REVIEW OF AUGUST RESULTS
OF THE COMPUTER GROUP
SEPTEMBER 15, 1978 BOARD OF DIRECTORS MEETING
R. M. PRICE

OUR PROGRESS TOWARD IMPROVED FINANCIAL RESULTS CONTINUED IN JULY AND AUGUST. REVENUES AND PROFITS FOR THESE MONTHS WERE SIGNIFICANTLY HIGHER THAN THE AVERAGE FOR THE FIRST 6 MONTHS OF 1978.

FOR JULY AND AUGUST, THE RESULTS OF COMPUTER PERIPHERALS, INC. ARE INCLUDED ON A CONSOLIDATED BASIS BECAUSE OUR OWNERSHIP NOW IS 60%. AS YOU KNOW, DURING THE FIRST SIX MONTHS OUR 42% SHARE OF CPI'S RESULTS WAS INCLUDED ON THE EQUITY IN AFFILIATES LINE OF THE P&L. THE CPI IMPACT ON PROFIT IS MINIMAL. IN JULY AND AUGUST, CPI REVENUE OF $7 MILLION AND GROSS PROFIT OF $1 MILLION ARE INCLUDED IN OUR CONSOLIDATED RESULTS.

THE IMPACT OF THE CPI TRANSACTION ON CONSOLIDATED ASSETS, HOWEVER, IS SIGNIFICANT. PREVIOUSLY WE HAD RECORDED AN INVESTMENT OF $24 MILLION IN CPI. NOW AS A CONSOLIDATED SUBSIDIARY WE REFLECT ALL OF CPI'S $45 MILLION OF ASSETS ON OUR BALANCE SHEET. THE $21 MILLION INCREASE IN ASSETS IS OFFSET BY A CORRESPONDING MINORITY INTEREST ACCOUNT SO THERE IS NO IMPACT ON CASH OR DEBT.
THE OBJECTIVE OF THE CPI TRANSACTION, OF COURSE, WAS NOT TO ACHIEVE IMPROVED SHORT TERM FINANCIAL RESULTS. IT WAS TO PROVIDE MORE CONSISTENT LONG TERM STRATEGIC DIRECTION THAN COULD BE ACHIEVED UNDER THE PREVIOUS OWNERSHIP STRUCTURE. WE HAVE A READY MADE MARKET FOR CPI TAPE AND PRINTER PRODUCTS IN OUR OEM AND END USER CUSTOMERS THAT ARE MAJOR USERS OF OUR DISK PRODUCTS. AS WE ALIGN THE CPI PRODUCT STRATEGIES MORE CLOSELY WITH THE NEEDS OF THESE MARKETS, WE EXPECT TO ACHIEVE CORRESPONDINGLY BETTER FINANCIAL RESULTS.

CHART 1

OUR COMPUTER GROUP REVENUE FOR JULY AND AUGUST TOTALLED $296 MILLION. EXCLUDING CPI SALES, OUR REVENUES WERE ABOUT 27% HIGHER THAN THE COMPARABLE TWO MONTHS IN 1977. PERIPHERAL PRODUCTS EXPERIENCED THE HIGHEST GROWTH WITH A 37% INCREASE OVER THE PRIOR YEAR.

YEAR-TO-DATE OUR REVENUES FOR THE COMPUTER GROUP WERE $1,122 MILLION OR ABOUT 5% HIGHER THAN BUDGET AND 22% HIGHER THAN LAST YEAR.

CHART 2

GROSS PROFIT TOTALLED $113 MILLION IN JULY AND AUGUST. YEAR-TO-DATE GROSS PROFIT IS $430 MILLION OR ABOUT 7% BETTER THAN BUDGET. WHILE MOST OF THE ADDITIONAL GROSS PROFIT REFLECTS
THE HIGHER VOLUME, WE HAVE BEEN SUCCESSFUL IN INCREASING OUR OVERALL GROSS PROFIT RATE TO 38.4% COMPARED TO A BUDGETED 38.0%. THIS IMPROVEMENT OCCURRED DESPITE A CHANGE IN MIX TOWARD THE LOWER MARGIN OEM BUSINESS. ALL MAJOR SEGMENTS ARE ACHIEVING HIGHER THAN BUDGETED MARGINS WITH PARTICULARLY GOOD RESULTS IN EDP SYSTEMS.

CHART 3

WHILE REVENUE IS RUNNING ABOUT 5% MORE THAN BUDGET, OUR EXPENSES ARE ESSENTIALLY ON PLAN. THE YEAR-TO-DATE EXPENSES ARE $367 MILLION COMPARED TO A BUDGET OF $366 MILLION. THE IMPACT OF THE GENERAL WEAKENING OF THE DOLLAR HAS BEEN TO RAISE OUR EXPENSES BY ABOUT $6 MILLION. IN OTHER WORDS, OUR EXPENSES AS MEASURED BY THE EXCHANGE RATES IN THE BUDGET ARE ABOUT $5 MILLION LESS THAN BUDGET. I SHOULD NOTE, HOWEVER, THAT PART OF OUR GROSS PROFIT IMPROVEMENT IS ALSO DUE TO CHANGES IN EXCHANGE RATES.

CHART 4

NET PROFIT BEFORE TAX FOR JULY AND AUGUST TOTALED $19 MILLION BRINGING OUR YEAR-TO-DATE PROFIT TO $63 MILLION.

THE YEAR-TO-DATE PROFIT OF $63 MILLION IS MORE THAN 70% AHEAD OF THE COMPARABLE PERIOD LAST YEAR SO OUR PERFORMANCE ON A
RELATIVE BASIS LOOKS FAVORABLE. ON AN ABSOLUTE BASIS, HOWEVER, IT STILL REPRESENTS ONLY ABOUT 5.6% OF REVENUE, PRE TAX. AS WE START ON OUR BUDGET FOR 1979, WE HAVE STILL THE MAJOR PROBLEM OF RAISING PROFITABILITY LEVELS. AND I DON'T MIND ADMITTING THAT I AM NOT MY USUAL CONFIDENT SELF. IT IS THE HARDEST TASK I HAVE EVER FACED. ONE THING THAT REALLY MAKES IT HARD IS THAT MANAGEMENT DUTIFULLY BOWS AT THE ALTER OF THE BOSS'S EXHORTATION AND THEN EACH INDIVIDUALLY GO OFF TO PURSUE THEIR PET PROJECTS WHICH "THEY KNOW" WE CAN AFFORD. THE REAL POINT, HOWEVER, IS NOT THE PET PROJECTS THEMSELVES, BUT RATHER THAT MANAGEMENT ATTENTION IS FOCUSED ON THESE FUN THINGS RATHER THAN ON THE MORE MUNDANE TASK OF IMPROVING THE PROFITABILITY OF CURRENT OPERATIONS. COMPOUNDING ALL THAT IS THE FACT THAT VOLUME INCREASE IS HAVING THE STANDARD IMPACT ON GROSS MARGINS WHICH FURTHER LULLS PEOPLE INTO THINKING THEY ARE DOING A SUPERB MANAGEMENT JOB. ANYWAY, WE ARE PLUGGING AWAY.

Here is the chart which reflects the CFO additions I mentioned.

With that quick look at the financial highlights, let me turn to a few noteworthy operational items.

OEM

CURRENT ORDER RECEIPTS OF $231 MILLION ARE DOUBLE OUR BUDGET, AND THE TOTAL OEM FORECAST FOR THE YEAR OF $260 MILLION IS $85 MILLION BETTER THAN BUDGET. DEMAND FOR OUR DISK PRODUCTS CONTINUES TO EXCEED OUR EXPECTATIONS. ON SEPTEMBER 12 WE
ANNOUNCED ADDITIONAL ENHANCEMENTS TO THE 3350 DISK LINE. THERE IS NO COMPETITIVE PRODUCT ON THE MARKET TODAY THAT CAN MATCH THE 3350 IN PRICE/PERFORMANCE OR FEATURES. WE HAVE UNITS INSTALLED AND RUNNING AT A CUSTOMER SITE AT 635 MEGABYTES, AND ANY 33801 CUSTOMER CAN FIELD-UPGRADE TO 635. THIS ANNOUNCEMENT IS SIGNIFICANT IN THAT IT CLEARLY SINGLES OUT CDC AS HAVING THE MOST ADVANCED AND COMPLETE FLEXIBLE DISK PRODUCT AVAILABLE IN THE WORLD.

PERIPHERAL SYSTEMS

WE HAVE RECEIVED TEN ORDERS FOR OUR MASS STORAGE SYSTEMS SINCE THE FIRST OF THE YEAR AND HAVE SUCCESSFULLY INSTALLED TWELVE SYSTEMS AT EIGHT CUSTOMER SITES. SINCE OUR FIRST INSTALLATION IN NOVEMBER 1976, WE HAVE INSTALLED A TOTAL OF TWENTY-SIX MASS STORAGE SYSTEMS.

BUSINESS PRODUCTS

ORDER LEVELS FOR BUSINESS PRODUCTS OPERATIONS OF $87.0 MILLION ARE NOW $13.0 MILLION AHEAD OF BUDGET. OMAHA AND WALES BOTH CONTINUE TO RUN AT MAXIMUM CAPACITY. THESE TWO PLANTS WERE SHIPPING 15,000 PACKS PER MONTH LAST YEAR AND WE ARE NOW SHIPPING AT A RATE OF 20,000.
EDP SYSTEMS

CYBER 175 DELIVERIES ARE AHEAD OF PLAN FOR 1978. THIS YEAR WE WILL SHIP 26 175'S. WE HAVE 42 IN NEXT YEAR'S SCHEDULE. OUR SCHEDULE OF ALL 170'S WILL INCREASE FROM 92 THIS YEAR TO 134 IN 1979.

AEROSPACE

WE CONTINUE TO MAKE PROGRESS IN OUR EFFORTS TO TURN AROUND THE AEROSPACE BUSINESS. THE COMPUTING DEVICES OPERATION IN CANADA AND OUR DIGITAL IMAGE DIVISION WILL BOTH PERFORM FAVORABLE TO BUDGET IN 1978. THE LOCAL AEROSPACE DIVISION IS RESPONSIBLE FOR THE SHORTFALL, BUT THERE ARE GOOD SIGNS IN THAT OPERATION. THE SPECIAL NAVY AIRBORNE COMPUTER PROGRAM IS NOW ON SCHEDULE. WE ARE RECEIVING NUMEROUS RFQ'S FOR OUR MIL DISK PRODUCT WHICH PROMISES TO BE A SUCCESSFUL PROGRAM.

THE MOST SIGNIFICANT EVENT IN THIS OPERATION RELATES TO THE POST OFFICE PROGRAM IN CANADA. OUR MANY MONTHS OF EFFORT AND NEGOTIATION HAVE RESULTS IN A REQUEST FROM THE GOVERNMENT FOR US TO DISCONTINUE OPERATIONS, WHICH WE DID LAST WEEK. THE GOVERNMENT IN TURN GAVE US A TIME AND MATERIAL CONTRACT WHICH EMPLOYS ALMOST ALL OF OUR PEOPLE ON A SOFTWARE MAINTENANCE CONTRACT. CONTROL DATA AND THE GOVERNMENT HAVE AGREED TO SETTLE ON PAYMENT DUE US FOR WORK ACCOMPLISHED TO
DATE. WE ANTICIPATE THAT WE WILL SETTLE THIS MATTER WITHIN THE RESERVE WE HAD SET UP WITHIN THE NEXT 30-60 DAYS.

DATA SERVICES

TICKETRON


BRAZIL

BRAZIL'S 6600 IS COMPLETELY SATURATED AND THEY ARE LINKING VIA SATELLITE TO THE ECC IN ROCKVILLE TO ACCOMMODATE THE INCREASED PROCESSING UNTIL THE CYBER 175 IS INSTALLED DURING 1Q79.

ARB

SYNDICATED TV REVENUE IS $600K OVER BUDGET THRU 8/30/78 DUE PRIMARILY TO THE SUCCESS OF THE EARLY RENEWAL CAMPAIGN IN MARKETS 4-100. SYNDICATED RADIO REVENUE IS $1200K OVER BUDGET THRU 8/30/78 DUE PRIMARILY TO A GAIN OF NET NEW CLIENT OVER LOST CLIENT EQUAL TO $450K. ANOTHER $450K GAIN IS CAUSED BY OUR CLIENTS BILLING RATES UPON WHICH OUR BILLING
RATES ARE BASED. RADIO COVERAGE PRODUCT (SPECIAL REPORTS BY COUNTY) IS $150K BETTER THAN PLAN.

SBC

NEW ACCOUNT PRODUCTIVITY FOR JUNE-AUGUST 1978 IS 45% AHEAD OF THE SAME PERIOD IN 1977. 585 NEW ACCOUNTS VERSUS 403 PREVIOUSLY - PRIMARILY AUGUST. YEAR IS UP 14% IN TOTAL.

CYBERNET

- AUGUST REVENUE PER DAY WAS $267K, UP $30K FROM THE 12 MONTH AVERAGE, WHICH REFLECTS A GENERAL INCREASE ACROSS ALL REGIONS AND ALL PRODUCT LINES. DURING THE FIRST SEVEN MONTHS OF 1978, CYBERNET'S REVENUE PER DAY HAD REMAINED BETWEEN $238K AND $244K.

- GSA REVENUE YEAR-TO-DATE IS $1.3M AND SHOWS AN INCREASE FROM $83K IN JANUARY TO $228K IN AUGUST. THE 1979 GSA/TSP PROPOSAL WAS COMPLETED AND SUBMITTED TO GSA IN AUGUST.

ENGINEERING SERVICES

OF SIGNIFICANT INTEREST IS OUR SOON-TO-BE-ANNOUNCED TUITION PAYMENT FOR FEMALE NON-EXEMPTS TO ENROLL IN CDI AND PREPARE TO BE CUSTOMER ENGINEERS. IT WILL BE A PLUS IN OUR AFFIRMATIVE
ACTION PLANS AS WELL AS PROVIDE A PROMOTIONAL OPPORTUNITY FOR A GROUP OF OUR EMPLOYEES WHO FEEL DEAD-ENDED IN THEIR PRESENT JOBS.

PSD

IN PSD, FOLLOWING A SUCCESSFUL OPENING OF OUR INAUGURAL FAIR BREAK CENTER IN ST. PAUL IN MAY, WE WILL BE OPENING A FULL CENTER IN DAKOTA COUNTY AND BE FURNISHING COMPONENT SERVICES IN ST. LOUIS COUNTY. BOTH WILL BE ACCEPTING CLIENTS ON MONDAY, SEPTEMBER 18. WE ARE ALSO FINDING AVID INTEREST AMONG RETAILERS IN OUR SKILLS TO PRODUCE APPLICATIONS FOR THE PERSONAL COMPUTERS.

MARKETING

THE ORDER AND REVENUE YEAR-END PROJECTIONS CONTINUE TO LOOK VERY STRONG ACROSS ALL PRODUCT FAMILIES AND GEOGRAPHIES. WE ARE AHEAD OF ALL YEAR-TO-DATE ORDER TARGETS AND REVENUE EXCEPT EDUCATION. THE U.S. DATA SERVICES, SYSTEMS, AND OEM LEADING THE WAY AND WEST EUROPE WITH OEM AND BUSINESS PRODUCTS IN THE LEADERSHIP ROLES ARE THE STRONGEST GEOGRAPHIC PERFORMERS.