications, Inc. reached resolution of the claims in Sprint's lawsuit against Cox, and the Delaware court dismissed Sprint's lawsuit against Cox on December 7, 2017.

We believe that Time Warner Cable continues to have strong non-infringement and invalidity defenses and arguments and/or that Sprint's damages claims are inconsistent with prevailing law at trial and/or on appeal. Due to the uncertainty surrounding the litigation process, we are unable to reasonably estimate the ultimate outcome of the Time Warner Cable litigation at this time. Should Sprint prevail in litigation, mediation, or settlement, we, in accordance with our agreements, may have an obligation to indemnify Time Warner Cable for damages, mediation awards, or settlement amounts arising from its use of our products.

On January 15, 2016, Huawei Technologies Co. Ltd. ("Huawei") filed four patent infringement actions against T-Mobile US, Inc. and T-Mobile USA, Inc. (collectively, "T-Mobile") in federal court in the Eastern District of Texas. Huawei alleged that T-Mobile's use of 3GPP standards to implement its 3G and 4G cellular networks infringed 12 patents. Huawei's infringement allegations for some of the patents were based on T-Mobile's use of products provided by us in combination with those of other manufacturers. T-Mobile requested indemnity by Cisco with respect to portions of the network that use our equipment. On December 22, 2017, the Eastern District of Texas court dismissed Huawei's four lawsuits after the parties reached settlement, and T-Mobile's indemnity request was subsequently resolved.

During fiscal 2018, we recorded legal and indemnification settlement charges of \$127 million to product cost of sales in relation to these matters. At this time, we do not anticipate that our obligations regarding the final outcome of the above matters would be material.

In addition, we have entered into indemnification agreements with our officers and directors, and our Amended and Restated Bylaws contain similar indemnification obligations to our agents.

It is not possible to determine the maximum potential amount under these indemnification agreements due to our limited history with prior indemnification claims and the unique facts and circumstances involved in each particular agreement. Historically, payments made by us under these agreements have not had a material effect on our operating results, financial position, or cash flows.

#### **(h) Legal Proceedings**

Brazil Brazilian authorities have investigated our Brazilian subsidiary and certain of our former employees, as well as a Brazilian importer of our products, and its affiliates and employees, relating to alleged evasion of import taxes and alleged improper transactions involving the subsidiary and the importer. Brazilian tax authorities have assessed claims against our Brazilian subsidiary based on a theory of joint liability with the Brazilian importer for import taxes, interest, and penalties. In addition to claims asserted by the Brazilian federal tax authorities in prior fiscal years, tax authorities from the Brazilian state of Sao Paulo have asserted similar claims on the same legal basis in prior fiscal years.

The asserted claims by Brazilian federal tax authorities that remain are for calendar years 2003 through 2007, and the asserted claims by the tax authorities from the state of Sao Paulo are for calendar years 2005 through 2007. The total asserted claims by Brazilian state and federal tax authorities aggregate to \$218 million for the alleged evasion of import and other taxes, \$1.4 billion for interest, and \$1.0 billion for various penalties, all determined using an exchange rate as of July 28, 2018. We have completed a thorough review of the matters and believe the asserted claims against our Brazilian subsidiary are without merit, and we are defending the claims vigorously. While we believe there is no legal basis for the alleged liability, due to the complexities and uncertainty surrounding the judicial process in Brazil and the nature of the claims asserting joint liability with the importer, we are unable to determine the likelihood of an unfavorable outcome against our Brazilian subsidiary and are unable to reasonably estimate a range of loss, if any. We do not expect a final judicial determination for several years.

SRI International On September 4, 2013, SRI International, Inc. ("SRI") asserted patent infringement claims against us in the U.S. District Court for the District of Delaware, accusing our products and services in the area of network intrusion detection of infringing two U.S. patents. SRI sought monetary damages of at least a reasonable royalty and enhanced damages. The trial on these claims began on May 2, 2016 and, on May 12, 2016, the jury returned a verdict finding willful infringement of the asserted patents. The jury awarded SRI damages of \$23.7 million. On May 25, 2017, the Court awarded SRI enhanced damages and attorneys' fees, entered judgment in the new amount of \$57.0 million, and ordered an ongoing royalty of 3.5% through the expiration of the patents in 2018. We have appealed to the United States Court of Appeals for the Federal Circuit on various grounds. We believe we have strong arguments to overturn the jury verdict and/or reduce the damages award. While the ultimate outcome of the case may still result in a loss, we do not expect it to be material.

SSL SSL Services, LLC ("SSL") has asserted claims for patent infringement against us in the U.S. District Court for the Eastern District of Texas. The proceeding was instituted on March 25, 2015. SSL alleges that our AnyConnect products that include Virtual Private Networking functions infringed a U.S. patent owned by SSL. SSL seeks money damages from us. On August 18, 2015, we petitioned the Patent Trial and Appeal Board ("PTAB") of the United States Patent and Trademark Office to review whether

the patent SSL has asserted against us is valid over prior art. On February 23, 2016, a PTAB multi-judge panel found a reasonable likelihood that we would prevail in showing that SSL's patent claims are unpatentable and instituted proceedings. On June 28, 2016, in light of the PTAB's decision to review the patent's validity, the district court issued an order staying the district court case pending the final written decision from the PTAB. On February 22, 2017, following a hearing, the PTAB issued its Final Written Decision that the patent's claims are unpatentable. SSL appealed this decision to the Court of Appeals for the Federal Circuit and, on May 7, 2018, the Federal Circuit summarily affirmed the PTAB's decision of unpatentability.

Straight Path On September 24, 2014, Straight Path IP Group, Inc. ("Straight Path") asserted patent infringement claims against us in the U.S. District Court for the Northern District of California, accusing our 9971 IP Phone, Unified Communications Manager working in conjunction with 9971 IP Phones, and Video Communication Server products of infringement. All of the asserted patents have expired and Straight Path was therefore limited to seeking monetary damages for the alleged past infringement. On November 13, 2017, the Court granted our motion for summary judgment of non-infringement, thereby dismissing Straight Path's claims against us and cancelling a trial which had been set for March 12, 2018. On January 16, 2018, Straight Path appealed to the U.S. Court of Appeal for the Federal Circuit.

DXC Technology On August 21, 2015, Cisco and Cisco Systems Capital Corporation ("Cisco Capital") filed an action in Santa Clara County Superior Court for declaratory judgment and breach of contract against HP Inc. ("HP") regarding a services agreement for management services of a third party's network. HP had prepaid the service agreement through a financing arrangement with Cisco Capital, and had terminated its agreement with us. Pursuant to the terms of the service agreement with HP, we determined the credit HP was entitled to receive under the agreement for certain prepaid amounts. HP disputed our credit calculation and contended that we owe a larger credit to HP than we had calculated. In December 2015, we filed an amended complaint which dropped the breach of contract claim in light of HP's continuing payments to Cisco Capital under the financing arrangement. On January 19, 2016, HP Inc. filed a counterclaim for breach of contract simultaneously with its answer to the amended complaint. DXC Technology Corporation ("DXC") reported that it is the party in interest in this matter pursuant to the Separation and Distribution Agreement between the then Hewlett-Packard Co. and Hewlett Packard Enterprise Company ("HPE") and the subsequent Separation and Distribution Agreement between HPE and DXC. On January 8, 2018, the court continued the trial date from March 12, 2018 to June 11, 2018. The parties entered into a settlement agreement effective June 30, 2018, resolving all of the claims and cross-claims in the case, and on August 1, 2018, the Court dismissed all claims and cross-claims with prejudice. The settlement did not have a material impact on our results of operations.

Arista Networks, Inc. On February 24, 2016, Arista Networks, Inc. ("Arista") filed a complaint against us in the U.S. District Court for the Northern District of California, asserting monopolization claims in violation of Section 2 of the Sherman Act and an unfair competition claim under California Bus. and Prof. Code § 17200. On October 31, 2017, Arista filed an amended complaint for Sherman Act monopolization and § 17200 claims, alleging an anticompetitive scheme comprising our copyright infringement action against Arista (which was based on Arista's copying of our copyright-protected user interfaces) and communications related to that litigation. Arista sought injunctive relief, lost profits, enhanced damages, and restitution. A jury trial was scheduled for August 6, 2018. On August 6, 2018, Cisco and Arista entered into a binding term sheet resolving, except as described below, all of the outstanding litigation between the companies. The terms are as follows: (i) Arista shall pay \$400 million to Cisco; (ii) Cisco will not assert against Arista patents that were included in the litigation as long as Arista continues to implement workarounds it had put in place to certain of those patents; (iii) for three years (subject to earlier termination in some circumstances), any claim against the other party regarding patent infringement for its new products, or new features of existing products, will be resolved by an arbitration process; the process will not apply to claims of copyright infringement, trade secret misappropriation or certain other claims; (iv) for five years, neither party will bring an action against the other for patent or copyright (except for any claims of source code misappropriation) infringement regarding their respective products on the market before August 6, 2018; and (v) certain limited changes shall be implemented by Arista to its user interfaces for operation of its products, and the parties will continue to undertake the appeal of the ruling in U.S. District Court for the Northern District of California regarding copyright infringement, with further limited changes if the case is remanded or reversed. The parties also agreed that for five years neither party would bring an action against the other's contract manufacturers, partners or customers for patent or copyright (excluding claims of source code misappropriation) infringement regarding the other party's products on the market before August 6, 2018. We received payment from Arista of \$400 million on August 20, 2018, which will be reflected in Cisco's first quarter fiscal 2019 results.

Oyster Optics On November 24, 2016, Oyster Optics, LLC ("Oyster") asserted patent infringement claims against us in the U.S. District Court for the Eastern District of Texas. Oyster alleges that certain Cisco ONS 15454 and NCS 2000 line cards infringe U.S. Patent No. 7,620,327 ("the '327 Patent"). Oyster seeks monetary damages. Oyster filed infringement claims based on the '327 Patent against other defendants, including ZTE, Nokia, NEC, Infinera, Huawei, Ciena, Alcatel-Lucent, and Fujitsu, and the court consolidated the cases alleging infringement of the '327 Patent. During the course of the case, defendants ZTE, Nokia, NEC, Fujitsu, Infinera and Huawei reached settlements with Oyster. On August 9, 2018, the court reset the trial for November 5, 2018. While we believe that we have strong non-infringement arguments and that the patent is invalid, if we do not

prevail in the District Court, we believe damages ultimately assessed would not be material. Due to uncertainty surrounding patent litigation processes, we are unable to reasonably estimate the ultimate outcome of this litigation at this time. However, we do not anticipate that any final outcome of the dispute would be material.

In addition, we are subject to legal proceedings, claims, and litigation arising in the ordinary course of business, including intellectual property litigation. While the outcome of these matters is currently not determinable, we do not expect that the ultimate costs to resolve these matters will have a material adverse effect on our consolidated financial position, results of operations, or cash flows.

For additional information regarding intellectual property litigation, see “Part I, Item 1A. Risk Factors-We may be found to infringe on intellectual property rights of others” of this Annual Report on Form 10-K.

### **13. Shareholders’ Equity**

#### **(a) Cash Dividends on Shares of Common Stock**

We declared and paid cash dividends of \$1.24, \$1.10 and \$0.94 per common share, or \$6.0 billion, \$5.5 billion and \$4.8 billion, on our outstanding common stock during fiscal 2018, 2017, and 2016, respectively.

Any future dividends will be subject to the approval of our Board of Directors.

#### **(b) Stock Repurchase Program**

In September 2001, our Board of Directors authorized a stock repurchase program. On February 14, 2018, our Board of Directors authorized a \$25 billion increase to the stock repurchase program. As of July 28, 2018, the remaining authorized amount for stock repurchases under this program, including the additional authorization, is approximately \$19.0 billion, with no termination date.

A summary of the stock repurchase activity under the stock repurchase program, reported based on the trade date, is as follows (in millions, except per-share amounts):

Years Ended	Shares	Weighted-Average Price per Share	Amount
<b>July 28, 2018</b>	<b>432</b>	<b>\$ 40.88</b>	<b>\$ 17,661</b>
July 29, 2017	118	\$ 31.38	\$ 3,706
July 30, 2016	148	\$ 26.45	\$ 3,918

There were \$180 million, \$66 million and \$45 million in stock repurchases pending settlement as of July 28, 2018, July 29, 2017 and July 30, 2016, respectively.

The purchase price for the shares of our stock repurchased is reflected as a reduction to shareholders’ equity. We are required to allocate the purchase price of the repurchased shares as (i) a reduction to retained earnings and (ii) a reduction of common stock and additional paid-in capital.

#### **(c) Restricted Stock Unit Withholdings**

We repurchased approximately 20 million, 20 million and 21 million shares, or \$703 million, \$619 million and \$557 million of common stock in settlement of employee tax withholding obligations due upon the vesting of restricted stock or stock units during fiscal 2018, 2017, and 2016, respectively.

#### **(d) Preferred Stock**

Under the terms of our Articles of Incorporation, the Board of Directors may determine the rights, preferences, and terms of our authorized but unissued shares of preferred stock.

## **14. Employee Benefit Plans**

### **(a) Employee Stock Incentive Plans**

Stock Incentive Plan Program Description As of July 28, 2018, we had one stock incentive plan: the 2005 Stock Incentive Plan (the “2005 Plan”). In addition, we have, in connection with our acquisitions of various companies, assumed the share-based awards granted under stock incentive plans of the acquired companies or issued share-based awards in replacement thereof. Share-based awards are designed to reward employees for their long-term contributions to us and provide incentives for them to remain with Cisco. The number and frequency of share-based awards are based on competitive practices, operating results of Cisco, government regulations, and other factors. Our primary stock incentive plan is summarized as follows:

2005 Plan As of July 28, 2018, the maximum number of shares issuable under the 2005 Plan over its term was 694 million shares, plus shares from certain previous plans that are forfeited or are terminated for any other reason before being exercised or settled. If any awards granted under the 2005 Plan are forfeited or are terminated for any other reason before being exercised or settled, the unexercised or unsettled shares underlying the awards will again be available under the 2005 Plan. In addition, starting November 19, 2013, shares withheld by Cisco from an award other than a stock option or stock appreciation right to satisfy withholding tax liabilities resulting from such award will again be available for issuance, based on the fungible share ratio in effect on the date of grant.

Pursuant to an amendment approved by our shareholders on November 12, 2009, the number of shares available for issuance under the 2005 Plan is reduced by 1.5 shares for each share awarded as a stock grant or a stock unit, and any shares underlying awards outstanding from certain previous plans that expire unexercised at the end of their maximum terms become available for reissuance under the 2005 Plan. The 2005 Plan permits the granting of stock options, restricted stock, and RSUs, the vesting of which may be performance-based or market-based along with the requisite service requirement, and stock appreciation rights to employees (including employee directors and officers), consultants of Cisco and its subsidiaries and affiliates, and non-employee directors of Cisco. Stock options and stock appreciation rights granted under the 2005 Plan have an exercise price of at least 100% of the fair market value of the underlying stock on the grant date. The expiration date for stock options and stock appreciation rights shall be no later than 10 years from the grant date.

The stock options will generally become exercisable for 20% or 25% of the option shares one year from the date of grant and then ratably over the following 48 months or 36 months, respectively. Time-based stock grants and time-based RSUs will generally vest over a four year term. The majority of the performance-based and market-based RSUs vests at the end of the three-year requisite service period or earlier if the award recipient meets certain retirement eligibility conditions. Certain performance-based RSUs that are based on the achievement of financial and/or non-financial operating goals typically vest upon the achievement of milestones (and may require subsequent service periods), with overall vesting of the shares underlying the award ranging from six months to three years. The Compensation and Management Development Committee of our Board of Directors has the discretion to use different vesting schedules. Stock appreciation rights may be awarded in combination with stock options or stock grants, and such awards shall provide that the stock appreciation rights will not be exercisable unless the related stock options or stock grants are forfeited. Stock grants may be awarded in combination with non-statutory stock options, and such awards may provide that the stock grants will be forfeited in the event that the related non-statutory stock options are exercised.

### **(b) Employee Stock Purchase Plan**

We have an Employee Stock Purchase Plan, which includes its subplan named the International Employee Stock Purchase Plan (together, the “Purchase Plan”), under which 621 million shares of our common stock have been reserved for issuance as of July 28, 2018. Eligible employees are offered shares through a 24-month offering period, which consists of four consecutive 6-month purchase periods. Employees may purchase a limited number of shares of our stock at a discount of up to 15% of the lesser of the market value at the beginning of the offering period or the end of each 6-month purchase period. The Purchase Plan is scheduled to terminate on January 3, 2020. We issued 22 million, 23 million, and 25 million shares under the Purchase Plan in fiscal 2018, 2017, and 2016, respectively. As of July 28, 2018, 78 million shares were available for issuance under the Purchase Plan.

**(c) Summary of Share-Based Compensation Expense**

Share-based compensation expense consists primarily of expenses for stock options, stock purchase rights, restricted stock, and RSUs granted to employees. The following table summarizes share-based compensation expense (in millions):

Years Ended	<u>July 28, 2018</u>	<u>July 29, 2017</u>	<u>July 30, 2016</u>
Cost of sales—product .....	\$ 94	\$ 85	\$ 70
Cost of sales—service .....	<u>133</u>	<u>134</u>	<u>142</u>
Share-based compensation expense in cost of sales .....	<u>227</u>	<u>219</u>	<u>212</u>
Research and development .....	538	529	470
Sales and marketing .....	555	542	545
General and administrative .....	246	236	205
Restructuring and other charges .....	33	3	26
Share-based compensation expense in operating expenses.....	<u>1,372</u>	<u>1,310</u>	<u>1,246</u>
Total share-based compensation expense.....	<u>\$ 1,599</u>	<u>\$ 1,529</u>	<u>\$ 1,458</u>
Income tax benefit for share-based compensation.....	<u>\$ 558</u>	<u>\$ 451</u>	<u>\$ 429</u>

As of July 28, 2018, the total compensation cost related to unvested share-based awards not yet recognized was \$3.1 billion, which is expected to be recognized over approximately 2.5 years on a weighted-average basis.

**(d) Share-Based Awards Available for Grant**

A summary of share-based awards available for grant is as follows (in millions):

Years Ended	<u>July 28, 2018</u>	<u>July 29, 2017</u>	<u>July 30, 2016</u>
Balance at beginning of fiscal year .....	272	242	276
Restricted stock, stock units, and other share-based awards granted .....	(70)	(76)	(96)
Share-based awards canceled/forfeited/expired.....	18	78	30
Shares withheld for taxes and not issued .....	25	28	30
Other.....	—	—	2
Balance at end of fiscal year.....	<u>245</u>	<u>272</u>	<u>242</u>

For each share awarded as restricted stock or a restricted stock unit award under the 2005 Plan, 1.5 shares was deducted from the available share-based award balance. For restricted stock units that were awarded with vesting contingent upon the achievement of future financial performance or market-based metrics, the maximum awards that can be achieved upon full vesting of such awards were reflected in the preceding table.

**(e) Restricted Stock and Stock Unit Awards**

A summary of the restricted stock and stock unit activity, which includes time-based and performance-based or market-based RSUs, is as follows (in millions, except per-share amounts):

	Restricted Stock/ Stock Units	Weighted-Average Grant Date Fair Value per Share	Aggregate Fair Value
<b>UNVESTED BALANCE AT JULY 25, 2015 . . . . .</b>	<b>143</b>	<b>\$ 22.08</b>	
Granted . . . . .	62	25.90	
Assumed from acquisitions . . . . .	6	24.58	
Vested . . . . .	(54)	20.68	\$ 1,428
Canceled/forfeited/other . . . . .	(12)	22.91	
<b>UNVESTED BALANCE AT JULY 30, 2016 . . . . .</b>	<b>145</b>	<b>24.26</b>	
Granted . . . . .	50	27.89	
Assumed from acquisitions . . . . .	15	32.21	
Vested . . . . .	(54)	23.14	\$ 1,701
Canceled/forfeited/other . . . . .	(15)	23.56	
<b>UNVESTED BALANCE AT JULY 29, 2017 . . . . .</b>	<b>141</b>	<b>26.94</b>	
Granted . . . . .	46	35.62	
<b>Assumed from acquisitions . . . . .</b>	<b>1</b>	<b>28.26</b>	
Vested . . . . .	(53)	26.02	\$ 1,909
Canceled/forfeited/other . . . . .	(16)	28.37	
<b>UNVESTED BALANCE AT JULY 28, 2018 . . . . .</b>	<b><u>119</u></b>	<b>\$ 30.56</b>	

**(f) Stock Option Awards**

A summary of the stock option activity is as follows (in millions, except per-share amounts):

	STOCK OPTIONS OUTSTANDING	
	Number Outstanding	Weighted-Average Exercise Price per Share
<b>BALANCE AT JULY 25, 2015 . . . . .</b>	<b>103</b>	<b>\$ 28.68</b>
Assumed from acquisitions . . . . .	18	5.17
Exercised . . . . .	(32)	19.22
Canceled/forfeited/expired . . . . .	(16)	30.01
<b>BALANCE AT JULY 30, 2016 . . . . .</b>	<b>73</b>	<b>26.78</b>
Assumed from acquisitions . . . . .	8	4.47
Exercised . . . . .	(14)	12.11
Canceled/forfeited/expired . . . . .	(55)	31.83
<b>BALANCE AT JULY 29, 2017 . . . . .</b>	<b>12</b>	<b>6.15</b>
<b>Assumed from acquisitions . . . . .</b>	<b>3</b>	<b>8.20</b>
<b>Exercised . . . . .</b>	<b>(8)</b>	<b>5.77</b>
<b>Canceled/forfeited/expired . . . . .</b>	<b>(1)</b>	<b>8.75</b>
<b>BALANCE AT JULY 28, 2018 . . . . .</b>	<b><u>6</u></b>	<b>\$ 7.18</b>

The total pretax intrinsic value of stock options exercised during fiscal 2018, 2017, and 2016 was \$257 million, \$283 million, and \$266 million, respectively.

The following table summarizes significant ranges of outstanding and exercisable stock options as of July 28, 2018 (in millions, except years and share prices):

Range of Exercise Prices	STOCK OPTIONS OUTSTANDING				STOCK OPTIONS EXERCISABLE			
	Number Outstanding	Weighted-Average Remaining Contractual Life (in Years)	Weighted-Average Exercise Price per Share	Aggregate Intrinsic Value	Number Exercisable	Weighted-Average Exercise Price per Share	Aggregate Intrinsic Value	
\$0.01 – 35.00 .....	6	5.9	\$ 7.18	\$ 228	4	\$ 6.84	\$ 153	

The aggregate intrinsic value represents the total pretax intrinsic value, based on Cisco's closing stock price of \$42.57 as of July 27, 2018. The total number of in-the-money stock options exercisable as of July 28, 2018 was 4 million. As of July 29, 2017, 6 million outstanding stock options were exercisable, and the weighted-average exercise price was \$5.61.

#### (g) Valuation of Employee Share-Based Awards

Time-based restricted stock units and PRSUs that are based on our financial performance metrics or non-financial operating goals are valued using the market value of our common stock on the date of grant, discounted for the present value of expected dividends. On the date of grant, we estimated the fair value of the total shareholder return (TSR) component of the PRSUs using a Monte Carlo simulation model. The assumptions for the valuation of time-based RSUs and PRSUs are summarized as follows:

Years Ended	RESTRICTED STOCK UNITS		
	July 28, 2018	July 29, 2017	July 30, 2016
Number of shares granted (in millions) .....	43	43	57
Grant date fair value per share .....	\$ 35.81	\$ 28.38	\$ 26.01
Weighted-average assumptions/inputs:			
Expected dividend yield .....	3.2%	3.5%	3.2%
Range of risk-free interest rates .....	0.0% – 2.7%	0.0% – 1.5%	0.0% – 1.2%
PERFORMANCE BASED RESTRICTED STOCK UNITS			
Years Ended	PERFORMANCE BASED RESTRICTED STOCK UNITS		
	July 28, 2018	July 29, 2017	July 30, 2016
Number of shares granted (in millions) .....	3	7	5
Grant date fair value per share .....	\$ 32.69	\$ 28.94	\$ 24.70
Weighted-average assumptions/inputs:			
Expected dividend yield .....	3.5%	3.4%	3.1%
Range of risk-free interest rates .....	1.0% – 2.7%	0.1% – 1.5%	0.0% – 1.2%
Range of expected volatilities for index .....	12.5% – 82.8%	16.7% – 46.8%	15.3% – 54.3%

The PRSUs granted during the fiscal years presented are contingent on the achievement of our financial performance metrics, our comparative market-based returns, or the achievement of financial and non-financial operating goals. For the awards based on financial performance metrics or comparative market-based returns, generally 50% of the PRSUs are earned based on the average of annual operating cash flow and earnings per share goals established at the beginning of each fiscal year over a three-year performance period. Generally, the remaining 50% of the PRSUs are earned based on our TSR measured against the benchmark TSR of a peer group over the same period. Each PRSU recipient could vest in 0% to 150% of the target shares granted contingent on the achievement of our financial performance metrics or our comparative market-based returns, and 0% to 100% of the target shares granted contingent on the achievement of non-financial operating goals.

The assumptions for the valuation of employee stock purchase rights are summarized as follows:

<u>Years Ended</u>	EMPLOYEE STOCK PURCHASE RIGHTS		
	<u>July 28, 2018</u>	<u>July 29, 2017</u>	<u>July 30, 2016</u>
<b>Weighted-average assumptions:</b>			
Expected volatility .....	<b>22.1%</b>	24.6%	23.9%
Risk-free interest rate.....	<b>1.3%</b>	0.7%	0.4%
Expected dividend .....	<b>3.1%</b>	3.2%	3.1%
Expected life (in years) .....	<b>1.3</b>	1.3	1.3
Weighted-average estimated grant date fair value per share .....	\$ <b>7.48</b>	\$ 6.52	\$ 5.73

The valuation of employee stock purchase rights and the related assumptions are for the employee stock purchases made during the respective fiscal years.

We used third-party analyses to assist in developing the assumptions used in our Black-Scholes model. We are responsible for determining the assumptions used in estimating the fair value of our share-based payment awards.

We used the implied volatility for traded options (with contract terms corresponding to the expected life of the employee stock purchase rights) on our stock as the expected volatility assumption required in the Black-Scholes model. The implied volatility is more representative of future stock price trends than historical volatility. The risk-free interest rate assumption is based upon observed interest rates appropriate for the term of our employee stock purchase rights. The dividend yield assumption is based on the history and expectation of dividend payouts at the grant date.

#### **(h) Employee 401(k) Plans**

We sponsor the Cisco Systems, Inc. 401(k) Plan (the “Plan”) to provide retirement benefits for our employees. As allowed under Section 401(k) of the Internal Revenue Code, the Plan provides for tax-deferred salary contributions and after-tax contributions for eligible employees. The Plan allows employees to contribute up to 75% of their annual eligible earnings to the Plan on a pretax and after-tax basis, including Roth contributions. Employee contributions are limited to a maximum annual amount as set periodically by the Internal Revenue Code. We match pretax and Roth employee contributions up to 100% of the first 4.5% of eligible earnings that are contributed by employees. Therefore, the maximum matching contribution that we may allocate to each participant’s account will not exceed \$12,375 for the 2018 calendar year due to the \$275,000 annual limit on eligible earnings imposed by the Internal Revenue Code. All matching contributions vest immediately. Our matching contributions to the Plan totaled \$269 million, \$265 million, and \$262 million in fiscal 2018, 2017, and 2016, respectively.

The Plan allows employees who meet the age requirements and reach the Plan contribution limits to make catch-up contributions (pretax or Roth) not to exceed the lesser of 75% of their annual eligible earnings or the limit set forth in the Internal Revenue Code. Catch-up contributions are not eligible for matching contributions. In addition, the Plan provides for discretionary profit-sharing contributions as determined by the Board of Directors. Such contributions to the Plan are allocated among eligible participants in the proportion of their salaries to the total salaries of all participants. There were no discretionary profit-sharing contributions made in fiscal 2018, 2017, and 2016.

We also sponsor other 401(k) plans as a result of acquisitions of other companies. Our contributions to these plans were not material to Cisco on either an individual or aggregate basis for any of the fiscal years presented.

#### **(i) Deferred Compensation Plans**

The Cisco Systems, Inc. Deferred Compensation Plan (the “Deferred Compensation Plan”), a nonqualified deferred compensation plan, became effective in 2007. As required by applicable law, participation in the Deferred Compensation Plan is limited to a select group of our management employees. Under the Deferred Compensation Plan, which is an unfunded and unsecured deferred compensation arrangement, a participant may elect to defer base salary, bonus, and/or commissions, pursuant to such rules as may be established by Cisco, up to the maximum percentages for each deferral election as described in the plan. We may also, at our discretion, make a matching contribution to the employee under the Deferred Compensation Plan. A matching contribution equal to 4.5% of eligible compensation in excess of the Internal Revenue Code limit for qualified plans for calendar year 2018 that is deferred by participants under the Deferred Compensation Plan (with a \$1.5 million cap on eligible compensation) will be made to eligible participants’ accounts at the end of calendar year 2018. The total deferred compensation liability under the Deferred Compensation Plan, together with deferred compensation plans assumed from acquired companies, was approximately \$651 million and \$622 million as of July 28, 2018 and July 29, 2017, respectively, and was recorded primarily in other long-term liabilities.

## 15. Comprehensive Income (Loss)

The components of AOCI, net of tax, and the other comprehensive income (loss), excluding noncontrolling interest, are summarized as follows (in millions):

	Net Unrealized Gains (Losses) on Available-for-Sale Investments	Net Unrealized Gains (Losses) Cash Flow Hedging Instruments	Cumulative Translation Adjustment and Actuarial Gains and Losses	Accumulated Other Comprehensive Income (Loss)
<b>BALANCE AT JULY 25, 2015</b>	\$ 310	\$ (16)	\$ (233)	\$ 61
Other comprehensive income (loss) before reclassifications attributable to Cisco Systems, Inc.	151	(66)	(399)	(314)
(Gains) losses reclassified out of AOCI	1	20	(6)	15
Tax benefit (expense)	(49)	3	(42)	(88)
Total change for the period	103	(43)	(447)	(387)
<b>BALANCE AT JULY 30, 2016</b>	413	(59)	(680)	(326)
Other comprehensive income (loss) before reclassifications attributable to Cisco Systems, Inc.	(164)	22	318	176
(Gains) losses reclassified out of AOCI	87	79	16	182
Tax benefit (expense)	37	(10)	(13)	14
Total change for the period	(40)	91	321	372
<b>BALANCE AT JULY 29, 2017</b>	373	32	(359)	46
Other comprehensive income (loss) before reclassifications attributable to Cisco Systems, Inc.	(543)	21	(159)	(681)
(Gains) losses reclassified out of AOCI	(287)	(68)	7	(348)
Tax benefit (expense)	93	4	(8)	89
Total change for the period	(737)	(43)	(160)	(940)
Effect of adoption of accounting standard	54	—	(9)	45
<b>BALANCE AT JULY 28, 2018</b>	<b>\$ (310)</b>	<b>\$ (11)</b>	<b>\$ (528)</b>	<b>\$ (849)</b>

The net gains (losses) reclassified out of AOCI into the Consolidated Statements of Operations, with line item location, during each period were as follows (in millions):

Comprehensive Income Components	July 28, 2018	July 29, 2017	July 30, 2016	Line Item in Statements of Operations	
				Income Before Taxes	
Net unrealized gains and losses on available-for-sale investments	\$ 287	\$ (87)	\$ (1)	Other income (loss), net	
Net unrealized gains and losses on cash flow hedging instruments					
Foreign currency derivatives	52	(59)	(15)	Operating expenses	
Foreign currency derivatives	16	(20)	(5)	Cost of sales—service	
	68	(79)	(20)		
Cumulative translation adjustment and actuarial gains and losses	(7)	(16)	6	Operating expenses	
Total amounts reclassified out of AOCI	<b>\$ 348</b>	<b>\$ (182)</b>	<b>\$ (15)</b>		

## 16. Income Taxes

### (a) Provision for Income Taxes

The provision for income taxes consists of the following (in millions):

<u>Years Ended</u>	<u>July 28, 2018</u>	<u>July 29, 2017</u>	<u>July 30, 2016</u>
<b>Federal:</b>			
Current.....	\$ 9,900	\$ 1,300	\$ 865
Deferred.....	1,156	(42)	(93)
	<b>11,056</b>	<b>1,258</b>	<b>772</b>
<b>State:</b>			
Current.....	340	86	78
Deferred.....	(232)	56	13
	<b>108</b>	<b>142</b>	<b>91</b>
<b>Foreign:</b>			
Current.....	1,789	1,416	1,432
Deferred.....	(24)	(138)	(114)
	<b>1,765</b>	<b>1,278</b>	<b>1,318</b>
Total .....	<b>\$ 12,929</b>	<b>\$ 2,678</b>	<b>\$ 2,181</b>

Income before provision for income taxes consists of the following (in millions):

<u>Years Ended</u>	<u>July 28, 2018</u>	<u>July 29, 2017</u>	<u>July 30, 2016</u>
United States .....	\$ 3,765	\$ 2,393	\$ 2,907
International.....	9,274	9,894	10,013
Total .....	<b>\$ 13,039</b>	<b>\$ 12,287</b>	<b>\$ 12,920</b>

The items accounting for the difference between income taxes computed at the federal statutory rate and the provision for income taxes consist of the following:

<u>Years Ended</u>	<u>July 28, 2018</u>	<u>July 29, 2017</u>	<u>July 30, 2016</u>
Federal statutory rate.....	<b>27.0%</b>	35.0%	35.0%
<b>Effect of:</b>			
State taxes, net of federal tax benefit.....	0.6	1.1	0.5
Foreign income at other than U.S. rates.....	(5.2)	(13.4)	(14.5)
Tax credits .....	(2.5)	(1.2)	(1.7)
Domestic manufacturing deduction .....	(0.5)	(0.4)	(0.6)
Stock-based compensation.....	(0.1)	1.4	1.4
Tax audit settlement.....	—	—	(2.8)
Impact of the Tax Act.....	<b>80.1</b>	—	—
Other, net .....	(0.2)	(0.7)	(0.4)
Total .....	<b>99.2%</b>	<b>21.8%</b>	<b>16.9%</b>

On December 22, 2017, the Tax Act was enacted. The Tax Act significantly revises the U.S. corporate income tax by, among other things, lowering the statutory corporate income tax rate ("federal tax rate") from 35% to 21% effective January 1, 2018, implementing a modified territorial tax system, and imposing a mandatory one-time transition tax on accumulated earnings of foreign subsidiaries. As a fiscal-year taxpayer, certain provisions of the Tax Act impact Cisco in fiscal 2018, including the change in the federal tax rate and the one-time transition tax, while other provisions will be effective at the beginning of fiscal 2019, including the implementation of a modified territorial tax system and other changes to how foreign earnings are subject to U.S. tax, and elimination of the domestic manufacturing deduction.

As a result of the decrease in the federal tax rate from 35% to 21% effective January 1, 2018, we have computed our income tax expense for the July 28, 2018 fiscal year using a blended federal tax rate of 27%. The 21% federal tax rate will apply to our fiscal year ending July 27, 2019 and each year thereafter. We must remeasure our deferred tax assets and liabilities ("DTA") using the federal tax rate that will apply when the related temporary differences are expected to reverse.

As of December 31, 2017, we had approximately \$76 billion in undistributed earnings for certain foreign subsidiaries. These undistributed earnings were subject to the U.S. mandatory one-time transition tax and are eligible to be repatriated to the U.S. without additional U.S. tax under the Tax Act. We have historically asserted our intention to indefinitely reinvest foreign earnings in certain foreign subsidiaries. We have reevaluated our historic assertion as a result of enactment of the Tax Act and no longer consider these earnings to be indefinitely reinvested in our foreign subsidiaries. As a result of this change in assertion, we recorded a \$1.2 billion tax expense for foreign withholding tax in the second quarter of fiscal 2018. In fiscal 2018, we repatriated \$70 billion of foreign subsidiary earnings to the U.S. (in the form of cash, cash equivalents, or investments), and paid foreign withholding tax of \$1.2 billion.

In the fourth quarter of fiscal 2018, we recorded adjustments to the provisional amounts originally recorded in the second quarter of fiscal 2018 related to the U.S. transition tax on accumulated earnings of foreign subsidiaries and re-measurement of net DTA. These adjustments include an \$863 million benefit to the U.S. transition tax provisional amount related to the U.S. taxation of deemed foreign dividends in the transition fiscal year. This benefit may be reduced or eliminated in future legislation. If such legislation is enacted, we will record the impact of the legislation in the quarter of enactment.

During fiscal 2018, we recorded a provisional tax expense of \$10.4 billion related to the Tax Act, comprised of \$8.1 billion of U.S. transition tax, \$1.2 billion of foreign withholding tax (discussed above), and \$1.1 billion re-measurement of net DTA. We plan to pay the transition tax in installments over eight years in accordance with the Tax Act. The \$1.2 billion foreign withholding tax was paid in February 2018.

In December 2017, the Securities and Exchange Commission staff issued Staff Accounting Bulletin No. 118, which addresses how a company recognizes provisional estimates when a company does not have the necessary information available, prepared or analyzed (including computations) in reasonable detail to complete its accounting for the effect of the changes in the Tax Act. The measurement period ends when a company has obtained, prepared, and analyzed the information necessary to finalize its accounting, but cannot extend beyond one year. The final impact of the Tax Act may differ from the above provisional estimates due to changes in interpretations of the Tax Act, any legislative action to address questions that arise because of the Tax Act, by changes in accounting standard for income taxes and related interpretations in response to the Tax Act, and any updates or changes to estimates used in the provisional amounts. We have determined that the \$8.1 billion of tax expense for the U.S. transition tax on accumulated earnings of foreign subsidiaries, the \$1.2 billion of foreign withholding tax, and the \$1.1 billion of tax expense for DTA re-measurement were each provisional amounts and reasonable estimates for fiscal 2018. Estimates used in the provisional amounts include: the anticipated reversal pattern of the gross DTAs; and earnings, cash positions, foreign taxes and withholding taxes attributable to foreign subsidiaries.

During fiscal 2016, the Internal Revenue Service (IRS) and Cisco settled all outstanding items related to the audit of our federal income tax returns for the fiscal years ended July 26, 2008 through July 31, 2010. As a result of the settlement, we recognized a net benefit to the provision for income taxes of \$367 million, which included a reduction of interest expense of \$21 million. In addition, the Protecting Americans from Tax Hikes Act of 2015 reinstated the U.S. federal R&D tax credit permanently. As a result, the tax provision in fiscal 2016 included a tax benefit of \$226 million related to the U.S. federal R&D tax credit, of which \$81 million was attributable to fiscal 2015.

Foreign taxes associated with the repatriation of earnings of foreign subsidiaries were not provided for on a cumulative total of \$77 million of undistributed earnings for certain foreign subsidiaries as of the end of fiscal 2018. We intend to reinvest these earnings indefinitely in such foreign subsidiaries. If these earnings were distributed in the form of dividends or otherwise, or if the shares of the relevant foreign subsidiaries were sold or otherwise transferred, we would be subject to additional foreign taxes. The amount of unrecognized deferred income tax liability related to these earnings is approximately \$15 million.

As a result of certain employment and capital investment actions, our income in certain foreign countries is subject to reduced tax rates. A portion of these incentives expired at the end of fiscal 2015. The majority of the remaining tax incentives are reasonably expected to expire at the end of fiscal 2019. The gross income tax benefit attributable to tax incentives was estimated to be \$0.9 billion (\$0.19 per diluted share) in fiscal 2018. As of the end of fiscal 2017 and 2016, the gross income tax benefits attributable to tax incentives were estimated to be \$1.3 billion and \$1.2 billion (\$0.25 and \$0.23 per diluted share) for the respective years. The gross income tax benefits were partially offset by accruals of U.S. income taxes on foreign earnings.

### Unrecognized Tax Benefits

The aggregate changes in the balance of gross unrecognized tax benefits were as follows (in millions):

Years Ended	<u>July 28, 2018</u>	July 29, 2017	July 30, 2016
Beginning balance . . . . .	\$ 1,973	\$ 1,627	\$ 2,029
Additions based on tax positions related to the current year . . . . .	251	336	255
Additions for tax positions of prior years . . . . .	84	180	116
Reductions for tax positions of prior years . . . . .	(129)	(78)	(457)
Settlements . . . . .	(124)	(43)	(241)
Lapse of statute of limitations . . . . .	(55)	(49)	(75)
Ending balance . . . . .	<u>\$ 2,000</u>	<u>\$ 1,973</u>	<u>\$ 1,627</u>

As a result of the IRS tax settlement related to the federal income tax returns for the fiscal years ended July 26, 2008 through July 31, 2010, the amount of gross unrecognized tax benefits in fiscal 2016 was reduced by approximately \$563 million. We also reduced the amount of accrued interest by \$63 million.

As of July 28, 2018, \$1.7 billion of the unrecognized tax benefits would affect the effective tax rate if realized. During fiscal 2018, we recognized \$10 million of net interest expense and reduced penalties by less than \$1 million. During fiscal 2017, we recognized \$26 million of net interest expense and a \$4 million reduction in penalties. During fiscal 2016, we recognized a \$55 million reduction in net interest expense and a \$40 million reduction in penalties. Our total accrual for interest and penalties was \$180 million, \$186 million, and \$154 million as of the end of fiscal 2018, 2017, and 2016, respectively. We are no longer subject to U.S. federal income tax audit for returns covering tax years through fiscal 2010. We are no longer subject to foreign or state income tax audits for returns covering tax years through fiscal 1999, and fiscal 2008, respectively.

We regularly engage in discussions and negotiations with tax authorities regarding tax matters in various jurisdictions. We believe it is reasonably possible that certain federal, foreign, and state tax matters may be concluded in the next 12 months. Specific positions that may be resolved include issues involving transfer pricing and various other matters. We estimate that the unrecognized tax benefits at July 28, 2018 could be reduced by approximately \$300 million in the next 12 months.

### **(b) Deferred Tax Assets and Liabilities**

The following table presents the breakdown for net deferred tax assets (in millions):

	<u>July 28, 2018</u>	July 29, 2017
Deferred tax assets. . . . .	\$ 3,219	\$ 4,239
Deferred tax liabilities. . . . .	(141)	(271)
Total net deferred tax assets. . . . .	<u>\$ 3,078</u>	<u>\$ 3,968</u>

The following table presents the components of the deferred tax assets and liabilities (in millions):

	<u>July 28, 2018</u>	<u>July 29, 2017</u>
<b>ASSETS</b>		
Allowance for doubtful accounts and returns . . . . .	\$ 285	\$ 443
Sales-type and direct-financing leases . . . . .	171	277
Inventory write-downs and capitalization . . . . .	289	446
Investment provisions . . . . .	54	171
IPR&D, goodwill, and purchased intangible assets . . . . .	63	125
Deferred revenue . . . . .	1,584	2,057
Credits and net operating loss carryforwards . . . . .	1,087	976
Share-based compensation expense . . . . .	190	273
Accrued compensation . . . . .	370	504
Other . . . . .	408	559
Gross deferred tax assets . . . . .	<u>4,501</u>	<u>5,831</u>
Valuation allowance . . . . .	<u>(374)</u>	<u>(244)</u>
Total deferred tax assets . . . . .	<u>4,127</u>	<u>5,587</u>
<b>LIABILITIES</b>		
Purchased intangible assets . . . . .	(753)	(1,037)
Depreciation . . . . .	(118)	(340)
Unrealized gains on investments . . . . .	(33)	(203)
Other . . . . .	(145)	(39)
Total deferred tax liabilities . . . . .	<u>(1,049)</u>	<u>(1,619)</u>
Total net deferred tax assets . . . . .	<u>\$ 3,078</u>	<u>\$ 3,968</u>

As of July 28, 2018, our federal, state, and foreign net operating loss carryforwards for income tax purposes were \$703 million, \$891 million, and \$808 million, respectively. A significant amount of the net operating loss carryforwards relates to acquisitions and, as a result, is limited in the amount that can be recognized in any one year. If not utilized, the federal, state and foreign net operating loss carryforwards will begin to expire in fiscal 2019. We have provided a valuation allowance of \$125 million for deferred tax assets related to foreign net operating losses that are not expected to be realized.

As of July 28, 2018, our federal, state, and foreign tax credit carryforwards for income tax purposes were approximately \$47 million, \$1.0 billion, and \$5 million, respectively. The federal tax credit carryforwards will begin to expire in fiscal 2019. The majority of state and foreign tax credits can be carried forward indefinitely. We have provided a valuation allowance of \$249 million for deferred tax assets related to state and foreign tax credits that are not expected to be realized.

## 17. Segment Information and Major Customers

### (a) Revenue and Gross Margin by Segment

We conduct business globally and are primarily managed on a geographic basis consisting of three segments: the Americas, EMEA, and APJC. Our management makes financial decisions and allocates resources based on the information it receives from our internal management system. Sales are attributed to a segment based on the ordering location of the customer. We do not allocate research and development, sales and marketing, or general and administrative expenses to our segments in this internal management system because management does not include the information in our measurement of the performance of the operating segments. In addition, we do not allocate amortization and impairment of acquisition-related intangible assets, share-based compensation expense, significant litigation settlements and other contingencies, charges related to asset impairments and restructurings, and certain other charges to the gross margin for each segment because management does not include this information in our measurement of the performance of the operating segments.

Summarized financial information by segment for fiscal 2018, 2017, and 2016, based on our internal management system and as utilized by our Chief Operating Decision Maker (“CODM”), is as follows (in millions):

Years Ended	<u>July 28, 2018</u>	<u>July 29, 2017</u>	<u>July 30, 2016</u>
Revenue:			
Americas .....	\$ <b>29,070</b>	\$ 28,351	\$ 29,392
EMEA .....	<b>12,425</b>	12,004	12,302
APJC .....	<b>7,834</b>	7,650	7,553
Total .....	<b>\$ 49,330</b>	\$ 48,005	\$ 49,247
Gross margin:			
Americas .....	\$ <b>18,792</b>	\$ 18,284	\$ 18,986
EMEA .....	<b>7,945</b>	7,855	7,998
APJC .....	<b>4,726</b>	4,741	4,620
Segment total .....	<b>31,463</b>	30,880	31,604
Unallocated corporate items .....	<b>(857)</b>	(656)	(644)
Total .....	<b>\$ 30,606</b>	\$ 30,224	\$ 30,960

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

Revenue in the United States was \$25.5 billion, \$25.0 billion, and \$25.9 billion for fiscal 2018, 2017, and 2016, respectively.

#### **(b) Revenue for Groups of Similar Products and Services**

We design, manufacture, and sell IP-based networking and other products related to the communications and IT industry and provide services associated with these products and their use. Effective in the first quarter of fiscal 2018, we began reporting our product and service revenue in the following five categories: Infrastructure Platforms, Applications, Security, Other Products, and Services. The change better aligns our product categories with our evolving business model. Prior period amounts have been reclassified to conform to the current period's presentation.

The following table presents revenue for groups of similar products and services (in millions):

Years Ended	<u>July 28, 2018</u>	<u>July 29, 2017</u>	<u>July 30, 2016</u>
Revenue:			
Infrastructure Platforms .....	\$ <b>28,270</b>	\$ 27,779	\$ 28,851
Applications .....	<b>5,035</b>	4,568	4,438
Security .....	<b>2,353</b>	2,153	1,969
Other Products <sup>(1)</sup> .....	<b>1,050</b>	1,205	1,996
Total Product .....	<b>36,709</b>	35,705	37,254
Services .....	<b>12,621</b>	12,300	11,993
Total .....	<b>\$ 49,330</b>	\$ 48,005	\$ 49,247

<sup>(1)</sup> During the second quarter of fiscal 2016, we completed the sale of our SP Video CPE Business. SP Video CPE Business revenue was \$504 million for fiscal 2016.

#### **(c) Additional Segment Information**

The majority of our assets as of July 28, 2018 and July 29, 2017 were attributable to our U.S. operations. In fiscal 2018, 2017, and 2016, no single customer accounted for 10% or more of revenue.

Property and equipment information is based on the physical location of the assets. The following table presents property and equipment information for geographic areas (in millions):

	<u>July 28, 2018</u>	<u>July 29, 2017</u>	<u>July 30, 2016</u>
Property and equipment, net:			
United States .....	\$ <b>2,487</b>	\$ 2,711	\$ 2,822
International .....	<b>519</b>	611	684
Total .....	<b>\$ 3,006</b>	\$ 3,322	\$ 3,506

## 18. Net Income per Share

The following table presents the calculation of basic and diluted net income per share (in millions, except per-share amounts):

Years Ended	<u>July 28, 2018</u>	<u>July 29, 2017</u>	<u>July 30, 2016</u>
Net income .....	<u>\$ 110</u>	<u>\$ 9,609</u>	<u>\$ 10,739</u>
Weighted-average shares—basic .....	<u>4,837</u>	<u>5,010</u>	<u>5,053</u>
Effect of dilutive potential common shares .....	<u>44</u>	<u>39</u>	<u>35</u>
Weighted-average shares—diluted.....	<u>4,881</u>	<u>5,049</u>	<u>5,088</u>
Net income per share—basic .....	<u>\$ 0.02</u>	<u>\$ 1.92</u>	<u>\$ 2.13</u>
Net income per share—diluted.....	<u>\$ 0.02</u>	<u>\$ 1.90</u>	<u>\$ 2.11</u>
Antidilutive employee share-based awards, excluded .....	<u>61</u>	<u>136</u>	<u>148</u>

Employee equity share options, unvested shares, and similar equity instruments granted and assumed by Cisco are treated as potential common shares outstanding in computing diluted earnings per share. Diluted shares outstanding include the dilutive effect of in-the-money options, unvested restricted stock, and restricted stock units. The dilutive effect of such equity awards is calculated based on the average share price for each fiscal period using the treasury stock method. Under the treasury stock method, the amount the employee must pay for exercising stock options and the amount of compensation cost for future service that has not yet recognized are collectively assumed to be used to repurchase shares.

## **Supplementary Financial Data (Unaudited)**

(in millions, except per-share amounts)

<u>Quarters Ended</u>	<u>July 28, 2018 <sup>(1)</sup></u>	<u>April 28, 2018</u>	<u>January 27, 2018 <sup>(2)</sup></u>	<u>October 28, 2017</u>
<b>Revenue</b> . . . . .	\$ 12,844	\$ 12,463	\$ 11,887	\$ 12,136
<b>Gross margin</b> . . . . .	\$ 7,922	\$ 7,759	\$ 7,498	\$ 7,427
<b>Operating income</b> . . . . .	\$ 3,346	\$ 3,134	\$ 3,073	\$ 2,756
<b>Net income (loss)</b> . . . . .	\$ 3,803	\$ 2,691	\$ (8,778)	\$ 2,394
<b>Net income (loss) per share - basic</b> . . . . .	\$ 0.81	\$ 0.56	\$ (1.78)	\$ 0.48
<b>Net income (loss) per share - diluted</b> . . . . .	\$ 0.81	\$ 0.56	\$ (1.78)	\$ 0.48
<b>Cash dividends declared per common share</b> . . . . .	\$ 0.33	\$ 0.33	\$ 0.29	\$ 0.29
<b>Cash and cash equivalents and investments</b> . . . . .	\$ 46,548	\$ 54,431	\$ 73,683	\$ 71,588

<u>Quarters Ended</u>	<u>July 29, 2017</u>	<u>April 29, 2017</u>	<u>January 28, 2017</u>	<u>October 29, 2016</u>
<b>Revenue</b> . . . . .	\$ 12,133	\$ 11,940	\$ 11,580	\$ 12,352
<b>Gross margin</b> . . . . .	\$ 7,546	\$ 7,518	\$ 7,276	\$ 7,884
<b>Operating income</b> . . . . .	\$ 3,034	\$ 3,169	\$ 2,893	\$ 2,877
<b>Net income</b> . . . . .	\$ 2,424	\$ 2,515	\$ 2,348	\$ 2,322
<b>Net income per share - basic</b> . . . . .	\$ 0.49	\$ 0.50	\$ 0.47	\$ 0.46
<b>Net income per share - diluted</b> . . . . .	\$ 0.48	\$ 0.50	\$ 0.47	\$ 0.46
<b>Cash dividends declared per common share</b> . . . . .	\$ 0.29	\$ 0.29	\$ 0.26	\$ 0.26
<b>Cash and cash equivalents and investments</b> . . . . .	\$ 70,492	\$ 67,974	\$ 71,845	\$ 70,968

<sup>(1)</sup> In the fourth quarter of fiscal 2018, we recorded adjustments to the provisional amounts related to the U.S. transition tax on accumulated earnings of foreign subsidiaries and re-measurement of net deferred tax assets. These adjustments included an \$863 million benefit to the U.S. transition tax provisional amount related to the U.S. taxation of deemed foreign dividends after the date of enactment in the transition fiscal year.

<sup>(2)</sup> In the second quarter of fiscal 2018, we recorded a provisional tax expense of \$11.1 billion related to the Tax Act, comprised of \$9.0 billion of U.S. transition tax, \$1.2 billion of foreign withholding tax, and \$0.9 billion re-measurement of net DTA.

## **Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosures**

None.

## **Item 9A. Controls and Procedures**

### **Evaluation of Disclosure Controls and Procedures**

Based on our management's evaluation (with the participation of our principal executive officer and principal financial officer), as of the end of the period covered by this report, our principal executive officer and principal financial officer have concluded that our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended, (the "Exchange Act")) are effective to ensure that information required to be disclosed by us in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms and is accumulated and communicated to our management, including our principal executive officer and principal financial officer, as appropriate to allow timely decisions regarding required disclosure.

## **Internal Control over Financial Reporting**

Management's report on our internal control over financial reporting and the report of our independent registered public accounting firm on our internal control over financial reporting are set forth, respectively, on page 62 under the caption "Management's Report on Internal Control Over Financial Reporting" and on page 61 of this report.

There was no change in our internal control over financial reporting during our fourth quarter of fiscal 2018 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

## **Item 9B. Other Information**

None.

## PART III

### **Item 10. Directors, Executive Officers and Corporate Governance**

The information required by this item relating to our directors and nominees is included under the captions “Board of Directors - Proposal No. 1 —Election of Directors,” “Board of Directors —Proposal No. 1 —Business Experience and Qualifications of Nominees,” and “Board of Directors —Proposal No. 1—Board Meetings and Committees —Nomination and Governance Committee” in our Proxy Statement related to the 2018 Annual Meeting of Shareholders and is incorporated herein by reference.

The information required by this item regarding our Audit Committee is included under the caption “Board of Directors —Proposal No. 1 —Board Meetings and Committees” and “Audit Committee Matters” in our Proxy Statement related to the 2018 Annual Meeting of Shareholders and is incorporated herein by reference.

Pursuant to General Instruction G(3) of Form 10-K, the information required by this item relating to our executive officers is included under the caption “Executive Officers of the Registrant” in Part I of this report.

The information required by this item regarding compliance with Section 16(a) of the Securities Act of 1934 is included under the caption “Compensation Committee Matters —Ownership of Securities —Section 16(a) Beneficial Ownership Reporting Compliance” in our Proxy Statement related to the 2018 Annual Meeting of Shareholders and is incorporated herein by reference.

We have adopted a code of ethics that applies to our principal executive officer and all members of our finance department, including the principal financial officer and principal accounting officer. This code of ethics is entitled “Special Ethics Obligations for Employees with Financial Reporting Responsibilities: Financial Officer Code of Ethics” and is posted on our website. The Internet address for our website is [www.cisco.com](http://www.cisco.com), and this code of ethics may be found from our main webpage by clicking first on “About Cisco,” then on “All Investor Relations,” then on “Corporate Governance,” and finally on “Financial Officer Code of Ethics”.

We intend to satisfy any disclosure requirement under Item 5.05 of Form 8-K regarding an amendment to, or waiver from, a provision of this code of ethics by posting such information on our website, on the webpage found by clicking through to “Financial Officer Code of Ethics” as specified above.

### **Item 11. Executive Compensation**

The information required by this item relating to executive compensation is included under the captions “Compensation Committee Matters — Proposal No. 3 — Advisory Vote to Approve Executive Compensation,” “Compensation Committee Matters —Compensation Discussion and Analysis,” “Compensation Committee Matters —Compensation Committee Report,” “Compensation Committee Matters —Compensation Committee Interlocks and Insider Participation,” “Compensation Committee Matters —Fiscal 2018 Compensation Tables —Summary Compensation Table,” “—Grants of Plan-Based Awards — Fiscal 2018” and “—CEO Pay Ratio” in our Proxy Statement related to the 2018 Annual Meeting of Shareholders and is incorporated herein by reference.

### **Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters**

The information required by this item relating to security ownership of certain beneficial owners and management is included under the caption “Compensation Committee Matters —Ownership of Securities,” and the information required by this item relating to securities authorized for issuance under equity compensation plans is included under the caption “ Compensation Committee Matters —Proposal No. 2 —Approval of Amendment and Restatement of the Employee Stock Purchase Plan —Equity Compensation Plan Information,” in each case in our Proxy Statement related to the 2018 Annual Meeting of Shareholders, and is incorporated herein by reference.

### **Item 13. Certain Relationships and Related Transactions, and Director Independence**

The information required by this item relating to review, approval or ratification of transactions with related persons is included under the caption “Audit Committee Matters —Certain Relationships and Transactions with Related Persons,” and the information required by this item relating to director independence is included under the caption “Board of Directors —Proposal No. 1 —Election of Directors —Independent Directors,” in each case in our Proxy Statement related to the 2018 Annual Meeting of Shareholders, and is incorporated herein by reference.

**Item 14. Principal Accountant Fees and Services**

The information required by this item is included under the captions “Audit Committee Matters —Proposal No. 4 — Ratification of Independent Registered Public Accounting Firm-Principal Accountant Fees and Services” and “Audit Committee Matters —Proposal No. 4 — Policy on Audit Committee Pre-Approval of Audit and Permissible Non-Audit Services of Independent Registered Public Accounting Firm” in our Proxy Statement related to the 2018 Annual Meeting of Shareholders, and is incorporated herein by reference.

**PART IV****Item 15. Exhibits and Financial Statement Schedules**(a) 1. **Financial Statements**

See the “Index to Consolidated Financial Statements” on page 60 of this report.

2. **Financial Statement Schedule**

See “Schedule II—Valuation and Qualifying Accounts” (below) within Item 15 of this report.

3. **Exhibits**

See the “Index to Exhibits” immediately before the signature page of this report.

**SCHEDULE II****VALUATION AND QUALIFYING ACCOUNTS  
(in millions)**

	<b>Allowances For</b>	
	<b>Financing Receivables</b>	<b>Accounts Receivable</b>
<b>Year ended July 30, 2016</b>		
Balance at beginning of fiscal year .....	\$ 382	\$ 302
Provisions (benefits) .....	17	(26)
Recoveries (write-offs), net .....	(15)	(28)
Foreign exchange and other .....	(9)	1
Balance at end of fiscal year .....	<u>\$ 375</u>	<u>\$ 249</u>
<b>Year ended July 29, 2017</b>		
Balance at beginning of fiscal year .....	\$ 375	\$ 249
Provisions (benefits) .....	(35)	27
Recoveries (write-offs), net .....	(49)	(61)
Foreign exchange and other .....	4	(4)
Balance at end of fiscal year .....	<u>\$ 295</u>	<u>\$ 211</u>
<b>Year ended July 28, 2018</b>		
<b>Balance at beginning of fiscal year.</b> .....	<b>\$ 295</b>	<b>\$ 211</b>
<b>Provisions (benefits).</b> .....	<b>(89)</b>	<b>(45)</b>
<b>Recoveries (write-offs), net</b> .....	<b>(6)</b>	<b>(37)</b>
<b>Foreign exchange and other</b> .....	<b>5</b>	<b>—</b>
<b>Balance at end of fiscal year</b> .....	<b><u>\$ 205</u></b>	<b><u>\$ 129</u></b>

Foreign exchange and other includes the impact of foreign exchange and certain immaterial reclassifications.

## INDEX TO EXHIBITS

Exhibit Number	Exhibit Description	Incorporated by Reference				Filed Herewith
		Form	File No.	Exhibit	Filing Date	
3.1	Restated Articles of Incorporation of Cisco Systems, Inc., as currently in effect	S-3	333-56004	4.1	2/21/2001	
3.2	Amended and Restated Bylaws of Cisco Systems, Inc., as currently in effect	8-K	000-18225	3.1	7/29/2016	
4.1	Indenture, dated February 17, 2009, between Cisco Systems, Inc. and the Bank of New York Mellon Trust Company, N.A., as trustee	8-K	000-18225	4.1	2/17/2009	
4.2	Indenture, dated November 17, 2009, between Cisco Systems, Inc. and the Bank of New York Mellon Trust Company, N.A., as trustee	8-K	000-18225	4.1	11/17/2009	
4.3	Indenture, dated March 16, 2011, between Cisco Systems, Inc. and the Bank of New York Mellon Trust Company, N.A., as trustee	8-K	000-18225	4.1	3/16/2011	
4.4	Indenture, dated March 3, 2014, between the Company and The Bank of New York Mellon Trust Company, N.A., as trustee	8-K	000-18225	4.1	3/3/2014	
4.5	Forms of Global Note for the registrant's 4.95% Senior Notes due 2019 and 5.90% Senior Notes due 2039	8-K	000-18225	4.1	2/17/2009	
4.6	Forms of Global Note for the registrant's 4.45% Senior Notes due 2020 and 5.50% Senior Notes due 2040	8-K	000-18225	4.1	11/17/2009	
4.7	Form of Officer's Certificate setting forth the terms of the Fixed and Floating Rate Notes issued in March 2014	8-K	000-18225	4.2	3/3/2014	
4.8	Form of Officer's Certificate setting forth the terms of the Fixed and Floating Notes issued in June 2015	8-K	000-18225	4.1	6/18/2015	
4.9	Form of Officer's Certificate setting forth the terms of the Fixed and Floating Notes issued in February 2016	8-K	000-18225	4.1	2/29/2016	
4.10	Form of Officer's Certificate setting forth the terms of the Fixed and Floating Notes issued in September 2016	8-K	000-18225	4.1	9/20/2016	
10.1*	Cisco Systems, Inc. 2005 Stock Incentive Plan (including related form agreements)					X
10.2*	Cisco Systems, Inc. Employee Stock Purchase Plan	8-K	000-18225	10.1	11/24/2014	
10.3*	Cisco Systems, Inc. Deferred Compensation Plan, as amended	10-Q	000-18225	10.1	2/21/2017	
10.4*	Cisco Systems, Inc. Executive Incentive Plan	8-K	000-18225	10.2	12/12/2017	
10.5*	Form of Executive Officer Indemnification Agreement	10-K	000-18225	10.7	9/20/2004	
10.6*	Form of Director Indemnification Agreement	10-K	000-18225	10.8	9/20/2004	
10.7*	Separation Agreement by and between Cisco Systems, Inc. and Pankaj Patel	8-K	000-18225	10.1	11/3/2016	
10.8*	International Transfer Agreement (Managed Move), Relocation Payback and International Transfer Tax Policy Agreements by and between Cisco Systems, Inc. and Chris Dedicat	10-Q	000-18225	10.2	11/22/2016	
10.9	Credit Agreement dated as of May 15, 2015, by and among Cisco Systems, Inc. and Lenders party thereto, and Bank of America, N.A., as administration agent, swing line lender and an L/C issuer	10-Q	000-18225	10.1	5/20/2015	

Exhibit Number	Exhibit Description	Incorporated by Reference				Filed Herewith
		Form	File No.	Exhibit	Filing Date	
10.10	364-Day Credit Agreement dated as of March 30, 2017, by and among Cisco Systems, Inc. and Lenders party thereto, and Bank of America, N.A., as administration agent and a Lender	8-K	000-18225	10.1	3/31/2017	
10.11	Form of Commercial Paper Dealer Agreement	10-Q	000-18225	10.1	2/23/2011	
10.12	Commercial Paper Issuing and Paying Agent Agreement dated January 31, 2011 between the Registrant and Bank of America, N.A.	10-Q	000-18225	10.2	2/23/2011	
21.1	Subsidiaries of the Registrant					X
23.1	Consent of Independent Registered Public Accounting Firm					X
24.1	Power of Attorney (included on page 119 of this Annual Report on Form 10-K)					X
31.1	Rule 13a-14(a)/15d-14(a) Certification of Principal Executive Officer					X
31.2	Rule 13a-14(a)/15d-14(a) Certification of Principal Financial Officer					X
32.1	Section 1350 Certification of Principal Executive Officer					X
32.2	Section 1350 Certification of Principal Financial Officer					X
101.INS	XBRL Instance Document					X
101.SCH	XBRL Taxonomy Extension Schema Document					X
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document					X
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document					X
101.LAB	XBRL Taxonomy Extension Label Linkbase Document					X
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document					X

\* Indicates a management contract or compensatory plan or arrangement.

## SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this Report on Form 10-K to be signed on its behalf by the undersigned, thereunto duly authorized.

September 6, 2018

CISCO SYSTEMS, INC.

/S/ CHARLES H. ROBBINS

**Charles H. Robbins**  
**Chairman and Chief Executive Officer**

## POWER OF ATTORNEY

KNOW ALL PERSONS BY THESE PRESENTS, that each person whose signature appears below constitutes and appoints Charles H. Robbins and Kelly A. Kramer, jointly and severally, his attorney-in-fact, each with the full power of substitution, for such person, in any and all capacities, to sign any and all amendments to this Annual Report on Form 10-K, and to file the same, with all exhibits thereto and other documents in connection therewith, with the Securities and Exchange Commission, granting unto said attorney-in-fact and agent full power and authority to do and perform each and every act and thing requisite and necessary to be done in connection therewith, as fully to all intents and purposes as he might do or could do in person hereby ratifying and confirming all that each of said attorneys-in-fact and agents, or his substitute, may do or cause to be done by virtue hereof.

Pursuant to the requirements of the Securities Exchange Act of 1934, this Report on Form 10-K has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

<u>Signature</u>	<u>Title</u>	<u>Date</u>
/S/ CHARLES H. ROBBINS <b>Charles H. Robbins</b>	Chairman and Chief Executive Officer (Principal Executive Officer)	September 6, 2018
/S/ KELLY A. KRAMER <b>Kelly A. Kramer</b>	Executive Vice President and Chief Financial Officer (Principal Financial Officer)	September 6, 2018
/S/ PRAT S. BHATT <b>Prat S. Bhatt</b>	Senior Vice President, Corporate Controller and Chief Accounting Officer (Principal Accounting Officer)	September 6, 2018

<u>Signature</u>	<u>Title</u>	<u>Date</u>
/S/ CAROL A. BARTZ <b>Carol A. Bartz</b>	Lead Independent Director	September 6, 2018
/S/ M. MICHELE BURNS <b>M. Michele Burns</b>	Director	September 6, 2018
/S/ MICHAEL D. CAPELLAS <b>Michael D. Capellas</b>	Director	September 6, 2018
/S/ MARK GARRETT <b>Mark Garrett</b>	Director	September 6, 2018
/S/ JOHN L. HENNESSY <b>Dr. John L. Hennessy</b>	Director	September 6, 2018
/S/ KRISTINA M. JOHNSON <b>Dr. Kristina M. Johnson</b>	Director	September 6, 2018
/S/ RODERICK C. McGEARY <b>Roderick C. McGeary</b>	Director	September 6, 2018
/S/ ARUN SARIN <b>Arun Sarin</b>	Director	September 6, 2018
/S/ BRENTON L. SAUNDERS <b>Brenton L. Saunders</b>	Director	September 6, 2018
/S/ STEVEN M. WEST <b>Steven M. West</b>	Director	September 6, 2018

# Shareholder Information and Forward-Looking Statements

## Executive Officers

### **Charles H. Robbins**

Chairman and Chief Executive Officer

### **Mark Chandler**

Executive Vice President, Chief Legal Officer, and Chief Compliance Officer

### **Gerri Elliott**

Executive Vice President and Chief Sales and Marketing Officer

### **David Goeckeler**

Executive Vice President and General Manager, Networking and Security Business

### **Kelly A. Kramer**

Executive Vice President and Chief Financial Officer

### **Maria Martinez**

Executive Vice President and Chief Customer Experience Officer

### **Irving Tan**

Senior Vice President, Operations

### **Principal Accounting Officer**

### **Prat S. Bhatt**

Senior Vice President, Corporate Controller and Chief Accounting Officer

## Resources

For more information about Cisco, to view the Annual Report online, or to obtain other financial information without charge, contact:

### **Investor Relations**

Cisco Systems, Inc.

170 West Tasman Drive  
San Jose, CA 95134-1706  
1 408 227 CSCO (2726)

<http://investor.cisco.com>

Cisco's stock trades on the NASDAQ Global Select Market under the ticker symbol CSCO.

### **Independent Registered Public Accounting Firm**

PricewaterhouseCoopers LLP  
San Jose, California

### **Transfer Agent and Registrar**

Computershare Investor Services  
P.O. Box 43078  
Providence, RI 02940-3078  
[www-us.computershare.com/investor](http://www-us.computershare.com/investor)  
Toll-free: 1 800 254 5194  
International: 1 781 575 2879

### **Notice of Annual Meeting**

Cisco Systems, Inc.  
Building 9  
260 East Tasman Drive  
San Jose, CA 95134  
Wednesday, December 12, 2018  
10 a.m. Pacific time

## Forward-Looking Statements

This Annual Report contains forward-looking statements regarding future events and our future results that are subject to the safe harbor provisions created under the Securities Act of 1933 and the Securities Exchange Act of 1934, each as amended. These statements are based on current expectations, estimates, forecasts, projections, and the beliefs and assumptions of our management. Words such as "expects," "anticipates," "targets," "goals," "projects," "intends," "plans," "believes," "momentum," "seeks," "estimates," "continues," "endeavors," "strives," "may," variations of such words, and similar expressions are intended to identify such forward-looking statements. In addition, any statements that refer to our anticipated growth, trends in our business, and other characterizations of future events or circumstances are forward-looking statements. 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; 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 and other customer markets; the return on our investments in certain priorities, key growth areas, and in certain geographical locations, as well as maintaining leadership in routing, switching, and services; the timing of orders and manufacturing and customer lead times; 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 service 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, intellectual property, antitrust, shareholder, and other matters, and governmental investigations; our ability to achieve the benefits of the announced restructuring and possible changes in the size and timing of the related charges; man-made problems such as cyberattacks, data protection breaches, malware, or terrorism; natural catastrophic events; a 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 contained in this Annual Report. Our results of operations for the year ended July 28, 2018, are not necessarily indicative of our operating results for any future periods. We undertake no obligation to revise or update any forward-looking statements for any reason.

**Americas Headquarters**

San Jose, CA, USA

**Asia Pacific Headquarters**

Singapore

**Europe Headquarters**

Amsterdam, The Netherlands

Cisco has more than 400 offices worldwide. Addresses, phone numbers, and fax numbers are listed on the Cisco Website at [www.cisco.com/go/offices](http://www.cisco.com/go/offices).

Published October 2018

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