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Cisco Systems, Inc. (CSCO) CEO Chuck Robbins on Q1 2020 Results - Earnings Call Transcript

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FQ1: 11-13-19 Earnings Summary

Press Release *10-Q* *Slides*

EPS of $0.84 beats by $0.03 | Revenue of $13.16B (0.67% Y/Y) beats by $64.46M

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Cisco Systems, Inc. (NASDAQ:CSCO) Q1 2020 Results Conference Call November 13, 2019 4:30 PM ET

Company Participants

Marilyn Mora - Head of Investor Relations

Chuck Robbins - Chairman and Chief Executive Officer

Kelly Kramer - Chief Financial Officer

Conference Call Participants

Ittai Kidron - Oppenheimer

Samik Chatterjee - JPMorgan

Paul Silverstein - Cowen

James Faucette - Morgan Stanley

Rod Hall - Goldman Sachs

Tejas Venkatesh - UBS

Tal Liani - Bank of America

Jim Suva - Citigroup

Aaron Rakers - Wells Fargo

James Fish - Piper Jaffray

Operator

Welcome to Cisco's First Quarter Fiscal Year 2020 Financial Results Conference Call. At the request of Cisco, today's conference is being recorded [Operator Instructions].

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

Marilyn Mora

Thanks, Michelle. Welcome everyone to Cisco's First Quarter Fiscal 2020 Quarterly Earnings Conference Call. This is Marilyn Mora, Head of Investor Relations. And I'm joined by Chuck Robbins, our Chairman and CEO and Kelly Kramer, our CFO. By now, you should have seen our earnings press release. A corresponding webcast with slides, including supplemental information, will be made available on our Web site in the Investor Relations section following the call.

As discussed in early in Q1, we have made certain reclassifications to prior period amounts to conform to the current period presentation. Income statements, full GAAP to non-GAAP reconciliation information, balance sheets, cash flow statements and other financial information, can also be found in the financial information section of our Investor Relations Web site. Throughout this conference call, we will be referencing both GAAP and non-GAAP financial results, and we will discuss product results in terms of revenue and geographic and customer results in terms of product orders, unless stated otherwise.

All comparisons made throughout this call will be made on a year-over-year basis. The matters we will be discussing today include forward-looking statements, including the guidance we will be providing for second first quarter of fiscal 2020. They are subject to the risks and uncertainties that we discuss in detail in our documents filed with the SEC, specifically the most recent reports on Forms 10-K, which identify important risk factors that could cause actual results to differ materially from those contained in the forward-looking statements. With respect to guidance, please also see the slides and press release that accompany this call for further details. Cisco will not comment on its financial guidance during the quarter, unless it is done through an explicit public disclosure.

In Q2 of fiscal 2019, we completed the sale of our SPVSS business and accordingly, had no revenue or expense from that business in Q1 fiscal 2020. As such, all of the revenue, non-GAAP and product orders information we will be discussing today is normalized to exclude the SPVSS business from our historical results. We have provided historical financial information for the SPVSS business in the slides that accompany this call and on our Web site to help to understand these impacts. The guidance we provided during our Q4 earnings call has been normalized in the same way.

I will now turn it over to Chuck.

Chuck Robbins

Thanks Marilyn. We delivered a solid quarter against a challenging macro environment. While we're pleased with this performance, we're most focused on the environment as we move forward. We'll discuss this more in a moment. What's happening inside Cisco regardless of the macro is an unrelenting focus on driving innovation, transforming our business and exceeding our customers' expectations.

In Q1, as you've seen, we have revenue growth of 2% and double digit non-GAAP earnings per share growth. We also delivered strong non-GAAP gross margins and non-GAAP operating margins along with solid operating cash flow. We continued to invest in innovation and expand our market opportunities, while maintaining our commitment to maximizing shareholder return.

Over the last year, many of you have heard me talk about the resilience of the global macro environment. However, on our last earnings call, we indicated that we had begun to see some weakness and that weakness continued throughout Q1 and was more broad-based. While the main challenges continue to be service provider in emerging markets, this quarter we also saw relative weakness in enterprise and commercial. Despite these headwinds and because of key decisions we made four years ago to change our business model, we remain well positioned to capitalize on the tremendous opportunities across cloud, automation, 5G, security and collaboration.

Our transition to software continues to progress and we are on track with where we said we would be at the end of fiscal year 2020. This transition to software not only aligns to how our customers want to consume our technology, but we also believe it will lessen the impact of macroeconomic shifts in the future. Despite the current uncertainty, our innovation pipeline remains strong. At our annual partner summit last week, we announced several exciting additions to our portfolio, including network automation and analytics, cloud based networking, collaboration, as well as new security capabilities. Over the next couple of months, you will see us deliver even more innovation to help our customers achieve their business objectives.

Now, I'd like to share some recent highlights across the business. Our enterprise networking portfolio continued to grow as customers increasingly adopt our intent-based networking portfolio, spanning our Catalyst 9000 family of switches, Meraki cloud based platforms and next generation data center solutions. Our customers today are running applications across multiple cloud environments and this shift requires a fundamental change in how they build their networks and their security architectures. To help them achieve this, we are automating connectivity across any cloud. A good example of this is our recently announced partnership with Microsoft to help our customers improve network connectivity with the highest level of security from branch offices to cloud based applications by integrating Cisco's SD-WAN solution with Azure’s virtual WAN.

To further extend our enterprise networking leadership, we continue to expand our cloud managed network and security offerings. Last week, we also announced an expansion of our Meraki portfolio, including continued integration between Meraki's dashboard and Cisco's switching portfolio, as well as innovative new LTE based WAN connectivity solutions. We believe our planned acquisition of Acacia will also play a critical role in building upon the strength of our switching, routing and optical networking portfolio. By utilizing our innovations across silicon, software and optics, we are enabling our customers to transform their networks.

Now let's turn to security, which is always at the heart of everything we do. It's deeply integrated into the fabric of our entire portfolio to help secure our customers' data and address their modern application and multi cloud environments. Cyber security continues to be a top concern for our customers as they evolve their enterprise architectures to address the challenges of an ever changing threat environment.

We have the most comprehensive integrated cyber security platform in the market designed to enable our customers to securely connect any application running on any cloud and deliver to any device. We've been building an expansive zero trust framework for securing access across the workforce, the workplace and the workload. As the leader in zero trust, our customers are increasingly turning to us to help them extend simple and trusted access to their users in hybrid and multi cloud environments.

This is leading to strong uptake of Duo, our identity access management solution, which provides continuous authentication, ensuring the right people are able to access the right applications. To further reduce complexity in our customers' environments, we recently announced new enhanced capabilities in our firewall, breach defense, endpoint protection and Talos incident response solutions. These innovations are designed to provide greater threat protection and enhance the benefits of our platform. We also continue to leverage AI and ML capabilities through our industry leading threat intelligence platform Talos, along with Stealthwatch and Umbrella to bring our customers simplicity, visibility and insight that no other company can deliver.

Moving to applications. We are rapidly becoming the center of our customer strategy for empowering teams and increasing productivity, as 95% of the Fortune 500 use our collaboration portfolio. This is leading to the solid performance in our businesses as growing number of customers adopt our unique solutions.

During the quarter, we expanded our offerings to empower our customers for the modern workplace protecting data from ever increasing cyber threats and delivering highly secure productivity and collaboration solutions. A good example of this is our next generation WebEx, our cloud based team collaboration platform, enabling better teamwork while helping users stay secure with integrated end-to-end encryption.

We also launched Single Platform Advantage, delivering all collaboration workloads, including calling, messaging, meeting and contact center from a single platform. In addition, we announced our new Cisco WebEx Edge for devices, as well as hardware-as-a-service options for phones, desks and room-based video systems.

We're raising the bar for the industry by continuing to drive innovation in our expanding family of cognitive collaboration offers with AI and ML integrated capabilities. During the quarter, we acquired CloudCherry, a market leading customer experience management solution to augment our contact center portfolio with cloud analytics and AI to increase productivity and enhance user experiences. We also achieved a strong quarter in our App Dynamics business with yet another quarter of double digit growth,

Our investments in App Dynamics have made Cisco the leader in application monitoring and analytics. We're helping our customers transform their digital businesses through our comprehensive portfolio of solutions that turns data into actionable real time insights by linking application performance to business outcomes.

To summarize, while we remain in a challenging macroeconomic environment, I'm proud of our progress, both in our own continued transformation and in how we are empowering customers to drive their own transformation and shift to the cloud. We have a clear vision and strategy and are executing well against it to capture the many opportunities ahead. I feel great about our portfolio and I believe fully in our customers' commitment to our technology solutions. We will also continue to invest in organic and inorganic innovation to position Cisco for the long term. We also remain committed to managing our business to ensure we drive the greatest long term value for our customers, employees, partners and shareholders.

Now, let me turn it over to Kelly.

Kelly Kramer

Thanks, Chuck. I'll start with a summary of our financial results for the quarter, followed by the guidance for Q2. Our overall Q1 results were solid. We executed well with revenue growth and strong margins, net income and EPS. Total Revenue was $13.2 billion, up 2%. Our non-GAAP operating margin rate was 33.6%, up 1.3 points; non-GAAP net income was $3.6 billion, up 5%; and non-GAAP EPS was $0.84, up 12%.

Let me provide some more detail on our Q1 revenue. Total product revenue was up 1% to $9.9 billion. Infrastructure platform was down 1%. All of the businesses were up except for routing. Switching had growth in both campus and data center with the continued ramp of the Cat9K and strength of the Nexus 9K.

Wireless grew driven by Meraki. Data center had solid growth, led by HyperFlex. Routing declined due to weakness in service provider. Applications was up 6% with growth across all the businesses, including double digit growth in app dynamics. Security was at 22% with strong performance in Identity and Access, advanced threat, unified threat and web security. Service revenue was up 4%, driven by software and solution support. And we continue to transform our business delivering more software offerings and driving more subscriptions. Software subscriptions were 71% of total software revenue, up 12 points year-over-year. When we look at the impact of acquisitions on our Q1 results year-over-year, there was a 50 basis point positive impact on revenue. In terms of orders in Q1, total product orders were down 4%.

Looking at the geographies, Americas and EMEA were each down 3% and APJC was down 5%. Total emerging markets were down 13% with the BRICS plus Mexico down 26%. In our customer segments, public sector was up 6%, enterprise and commercial were each down 5% and service provider was down 13%.

Remaining performance obligations, or RPO, at the end of Q1 were $24.9 billion, up 11%. RPO is our total deferred revenue plus unbilled differed and represents total committed non-cancelable future revenue. From a non-GAAP profitability perspective, total Q1 gross margin was 65.9%, up 1.7 points. Product gross margin was 66.1%, up 2.5 points and service gross margin was 65.4%, down 0.4 points. In terms of the bottom line from a GAAP perspective, Q1 net income was $2.9 billion and EPS was $0.68.

We ended Q1 the total cash, cash equivalents and investments of $28 billion. Operating cash flow was $3.6 billion, down 5%. Normalized for the $400 million legal settlement we received from a risk debt in Q1 of fiscal '19, operating cash flow was up 7%. From a capital allocation perspective, we returned $2.3 billion to shareholders during the quarter that was comprised of $0.8 billion of share repurchases and $1.5 billion for our quarterly dividend. We continue to invest organically and inorganically in our innovation pipeline.

During Q1, we closed four acquisitions all in the applications area. These moves are consistent with our strategy of increasing investment in innovation and R&D for our growth areas. To summarize, we had a solid Q1. We executed well with top line growth and strong profitability. We're seeing the returns on the investments we're making in innovation, and driving the shift to more software and subscription, delivering long term growth and shareholder value.

Let me reiterate our guidance for the second quarter of fiscal '20. This guidance includes the type of forward looking information that Marilyn referred to earlier; we expect revenues to decline in the range of minus 3% to minus 5% year-over-year; we anticipate the non-GAAP gross margin rate to be in the range of 64.5% to 65.5%; the non-GAAP operating margin rate is expected to be in the range of 32.5% to 33.5%, and the non-GAAP tax provision rate is expected to be 20%; non-GAAP earnings per share is expected to range from $0.75 to $0.77.

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

Marilyn Mora

Thanks, Kelly. Michelle, let's go ahead and open the line for questions. And while Michelle is doing that, I'd like to ask the audience to address one question only, so that we have plenty of time for the others. Michelle, I'll turn it over to you.

Question-and-Answer Session

Operator

Thank you. Ittai Kidron from Oppenheimer, you may go ahead.

Ittai Kidron

Chuck, maybe you can kind of walk us through a little bit kind of how the quarter evolved as far as the demand pattern. You're talked about weakness became, first of all, more broad based but also started into the enterprise and commercial. Any more color you can give us there, either from a product or regional standpoint. And with regards to your working assumptions into the next quarter, into the January quarter, is it your assumption that the intensity of the softness you're seeing right now will just stay as is, or getting worse? Help us think about the framework you have in mind when you give the guidance.

Chuck Robbins

If you recall in the last earnings call, I did say that we began to see some early signs of some macro impact towards the end of Q4. And then we just basically saw that continue throughout the quarter and as obviously the entire quarter was worse than we had expected when we began. And it was fairly broad based. It was -- I mean Kelly just read the regional numbers off from an orders perspective. So you saw negative 3, negative 3, negative 5, from Americas, EMEA and Asia.

I'd say across the technology areas, it was pretty broad based. The segments that we saw, public sector continue to be strong but the rest were -- enterprise commercial did weaken. Service provider and emerging markets, which were stressed last quarter, were about the same. We had shown the ability to offset that with strength in commercial, and enterprise and public sector. And when those weakened, obviously this quarter that impacted our ability to offset them.

And while all that might seem like this excuse, it also had to happen in a quarter where we did have incredibly tough compare. So this is the worst quarter that could have occurred for us. But that's really what we saw. As far as what we've modeled going forward, we've effectively assumed that it will stay as is. I don't think -- we haven't modeled any material further deterioration or improvement, I think than what we what we put forward today.

Operator

Thank you. Samik Chatterjee from JPMorgan, you may go ahead.

Samik Chatterjee

Chuck, thanks for the detail on the last question. I just wanted to get a sense of what you're hearing from your customers in terms of are you hearing that if some of the trade aspects of that are depressing the macro get resolved. Do you expect some of them to come back in terms of spending, what are you hearing from your customers? And if you can give us an update on the order trends in China as well that would be helpful?

Chuck Robbins

So from the customers, it feels like there's not a broad base loud noise out there. It feels like there's a bit of a pause. We saw things like conversion rates on our pipeline were lower than normal, which says that things didn't closed the way we've historically seen it. We didn't see any incremental loss ratios. It was really just stuff slipping. We saw some large deals get done but got done smaller. Kelly and I were involved in a couple personally that we saw that when we began talking to the customers about the transactions and by the time they got done, they were smaller than when we have begun. So that happened. And then we just saw deals that slipped, and so we saw little bit of all that.

But it's not -- I'd say we also had our teams telling us that the approval process in several customers across different number of industries were changing, which is usually indicative of, hey, let's add another signature requirement, because we want to just put another set of eyes on every expenditure right now. So those are the things we've seen. And unfortunately, I've done this long enough that I've seen it before. So you recognize it when you see it, and that's really effectively what we saw during the quarter. In China, Kelly was…

Kelly Kramer

China continued its decline. It was down 31% versus last quarter we -- it was down 26%. So that momentum continuing to just accelerate the decline in China.

Operator

Thank you. Paul Silverstein from Cowen, you may go ahead.

Paul Silverstein

Kelly, if you could tell us pricing, I know we're going to see in the Q. But if you could tell us the rate of price erosion, if there has been a change. And then if I did the math correctly on OpEx, it looks like your guidance would suggest around $3.8 billion for the January quarter, that'd be down $400 million sequentially and $150 million year-over-year. Do I have that right? Is that the way you're thinking about it? And related to that, how should we think about OpEx going forward throughout the year? How do you plan on managing expenses given the less than expected revenue outlook?

Kelly Kramer

So let me take those. So on price, we had a really very, very good quarter on price. It is the lowest in some time in terms of the least amount of price erosion. So from impact on our product gross margin rate, Paul, which is I know the metric you're looking at, it was only 40 basis points. Now I will say, that's great, and I think we've done a lot of great things on our pricing. For example, we've been selectively -- where we have price elasticity, we will raise prices, and we've been effective on driving some product transitions and we've been realizing that benefit.

I will say we are starting to see, we didn't feel the impact of it this quarter, but we are starting to see pricing pressure in the server market that we expect to accelerate next quarter, but that's, of course, including the guide. But for Q1, it was a very, very strong pricing quarter, which has been fantastic. From an OpEx perspective, if you play down the ranges I just gave you, it does show that OpEx will be down and how you're thinking about it. And yes, we are managing it like we always do, which is balancing the investments we're making plus driving trade off and cost out. So you're looking at it correctly and that's what we're driving it to.

Paul Silverstein

Kelly, the real question is, can operating margin go up with revenue being slightly down, could you drive higher operating margin…

Kelly Kramer

So let me break down the margins overall, because I think that is the key question. I would say our margins are -- there's positive certainly driving the margin increase that you're seeing and you're seeing that in the guide. On the positive side, we are definitely feeling the positive impact of the software mix on our margins. So that is driving benefit to us just purely on the increased software content that we have and what we're selling, so that's helping tremendously.

I do think we're going to see some more pricing erosion as we go forward for some of the things that are specific, like of course, the server market is going to get tougher now that the DRAM prices are going down. So that will be a little bit of a negative next quarter, but that's okay. And then of course, we are still benefiting from the DRAM price decrease related to the server market, that we started to feel the benefit of a couple quarters ago. It's a very large impact this quarter favorable to us that will I expect to continue next quarter. But after that, as you recall, we started seeing the benefit on the Q3 of '19. So that'll become less of a year-over-year favor ability for us. And then, we'll see what happens to the pricing there.

So net-net to your question, I don't think it will stay at this rate that we delivered in Q1, which is the highest than it's been, because of those key things. But the underlying trends are all going in the right direction with software that's benefiting and driving the favorable mix. And then the real strong product management we're doing around managing pricing elasticity.

Operator

Thank you. James Faucette from Morgan Stanley Investment Research, you may go ahead.

James Faucette

I'm wondering, Chuck, or Kelly or maybe both of you. Can you talk a little bit about the order of growth versus your current expectations for economic development? Clearly, Chuck, as you pointed out and Kelly, we saw weakness kind of across the board in orders.

But if we think about kind of a relatively flat environment from here going forward, as you said you're forecasting on. How long does it take us to start to get to more of a flattish and then even recovering order book in that kind of scenario and environment? Thanks a lot.

Chuck Robbins

Kelly, I'll let you handle that.

Kelly Kramer

James, that's a tough question, right? I mean, I'd say, certainly, the headwinds we have right now are going to be with us I think in the short term. Again, whether it's just the -- I don't see any catalyst to changed momentum right now with uncertainty and business confidence in the macro like Chuck talked about. I do think from a portfolio perspective, obviously, we feel good about portfolio and you're seeing still, regardless of macro the improvement we're making on the software metric that continues regardless.

Going forward, we do have easier compares as the second half comes around, it's not that that's a big victory but that is the reality. And I think we're just going to keep executing through whatever the macro is. I don't know if you want to add, Chuck.

Chuck Robbins

James, I would say that, if you just go around the world right now and you look at what's happening in Hong Kong, you look at the China-U.S. trade situation, you look at what's going on in DC. You've got Brexit. And you've got uncertainty in Latin America. I mean, I think it's -- in any of those that are big issues if they get resolved then you could see some of the uncertainty removed, and I think that's what -- business confidence just suffers when there's lack of clarity. And there's been lack of clarity for so long that I think it's finally just came into play.

So I think, you're probably able to guess that, as well as we are, based on some of these bigger issues sort of coming to some level of conclusion. And then obviously, we have the elections coming in next year that we have to see how they work. But I will reiterate what Kelly said. Despite the order growth rate, this software transition that we've been embarking on is going exactly as we planned. It continued this quarter. We had solid results in our software portfolio again this quarter. And we put up some numbers at our analyst conference that we said we would hit by the end of 2020, we're on track to get there. So we feel good about that. And we're going to keep on executing.

I think the teams have done a phenomenal job of getting our portfolio in the position that it's at. And that's why I said I have full confidence that our customers are committed to these technologies, just because they pause and we see a slowdown in one quarter. I think for the long term, we're in good shape, and I feel good about where we are.

Operator

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

Rod Hall

I wanted to ask about the commercial order rate deterioration. I think last quarter you guys hadn't really seen much deterioration at that at the end of the quarter. And then I'm assuming through this quarter, it's been getting worse. But wondering if you could just comment on what you're seeing there in that particular market. And regionally, are you seeing -- is it mainly in U.S. where you see that weakness, do you see the weakness all over the place. Just any further color you could give there would be helpful.

Chuck Robbins

Rod, that was one of the big -- that's a good question. That was one of the big signals to us that this thing is -- that there's definitely something going on to, because the commercial business is usually fairly resilient. And it was broad based across the globe in each of the regions. I think all three were negative. So it was it was broad based. But I think that also be one of the first to bounce back when we start seeing that come back, that's a good sign.

Operator

Thank you. Tejas Venkatesh from UBS, you may go ahead.

Tejas Venkatesh

I wonder if you could provide more color on what you're seeing in the U.S. service provider business and also more broadly, how you're thinking about the service provider vertical going forward. Obviously, it's been weak for a while, but assuming that that environment stays that way. Are there product refreshes and so forth coming down the pipe that can better the year-over-year trends? Thank you.

Chuck Robbins

So in the U.S., I think it's pretty clear if you just follow what's going on with the major players here, and we talked about this on the last call that they're currently focused on building out their trials and then their broader consumer based 5G services. And that's an area that frankly they'll run most of that traffic across their existing networks. We've said that when they begin to build out the broad based enterprise service delivery 5G networks that that's where we would really come into play on helping re-engineer backbones for higher throughput and more traffic. And I would suspect that we'll see them start to do some of that maybe in the second half of 2021, we'll have to see how fast they get moving.

And we have some announcements coming over the next couple of months that I think line up with what they're trying to accomplish. And so we'll see how it moves. But that's the transition that we would be looking for that could help get this business to a little better position. It was -- and on a global basis, I'll tell you, it was -- it got much weaker in Europe. It was about the same in the U.S., I think. And we've had some pockets of strength in Asia. Outside of China, we had some strength in, particularly in Japan. So as we've always said about this business, it's so big deal driven. But for right now, I think that's the story of what we see.

Operator

Thank you. Tal Liani with Bank of America, you may go ahead, sir.

Tal Liani

So if I take a five quarter view, six quarter view, on your results, not just this quarter on the guidance, I see constant deterioration in the growth rate, organically from about 4.5% now we're getting to minus 5%, or I have to look exactly at the guidance where we are. And the question I have is, not about the environment but rather about the portfolio. If you ignore the environment as much as we can, what can you do with the portfolio in order to change the trend line and reaccelerate the growth? Maybe even start with, can you identify what are the weak areas versus what are the strong areas and then what's in your power to change versus something that may take longer? Thanks.

Chuck Robbins

Tal, it's a good question and that's actually what we spend every day doing. I will tell you that we saw strength, continued strength in the campus refresh in the portfolio that we brought forward there, which obviously, if you think about what we've been doing over the last couple of years, and I made a comment in my opening remarks about this is, we have now transitioned our entire enterprise networking portfolio to a mandatory subscription model and those products and that those area, those new products are still, they're growing very strongly right now as customers continue to deploy.

So one of the big things we want to do is continue to transition towards the software model. We had 30 years of a net 30 CapEx model. So it's, we're in the midst of that transition. We're making progress on the timeline that we expected. That's the biggest strategic thing I think we can do. From a portfolio perspective, I think you have -- if you go across the portfolio, we made a lot of new announcements last week, we've got new announcements coming up. And I think that, clearly, we have a lot of customers that are still buying a lot of stuff.

So while there's a slowdown, I think there's still meaningful value that our customers are seeing with our technology, and we'll continue to do everything we can to try to find those areas that resonate the most right now. I think you saw you see it with security given the importance of that technology to them. And we're working on some other things that we haven't announced yet. So we're going to continue to do all the things that you described.

Operator

Thank you. Jim Suva from Citigroup Global Markets, you may go ahead, sir.

Jim Suva

Obviously, you laid out a lot of the details about the challenges. When we look back historically over Cisco, their history, the last time we kind of saw such negative trends, were kind of July 2017. There was kind of about a fourth quarter pause before recovery. Is there anything different about it this time? And some people will say, well, white boxes starting to hurt you a lot. Is it white boxes? Is it generally macro? Or why wouldn't it be, like four quarters, like what we saw last year in 2017? Thank you.

Chuck Robbins

First of all, I think that given the broad based and the rapid change that we saw, I don't believe it's anything like white box or anything like that. It's broad across the portfolio. It's broad across geographies. And we're, as Kelly said, obviously, in the second half. We don't like to talk about comps. But the math is different in the second half of the year. But we also have all the things that I just talked about with Tal. We also have this Wi-Fi 6 transition.

At some point, we will have some spinning going on around the 5G backbone transitions. We got 400 gig coming next year. So there are a lot of things. And I also believe that our customers, they will pause for a while. But technology is so absolutely core to their fundamental strategies that it just seems to me that the time that they're going to be able to pause is going to be shorter than what you would have seen in the past. I mean, they worry about their competitors' investments, they worry about falling behind.

So I think they'll hit the pause button because of all the uncertainty. I think we have to just see how long it lasts in today's world, given the strategic value of all the technology. And frankly, everything that we're building is incredibly important to them as they deal with this new cloud world and re-architecting their traffic flows and their security architecture. And there's only so long they're going to build a pause on doing that. But we'll see how it turns out.

Operator

Thank you. Aaron Rakers from Wells Fargo, you may go ahead.

Aaron Rakers

I want to go back to kind of the comments earlier made around kind of the software expansion, and kind of progressing to what you laid out at past analyst days. If I recall, it seemed to kind of map out that you would have about 20% of your total kind of revenue being -- product revenue being contributed from software. As we think about the product portfolio and the push to subscription, is that the right trajectory to think about? And as we look even beyond that, could you see even higher mix of kind of just recurring nature of your business? I'm just trying to understand what more is left to kind of build out the product portfolio around this kind of subscription motion for the company.

Kelly Kramer

I'd say what we laid out is we said by the end of '20, we should have 30% of our revenue be software, and software and services be 50%. So that's the metric we are pacing towards. And your 20% number, we are already passed. So we are driving to be at that that 30% by the end of this year. So like Jeff mentioned, we are pacing well with that. This transition that we're driving has greatly increased the amount of software we are selling with our system. So that is all going well.

Chuck Robbins

Yes, I think if you just -- I think Kelly said, by the end of 2020, our target was to be at 30% of our revenue coming from software. And if you also correlate the metric we shared today, which is in Q1 71% of our software was coming from subscription and SaaS, which four years ago that number was probably a third or less. So that's the nature of the success of the transition that we've been driving so far.

Kelly Kramer

Yes, it’s a good point. Actually, the target for the end of '20 for that was to be 66%, so we've passed that metric already.

Operator

Thank you. James Fish from Piper Jaffray, you may go ahead, sir.

James Fish

I just hoping to get more color on sort of the campus switching cycles with the Cat9K, and just kind of where you think we are, especially with large enterprises as that really drives, it seems like more of the growth of the business anyways and just trying to understand that. And then just make sure that we're thinking about it correct. When you're talking subscription within this business line, you're talking more of a term license than kind of recurring monthly, correct?

Kelly Kramer

Yes, on that one, subscription meaning. Yes. So if I sell a Catalyst 9K switch now, it's sold with a subscription that gets renewed three or five years since putting on the term from now. So that's what we're talking about. So of all the software we're selling is it based on a term based value that gets renewed.

Chuck Robbins

And Jim, just to give you a little sense of where we are. I mean, we're still -- we're seeing very strong growth year-over-year on those platforms, the transitions happening from the old to the new, just like we would have expected. And we were actually talking about yesterday how we would answer the question relative to where we are in this, because I think I said last time we were in the second inning, and we joked that maybe we're in the bottom of the second inning now. But we're still very early in this transition and it's going very well.

And we now have the entire enterprise networking portfolio in refresh mode with Wi-Fi 6 access points, with the new Catalyst 9000. And then one of the things we announced last week was the ability to manage the Cat 9K, one of the products in the Cat 9K under the Meraki platform, so customers could take advantage of it and we'll continue to extend that across the other portfolio of products. So it's going very well and it's still early.

James Fish

Thanks for that color, Chuck.

Chuck Robbins

Thank you, Jim. So let me just wrap up and say that, obviously, it's a complicated world right now. And we certainly felt the continuing impact that we talked about at the end of our last quarter. That being said, I have great confidence in where we are with the portfolio. We shared some metrics today on the software transition that I think is going incredibly well. And notwithstanding, you know, the short term challenges, we feel really good about the future. And so thank you all for being with us today. And I'll kick it back to Marilyn.

Marilyn Mora

Thanks, Chuck. Cisco's next quarterly earnings conference call, which will reflect our fiscal 2020 second quarter results, will be on Wednesday, February 12, 2020, at 1:30 PM Pacific Time, 4:30 PM Eastern Time. Again, I'd like to remind the audience that in light of regulation FD, Cisco's policy is not to comment on its financial guidance during the quarter, unless it is done through an explicit public disclosure.

We now plan to close the call. If you have any further questions, please feel free to contact the Cisco Investor Relations Department. And we thank you very much for joining the call today.

Operator

Thank you for participating on today's conference call. If you would like to listen to the call in its entirety, you may call 800-835-4610. For participants dialing from outside the U.S., please dial 203-369-3352. This concludes today's call. You may disconnect at this time.