

TELECOM NEWS

Cisco: Bad luck or bad attitude?

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May 11, 2001 2:48 PM ET

It's a simple problem: A great company miscalculated demand in a baffling economy. That's essentially all Cisco Systems Inc.'s \$2.69 billion loss for its fiscal third quarter is about. Or is it?

Executives of the San Jose, Calif., networking equipment giant this week described the company's loss--its first since going public 11 years ago--as an "anomaly" and a simple matter of over-ordering parts and subassemblies in advance of demand that never materialized.

But a closer look at the shocking plight of the once peerless company exposes a company with questionable fundamental business practices. In fact, some customers and analysts contacted this week said Cisco's problems can be traced directly to an arrogant and even lazy sales force, which is too used to taking orders rather than aggressively selling and serving customers. Others flat out question the innovation-by-acquisition strategy that has been the hallmark of President and CEO John Chambers' regime.

If Cisco cannot answer these questions effectively--and the company's performance over the next six months will tell much--then it may never match the heights it attained in recent years, when, for a time, it had the largest market capitalization of any business in the world.

"I came right out and said, 'I think you guys are lazy, you're waiting for people to be coming to you,'" said Ginger Smith, a voice analyst in the Midwest who asked that her company not be named. Smith was interested in VOIP (voice-over-IP) products, but when she called her Cisco representative about 10 months ago, she said she was told by her rep to come into the Cisco office and speak about it. Then she was told, to her surprise, that Cisco offered the kinds of products she was looking for. She rejected the offer to come in, saying it was Cisco's responsibility to come to her.

A week later, Smith received a Cisco textbook on VOIP in the mail with a note from her rep saying, "This might help you."

"At first I thought, 'That was nice,'" Smith said. "Then I was a little bit offended because rather than coming out and explaining it to me--I mean it was a textbook." Smith never worked with Cisco on the project and remains leery of the company's ability in VOIP.

Tom Miller, senior director of corporate information systems at Affymetrix Inc., in Santa Clara, Calif., and an eWEEK Corporate Partner, looked at Cisco for switches but went with Foundry Networks Inc. "We thought that Foundry was a lot more innovative and able to turn around products faster." Foundry's BigIron 8000 and 4000 network switches, Miller said, offered better price/performance than comparable Cisco products.

From Miller's perspective, Cisco has reached the same point IBM reached more than a decade ago. "Cisco is a safe bet. It's conservative, it's expensive," he said. "But what real value are they bringing to the industry these days?" Further, Miller finds the company's dabbling in diverse technologies like optical networking confusing: "Where is John (Chambers) taking Cisco?"

"They got fat and happy and got into just taking orders," said Aaron Goldberg, industry analyst and vice president of Ziff Davis Media Inc., which publishes eWEEK. "Turning this around is going to be hard, and if they trip, this is where it will happen."

Climbing from the wreckage

Whether Cisco officials recognize the problem is another question. In addressing the company's problems in an analysts conference call this week, however, Chambers laid the blame at the doorstep of the economy. He said the company's long-term growth estimates for countries with good economies remain unchanged at between 30 percent and 50 percent.

"The speed with which this New Economy moves, and the associated peaks and valleys, will be much higher and lower than anyone anticipated," Chambers said. "One of the lessons learned is that we must prepare for the speed and depth of these changes."

Cisco Chief Financial Officer Larry Carter summed up the company's performance: "This is an unusual quarter. ... This is an anomaly. ... This is very unusual."

For the third quarter of its fiscal 2001, Cisco posted net sales of \$4.73 billion and a net loss of \$2.69 billion. For the year-ago period, Cisco posted sales of \$4.93 billion and a net profit of \$641 million.

The losses, which have been anticipated since Cisco issued a warning a month ago, came to a \$2.2 billion excess inventory charge and a \$1.17 restructuring charge. In March, the company said it would lay off 17 percent of its work force, or 8,000 employees, a number that was later upped to 8,500. The quarterly loss is the company's first in the 11 years since it has been publicly traded.

In the current crisis, Cisco has no plans to resume the feverish pace of acquisitions, said Cisco Vice President of Marketing for Enterprise Systems James Richardson in a press interview following his speech at NetWorld+Interop in Las Vegas this week. However, Richardson noted that Cisco continues to have sufficient market capitalization -- even with its current depressed stock price -- to acquire companies, should it choose to.

Out of shape?

Laurie Vickers, senior analyst at the Cahners, In-stat Group, in Scottsdale, Ariz., said that innovation by acquisition ought to be used to fill occasional holes, not as an outright substitute for classical research and development, which had become the case at Cisco.

"I think they're out of shape," Vickers said. "Organically developed technology in a cutting-edge market -- I haven't been seeing it."

The cause, Vickers said is simple: "Acquisitions create a lot of debris and inertia to clean up. That takes a lot of energy." As a result, she said, "Cisco is no longer on the very cutting edge of most of their major segments."

Cisco officials candidly admit as much. "Juniper (Networks) has leapfrogged us," Richardson said. He asserted, however, that Cisco is hard at work, spending its more than \$4 billion R&D war chest on work that will in turn allow Cisco to leapfrog Juniper, a maker of backbone routers that are popular among Internet service providers.

Vickers warned, however, that unless the trend is reversed, Cisco could be further behind in six to nine months.

But with all Cisco's problems, few observers are going so far as to write off the company.

"They are going to carry a lot of the Internet traffic in the future," Goldberg said. "But they're not going to grow at 30 percent any more."