INTRODUCTION

Today I want to cover with you the outlook for this year and next as well as some longer range aspects of our business. In addition, we should review a few fundamentals with regard to running our business and, cover some operating guidelines.

RECENT PAST

No comments regarding 1975 or 1976 could really be in context without reviewing the recent past and in particular, the events of the last year since July of 1974. It is an understatement to say that the months since July of 1974 have been ones of great trial for Control Data. Certainly this has been true for our Systems business and for our Services business. For example, our Systems business reported a loss of $77 million in the last six months of 1974. Expenses in the fourth quarter were at an all time high. Revenues were the lowest that they had been in four quarters. Gross profit rate in the last six months of last year dropped almost in half from previous periods as write-offs and expenses were taken into the P&L to compensate for some of the discontinued and mismanaged programs. With regard to all these dire statistics, however, I am reminded of Justice Holmes who once remarked, "I have no belief in panaceas and almost none in sudden ruin." To the extent that last year was a
disaster, it's roots lay as much in the distant past as in its present problems and, to the extent that we want to prevent such problems in the future, there can be no panaceas. It really is a question of fundamentals, a subject to which I will turn in a moment.

But there are two other aspects of this period that I want to share with you. Those aspects are that of a balanced perspective and the matter of change.

First, balanced perspective. On the one hand we could not dismiss the problems that overcame us last year by just laying the blame on the past. We had to meet them head on. On the other hand, the presence of those problems also could not allow us to falter in our drive to improve the long term fundamentals of our business. By and large, this balance has been maintained over the last year. And this is a source of great pride to us in Systems & Services.

A word or two about change. The past year has also been one of great change. From the rising storm of a year ago, we have seen each month an improving outlook in Systems & Services through this year. There have also been significant organization changes in the last year which have in one way or another affected most of you in this room. As always there are and have been changes in our economic and our competitive environment. With regard to change, however, it is most important
for us to remember that while change may facilitate an improvement in our fundamentals, it can never compensate for a lack of fundamentals. Nor can change by itself improve fundamentals. It is up to us to achieve that.

Likewise, as things improve it is important for us to remember that a change in fortunes, that is an improvement in fortunes, is not at all an indication that fundamentals are necessarily satisfactory. Rather it must be taken as an opportunity to apply greater effort to the further improvement of the fundamentals of our business.

Not every day of the past year has been a pleasant one for any of us at Control Data, but for me at least they have been mostly days of pride in the abilities of you and your colleagues in the other services and systems businesses to manage the present difficulties while driving toward future improvement. For example, the paycut. We knew at the end of 1974, that we had already instituted basic improvements in our business which would make us viable in 1975. On the other hand, we were sensitive to the fact that the severity of our cash outflow and our P&L problems was such that some dramatic steps had to be taken to tide us over until the fundamental improvement could be made to work. The paycut which we undertook was just such a measure, and it worked.
A few other items with regard to the past year. This year employment in the computer business is down 3,537 people. Over the last 12 months in our Systems & Services business it has dropped some 2,000 people. Almost half of that drop has occurred since last December. On the other hand, revenues over that same period in Systems & Services, have increased 15% and profitability, of course, is incomparably better.

Our assets actually peaked in the third quarter of last year and have dropped steadily ever since. Again, with revenues up and assets down, our asset to revenue ratio has improved by 12% from second quarter 1974 to second quarter 1975. Still at 1.25 it is unacceptably high. Stimulated and guided by Bill Hultgren of Chuck Roskam's financial staff, each of you will play an increasing role in further improving our use of assets.

Finally, I can't leave the subject of the past year without noting the dramatic difference in the situation with respect to some major programs such as ALS, STAR, and NASA Langley. Dramatic improvement in these programs from a year ago is a significant part of the turn around in our business and all of us should recognize the great effort that has been put forth by the people who are on these programs.

Moreover, the 170 has come into fruition and provides a basis for more optimism for the future than we have known for many years. At the September 12 meeting of Control Data's Board of
Directors, I addressed this subject. The following is a quote from my remarks to Control Data's Board.

"Recent CYBER 170 events represent much more than the successful first shipments of a new computer line. They represent the change from a no strategy, no win systems picture of two years ago -- dependent mostly on special bids and heavy discounts -- to a viable computer systems product line for protection of our installed base and expansion within our traditional markets. Add additional vitality from reduced support costs which has resulted from a more cohesive software strategy. Add additional vitality from new applications in Utilities and in Education -- all in all, it lends an optimism to our systems business that we have not seen in a long time."

All in all, with sunshine in the future and memories of the recent past, it would be more than a disgrace for any of us to slacken now...so let's discuss fundamentals.

FUNDAMENTALS

There are, of course, many ways to approach the subject of fundamentals, but a way I like to think is in terms of three fundamentals. These three fundamentals of the business are first a strategy and basic to having a strategy is a sound and comprehensive concept of the business you want to be in.
Second, a management system -- or better said, a system of management -- and basic to a sound management system, is understanding the essentials of revenue, of cost and expenses, and their relationship one to another, so that they can be given both visibility and measurement. Third, is execution and execution is the matter of people.

I can't cover every aspect of these fundamentals today, but I do want to mention some examples. First, let's talk about --

**Strategy and Concept** - Probably Control Data's greatest strength has been in its strategy. In fact, it might not be overstating to say that Control Data has survived mostly because of the strength of its basic strategic approach to the marketplace. A year or so ago, you will recall that a conceptualization of Control Data's business was given more concrete form in its Corporate Mission Statement and in the expression of the relation of its various products and services in the levels of service concept.

Another aspect of strategy and concept is product strategy for systems. This was allowed to languish for several years. As I have mentioned, the situation is much better now. All in all, we have today in place a sound concept of our business; a means of evaluating the relationships of our various products and services and individual product strategies to carry us forward into the future. Let me move on to the second fundamental of the management system.
Management System - While we have made some progress, this is something that needs far more attention for the future. It should be higher on our priority list than strategy. In one sense, it is even higher than execution, the third fundamental. That's because outstanding but **uncoordinated** execution can only lead to frustration and failure. Some examples needing much more attention and needing a better system of management are quality, asset and cash management, and linked goals for field operations, development, manufacturing, and systems operations.

In the area of cash management, we have made progress in trade receivables and those aspects of inventory management that have to do with stores and work in progress. This is because those things exist more on a "stand-alone" basis and are therefore, more susceptible to brute force and "exhortation of the troops." On the other hand, our computer business total receivables are 452 of which only 180 are trade receivables. That is, some 40% of the total. The remaining 60% are unaffected by our efforts thus far nor can they be affected by mere brute force. They can really only be affected by policy -- financing, accounting, measurement and incentive policy. In Systems & Services the lease base represents 17% of our assets. Yet what happens to these assets is neither planned nor subject to concerted management action. Clearly a system for managing the lease base is a top priority item.
Quality is even a more vital fundamental. It should have our highest priority. I have listed quality as an element needing attention as to management system. Just as clearly, it's also an item needing attention as to execution.

Execution. I said a moment ago that management systems may be more important to us at this point in time than execution. But that was only from one perspective. In another sense, execution is our most important fundamental because it is actually the most difficult to achieve. Finally, it rests on the leadership ability of you General Managers.

The aspects of execution that are most pressing are quality and cost control. In that regard, let me turn to the interaction between the fundamentals. For not only are all of these fundamentals of strategy, management system and execution important in themselves, they interact in a highly leveraged way. Also in that way I think I can further illustrate the importance of both quality and cost control.

Poor quality breeds uncontrolled costs and likewise poor cost control breeds poor quality. Now the first half of that statement is almost a cliche. Certainly anyone in our Engineering Services organization can expound at great lengths on the subject. But it is important to understand that the latter half of this statement, that is poor cost control breeds poor quality is equally valid. Why is this true? Because poor cost control means lack of attention to the essential elements of cost, to
how which costs affect the final product. Cost cannot be
controlled without this understanding. Given this understanding,
costs can be controlled. Without this understanding, costs
will not be cut by means of attention to critical factors or by
innovation with respect to critical factors. But only by
skimping, by shaving, or equivalently by a meat axe approach.
Either one of which will lead inexorably to poor quality.

Let me mention one other example of interaction. In this
case, let's take the interaction of quality as an element of
the management system with quality as a factor of execution.
Quality finally, is dependent on professionalism. In sport,
in business, in any human endeavor, professionalism -- that is
quality -- is apparent where it is clear that the details are
well attended to, well executed so that the final result is a
thing of pride and beauty.

And, so it is with us and a much more complex undertaking of
our computer business. To finally achieve quality, we must
have a system of management and of information flow that
allows managers to gain insight into the leverage points of
quality in our several businesses. Commitment to quality in
the absence of such an approach is empty sloganeering. Commit-
ment to quality in the context of a management system that
generates knowledge, experience, and professionalism will make us great.

I cannot leave the subject of fundamentals and teamwork without expressing a few more guidelines for us as a management team.

As a team, we should understand who or what we are attacking. Who in other words, is the enemy. Otherwise, we will find in the words of Pogo, "We have met the enemy and he is us."

Our enemies are excess assets, excess people, poor performers, inadequate management systems, lack of training and discipline, and unstable Systems business, lack of quality in products and services. In other words, generally poor execution and poor system of management, not poor strategy.

I am proud of our team. In one form or another, in one role or another, over the past ten years I have recruited almost every one of you, so I am proud of you, I know you and I like to work with you. On the other hand it is important that you understand that none of you are, to say the least, overqualified for your job. All of you need to grow. To the extent that you want to solve problems rather than build yourself up by deprecating others. To the extent that you are willing to grow and to learn rather than bitch or sulk. To the extent that you are positive and creative in finding a "better way" rather than hiding in the comfort of blaming the system. To that extent will you be successful.
Let me put it another way. If I filled out at this point in time, a performance appraisal on our Systems & Services Company it would have to be Level 5. Let me read you what Level 5 says in our Merit Appraisal Form. "Performance is less than satisfactory. Employee does not consistently achieve the minimal requirements. Performance improvement must be accomplished in order to justify retention in grade and position." Our appraiser, the financial community, feels that way about us.

But none of you are rated Level 5 so what we must have then is a great inverse synergism at work. The sum of the whole is worse than any of the parts. We are going to change that. Our Operation, our Company is going to be better than any one of us individually, not worse. In this regard with respect to execution and teamwork, I am reminded of an event that occurred many years ago.

(GENERAL MARSHALL STORY)

We are 60 million dollars ahead of last year at this same time in orders and if we meet our objectives we will be up 100 million over 1974. We have no orders with high risk and a dramatic reduction in total technical effort ordered. The gross profit in the incoming order stream is both better than
the goals and significantly better than past history. It is
good, broad growth; and we have every reason to believe this is
a sustainable trend into the coming year. We are accomplishing
these objectives while staying in our expense budget. If you
discount the effects of revaluation, we will be under our
profit improvement plan budget by 1 1/2 million dollars for the
year.

ASSETS

I have already mentioned asset improvement. Let's look at
some detail. Of the total computer business assets of 1,320
million, we have experienced improvement compared to 1974, in
almost all categories. Here are some Second quarter 1974 to
second quarter 1975 comparisons:

<table>
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<tr>
<th>Category</th>
<th>1974</th>
<th>1975</th>
<th>% Change</th>
</tr>
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<tbody>
<tr>
<td>Receivables</td>
<td>Down 18.7</td>
<td></td>
<td></td>
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<tr>
<td>Prop. Plant &amp; Equip.</td>
<td>Down 6.8</td>
<td></td>
<td></td>
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<tr>
<td>Deferred</td>
<td>Down 19.3</td>
<td></td>
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</tr>
<tr>
<td>NET Inventory</td>
<td>N/C</td>
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<tr>
<td>Leased &amp; Data CTR Equip.</td>
<td>Up 19.8</td>
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<tr>
<td><strong>TOTAL NET ASSETS</strong></td>
<td><strong>Down $37.1 Million</strong></td>
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As far as the total computer systems business is concerned, progress in continuing in achieving overall better asset utilization and further reductions in debt.

Domestic and international bank borrowings are down year-to-date through July by 57.3 million and in recent weeks borrowings under our $165 million credit agreement have been in the 45-60 million dollar range.

Those are dramatic improvements, they cannot continue without aggressive, creative programs on our part. We must do things differently as well as harder if progress is to continue. In fact, if we don't do things differently, the situation will worsen again.

For Control Data and total earnings per share through August were 1.80 compared to a budget of 1.79 (Bd. of Directors) and 1974 results of 1.74. Fall off in earnings in Commercial Credit — primarily in the insurance business — will mean that budgeted earnings per share will not be achieved although there will be great improvement compared to 1974.

The numbers I have given you are visible results of strategy, of system and of execution. However, there is other progress as well. First, we are increasing our emphasis on Application Services and the "levels of service" concept which underlies the Corporate mission. Three important additions to our
service organization are Techmatic, the Education Services Company of Commercial Credit and the Diversified Services Company also of Commercial Credit. With regard to Education Services. The Education Services Company of CCC will be concerned with the development and marketing of education (courseware) for all market areas. It will also be responsible for courseware publishing.

The Education Group of Systems and Services Company will be concerned with the development and marketing of delivery systems for computer-based education, but not education (courseware) itself. Initially, at least, this group will also have responsibility for the Iran, Venezuela and USSR projects.

Diversified Services will have its principle thrust in the area of EFTS. Both operations mark the beginning of Commercial Credit's long needed move from a pure financial services business to a business of financial and related non-financial services. Perhaps some of you recall that this need, in fact, the decaying prospect for a pure finance company was what brought Commercial Credit and Control Data together in the first place.

I have already mentioned the shortfalls, especially in Data Services in Mexico, Brazil and Australia. These countries need concentrated management attention if the situation is to change. We are going to give them that. On December 1, Herb Hughes whose experience in this area is as great as anyone in
the company, will assume total financial and operating responsibility for these subsidiaries. He will report to Jack von Gillern.

Another management change is in Systems. We have asked Boyd Jones to assume responsibility for STAR in the Large Computer Systems. His knowledge and understanding of this critical market area, which is so important to us, will be of great benefit to our Systems business as we move forward.

FUTURE OUTLOOK

Now let me turn to the future. The essential thing that you have to keep in mind is that Control Data stands in the most highly leveraged position in its history. What do I mean by "highly leveraged"? It is this: We have assembled the products and services, we have assembled the customer base and we have assembled the talents and strategic concept relating all those things on which a great company can be built. I say, can be. For if we continue to execute to manage our assets, our costs and expenses, our pricing in the manner of the past, we will not build that company. On the other hand, it is perfectly within our capability to change. The great thing is that it does not require genius, it does not require quantum jumps or a totally revolutionary approach. It requires an attitude of willingness to change, to learn, to grow, to find a better way. It requires more than anything, a willingness to work, to discipline ourselves and to pay attention to detail. And it requires teamwork.
In June, along with the five year strategic plan, we presented some historical analysis and commentary regarding the implications of the plan. I want to make one or two observations on this and also emphasize a few key numbers.

First of all, for some numbers.... Control Data computer business in 17 years through 1974 will have achieved total revenues of over $5.5 billion yet will probably surpass this revenue in the next 4+ years of its operation. Computer business profit before taxes have been approximately $80 million in that same period of time and these accumulative profits should be exceeded by S & S Company alone in the next five years. While assets have grown to $1.3 billion in 16 years, there are many reasons to believe that the next five years of progress will result in a net cash contribution as opposed to increased debt to finance our historically meager earnings and huge asset growths. Some other highlights worth noting are 1) our expense ratios in total were good up to 1966 and have never been as good since -- until 1975. 2) There has been an inclination, perhaps a necessity, always to sell off the lease base to meet some short term need or desire. SOLR was the worst example of this.

One observation has to do with the planning process itself. In the past plans were mostly statistical extrapolation. For example, "We have experienced a historical gross profit rate
of X% on this product and we have shipped N Systems per year about Z% of which is purchased. We plan to grow (or decrease) Marketing effort-wide percent. Therefore the plan is ...."

And what followed was obvious. A lot of arithmetic and no thinking. A wholly separate exercise involved technical effort which started with a wish list and got cut back until it fit within the expenses permitted by the assumed and as you might guess optimistic revenue and gross profit projection.

This has changed. Up until 1974, we never had a truly integrated marketing and systems plan. Last year we produced a prototype that took us 13 months to put together. This year it took three months but it involved process, commitment, and a better understanding of basic cost elements. Our people are finally beginning to think in terms of markets. What is required to sell, and to whom we are selling. Marketing and operations talk much more about to whom we are selling. Whatever else they may or may not have achieved, the IMO's have brought this kind of thinking to our products people.

Another observation has to do with assets. The most striking factor is that we can achieve major improvements in asset and cash utilization in the next five years. 1975 improvements were achieved solely by means of exhortation. Those things most amenable to exhortation - receivables and inventory responded.
Using 1974 ratios our business would increase its net assets by approximately $700 million in the next five years and its "debt" by $400 million. With the new programs we now see assets could increase by only $60 million and "debt" could decrease by $200 million. But once again it is important to note that we must and will change to achieve that.

Our priorities are on better measurement and linking of goals. As an example of this, Marketing is changing to a "targeted incentive" compensation plan — a fundamental change and one vital to a linked goal process. The lease base management system will come into use in 1976. We must further reduce costs and expenses and people that our dependence on such things as booking long-term leases as purchase, and purchase conversions in order to generate enough gross profit to cover expenses can be reduced. Turnaround in vital Data Services segments: Brazil, Mexico, Australia, Ticketron, COMPU/NET must be achieved in 1976.

New applications for our Systems and Services in energy management, engineering design and education are planned. CBE is critical to internal improvement in training as well as to Education Services business.

I hope that you can sense the opportunities that lie ahead for all of us. Our basic business strategy has put us on the right
track. We are building momentum toward a better system of management. Our 1976 mission in a word is "Execution". The result will be quality - quality performance. And I look forward to sharing that performance with you.