Control Data Board of Directors
March 10, 1978
R. M. Price

Introduction & Overview

We are off to a good start in 1978. Our overall Computer Group results were favorable to plan in both January and February. Six of the 11 Product Families were ahead of the profit budget including all three of the major profit producers: Data Services, EDP Systems and OEM. The shortfalls relative to budget were in the smaller product families.

With regard to these latter areas, Small Systems is by far the most difficult. In brief we have a classic case of an over-extended organization whose difficulties are compounded by a major critical situation. In this case the critical situation is the delivery of Automated Wagering Systems to two Australian customers. These deliveries are seriously late. We have now passed dates which have been renegotiated twice. The more serious of the two is the Victoria TAB. I was in Australia last week to meet with their board. We have been given a further few months which have been renegotiated twice. The next few months will be very difficult and success is by no means assured. The situation is just about as bad as you come across.

(1) First we are dealing with a very weak customer. History.
(2) That's no excuse because dealing with weak customers is a part of being in business.

(3) The program has not been well managed either locally or here in Minneapolis.

(4) The result is that over time the project and the customer have come to a point of specification lawyering as opposed to getting a workable system.

We are taking strong action, of course. As I told the Victoria TAB Board I am confident that we can achieve a workable system but we will not achieve one unless changes in approach occur. This is by no means easy at this point in the game.

REVENUE

At the end of February our revenues were $244 million or $1M ahead of budget. We were below budget in January but an excellent February has put us ahead of plan year to date.

Our data services revenue was ahead of budget despite the impact of bad weather in some of our principal business areas. We do have some concern about the potential impact of the coal strike. If we are forced to curtail operations, we could have a significant revenue impact. In Cybernet at the moment we are somewhat less concerned about the Cleveland Center than the Rockville Center even though the utilities in Ohio are in bad shape.
EDP Systems revenue is essentially on budget year to date. To continue to achieve budgeted revenue we need to get $64M of purchase revenue in 1978 from orders booked in 1978. This is a significant challenge for our EDP and Marketing organizations and considerable management attention is being given to this requirement.

In Peripheral Products, our OEM business continues strong. Revenues, while slightly less than budget are still running more than 40% higher than last year. The incoming order rate is excellent and we should have another very good year in OEM.

Gross Profit

Our efforts to improve the quality of incoming business and reduce manufacturing and operational costs are reflected in the higher gross profit rates. Thus, February total GP of $94.8 million represented rate of 38.9% compared to a budget of 37.6%. This was particularly true in EDP systems which achieved a gross profit rate of 68% compared to a budget of 60% and actual rates a year ago of 61%. (Rate is through February.)

The principal adverse impact on gross profit rates comes from our international wagering business.
EXPENSES

The expense levels were also held below budget in the first two months by $3.8 million. The savings were generally in all categories of expense. The largest savings were in technical effort, but selling, administrative and interest were all below budget.

General expense was higher with some adverse impacts from balance sheet translation which totaled $1.5 million in the first two months. While the weakening of the dollar will produce P&L benefits during the year, the immediate effect due to balance sheet translation is unfavorable because of our short position in some strong currencies such as the Belgian franc. The Belgian government’s financing for the Brussels Cluster Center is the principal reason for our short position.

NET PROFIT

Net profit for the first two months was $9.5 million compared to a budget of $2.3. About half of this improvement was due to gross profit and half to lower expenses.

As I indicated earlier the large product families beat their profit targets. We are working with those that are behind – notably Aerospace, Small Systems and Miniperipherals – to get them back on plan.
ASSETS

Total assets were $1,227 million or $34 million below budget. Compared to last year our assets are up 1.4% while revenues are up about 16% reflecting substantial asset efficiency improvements. We are, however, concerned about the $14 million increase in February. About $3 million was in receivables and most of the rest in inventory. We are reviewing our efforts to improve collection of receivables. During the next three months, a special team will make on site reviews of organizations with significant amounts of past due receivables. We expect to improve the near term performance and also the process for billing and collection.

The increases in inventories were primarily in OEM and Systems product families, and reflect increased build schedules to meet higher order requirements.

SUMMARY AND OUTLOOK

So all in all we are off to a reasonable start for the year. In terms of product strategy and marketing capability I can truly say that I never have felt better. Data Services is doing well and I feel with a few things in the cooker like AGSERV, Industrial Weather Service, Medical Services and some other fledging businesses that we are truly growing the data services business and not just getting it respectable. At the same
TIME OUR PEOPLE ARE MUCH MORE COMFORTABLE WITH THE TRIPARTITE APPROACH OF SERVICES, PERIPHERALS AND SYSTEMS. LAST YEAR WE BEGAN TO SEE SOME REAL FRUITS OF THIS. BACK IN THE 60’S BOB SCHMIDT, VERN SIELING, BOB CHINN AND I TRIED EVERY IMAGINABLE WAY TO CRACK IBM’S IMPERISHABLE FORTRESS AT FORD AND IT WAS JUST TOO HARD. LAST YEAR WE HAD A SUCCESS STORY AT FORD THAT IS SO SWEET I WANTED YOU TO HEAR IT FROM THE REGIONAL MARKETING MANAGER WHO DIRECTED THE EFFORT. SO A LITTLE LATER WE WILL INTRODUCE MR. ROGER SHOBER TO YOU.

ON THE OTHER SIDE OF THE BALANCE IS THE CONCERN FOR THE YEAR AS A WHOLE. THE RECEIVABLES ISSUE FOR EXAMPLE. WE HAVE MADE GOOD PROGRESS IN RECEIVABLES FOR TWO STRAIGHT YEARS. BUT NOT ONLY ARE THEIR LARGE PACKETS OF INTRANSIGENCE SUCH AS EUROPE, THE RECEIVABLES SITUATION INDICATES TIGHTENING MONEY – ESPECIALLY FOR SMALLER COMPANIES.

AUTOMATED WAGERING IS A SERIOUS SITUATION AND CANNOT BE BRUSHED ASIDE.

ALL-IN-ALL TWO MONTHS INTO THE YEAR IT’S SO FAR SO GOOD AND A FEW CLOUDS OF MORE THAN NORMAL CONCERN.