F5 NETWORKS INC

FORM 10-Q
(Quarterly Report)

Filed 5/10/2000 For Period Ending 3/31/2000

Address	401 ELLIOT AVE WEST STE 500
	SEATTLE, Washington 98119
Telephone	206-272-5555
CIK	0001048695
Industry	Computer Networks
Sector	Technology
Fiscal Year	09/30

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended March 31, 2000

OR

[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from to

Commission File Number 000-26041

F5 NETWORKS, INC.
(Exact name of registrant as specified in its charter)

WASHINGTON	91-1714307
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No.)

200 FIRST AVENUE WEST, SUITE 500
SEATTLE, WASHINGTON 98119
(Address of principal executive offices and zip code)

(206) 505-0800
(Registrant's telephone number, including area code)

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

Indicate the number of shares outstanding of each of the registrant's classes of common stock as of the latest practicable date: 21,306,824 shares of common stock, no par value, as of May 1, 2000.

F5 NETWORKS, INC.

FORM 10-Q

FOR THE QUARTER ENDED MARCH 31, 2000

TABLE OF CONTENTS

PART I
FINANCIAL INFORMATION

ITEM 1. Financial Statements

F5 NETWORKS, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(in thousands, except share data)

	MARCH 31, 2000 (unaudited)	SEPTEMBER 30, 1999
ASSETS		
Current assets:		
Cash and cash equivalents	$ 61,225	$ 24,797
Restricted cash	3,079	3,013
Accounts receivable, net of allowances of $900 and $826	21,147	10,353
Inventories	1,566	618
Other current assets	1,804	981
Total current assets	88,821	39,762
Property and equipment, net	5,273	2,834
Other assets	295	250
Total assets	$ 94,389	$ 42,846
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 4,792	$ 2,700
Accrued liabilities	4,255	3,808
Deferred revenue	9,903	4,365
Total current liabilities	18,950	10,873
Commitments and Contingencies:		
Shareholders' equity:		
Common stock, no par value; 100,000,000 shares authorized, 21,271,000 and 18,161,000 shares issued and outstanding	79,557	45,760
Note receivable from shareholder	(563)	(750)
Accumulated other comprehensive income (loss)	77	(3)
Unearned compensation	(2,219)	(3,232)
Accumulated deficit	(1,413)	(9,802)
Total shareholders' equity	75,439	31,973
Total liabilities and shareholders' equity	$ 94,389	$ 42,846

The accompanying notes are an integral part of these consolidated financial statements.

F5 NETWORKS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(unaudited, in thousands, except per share amounts)

	THREE MONTHS ENDED MARCH 31,		SIX MONTHS ENDED MARCH 31,	
	2000	1999	2000	1999
Net revenues:				
Products	$18,532	$ 3,146	$34,814	$ 5,428
Services	5,072	616	7,963	1,029
Total net revenues	23,604	3,762	42,777	6,457
Cost of net revenues:				
Products	5,053	825	9,677	1,449
Services	1,792	384	2,851	580
Total cost of net revenues	6,845	1,209	12,528	2,029
Gross profit	16,759	2,553	30,249	4,428
Operating expenses:				
Sales and marketing	8,452	2,887	14,194	5,103
Research and development	2,761	1,324	4,986	2,345
General and administrative	1,748	666	3,226	1,191
Amortization of unearned compensation	470	670	1,013	1,038
Total operating expenses	13,431	5,547	23,419	9,677
Income (loss) from operations	3,328	(2,994)	6,830	(5,249)
Interest income, net	818	31	1,559	89
Net income (loss)	$ 4,146	$(2,963)	$ 8,389	$(5,160)
Net income (loss) per share - basic	$ 0.20	$ (0.45)	$ 0.40	$ (0.82)
Weighted average shares - basic	21,198	6,555	20,811	6,297
Net income (loss) per share - diluted	$ 0.18	$ (0.45)	$ 0.36	$ (0.82)
Weighted average shares - diluted	23,105	6,555	23,092	6,297

The accompanying notes are an integral part of these consolidated financial statements.

F5 NETWORKS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(unaudited, in thousands)

	SIX MONTHS ENDED MARCH 31,	
	2000	1999
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income (loss)	$ 8,389	$ (5,160)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Unrealized gain on marketable securities	87	--
Amortization of unearned compensation	1,013	1,038
Provision for doubtful accounts and sales returns	702	667
Depreciation and amortization	870	235
Changes in operating assets and liabilities:		
Accounts receivable	(11,506)	(2,014)
Inventories	(950)	(299)
Other assets	(889)	(303)
Accounts payable and accrued liabilities	2,546	1,510
Deferred revenue	5,543	780
Net cash provided by (used in) operating activities	5,805	(3,546)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Investment in restricted cash	(66)	--
Purchases of property and equipment	(3,288)	(720)
Net cash used in investing activities	(3,354)	(720)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from payments on shareholder loan	187	--
Proceeds from the secondary offering, net of issuance costs	31,475	--
Proceeds from option and warrant exercises	2,322	520
Net cash provided by financing activities	33,984	520
Net increase (decrease) in cash and cash equivalents	36,435	(3,746)
Effect of exchange rate changes on cash and cash equivalents	(7)	--
Cash and cash equivalents, at beginning of period	24,797	6,206
Cash and cash equivalents, at end of period	$ 61,225	$ 2,460

The accompanying notes are an integral part of these consolidated financial statements.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(unaudited)

1. THE COMPANY AND BASIS OF PRESENTATION

F5 Networks, Inc. ("F5" or the "Company") was incorporated on February 26, 1996 in the State of Washington.

F5 is a leading provider of integrated Internet traffic and content management solutions designed to improve the availability and performance of mission-critical Internet-based servers and applications. F5's proprietary software-based solutions monitor and manage local and geographically dispersed servers and intelligently direct traffic to the server best able to handle a user's request.

The accompanying unaudited condensed consolidated financial statements have been prepared by F5 in accordance with the rules and regulations of the Securities and Exchange Commission for interim financial statements. Accordingly, certain information and footnote disclosures, normally included in financial statements prepared in accordance with generally accepted accounting principles, have been condensed or omitted pursuant to such rules and regulations. In the opinion of management of the Company, the unaudited financial statements reflect all adjustments, consisting only of normal recurring adjustments, necessary for a fair presentation of the Company's financial position at March 31, 2000, its operating results for the three and six months ended March 31, 2000 and 1999 and cash flows for the six months ended March 31, 2000 and 1999. The condensed consolidated balance sheet at September 30, 1999 has been derived from the Company's audited consolidated financial statements as of that date. These financial statements and the notes should be read in conjunction with the Company's audited consolidated financial statements and notes thereto contained in the Company's annual report on Form 10-K filed with the Securities and Exchange Commission on December 28, 1999.

The results of operations for the three and six months ended March 31, 2000 are not necessarily indicative of the results that may be expected for future quarters or the year ending September 30, 2000.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

PRINCIPLES OF CONSOLIDATION

The financial statements consolidate the accounts of F5 Networks, Inc. and its wholly owned subsidiary F5 Networks, Ltd. All intercompany transactions have been eliminated.

SEGMENT INFORMATION

The Company has adopted Statement of Financial Accounting Standards No. 131, "Disclosures about Segments of an Enterprise and Related Information" ("SFAS No. 131"). SFAS No. 131 supersedes Statement of Financial Accounting Standards No. 14, "Financial Reporting for Segments of a Business Enterprise," replacing the "industry segment" approach with the "management" approach. The management approach designates the internal organization that is used by management for making operating decisions and assessing performance as the source of the Company's reportable segments. SFAS No. 131 also requires disclosures about products and services, geographic areas, and major customers. In the opinion of management, the Company operates in one segment providing integrated Internet traffic and content management solutions.

USE OF ESTIMATES

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities as of the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could materially differ from these estimates.

CASH EQUIVALENTS AND SHORT-TERM INVESTMENTS

Cash equivalents are highly liquid investments, consisting of investments in money market funds and marketable securities which are readily convertible to cash without penalty and subject to insignificant risk of changes in value. The Company's cash and cash equivalents balance consists of the following:

	MARCH 31, 2000	SEPTEMBER 30, 1999
	(IN THOUSANDS)	
Cash	$ 25,140	$ 15,671
Marketable securities ...	36,085	9,126
	$ 61,225	$ 24,797

CONCENTRATION OF CREDIT RISK

The Company places its temporary cash investments with major financial institutions. As of March 31, 2000, all of the Company's temporary cash investments were placed with four institutions.

The Company's customers are from diverse industries and geographic locations. Net revenues from international customers are denominated in U.S. Dollars and were approximately $6.6 million for the six months ended March 31, 2000 and $4.4 million for the three months ended March 31, 2000. One customer accounted for 19.6% of net revenues for the six months ended March 31, 2000 and 15.8% of net revenues for the three months ended March 31, 2000. This customer also accounted for 10.6% and 15.4% of the Company's accounts receivable balance at March 31, 2000 and 1999, respectively.

INVENTORIES

Inventories consist of hardware, software and related component parts and are recorded at the lower of cost or market (as determined by the first-in, first-out method).

Inventories are comprised of the following:

	MARCH 31, 2000	SEPTEMBER 30, 1999
	(IN THOUSANDS)	
Finished goods	$ 1,000	$ 420
Raw materials	566	198
	$ 1,566	$ 618

COMPREHENSIVE INCOME (LOSS)

The Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 130, "Reporting Comprehensive Income," in June 1997. This statement established new standards for reporting and displaying comprehensive income in the financial statements and was adopted by the Company during the quarter ended September 30, 1999. In addition to net income, comprehensive income includes charges or credits to equity that are not the result of transactions with shareholders.

The following table sets forth a reconciliation of net income (loss) to comprehensive income (loss), net of tax:

	THREE MONTHS ENDED MARCH 31,		SIX MONTHS ENDED MARCH 31,	
	2000	1999	2000	1999
Net income (loss)	$ 4,146	$(2,963)	$ 8,389	$(5,160)
Unrealized gain on investments	31	--	87	--
Foreign currency translation adjustment	(6)	--	(7)	--
Comprehensive income (loss)	$ 4,171	$(2,963)	$ 8,469	$(5,160)

REVENUE RECOGNITION

The Company recognizes software revenue under Statement of Position 97-2, "Software Revenue Recognition," and SOP 98-9 "Modification of SOP 97-2, Software Revenue Recognition, with Respect to Certain Transactions."

The Company sells products through resellers, original equipment manufacturers and other channel partners, as well as to end users, under similar terms. The Company generally combines software license, hardware, installation and customer support elements into a package with a single "bundled" price. The Company allocates a portion of the sales price to each element of the bundled package based on their respective fair values when the individual elements are sold separately. Revenues from the license of software, net of an allowance for estimated returns, are recognized when the product has been shipped and the customer is obligated to pay for the product. Installation revenue is recognized when the product has been installed at the customer's site. Revenues for customer support are recognized on a straight-line basis over the service contract term. Estimated sales returns are based on historical experience by product and are recorded at the time revenues are recognized. Additionally, the Company offers extended payment terms. For these arrangements, revenue is recognized ratably over the terms of the arrangement.

NET INCOME (LOSS) PER SHARE

In accordance with SFAS No. 128, basic net income (loss) per share has been computed using the weighted-average number of shares of common stock outstanding during the period, except that pursuant to Securities and Exchange Commission Staff Accounting Bulletin No. 98, if applicable, common shares issued in each of the periods presented for nominal consideration have been included in the calculation as if they were outstanding for all periods presented.

Basic net income (loss) per share is computed by dividing net income (loss) by the weighted average number of common shares outstanding during the period. Diluted net income (loss) per share is computed by dividing net income (loss) by the weighted average number of common and dilutive common stock equivalent shares outstanding during the period.

The following table sets forth the computation of basic and diluted net income (loss) per share for the three and six months ended March 31:

	THREE MONTHS ENDED MARCH 31, 2000	THREE MONTHS ENDED MARCH 31, 1999	SIX MONTHS ENDED MARCH 31, 2000	SIX MONTHS ENDED MARCH 31, 1999
	(unaudited, in thousands except for per share data)			
Numerator:				
Net income (loss)	$ 4,146	$ (2,963)	$ 8,389	$ (5,160)
Denominator:				
Weighted average shares outstanding - basic	21,198	6,555	20,811	6,297
Dilutive effect of common shares from stock options	1,896	--	2,034	--
Dilutive effect of common shares from warrants	11	--	247	--
Weighted average shares outstanding - diluted	23,105	6,555	23,092	6,297
Basic net income (loss) per share	$ 0.20	$ (0.45)	$ 0.40	$ (0.82)
Diluted net income (loss) per share	$ 0.18	$ (0.45)	$ 0.36	$ (0.82)

NEW ACCOUNTING PRONOUNCEMENTS

In December 1999, SEC Staff Accounting Bulletin No. 101 ("SAB 101"), "Revenue Recognition in Financial Statements," was issued. This pronouncement summarizes certain of the SEC staff's views in applying generally accepted accounting principles to revenue recognition. SAB 101 is required to be adopted by the Company beginning October 1, 2000. The Company is currently reviewing the requirements of SAB 101 and assessing its potential impact on the Company's financial statements.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Statements in this report concerning future events or future performance, financial results or achievements of F5, or other statements which are not statements of historical facts are forward-looking statements. These statements may be identified by terminology such as "may," "will," "should," "expects," "plans," "anticipates," "believes," "estimates," "predicts", "potential" or "continue" or the negative of such terms or comparable terms. These statements are subject to a number of known and unknown risks, uncertainties and other factors which may cause our actual results, performance or achievements to differ from those expressed or implied by those statements. Relevant risks and uncertainties include among others: our limited operating history; variability of our operating results; market acceptance of our Internet traffic and content management products; our timely development of new products and features; our ability to manage its growth; our ability to maintain and develop distribution relationships; competition in the Internet traffic and content management market; our ability to expand in the international markets; unpredictability of our sales cycle and other risk factors referenced in our public filings with the Securities and Exchange Commission, and in particular, those set forth under the heading "Risk Factors" in our Annual Report on Form 10-K filed with the SEC on December 28, 1999. These forward-looking statements speak only as of the date of this report. We expressly disclaim any obligation or undertaking to release publicly any updates or revisions to any forward-looking statements contained in this report to reflect any change in our expectations with regard to such statements or any change in events, conditions or circumstances on which any statement is based.

The following information should be read in conjunction with the "Management's Discussion and Analysis of Financial Condition and Results of Operations" on pages 15 through 27 of our annual report on Form 10-K.

OVERVIEW

F5 is a leading provider of integrated Internet traffic and content management solutions designed to improve the availability and performance of mission-critical Internet-based servers and applications. Our products monitor and manage an organization's geographically dispersed servers and intelligently direct traffic to the server best able to handle a user's request, preventing system failure and providing timely responses and optimal data flow.

We were incorporated on February 26, 1996 and began operations in April 1996. During the period from February 26, 1996 through September 30, 1996, we were a development stage enterprise and had no product revenues. Our operating activities during this period related primarily to developing our initial product, recruiting personnel, building our corporate infrastructure and raising capital.

In July 1997, we released our first version of our BIG/ip(R) Controller and began to expand our operations. We continue to commit a significant amount of resources to research and development, marketing programs, domestic and international sales channels, customer support and services and our general and administrative infrastructure. As of March 31, 2000, we have:

- hired more than 300 employees;

- hired sales, professional services and customer support personnel in U.S., Canada, Europe and Asia Pacific;

- released several upgrades to our suite of products;

- released three new products: our 3DNS(TM) Controller, our see/IT(TM) Network Manager and our global/SITE(TM) Controller;

- engaged sales representatives in the European and Asia Pacific markets; and

- established twenty-two international reseller relationships.

Our net revenues grew from $3.8 million for the three months ended March 31, 1999 to $23.6 million for the three months ended March 31, 2000. Currently, we derive approximately 62% of our net revenues from sales of BIG/ip. We expect to continue to derive a significant portion of our net revenues from sales of BIG/ip in the future. One of our resellers, accounted for 15.8% of our net revenues for the three months ended March 31, 2000 and 10.6% of our accounts receivable balance at March 31, 2000.

Net revenues derived from customers located outside of the United States were $266,000 and $4.4 million for the three months ended March 31, 1999 and 2000, respectively. Net revenues derived from customers located outside of the United States were $327,000 and $6.6 million for the six months ended March 31, 1999 and 2000, respectively. We plan to continue expanding our international operations significantly, particularly in selected countries in the European and Asia Pacific markets, because we believe international markets represent a significant growth opportunity. The expansion of our international operations will be subject to a variety of risks that could significantly harm our business and results of operations.

Customers who purchase our products receive installation services and an initial customer support contract, typically covering a 12-month period. We generally combine the software license, hardware, installation, and customer support elements of our products into a package for a single price. We allocate a portion of the sales price to each element of the bundled package based on their respective fair values when the individual elements are sold separately. Revenues from the license of software are recognized, net of allowances for estimated returns, when the product has been shipped and the customer is obligated to pay for the product. Installation revenue is recognized when the product has been installed at the customer's site. Revenues for customer support are recognized on a straight-line basis over the service contract term. Our ordinary payment terms to our customers are net 30 days, but we have extended payment terms beyond net 30 days to some customers. For extended payment term arrangements, revenue is deferred, and recognized ratably over the term of the arrangement. Estimated sales returns are based on historical experience by product and are recorded at the time revenues are recognized. Consulting services are customarily billed at fixed rates, plus out-of-pocket expenses. Customers may also purchase consulting services and renew their initial customer support contract. Based on our limited operating history, it is difficult to predict what our rate of renewals will be in the future.

As of March 31, 2000, we had an accumulated deficit of $1.4 million. Our success in growing net revenues depends on increasing our customer base and expanding our product line as well as continued growth of the emerging Internet traffic and content management market. Accordingly, we intend to continue to invest heavily in sales and marketing, promotion of the F5 brand, customer service and support, research and development, operating infrastructure and general and administrative staff to support our growth. As a result of these investments, we expect that our operating expenses will continue to increase significantly. Despite growing revenues, we have only begun to generate profits during our three most recent quarters ended September 30, 1999, December 31, 1999 and March 31, 2000.

We have recorded a total of $6.2 million of unearned compensation costs since our inception through March 31, 2000. These charges represent the difference between the exercise price and the estimated fair value of certain stock options granted to our employees and outside directors. These options generally vest ratably over a four-year period. We are amortizing these costs over the vesting period of the options and have recorded unearned compensation charges of $670,000 and $470,000 for the three months ended March 31, 1999 and 2000, respectively.

We expect to recognize amortization expense related to unearned compensation of approximately $1.8 million, $965,000, $411,000 and $60,000 during the years ended September 30, 2000, 2001, 2002 and 2003, respectively. We cannot guarantee, however, that we will not accrue additional unearned compensation costs in the future.

In view of the rapidly changing nature of our business and our limited operating history, we believe that period-to-period comparisons of net revenues and operating results are not necessarily meaningful and should not be relied upon as indications of future performance. To maintain profitability we will need to increase our net revenues significantly. Although we have experienced rapid growth in net revenues in recent periods, we may not be able to sustain these growth rates to maintain profitability.

RESULTS OF OPERATIONS

The following table sets forth financial data as a percentage of total net revenues for the periods indicated.

	THREE MONTHS ENDED MARCH 31,		SIX MONTHS ENDED MARCH 31,	
	2000	1999	2000	1999
STATEMENT OF OPERATIONS DATA:				
Net revenues:				
Products	78.5%	83.6%	81.4%	84.1%
Services	21.5	16.4	18.6	15.9
Total net revenues	100.0	100.0	100.0	100.0
Cost of net revenues:				
Products	21.4	22.0	22.6	22.4
Services	7.6	10.2	6.7	9.0
Total cost of net revenues	29.0	32.2	29.3	31.4
Gross margin	71.0	67.8	70.7	68.6
Operating expenses:				
Sales and marketing	35.8	76.7	33.2	79.0
Research and development	11.7	35.2	11.7	36.3
General and administrative	7.4	17.7	7.5	18.5
Amortization of unearned compensation	2.0	17.8	2.3	16.1
Total operating expenses	56.9	147.4	54.7	149.9
Income (loss) from operations	14.1	(79.6)	16.0	(81.3)
Interest income, net	3.5	.8	3.6	1.4
Net income (loss)	17.6%	(78.8)%	19.6%	(79.9)%

NET REVENUES:

Net revenues consist of sales of our products and services, which primarily include software licenses and services. Product revenues include revenue from software licenses and hardware sales. Service revenues include revenue from service and support agreements provided as part of the initial product sale, sales of extended service and support contracts and consulting services.

Product revenues. Product revenues increased by 489.1% from $3.1 million for the three months ended March 31, 1999 to $18.5 million for the three months ended March 31, 2000. Product revenues increased 541.4% from $5.4 million for the six months ended March 31, 1999 to $34.8 million for the six months ended March 31, 2000. These increases in product revenues were due primarily to an increase in the quantity of our products sold. These increases also reflect the continued addition of new customers, as well as repeat sales to existing customers.

Service revenues. Service revenues increased by 723.4% from $616,000 for the three months ended March 31, 1999 to $5.1 million for the three months ended March 31, 2000. Service revenues increased 673.9% from $1.0 million for the six months ended March 31, 1999 to $8.0 million for the six months ended March 31, 2000. The increases in service revenues were due primarily to an increase in the installed base of our products and the renewal of service and support contracts during the six months ended March 31, 2000.

As our net revenue base increases, we do not believe we can sustain the percentage growth rates of net revenues that we have experienced historically.

COST OF NET REVENUES:

Cost of net revenues consists primarily of outsourced hardware components and manufacturing, fees for third-party software products integrated into our products, manufacturing and service and support personnel and an allocation of our facilities and depreciation expenses.

Cost of product revenues. Cost of product revenues increased by 512.5%, from $825,000 for the three months ended March 31, 1999 to $5.0 million for the three months ended March 31, 2000 and increased as a percentage of product revenues from 26.7% to 27.8%. Cost of product revenues increased by 567.8% from $1.5 million for the six months ended March 31, 1999 to $9.7 million for the six months ended March 31, 2000 and increased as a percentage of product revenues from 26.7% to 27.8%. The increases in product cost were due primarily to increased product revenues.

Cost of service revenues. Cost of service revenues increased by 366.7%, from $384,000 for the three months ended March 31, 1999 to $1.8 million for the three months ended March 31, 2000 and decreased as a percentage of service revenues to 35.3% from 62.3% for the same periods. Cost of service revenues increased by 391.6% from $580,000 for the six months ended March 31, 1999 to $2.9 million for the six months ended March 31, 2000 and decreased as a percentage of service revenues to 35.8% from 56.4%. The increases in cost of service revenues in absolute dollars were due primarily to increased personnel costs, including training and consulting expenses related to hiring, as well as additional salaries. The decreases in cost of service revenues as a percentage of service revenues were primarily due to increased economies of scale achieved from increased service revenues.

Sales and marketing. Our sales and marketing expenses consist primarily of salaries, commissions and related benefits to our sales and marketing staff, costs of our marketing programs, including public relations, advertising and trade shows and an allocation of our facilities and depreciation expenses. Sales and marketing expenses increased by 192.8%, from $2.9 million for the three months ended March 31, 1999 to $8.4 million for the three months ended March 31, 2000. Sales and marketing expenses increased by 178.2% from $5.1 million for the six months ended March 31, 1999 to $14.2 million for the six months ended March 31, 2000. These increases were due to an increase in sales and marketing and professional services personnel from 54 to 170, increased commissions, and increased advertising and promotional activities. We expect to continue increasing sales and marketing expenses in order to grow net revenues and expand our brand awareness.

Research and development. Our research and development expenses consist primarily of salaries and related benefits for our product development personnel and an allocation of our facilities and depreciation expenses. Research and development expenses increased by 108.5%, from $1.3 million for the three months ended March 31, 1999 to $2.8 million for the three months ended March 31, 2000. Research and development expenses increased by 112.6% from $2.3 million for the six months ended March 31, 1999 to $5.0 million for the six months ended March 31, 2000. These increases were due primarily to an increase in product development personnel from 46 to 89. Our future success is dependent in large part on the continued enhancement of our current products and our ability to develop new, technologically advanced products that meet the sophisticated needs of our customers. We expect research and development expenses to increase in absolute dollars in future periods.

General and administrative. Our general and administrative expenses consist primarily of salaries, benefits and related costs of our executive, finance, information technology, human resource and legal personnel, third-party professional service fees, and an allocation of our facilities and depreciation expenses. General and administrative expenses increased by 162.5% from $666,000 for the three months ended March 31, 1999 to $1.8 million for the three months ended March 31, 2000. General and administrative expenses increased by 170.9% from $1.2 million for the six months ended March 31, 1999 to $3.2 million for the six months ended March 31, 2000. These increases were due primarily to an increase in general and administrative personnel from 24 to 48. We expect general and administrative expenses to increase in absolute dollars as we expand our staff and further develop our internal information systems and incur costs associated with being a public company.

Unearned compensation. We recorded amortization expense of unearned compensation of $670,000 and $470,000 for the three months ended March 31, 1999 and 2000, respectively. For the six months ended March 31, 1999 and 2000, we recorded unearned compensation charges of $1.0 million for each period, respectively.

Interest income, net. Interest income consists of earnings on our cash and cash equivalent balances offset by interest expense associated with debt obligations. Interest income, net was $31,000 for the three months ended March 31, 1999 and $818,000 for the three months ended March 31, 2000. For the six months ended March 31, 1999 and 2000, interest income, net was $89,000 and $1.6 million, respectively. These increases were due primarily to the investment of the proceeds received from our initial and secondary public offerings in June and October 1999.

Income taxes. As of September 30, 1999, we had approximately $7.8 million of net operating loss carryforwards for federal income tax purposes. Accordingly, there was no provision for federal or state income taxes for any prior period. Utilization of the net operating loss carryforwards may be subject to annual limitations due to the ownership change limitations contained in the Internal Revenue Code of 1986 and similar state provisions. Annual limitations may result in the expiration of the net operating losses before we can utilize them. The federal net operating loss carryforwards will expire at various dates beginning in 2011 through 2019 if we do not use them.

FASB Statement No. 109 provides for the recognition of deferred tax assets if realization is more likely than not. Based on available evidence, which includes our historical operating performance and the reported cumulative net losses in all prior years, we have provided a full valuation allowance against our net deferred tax assets. We intend to evaluate the realizability of the deferred tax assets on a quarterly basis.

LIQUIDITY AND CAPITAL RESOURCES

From our inception through May 1999, we financed our operations and capital expenditures primarily through the sale of approximately $12.4 million in equity securities. In June 1999 we completed an initial public offering of 2,860,000 shares of common stock and raised approximately $25.5 million, net of offering costs. In October 1999, we completed a secondary public offering of 500,000 shares of common stock and raised approximately $31.5 million, net of offering costs.

Cash provided by (used in) our operating activities was $(3.5) million for the six months ended March 31, 1999 and $5.8 million for the six months ended March 31, 2000. As of March 31, 2000, we had $61.2 million in cash and cash equivalents and $3.1 million in restricted cash. We expect that accounts receivable and inventories will continue to increase to the extent our revenues continue to increase. Any such increases can be expected to reduce cash and cash equivalents. We have provided extended payment terms to one of our resellers and may offer similar financing to other resellers in the future. To the extent such financing is offered, cash used in operating activities would increase to fund the increase in outstanding receivables.

Cash used in investing activities was $720,000 for the six months ended March 31, 1999 and $3.4 million for the six months ended March 31, 2000, substantially all of which was used for the purchase of property and equipment. We expect capital expenditures to continue to increase through the end of 2000, due to the costs of expansion and expenditures for information systems and test equipment.

As of March 31, 2000, our principal commitments consisted of obligations outstanding under operating leases. In March 1999 we began leasing approximately 20,000 square feet in a facility located in Seattle, Washington for a term of 60 months. In June 1999, we agreed to lease an additional 8,000 square feet in this facility for a term of 84 months. In December 1999 we began leasing approximately 13,000 square feet in an additional facility located in Seattle, Washington for a term of eleven months. The annual cost of these leases is approximately $854,000, subject to annual adjustments. We have also signed a lease for approximately 84,000 square feet of new office space in Seattle, Washington in a building which is currently under construction. This lease will commence on approximately June 1, 2000 with a term of 12 years. The annual cost of this lease is approximately $2 million, subject to annual adjustments. Our obligation under this lease is collateralized by a secured letter of credit in the amount of $2.5 million. As of March 31, 2000 we had no other material commitments. However, in April 2000, we entered into an agreement to lease approximately 110,000 square feet in Seattle, Washington in a building currently under construction. We anticipate a substantial increase in our capital expenditures and lease commitments consistent with our anticipated growth in our operations, infrastructure and personnel. In the future we may also require a larger inventory of products in order to provide better availability to customers and achieve purchasing efficiencies. We expect that our existing cash balances and cash from operations will be sufficient to meet our anticipated working capital and capital expenditures for the foreseeable future.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURE ABOUT MARKET RISK.

Interest Rate Risk. We do not hold derivative financial instruments or equity securities in our investment portfolio. Our cash equivalents consist of high-quality securities, as specified in our investment policy guidelines. The policy limits the amount of credit exposure to any one issue or issuer to a maximum of 20% of the total portfolio with the exception of treasury securities, commercial paper and money market funds, which are exempt from size limitation. The policy limits all short-term investments to mature in two years or less, with the average maturity being one year or less. These securities are subject to interest rate risk and will decrease in value if interest rates increase.

Foreign Currency Risk. Currently the majority of our sales and expenses are denominated in U.S. dollars and as a result, we have not experienced significant foreign exchange gains and losses to date. While we have conducted some transactions in foreign currencies during the fiscal year ended September 30, 1999 and the three and six months ended March 31, 2000 and expect to continue to do so, we do not anticipate that foreign exchange gains and losses will be significant. We have not engaged in foreign currency hedging to date, however we may do so in the future.

PART II
OTHER INFORMATION

ITEM 2. CHANGES IN SECURITIES AND USE OF PROCEEDS

Our registration statement (No. 333-75817) under the Securities Act of 1933, as amended, for our initial public offering of common stock became effective on June 4, 1999. Offering proceeds to the Company, net of aggregate expenses of approximately $1.0 million, were approximately $25.5 million. From the time of receipt through March 31, 2000, the proceeds were applied as follows:

- $2,500,000 was applied toward lease obligations for new office space secured by an irrevocable standby letter of credit.

- $500,000 was allocated to purchase inventory on credit secured by an irrevocable standby letter of credit; and

- Approximately $3,000,000 was applied toward working capital expenditures, including expenditures to sales and marketing, research and development and professional services.

The remaining proceeds are being held as cash, cash equivalents and short-term investments.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

The Company held its Annual Meeting of Shareholders on February 17, 2000 to elect two class I directors and amend the Company's 1998 Equity Incentive Plan to increase the number of shares issuable by an additional 1,000,000 shares. At the Annual Meeting, the following nominees were elected as follows:

	Votes	
	For	Against
Karl Guelich	15,448,458	10,289
Keith Grinstein	15,448,458	10,289

The shareholders voted in favor of amending the Company's 1998 Equity Incentive Plan to increase the number of shares issuable by an additional 1,000,000 shares, with voting as follows: 10,771,580 for, 4,699,620 against, and 89,086 abstain.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits:

27.1 Financial Data Schedule (filed only with the electronic submission of Form 10-Q in accordance with the Edgar requirements).

(b) Reports on Form 8-K:

No reports on Form 8-K were filed by the Company during the period ended March 31, 2000.

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized on this 10th day of May, 2000.

F5 Networks, Inc.
(Registrant)

By: /s/ Robert J. Chamberlain
--
Robert J. Chamberlain
Chief Financial Officer

(Duly Authorized Officer and Principal Financial and Accounting Officer)

EXHIBIT INDEX

Exhibit Index	Title
27.1	Financial Data Schedule

ARTICLE 5

THIS SCHEDULE CONTAINS SUMMARY FINANCIAL INFORMATION EXTRACTED FROM THE CONDENSED BALANCE SHEET AS OF MARCH 31, 2000 AND THE RELATED CONDENSED STATEMENTS OF OPERATIONS FOR THE SIX MONTH PERIOD ENDED MARCH 31, 2000 AND IS QUALIFIED IN ITS ENTIRETY BY REFERENCE TO SUCH FINANCIAL STATEMENTS.

PERIOD TYPE	6 MOS
FISCAL YEAR END	SEP 30 2000
PERIOD END	MAR 31 2000
CASH	61,225
SECURITIES	0
RECEIVABLES	22,047
ALLOWANCES	(900)
INVENTORY	1,566
CURRENT ASSETS	88,821
PP&E	6,914
DEPRECIATION	(1,641)
TOTAL ASSETS	94,389
CURRENT LIABILITIES	18,950
BONDS	0
PREFERRED MANDATORY	0
PREFERRED	0
COMMON	79,557
OTHER SE	(4,118)
TOTAL LIABILITY AND EQUITY	94,389
SALES	42,777
TOTAL REVENUES	42,777
CGS	12,528
TOTAL COSTS	23,419
OTHER EXPENSES	0
LOSS PROVISION	0
INTEREST EXPENSE	(1,559)
INCOME PRETAX	8,389
INCOME TAX	0
INCOME CONTINUING	8,389
DISCONTINUED	0
EXTRAORDINARY	0
CHANGES	0
NET INCOME	8,389
EPS BASIC	0.40
EPS DILUTED	0.36

End of Filing