

REVLOM INC /DE/
Form 4
April 15, 2005

FORM 4

**UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549**

OMB APPROVAL

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STATEMENT OF CHANGES IN BENEFICIAL OWNERSHIP OF SECURITIES

Filed pursuant to Section 16(a) of the Securities Exchange Act of 1934, Section 17(a) of the Public Utility Holding Company Act of 1935 or Section 30(h) of the Investment Company Act of 1940

(Print or Type Responses)

1. Name and Address of Reporting Person *
MCGUIRE THOMAS E

(Last) (First) (Middle)
237 PARK AVENUE
(Street)

NEW YORK, NY 10017

(City) (State) (Zip)

2. Issuer Name and Ticker or Trading Symbol
REVLOM INC /DE/ [REV]

3. Date of Earliest Transaction
(Month/Day/Year)
04/14/2005

4. If Amendment, Date Original Filed(Month/Day/Year)

5. Relationship of Reporting Person(s) to Issuer

(Check all applicable)

____ Director _____ 10% Owner
X Officer (give title below) _____ Other (specify below)
Executive Vice President & CFO

6. Individual or Joint/Group Filing(Check Applicable Line)
X Form filed by One Reporting Person
____ Form filed by More than One Reporting Person

Table I - Non-Derivative Securities Acquired, Disposed of, or Beneficially Owned

1. Title of Security (Instr. 3)	2. Transaction Date (Month/Day/Year)	2A. Deemed Execution Date, if any (Month/Day/Year)	3. Transaction Code (Instr. 8)	4. Securities Acquired (A) or Disposed of (D) (Instr. 3, 4 and 5)	5. Amount of Securities Beneficially Owned Following Reported Transaction(s) (Instr. 3 and 4)	6. Ownership Form: Direct (D) or Indirect (I) (Instr. 4)	7. Nature of Ownership (Instr. 4)
			Code	V	Amount	(D)	Price
Class A Common Stock	04/14/2005		F		25,643 (1)	D	\$ 3.29
					219,357	D	

Reminder: Report on a separate line for each class of securities beneficially owned directly or indirectly.

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SEC 1474
(9-02)

Table II - Derivative Securities Acquired, Disposed of, or Beneficially Owned (e.g., puts, calls, warrants, options, convertible securities)

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1. Title of Derivative Security (Instr. 3)	2. Conversion or Exercise Price of Derivative Security	3. Transaction Date (Month/Day/Year)	3A. Deemed Execution Date, if any (Month/Day/Year)	4. Transaction Code (Instr. 8)	5. Number of Derivative Securities Acquired (A) or Disposed of (D) (Instr. 3, 4, and 5)	6. Date Exercisable and Expiration Date (Month/Day/Year)	7. Title and Amount of Underlying Securities (Instr. 3 and 4)	8. Price of Derivative Security (Instr. 5)	9. Number of Derivative Securities Owned Following Reporting Transaction (Instr. 6)
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Reporting Owners

Reporting Owner Name / Address	Relationships			
	Director	10% Owner	Officer	Other
MCGUIRE THOMAS E 237 PARK AVENUE NEW YORK, NY 10017			Executive Vice President & CFO	

Signatures

/s/ Robert K. Kretzman for Thomas E. McGuire pursuant to a Power of Attorney granted on August 18, 2003 04/15/2005

__Signature of Reporting Person Date

Explanation of Responses:

- * If the form is filed by more than one reporting person, *see* Instruction 4(b)(v).
- ** Intentional misstatements or omissions of facts constitute Federal Criminal Violations. *See* 18 U.S.C. 1001 and 15 U.S.C. 78ff(a).
- (1) Represents shares withheld from vested restricted stock pursuant to the terms of a shareholder approved stock plan for the payment of federal and state withholding taxes due on vesting.

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Operating expenses
Foreign currency derivatives

(5
)

3

(6
)

5

Cost of sales—service

(26
)

19

(30
)

28

Total amounts reclassified out of other comprehensive income

\$
43

\$
101

\$
46

\$
193

Table of Contents

CISCO SYSTEMS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

16. Income Taxes

The following table provides details of income taxes (in millions, except percentages):

	Three Months Ended		Six Months Ended		
	January 24, 2015	January 25, 2014	January 24, 2015	January 25, 2014	
Income before provision for income taxes	\$2,873	\$1,755	\$5,233	\$4,295	
Provision for income taxes	\$476	\$326	\$1,008	\$870	
Effective tax rate	16.6	% 18.6	% 19.3	% 20.3	%

During the three months ended January 24, 2015, the Tax Increase Prevention Act of 2014 reinstated the U.S. federal R&D tax credit for calendar year 2014 R&D expenses. As a result, the effective tax rate for the three and six months ended January 24, 2015 reflected tax benefits related to fiscal 2015 R&D expenses and a tax benefit of \$91 million related to fiscal 2014 R&D expenses.

As of January 24, 2015, the Company had \$2.0 billion of unrecognized tax benefits, of which \$1.8 billion, if recognized, would favorably impact the effective tax rate. The Company regularly engages in discussions and negotiations with tax authorities regarding tax matters in various jurisdictions. The Company believes 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. Accordingly, the Company estimates that it is reasonably possible that the unrecognized tax benefits at January 24, 2015 could be reduced by \$300 million in the next 12 months.

17. Segment Information and Major Customers

(a) Revenue and Gross Margin by Segment

The Company conducts business globally and is primarily managed on a geographic basis consisting of three segments: the Americas, EMEA, and APJC. The Company's management makes financial decisions and allocates resources based on the information it receives from its internal management system. Sales are attributed to a segment based on the ordering location of the customer. The Company does not allocate research and development, sales and marketing, or general and administrative expenses to its segments in this internal management system because management does not include the information in its measurement of the performance of the operating segments. In addition, the Company does not allocate amortization and impairment of acquisition-related intangible assets, share-based compensation expense, significant litigation and other contingencies, impacts to cost of sales from purchase accounting adjustments to inventory, 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 its measurement of the performance of the operating segments.

Table of Contents

CISCO SYSTEMS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

Summarized financial information by segment for the three and six months ended January 24, 2015 and January 25, 2014, based on the Company's internal management system and as utilized by the Company's Chief Operating Decision Maker ("CODM"), is as follows (in millions):

	Three Months Ended		Six Months Ended	
	January 24, 2015	January 25, 2014	January 24, 2015	January 25, 2014
Revenue:				
Americas	\$7,101	\$6,460	\$14,602	\$13,776
EMEA	3,091	2,896	6,093	5,829
APJC	1,744	1,799	3,486	3,635
Total	\$11,936	\$11,155	\$24,181	\$23,240
Gross margin:				
Americas	\$4,406	\$3,977	\$9,216	\$8,627
EMEA	1,910	1,870	3,825	3,758
APJC	1,052	993	2,077	2,072
Segment total	7,368	6,840	15,118	14,457
Unallocated corporate items	(278	) (889	) (695	) (1,099
Total	\$7,090	\$5,951	\$14,423	\$13,358

Revenue in the United States was \$6.1 billion and \$5.6 billion for the three months ended January 24, 2015 and January 25, 2014, respectively, and was \$12.7 billion and \$12.0 billion for the six months ended January 24, 2015 and January 25, 2014, respectively.

(b) Revenue for Groups of Similar Products and Services

The Company designs, manufactures, and sells Internet Protocol (IP)-based networking and other products related to the communications and IT industry and provides services associated with these products and their use. The Company groups its products and technologies into the following categories: Switching, NGN Routing, Collaboration, Service Provider Video, Data Center, Wireless, Security, and Other Products. These products, primarily integrated by Cisco IOS Software, link geographically dispersed local-area networks (LANs), metropolitan-area networks (MANs), and wide-area networks (WANs).

The following table presents revenue for groups of similar products and services (in millions):

	Three Months Ended		Six Months Ended	
	January 24, 2015	January 25, 2014	January 24, 2015	January 25, 2014
Revenue:				
Switching	\$3,616	\$3,258	\$7,462	\$6,998
NGN Routing	1,764	1,730	3,713	3,756
Collaboration	990	899	1,939	1,950
Service Provider Video	776	957	1,647	1,944
Data Center	846	605	1,539	1,206
Wireless	611	517	1,216	1,064
Security	416	393	871	758
Other	59	64	126	144
Product	9,078	8,423	18,513	17,820
Service	2,858	2,732	5,668	5,420
Total	\$11,936	\$11,155	\$24,181	\$23,240

Explanation of Responses:

The Company has made certain reclassifications to the product revenue amounts for prior periods to conform to the current period's presentation.

40

Table of Contents

CISCO SYSTEMS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

(c) Additional Segment Information

The majority of the Company's assets, excluding cash and cash equivalents and investments, as of January 24, 2015 and July 26, 2014 were attributable to its U.S. operations. The Company's total cash and cash equivalents and investments held by various foreign subsidiaries were \$49.8 billion and \$47.4 billion as of January 24, 2015 and July 26, 2014, respectively, and the remaining \$3.2 billion and \$4.7 billion at the respective period ends were available in the United States.

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):

	January 24, 2015	July 26, 2014
Property and equipment, net:		
United States	\$2,668	\$2,697
International	544	555
Total	\$3,212	\$3,252

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):

	Three Months Ended		Six Months Ended	
	January 24, 2015	January 25, 2014	January 24, 2015	January 25, 2014
Net income	\$2,397	\$1,429	\$4,225	\$3,425
Weighted-average shares—basic	5,117	5,294	5,115	5,336
Effect of dilutive potential common shares	43	33	44	47
Weighted-average shares—diluted	5,160	5,327	5,159	5,383
Net income per share—basic	\$0.47	\$0.27	\$0.83	\$0.64
Net income per share—diluted	\$0.46	\$0.27	\$0.82	\$0.64
Antidilutive employee share-based awards, excluded	83	278	156	252

Employee equity share options, unvested shares, and similar equity instruments granted by the Company 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, the amount of compensation cost for future service that the Company has not yet recognized, and the amount of tax benefits that would be recorded in additional paid-in capital when the award becomes deductible are collectively assumed to be used to repurchase shares.

Table of ContentsItem 2. Management's Discussion and Analysis of Financial Condition and Results of Operations
Forward-Looking Statements

This Quarterly Report on Form 10-Q, 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," "seeks," "estimates," "continues," "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 "Part II, 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

We design, manufacture, and sell Internet Protocol (IP) based networking products and services related to the communications and information technology (IT) industry. Our customers include businesses of all sizes, public institutions, telecommunications companies, other service providers and individuals. We connect people, process, data and things with products that transport data, voice, and video within buildings, across campuses, and around the world. We are a key strategic partner to companies that helps them as they seek to make the most of the Internet of Everything (IoE) and connect the unconnected.

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

	Three Months Ended				Six Months Ended			
	January 24, 2015	January 25, 2014	Variance		January 24, 2015	January 25, 2014	Variance	
Revenue	\$11,936	\$11,155	7.0	%	\$24,181	\$23,240	4.0	%
Gross margin percentage	59.4	% 53.3	% 6.1	pts	59.6	% 57.5	% 2.1	pts
Research and development	\$1,529	\$1,412	8.3	%	\$3,112	\$3,136	(0.8))%
Sales and marketing	\$2,308	\$2,277	1.4	%	\$4,823	\$4,688	2.9	%
General and administrative	\$490	\$451	8.6	%	\$994	\$966	2.9	%
Total R&D, sales and marketing, general and administrative	\$4,327	\$4,140	4.5	%	\$8,929	\$8,790	1.6	%
Total as a percentage of revenue	36.3	% 37.1	% (0.8)	) pts	36.9	% 37.8	% (0.9)	) pts
Amortization of purchased intangible assets included in operating expenses	\$72	\$71	1.4	%	\$143	\$136	5.1	%
Restructuring and other charges	\$69	\$73	(5.5)	)%	\$387	\$310	24.8	%
Operating income as a percentage of revenue	22.0	% 14.9	% 7.1	pts	20.5	% 17.7	% 2.8	pts
Income tax percentage	16.6	% 18.6	% (2.0)	) pts	19.3	% 20.3	% (1.0)	) pts
Net income	\$2,397	\$1,429	67.7	%	\$4,225	\$3,425	23.4	%
	20.1	% 12.8	% 7.3	pts	17.5	% 14.7	% 2.8	pts

Explanation of Responses:

Net income as a percentage of
revenue

Earnings per share—diluted	\$0.46	\$0.27	70.4	%	\$0.82	\$0.64	28.1	%
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42

Table of Contents

CISCO SYSTEMS, INC.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

Three Months Ended January 24, 2015 Compared with Three Months Ended January 25, 2014

In the second quarter of fiscal 2015, revenue increased by 7% as compared with the second quarter of fiscal 2014. Within the total revenue change, product revenue increased 8% while service revenue increased 5%. Total gross margin increased by 6.1 percentage points, primarily as a result of the \$655 million charge to product cost of sales recorded in the second quarter of fiscal 2014 for which there was no corresponding charge in fiscal 2015. As a percentage of revenue, research and development, sales and marketing, and general and administrative expenses, collectively, decreased by 0.8 percentage points. Operating income as a percentage of revenue increased by 7.1 percentage points. Diluted earnings per share increased by 70% from the prior year, driven by a 68% increase in net income, with the net income increase driven by the factors discussed above, as well as higher other income driven by higher net gains on investments, and a lower effective tax rate driven by the retroactive reinstatement of the U.S. federal R&D tax credit for calendar year 2014.

In the second quarter of fiscal 2015, total revenue increased by \$0.8 billion as compared with the second quarter of fiscal 2014. Revenue for the Americas increased by \$0.6 billion, driven in large part by higher product revenue in the United States. EMEA revenue increased by \$0.2 billion, led by higher product revenue in the United Kingdom. Revenue in our APJC segment decreased by \$0.1 billion, led by a product revenue decline in China. The challenges we encountered in certain emerging countries in the previous quarters continued in the second quarter of fiscal 2015. We experienced increased product revenue in the emerging countries of Brazil, India, and Mexico and decreased revenue in China and Russia, as the "BRICM" countries experienced, in the aggregate, product revenue growth of 2%. We believe that the limited growth we experienced in various emerging countries reflected the impact of economic and geopolitical challenges in these countries.

From a customer market standpoint, in the second quarter of fiscal 2015, while the service provider market continued to experience a decline in product revenue, we had solid product revenue growth in the public sector, enterprise and commercial markets. The product revenue increase in the public sector market was led by higher spending from the U.S. federal government.

From a product category perspective, the product revenue increase of 8% year-over-year was driven by product revenue growth in our core Switching and NGN Routing products which grew 11% and 2%, respectively. We also experienced 40% revenue growth from Data Center products due to continued strong customer demand. Our other major product categories experienced revenue changes ranging from an 18% increase in Wireless products to a 19% decrease in Service Provider Video. Service revenue increased by 5% year over year.

In summary, during the second quarter of fiscal 2015, we achieved solid and profitable growth despite encountering several of the challenges we have experienced in recent quarters, including reduced spending by our service provider customers and challenges in certain emerging countries. While we believe we are well positioned for an upturn in these areas, we are not expecting the challenges in service provider and certain emerging countries to improve for at least a few quarters.

Six Months Ended January 24, 2015 Compared with Six Months Ended January 25, 2014

Diluted earnings per share increased by 28% from the prior year, a result of both a 23% increase in net income and a decrease in diluted share count by 224 million shares. Revenue increased 4%, with product revenue increasing 4% and service revenue increasing 5%. Total gross margin increased by 2.1 percentage points driven in part by the \$655 million supplier component remediation charge recorded in the second quarter of fiscal 2014 partially offset by the unfavorable impact of the Rockstar patent portfolio charge of \$188 million (or 0.8 percentage points). As a percentage of revenue, research and development, sales and marketing, and general and administrative expenses collectively decreased by 0.9 percentage points. Operating income as a percentage of revenue increased by 2.8 percentage points.

Table of Contents

CISCO SYSTEMS, INC.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

Strategy and Focus Areas

Our strategy is to deliver the integrated architectures, solutions, and outcomes to help our customers grow, manage costs, and mitigate risk. We see our customers, in almost every industry, becoming increasingly reliant on technology—and specifically the network—to meet their business objectives and compete successfully in the market. Our focus continues to be on capitalizing on market transitions to maintain leadership in our core markets and to enter new markets where the network is foundational. We believe this focus best positions us to become a more relevant and trusted partner to our customers and to expand our share of our customers' IT spending. We are focused on driving the innovation, speed, agility, and efficiencies in our company required to deliver leading technology solutions for our customers and shareholder value for our investors.

Over the last few years, we have been working to transform our business to move from selling individual products and services to selling products and services integrated into architectures and solutions, as well as to meet customers' business outcomes. As a part of this transformation, we are making changes to how we are organized and how we deliver our technology. We believe these changes enable us to better meet our customers' requirements and help them stay ahead of market transitions.

For a full discussion of our strategy and focus areas, see Item 1. Business in our Annual Report on Form 10-K for the year ended July 26, 2014.

Other Key Financial Measures

The following is a summary of our other key financial measures for the second quarter and first six months of fiscal 2015 (in millions, except days sales outstanding in accounts receivable (DSO) and annualized inventory turns):

	January 24, 2015	July 26, 2014
Cash and cash equivalents and investments	\$53,022	\$52,074
Deferred revenue	\$14,021	\$14,142
DSO	35 days	38 days
Inventories	\$1,890	\$1,591
Annualized inventory turns	10.9	12.7
	Six Months Ended	
	January 24, 2015	January 25, 2014
Cash provided by operating activities	\$5,374	\$5,522
Repurchases of common stock—stock repurchase program	\$2,221	\$6,020
Dividends	\$1,947	\$1,810

Table of Contents

CISCO SYSTEMS, INC.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

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 in our Annual Report on Form 10-K for the year ended July 26, 2014, as updated as applicable in Note 2 to the Consolidated Financial Statements herein, 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.
- 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 subscription revenue ratably over the subscription 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 product and service 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 for multiple deliverables. According to the accounting guidance prescribed in Accounting Standards Codification (ASC) 605, Revenue Recognition, 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 facts and circumstances of the arrangement. 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. Some of our sales arrangements have multiple deliverables containing software and related software support components. Such sales arrangements are subject to the accounting guidance in ASC 985-605, Software-Revenue

Recognition.

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 the first six months of fiscal 2015, nor do we currently expect a material impact in the next 12 months on our revenue recognition due to any changes in our VSOE, TPE, or ESP.

45

Table of Contents

CISCO SYSTEMS, INC.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

Revenue deferrals relate to the timing of revenue recognition for specific transactions based on financing arrangements, service, support, and other factors. Financing arrangements may include sales-type, direct-financing, and operating leases, loans, and guarantees of third-party financing. Our deferred revenue for products was \$5.0 billion and \$4.5 billion as of January 24, 2015 and July 26, 2014, respectively. Technical support services revenue is deferred and recognized ratably over the period during which the services are to be performed, which typically is from one to three years. Advanced services revenue is recognized upon delivery or completion of performance. Our deferred revenue for services was \$9.0 billion and \$9.6 billion as of January 24, 2015 and July 26, 2014, respectively. We make sales to distributors which we refer to as two-tier systems of sales to the end customer. Revenue from distributors is recognized based on a sell-through method using information provided by them. Our distributors participate in various cooperative marketing and other programs, and we maintain estimated accruals and allowances for these programs. If actual credits received by our distributors under these programs were to deviate significantly from our estimates, which are based on historical experience, our revenue could be adversely affected.

Allowances for Receivables and Sales Returns

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

	January 24, 2015	July 26, 2014		
Allowance for doubtful accounts	\$270	\$265		
Percentage of gross accounts receivable	5.6	% 4.9		%
Allowance for credit loss—lease receivables	\$250	\$233		
Percentage of gross lease receivables ⁽¹⁾	7.0	% 6.2		%
Allowance for credit loss—loan receivables	\$85	\$98		
Percentage of gross loan receivables	5.1	% 5.8		%

⁽¹⁾ Calculated as allowance for credit loss on lease receivables as a percentage of gross lease receivables 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 and expected default frequency rates, which are published by major third-party credit-rating agencies and are generally 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 January 24, 2015 and July 26, 2014 was \$90 million and \$135 million, respectively, and was recorded as a reduction of our accounts receivable. 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.

46

Table of Contents

CISCO SYSTEMS, INC.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

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

Our inventory balance was \$1.9 billion and \$1.6 billion as of January 24, 2015 and July 26, 2014, respectively.

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. As of January 24, 2015, the liability for these purchase commitments was \$165 million, compared with \$162 million as of July 26, 2014, and was included in other current liabilities.

Our provision for inventory was \$21 million and \$35 million for the first six months of fiscal 2015 and 2014, respectively. The provision for the liability related to purchase commitments with contract manufacturers and suppliers was \$59 million and \$78 million for the first six months of fiscal 2015 and 2014, 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. 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, particularly in light of current macroeconomic uncertainties and conditions and the resulting potential for changes in future demand forecast.

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.

We have recorded a liability 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. In February 2014, on the basis of the growing number of failures as described in Note 12 (f) to the Consolidated Financial Statements, we decided to expand our approach, which resulted in an additional charge to product cost of sales of \$655 million being recorded for the second quarter of fiscal 2014. Estimating this liability is complex and subjective, and if we experience changes in a number of underlying assumptions and estimates such as a change in claims compared with our expectations, or if the cost of servicing these claims is different than expected, our estimated liability may be impacted.

Our liability for product warranties, included in other current liabilities, was \$474 million as of January 24, 2015, compared with \$446 million as of July 26, 2014. 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.

The provision for product warranties during the first six months of fiscal 2015 and 2014 was \$355 million and \$356 million, respectively. 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.

Table of Contents

CISCO SYSTEMS, INC.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

Fair Value Measurements

Our fixed income and publicly traded equity securities, collectively, are reflected in the Consolidated Balance Sheets at a fair value of \$48.2 billion as of January 24, 2015, compared with \$45.3 billion as of July 26, 2014. Our fixed income investment portfolio as of January 24, 2015 consisted primarily of high quality investment-grade securities. See Note 8 to the Consolidated Financial Statements.

As described more fully in Note 9 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 the periods presented, 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 January 24, 2015. We had no Level 3 assets measured at fair value on a recurring basis as of January 24, 2015.

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.

There were no impairment charges on our investments in publicly traded equity securities in the first six months of fiscal 2015, while \$11 million of such impairment charges were recognized in earnings for the first six months of fiscal 2014. There were no impairment charges on our investments in fixed income securities in the first six months of fiscal 2015 and 2014. 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.

48

Table of Contents

CISCO SYSTEMS, INC.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

We also have investments in privately held companies, some of which are in the startup or development stages. Our investments in privately held companies as of January 24, 2015 were \$857 million, compared with \$899 million as of July 26, 2014, 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. Our impairment charges on investments in privately held companies were \$3 million and \$10 million for the first six months of fiscal 2015 and 2014, respectively.

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 January 24, 2015 and July 26, 2014 was \$24.4 billion and \$24.2 billion, respectively. 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 the first six months of fiscal 2015 and 2014.

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. For the first six months of fiscal 2015, impairment charges of \$56 million on purchased intangible assets were recognized in earnings, while there were no such impairment charges in the first six months of fiscal 2014. 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 16.6% and 18.6% in the second quarter of fiscal 2015 and 2014, respectively. Our effective tax rate was 19.3% and 20.3% in the first six months of fiscal 2015 and 2014, respectively. 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.

Table of Contents

CISCO SYSTEMS, INC.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

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 expiration of or lapses in the R&D tax credit or domestic manufacturing deduction laws; by expiration of or lapses in tax incentives; by transfer pricing adjustments, including the effect of acquisitions on our intercompany R&D cost-sharing arrangement and 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 possible changes to the taxation of earnings of our foreign subsidiaries, the deductibility of expenses attributable to foreign income, or 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 34 countries, including the United States, is contemplating changes to numerous long-standing tax principles. These contemplated changes, if finalized and adopted by countries, will increase tax uncertainty and may adversely affect 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 and in some cases is wholly exempt from tax. 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.

50

Table of Contents

CISCO SYSTEMS, INC.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

RESULTS OF OPERATIONS

Revenue

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

	Three Months Ended				Six Months Ended					
	January 24, 2015	January 25, 2014	Variance in Dollars	Variance in Percent	January 24, 2015	January 25, 2014	Variance in Dollars	Variance in Percent		
Revenue:										
Product	\$9,078	\$8,423	\$655	7.8 %	\$18,513	\$17,820	\$693	3.9 %		
Percentage of revenue	76.1 %	75.5 %			76.6 %	76.7 %				
Service	2,858	2,732	126	4.6 %	5,668	5,420	248	4.6 %		
Percentage of revenue	23.9 %	24.5 %			23.4 %	23.3 %				
Total	\$11,936	\$11,155	\$781	7.0 %	\$24,181	\$23,240	\$941	4.0 %		

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):

	Three Months Ended				Six Months Ended					
	January 24, 2015	January 25, 2014	Variance in Dollars	Variance in Percent	January 24, 2015	January 25, 2014	Variance in Dollars	Variance in Percent		
Revenue:										
Americas	\$7,101	\$6,460	\$641	9.9 %	\$14,602	\$13,776	\$826	6.0 %		
Percentage of revenue	59.5 %	57.9 %			60.4 %	59.3 %				
EMEA	3,091	2,896	195	6.7 %	6,093	5,829	264	4.5 %		
Percentage of revenue	25.9 %	26.0 %			25.2 %	25.1 %				
APJC	1,744	1,799	(55)	(3.1)%	3,486	3,635	(149)	(4.1)%		
Percentage of revenue	14.6 %	16.1 %			14.4 %	15.6 %				
Total	\$11,936	\$11,155	\$781	7.0 %	\$24,181	\$23,240	\$941	4.0 %		

Three Months Ended January 24, 2015 Compared with Three Months Ended January 25, 2014

For the second quarter of fiscal 2015, as compared with the second quarter of fiscal 2014, total revenue increased by 7%. Product revenue increased by 8%, while service revenue increased by 5%. Our total revenue reflected growth in our Americas and EMEA geographic segments, while revenue declined in the APJC segment. The emerging countries of BRICM, in the aggregate, experienced a slower product revenue growth of 2%, with growth in Brazil, India, and Mexico, partially offset by decreases in the other two countries.

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. It is possible that our revenue in the second quarter of fiscal 2015 may have been adversely affected by the depreciation of

the local currency relative to the U.S. dollar, although as noted above, such indirect effects are difficult to measure. In addition to the impact of macroeconomic factors, 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 our 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 of our 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.

51

Table of Contents

CISCO SYSTEMS, INC.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

Six Months Ended January 24, 2015 Compared with Six Months Ended January 25, 2014

For the first six months of fiscal 2015, as compared with the first six months of fiscal 2014, total revenue increased by 4%. Product revenue increased 4%, while service revenue increased by 5%. Our total revenue reflected growth in our Americas and EMEA geographic segments, while revenue declined in the APJC segment. The emerging countries of BRICM, in the aggregate, experienced a 3% product revenue decline, with declines in China and Russia, partially offset by increases in the other three countries.

Product Revenue by Segment

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

	Three Months Ended			Six Months Ended					
	January 24, 2015	January 25, 2014	Variance in Dollars	Variance in Percent	January 24, 2015	January 25, 2014	Variance in Dollars	Variance in Percent	
Product revenue:									
Americas	\$5,243	\$4,676	\$567	12.1 %	\$10,927	\$10,209	\$718	7.0 %	
Percentage of product revenue	57.8 %	55.6 %			59.1 %	57.3 %			
EMEA	2,480	2,328	152	6.5 %	4,876	4,709	167	3.5 %	
Percentage of product revenue	27.3 %	27.6 %			26.3 %	26.4 %			
APJC	1,355	1,419	(64)	(4.5)%	2,710	2,902	(192)	(6.6)%	
Percentage of product revenue	14.9 %	16.8 %			14.6 %	16.3 %			
Total	\$9,078	\$8,423	\$655	7.8 %	\$18,513	\$17,820	\$693	3.9 %	

Americas

Three Months Ended January 24, 2015 Compared with Three Months Ended January 25, 2014

Product revenue in the Americas segment increased by 12%, led by strong growth in the public sector market and solid growth in the enterprise and commercial markets. Product revenue increased in the U.S. public sector market, led by higher sales to the U.S. federal government and, to a lesser extent, higher sales to state and local governments. Within the Americas segment, we continued to experience a product revenue decline in the service provider market. From a country perspective, product revenue increased by 12% in the United States, 44% in Brazil, 26% in Mexico and 1% in Canada.

Six Months Ended January 24, 2015 Compared with Six Months Ended January 25, 2014

The increase in product revenue in the Americas segment of 7% was led by solid growth in the public sector, enterprise and commercial markets. The product revenue growth in the public sector market was due primarily to higher sales to the U.S. federal government and, to a lesser extent, higher sales to state and local governments. Product revenue decreased in the service provider market. From a country perspective, product revenue increased by 7% in the United States, 24% in Brazil, 19% in Mexico and 1% in Canada.

EMEA

Three Months Ended January 24, 2015 Compared with Three Months Ended January 25, 2014

Product revenue in the EMEA segment increased by 7%, led by growth in the enterprise and commercial markets, and to a lesser extent, growth in the service provider market. We experienced a slight product revenue decline in the public sector market. Product revenue from emerging countries within EMEA increased by 2% and product revenue for the remainder of EMEA, which primarily consists of countries in Western Europe, grew by 8%.

Six Months Ended January 24, 2015 Compared with Six Months Ended January 25, 2014

Product revenue in the EMEA segment increased by 4%, driven by growth in the commercial market and, to a lesser degree, in the enterprise and service provider markets. We experienced a slight product revenue decline in the public sector market. Product revenue from emerging countries within EMEA decreased by 2%, led by a 20% decrease in Russia. Product revenue for the remainder of EMEA grew by 6%.

52

Table of Contents

CISCO SYSTEMS, INC.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

APJC

Three Months Ended January 24, 2015 Compared with Three Months Ended January 25, 2014

The decrease in product revenue in the APJC segment of 5% was led by a significant decline in the service provider market and, to a lesser extent, in the public sector market. These decreases were partially offset by solid growth in the commercial and enterprise markets. From a country perspective, we experienced year-over-year product revenue declines of 20% in China and 10% in Japan. These decreases were partially offset by product revenue growth of 21% in India and 3% in Australia.

Six Months Ended January 24, 2015 Compared with Six Months Ended January 25, 2014

Product revenue in the APJC segment decreased by 7%. The product revenue decline was led by a significant decline in the service provider market and, to a lesser degree, in the public sector market. These decreases were partially offset by slow growth in the commercial and enterprise markets. From a country perspective, product revenue decreased by 22% in China, 7% in Japan and 5% in Australia. We experienced product revenue growth of 25% in India.

Table of Contents

CISCO SYSTEMS, INC.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

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. Our product categories consist of the following categories (with subcategories in parentheses): Switching (fixed switching, modular switching, and storage); NGN Routing (high-end routers, mid-range and low-end routers, and other NGN Routing products); Collaboration (unified communications, Cisco TelePresence, and conferencing); Service Provider Video (infrastructure, video software, and solutions and cable access); Data Center; Wireless; Security; and Other Products. The Other Products category consists primarily of emerging technology products and other networking products.

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

	Three Months Ended			Six Months Ended					
	January 24, 2015	January 25, 2014	Variance in Dollars	Variance in Percent	January 24, 2015	January 25, 2014	Variance in Dollars	Variance in Percent	
Product revenue:									
Switching	\$3,616	\$3,258	\$358	11.0 %	\$7,462	\$6,998	\$464	6.6 %	
Percentage of product revenue	39.8 %	38.7 %			40.3 %	39.3 %			
NGN Routing	1,764	1,730	34	2.0 %	3,713	3,756	(43)	(1.1)%	
Percentage of product revenue	19.4 %	20.5 %			20.1 %	21.1 %			
Collaboration	990	899	91	10.1 %	1,939	1,950	(11)	(0.6)%	
Percentage of product revenue	10.9 %	10.7 %			10.5 %	10.9 %			
Service Provider Video	776	957	(181)	(18.9)%	1,647	1,944	(297)	(15.3)%	
Percentage of product revenue	8.5 %	11.4 %			8.9 %	10.9 %			
Data Center	846	605	241	39.8 %	1,539	1,206	333	27.6 %	
Percentage of product revenue	9.3 %	7.2 %			8.3 %	6.8 %			
Wireless	611	517	94	18.2 %	1,216	1,064	152	14.3 %	
Percentage of product revenue	6.7 %	6.1 %			6.6 %	6.0 %			
Security	416	393	23	5.9 %	871	758	113	14.9 %	
Percentage of product revenue	4.6 %	4.7 %			4.7 %	4.3 %			
Other	59	64	(5)	(7.8)%	126	144	(18)	(12.5)%	
Percentage of product revenue	0.8 %	0.7 %			0.6 %	0.7 %			
Total	\$9,078	\$8,423	\$655	7.8 %	\$18,513	\$17,820	\$693	3.9 %	

Certain reclassifications have been made to the prior period amounts to conform to the current period's presentation.

Switching

Three Months Ended January 24, 2015 Compared with Three Months Ended January 25, 2014

Revenue in our Switching product category increased by 11%, or \$358 million, driven by a 17%, or \$337 million, increase in revenue from our LAN fixed-configuration switches. Revenue from our LAN fixed-configuration switches increased due to the continued adoption of Cisco Catalyst 3650 Series Switches and Cisco Catalyst 3850 Series

Switches. Higher revenue from fixed-configuration Cisco Nexus Series Switches also contributed to the increase. We also experienced a 31%, or \$36 million, increase in sales of storage products within this category. Partially offsetting these increases was a decrease in revenue from our modular switches of 1%, or \$15 million, driven by lower sales of Cisco Nexus 7000 Series Switches and Cisco Catalyst 6500-E Series Switches.

54

Table of Contents

CISCO SYSTEMS, INC.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

Six Months Ended January 24, 2015 Compared with Six Months Ended January 25, 2014

The increase in revenue in our Switching product category of 7%, or \$464 million, was driven by a 12%, or \$507 million, increase in revenue from our LAN fixed-configuration switches and, to a lesser extent, a 45%, or \$96 million, increase in sales of storage products. Revenue from LAN fixed-configuration switches increased due to higher sales of most of our Cisco Nexus Series Switches and Cisco Catalyst Series Switches within this category. We experienced a decrease in revenue from our modular switches of 6%, or \$139 million, driven by lower sales of Cisco Catalyst 6500-E Series Switches and Cisco Nexus 7000 Series Switches.

NGN Routing

Three Months Ended January 24, 2015 Compared with Three Months Ended January 25, 2014

The increase in revenue in our NGN Routing product category of 2%, or \$34 million, was driven by a 5%, or \$53 million, increase in revenue from our high-end router products and a 3%, or \$19 million, increase in revenue from our midrange and low-end router products. These increases were partially offset by a 28%, or \$38 million, decrease in revenue from what we categorize as other NGN Routing products. Within the high-end router product category, we experienced increased sales of most of our products within our Cisco Aggregation Services Routers category and the adoption of our Cisco Network Convergence System platform partially offset by lower sales of Cisco Carrier Routing System products and our legacy high-end router products. The increase in revenue from our midrange and low-end router products was due to higher sales of our Cisco Integrated Services Routers products. Revenue from other NGN Routing products decreased due to lower sales of certain optical networking products.

Six Months Ended January 24, 2015 Compared with Six Months Ended January 25, 2014

Revenue in our NGN Routing product category decreased by 1%, or \$43 million, driven by a 34%, or \$108 million, decrease in revenue from other NGN Routing products and a 2%, or \$31 million, decrease in revenue from our midrange and low-end router products. These decreases were partially offset by a 4%, or \$96 million, increase in revenue from our high-end router products. Revenue from other NGN Routing products decreased due to lower sales of certain optical networking products. The decrease in revenue from our midrange and low-end router products was due to lower sales of certain of our access products, partially offset by higher sales of our Cisco Integrated Services Routers products. Revenue from high-end router product increased due to an increase in revenue from most of our products within our Cisco Aggregation Services Routers category and the adoption of our Cisco Network Convergence System platform, partially offset by lower sales of Cisco Carrier Routing System products and our legacy high-end router products.

Collaboration

Three Months Ended January 24, 2015 Compared with Three Months Ended January 25, 2014

Overall, revenue in our Collaboration product category increased by 10%, or \$91 million, primarily due to increased revenue from our Unified Communications and Cisco TelePresence products, driven by higher revenue in endpoint products as a result of new product introductions. These increases were partially offset by decreased revenue from our conferencing products. We continue to increase the amount of deferred revenue related to our Collaboration product category.

Six Months Ended January 24, 2015 Compared with Six Months Ended January 25, 2014

Revenue in our Collaboration product category decreased by 1%, or \$11 million, primarily due to decreased revenue from our Cisco TelePresence products and, to a lesser extent, a slight decrease in revenue from our conferencing products, partially offset by increased revenue from our Unified Communications products.

Service Provider Video

Three Months Ended January 24, 2015 Compared with Three Months Ended January 25, 2014

Revenue in our Service Provider Video product category decreased by 19%, or \$181 million, driven by a decrease in sales of our Service Provider Video infrastructure products. The revenue decline in Service Provider Video infrastructure products was due primarily to lower sales of set-top boxes.

Six Months Ended January 24, 2015 Compared with Six Months Ended January 25, 2014

Explanation of Responses:

The decrease in revenue from our Service Provider Video product category of 15%, or \$297 million, was driven by a 25%, or \$269 million, decrease in sales of our Service Provider Video infrastructure products, due primarily to lower sales of set-top boxes. We also experienced a decrease in revenue from cable access products within this product category.

55

Table of Contents

CISCO SYSTEMS, INC.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

Data Center

Three Months Ended January 24, 2015 Compared with Three Months Ended January 25, 2014

We continued to experience solid growth in our Data Center product category, which grew by 40%, or \$241 million, with sales growth of our Cisco Unified Computing System products occurring across all geographic segments and customer markets. The increase was due in large part to the continued momentum we are experiencing in both data center and cloud environments, as current customers increase their data center build-outs and as new customers deploy these offerings.

Six Months Ended January 24, 2015 Compared with Six Months Ended January 25, 2014

We experienced solid growth in our Data Center product category, which grew by 28%, or \$333 million, with sales growth of our Cisco Unified Computing System products occurring across all geographic segments and customer markets. The increase in this product category was driven by similar factors as discussed in the three month period immediately above.

Wireless

Three Months Ended January 24, 2015 Compared with Three Months Ended January 25, 2014

Revenue in our Wireless product category increased by 18%, or \$94 million, driven by continued growth in Meraki combined with continued strength in our 802.11ac portfolio. We continue to increase the proportion of recurring revenue in our Wireless product category.

Six Months Ended January 24, 2015 Compared with Six Months Ended January 25, 2014

Revenue in our Wireless product category increased by 14%, or \$152 million, due primarily to higher sales of Meraki products and 802.11ac products.

Security

Three Months Ended January 24, 2015 Compared with Three Months Ended January 25, 2014

Revenue in our Security product category experienced growth of 6%, or \$23 million, driven by higher Network Security sales as a result of product integration with Sourcefire, which we acquired in the first quarter of fiscal 2014. This increase was partially offset by decrease in revenue from our Content Security products due to lower sales of Web and E-mail security products. Our software and subscription sales continue to drive an increase in the proportion of recurring revenue in our Security product category.

Six Months Ended January 24, 2015 Compared with Six Months Ended January 25, 2014

Revenue in our Security product category was up 15%, or \$113 million, driven primarily by sales of Sourcefire products and, to a lesser extent, by higher sales of our high-end Firewall products within our Network Security product portfolio.

Other Products

We experienced a year-over-year decrease in revenue in our Other Products category for the second quarter and first six months of fiscal 2015 due in large part to the decrease in sales of our other networking products.

Table of Contents

CISCO SYSTEMS, INC.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

Service Revenue by Segment

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

	Three Months Ended				Six Months Ended				
	January 24, 2015	January 25, 2014	Variance in Dollars	Variance in Percent	January 24, 2015	January 25, 2014	Variance in Dollars	Variance in Percent	
Service revenue:									
Americas	\$1,858	\$1,784	\$74	4.1 %	\$3,675	\$3,567	\$108	3.0 %	
Percentage of service revenue	65.0 %	65.3 %			64.8 %	65.8 %			
EMEA	611	568	43	7.6 %	1,217	1,120	97	8.7 %	
Percentage of service revenue	21.4 %	20.8 %			21.5 %	20.7 %			
APJC	389	380	9	2.4 %	776	733	43	5.9 %	
Percentage of service revenue	13.6 %	13.9 %			13.7 %	13.5 %			
Total	\$2,858	\$2,732	\$126	4.6 %	\$5,668	\$5,420	\$248	4.6 %	

Three Months Ended January 24, 2015 Compared with Three Months Ended January 25, 2014

Service revenue increased across all of our geographic segments. Worldwide technical support services revenue increased by 4% and worldwide advanced services revenue increased by 6%, driven by growth in subscription revenues. Technical support service revenue experienced growth across all geographic segments, led by growth in our EMEA segment. Renewals and technical support service contract initiations associated with product sales provided an installed base of equipment being serviced which, in concert with new service offerings, were the primary factors driving the revenue increases. Advanced services revenue, which relates to consulting support services for specific customer network needs, grew across all geographic segments, led by solid growth in our EMEA segment.

Six Months Ended January 24, 2015 Compared with Six Months Ended January 25, 2014

Service revenue grew by 5%, with growth across all of our geographic segments. Worldwide technical support services revenue increased by 5% and worldwide advanced services experienced 4% revenue growth. Technical support services revenue grew across all geographic segments, led by growth in our EMEA segment. Advanced services revenue also grew across all geographic segments, led by solid growth in our EMEA segment.

Table of Contents

CISCO SYSTEMS, INC.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

Gross Margin

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

	Three Months Ended				Six Months Ended				
	AMOUNT		PERCENTAGE		AMOUNT		PERCENTAGE		
	January 24, 2015	January 25, 2014	January 24, 2015	January 25, 2014	January 24, 2015	January 25, 2014	January 24, 2015	January 25, 2014	
Gross margin:									
Product	\$5,272	\$4,100	58.1	% 48.7	% \$10,788	\$9,750	58.3	% 54.7	%
Service	1,818	1,851	63.6	% 67.8	% 3,635	3,608	64.1	% 66.6	%
Total	\$7,090	\$5,951	59.4	% 53.3	% \$14,423	\$13,358	59.6	% 57.5	%

Product Gross Margin

The following table summarizes the key factors that contributed to the change in product gross margin percentage for the second quarter and first six months of fiscal 2015 as compared with the corresponding prior year periods:

	Product Gross Margin Percentage		
	Three Months Ended	Six Months Ended	
Fiscal 2014	48.7	% 54.7	%
Supplier component remediation charge	7.8	% 3.7	%
Productivity ⁽¹⁾	3.6	% 2.8	%
Mix of products sold	1.4	% 1.1	%
Product pricing	(3.0)	)% (2.7))%
Amortization of purchased intangible assets	(0.4)	)% (0.3))%
Rockstar patent portfolio charge	—	% (1.0))%
Fiscal 2015	58.1	% 58.3	%

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

Three Months Ended January 24, 2015 Compared with Three Months Ended January 25, 2014

Product gross margin increased by 9.4 percentage points as compared with the second quarter of fiscal 2014.

The increase in product gross margin was primarily a result of the \$655 million charge to product cost of sales recorded in the second quarter fiscal 2014 related to the expected cost of remediation of issues with memory components in certain products sold in prior fiscal years, for which there was no corresponding charge in fiscal 2015. Benefits from productivity and the mix of products sold also contributed to the increase. The productivity benefits we experienced in the second quarter of fiscal 2015 were driven by value engineering efforts; favorable component pricing; and continued operational efficiency in manufacturing operations. Value engineering is the process by which production costs are reduced through component redesign, board configuration, test processes, and transformation processes. The mix of products sold was favorable primarily as a result of a revenue decrease from our relatively lower margin Service Provider Video products, partially offset by a revenue increase in our relatively lower margin Cisco Unified Computing System products.

The various factors contributing to the product gross margin increase were partially offset by unfavorable impacts from product pricing, which were driven by typical market factors and impacted each of our geographic segments and customer markets. Our product gross margin for the second quarter of fiscal 2015 was also negatively impacted by impairment charges related to acquisition-related intangible assets.

Our future gross margins could be impacted by our product mix and could be adversely affected by further growth in sales of products that have lower gross margins, such as Cisco Unified Computing System products. Our gross margins may also be impacted by the geographic mix of our revenue and may be adversely affected by product pricing attributable to competitive factors. Additionally, our manufacturing-related costs may be negatively impacted by

constraints in our supply chain, which in turn could negatively affect gross margin. If any of the preceding factors that in the past have negatively impacted our gross margins arise in future periods, our gross margins could continue to decline.

58

Table of Contents

CISCO SYSTEMS, INC.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

Six Months Ended January 24, 2015 Compared with Six Months Ended January 25, 2014

Product gross margin increased by 3.6 percentage points as compared with the first six months of fiscal 2014. The increase was driven by the \$655 million charge to product cost of sales for the second quarter of fiscal 2014 related to the expected cost of remediation of issues with memory components in certain products sold in prior fiscal years. Additionally, gross margin increased due to benefits from productivity improvements driven by similar factors as discussed in the three-month period immediately above and the mix of products sold. The shift in the mix of products sold was primarily a result of revenue decreases from our relatively lower margin Service Provider Video products, partially offset by increased in revenue from our relatively lower margin Cisco Unified Computing System products. These factors were partially offset by unfavorable impacts from product pricing, the unfavorable impact of the \$188 million charge to product cost of sales recorded in the first quarter fiscal 2015 related to the Rockstar patent portfolio, and impairment charges related to acquisition-related intangible assets.

Service Gross Margin

Three Months Ended January 24, 2015 Compared with Three Months Ended January 25, 2014

Our service gross margin percentage decreased by 4.2 percentage points compared with the second quarter of fiscal 2014 due to increased costs such as headcount-related costs associated with higher investments in security and cloud managed services and higher variable compensation expense. Higher partner delivery costs also contributed to increased 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 and 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.

Six Months Ended January 24, 2015 Compared with Six Months Ended January 25, 2014

Service gross margin percentage decreased by 2.5 percentage points as compared with the first six months of fiscal 2014, driven by increased cost impacts such as headcount-related costs and partner 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.

Table of Contents

CISCO SYSTEMS, INC.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

Gross Margin by Segment

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

	Three Months Ended				Six Months Ended			
	AMOUNT		PERCENTAGE		AMOUNT		PERCENTAGE	
	January 24, 2015	January 25, 2014	January 24, 2015	January 25, 2014	January 24, 2015	January 25, 2014	January 24, 2015	January 25, 2014
Gross margin:								
Americas	\$4,406	\$3,977	62.0 %	61.6 %	\$9,216	\$8,627	63.1 %	62.6 %
EMEA	1,910	1,870	61.8 %	64.6 %	3,825	3,758	62.8 %	64.5 %
APJC	1,052	993	60.3 %	55.2 %	2,077	2,072	59.6 %	57.0 %
Segment total	7,368	6,840	61.7 %	61.3 %	15,118	14,457	62.5 %	62.2 %
Unallocated corporate items ⁽¹⁾	(278)	(889)			(695)	(1,099)		
Total	\$7,090	\$5,951	59.4 %	53.3 %	\$14,423	\$13,358	59.6 %	57.5 %

⁽¹⁾ The unallocated corporate items for the periods presented include the effects of amortization and impairments of acquisition-related intangible assets, share-based compensation expense, significant litigation and other contingencies, 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.

Three Months Ended January 24, 2015 Compared with Three Months Ended January 25, 2014

The Americas segment experienced a gross margin percentage increase due to productivity improvements from lower overall manufacturing costs and, to a lesser extent, a favorable mix impact. The favorable mix impact in this geographic segment was driven by lower sales of our relatively lower margin Service Provider Video products, partially offset by an increase in revenue from our relatively lower margin Cisco Unified Computing System products. Partially offsetting these favorable impacts to gross margin were negative impacts from pricing.

The gross margin percentage decrease in our EMEA segment was due primarily to lower productivity and unfavorable impacts from pricing, partially offset by a favorable mix impact. The favorable mix impact was driven by an increase in revenue from certain of our higher margin core products. Lower service gross margin also contributed to the decrease in gross margin in this segment.

Our APJC segment gross margin percentage increased due to productivity improvements and a favorable mix impact, partially offset by unfavorable impacts from pricing and lower service gross margin. The favorable mix impact was driven by a decrease in revenue from our relatively lower margin Service Provider Video products and an increase in revenue from certain of our higher margin core products.

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. Our product and service gross margins may be impacted by economic downturns or uncertain economic conditions as well as our movement into new market opportunities, and could decline if any of the factors that impact our gross margins are adversely affected in future periods.

Six Months Ended January 24, 2015 Compared with Six Months Ended January 25, 2014

We experienced a gross margin percentage increase in our Americas segment due to productivity improvements and a favorable mix impact, partially offset by unfavorable impacts from pricing. The favorable mix impact in this geographic segment was driven by lower sales of our relatively lower margin Service Provider Video products, partially offset by an increase in revenue from our relatively lower margin Cisco Unified Computing System products. The gross margin percentage decrease in our EMEA segment was primarily due to negative impacts from pricing within this segment and, to a lesser extent, lower productivity. These factors were partially offset by a slightly favorable mix impact. The favorable mix impact was driven by an increase in revenue from certain of our higher margin core products.

The APJC segment gross margin percentage increased due to productivity improvements and a favorable mix impact, partially offset by unfavorable impacts from pricing. The favorable mix impact was driven by a decrease in revenue from our relatively lower margin Service Provider Video products and an increase in revenue from certain of our higher margin core products.

60

Table of Contents

CISCO SYSTEMS, INC.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

Factors That May Impact Revenue and Gross Margin

Product revenue may continue to be affected by factors, including global economic downturns and related market uncertainty, that have resulted in reduced IT-related capital spending in certain segments within our enterprise, service provider, public sector, and commercial markets; changes in the geopolitical environment and global economic conditions; competition, including price-focused competitors from Asia, especially from China; new product introductions; sales cycles and product implementation cycles; changes in the mix of our customers between service provider and enterprise markets; changes in the mix of direct sales and indirect sales; variations in sales channels; and final acceptance criteria of the product, system, or solution as specified by the customer. Sales to the service provider market have been and may be in the future characterized by large and sporadic purchases, especially relating to our router sales and sales of certain products within our Collaboration, Data Center, and Service Provider Video product categories. In addition, service provider customers typically have longer implementation cycles; require a broader range of services, including network design services; and often have acceptance provisions that can lead to a delay in revenue recognition. Certain of our customers in certain emerging countries also tend to make large and sporadic purchases, and the revenue related to these transactions may similarly be affected by the timing of revenue recognition. As we focus on new market opportunities, customers may require greater levels of financing arrangements, service, and support, especially in certain emerging countries, which in turn may result in a delay in the timing of revenue recognition. To improve customer satisfaction, we continue to focus on managing our manufacturing lead-time performance, which 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.

Product revenue may also be adversely affected by fluctuations in demand for our products, especially with respect to telecommunications service providers and Internet businesses, whether or not driven by any slowdown in capital expenditures in the service provider market; price and product competition in the communications and information technology industry; introduction and market acceptance of new technologies and products; adoption of new networking standards; and financial difficulties experienced by our customers. We may, from time to time, experience manufacturing issues that create a delay in our suppliers' ability to provide specific components, resulting in delayed shipments. To the extent that manufacturing issues and any related component shortages result in delayed shipments in the future, and particularly in periods when we and our suppliers are operating at higher levels of capacity, it is possible that revenue for a quarter could be adversely affected if such matters are not remediated within the same quarter. For additional factors that may impact product revenue, see "Part II, Item 1A. Risk Factors."

Our distributors participate in various cooperative marketing and other programs. Increased sales to our distributors generally result in greater difficulty in forecasting the mix of our products and, to a certain degree, the timing of orders from our customers. We recognize revenue for sales to our distributors generally based on a sell-through method using information provided by them, and we maintain estimated accruals and allowances for all cooperative marketing and other programs.

Product gross margin may be adversely affected in the future by changes in the mix of products sold, including periods of increased growth of some of our lower margin products; introduction of new products, including products with price-performance advantages and new business models for our offerings such as other-as-a-service ("XaaS"); our ability to reduce production costs; entry into new markets, including markets with different pricing structures and cost structures, as a result of internal development or through acquisitions; changes in distribution channels; price competition, including competitors from Asia, especially those from China; changes in geographic mix of our product revenue; the timing of revenue recognition and revenue deferrals; sales discounts; increases in material or labor costs, including share-based compensation expense; excess inventory and obsolescence charges; warranty costs; changes in shipment volume; loss of cost savings due to changes in component pricing; effects of value engineering; inventory holding charges; and the extent to which we successfully execute on our strategy and operating plans. Additionally, our manufacturing-related costs may be negatively impacted by constraints in our supply chain. Service gross margin

may be impacted by various factors such as the change in mix between technical support services and advanced services; the timing of technical support service contract initiations and renewals; share-based compensation expense; and the timing of our strategic investments in headcount and resources to support this business.

61

Table of Contents

CISCO SYSTEMS, INC.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

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):

	Three Months Ended				Six Months Ended			
	January 24, 2015	January 25, 2014	Variance in Dollars	Variance in Percent	January 24, 2015	January 25, 2014	Variance in Dollars	Variance in Percent
Research and development	\$1,529	\$1,412	\$117	8.3 %	\$3,112	\$3,136	\$(24)	(0.8)%
Percentage of revenue	12.8 %	12.7 %			12.9 %	13.5 %		
Sales and marketing	2,308	2,277	31	1.4 %	4,823	4,688	135	2.9 %
Percentage of revenue	19.3 %	20.4 %			19.9 %	20.2 %		
General and administrative	490	451	39	8.6 %	994	966	28	2.9 %
Percentage of revenue	4.1 %	4.0 %			4.1 %	4.2 %		
Total	\$4,327	\$4,140	\$187	4.5 %	\$8,929	\$8,790	\$139	1.6 %
Percentage of revenue	36.3 %	37.1 %			36.9 %	37.8 %		

R&D Expenses

R&D expenses increased for the second quarter of fiscal 2015, as compared with the second quarter of fiscal 2014, primarily due to higher headcount-related expenses driven by increased variable compensation expense as a result of our financial performance. Higher discretionary spending and higher contracted services, to a lesser extent, also contributed to the increase.

The decrease in R&D expenses for the first six months of fiscal 2015, as compared with the first six months of fiscal 2014, was primarily due to higher compensation expense recorded in the first six months of fiscal 2014 in connection with our acquisition of the remaining interest in Insieme partially offset by higher headcount-related expenses and higher contracted services. The higher headcount-related expenses were due to increased variable compensation expense partially offset by efficiencies related to our restructuring actions.

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.

Sales and Marketing Expenses

Sales and marketing expenses increased for the second quarter of fiscal 2015, as compared with the second quarter of fiscal 2014, due to higher headcount-related expenses and, to a lesser extent, higher contracted services, partially offset by lower share-based compensation expense. Higher headcount-related expenses were due to increased variable compensation expense as a result of our financial performance.

Sales and marketing expenses increased for the first six months of fiscal 2015, as compared with the first six months of fiscal 2014, due to higher headcount-related expenses, driven by increased variable compensation expense, and higher discretionary spending.

G&A Expenses

G&A expenses increased in the second quarter of fiscal 2015, as compared with the second quarter of fiscal 2014, primarily due to increased variable compensation expense as a result of our financial performance and timing of corporate-level expenses, which tend to vary from period to period.

Explanation of Responses:

G&A expenses increased in the first six months of fiscal 2015, as compared with the corresponding period in fiscal 2014, primarily due to increased variable compensation expense as a result of our financial performance and timing of corporate-level expenses, which tend to vary from period to period, partially offset by higher compensation expense recorded in the first six months of fiscal 2014 in connection with our acquisition of the remaining interest in Insieme.

Effect of Foreign Currency

In the second quarter of fiscal 2015, foreign currency fluctuations, net of hedging, decreased the combined R&D, sales and marketing, and G&A expenses by \$60 million, or approximately 1.5%, compared with the second quarter of fiscal 2014.

In the first six months of fiscal 2015, foreign currency fluctuations, net of hedging, decreased the combined R&D, sales and marketing, and G&A expenses by \$56 million, or approximately 0.6%, compared with the first six months of fiscal 2014.

Table of Contents

CISCO SYSTEMS, INC.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

Headcount

Our headcount decreased by approximately 2,135 employees in the second quarter of fiscal 2015 and decreased by approximately 3,930 in the first six months of fiscal 2015, as compared with the total headcount at the end of fiscal 2014. The decrease was due to headcount reductions from our workforce reduction under the Fiscal 2015 Plan. These headcount reductions were partially offset by headcount additions from targeted hiring in engineering, services and sales, and also by headcount additions from our recent acquisitions.

Share-Based Compensation Expense

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

	Three Months Ended		Six Months Ended	
	January 24, 2015	January 25, 2014	January 24, 2015	January 25, 2014
Cost of sales—product	\$11	\$12	\$22	\$22
Cost of sales—service	34	40	71	73
Share-based compensation expense in cost of sales	45	52	93	95
Research and development	105	108	224	200
Sales and marketing	114	141	261	264
General and administrative	42	47	101	101
Restructuring and other charges	2	(1)	(2)	(4)
Share-based compensation expense in operating expenses	263	295	584	561
Total share-based compensation expense	\$308	\$347	\$677	\$656

The decrease in share-based compensation expense for the second quarter of fiscal 2015, as compared with the second quarter of fiscal 2014, was due primarily to the timing of annual RSU grants partially offset by higher expense associated with PRSUs.

The increase in share-based compensation expense for the first six months of fiscal 2015, as compared with the corresponding period in fiscal 2014, was due primarily to higher expense associated with the PRSUs and equity awards assumed with respect to our recent acquisitions, partially offset by the timing of annual RSU grants.

Amortization of Purchased Intangible Assets

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

	Three Months Ended		Six Months Ended	
	January 24, 2015	January 25, 2014	January 24, 2015	January 25, 2014
Amortization of purchased intangible assets:				
Cost of sales	\$242	\$189	\$431	\$363
Operating expenses	72	71	143	136
Total	\$314	\$260	\$574	\$499

Amortization of purchased intangible assets increased for the second quarter and first six months of fiscal 2015, as compared with the corresponding periods of fiscal 2014, due to the impairment charges of approximately \$56 million recorded in the second quarter of fiscal 2015. The impairment charges were primarily due to reductions in expected future cash flows related to certain of our technology intangible assets.

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.

63

Table of Contents

CISCO SYSTEMS, INC.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

Restructuring and Other Charges

In the second quarter and first six months of fiscal 2015, we incurred within operating expenses restructuring and other charges of approximately \$69 million and \$387 million, respectively, which were related primarily to employee severance charges for employees impacted by our workforce reduction under the Fiscal 2015 Plan. We expect the remaining charges under this plan to be incurred within the remainder of fiscal 2015. We plan to reinvest substantially all of the cost savings from the restructuring actions in key growth areas of our business such as data center, software, security, and cloud. The overall cost savings from these restructuring actions were not material for the periods presented and are not expected to be material for future periods.

In the second quarter and first six months of fiscal 2014, we incurred within operating expenses net restructuring and other charges of \$73 million and \$310 million, respectively, which were related primarily to employee severance charges for employees impacted by our workforce reduction under the Fiscal 2014 Plan. See Note 5 to the Consolidated Financial Statements.

Operating Income

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

	Three Months Ended		Six Months Ended		
	January 24, 2015	January 25, 2014	January 24, 2015	January 25, 2014	
Operating income	\$2,622	\$1,667	\$4,964	\$4,122	
Operating income as a percentage of revenue	22.0	% 14.9	% 20.5	% 17.7	%

For the second quarter of fiscal 2015, as compared with the second quarter of fiscal 2014, operating income increased by 57%, and as a percentage of revenue operating income increased by 7.1 percentage points. The increase resulted from an increase in revenue and a gross margin percentage increase, with the gross margin increase driven in large part by the \$655 million supplier component remediation charge (or 5.9 percentage points) recorded in the second quarter of fiscal 2014 for which there was no corresponding charge in fiscal 2015.

In the first six months of fiscal 2015, as compared with the first six months of fiscal 2014, operating income increased by 20%, and as a percentage of revenue operating income increased by 2.8 percentage points. The increase resulted from the following: an increase in revenue; a gross margin percentage increase, driven in part by the \$655 million supplier component remediation charge (or 2.8 percentage points) recorded in the second quarter of fiscal 2014 partially offset by the unfavorable impact of the Rockstar patent portfolio charge of \$188 million (or 0.8 percentage points); and higher compensation expense recorded in the first six months of fiscal 2014 in connection with our acquisition of the remaining interest in Insieme.

Interest and Other Income (Loss), Net

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

	Three Months Ended			Six Months Ended		
	January 24, 2015	January 25, 2014	Variance in Dollars	January 24, 2015	January 25, 2014	Variance in Dollars
Interest income	\$189	\$169	\$20	\$368	\$338	\$30
Interest expense	(139)	(136)	(3)	(278)	(276)	(2)
Interest income (expense), net	\$50	\$33	\$17	\$90	\$62	\$28

For the second quarter and first six months of fiscal 2015, interest income increased by 12% and 9%, respectively, compared with the corresponding periods in fiscal 2014, driven by an increase in our portfolio of cash, cash equivalents, and fixed income investments. Interest expense in the second quarter and first six months of fiscal 2015, compared with the corresponding periods in fiscal 2014, was higher driven by higher average debt balance.

Table of Contents

CISCO SYSTEMS, INC.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

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

	Three Months Ended			Six Months Ended		
	January 24,	January 25,	Variance	January 24,	January 25,	Variance
	2015	2014	in Dollars	2015	2014	in Dollars
Gains (losses) on investments, net:						
Publicly traded equity securities	\$60	\$69	\$(9)	\$56	\$144	\$(88)
Fixed income securities	9	13	(4)	20	21	(1)
Total available-for-sale investments	69	82	(13)	76	165	(89)
Privately held companies	134	(35)	169	101	(66)	167
Net gains (losses) on investments	203	47	156	177	99	78
Other gains (losses), net	(2)	8	(10)	2	12	(10)
Other income (loss), net	\$201	\$55	\$146	\$179	\$111	\$68

The decrease in total net gains on available-for-sale investments in the second quarter and first six months of fiscal 2015, as compared with the corresponding periods in fiscal 2014, was primarily attributable to lower gains on publicly traded equity securities in the current periods 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 for the second quarter and first six months of fiscal 2015, as compared with the corresponding periods in fiscal 2014, was primarily due to a gain of \$126 million related to the reorganization of our investment in VCE and the absence of losses from VCE for the second quarter of fiscal 2015 and lower losses for the first six months of fiscal 2015 related to this investment under the equity method. We ceased accounting for VCE under the equity method in October 2014.

The change in other gains (losses), net in the second quarter and first six months of fiscal 2015, as compared with the corresponding periods in fiscal 2014, was driven by lower gains from equity derivative instruments, and for the six month period this impact was partially offset by net favorable foreign exchange impacts.

Provision for Income Taxes

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, higher than anticipated in countries that have higher tax rates, and expiration of or lapses in tax incentives. Our provision for income taxes does not include provisions for U.S. income taxes and foreign withholding taxes associated with the repatriation of undistributed earnings of certain foreign subsidiaries that we intend to reinvest indefinitely in our foreign subsidiaries. If these earnings were distributed from the foreign subsidiaries to the United States 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 U.S. income taxes (subject to an adjustment for foreign tax credits) and foreign withholding 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 and in some cases is wholly exempt from tax. Our failure to meet these commitments could adversely impact our provision for income taxes.

The provision for income taxes resulted in an effective tax rate of 16.6% for the second quarter of fiscal 2015, compared with 18.6% for the second quarter of fiscal 2014, which resulted in a net 2.0 percentage point decrease in the effective tax rate for the second quarter of fiscal 2015 as compared with the second quarter of fiscal 2014. The provision for income taxes resulted in an effective tax rate of 19.3% for the first six months of fiscal 2015, as compared with an effective tax rate of 20.3% for the first six months of fiscal 2014, which resulted in a net 1.0 percentage point decrease in the effective tax rate for the first six months of fiscal 2015 as compared with the first six months of fiscal 2014. The decrease in the effective tax rates for both the second quarter and first six months of fiscal 2015, as compared with the second quarter and first six months of fiscal 2014, was primarily due to the retroactive reinstatement of the U.S. federal R&D tax credit for calendar year 2014 in the second quarter of fiscal 2015.

Table of Contents

CISCO SYSTEMS, INC.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

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):

	January 24, 2015	July 26, 2014	Increase (Decrease)
Cash and cash equivalents	\$4,797	\$6,726	\$(1,929)
Fixed income securities	46,377	43,396	2,981
Publicly traded equity securities	1,848	1,952	(104)
Total	\$53,022	\$52,074	\$948

The net increase in cash and cash equivalents and investments in the first six months of fiscal 2015 was primarily the result of cash provided by operating activities of \$5.4 billion and proceeds from the issuance of common stock of \$1.2 billion pursuant to employee stock incentive plans. These sources of cash were partially offset by the repurchase of common stock of \$2.2 billion under the stock repurchase program, cash dividends paid of \$1.9 billion, capital expenditures of \$0.6 billion, repayment of debt of \$0.5 billion and net cash paid for acquisitions of \$0.2 billion.

Our total in cash and cash equivalents and investments held by various foreign subsidiaries was \$49.8 billion and \$47.4 billion as of January 24, 2015 and July 26, 2014, respectively. Under current tax laws and regulations, if these assets were to be distributed from the foreign subsidiaries to the United States in the form of dividends or otherwise, we would be subject to additional U.S. income taxes (subject to an adjustment for foreign tax credits) and foreign withholding taxes. The balance of cash and cash equivalents and investments available in the United States as of January 24, 2015 and July 26, 2014 was \$3.2 billion and \$4.7 billion, respectively.

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):

	Six Months Ended	
	January 24, 2015	January 25, 2014
Net cash provided by operating activities	\$5,374	\$5,522
Acquisition of property and equipment	(550)	(577)
Free cash flow	\$4,824	\$4,945

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, excess tax benefits resulting from share-based compensation, and the timing and amount of tax and other payments. For additional discussion, see "Part II, 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

66

Table of Contents

CISCO SYSTEMS, INC.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

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):

Quarter Ended	DIVIDENDS		STOCK REPURCHASE PROGRAM			TOTAL
	Per Share	Amount	Shares	Weighted-Average Price per Share	Amount	
Fiscal 2015						
January 24, 2015	\$0.19	\$974	44	\$ 27.63	\$1,208	\$2,182
October 25, 2014	\$0.19	\$973	41	\$ 24.58	\$1,013	\$1,986
Fiscal 2014						
July 26, 2014	\$0.19	\$974	61	\$ 25.11	\$1,514	\$2,488
April 26, 2014	\$0.19	\$974	90	\$ 22.24	\$2,005	\$2,979
January 25, 2014	\$0.17	\$896	185	\$ 21.73	\$4,020	\$4,916
October 26, 2013	\$0.17	\$914	84	\$ 23.65	\$2,000	\$2,914

On February 11, 2015, our Board of Directors declared a quarterly dividend of \$0.21 per common share to be paid on April 22, 2015 to all shareholders of record as of the close of business on April 2, 2015. Any future dividends will be subject to the approval of our Board of Directors.

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

	January 24, 2015	July 26, 2014	Increase (Decrease)
Accounts receivable, net	\$4,541	\$5,157	\$(616)
DSO	35	38	(3)

Our accounts receivable net, as of January 24, 2015 decreased by approximately 12% compared with the end of fiscal 2014. Our DSO as of January 24, 2015 was lower by 3 days compared with the end of fiscal 2014, primarily due to product billings being more linear in the second quarter of fiscal 2015 compared with the fourth quarter of fiscal 2014.

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

	January 24, 2015	July 26, 2014	Increase (Decrease)
Inventories	\$1,890	\$1,591	\$299
Annualized inventory turns	10.9	12.7	(1.8)
Purchase commitments with contract manufacturers and suppliers	\$4,257	\$4,169	\$88

Inventory as of January 24, 2015 increased by 19% from our inventory balance at the end of fiscal 2014, and for the same period purchase commitments with contract manufacturers and suppliers increased by approximately 2%. On a combined basis, inventories and purchase commitments with contract manufacturers and suppliers increased by 7% compared with the end of fiscal 2014.

The inventory increase was primarily due to higher levels of raw materials primarily from insourcing of certain memory components. We believe our inventory and purchase commitments levels are in line with our current demand forecasts.

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.

67

Table of Contents

CISCO SYSTEMS, INC.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

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. 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. Our purchase commitments are for short-term product manufacturing requirements as well as for commitments to suppliers to secure manufacturing capacity.

We record a liability, included in other current liabilities, 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. The purchase commitments for inventory are expected to be primarily fulfilled within one year. 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 We measure our net balance sheet exposure position related to our financing receivables and financing guarantees by reducing the total of gross financing receivables and financing guarantees by the associated allowances for credit loss and deferred revenue. As of January 24, 2015, our net balance sheet exposure position related to financing receivables and financing guarantees was as follows (in millions):

	FINANCING RECEIVABLES				FINANCING GUARANTEES			TOTAL
	Lease Receivables	Loan Receivables	Financed Service Contracts and Other	Total	Channel Partner	End-User Customers	Total	
January 24, 2015								
Financing receivables less unearned income	\$3,391	\$ 1,674	\$ 3,069	\$8,134	\$316	\$ 155	\$471	\$8,605
Allowance for credit loss	(250)	(85)	(40)	(375)	—	—	—	(375)
Deferred revenue	(10)	(13)	(1,530)	(1,553)	(148)	(121)	(269)	(1,822)
Net balance sheet exposure	\$3,131	\$ 1,576	\$ 1,499	\$6,206	\$168	\$ 34	\$202	\$6,408

Financing Receivables Financing receivables less unearned income decreased by 3% compared with the end of fiscal 2014. The change was primarily due to a 4% decrease in both lease receivables and financed service contracts and other, as well as a 1% decrease in loan receivables. We provide financing to certain end-user customers and channel partners to enable sales of our products, services, and networking solutions. These financing arrangements include leases, financed service contracts, and loans. Arrangements related to leases are generally collateralized by a security interest in the underlying assets. Lease receivables include sales-type and direct-financing leases. We also provide certain qualified customers financing for long-term service contracts, which primarily relate to technical support services and advanced services. 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. 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. These financing arrangements facilitate the working capital requirements of the channel partners, and in some cases, we guarantee a portion of these arrangements. 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.

68

Table of Contents

CISCO SYSTEMS, INC.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

Deferred Revenue Related to Financing Receivables and Guarantees The majority of the deferred revenue in the preceding table is related to financed service contracts. The majority of the revenue related to financed service contracts, which primarily relates to technical support services, is deferred as the revenue related to financed service contracts is recognized ratably over the period during which the related services are to be performed. A portion of the revenue related to lease and loan receivables is also deferred and included in deferred product revenue based on revenue recognition criteria not currently having been met.

Borrowings

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

	Maturity Date	January 24, 2015	July 26, 2014
Senior notes:			
Floating-rate notes:			
Three-month LIBOR plus 0.05%	September 3, 2015	\$850	\$850
Three-month LIBOR plus 0.28%	March 3, 2017	1,000	1,000
Three-month LIBOR plus 0.50%	March 1, 2019	500	500
Fixed-rate notes:			
2.90%	November 17, 2014	—	500
5.50%	February 22, 2016	3,000	3,000
1.10%	March 3, 2017	2,400	2,400
3.15%	March 14, 2017	750	750
4.95%	February 15, 2019	2,000	2,000
2.125%	March 1, 2019	1,750	1,750
4.45%	January 15, 2020	2,500	2,500
2.90%	March 4, 2021	500	500
3.625%	March 4, 2024	1,000	1,000
5.90%	February 15, 2039	2,000	2,000
5.50%	January 15, 2040	2,000	2,000
Total		\$20,250	\$20,750

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 January 24, 2015.

On November 17, 2014, upon the maturity of our 2014 Fixed-Rate Notes (2.90%), we repaid an aggregate principal amount of \$500 million.

Other Debt Other debt as of January 24, 2015 and July 26, 2014 included secured borrowings associated with customer financing arrangements. The amount of borrowings outstanding under these arrangements was \$7 million and \$12 million as of January 24, 2015 and July 26, 2014, respectively.

Commercial Paper In fiscal 2011, we established a short-term debt financing program of up to \$3.0 billion 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 outstanding as of each of January 24, 2015 and July 26, 2014.

Credit Facility On February 17, 2012, 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 February 17, 2017. Any advances under the credit agreement will accrue interest at rates that are equal to, based on certain conditions, either (i) the higher of the Federal Funds rate plus 0.50%, Bank of America's "prime rate" as announced from time to time, or one-month LIBOR plus 1.00% or (ii) LIBOR 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. The credit agreement requires that we comply with certain covenants, including that we maintain an interest coverage ratio as defined in the agreement.

As of January 24, 2015, 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.

69

Table of Contents

CISCO SYSTEMS, INC.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

We may also, upon the agreement of either the 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 by up to two additional years, or up to February 17, 2019.

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

	January 24, 2015	July 26, 2014	Increase (Decrease)	
Service	\$9,020	\$9,640	\$(620))
Product	5,001	4,502	499)
Total	\$14,021	\$14,142	\$(121))
Reported as:				
Current	\$9,369	\$9,478	\$(109))
Noncurrent	4,652	4,664	(12))
Total	\$14,021	\$14,142	\$(121))

The 6% decrease in deferred service revenue was driven by the timing of multiyear arrangements, an increase in customers paying technical support service contracts over time and the impact of ongoing amortization of deferred service revenue. The 11% increase in deferred product revenue was primarily due to increased deferrals related to subscription revenue arrangements and also was due, to a lesser extent, to an increase in shipments not having met revenue recognition criteria as of January 24, 2015.

Contractual Obligations

Operating Leases

We lease office space in many U.S. locations. Outside the United States, larger leased sites include sites in Belgium, Canada, China, France, Germany, India, Israel, Japan, Norway, and the United Kingdom. We also lease equipment and vehicles. The future minimum lease payments under all of our noncancelable operating leases with an initial term in excess of one year as of January 24, 2015 were \$1.1 billion.

Other Commitments

In connection with our business combinations and asset purchases, 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.

Insieme Networks, Inc. In the third quarter of fiscal 2012, we made an investment in Insieme, an early stage company focused on research and development in the data center market. As set forth in the agreement between Cisco and Insieme, this investment included \$100 million of funding and a license to certain of our technology. Immediately prior to the call option exercise and acquisition described below, we owned approximately 83% of Insieme as a result of these investments and have consolidated the results of Insieme in our Consolidated Financial Statements. In connection with this investment, we entered into a put/call option agreement that provided us with the right to purchase the remaining interests in Insieme. In addition, the noncontrolling interest holders could require us to purchase their shares upon the occurrence of certain events.

During the first quarter of fiscal 2014, we exercised our call option and entered into an agreement to purchase the remaining interests in Insieme. The acquisition closed in the second quarter of fiscal 2014, at which time the former noncontrolling interest holders became eligible to receive up to two milestone payments, which will be determined using agreed-upon formulas based primarily on revenue for certain of Insieme's products. During the six months ended January 24, 2015 and January 25, 2014, we recorded compensation expense of \$104 million and \$311 million, respectively, related to the fair value of the vested portion of amounts that are expected to be earned by the former noncontrolling interest holders. Continued vesting and changes to the fair value of the amounts probable of being earned will result in adjustments to the recorded compensation expense in future periods. Based on the terms of the agreement, we have determined that the maximum amount that could be recorded as compensation expense by us is

approximately \$845 million (which includes the \$520 million that has been expensed to date), net of forfeitures. The milestone payments, if earned, are expected to be paid primarily during fiscal 2016 and fiscal 2017.

Other Funding Commitments 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 \$230 million as of January 24, 2015, compared with \$255 million as of July 26, 2014.

70

Table of Contents

CISCO SYSTEMS, INC.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

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 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 customer financings, and we have determined that as of January 24, 2015 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."

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 the six months ended January 24, 2015 and January 25, 2014 was \$0.6 billion and \$0.9 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. As of January 24, 2015 and July 26, 2014, we had no outstanding securities lending transactions. We believe these arrangements do not present a material risk or impact to our liquidity requirements.

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, 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.

Table of Contents

Item 3. 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 January 24, 2015. Our fixed income investments are held for purposes other than trading. Our fixed income investments are not leveraged as of January 24, 2015. We monitor our interest rate and credit risks, including our credit exposures to specific rating categories and to individual issuers. As of January 24, 2015, approximately 70% of our fixed income securities balance consisted of U.S. government and U.S. government agency securities. We believe the overall credit quality of our portfolio is strong.

Financing Receivables As of January 24, 2015, our financing receivables had a carrying value of \$7.8 billion, compared with \$8.1 billion as of July 26, 2014. As of January 24, 2015, a hypothetical 50 basis points ("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 January 24, 2015, we had \$20.3 billion in principal amount of senior notes outstanding, which consisted of \$2.4 billion floating-rate notes and \$17.9 billion fixed-rate notes. The carrying amount of the senior notes was \$20.5 billion, and the related fair value based on market prices was \$22.3 billion. As of January 24, 2015, a hypothetical 50 BPS increase or decrease in market interest rates would change the fair value of the fixed-rate debt, excluding the \$10.4 billion of hedged debt, by a decrease or increase of approximately \$0.4 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 January 24, 2015 and July 26, 2014 are as follows (in millions):

	VALUATION OF SECURITIES GIVEN AN X% DECREASE IN EACH STOCK'S PRICE			FAIR VALUE AS OF JANUARY 24, 2015	VALUATION OF SECURITIES GIVEN AN X% INCREASE IN EACH STOCK'S PRICE		
	(30)%	(20)%	(10)%		10%	20%	30%
Publicly traded equity securities	\$1,063	\$1,215	\$1,367	\$ 1,519	\$1,671	\$1,823	\$1,975

	VALUATION OF SECURITIES GIVEN AN X%	FAIR VALUE AS OF JULY 26,	VALUATION OF SECURITIES GIVEN AN X%
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	DECREASE IN EACH STOCK'S PRICE			2014	INCREASE IN EACH STOCK'S PRICE		
	(30)%	(20)%	(10)%		10%	20%	30%
Publicly traded equity securities	\$ 1,144	\$ 1,307	\$ 1,471	\$ 1,634	\$ 1,797	\$ 1,961	\$ 2,124

72

Table of Contents

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 January 24, 2015, the total carrying amount of our investments in privately held companies was \$857 million, compared with \$899 million at July 26, 2014. 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 as of respective period-ends are summarized in U.S. dollar equivalents as follows (in millions):

	January 24, 2015		July 26, 2014	
	Notional Amount	Fair Value	Notional Amount	Fair Value
Forward contracts:				
Purchased	\$2,038	\$(41)	\$2,635	\$(3)
Sold	\$563	\$4	\$896	\$2
Option contracts:				
Purchased	\$671	\$—	\$494	\$5
Sold	\$554	\$(48)	\$466	\$(2)

We conduct business globally in numerous currencies. The direct effect of foreign currency fluctuations on revenue has not been material because our sales are 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 sales are influenced by many factors in addition to the impact of such currency fluctuations.

Approximately 65% of our operating expenses are U.S.-dollar denominated. In the first six months of fiscal 2015, foreign currency fluctuations, net of hedging, decreased our combined R&D, sales and marketing, and G&A expenses by \$56 million, or approximately 0.6%, compared with the first six months of fiscal 2014. To reduce variability in operating expenses and service cost of sales caused by non-U.S.-dollar denominated operating expenses and costs, we 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. Our forward and option contracts generally have the following maturities:

	Maturities
Forward and option contracts—forecasted transactions related to operating expenses and service cost of sales	Up to 18 months
Forward contracts—current assets and liabilities	Up to 3 months
Forward contracts—net investments in foreign subsidiaries	Up to 6 months
Forward contracts—long-term customer financings	Up to 2 years

We do not enter into foreign exchange forward or option contracts for trading purposes.

73

Table of Contents

Item 4. 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.

Changes in internal control over financial reporting. There was no change in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during our second quarter of fiscal 2015 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

Brazil Brazilian authorities have investigated our Brazilian subsidiary and certain of its current and 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. In the first quarter of fiscal 2013, the Brazilian federal tax authorities asserted an additional claim against our Brazilian subsidiary based on a theory of joint liability with respect to an alleged underpayment of income taxes, social taxes, interest, and penalties by a Brazilian distributor.

The asserted claims by Brazilian federal tax authorities are for calendar years 2003 through 2008, 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 approximately \$335 million for the alleged evasion of import and other taxes, approximately \$1.3 billion for interest, and approximately \$1.5 billion for various penalties, all determined using an exchange rate as of January 24, 2015. 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.

Russia and the Commonwealth of Independent States At the request of the U.S. Securities and Exchange Commission (SEC) and the U.S. Department of Justice, we are conducting an investigation into allegations which we and those agencies received regarding possible violations of the U.S. Foreign Corrupt Practices Act involving business activities of Cisco's operations in Russia and certain of the Commonwealth of Independent States, and by certain resellers of our products in those countries. We take any such allegations very seriously and are fully cooperating with and sharing the results of our investigation with the SEC and the Department of Justice. While the outcome of our investigation is currently not determinable, we do not expect that it will have a material adverse effect on our consolidated financial position, results of operations, or cash flows. The countries that are the subject of the investigation collectively comprise less than 2% of our revenues.

Rockstar We and some of our service provider customers were subject to patent claims asserted in December 2013 in the Eastern District of Texas and the District of Delaware by subsidiaries of the Rockstar Consortium ("Rockstar").

Rockstar, whose members include Apple, Microsoft, LM Ericsson, Sony, and Blackberry, had purchased a portfolio of patents out of the Nortel Networks' bankruptcy proceedings (the "Nortel Portfolio"). In connection with this matter, during the first quarter of fiscal 2015 we recorded a charge to product cost of sales of \$188 million.

In December 2014, RPX Corporation ("RPX") and Rockstar entered into an agreement, which closed on January 28, 2015, resulting in over 30 technology companies, including Cisco and the various service provider customers described above, obtaining a license to the patents owned by Rockstar. We paid approximately \$300 million in connection with this transaction, with the payment recorded against the amount previously reserved and as an intangible asset to be amortized over its estimated useful life. In connection with the closing of the transaction, Rockstar dismissed all litigation it had brought against the participating companies.

Table of Contents

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 II, Item 1A. Risk Factors-We may be found to infringe on intellectual property rights of others” herein.

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. The descriptions below include any material changes to and supersede the description of the risk factors affecting our business previously disclosed in “Part I, Item 1A. Risk Factors” of our Annual Report on Form 10-K for the fiscal year ended July 26, 2014.

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 telecommunications 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, including in our newer product categories such as data center and collaboration and in emerging technologies, as well as the adoption of new standards
- New business models for our offerings, such as XaaS, where costs are borne up front while revenue is recognized over time
- Variations in sales channels, product costs, or mix of products sold
- 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
- Share-based compensation expense
- 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

Table of Contents

- 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 the U.S. federal budget including the effect of the sequestration beginning in 2013, global central bank monetary policy, the instability in the geopolitical environment in many parts of the world 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, sales in several of our emerging countries decreased in recent periods, including the first half of fiscal 2015, and we expect that this weakness will continue for at least a few quarters.

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 GROWTH AREAS AS WELL AS MAINTAINING LEADERSHIP IN ROUTING, SWITCHING AND 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 growth areas, such as data center virtualization, software, security, and cloud, while also focusing on maintaining leadership in routing, switching and 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.

Table of Contents

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 fiscal 2014 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 level of product gross margins declined in recent periods and may continue to decline and be adversely affected by numerous 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 for our offerings such as XaaS
- 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
- Excess inventory and inventory holding charges

Table of Contents

- Obsolescence charges
- Changes in shipment volume
- The timing of revenue recognition and revenue deferrals
- Increased cost, 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 SALES 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 products in our newer product categories such as Data Center, Collaboration, and Service Provider Video, in addition to longer sales cycles. At various times in the past including fiscal 2014 and the first quarter of fiscal 2015, we experienced significant weakness in sales to service providers, sometimes lasting over extended periods of time as market conditions have fluctuated. We expect that the weakness we experienced in fiscal 2014 and the first half of fiscal 2015 will continue for at least a few quarters. 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 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

Table of Contents

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 categories such as data center and collaboration and in key growth areas. For example, as products related to network programmability, such as software-defined-networking products, become more prevalent, we expect to face increased competition from companies who 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. Our competitors include Alcatel-Lucent; Amazon Web Services LLC; Arista Networks, Inc.; ARRIS Group, Inc.; Aruba Networks, Inc.; Avaya Inc.; Brocade Communications Systems, Inc.; Check Point Software Technologies Ltd.; Citrix Systems, Inc.; Dell Inc.; LM Ericsson Telephone Company; Extreme Networks, Inc.; F5 Networks, Inc.; FireEye, Inc.; Fortinet, Inc.; Hewlett-Packard Company; Huawei Technologies Co., Ltd.; International Business Machines Corporation; Juniper Networks, Inc.; Lenovo Group Limited; Microsoft Corporation; Palo Alto Networks, Inc.; Polycom, Inc.; Riverbed Technology, Inc.; Ruckus Wireless, Inc.; Symantec Corporation; 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 whom 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, application-specific integrated circuits offering advanced services, standards based protocols, cloud computing and virtualization, the convergence of technologies within the enterprise

Table of Contents

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 provide a broad range of networking and communications products and services
- Product performance
- Price
- The ability to introduce new products, including 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.

Table of Contents

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

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, 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

Table of Contents

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 are aimed at meeting the requirements that a network capable of multiple-party, collaborative interaction would demand, and the investments we have made and our architectural approach are designed to enable the increased use of the network as the platform for all forms of communications and IT. For example, in fiscal 2009 we launched our Cisco Unified Computing System (UCS), our next-generation enterprise data center platform architected to unite computing, network, storage access and virtualization resources in a single system, which is designed to address the fundamental transformation occurring in the enterprise data center. While our Cisco UCS offering remains a significant focus area for us, several market transitions are also shaping our strategies and investments.

One such market transition we are focusing on is the move towards more programmable, flexible and virtual networks. In our view, this evolution is in its very early stages, and we believe the successful products and solutions in this market will combine application-specific integrated circuits (ASICs), hardware and software elements together. Other examples include our focus on the IoE market transition, a potentially significant transition in the IT industry, and a transition in cloud where we have announced plans to architect the Cisco Intercloud solution.

The process of developing new technology, including technology related to more programmable, flexible and virtual networks and technology related to other market transitions, including IoE 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.

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 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.

82

Table of Contents

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.

In August 2014, as part of our strategy of continuing to invest in growth, innovation and talent, while also managing costs and driving efficiencies, we announced a restructuring plan. We began taking action under this plan in the first quarter of fiscal 2015. 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 growth areas, such as data center virtualization, software, security, and cloud, and we also intend to focus on maintaining leadership in routing, switching and 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 transition to IoE, 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 IoE, 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, such as Scientific-Atlanta, WebEx, Starent, Tandberg and NDS Group Limited

Table of Contents

- 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, as we did in fiscal 2006 when we issued and sold \$6.5 billion in senior unsecured notes to fund our acquisition of Scientific-Atlanta
- 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 intercompany R&D cost sharing arrangement and 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. Please 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 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

Table of Contents

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 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. Although sales in several of our emerging countries decreased in recent periods, including in fiscal 2014 and the first half of fiscal 2015, several of our emerging countries generally have been relatively fast growing, and we have announced plans to expand our commitments and expectations in certain of those countries. We expect that the weakness we experienced in recent periods in several emerging countries will continue for at least a few quarters. 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 the U.S. federal budget including the effect of the sequestration beginning in 2013; global

central bank monetary policy; issues related to the political relationship between the United States and other countries which 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; environmental and trade protection measures 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

Table of Contents

- 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, 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-

86

Table of Contents

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.

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

Table of Contents

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 proposed "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 current and 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

Table of Contents

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 the first quarter of fiscal 2013, the Brazilian federal tax authorities asserted an additional claim against our Brazilian subsidiary based on a theory of joint liability with respect to an alleged underpayment of income taxes, social taxes, interest, and penalties by a Brazilian distributor. The asserted claims by Brazilian federal tax authorities are for calendar years 2003 through 2008 and the related 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 approximately \$335 million for the alleged evasion of import and other taxes, approximately \$1.3 billion for interest, and approximately \$1.5 billion for various penalties, all determined using an exchange rate as of January 24, 2015. 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 Item 1, "Legal Proceedings," contained in Part II of this report.

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 expiration of or lapses in the R&D tax credit or domestic manufacturing deduction laws; by expiration of or lapses in tax incentives; by transfer pricing adjustments, including the effect of acquisitions on our intercompany R&D cost sharing arrangement and 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 possible changes to the taxation of earnings of our foreign subsidiaries, the deductibility of expenses attributable to foreign income, or 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 of 34 countries including the United States, is contemplating changes to numerous long-standing tax principles. These contemplated changes, if finalized and adopted by countries, will increase tax uncertainty and may adversely affect 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 and in some cases is wholly exempt from tax. 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 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 COMPUTER VIRUSES OR TERRORISM MAY DISRUPT OUR OPERATIONS AND HARM OUR OPERATING RESULTS

Despite our implementation of network security measures our servers are vulnerable to computer viruses, break-ins, and similar disruptions from unauthorized tampering with our computer systems. Any such event could have a material adverse effect on our business, operating results, and financial condition. Efforts to limit the ability of malicious third parties to disrupt the operations of the Internet or undermine our own security efforts may meet with resistance. 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 widespread blackouts 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.

Table of Contents**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 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 the second quarter of fiscal 2015, we have senior unsecured notes outstanding in an aggregate principal amount of \$20.3 billion that mature at specific dates from calendar year 2015 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 \$3.0 billion, and we had no commercial paper notes outstanding under this program as of January 24, 2015. The outstanding senior unsecured notes bear fixed-rate interest payable semiannually, except \$2.35 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, including cash currently held offshore. 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.

Table of Contents

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

(a) None.

(b) None.

(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
October 26, 2014 to November 22, 2014	2	\$ 26.63	2	\$ 7,489
November 23, 2014 to December 20, 2014	14	\$ 27.20	14	\$ 7,116
December 21, 2014 to January 24, 2015	28	\$ 27.91	28	\$ 6,334
Total	44	\$ 27.63	44	

On September 13, 2001, we announced that our Board of Directors had authorized a stock repurchase program. As of January 24, 2015, our Board of Directors had authorized the repurchase of up to \$97 billion of common stock under this program. As of January 24, 2015, we had repurchased and retired 4.4 billion shares of our common stock at an average price of \$20.73 per share for an aggregate purchase price of \$90.7 billion since inception of the stock repurchase program, and the remaining authorized amount for stock repurchases under this program was \$6.3 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).

Table of Contents

Item 3. Defaults Upon Senior Securities
None.

Item 4. Mine Safety Disclosures
Not Applicable.

Item 5. Other Information
None.

Item 6. Exhibits

The following documents are filed as Exhibits to this report:

- 31.1 Rule 13a-14(a)/15d-14(a) Certification of Principal Executive Officer
- 31.2 Rule 13a-14(a)/15d-14(a) Certification of Principal Financial Officer
- 32.1 Section 1350 Certification of Principal Executive Officer
- 32.2 Section 1350 Certification of Principal Financial Officer
- 10.1 Cisco Systems, Inc. Employee Stock Purchase Plan (incorporated by reference to Exhibit 10.1 of Form 8-K (File No. 000-18225) filed November 24, 2014)
- 10.2 Letter Agreement by and between Cisco Systems, Inc. and Kelly A. Kramer (incorporated by reference to Exhibit 10.2 of Form 8-K (File No. 000-18225) filed November 24, 2014)
- 10.3 Transition and Separation Agreement by and between Cisco Systems, Inc. and Frank A. Calderoni (incorporated by reference to Exhibit 10.3 of Form 8-K (File No. 000-18225) filed November 24, 2014)
- 10.4 Cisco Systems, Inc. 2005 Stock Incentive Plan including related form agreements
- 10.5 Cisco Systems, Inc. Deferred Compensation Plan, as amended
- 101.INS XBRL Instance Document
- 101.SCH XBRL Taxonomy Extension Schema Document
- 101.CAL XBRL Taxonomy Extension Calculation Linkbase Document
- 101.DEF XBRL Taxonomy Extension Definition Linkbase Document
- 101.LAB XBRL Taxonomy Extension Label Linkbase Document
- 101.PRE XBRL Taxonomy Extension Presentation Linkbase Document

Table of Contents

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Cisco Systems, Inc.

Date: February 18, 2015

By /s/ Kelly A. Kramer
Kelly A. Kramer
Executive Vice President and
Chief Financial Officer
(Principal Financial Officer and duly authorized signatory)

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