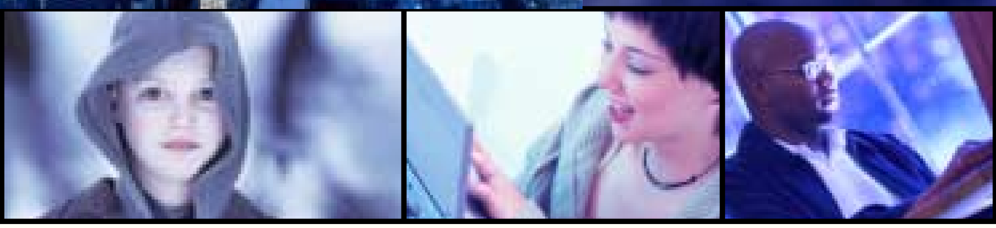
Cisco Systems



2000 ANNUAL REPORT

DISCOVER ALL THAT'S POSSIBLE ON THE INTERNET

CISCO SYSTEMS, INC.

PROFILE

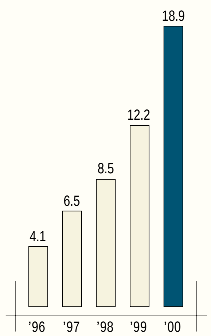
CISCO SYSTEMS, INC. is the worldwide leader in networking for the Internet. Cisco hardware, software, and service offerings are used to create Internet solutions so that individuals, companies, and countries have seamless access to information—regardless of differences in time and place. Cisco solutions provide competitive advantage to our customers through more efficient and timely exchange of information, which in turn leads to cost savings, process efficiencies, and closer relationships with their customers, prospects, business partners, suppliers, and employees. These solutions form the networking foundation for companies, universities, utilities, and government agencies worldwide.

The company was founded in 1984 by a small group of computer scientists from Stanford University seeking an easier way to connect different types of computer systems. Cisco Systems shipped its first product in 1986. Since then, Cisco has grown into a multinational corporation with more than 34,000 employees around the world. We invite you to learn more about Cisco Systems at www.cisco.com.

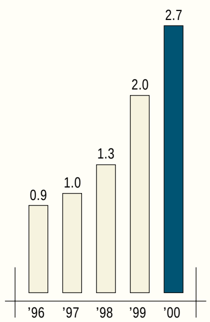
TABLE OF CONTENTS

This report may contain projections or other forward-looking statements regarding future events or the future financial performance of the Company that involve risks and uncertainties. Readers are cautioned that these forward-looking statements are only predictions and may differ materially from actual future events or results. Readers are referred to the documents filed by Cisco with the Securities and Exchange Commission, specifically the most recent reports on Forms 10-K, 8-K, and 10-Q, including amendments thereto, which identify important risk factors that could cause actual results to differ from those contained in the forward-looking statements, including risks associated with acquisition strategy, dependence on new product offerings, competition, patents, intellectual property and licensing, future growth, rapid technological and market change, manufacturing and sourcing risks, Internet infrastructure and regulation, international operations, volatility of stock price, financial risk management, and potential volatility in operating results, among others.

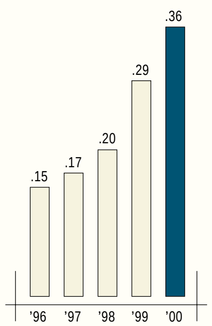
FINANCIAL HIGHLIGHTS[1]



NET SALES
(Dollars in billions)



NET INCOME
(Dollars in billions)



DILUTED NET INCOME PER SHARE
(In dollars)

CONSOLIDATED STATEMENTS OF OPERATIONS DATA[1]

(In millions, except per-share amounts)

Years Ended	July 29, 2000	July 31, 1999	July 25, 1998
Net sales	**$18,928**	$12,173	$8,489
Income before provision for income taxes	**$ 4,343**	$ 3,203	$2,271
Net income	**$ 2,668**[a]	$ 2,023[b]	$1,331[c]
Net income per common share—diluted*	**$ 0.36**[a]	$ 0.29[b]	$ 0.20[c]
Shares used in per-common share calculation—diluted*	**7,438**	7,062	6,658

* Reflects the two-for-one stock split effective March 2000.

(a) Net income and net income per common share include in-process research and development expenses of $1.37 billion, amortization of goodwill and purchased intangible assets of $291 million, acquisition-related costs of $62 million, payroll tax on stock option exercises of $51 million, and net gains realized on minority investments of $531 million. Pro forma net income and diluted net income per common share, excluding these items net of tax of $0, were $3.91 billion and $0.53, respectively.

(b) Net income and net income per common share include in-process research and development expenses of $471 million, amortization of goodwill and purchased intangible assets of $61 million, and acquisition-related costs of $16 million. Pro forma net income and diluted net income per common share, excluding these items net of related tax benefits of $54 million, were $2.52 billion and $0.36, respectively.

(c) Net income and net income per common share include in-process research and development expenses of $594 million, amortization of goodwill and purchased intangible assets of $23 million, and net gains realized on minority investments of $5 million. Pro forma net income and diluted net income per common share, excluding these items net of related tax benefits of $67 million, were $1.88 billion and $0.28, respectively.

CONSOLIDATED BALANCE SHEETS DATA[1]

(In millions)

	July 29, 2000	July 31, 1999	July 25, 1998
Working capital	**$ 5,914**	$ 1,723	$2,057
Total assets	**$32,870**	$14,893	$9,043
Shareholders' equity	**$26,497**	$11,811	$7,197

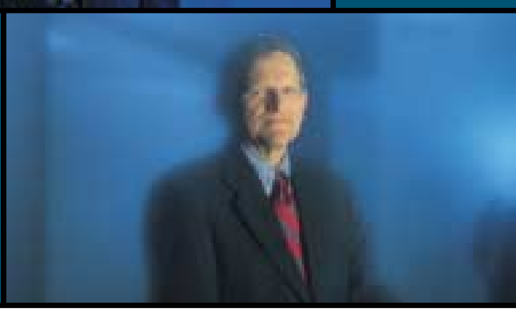
(1) All historical financial information has been restated to reflect the acquisitions of StratumOne Communications, Inc. and TransMedia Communications, Inc. in the first quarter of fiscal 2000, Cerent Corporation and WebLine Communications Corporation in the second quarter of fiscal 2000, and ArrowPoint Communications, Inc., InfoGear Technology Corporation, and SightPath, Inc. in the fourth quarter of fiscal 2000, which were accounted for as poolings of interests. In addition, the historical financial information has been restated to reflect the acquisition of Fibex Systems, which was completed in the fourth quarter of fiscal 1999 and accounted for as a pooling of interests.

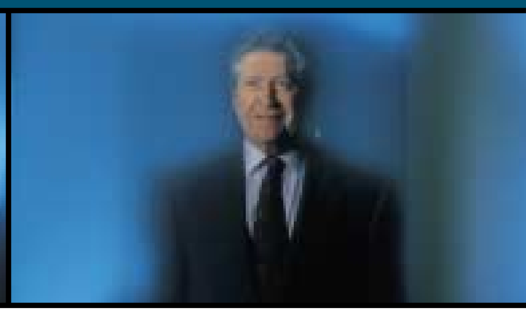
TO OUR SHAREHOLDERS

JOHN T. CHAMBERS
PRESIDENT AND CHIEF EXECUTIVE OFFICER

JOHN P. MORGRIDGE
CHAIRMAN OF THE BOARD

DONALD T. VALENTINE
VICE CHAIRMAN OF THE BOARD





Over the next two decades, the Internet economy will bring about more dramatic changes in the way we work, live, play, and learn than we witnessed during the last 200 years of the Industrial Revolution. Cisco is well-positioned to help our customers survive the Internet Revolution by turning these changes into competitive advantage. We provide the Internet solutions that will help our customers generate new revenue, reduce costs, increase productivity, and empower their employees.

For the past two years, Cisco has been asking business and government leaders around the world, “Are you ready?” Using our company as an example, our focus has been on educating customers about how effective use of the Internet can increase productivity and revolutionize their business models. Today, our customers are not only ready, but are turning to Cisco to show them how to capture the power of the Internet by implementing open standards-based Internet business models.

During the last decade, our passion has been to increase customer satisfaction and to achieve our stretch goal of maintaining the number-one or -two market share position in every market in which we compete. Today, Cisco holds a leadership position in 16 of our 17 key markets. Cisco’s success is the result of our solutions that provide data, voice, and video over a single network and our ability to blend internal development, acquisitions, and partnerships.

Cisco benefited from exceptional returns this past year because we successfully increased our customers’ satisfaction. For fiscal 2000, Cisco reported revenue of $18.93 billion, a 55-percent increase when compared with revenue of $12.17 billion in fiscal 1999. Pro forma net income was $3.91 billion or $0.53 per share for fiscal 2000, compared with pro forma net income of $2.52 billion or $0.36 per share for fiscal 1999, increases of 56 percent and 47 percent, respectively. Actual net income for the year was $2.67 billion or $0.36 per share, compared with fiscal 1999 net income of $2.02 billion or $0.29 per share.

Cisco has been one of the fastest-growing and most profitable companies in the history of the computer industry. We are widely accepted as the Internet expert and the Internet company, which is an obvious advantage when we talk to customers about their futures. Our success has been rewarded with one of the highest market capitalizations in the world. This achievement is the result of our commitment to help customers become successful in today’s ever-changing, competitive landscape.

The Internet economy has grown more rapidly than even our most optimistic predictions and fuels the strongest period of economic prosperity in history. In the United States alone, this economy added 650,000 jobs and generated revenue in excess of half a trillion dollars in 1999. To put this in perspective, the Internet economy’s workforce now surpasses the entire active U.S. military, insurance, communications, and public utilities industries and is twice the size of the airline, chemical and allied products, legal, and real-estate industries.

There is a direct correlation between the strength of this economy and the unprecedented productivity gains we are witnessing today. We refer to this phenomenon as the "Network Effect," which is the result of information technology becoming networked and Internet applications being used to re-engineer business processes. Companies that understand the Network Effect can gain competitive advantage by quickly detecting and responding to situations such as real-time changes in customer demand.

Cisco has become a trusted technology partner and business advisor to many of the largest companies in the world. We are not only a technology advisor, but also an advanced user of Internet technology to run our own business. The adoption of Internet applications in each of Cisco's functional areas is an integral part of our business-planning process and results in tremendous productivity benefits and cost savings. During this past fiscal year, for example, 90 percent of our customer orders were transacted over the Internet. We have created world-class e-commerce, customer support, and workforce optimization applications and are the leader in virtual manufacturing, virtual close, and e-learning solutions.

Our goal is to help customers develop similar, Internet-centric business models so that they can benefit from productivity improvements. For example, our Internet Business Solutions Group has consulted with executives in more than 50 percent of the Fortune 250 companies, 45 percent of the top companies in Europe, the Middle East, Africa, and Asia, and 65 percent of the leading service providers. This group provides business-strategy consulting and helps move our relationships with customers from that of a vendor to a strategic partner.

Successful companies in the 1980s achieved their leadership positions with a vertical business model and an internal focus. In the 1990s, Cisco changed the dynamics of market leadership by focusing on a combination of internal development and acquisitions. This decade, leading companies will develop internally, acquire effectively, and form an "ecosystem" of partnerships in a horizontal, rather than a vertical, business model.

Companies participating in an ecosystem—an open standards-based community that works toward a common goal—will emerge as the market and industry leaders of the future. Customers are the real beneficiaries of our ecosystem model because it allows us to remain agile, quickly enter new markets, and provide both breadth and depth of solutions through the ecosystem community.

In addition to expanding our ecosystem, we also increased our investment in internal product development by 61 percent and continued to grow through acquisitions. Since 1993, we have acquired or announced our intent to acquire 65 companies. Moving forward, our technology strategy will continue to be driven by internal development complemented by acquisitions and strategic alliances.

INSIDE CISCO

Five years ago it took Cisco 14 days to close its books each quarter. Now, with the "virtual close," using powerful Internet technology, Cisco executives have real-time, daily access to company financial information, empowering them and their employees to instantly react to market shifts and changing business requirements.

Following the lead of business, we saw governments from around the world begin to recognize the strong correlation between the Internet and economic success. This past year, we met with government leaders from many countries, including Argentina, Chile, China, France, Germany, Italy, Japan, Jordan, Korea, South Africa, Taiwan, and the United Kingdom. They all realized the Internet's potential impact on their country's future and were eager to learn how to use the Internet more effectively.

The Industrial Revolution of 200 years ago divided society by creating a gap between the "haves" and "have-nots." Today's Internet Revolution has the potential to unite everyone by combining the strength of the Internet and education, the two great equalizers in life. By applying what we've learned in business to all aspects of society, we have the power to use technology to create an Internet gateway that has the potential to positively change people's lives.

Cisco is in a unique position to be a pioneer in embracing this digital opportunity and closing the gap. As such, our philanthropy strategy focuses on education, workforce development, and basic human needs. We continue to invest and grow the Cisco Networking Academy Program, which has enrolled more than 81,000 students in 83 countries. These academies provide networking skills to a broad range of students, including those in high school, community colleges, homeless shelters, and juvenile centers and outgoing military personnel.

In addition, our employees contributed more than $1 million to the Second Harvest Food Bank this past year. Cisco gave more than $2.5 million in grants to our global community and committed another $5 million to Habitat for Humanity over the next five years. We also launched the Netaid.org Web site and movement, a joint initiative with the United Nations Development Program, a number of talented musicians, and several technology companies, to help end the cycle of extreme poverty. Our employees supported additional programs such as the Special Olympics, InnVision, the National Teacher Training Institute, and a variety of global relief efforts. These efforts are Cisco's way of preparing future generations and less-developed nations to participate in the Internet economy.

In our opinion, the radical business transformations taking place around the world will accelerate, making the opportunities ahead of Cisco far greater than ever before. We believe that Cisco has the potential to be the most influential and generous company in history. We are in the fortunate position to be at the center of the Internet economy, and we recognize that although this position gives us confidence, we must balance this confidence with healthy paranoia.

We are proud of our accomplishments and want to thank our shareholders, customers, employees, partners, and suppliers for their continued commitment and confidence in our ability to execute. Together, we are only beginning to explore all that's possible on the Internet.

JOHN T. CHAMBERS
PRESIDENT AND
CHIEF EXECUTIVE OFFICER

JOHN P. MORGRIDGE
CHAIRMAN OF THE BOARD

DONALD T. VALENTINE
VICE CHAIRMAN OF THE BOARD

DISCOVER ALL THAT'S POSSIBLE ON THE INTERNET...

For several years we have asked our customers, "Are you ready?" for the Internet. Today, they are ready and they want to know how to get there, quickly and successfully. Organizations and governments are rethinking their business models. They are looking for a road map to chart their company's course through the Internet economy. And they are turning to Cisco to help them discover all that's possible on the Internet.

To transform a "bricks-and-mortar" organization into an Internet organization takes more than just adding an e-commerce veneer. It takes rethinking the entire business from the inside out and making investments in your Internet technology portfolio to bring home the best return. It impacts groups across the entire organization, changing the way companies work internally and how they work with their customers, partners, suppliers, and employees. In the near future, a business not on the Internet will not be in business. On the following pages, we have highlighted a few examples of how the Internet has changed the way that people work, live, play, and learn.

Cisco itself often serves as the best example of a business that has changed itself by using the Internet. We have always believed that technology could help us do things that our competitors could not. Customer service was the first application to go on line. This was quickly followed by operations in manufacturing, commerce, finance, recruiting, marketing, training, and sales. It has given us a competitive advantage in our industry. It has allowed us to remain agile and responsive, and it is based on employee and customer empowerment through the Internet. We provide this same expertise to our customers, helping them create Internet solutions for their organizations.

THE **INTERNET** IS CHANGING EVERYTHING,
INCLUDING EVERY **IDEA** OF WHAT IS **POSSIBLE.**

...FROM THE COMPANY THAT CAN SHOW YOU HOW

FROM CUSTOMER SUPPORT TO CUSTOMER DELIGHT

CUSTOMER CARE: LANDS' END www.landsend.com

INSIDE CISCO

The Cisco Technical Assistance Center (TAC) Web site was one of the first to add real-time assistance for its customers, enhancing the company's ability to close out inquiries with one customer interaction. Approximately 80 percent of all support questions are answered on line. Customer-care solutions across the company saved Cisco $270 million and increased customer satisfaction by 25 percent.

Building strong customer loyalty is important for organizations in today's ever-changing Internet economy. Good customer service is just as critical for online services as it is with a personal sales call or in a retail environment. An online customer-care strategy that focuses on consumer needs can ensure high customer satisfaction and retention while also reducing sales, marketing, and service costs.

Casual clothing and home retailer Lands' End knows this firsthand. Being the first direct merchant to offer a toll-free number to customers and also one of the first to establish an online presence, the company was no stranger to new technologies. While competitors were eliminating live customer service phone calls to reduce costs, Lands' End wanted to make online shopping more personal. In September 1999, it launched Lands' End Live, an interactive site where customers and service representatives can communicate in real time while shopping on line. Shoppers ask questions and get instant answers, via either text-based Internet chat or an instant telephone callback, making the experience more personal. They can also use the "Shop With A Friend" tool to browse the site with anyone, anywhere in the world, or shop along with a service representative.

To implement the solution, Lands' End put together a team with members from all areas of the organization. The team set deadlines, established procedures, and evaluated several solutions. It chose an easy-to-use, reliable system that would integrate into its existing call-center infrastructure. With the help of Cisco, Lands' End also established a customized training program for all online service representatives and conducted usability tests before launching the new site features. All of this was done in just four months.

Since the introduction of Lands' End Live, the company has received several hundred chat and callback requests each week. Today, its Web sales comprise more than 10 percent of its total business—$138 million in fiscal 2000. Customers say they are getting better service and enjoy the human touch provided by Lands' End Live. The bottom line is that Lands' End is paying attention to the most important element of its business—the customer. And it shows.

WHEN WE **MOVED OUR CUSTOMERS** FROM
“ON HOLD” TO “ON LINE,” WE MOVED FROM
CUSTOMER SUPPORT TO CUSTOMER DELIGHT.

FROM CORNER STORE TO ONLINE STORE

COMMERCE: CHAPTERS ONLINE www.chapters.ca

Moving from a successful "bricks-and-mortar" retailer to an equally successful "clicks-and-mortar" strategy can be daunting. But recent studies from the University of Texas and the U.S. Department of Commerce predict that e-commerce will comprise 4.4 percent of the U.S. gross domestic product by 2002. Canadian-based book retailer Chapters, Inc. recognized the possibilities that the Internet provides and launched Chapters Online.

Chapters, Canada's largest book retailer, operates 70 superstores and 243 smaller stores. When the retailer expanded into the online world, the company knew that it had to stick to its original mission of providing a world-class selection emphasizing products and content of interest to Canadians. Chapters designed its site with a focus on Canadian books, music, and movies, with reviews by Canadian critics and Canadian best-seller lists. It also extended the online experience to its retail stores. Its 70 superstores house kiosks that conveniently provide online ordering when a book is out of stock. The company teamed up with established technology leaders Cisco and AT&T (a Cisco Powered Network provider) to maximize time and resources to quickly launch the best possible site. Chapters Online launched its Web site, www.chapters.ca, three months after concept, in April 1999.

INSIDE CISCO

Cisco operates the world's largest e-commerce site, with 90 percent of its orders placed on line. Using networked applications, orders are 99-percent accurate the first time they are entered, saving time and money. Cisco gains a financial contribution of $60 million in operating cost savings from its e-commerce applications.

While planning an e-commerce strategy, network reliability and redundancy are crucial for the best customer experience. To address reliability issues, Chapters Online deployed Cisco software to prevent any bottlenecks, giving online shoppers quick access to all areas of the site at all times. To successfully handle redundancy concerns, Chapters erred on the side of caution and added backup systems to ensure uninterrupted service. It knew even the smallest degree of visitor frustration might prompt potential customers to flee the site. To date, the site has yet to experience any downtime.

Today, Chapters Online is Canada's most popular online retailer. In its holiday quarter, revenue was 2,000 percent higher over the same quarter just one year earlier. In 1999, Chapters sold Canadian-focused merchandise to more than 400,000 online customers. Industry experts say that the company is at least one year ahead of the country's other online retailers. This example shows that with careful planning and the right alliances, a bricks-and-mortar company can transform itself into an e-commerce powerhouse.

REAL ESTATE WAS LIMITING OUR GROWTH.
SO WE WENT FROM BUILDING NEW STORES ON EVERY CORNER,
TO OPENING ONLINE **STORES IN EVERY HOME**.

FROM JUST IN TIME TO REAL TIME

SUPPLY–CHAIN MANAGEMENT: HONEYWELL INTERNATIONAL www.honeywell.com

In today's economy, implementing a "virtual" supply-chain system is a vital element of success. From aerospace and automotive to construction and manufacturing organizations, companies worldwide are taking advantage of the Internet to create electronic marketplaces where customers, suppliers, and business partners collaborate with real-time results.

Honeywell International, one of the world's most successful and established manufacturing companies, is reshaping itself in the Internet economy. Honeywell's management vowed to increase its use of the Internet to expand its business. In July 1999, it launched MyPlant.com, a business-to-business Web site that connects customers and suppliers in the manufacturing industry. At the site, large and small companies from around the world share procurement and manufacturing strategies, download software, and participate in valuable industry discussions. The site has huge potential for Honeywell since it caters to virtually any industry that manufactures goods in a factory.

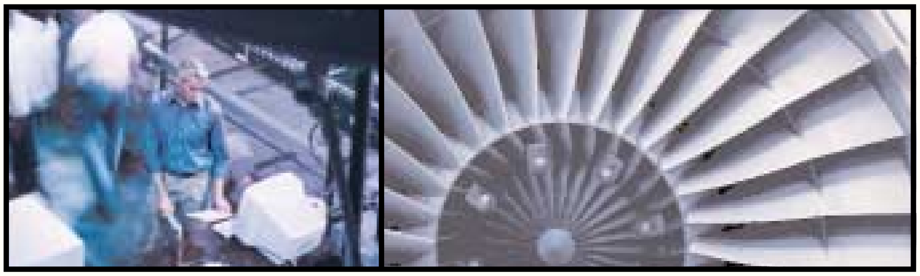
When MyPlant.com was first launched, the site offered only Honeywell software products. Now 400 software suppliers provide 650 manufacturing applications on the site for a small transaction fee. In the past, solving a recurring manufacturing problem could take days or weeks. With MyPlant.com, users take matters into their own hands in real time. The practice is revolutionary, saving companies time, money, and risk. Recently, MyPlant.com hosted 60,000 user sessions, and the company estimates that one-third of the site's users are new Honeywell customers.

The advantage of creating a single electronic marketplace is that everyone emerges a winner. For example, two rival companies that both build engines, but don't make the same replacement parts, can ultimately share resources. Collaborating over the Internet also results in economies of scale. In the next year, Honeywell plans to implement MyAircraft.com, a joint venture with United Technologies and I2, to focus on supply-chain management for the aerospace industry, and MyFacilities.com for the facilities management industry. Both sites will match customers and suppliers, providing instant results with improved inventory turns, corrected purchasing inefficiencies, and reduced overhead. It is exactly what customers and companies need in today's fast-paced economy.

INSIDE CISCO

By implementing its own virtual supply chain, Cisco reduced inventory levels by 45 percent over the past six years and decreased the time to market for its products by as much as 12 weeks. "Virtual manufacturing" saves Cisco upward of $175 million in annual operating costs. Cisco will also provide networking products in a quick-start kit for suppliers to give component makers immediate and secure access to the site.

THE MOST EXPENSIVE **BOX** OF ANYTHING IS
THE ONE SITTING STILL. FORGET JUST IN TIME.
WE'RE MANAGING **INVENTORY IN REAL TIME.**



FROM TRAINING DOWNTIME TO LEARNING ANYTIME

WORKFORCE OPTIMIZATION: GENUITY www.genuity.com

Streamlining business practices translates to all areas of the organization, not just those that touch customers. From human resources to training, companies can use the Internet to optimize their workforce and make themselves more agile in response to rapidly changing market conditions. Electronic-based learning, or e-learning, is one critical Internet application that yields significant results for Genuity Inc., a newly independent Internet service provider (ISP), formerly a division of the GTE Corporation.

Genuity faced a training challenge in April 1998 due to the sweeping changes brought on by the GTE acquisition. The company's sales force was expected to grow from 200 to 1,000 and was now responsible for selling a new product set and a full spectrum of Internet services. Not only was the sales team rapidly expanding, but it was also moving into new worldwide territories. Genuity had to quickly find an efficient, scalable solution that would reduce time spent in a classroom and increase effectiveness with customers.

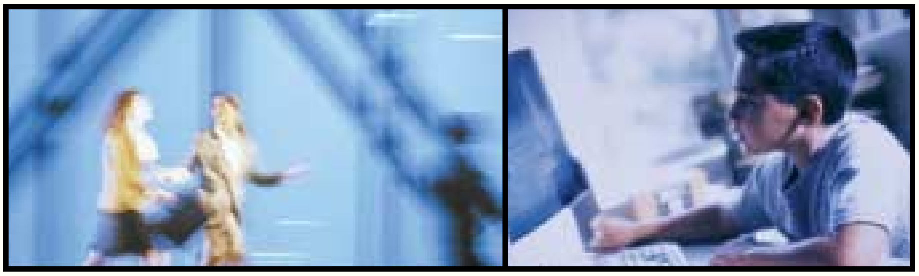
INSIDE CISCO

By the end of 2000, 100 percent of Cisco sales and technical staff will participate in online training. The e-learning program has reduced the company's training expenses by 60 percent. Cisco can train up to 3,000 people worldwide in a single online session for $250,000. It also means more time spent with customers and less time in a classroom—perhaps the biggest benefit of all.

Genuity leveraged the power of the Internet and created an e-learning solution with the assistance of the GTE Learning Systems group's 30 years of experience in training government agencies and corporations. In July 1998, Genuity launched Virtual University, which allowed salespeople to obtain real-time virtual instruction along with the latest product information on their highly secure Web site. Genuity had an end-to-end Cisco network that was immediately deployed to support the multimedia-rich applications based on integrated data, voice, and video networking technologies.

To measure the effectiveness of Virtual University, Genuity trained a pilot sales group on the new e-learning system and another group using traditional instruction. The benefits were immediately evident. Those trained using the e-learning system made their first sale 25 percent faster than those who didn't, and their revenue numbers were twice the dollar amount of the "traditional" group. Virtual University was so effective that the company is planning more Internet-optimized learning programs to increase productivity. As far as Genuity is concerned, empowering employees through e-learning allows them to do the best job possible. It has had a clear effect on sales, productivity, and customer satisfaction.

TRAINING WASN'T DELIVERING HUGE LEAPS IN PRODUCTIVITY, SO WE MADE THE LEAP FROM TRAINING DOWNTIME TO **LEARNING ON LINE ANYTIME, ANYWHERE**.



FINANCIAL REVIEW

SELECTED FINANCIAL DATA[1]

Five Years Ended July 29, 2000 (In millions, except per-share amounts)

	July 29, 2000	July 31, 1999	July 25, 1998	July 26, 1997	July 28, 1996
Net sales	**$18,928**	$12,173	$8,489	$6,452	$4,101
Net income	**$ 2,668[2]**	$ 2,023[3]	$1,331[4]	$1,047[5]	$ 915[6]
Net income per common share—basic	**$ 0.39**	$ 0.30	$ 0.21	$ 0.17	$ 0.16
Net income per common share—diluted	**$ 0.36[2]**	$ 0.29[3]	$ 0.20[4]	$ 0.17[5]	$ 0.15[6]
Shares used in per-common share calculation—basic*	**6,917**	6,646	6,312	6,007	5,758
Shares used in per-common share calculation—diluted*	**7,438**	7,062	6,658	6,287	6,008
Total assets	**$32,870**	$14,893	$9,043	$5,504	$3,647

* Reflects the two-for-one stock split effective March 2000.

(1) All historical financial information has been restated to reflect the acquisitions that were accounted for as poolings of interests (see Note 3 to the Consolidated Financial Statements).

(2) Net income and net income per common share include in-process research and development expenses of $1.37 billion, amortization of goodwill and purchased intangible assets of $291 million, acquisition-related costs of $62 million, payroll tax on stock option exercises of $51 million, and net gains realized on minority investments of $531 million. Pro forma net income and diluted net income per common share, excluding these items net of tax of $0, were $3.91 billion and $0.53, respectively.

(3) Net income and net income per common share include in-process research and development expenses of $471 million, amortization of goodwill and purchased intangible assets of $61 million, and acquisition-related costs of $16 million. Pro forma net income and diluted net income per common share, excluding these items net of tax benefits of $54 million, were $2.52 billion and $0.36, respectively.

(4) Net income and net income per common share include in-process research and development expenses of $594 million, amortization of goodwill and purchased intangible assets of $23 million, and net gains realized on minority investments of $5 million. Pro forma net income and diluted net income per common share, excluding these items net of tax benefits of $67 million, were $1.88 billion and $0.28, respectively.

(5) Net income and net income per common share include in-process research and development expenses of $508 million, amortization of goodwill and purchased intangible assets of $11 million, and net gains realized on minority investments of $152 million. Pro forma net income and diluted net income per common share, excluding these items net of tax benefits of $7 million, were $1.42 billion and $0.23, respectively.

(6) Net income and net income per common share include amortization of goodwill and purchased intangible assets of $14 million. Pro forma net income and diluted net income per common share, excluding this item net of a tax benefit of $2 million, were $927 million and $0.15, respectively.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

All historical financial information has been restated to reflect the acquisitions that were accounted for as poolings of interests (see Note 3 to the Consolidated Financial Statements).

FORWARD-LOOKING STATEMENTS

Certain statements contained in this Annual Report, including, without limitation, statements containing the words "believes," "anticipates," "estimates," "expects," "projections," and words of similar import, constitute "forward-looking statements." You should not place undue reliance on these forward-looking statements. Our actual results could differ materially from those anticipated in these forward-looking statements for many reasons, including risks faced by us described in the Risk Factors sections, among others, included in the documents we file with the Securities and Exchange Commission ("SEC"), including our most recent reports on Form 10-K, Form 8-K, and Form 10-Q, and amendments thereto.

COMPARISON OF FISCAL 2000 AND FISCAL 1999

Net sales in fiscal 2000 were $18.93 billion, compared with $12.17 billion in fiscal 1999, an increase of 55.5%. The increase in net sales was primarily a result of increased unit sales of switch, router, and access products; growth in the sales of add-on boards that provide increased functionality; optical transport products; and maintenance, service, and support sales (see Note 12 to the Consolidated Financial Statements).

We manage our business on four geographic theaters: the Americas; Europe, the Middle East, and Africa ("EMEA"); Asia Pacific; and Japan. Summarized financial information by theater for fiscal 2000 and 1999 is presented in the following table (in millions):

	Amount		Percentage of Net Sales	
Years Ended	July 29, 2000	July 31, 1999	July 29, 2000	July 31, 1999
Net sales:				
Americas	**$12,924**	$ 8,088	**68.3%**	66.4%
EMEA	**4,770**	3,216	**25.2**	26.4
Asia Pacific	**1,705**	825	**9.0**	6.8
Japan	**935**	566	**4.9**	4.7
Sales adjustments	**(1,406)**	(522)	**(7.4)**	(4.3)
Total	**$18,928**	$12,173	**100.0%**	100.0%

The revenue growth for each theater was primarily driven by market demand and the deployment of Internet technologies and business solutions.

Gross margin in fiscal 2000 was 64.4%, compared with 65.0% in fiscal 1999. The following table shows the standard margins for each theater:

Years Ended	July 29, 2000	July 31, 1999
Standard margins:		
Americas	**72.8%**	72.2%
EMEA	**75.1%**	74.0%
Asia Pacific	**71.3%**	71.0%
Japan	**78.8%**	77.0%

The net sales and standard margins by geographic theater differ from the amounts recognized under generally accepted accounting principles because we do not allocate certain sales adjustments, production overhead, and manufacturing variances and other related costs to the theaters. Sales adjustments relate to revenue deferrals and reserves, credit memos, returns, and other timing differences.

Standard margins increased for all geographic theaters as compared with fiscal 1999. The decrease in the overall gross margin was primarily due to shifts in product mix, introduction of new products, which generally have lower margins when first released, higher production-related costs, the continued pricing pressure seen from competitors in certain product areas, and the above-mentioned sales adjustments, which were not included in the standard margins.

We expect gross margin may be adversely affected by increases in material or labor costs, heightened price competition, increasing levels of services, higher inventory balances, introduction of new products for new high-growth markets, and changes in channels of distribution or in the mix of products sold. We believe gross margin may additionally be impacted due to constraints relating to certain component shortages that currently exist in the supply chain. We may also experience a lower gross margin as the product mix for access and optical product volume grows.

We have recently introduced several new products, with additional new products scheduled to be released in the future. Increase in demand would result in increased manufacturing capacity, which in turn would result in higher inventory balances. In addition, our vendor base is capacity-constrained, and this could result in increased cost pressure on certain components. If product or related warranty costs associated with these new products are greater than we have experienced, gross margin may be adversely affected. Our gross margin may also be impacted by geographic mix, as well as the mix of configurations within each product group. We continue to expand into third-party or indirect-distribution channels, which generally results in a lower gross margin. In addition, increasing third-party and indirect-distribution channels generally results in greater difficulty in forecasting the mix of our product, and to a certain degree, the timing of orders from our customers. Downward pressures on our gross margin may be further impacted by other factors, such as increased percentage of revenue from service provider markets, which may have lower margins or an increase in product costs, which could adversely affect our future operating results.

Research and development (“R&D”) expenses in fiscal 2000 were $2.70 billion, compared with $1.66 billion in fiscal 1999, an increase of 62.6%. R&D expenses, as a percentage of net sales, increased to 14.3% in fiscal 2000, compared with 13.7% in fiscal 1999. The increase reflected our ongoing R&D efforts in a wide variety of areas such as data, voice, and video integration, digital subscriber line (“DSL”) technologies, cable modem technology, wireless access, dial access, enterprise switching, optical transport, security, network management, and high-end routing technologies, among others. A significant portion of the increase was due to the addition of new personnel, partly through acquisitions, as well as higher expenditures on prototypes and depreciation on additional lab equipment. We also continued to purchase technology in order to bring a broad range of products to the 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 license technology from other businesses or acquire businesses as an alternative to internal R&D. All of our R&D costs are expensed as incurred. We currently expect that R&D expenses will continue to increase in absolute dollars as we continue to invest in technology to address potential market opportunities.

Sales and marketing expenses in fiscal 2000 were $3.95 billion, compared with $2.46 billion in fiscal 1999, an increase of 60.1%. Sales and marketing expenses, as a percentage of net sales, increased to 20.8% in fiscal 2000, compared with 20.2% in fiscal 1999. The increase was principally due to an increase in the size of our direct sales force and related commissions, additional marketing and advertising investments associated with the introduction of new products, the expansion of distribution channels, and general corporate branding. The increase also reflected our efforts to invest in certain key areas, such as expansion of our end-to-end networking strategy and service provider coverage, in order to be positioned to take advantage of future market opportunities. We currently expect that sales and marketing expenses will continue to increase in absolute dollars.

General and administrative (“G&A”) expenses in fiscal 2000 were $633 million, compared with $381 million in fiscal 1999, an increase of 66.1%. G&A expenses, as a percentage of net sales, increased to 3.3% in fiscal 2000, compared with 3.1% in fiscal 1999. G&A expenses for fiscal 2000 and 1999 included acquisition-related costs of approximately $62 million and $16 million, respectively. Excluding the acquisition-related costs, the increase in G&A expenses was primarily related to the addition of new personnel and investments in infrastructure. We intend to keep G&A expenses relatively constant as a percentage of net sales; however, this depends on the level of acquisition activity and our growth, among other factors.

Amortization of goodwill and purchased intangible assets included in operating expenses was $291 million in fiscal 2000, compared with $61 million in fiscal 1999. Amortization of goodwill and purchased intangible assets primarily relates to various purchase acquisitions (see Note 3 and Note 4 to the Consolidated Financial Statements). Amortization of goodwill and purchased intangible assets will continue to increase as we acquire companies and technologies.

The amount expensed to in-process research and development ("in-process R&D") arose from the purchase acquisitions completed in fiscal 2000 (see Note 3 to the Consolidated Financial Statements).

The fair values of the existing products and patents, as well as the technology currently under development, were determined using the income approach, which discounts expected future cash flows to present value. The discount rates used in the present value calculations were typically derived from a weighted-average cost of capital analysis and venture capital surveys, adjusted upward to reflect additional risks inherent in the development life cycle. These risk factors have increased the overall discount rate for acquisitions in the current year. We consider the pricing model for products related to these acquisitions to be standard within the high-technology communications equipment industry. However, we do not expect to achieve a material amount of expense reductions or synergies as a result of integrating the acquired in-process technology. Therefore, the valuation assumptions do not include significant anticipated cost savings.

The development of these technologies remains a significant risk due to the remaining effort to achieve technical viability, rapidly changing customer markets, uncertain standards for new products, and significant competitive threats from numerous companies. The nature of the efforts to develop the acquired technologies into commercially viable products consists principally of planning, designing, and testing activities necessary to determine that the products can meet market expectations, including functionality and technical requirements. Failure to bring these products to market in a timely manner could result in a loss of market share or a lost opportunity to capitalize on emerging markets and could have a material adverse impact on our business and operating results.

The following table summarizes the significant assumptions underlying the valuations for our significant purchase acquisitions completed in fiscal 2000 and 1999 (in millions, except percentages):

	Acquisition Assumptions	
Acquired Company	Estimated Cost to Complete Technology at Time of Acquisition	Risk-Adjusted Discount Rate for In-Process R&D
FISCAL 2000		
Monterey Networks, Inc.	**$ 4**	**30.0%**
The optical systems business of Pirelli S.p.A.	**$ 5**	**20.0%**
Aironet Wireless Communications, Inc.	**$ 3**	**23.5%**
Atlantech Technologies	**$ 6**	**37.5%**
JetCell, Inc.	**$ 7**	**30.5%**
PentaCom, Ltd.	**$13**	**30.0%**
Qeyton Systems	**$ 6**	**35.0%**
FISCAL 1999		
Summa Four, Inc.	$ 5	25.0%
Clarity Wireless, Inc.	$42	32.0%
Selsius Systems, Inc.	$15	31.0%
PipeLinks, Inc.	$ 5	31.0%
Amteva Technologies	$ 4	35.0%

Regarding our purchase acquisitions completed in fiscal 2000 and 1999, actual results to date have been consistent, in all material respects, with our assumptions at the time of the acquisitions. The assumptions primarily consist of an expected completion date for the in-process projects, estimated costs to complete the projects, and revenue and expense projections once the products have entered the market. Shipment volumes of products from the above-acquired technologies are not material to our overall financial results at the present time. Therefore, it is difficult to determine the accuracy of overall revenue projections early in the technology or product life cycle. Failure to achieve the expected levels of revenue and net income from these products will negatively impact the return on investment expected at the time that the acquisitions were completed and potentially result in impairment of any other assets related to the development activities.

Interest and other income, net, was $577 million in fiscal 2000, compared with $330 million in fiscal 1999. The increase was primarily due to interest income related to the general increase in cash and investments, which was generated from our operations. Net gains realized on minority investments were $531 million in fiscal 2000. The net gains realized on minority investments were not material in fiscal 1999.

Our pro forma effective tax rate for fiscal 2000 was 30.0%. The actual effective tax rate was 38.6%, which included the impact of nondeductible in-process R&D and acquisition-related costs. Our future effective tax rates could be adversely affected if earnings are lower than anticipated in countries where we have lower effective rates or by unfavorable changes in tax laws and regulations. Additionally, we have provided a valuation allowance on certain of our deferred tax assets because of uncertainty regarding their realizability due to expectation of future employee stock option exercises (see Note 11 to the Consolidated Financial Statements).

COMPARISON OF FISCAL 1999 AND FISCAL 1998

Net sales in fiscal 1999 were $12.17 billion, compared with $8.49 billion in fiscal 1998, an increase of 43.4%. The increase in net sales was primarily a result of increased unit sales of LAN switching products, access servers, high-performance WAN switching and routing products, and maintenance service contracts.

Gross margin in fiscal 1999 was 65.0%, compared with 65.6% in fiscal 1998. The decrease in the overall gross margin was primarily due to our continued shift in revenue mix toward our lower-margin products and the continued pricing pressure seen from competitors in certain product areas.

R&D expenses in fiscal 1999 were $1.66 billion, compared with $1.05 billion in fiscal 1998, an increase of 58.1%. R&D expenses, as a percentage of net sales, increased to 13.7% in fiscal 1999, compared with 12.4% in fiscal 1998. The increase reflected our ongoing R&D efforts in a wide variety of areas such as data, voice, and video integration, DSL technologies, cable modem technology, wireless access, dial access, enterprise switching, security, network management, and high-end routing technologies, among others. A significant portion of the increase was due to the addition of new personnel, partly through acquisitions, as well as higher expenditures on prototypes and depreciation on additional lab equipment.

Sales and marketing expenses in fiscal 1999 were $2.46 billion, compared with $1.58 billion in fiscal 1998, an increase of 56.1%. Sales and marketing expenses, as a percentage of net sales, increased to 20.2% in fiscal 1999, compared with 18.6% in fiscal 1998. The increase was principally due to an increase in the size of our direct sales force and related commissions, television advertising campaigns to build brand awareness, additional marketing and advertising costs associated with the introduction of new products, and the expansion of distribution channels. The increase also reflected our efforts to invest in certain key areas, such as expansion of our end-to-end networking strategy and service provider coverage, in order to be positioned to take advantage of future market opportunities.

G&A expenses in fiscal 1999 were $381 million, compared with $247 million in fiscal 1998, an increase of 54.3%. G&A expenses, as a percentage of net sales, increased to 3.1% in fiscal 1999, compared with 2.9% in fiscal 1998. The increase was primarily related to additional personnel and acquisition-related costs of $16 million.

Amortization of goodwill and purchased intangible assets included in operating expenses was $61 million in fiscal 1999, compared with $23 million in fiscal 1998. Amortization of goodwill and purchased intangible assets increased as we acquired companies and technologies.

Interest and other income, net, in fiscal 1999 was $330 million, compared with $196 million in fiscal 1998. Interest income rose primarily as a result of additional investment income on our increased investment balances.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

RECENT ACCOUNTING PRONOUNCEMENTS

In June 1998, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards No. 133, "Accounting for Derivative Instruments and Hedging Activities" ("SFAS 133"). SFAS 133, as amended, establishes accounting and reporting standards for derivative instruments and hedging activities. It requires an entity to recognize all derivatives as either assets or liabilities on the balance sheet and measure those instruments at fair value. We do not expect the initial adoption of SFAS 133 to have a material effect on our operations or financial position. We are required to adopt SFAS 133 in the first quarter of fiscal 2001.

In September 1999, the FASB issued Emerging Issues Task Force Topic No. D-83, "Accounting for Payroll Taxes Associated with Stock Option Exercises" ("EITF D-83"). EITF D-83 requires that payroll tax paid on the difference between the exercise price and the fair value of acquired stock in association with an employee's exercise of stock options be recorded as operating expenses. Payroll tax on stock option exercises of $51 million was expensed in fiscal 2000.

In December 1999, the SEC issued Staff Accounting Bulletin No. 101, "Revenue Recognition in Financial Statements" ("SAB 101"). SAB 101, as amended, summarizes certain of the SEC's views in applying generally accepted accounting principles to revenue recognition in financial statements. At this time, we do not expect the adoption of SAB 101 to have a material effect on our operations or financial position; however, the SEC's final guidance for implementation has not been released to date. We are required to adopt SAB 101 in the fourth quarter of fiscal 2001.

LIQUIDITY AND CAPITAL RESOURCES

Cash and cash equivalents, short-term investments, and investments were $20.50 billion at July 29, 2000, an increase of $10.28 billion from July 31, 1999. The increase was primarily a result of $5.00 billion of net unrealized gains on publicly held investments and $7.70 billion of cash generated by operating and financing activities partially offset by investing activities, including net capital expenditures of $1.09 billion, purchases of technology licenses of $444 million, and investments in lease receivables of $535 million.

Accounts receivable increased 83.9% during fiscal 2000. Days sales outstanding in receivables increased to 37 days for fiscal 2000, from 32 days for fiscal 1999. The increase in accounts receivable and days sales outstanding was due, in part, to growth in total net sales combined with conditions in a number of markets, resulting in longer payment terms.

Inventories increased 87.2% during fiscal 2000; however, inventory turns remained constant at 7.8 times. The increase in inventory levels reflected new product introductions, continued growth in our two-tier distribution system, and increased purchases to secure the supply of certain components. Inventory management remains an area of focus as we balance the need to maintain strategic inventory levels to ensure competitive lead times with the risk of inventory obsolescence due to rapidly changing technology and customer requirements.

At July 29, 2000, we had a line of credit totaling $500 million, which expires in July 2002. There have been no borrowings under this agreement (see Note 7 to the Consolidated Financial Statements).

We have entered into several agreements to lease 448 acres of land located in San Jose, California, where our headquarters operations are established, and 759 acres of land located in Boxborough, Massachusetts; Salem, New Hampshire; Richardson, Texas; and Research Triangle Park, North Carolina, where we have expanded certain R&D and customer-support activities. In connection with these transactions, we have pledged $1.29 billion of our investments as collateral for certain obligations of the leases. We anticipate that we will occupy more leased property in the future that will require similar pledged securities; however, we do not expect the impact of this activity to be material to our liquidity position (see Note 8 to the Consolidated Financial Statements).

We believe that our current cash and cash equivalents, short-term investments, line of credit, and cash generated from operations will satisfy our expected working capital, capital expenditure, and investment requirements through at least the next 12 months.

QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

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 the balance sheet at fair value with unrealized gains or losses reported as a separate component of accumulated other comprehensive income, net of tax. Part of this portfolio includes minority equity investments in several publicly traded companies, the values of which are subject to market price volatility. For example, as a result of recent market price volatility of our publicly traded equity investments, we experienced a $111 million after-tax unrealized loss during the third quarter of fiscal 2000 and a $1.83 billion after-tax unrealized gain during the fourth quarter of fiscal 2000 on these investments. We have also invested in numerous privately held companies, many of which can still be considered in the start-up or development stages. These investments are inherently risky as the market for the technologies or products they have under development are typically in the early stages and may never materialize. We could lose our entire initial investment in these companies. We also have certain real estate lease commitments with payments tied to short-term interest rates. At any time, a sharp rise in interest rates could have a material adverse impact on the fair value of our investment portfolio while increasing the costs associated with our lease commitments. Conversely, declines in interest rates could have a material impact on interest earnings for our investment portfolio. We do not currently hedge these interest rate exposures.

INVESTMENTS

The following table presents the hypothetical changes in fair values in the financial instruments held at July 29, 2000 that are sensitive to changes in interest rates. These instruments are not leveraged and are held for purposes other than trading. The modeling technique used measures the change in fair values arising from selected potential changes in interest rates. Market changes reflect immediate hypothetical parallel shifts in the yield curve of plus or minus 50 basis points ("BPS"), 100 BPS, and 150 BPS over a 12-month horizon. Beginning fair values represent the principal plus accrued interest and dividends of the interest rate-sensitive financial instruments at July 29, 2000. Ending fair values are the market principal plus accrued interest, dividends, and reinvestment income at a 12-month horizon. The following table estimates the fair value of the portfolio at a 12-month horizon (in millions):

Issuer	Valuation of Securities Given an Interest Rate Decrease of X Basis Points (150 BPS)	(100 BPS)	(50 BPS)	Fair Value as of July 29, 2000	Valuation of Securities Given an Interest Rate Increase of X Basis Points 50 BPS	100 BPS	150 BPS
U.S. government notes and bonds	$2,350	$2,329	$2,307	$2,285	$2,262	$2,240	$2,218
State, municipal, and county government notes and bonds	3,666	3,632	3,598	3,564	3,529	3,494	3,459
Corporate notes and bonds	3,296	3,266	3,235	3,204	3,173	3,141	3,110
Total	$9,312	$9,227	$9,140	$9,053	$8,964	$8,875	$8,787

A 50 BPS move in the Federal Funds Rate has occurred in nine of the last 10 years; a 100 BPS move in the Federal Funds Rate has occurred in six of the last 10 years; and a 150 BPS move in the Federal Funds Rate has occurred in four of the last 10 years.

QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The following analysis presents the hypothetical changes in fair values of public equity investments that are sensitive to changes in the stock market. These equity securities are held for purposes other than trading. The modeling technique used measures the hypothetical change in fair values arising from selected hypothetical changes in each stock's price. Stock price fluctuations of plus or minus 15%, plus or minus 35%, and plus or minus 50% were selected based on the probability of their occurrence. The following table estimates the fair value of the publicly traded corporate equities at a 12-month horizon (in millions):

	Valuation of Securities Given X% Decrease in Each Stock's Price			Fair Value as of	Valuation of Securities Given X% Increase in Each Stock's Price		
	(50%)	(35%)	(15%)	July 29, 2000	15%	35%	50%
Corporate equities	$3,112	$4,046	$5,291	$6,225	$7,159	$8,404	$9,337

Our equity portfolio consists of securities with characteristics that most closely match the S&P Index or companies traded on the NASDAQ National Market. The NASDAQ Composite Index has shown a 15% movement in each of the last three years and a 35% and 50% movement in at least one of the last three years.

We also have an investment in KPMG Consulting, Inc. in the principal amount of $1.05 billion of Series A Mandatorily Redeemable Convertible Preferred Stock, which carries a 6% dividend rate on the original issue price until converted to common stock. Conversion is at our option upon or after the completion of an initial public offering of KPMG Consulting, Inc. We have not included the investment in the above sensitivity analyses due to the nature of this investment.

LEASES

We are exposed to interest rate risk associated with leases on our facilities where payments are tied to the London Interbank Offered Rate ("LIBOR"). We have evaluated the hypothetical change in lease obligations held at July 29, 2000 due to changes in the LIBOR. The modeling technique used measures hypothetical changes in lease obligations arising from selected hypothetical changes in the LIBOR. The hypothetical market changes reflected immediate parallel shifts in the LIBOR curve of plus or minus 50 BPS, 100 BPS, and 150 BPS over a 12-month period. The results of this analysis were not material in comparison to our financial results.

FOREIGN EXCHANGE FORWARD AND OPTION CONTRACTS

We enter into foreign exchange forward contracts to offset the impact of currency fluctuations on certain nonfunctional currency assets and liabilities, primarily denominated in Australian, Canadian, Japanese, Korean, and several European currencies, primarily the euro and British pound. We also periodically hedge anticipated transactions with purchased currency options.

The foreign exchange forward and option contracts we enter into generally have original maturities ranging from one to three months. We do not enter into foreign exchange forward and option contracts for trading purposes. We do not expect gains or losses on these contracts to have a material impact on our financial results (see Note 8 to the Consolidated Financial Statements).

CONSOLIDATED STATEMENTS OF OPERATIONS

(In millions, except per-share amounts)

Years Ended	July 29, 2000	July 31, 1999	July 25, 1998
NET SALES	**$18,928**	$12,173	$8,489
Cost of sales	**6,746**	4,259	2,924
GROSS MARGIN	**12,182**	7,914	5,565
Operating expenses:			
Research and development	**2,704**	1,663	1,052
Sales and marketing	**3,946**	2,465	1,579
General and administrative	**633**	381	247
Amortization of goodwill and purchased intangible assets	**291**	61	23
In-process research and development	**1,373**	471	594
Total operating expenses	**8,947**	5,041	3,495
OPERATING INCOME	**3,235**	2,873	2,070
Net gains realized on minority investments	**531**	–	5
Interest and other income, net	**577**	330	196
INCOME BEFORE PROVISION FOR INCOME TAXES	**4,343**	3,203	2,271
Provision for income taxes	**1,675**	1,180	940
NET INCOME	**$ 2,668**	$ 2,023	$1,331
Net income per common share—basic	**$ 0.39**	$ 0.30	$ 0.21
Net income per common share—diluted	**$ 0.36**	$ 0.29	$ 0.20
Shares used in per-common share calculation—basic	**6,917**	6,646	6,312
Shares used in per-common share calculation—diluted	**7,438**	7,062	6,658

See Notes to Consolidated Financial Statements.

CONSOLIDATED BALANCE SHEETS
(In millions, except par value)

	July 29, 2000	July 31, 1999
ASSETS		
Current assets:		
Cash and cash equivalents	**$ 4,234**	$ 913
Short-term investments	**1,291**	1,189
Accounts receivable, net of allowances for doubtful accounts of $43 at 2000 and $27 at 1999	**2,299**	1,250
Inventories, net	**1,232**	658
Deferred tax assets	**1,091**	580
Prepaid expenses and other current assets	**963**	171
Total current assets	**11,110**	4,761
Investments	**13,688**	7,032
Restricted investments	**1,286**	1,080
Property and equipment, net	**1,426**	825
Goodwill and purchased intangible assets, net	**4,087**	460
Lease receivables	**527**	500
Other assets	**746**	235
TOTAL ASSETS	**$32,870**	$14,893
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	**$ 739**	$ 374
Income taxes payable	**233**	630
Accrued compensation	**1,317**	679
Deferred revenue	**1,386**	724
Other accrued liabilities	**1,521**	631
Total current liabilities	**5,196**	3,038
Commitments and contingencies (Note 8)		
Deferred tax liabilities	**1,132**	–
Minority interest	**45**	44
Shareholders' equity:		
Preferred stock, no par value: 5 shares authorized; none issued and outstanding	**–**	–
Common stock and additional paid-in capital, $0.001 par value: 20,000 shares authorized; 7,138 and 6,821 shares issued and outstanding at 2000 and 1999, respectively	**14,609**	5,731
Retained earnings	**8,358**	5,782
Accumulated other comprehensive income	**3,530**	298
Total shareholders' equity	**26,497**	11,811
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	**$32,870**	$14,893

See Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS
(In millions)

Years Ended	July 29, 2000	July 31, 1999	July 25, 1998
Cash flows from operating activities:			
Net income	**$ 2,668**	$ 2,023	$ 1,331
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	**863**	489	329
Provision for doubtful accounts	**40**	19	43
Provision for inventory allowances	**339**	151	161
Deferred income taxes	**(782)**	(247)	(76)
Tax benefits from employee stock option plans	**2,495**	837	422
Adjustment to conform fiscal year ends of pooled acquisitions	**(18)**	1	–
In-process research and development	**1,279**	379	436
Gains on minority investments	**(92)**	–	–
Change in operating assets and liabilities:			
Accounts receivable	**(1,043)**	45	(166)
Inventories	**(887)**	(443)	(267)
Prepaid expenses and other current assets	**(249)**	(101)	21
Accounts payable	**286**	111	32
Income taxes payable	**(365)**	217	155
Accrued compensation	**576**	285	123
Deferred revenue	**662**	385	156
Other accrued liabilities	**369**	174	165
Net cash provided by operating activities	**6,141**	4,325	2,865
Cash flows from investing activities:			
Purchases of short-term investments	**(2,473)**	(1,250)	(1,611)
Proceeds from sales and maturities of short-term investments	**2,481**	1,660	1,751
Purchases of investments	**(14,778)**	(5,632)	(3,561)
Proceeds from sales and maturities of investments	**13,240**	1,994	1,107
Purchases of restricted investments	**(458)**	(1,101)	(527)
Proceeds from sales and maturities of restricted investments	**206**	560	337
Acquisition of property and equipment	**(1,086)**	(602)	(429)
Purchases of technology licenses	**(444)**	(95)	–
Acquisition of businesses, net of cash and cash equivalents	**24**	(19)	–
Net investment in lease receivables	**(535)**	(310)	(171)
Other	**(554)**	(190)	1
Net cash used in investing activities	**(4,377)**	(4,985)	(3,103)
Cash flows from financing activities:			
Issuance of common stock	**1,564**	947	555
Other	**(7)**	7	(7)
Net cash provided by financing activities	**1,557**	954	548
Net increase in cash and cash equivalents	**3,321**	294	310
Cash and cash equivalents, beginning of fiscal year	**913**	619	309
Cash and cash equivalents, end of fiscal year	**$ 4,234**	$ 913	$ 619

See Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

(In millions)

	Common Stock Number of Shares	Common Stock and Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income	Total Shareholders' Equity
BALANCE AT JULY 26, 1997	6,163	$ 1,814	$2,478	$ 40	$ 4,332
Net income	–	–	1,331	–	1,331
Change in net unrealized gains on investments	–	–	–	28	28
Translation adjustments	–	–	–	(10)	(10)
Comprehensive income	–	–	–	–	1,349
Issuance of common stock	280	555	–	–	555
Tax benefits from employee stock option plans	–	422	–	–	422
Pooling of interests acquisitions	6	12	(9)	–	3
Purchase acquisitions	42	536	–	–	536
BALANCE AT JULY 25, 1998	6,491	3,339	3,800	58	7,197
Net income	–	–	2,023	–	2,023
Change in net unrealized gains on investments	–	–	–	234	234
Translation adjustments	–	–	–	6	6
Comprehensive income	–	–	–	–	2,263
Issuance of common stock	300	947	–	–	947
Tax benefits from employee stock option plans	–	837	–	–	837
Pooling of interests acquisitions	4	38	(42)	–	(4)
Purchase acquisitions	26	570	–	–	570
Adjustment to conform fiscal year ends of pooled acquisitions	–	–	1	–	1
BALANCE AT JULY 31, 1999	6,821	5,731	5,782	298	11,811
Net income	–	–	2,668	–	2,668
Change in net unrealized gains on investments	–	–	–	3,240	3,240
Translation adjustments	–	–	–	(8)	(8)
Comprehensive income	–	–	–	–	5,900
Issuance of common stock	219	1,564	–	–	1,564
Tax benefits from employee stock option plans	–	3,077	–	–	3,077
Pooling of interests acquisitions	20	75	(74)	–	1
Purchase acquisitions	78	4,162	–	–	4,162
Adjustment to conform fiscal year ends of pooled acquisitions	–	–	(18)	–	(18)
BALANCE AT JULY 29, 2000	**7,138**	**$14,609**	**$8,358**	**$3,530**	**$26,497**

See Notes to Consolidated Financial Statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. DESCRIPTION OF BUSINESS

Cisco Systems, Inc. and its subsidiaries ("Cisco" or the "Company") is the worldwide leader in networking for the Internet. Cisco hardware, software, and service offerings are used to create Internet solutions so that individuals, companies, and countries have seamless access to information—regardless of differences in time and place. Cisco solutions provide competitive advantage to our customers through more efficient and timely exchange of information, which in turn leads to cost savings, process efficiencies, and closer relationships with their customers, prospects, business partners, suppliers, and employees. These solutions form the networking foundation for companies, universities, utilities, and government agencies worldwide.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Fiscal Year The Company's fiscal year is the 52 or 53 weeks ending on the last Saturday in July. Fiscal 2000, 1999, and 1998 were 52-week, 53-week, and 52-week fiscal years, respectively.

Principles of Consolidation The Consolidated Financial Statements include the accounts of Cisco Systems, Inc. and its subsidiaries. All significant intercompany accounts and transactions have been eliminated.

Cash and Cash Equivalents The Company considers all highly liquid investments purchased with an original or remaining maturity of less than three months at the date of purchase to be cash equivalents. Substantially all cash and cash equivalents are custodied with three major financial institutions.

Investments The Company's investments comprise U.S., state, and municipal government obligations; corporate debt securities; and public corporate equity securities. Investments with maturities of less than one year are considered short-term and are carried at fair value. All investments are primarily held in the Company's name and custodied with two major financial institutions. The specific identification method is used to determine the cost of securities disposed. At July 29, 2000 and July 31, 1999, substantially all of the Company's investments were classified as available for sale. Unrealized gains and losses on these investments are included as a separate component of shareholders' equity, net of any related tax effect.

The Company also has certain other minority investments in nonpublicly traded companies. These investments are included in other assets on the Company's balance sheet and are generally carried at cost. The Company monitors these investments for impairment and makes appropriate reductions in carrying values when necessary.

Inventories Inventories are stated at the lower of cost or market. Cost is computed using standard cost, which approximates actual cost on a first-in, first-out basis.

Restricted Investments Restricted investments consist of U.S. government obligations with maturities of more than one year. These investments are carried at fair value and are restricted as to withdrawal. Restricted investments are held in the Company's name and custodied with two major financial institutions.

Fair Value of Financial Instruments Carrying amounts of certain of the Company's financial instruments, including cash and cash equivalents, accrued compensation, and other accrued liabilities, approximate fair value because of their short maturities. The fair values of investments are determined using quoted market prices for those securities or similar financial instruments.

Concentrations Cash and cash equivalents are primarily maintained with three major financial institutions in the United States. Deposits held with banks may exceed the amount of insurance provided on such deposits. Generally, these deposits may be redeemed upon demand and, therefore, bear minimal risk.

The Company performs ongoing credit evaluations of its customers and, with the exception of certain financing transactions, does not require collateral from its customers.

The Company receives certain of its components from sole suppliers. Additionally, the Company relies on a limited number of hardware manufacturers. The inability of any supplier or manufacturer to fulfill supply requirements of the Company could materially impact future operating results.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Revenue Recognition The Company generally recognizes product revenue when persuasive evidence of an arrangement exists, delivery has occurred, fee is fixed or determinable, and collectibility is probable. Revenue from service obligations is deferred and generally recognized ratably over the period of the obligation. The Company makes certain sales to partners in two-tier distribution channels. These partners are generally given privileges to return a portion of inventory and participate in various cooperative marketing programs. The Company recognizes revenue to two-tier distributors based on estimates which approximate the point products have been sold by the distributors and also maintains accruals and allowances for all cooperative marketing and other programs. The Company accrues for warranty costs, sales returns, and other allowances based on its experience.

Lease Receivables Cisco provides a variety of lease financing services to its customers to build, maintain, and upgrade their networks. Lease receivables represent the principal balance remaining in sales-type and direct-financing leases under these programs. These leases typically have two to three year terms and are collateralized by a security interest in the underlying assets.

Advertising Costs The Company expenses all advertising costs as incurred.

Software Development Costs Software development costs, which are required to be capitalized pursuant to Statement of Financial Accounting Standards No. 86, "Accounting for the Costs of Computer Software to Be Sold, Leased, or Otherwise Marketed," have not been material to date.

Depreciation and Amortization Property and equipment are stated at cost less accumulated depreciation and amortization. Depreciation and amortization is computed using the straight-line method over the estimated useful lives of the assets. Estimated useful lives of 24 to 30 months are used on computer equipment and related software and production and engineering equipment and five years for office equipment, furniture, and fixtures. Depreciation and amortization of leasehold improvements is computed using the shorter of the remaining lease term or five years.

Goodwill and Purchased Intangible Assets Goodwill and purchased intangible assets are carried at cost less accumulated amortization. Amortization is computed using the straight-line method over the economic lives of the respective assets, generally three to five years.

Income Taxes Income tax expense is based on pre-tax financial accounting income. Deferred tax assets and liabilities are recognized for the expected tax consequences of temporary differences between the tax bases of assets and liabilities and their reported amounts.

Computation of Net Income per Common Share Basic net income per common share is computed using the weighted-average number of common shares outstanding during the period. Diluted net income per common share is computed using the weighted-average number of common and dilutive common equivalent shares outstanding during the period. Dilutive common equivalent shares consist of stock options. Share and per-common share data for all periods presented reflect the two-for-one stock split effective March 2000.

Foreign Currency Translation Assets and liabilities of non-U.S. subsidiaries that operate in a local currency environment are translated to U.S. dollars at exchange rates in effect at the balance sheet date with the resulting translation adjustments recorded directly to a separate component of shareholders' equity. Income and expense accounts are translated at average exchange rates during the year. Where the U.S. dollar is the functional currency, translation adjustments are recorded in income.

Derivatives The Company enters into foreign exchange forward contracts to minimize the short-term impact of foreign currency fluctuations on assets and liabilities denominated in currencies other than the functional currency of the reporting entity. All foreign exchange forward contracts are highly inversely correlated to the hedged items and are designated as, and considered effective as, hedges of the underlying assets or liabilities. Gains and losses on the contracts are included in interest and other income, net, and offset foreign exchange gains or losses from the revaluation of intercompany balances or other current assets and liabilities denominated in currencies other than the functional currency of the reporting entity. Fair values of foreign exchange forward contracts are determined using published rates. If a derivative contract terminates prior to maturity, the investment is shown at its fair value with the resulting gain or loss reflected in interest and other income, net. The Company periodically hedges anticipated transactions with purchased currency options. The premium paid is amortized over the life of the option while any intrinsic value is recognized in income during the same period as the hedged transaction.

Minority Interest Minority interest represents the preferred stockholders' proportionate share of the equity of Cisco Systems, K.K. (Japan). At July 29, 2000, the Company owned all issued and outstanding common stock amounting to 73.2% of the voting rights. Each share of preferred stock is convertible into one share of common stock at any time at the option of the holder.

Use of Estimates The preparation of financial statements and related disclosures in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the Consolidated Financial Statements and accompanying notes. Estimates are used for, but not limited to, the accounting for the allowance for doubtful accounts, inventory allowances, depreciation and amortization, sales returns, warranty costs, taxes, and contingencies. Actual results could differ from these estimates.

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

Recent Accounting Pronouncements In June 1998, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards No. 133, "Accounting for Derivative Instruments and Hedging Activities" ("SFAS 133"). SFAS 133, as amended, establishes accounting and reporting standards for derivative instruments and hedging activities. It requires an entity to recognize all derivatives as either assets or liabilities on the balance sheet and measure those instruments at fair value. Management does not expect the initial adoption of SFAS 133 to have a material effect on the Company's operations or financial position. The Company is required to adopt SFAS 133 in the first quarter of fiscal 2001.

In September 1999, the FASB issued Emerging Issues Task Force Topic No. D-83, "Accounting for Payroll Taxes Associated with Stock Option Exercises" ("EITF D-83"). EITF D-83 requires that payroll tax paid on the difference between the exercise price and the fair value of acquired stock in association with an employee's exercise of stock options be recorded as operating expenses. Payroll tax on stock option exercises of $51 million was expensed in fiscal 2000.

In December 1999, the Securities and Exchange Commission ("SEC") issued Staff Accounting Bulletin No. 101, "Revenue Recognition in Financial Statements" ("SAB 101"). SAB 101, as amended, summarizes certain of the SEC's views in applying generally accepted accounting principles to revenue recognition in financial statements. At this time, management does not expect the adoption of SAB 101 to have a material effect on the Company's operations or financial position; however, the SEC's final guidance for implementation has not been released to date. The Company is required to adopt SAB 101 in the fourth quarter of fiscal 2001.

Reclassifications Certain reclassifications have been made to prior year balances in order to conform to the current year presentation.

3. BUSINESS COMBINATIONS

Pooling of Interests Combinations

In fiscal 2000, the Company acquired StratumOne Communications, Inc. ("StratumOne"); TransMedia Communications, Inc. ("TransMedia"); Cerent Corporation ("Cerent"); WebLine Communications Corporation ("WebLine"); SightPath, Inc. ("SightPath"); InfoGear Technology Corporation ("InfoGear"); and ArrowPoint Communications, Inc. ("ArrowPoint"), which were accounted for as poolings of interests. All historical financial information has been restated to reflect these acquisitions. In addition, the historical financial information has been restated to reflect the acquisition of Fibex Systems ("Fibex"), which was completed in the fourth quarter of fiscal 1999 and accounted for as a pooling of interests. These transactions are summarized as follows (in millions):

Acquisition Date	Acquired Company	Shares of Cisco Stock Issued, Including Options Assumed	Fair Value of Acquisition
May 1999	Fibex	11.5	$ 314
September 1999	StratumOne	13.3	$ 435
September 1999	TransMedia	13.9	$ 407
November 1999	Cerent	200.0	$6,900
November 1999	WebLine	8.6	$ 325
May 2000	SightPath	11.4	$ 800
June 2000	InfoGear	4.7	$ 301
June 2000	ArrowPoint	90.2	$5,700

All of these acquired companies used a calendar year end. In order for all companies to operate on the same fiscal year, operations for the one-month period ending July 31, 1999, which were not significant to the Company, have been reflected as an adjustment to retained earnings in fiscal 2000. No significant adjustments were necessary to conform accounting policies. However, the companies' historical results have been adjusted to reflect the elimination of previously provided valuation allowances on deferred tax assets. There were no intercompany transactions requiring elimination in any period presented. The following table shows the historical results for the periods prior to the mergers of these entities (in millions):

	Nine Months Ended	Years Ended	
	April 29, 2000	July 31, 1999	July 25, 1998
Net sales:			
Cisco	**$13,147**	$12,154	$8,488
Fibex	**–**	3	–
StratumOne	**–**	–	–
TransMedia	**–**	–	–
Cerent	**35**	10	–
WebLine	**1**	3	1
SightPath	**–**	–	–
InfoGear	**–**	–	–
ArrowPoint	**25**	3	–
Total	**$13,208**	$12,173	$8,489
Net income (loss):			
Cisco	**$ 1,932**	$ 2,096	$1,355
Fibex	**–**	(13)	(3)
StratumOne	**(3)**	(6)	(1)
TransMedia	**(4)**	(7)	–
Cerent	**(15)**	(31)	(9)
WebLine	**(3)**	(4)	(2)
SightPath	**(8)**	(2)	–
InfoGear	**(15)**	(5)	(5)
ArrowPoint	**(12)**	(5)	(4)
Total	**$ 1,872**	$ 2,023	$1,331

In fiscal 1999, the Company acquired GeoTel Communications Corporation and approximately 68 million shares of common stock were exchanged and options were assumed for a fair value of $2 billion. The transaction was accounted for as a pooling of interests and all periods presented prior to fiscal 1999 were restated.

Other Pooling of Interests Combinations Completed as of July 29, 2000

The Company has also completed a number of other pooling transactions during the three years ended July 29, 2000. The historical operations of these entities were not material to the Company's consolidated operations on either an individual or aggregate basis; therefore, prior period financial statements have not been restated for these acquisitions. These transactions are summarized as follows (in millions):

Fiscal Year	Acquired Company	Shares of Cisco Stock Issued, Including Options Assumed	Fair Value of Acquisition
1998	Precept Software, Inc.	6.0	$ 84
1999	Sentient Networks, Inc.	4.0	$131
2000	Cocom A/S	**1.9**	**$ 66**
2000	V-Bits, Inc.	**2.8**	**$128**
2000	Growth Networks, Inc.	**5.6**	**$355**
2000	Altiga Networks, Inc.	**6.3**	**$335**
2000	Compatible Systems Corporation	**3.8**	**$232**

Purchase Combinations

During the three years ended July 29, 2000, the Company completed a number of purchase acquisitions. The Consolidated Financial Statements include the operating results of each business from the date of acquisition. Pro forma results of operations have not been presented because the effects of these acquisitions were not material on either an individual or an aggregate basis.

The amounts allocated to in-process research and development ("in-process R&D") were determined through established valuation techniques in the high-technology communications equipment industry and were expensed upon acquisition because technological feasibility had not been established and no future alternative uses existed. Amounts allocated to goodwill and purchased intangible assets are amortized on a straight-line basis over periods not exceeding five years. A summary of purchase transactions is outlined as follows (in millions):

Acquired Company	Consideration	In-Process R&D Expense	Form of Consideration and Other Notes to Acquisition
FISCAL 2000			
Monterey Networks, Inc.	**$ 517**	**$354**	Common stock and options assumed; $14 in liabilities assumed; goodwill and other intangibles recorded of $154
The optical systems business of Pirelli S.p.A.	**$2,018**	**$245**	Common stock; $362 in liabilities assumed; goodwill and other intangibles recorded of $1,717
Aironet Wireless Communications, Inc.	**$ 835**	**$243**	Common stock and options assumed; $34 in liabilities assumed; goodwill and other intangibles recorded of $589
Atlantech Technologies	**$ 179**	**$ 63**	Cash of $92; common stock and options assumed; $1 in liabilities assumed; goodwill and other intangibles recorded of $140
JetCell, Inc.	**$ 203**	**$ 88**	Cash of $5; common stock and options assumed; $2 in liabilities assumed; goodwill and other intangibles recorded of $137
PentaCom, Ltd.	**$ 102**	**$ 49**	Cash of $26; common stock and options assumed; goodwill and other intangibles recorded of $40
Qeyton Systems	**$ 887**	**$260**	Common stock; goodwill and other intangibles recorded of $567
Other	**$ 228**	**$ 71**	Cash of $31; common stock and options assumed; $5 in liabilities assumed; goodwill and other intangibles recorded of $155
FISCAL 1999			
Summa Four, Inc.	$ 129	$ 64	Common stock and options assumed; $16 in liabilities assumed; goodwill and other intangibles recorded of $29
Clarity Wireless, Inc.	$ 153	$ 94	Common stock and options assumed; goodwill and other intangibles recorded of $73
Selsius Systems, Inc.	$ 134	$ 92	Cash of $111; options assumed; goodwill and other intangibles recorded of $41
PipeLinks, Inc.	$ 118	$ 99	Common stock and options assumed; goodwill and other intangibles recorded of $11
Amteva Technologies, Inc.	$ 159	$ 81	Common stock and options assumed; $9 in liabilities assumed; goodwill and other intangibles recorded of $85
Other	$ 58	$ 41	Common stock and options assumed; goodwill and other intangibles recorded of $18
FISCAL 1998			
Dagaz Technologies, Inc.	$ 130	$127	Cash of $108; $18 in common stock; liabilities assumed of $4
LightSpeed International, Inc.	$ 161	$143	Common stock and options assumed; other intangibles recorded of $15
WheelGroup Corporation	$ 124	$ 97	Common stock and options assumed; goodwill and other intangibles recorded of $38
NetSpeed International, Inc.	$ 252	$179	Cash of $12; common stock and options assumed; liabilities assumed of $18; goodwill and other intangibles recorded of $76
Other	$ 51	$ 48	Cash of $38 and options assumed

Other Purchase Combinations Completed as of July 29, 2000

In fiscal 2000, the Company acquired Maxcomm Technologies, Inc.; Calista, Inc.; Tasmania Network Systems, Inc.; Internet Engineering Group, LLC; Worldwide Data Systems, Inc.; and Seagull Networks, Ltd. for a total purchase price of $228 million, paid in common stock and cash. Total in-process R&D related to these acquisitions amounted to $71 million.

Total in-process R&D expense in fiscal 2000, 1999, and 1998 was $1.37 billion, $471 million, and $594 million, respectively. The in-process R&D expense that was attributable to stock consideration for the same periods was $1.28 billion, $379 million, and $436 million, respectively.

4. BALANCE SHEET DETAIL

The following tables provide details of selected balance sheet items (in millions):

	July 29, 2000	July 31, 1999
INVENTORIES, NET:		
Raw materials	**$ 145**	$ 143
Work in process	**472**	198
Finished goods	**496**	282
Demonstration systems	**119**	35
Total	**$1,232**	$ 658
PROPERTY AND EQUIPMENT, NET:		
Leasehold improvements	**$ 607**	$ 289
Computer equipment and related software	**908**	639
Production and engineering equipment	**407**	238
Office equipment, furniture, and fixtures	**1,083**	685
	3,005	1,851
Less, accumulated depreciation and amortization	**(1,579)**	(1,026)
Total	**$1,426**	$ 825
GOODWILL AND PURCHASED INTANGIBLE ASSETS, NET:		
Goodwill	**$2,937**	$ 157
Purchased intangible assets	**1,558**	395
	4,495	552
Less, accumulated amortization	**(408)**	(92)
Total	**$4,087**	$ 460

The following table presents the details of the amortization of goodwill and purchased intangible assets as reported in the Consolidated Statements of Operations:

Years Ended	July 29, 2000	July 31, 1999	July 25, 1998
Reported as:			
Cost of sales	**$ 25**	$ 1	$ –
Operating expenses	**291**	61	23
Total	**$316**	$62	$23

5. LEASE RECEIVABLES

Lease receivables represent sales-type and direct-financing leases resulting from the sale of the Company's and complementary third-party products and services. These lease arrangements typically have terms from two to three years and are usually collateralized by a security interest in the underlying assets. The net lease receivables are summarized as follows (in millions):

	July 29, 2000	July 31, 1999
Gross lease receivables	**$1,310**	$663
Unearned income and other reserves	**(195)**	(83)
Total	**1,115**	580
Less, current portion	**(588)**	(80)
Long-term lease receivables, net	**$ 527**	$500

Contractual maturities of the gross lease receivables at July 29, 2000 were $588 million in fiscal 2001, $354 million in fiscal 2002, $337 million in fiscal 2003, $29 million in fiscal 2004, and $2 million in fiscal 2005. Actual cash collections may differ from the contractual maturities due to early customer buyouts or refinancings. The current portion of lease receivables is included in prepaid expenses and other current assets.

6. INVESTMENTS

The following tables summarize the Company's investments in securities (in millions):

JULY 29, 2000	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. government notes and bonds	**$ 2,317**	**$ –**	**$ (32)**	**$ 2,285**
State, municipal, and county government notes and bonds	**3,592**	**13**	**(41)**	**3,564**
Corporate notes and bonds	**3,222**	**1**	**(19)**	**3,204**
Corporate equity securities	**641**	**5,621**	**(37)**	**6,225**
Mandatorily redeemable convertible preferred stock	**987**	**–**	**–**	**987**
Total	**$10,759**	**$5,635**	**$(129)**	**$16,265**
Reported as:				
Short-term investments				**$ 1,291**
Investments				**13,688**
Restricted investments				**1,286**
Total				**$16,265**

JULY 31, 1999	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. government notes and bonds	$ 2,187	$ –	$ (29)	$ 2,158
State, municipal, and county government notes and bonds	5,177	5	(44)	5,138
Corporate notes and bonds	1,145	–	(17)	1,128
Corporate equity securities	288	615	(26)	877
Total	$ 8,797	$ 620	$(116)	$ 9,301
Reported as:				
Short-term investments				$ 1,189
Investments				7,032
Restricted investments				1,080
Total				$ 9,301

Net gains realized on minority investments were $531 million in fiscal 2000. The net gains realized on minority investments that were attributable to noncash activity were $92 million in fiscal 2000. The net gains realized on minority investments were not material in fiscal 1999 and were $5 million in fiscal 1998.

The following table summarizes debt investment and mandatorily redeemable convertible preferred stock maturities (including restricted investments) at July 29, 2000 (in millions):

	Amortized Cost	Fair Value
Less than one year	$ 1,753	$ 1,744
Due in 1–2 years	1,930	1,922
Due in 2–5 years	4,218	4,161
Due after 5 years	2,217	2,213
Total	$10,118	$10,040

7. LINE OF CREDIT

At July 29, 2000, the Company had a syndicated credit agreement under the terms of which a group of banks committed a maximum of $500 million on an unsecured, revolving basis for borrowings of various maturities. The commitments made under this agreement expire on July 1, 2002. Under the terms of the agreement, borrowings bear interest at a spread over the London Interbank Offered Rate based on certain financial criteria and third-party rating assessments. As of July 29, 2000, this spread was 17.5 basis points. From this spread, a commitment fee of 5.5 basis points is assessed against any undrawn amounts. The agreement includes a single financial covenant that places a variable floor on tangible net worth, as defined, if certain leverage ratios are exceeded. There have been no borrowings under this agreement to date.

8. COMMITMENTS AND CONTINGENCIES

Leases

The Company has entered into several agreements to lease 448 acres of land located in San Jose, California, where it has established its headquarters operations, and 759 acres of land located in Boxborough, Massachusetts; Salem, New Hampshire; Richardson, Texas; and Research Triangle Park, North Carolina, where it has expanded certain research and development and customer-support activities.

All of the leases have initial terms of five to seven years and options to renew for an additional three to five years, subject to certain conditions. At any time during the terms of these leases, the Company may purchase the land. If the Company elects not to purchase the land at the end of each of the leases, the Company has guaranteed a residual value of $624 million.

The Company has also entered into agreements to lease certain buildings standing or to be constructed on the land described above. The lessors of the buildings have committed to fund up to a maximum of $1.40 billion (subject to reductions based on certain conditions in the respective leases) for the construction of the buildings, with the portion of the committed amount actually used to be determined by the Company. Rent obligations for the buildings commenced on various dates and will expire at the same time as the land leases.

The Company has options to renew the building leases for an additional three to five years, subject to certain conditions. The Company may, at its option, purchase the buildings during or at the end of the terms of the leases at approximately the amount expended by the lessors to construct the buildings. If the Company does not exercise the purchase options by the end of the leases, the Company will guarantee a residual value of the buildings as determined at the lease inception date of each agreement (approximately $748 million at July 29, 2000).

As part of the above lease transactions, the Company restricted $1.29 billion of its investment securities as collateral for specified obligations of the lessors under the leases. These investment securities are restricted as to withdrawal and are managed by a third party subject to certain limitations under the Company's investment policy. In addition, the Company must maintain a minimum consolidated tangible net worth, as defined.

The Company also leases office space in Santa Clara, California; Chelmsford, Massachusetts; and for its various U.S. and international sales offices.

Future annual minimum lease payments under all noncancelable operating leases as of July 29, 2000 are as follows (in millions):

Fiscal Year	
2001	$ 302
2002	299
2003	310
2004	251
2005	237
Thereafter	1,506
Total	$2,905

Rent expense totaled $229 million, $123 million, and $90 million for fiscal 2000, 1999, and 1998, respectively.

Foreign Exchange Forward and Option Contracts

The Company conducts business on a global basis in several major currencies. As such, it is exposed to adverse movements in foreign currency exchange rates. The Company enters into foreign exchange forward contracts to reduce the impact of certain currency exposures. These contracts hedge exposures associated with nonfunctional currency assets and liabilities denominated in Australian, Canadian, Japanese, Korean, and several European currencies, primarily the euro and British pound.

The Company does not enter into foreign exchange forward contracts for trading purposes. Gains and losses on the contracts are included in interest and other income, net, and offset foreign exchange gains or losses from the revaluation of intercompany balances or other current assets and liabilities denominated in currencies other than the functional currency of the reporting entity. The Company's foreign exchange forward contracts generally range from one to three months in original maturity.

The Company periodically hedges anticipated transactions with purchased currency options. A purchased currency option's premium is amortized over the life of the option while any intrinsic value is recognized in income during the same period as the hedged transaction. The deferred premium and intrinsic value from hedging anticipated transactions were not material at July 29, 2000. In the unlikely event that the underlying transaction terminates or becomes improbable, the remaining premium or deferred intrinsic value will be recorded in the Consolidated Statements of Operations. The Company does not purchase currency options for trading purposes. Foreign exchange forward and option contracts as of July 29, 2000 are summarized as follows (in millions):

	Notional Amount	Carrying Value	Fair Value
Forward contracts:			
Assets	$1,377	$(5)	$(15)
Liabilities	$1,500	$12	$ 37
Option contracts:			
Assets	$ 561	$12	$ 14

The Company's foreign exchange forward and option contracts contain credit risk to the extent that its bank counterparties may be unable to meet the terms of the agreements. The Company minimizes such risk by limiting its counterparties to major financial institutions. In addition, the potential risk of loss with any one party resulting from this type of credit risk is monitored. Management does not expect any material losses as a result of default by other parties.

Legal Proceedings

The Company is subject to legal proceedings, claims, and litigation arising in the ordinary course of business. While the outcome of these matters is currently not determinable, management does not expect that the ultimate costs to resolve these matters will have a material adverse effect on the Company's consolidated financial position, results of operations, or cash flows.

9. SHAREHOLDERS' EQUITY

Authorized Shares

On November 10, 1999, the shareholders of the Company approved an increase to the authorized number of shares of common stock from 5.40 billion to 10 billion shares. On March 20, 2000, the Board of Directors of the Company approved an increase to the authorized number of shares of common stock from 10 billion to 20 billion shares relating to the two-for-one stock split distributed on March 22, 2000.

Stock Split

The Board of Directors authorized the splitting of the Company's common stock on a two-for-one basis for shareholders of record on February 22, 2000 and the resulting shares from the split were distributed on March 22, 2000. All references to share and per-share data for all periods presented have been adjusted to give effect to this two-for-one stock split.

Shareholders' Rights Plan

In June 1998, the Board of Directors approved a Shareholders' Rights Plan ("Rights Plan"). The Rights Plan is intended to protect shareholders' rights in the event of an unsolicited takeover attempt. It is not intended to prevent a takeover of the Company on terms that are favorable and fair to all shareholders and will not interfere with a merger approved by the Board of Directors. Each right entitles shareholders to buy a unit equal to a portion of a new share of Series A Preferred Stock of the Company. The rights will be exercisable only if a person or a group acquires or announces a tender or exchange offer to acquire 15% or more of the Company's common stock.

In the event the rights become exercisable, the Rights Plan allows for Cisco shareholders to acquire, at an exercise price of $108 per right owned, stock of the surviving corporation having a market value of $217, whether or not Cisco is the surviving corporation. The rights, which expire in June 2008, are redeemable for $0.00017 per right at the approval of the Board of Directors.

Preferred Stock

Under the terms of the Company's Articles of Incorporation, the Board of Directors may determine the rights, preferences, and terms of the Company's authorized but unissued shares of preferred stock.

Comprehensive Income

The components of comprehensive income, net of tax, are as follows (in millions):

Years Ended	July 29, 2000	July 31, 1999	July 25, 1998
Net income	**$2,668**	$2,023	$1,331
Other comprehensive income (loss):			
Change in net unrealized gains on investments, net of tax of $1,762, $144, and $17 in fiscal 2000, 1999, and 1998, respectively	**3,240**	234	25
Reclassification for net unrealized gains previously included in net income, net of tax of $2 in fiscal 1998	**–**	–	3
Net unrealized gains	**3,240**	234	28
Change in accumulated translation adjustments	**(8)**	6	(10)
Total	**$5,900**	$2,263	$1,349

10. EMPLOYEE BENEFIT PLANS

Employee Stock Purchase Plan

The Company has an Employee Stock Purchase Plan (the "Purchase Plan") under which 222 million shares of common stock have been reserved for issuance. Eligible employees may purchase a limited number of shares of the Company's common stock at 85% of the market value at certain plan-defined dates. The Purchase Plan terminates on January 3, 2005. In fiscal 2000, 1999, and 1998, seven million, 10 million, and 14 million shares, respectively, were issued under the Purchase Plan. At July 29, 2000, 123 million shares were available for issuance under the Purchase Plan.

Employee Stock Option Plans

The Company has two main stock option plans: the 1987 Stock Option Plan (the "Predecessor Plan") and the 1996 Stock Incentive Plan (the "1996 Plan"). The Predecessor Plan was terminated in 1996. All outstanding options under the Predecessor Plan were transferred to the 1996 Plan. However, all outstanding options under the Predecessor Plan continue to be governed by the terms and conditions of the existing option agreements for those grants.

The maximum number of shares under the 1996 Plan was initially limited to the 620 million shares transferred from the Predecessor Plan. However, under the terms of the 1996 Plan, the share reserve increased each December for the three fiscal years beginning with fiscal 1997, by an amount equal to 4.75% of the outstanding shares on the last trading day of the immediately preceding November. In fiscal 1999, the Company's shareholders approved the extension of the automatic share increase provision of the 1996 Plan for an additional three-year period.

Although the Board of Directors has the authority to set other terms, the options are generally 20% or 25% exercisable one year from the date of grant and then ratably over the following 48 or 36 months, respectively. Options issued under the Predecessor Plan generally had terms of four years. New options granted under the 1996 Plan expire no later than nine years from the grant date. A summary of option activity follows (in millions, except per-share amounts):

		Options Outstanding	
	Options Available for Grant	Options	Weighted-Average Exercise Price per Share
BALANCE AT JULY 26, 1997	96	810	$ 4.05
Granted and assumed	(282)	282	10.00
Exercised	–	(168)	2.40
Canceled	48	(48)	4.59
Additional shares reserved	314	–	–
BALANCE AT JULY 25, 1998	176	876	6.25
Granted and assumed	(245)	245	22.22
Exercised	–	(210)	3.09
Canceled	22	(22)	10.85
Additional shares reserved	359	–	–
BALANCE AT JULY 31, 1999	312	889	11.22
Granted and assumed	(295)	295	52.10
Exercised	–	(176)	5.75
Canceled	37	(37)	22.70
Additional shares reserved	339	–	–
BALANCE AT JULY 29, 2000	**393**	**971**	**$24.19**

The Company has, in connection with the acquisitions of various companies, assumed the stock option plans of each acquired company. During fiscal 2000, a total of approximately 31 million shares of the Company's common stock have been reserved for issuance under the assumed plans and the related options are included in the preceding table.

In 1997, the Company adopted a Supplemental Stock Incentive Plan (the "Supplemental Plan") under which options can be granted or shares can be directly issued to eligible employees. Officers and members of the Company's Board of Directors are not eligible to participate in the Supplemental Plan. Nine million shares have been reserved for issuance under the Supplemental Plan, of which 9,000 shares are subject to outstanding options and 66,600 shares have been issued in fiscal 2000.

The following table summarizes information concerning outstanding and exercisable options at July 29, 2000 (in millions, except number of years and per-share amounts):

	Options Outstanding			Options Exercisable	
Range of Exercise Prices	Number Outstanding	Weighted-Average Remaining Contractual Life (in Years)	Weighted-Average Exercise Price per Share	Number Exercisable	Weighted-Average Exercise Price per Share
$ 0.01 – 5.56	229	5.20	$ 5.23	188	$ 4.44
5.57 – 12.27	258	6.16	9.56	162	8.95
12.28 – 28.61	194	7.49	23.59	63	22.47
28.62 – 54.53	241	8.34	49.91	5	31.02
54.54 – 72.56	49	8.64	65.65	–	–
Total	971	6.87	$ 24.19	418	$ 9.22

At July 31, 1999 and July 25, 1998, approximately 370 million and 312 million outstanding options, respectively, were exercisable. The weighted-average exercise prices for outstanding options were $5.75 and $3.64 at July 31, 1999 and July 25, 1998, respectively.

The Company is required under Statement of Financial Accounting Standards No. 123, "Accounting for Stock-Based Compensation" ("SFAS 123"), to disclose pro forma information regarding option grants made to its employees based on specified valuation techniques that produce estimated compensation charges. These amounts have not been reflected in the Company's Consolidated Statements of Operations because no compensation charge arises when the price of the employees' stock options equals the market value of the underlying stock at the grant date, as in the case of options granted to the Company's employees. Pro forma information under SFAS 123 is as follows (in millions, except per-share amounts):

Years Ended	**July 29, 2000**	July 31, 1999	July 25, 1998
Net income—as reported	**$2,668**	$2,023	$1,331
Net income—pro forma	**$1,549**	$1,487	$1,074
Basic net income per common share—as reported	**$ 0.39**	$ 0.30	$ 0.21
Diluted net income per common share—as reported	**$ 0.36**	$ 0.29	$ 0.20
Basic net income per common share—pro forma	**$ 0.22**	$ 0.22	$ 0.17
Diluted net income per common share—pro forma	**$ 0.21**	$ 0.21	$ 0.16

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option pricing model with the following weighted-average assumptions:

	Employee Stock Option Plans			Employee Stock Purchase Plan		
	July 29, 2000	July 31, 1999	July 25,1998	**July 29, 2000**	July 31, 1999	July 25,1998
Expected dividend yield	**0.0%**	0.0%	0.0%	**0.0%**	0.0%	0.0%
Risk-free interest rate	**6.4%**	5.1%	5.7%	**5.3%**	4.9%	5.4%
Expected volatility	**33.9%**	40.2%	35.6%	**43.3%**	47.2%	44.8%
Expected life (in years)	**3.1**	3.1	3.1	**0.5**	0.5	0.5

The Black-Scholes option pricing model was developed for use in estimating the fair value of traded options that have no vesting restrictions and are fully transferable. In addition, option pricing models require the input of highly subjective assumptions including the expected stock price volatility. The Company uses projected volatility rates which are based upon historical volatility rates trended into future years. Because the Company's employee stock options have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect the fair value estimate, in management's opinion, the existing models do not necessarily provide a reliable single measure of the fair value of the Company's options. The weighted-average estimated fair values of employee stock options granted during fiscal 2000, 1999, and 1998 were $19.44, $8.40, and $3.57 per share, respectively.

The above pro forma disclosures under SFAS 123 are also not likely to be representative of the effects on net income and net income per common share in future years, because they do not take into consideration pro forma compensation expense related to grants made prior to fiscal 1996.

Employee 401(k) Plans

The Company sponsors the Cisco Systems, Inc. 401(k) Plan (the "Plan") to provide retirement benefits for its employees. As allowed under Section 401(k) of the Internal Revenue Code, the Plan provides tax-deferred salary deductions for eligible employees. The Company also has other 401(k) plans that it sponsors. These plans arose from acquisitions of other companies and are not material to the Company on either an individual or aggregate basis.

Employees may contribute from 1% to 15% of their annual compensation to the Plan, limited to a maximum annual amount as set periodically by the Internal Revenue Service. The Company matches employee contributions dollar for dollar up to a maximum of $1,500 per year per person. All matching contributions vest immediately. In addition, the Plan provides for discretionary contributions as determined by the Board of Directors. Such contributions to the Plan are allocated among eligible participants in the proportion of their salaries to the total salaries of all participants. The Company's matching contributions to the Plan totaled $34 million, $20 million, and $15 million in fiscal 2000, 1999, and 1998, respectively. No discretionary contributions were made in fiscal 2000, 1999, or 1998.

11. INCOME TAXES

The provision for (benefit from) income taxes consisted of (in millions):

Years Ended	July 29, 2000	July 31, 1999	July 25, 1998
Federal:			
Current	**$1,843**	$ 1,164	$855
Deferred	**(652)**	(221)	(54)
	1,191	943	801
State:			
Current	**282**	112	87
Deferred	**(118)**	(24)	(8)
	164	88	79
Foreign:			
Current	**332**	151	74
Deferred	**(12)**	(2)	(14)
	320	149	60
Total provision for income taxes	**$1,675**	$ 1,180	$940

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The Company paid income taxes of $327 million, $301 million, and $440 million in fiscal 2000, 1999, and 1998, respectively. Income before provision for income taxes consisted of (in millions):

Years Ended	July 29, 2000	July 31, 1999	July 25, 1998
United States	**$2,544**	$2,092	$1,950
International	**1,799**	1,111	321
	$4,343	$3,203	$2,271

The items accounting for the difference between income taxes computed at the federal statutory rate and the provision for income taxes consisted of:

Years Ended	July 29, 2000	July 31, 1999	July 25, 1998
Federal statutory rate	**35.0%**	35.0%	35.0%
Effect of:			
State taxes, net of federal tax benefit	**1.9**	2.2	2.2
Foreign sales corporation	**(1.9)**	(1.6)	(2.4)
Foreign income at other than U.S. rates	**(1.6)**	(1.0)	–
Nondeductible in-process R&D	**8.1**	3.9	6.4
Tax-exempt interest	**(1.8)**	(1.9)	(1.6)
Tax credits	**(1.6)**	(1.2)	(1.4)
Other, net	**0.5**	1.5	3.2
Total	**38.6%**	36.9%	41.4%

U.S. income taxes and foreign withholding taxes were not provided for on a cumulative total of approximately $411 million of undistributed earnings for certain non-U.S. subsidiaries. The Company intends to reinvest these earnings indefinitely in operations outside the United States. The components of the deferred tax assets (liabilities) follow (in millions):

	July 29, 2000	July 31, 1999
ASSETS		
Allowance for doubtful accounts and returns	**$ 418**	$ 185
In-process R&D	**265**	163
Inventory allowances and capitalization	**94**	57
Accrued state franchise tax	**–**	32
Depreciation	**41**	28
Deferred revenue	**177**	65
Credits and net operating loss carryforwards	**1,023**	–
Other	**451**	256
Gross deferred tax assets	**2,469**	786
Valuation allowance	**(299)**	–
Total deferred tax assets	**2,170**	786
LIABILITIES		
Purchased intangible assets	**(257)**	(88)
Unrealized gain on investments	**(1,954)**	(192)
Total deferred tax liabilities	**(2,211)**	(280)
Total	**$ (41)**	$ 506

The noncurrent portion of the deferred tax liabilities, which totaled $74 million at July 31, 1999, is included in other assets.

The Company has provided a valuation allowance on certain of its deferred tax assets because of uncertainty regarding their realizability due to expectation of future employee stock option exercises. Deferred tax assets of approximately $963 million at July 29, 2000 pertain to certain tax credits and net operating loss carryforwards resulting from the exercise of employee stock options. When recognized, the tax benefit of these credits and losses will be accounted for as a credit to shareholders' equity rather than as a reduction of the income tax provision.

As of July 29, 2000, the Company's federal and state net operating loss carryforwards for income tax purposes were approximately $496 million and $865 million, respectively. If not utilized, the federal net operating loss carryforwards will begin to expire in fiscal 2020, and the state net operating loss carryforwards will begin to expire in fiscal 2005. As of July 29, 2000, the Company's federal and state tax credit carryforwards for income tax purposes were approximately $678 million and $197 million, respectively. If not utilized, the federal and state tax credit carryforwards will begin to expire in fiscal 2005.

The Company's income taxes payable for federal, state, and foreign purposes have been reduced, and the deferred tax assets increased, by the tax benefits associated with dispositions of employee stock options. The Company receives an income tax benefit calculated as the difference between the fair market value of the stock issued at the time of exercise and the option price, tax effected. These benefits were credited directly to shareholders' equity and amounted to $3.08 billion, $837 million, and $422 million for fiscal 2000, 1999, and 1998, respectively. Benefits reducing taxes payable amounted to $2.49 billion, $837 million, and $422 million for fiscal 2000, 1999, and 1998, respectively. Benefits increasing gross deferred tax assets amounted to $582 million in fiscal 2000.

12. SEGMENT INFORMATION AND MAJOR CUSTOMERS

The Company's operations involve the design, development, manufacture, marketing, and technical support of networking products and services. The Company offers end-to-end networking solutions for its customers. Cisco products include routers, LAN and ATM switches, dial-up access servers, and network-management software. These products, integrated by the Cisco IOS® software, link geographically dispersed LANs, WANs, and IBM networks.

The Company conducts business globally and is managed geographically. The Company's management relies on an internal management system that provides sales and standard cost information by geographic theater. Sales are attributed to a theater based on the ordering location of the customer. The Company's management makes financial decisions and allocates resources based on the information it receives from this internal management system. The Company does not allocate research and development, sales and marketing, or general and administrative expenses to its geographic theaters as management does not use this information to measure the performance of the operating segments. Management does not believe that allocating these expenses is material in evaluating a geographic theater's performance. Information from this internal management system differs from the amounts reported under generally accepted accounting principles due to certain corporate level adjustments not included in the internal management system. These corporate level adjustments are primarily sales adjustments relating to revenue deferrals and reserves, credit memos, returns, and other timing differences. Based on established criteria, the Company has four reportable segments: the Americas; Europe, the Middle East, and Africa ("EMEA"); Asia Pacific; and Japan.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Summarized financial information by theater for fiscal 2000, 1999, and 1998, as taken from the internal management system discussed previously, is as follows (in millions):

Years Ended	July 29, 2000	July 31, 1999	July 25, 1998
Net sales:			
Americas	**$12,924**	$ 8,088	$5,732
EMEA	**4,770**	3,216	2,114
Asia Pacific	**1,705**	825	535
Japan	**935**	566	459
Sales adjustments	**(1,406)**	(522)	(351)
Total	**$18,928**	$12,173	$8,489
Gross margin:			
Americas	**$ 9,412**	$ 5,836	$4,261
EMEA	**3,581**	2,380	1,565
Asia Pacific	**1,215**	586	395
Japan	**737**	436	340
Standard margins	**14,945**	9,238	6,561
Sales adjustments	**(1,406)**	(522)	(351)
Production overhead	**(455)**	(255)	(207)
Manufacturing variances and other related costs	**(902)**	(547)	(438)
Total	**$12,182**	$ 7,914	$5,565

The standard margins by geographic theater differ from the amounts recognized under generally accepted accounting principles because the Company does not allocate certain sales adjustments, production overhead, and manufacturing variances and other related costs to the theaters. The above table reconciles the net sales and standard margins by geographic theater to net sales and gross margin as reported in the Consolidated Statements of Operations by including such adjustments.

Enterprise-wide information provided on geographic sales is based on the ordering location of the customer. Property and equipment information is based on the physical location of the assets. The following table presents net sales and property and equipment information for geographic areas (in millions):

	July 29, 2000	July 31, 1999	July 25,1998
Net sales:			
United States	**$ 12,013**	$ 7,454	$ 5,232
International	**8,321**	5,241	3,608
Sales adjustments	**(1,406)**	(522)	(351)
Total	**$ 18,928**	$12,173	$ 8,489
Property and equipment, net:			
United States	**$ 1,242**	$ 711	$ 537
International	**184**	114	72
Total	**$ 1,426**	$ 825	$ 609

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

Years Ended	July 29, 2000	July 31, 1999	July 25, 1998
Net sales:			
Routers	**$ 7,611**	$ 5,196	$3,856
Switches	**7,509**	5,167	3,613
Access	**2,396**	1,127	630
Other	**2,818**	1,205	741
Sales adjustments	**(1,406)**	(522)	(351)
Total	**$18,928**	$12,173	$8,489

Substantially all of the Company's assets at July 29, 2000 and July 31, 1999 were attributable to U.S. operations. In fiscal 2000, 1999, and 1998, no single customer accounted for 10% or more of the Company's net sales.

13. NET INCOME PER COMMON SHARE

The following table presents the calculation of basic and diluted net income per common share (in millions, except per-share amounts):

Years Ended	July 29, 2000	July 31, 1999	July 25, 1998
Net income	**$2,668**	$2,023	$1,331
Weighted-average shares—basic	**6,917**	6,646	6,312
Effect of dilutive securities:			
Employee stock options	**521**	416	346
Weighted-average shares—diluted	**7,438**	7,062	6,658
Net income per common share—basic	**$ 0.39**	$ 0.30	$ 0.21
Net income per common share—diluted	**$ 0.36**	$ 0.29	$ 0.20

14. SUBSEQUENT EVENTS (UNAUDITED)

Pending Business Combinations

The Company announced definitive agreements to acquire HyNEX, Ltd.; Netiverse, Inc.; Komodo Technology, Inc.; NuSpeed Internet Systems, Inc.; IPmobile, Inc.; and PixStream Incorporated for a total purchase price of approximately $1.76 billion, payable in common stock and cash. These acquisitions will be accounted for as purchases and are expected to close in the first quarter of fiscal 2001.

REPORT OF INDEPENDENT ACCOUNTANTS

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

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of operations and of shareholders' equity and of cash flows present fairly, in all material respects, the financial position of Cisco Systems, Inc. and its subsidiaries at July 29, 2000 and July 31, 1999, and the results of their operations and their cash flows for each of the three years in the period ended July 29, 2000, in conformity with accounting principles generally accepted in the United States. These financial statements are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States, which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for the opinion expressed above.

PricewaterhouseCoopers LLP

San Jose, California
August 8, 2000

SUPPLEMENTARY FINANCIAL DATA[1] (Unaudited)

(In millions, except per-share amounts)

	July 29, 2000	April 29, 2000	Jan. 29, 2000	Oct. 30, 1999	July 31, 1999	May 1, 1999	Jan. 23, 1999	Oct. 24, 1998
Net sales	**$5,720**	**$4,933**	**$4,357**	**$3,918**	$3,558	$3,172	$2,845	$2,598
Gross margin	**$3,662**	**$3,172**	**$2,818**	**$2,530**	$2,297	$2,059	$1,857	$1,701
Net income	**$ 796**[2]	**$ 641**[3]	**$ 816**[4]	**$ 415**[5]	$ 605[6]	$ 632[7]	$ 279[8]	$ 507[9]
Net income per common share—basic*	**$ 0.11**	**$ 0.09**	**$ 0.12**	**$ 0.06**	$ 0.09	$ 0.09	$ 0.04	$ 0.08
Net income per common share—diluted*	**$ 0.11**[2]	**$ 0.08**[3]	**$ 0.11**[4]	**$ 0.06**[5]	$ 0.08[6]	$ 0.09[7]	$ 0.04[8]	$ 0.07[9]

* Reflects the two-for-one stock split effective March 2000.

(1) All historical financial information has been restated to reflect the acquisitions that were accounted for as poolings of interests (see Note 3 to the Consolidated Financial Statements).

(2) Net income and net income per common share include in-process research and development expenses of $461 million, payroll tax on stock option exercises of $26 million, amortization of goodwill and purchased intangible assets of $169 million, acquisition-related costs of $37 million, and net gains realized on minority investments of $344 million. Pro forma net income and diluted net income per common share, excluding these items net of tax of $53 million, were $1.20 billion and $0.16, respectively.

(3) Net income and net income per common share include in-process research and development expenses of $488 million, payroll tax on stock option exercises of $25 million, amortization of goodwill and purchased intangible assets of $51 million, and net gains realized on minority investments of $156 million. Pro forma net income and diluted net income per common share, excluding these items net of tax benefits of $44 million, were $1.01 billion and $0.13, respectively.

(4) Net income and net income per common share include in-process research and development expenses of $43 million, amortization of goodwill and purchased intangible assets of $47 million, acquisition-related costs of $25 million, and net gains realized on minority investments of $31 million. Pro forma net income and diluted net income per common share, excluding these items net of tax benefits of $3 million, were $897 million and $0.12, respectively.

(5) Net income and net income per common share include in-process research and development expenses of $381 million and amortization of goodwill and purchased intangible assets of $24 million. Pro forma net income and diluted net income per common share, excluding these items net of tax benefits of $6 million, were $814 million and $0.11, respectively.

(6) Net income and net income per common share include in-process research and development expenses of $81 million, amortization of goodwill and purchased intangible assets of $19 million, and acquisition-related costs of $16 million. Pro forma net income and diluted net income per common share, excluding these items net of tax benefits of $11 million, were $710 million and $0.10, respectively.

(7) Net income and net income per common share include amortization of goodwill and purchased intangible assets of $19 million. Pro forma net income and diluted net income per common share, excluding this item net of a tax benefit of $6 million, were $645 million and $0.09, respectively.

(8) Net income and net income per common share include in-process research and development expenses of $349 million and amortization of goodwill and purchased intangible assets of $12 million. Pro forma net income and diluted net income per common share, excluding these items net of tax benefits of $34 million, were $606 million and $0.09, respectively.

(9) Net income and net income per common share include in-process research and development expenses of $41 million and amortization of goodwill and purchased intangible assets of $11 million. Pro forma net income and diluted net income per common share, excluding these items net of tax benefits of $3 million, were $556 million and $0.08, respectively.

STOCK MARKET INFORMATION

Cisco common stock (NASDAQ symbol CSCO) is traded on the NASDAQ National Market. The following table sets forth the range of high and low closing prices for each period indicated, adjusted to reflect the two-for-one split effective March 2000:

	2000		1999		1998	
	High	Low	High	Low	High	Low
First quarter	**$37.00**	**$29.38**	$17.32	$10.97	$ 9.37	$ 7.75
Second quarter	**$57.63**	**$35.00**	$26.67	$15.19	$10.05	$ 8.10
Third quarter	**$80.06**	**$54.75**	$29.69	$23.78	$12.31	$ 9.44
Fourth quarter	**$71.44**	**$50.55**	$33.53	$26.09	$17.20	$11.74

The Company has never paid cash dividends on its common stock and has no present plans to do so. There were approximately 60,150 shareholders of record at July 29, 2000.

SHAREHOLDER INFORMATION

DIRECTORS AND OFFICERS

Directors

Carol A. Bartz (2) (4) (5) (6) (8)
Chairman and Chief Executive Officer
Autodesk, Inc.

Larry R. Carter
Senior Vice President, Finance and Administration
Chief Financial Officer and Secretary
Cisco Systems, Inc.

John T. Chambers (1) (4) (5) (6) (8)
President and Chief Executive Officer
Cisco Systems, Inc.

Mary Cirillo (3) (7)
Chairman and Chief Executive Officer
OPCENTER, LLC

James F. Gibbons, Ph.D. (2) (4)
Reid Weaver Dennis Professor of Electrical Engineering and
Special Consul to the President for Industrial Relations
Stanford University

Edward R. Kozel (7) (8)
Managing Member
Open Range Ventures

James C. Morgan (2)
Chairman and Chief Executive Officer
Applied Materials, Inc.

John P. Morgridge (1) (5) (6) (7)
Chairman of the Board
Cisco Systems, Inc.

Arun Sarin (3) (5)
Chief Executive Officer
InfoSpace, Inc.

Donald T. Valentine (1) (5) (7)
General Partner
Sequoia Capital

Steven M. West (3)
President and Chief Executive Officer
Entera, Inc.

Jerry Yang
Cofounder and Chief Yahoo!
Yahoo!

(1) Member of the Executive Committee
(2) Member of the Compensation/Stock Option Committee
(3) Member of the Audit Committee
(4) Member of the Nomination Committee
(5) Member of the Acquisition Committee
(6) Member of the Special Stock Option Committee
(7) Member of the Investment/Finance Committee
(8) Member of the Special Acquisition Committee

Officers

Larry R. Carter
Senior Vice President, Finance and Administration
Chief Financial Officer and Secretary

John T. Chambers
President and Chief Executive Officer

Gary J. Daichendt
Executive Vice President
Worldwide Operations

Charles H. Giancarlo
Senior Vice President
Small/Medium Business Line of Business
Consumer Line of Business

Richard J. Justice
Senior Vice President
Worldwide Field Operations

Carl Redfield
Senior Vice President, Manufacturing and
Worldwide Logistics

James Richardson
Senior Vice President, Enterprise Line of Business and
Internet Communications Software Group

Michelangelo Volpi
Senior Vice President, Chief Strategy Officer

OTHER SENIOR VICE PRESIDENTS

Douglas C. Allred
Senior Vice President, Customer Advocacy

Vernon E. Altman
Senior Vice President, Strategic Business Partnerships

Barbara Beck
Senior Vice President, Human Resources

Susan L. Bostrom
Senior Vice President, Internet Business Solutions Group

Howard S. Charney
Senior Vice President, Office of the President

William G. Conlon
Senior Vice President
Customer Advocacy Global Support Operations

Doug Dennerline
Senior Vice President
U.S. Enterprise and Federal Sales

Kevin A. DeNuccio
Senior Vice President
Worldwide Service Provider Field Operations

Richard Freemantle
Senior Vice President, Asia Pacific

Kevin J. Kennedy
Senior Vice President
Service Provider Line of Business and
Cisco IOS® Technologies Division

David Kirk
Senior Vice President
Internet Communications Software Group

Mario Mazzola
Senior Vice President, New Business Ventures

William R. Nuti
Senior Vice President, EMEA Operations

Randy Pond
Senior Vice President, Operations

Daniel Scheinman
Senior Vice President, Corporate Affairs

Cas Skrzypczak
Senior Vice President
Customer Advocacy for Service Provider and
Consumer Lines of Business

Peter Solvik
Senior Vice President, Chief Information Officer

SHAREHOLDER INFORMATION

Online Annual Report

We invite you to visit our online interactive report at **www.cisco.com/annualreport/2000.** In this version you will find our shareholders' letter in multiple languages, a financial section, and additional company and product information. This Web-based report complements our printed report, giving you a comprehensive understanding of Cisco Systems.

iQ™

Cisco recently introduced the iQ Web site and *iQ* magazine with additional information to help business executives implement effective Internet business solutions. *iQ* magazine is the senior executive's atlas to the Internet economy. Using the successful models of Cisco and its customers, the site and magazine detail how businesses can harness the power of the Internet to gain a competitive advantage and increase profitability. Visit the site at **www.cisco.com/go/iqmagazine.**

Investor Relations

For further information on the Company, additional copies of this report, Form 10-K, or other financial information, contact:

Investor Relations
Cisco Systems, Inc.
170 West Tasman Drive
San Jose, CA 95134-1706
(408) 227-CSCO (2726)

You may also contact us by sending an e-mail to investor-relations@cisco.com or by visiting the Investor Relations section on the Company's Web site at www.cisco.com.

Transfer Agent and Registrar

Fleet National Bank
(f/k/a BankBoston, N.A.)
c/o EquiServe Limited Partnership
P.O. Box 8040
Boston, MA 02266-8040
www.equiserve.com
(800) 730-6001

Independent Accountants

PricewaterhouseCoopers LLP
San Jose, CA

Legal Counsel

Brobeck, Phleger & Harrison LLP
Palo Alto, CA

Notice of Annual Meeting

Paramount's Great America
Paramount Theater
1 Great America Parkway
Santa Clara, CA
November 14, 2000
10 a.m. Pacific Standard Time

WORLDWIDE OFFICES

CORPORATE HEADQUARTERS
San Jose, California, USA

EUROPEAN HEADQUARTERS
Issy les Moulineaux, France

AMERICAS HEADQUARTERS
San Jose, California, USA

ASIA PACIFIC HEADQUARTERS
North Sydney, Australia

Cisco Systems has offices in the following countries. Addresses, phone numbers, and fax numbers are listed at **www.cisco.com/go/offices.**

ARGENTINA • AUSTRALIA • AUSTRIA • BELGIUM • BRAZIL • BULGARIA • CANADA • CHILE • CHINA • COLOMBIA • COSTA RICA
CROATIA • CZECH REPUBLIC • DENMARK • DUBAI, UAE • FINLAND • FRANCE • GERMANY • GREECE • HONG KONG • HUNGARY
INDIA • INDONESIA • IRELAND • ISRAEL • ITALY • JAPAN • KOREA • LUXEMBOURG • MALAYSIA • MEXICO • THE NETHERLANDS
NEW ZEALAND • NORWAY • PERU • PHILIPPINES • POLAND • PORTUGAL • PUERTO RICO • ROMANIA • RUSSIA • SAUDI ARABIA
SCOTLAND • SINGAPORE • SLOVAKIA • SLOVENIA • SOUTH AFRICA • SPAIN • SWEDEN • SWITZERLAND • TAIWAN • THAILAND
TURKEY • UKRAINE • UNITED KINGDOM • UNITED STATES • VENEZUELA • VIETNAM • ZIMBABWE

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

Tel: (408) 526-4000
(800) 553-NETS (6387)
www.cisco.com

Printed on recycled paper.

Lit# 954965
SKU# 1028-AR-00