SUMMARY OF COMPUTER COMPANY RESULTS
BOARD OF DIRECTORS
NOVEMBER 16, 1979
R. M. PRICE

THIS IS THE LAST TIME I WILL BE SPEAKING TO YOU BEFORE YEAR-END AND I AM PLEASED TO BE ABLE TO TELL YOU THAT WE CONTINUE TO MAKE PROGRESS, WITH MOST OF OUR INDICATORS SHOWING STEADY IMPROVEMENT. I AM GOING TO GO OVER THE NUMBERS FAIRLY QUICKLY TODAY -- NOT BECAUSE I AM NOT PROUD OF THEM -- BELIEVE ME, I AM -- BUT REALLY IN ORDER TO HAVE A FEW MINUTES TO COVER A SOMEWHAT BROADER PERSPECTIVE OF THE BUSINESS.

RC-2
FOR THE FIRST TEN MONTHS OF THIS YEAR TOTAL REVENUES WERE $1.8 BILLION, WHICH IS 7 PERCENT BETTER THAN BUDGET AND 20 PERCENT AHEAD OF 1978. WITHIN THE NEXT TWO OR THREE WEEKS, CONTROL DATA'S COMPUTER BUSINESS WILL, FOR THE FIRST TIME, CROSS THE $2 BILLION MARK IN REVENUE. CONTRIBUTING MOST SIGNIFICANTLY TO THIS GROWTH WERE PERIPHERAL PRODUCTS, UP 34 PERCENT, AND DATA SERVICES, UP 20 PERCENT, FROM THE COMPARABLE PERIOD IN 1978.

RC-3
GROSS PROFIT MARGINS CONTINUE TO IMPROVE. THROUGH OCTOBER TOTAL GROSS PROFIT WAS 7 PERCENT HIGHER THAN BUDGET. THE GROSS PROFIT RATE IS 32.3 PERCENT. FOR THE FIRST 10 MONTHS OF 1978 IT WAS TO 38.1 PERCENT. THE MOST SIGNIFICANT CONTRIBUTOR TO THIS YEAR-TO-YEAR GROSS MARGIN IMPROVEMENT WAS EDP SYSTEMS.
TOTAL EXPENSES FOR THE PERIOD WERE $580 MILLION, VIRTUALLY ON BUDGET. THIS TRANSLATES TO 32.4 PERCENT OF REVENUE COMPARED TO 33.1 PERCENT LAST YEAR. MARKETING EXPENSES REPRESENTED THE BIGGEST INCREASE OVER LAST YEAR, 21 PERCENT, AS WE HAVE ADDED TO OUR SALES FORCE IN SEVERAL OF THE BUSINESSES. ADMINISTRATIVE EXPENSES WERE UP 20 PERCENT -- EXACTLY THE SAME AS REVENUE. I'LL COMMENT MORE ON THAT IN A MOMENT.

INTEREST EXPENSE OF $40 MILLION WAS $7 MILLION BELOW BUDGET AND $1 MILLION BELOW LAST YEAR DESPITE INCREASING INTEREST RATES. ASSET EFFICIENCIES AND THE IMPROVED EARNINGS PERFORMANCE HAVE MADE THIS POSSIBLE.

ON AN ANNUALIZED BASIS, WE ARE EMPLOYING 54 CENTS OF ASSETS TO ACHIEVE AN INCREMENTAL DOLLAR OF REVENUE. TOTAL ASSETS AS OF OCTOBER 31 WERE $1490 MILLION OR 2 PERCENT HIGHER THAN BUDGET.

INVENTORIES, HOWEVER, CONTINUE TO BE UP 28 PERCENT FROM A YEAR AGO AT $542 MILLION, WHICH IS 21 PERCENT HIGHER THAN BUDGET. EDP SYSTEMS INVENTORIES ARE UP 36 PERCENT. HOWEVER, WITH THE SHIPMENT OF SEVEN SYSTEMS BEFORE YEAR END, SYSTEMS' INVENTORY SHOULD ACTUALLY DECREASE OVER THE NEXT TWO MONTHS.

PERIPHERAL PRODUCTS INVENTORIES ARE UP 48 PERCENT BUT ARE ALSO PLANNED TO LEVEL OFF OVER THE NEXT TWO MONTHS.
RC-5

NET PROFIT BEFORE TAXES FOR THE 10-MONTH PERIOD WAS $123 MILLION COMPARED TO $74 MILLION A YEAR AGO. THAT REPRESENTS A NET PROFIT MARGIN OF 6.9 PERCENT, UP FROM 4.9 PERCENT LAST YEAR.

DATA SERVICES

RC-2

DATA SERVICES OCTOBER REVENUE REACHED A NEW MONTHLY HIGH OF $38.6 MILLION WITH SBC EXCEEDING $18 MILLION IN REVENUE FOR THE FIRST TIME.

THE FIRST 10 MONTHS' REVENUE WAS $347 MILLION, $100 MILLION HIGHER THAN BUDGET AND 20 PERCENT OVER 1978.

RC-5

NET PROFIT FOR THE FIRST 10 MONTHS WAS $35 MILLION. NET PROFIT MARGIN WAS 10 PERCENT, THROUGH 10 MONTHS COMPARED TO 8.4 PERCENT FOR THE SAME PERIOD IN 1978.

THE GROWTH IS PRIMARILY DUE TO HIGHER REVENUES CAUSING INCREASED ACCOUNTS RECEIVABLE LEVELS AND TO INCREASED INVESTMENT IN REVENUE PRODUCING EQUIPMENT.
SYSTEMS

RC-2


RC-5

DUE TO THE IMPROVED GROSS PROFIT MARGINS I MENTIONED EARLIER, SYSTEMS' NET PROFIT BEFORE TAXES WAS 2 PERCENT BETTER THAN BUDGET THROUGH OCTOBER. SPECIFICALLY, THE GROSS PROFIT RATE IMPROVED FROM 53.9 PERCENT FOR THE 10-MONTH PERIOD IN 1978 TO 59.4 PERCENT. NET PROFIT AS A PERCENT OF REVENUE WAS 8.5 PERCENT COMPARED TO 8.5 PERCENT LAST YEAR.

PERIPHERAL PRODUCTS

RC-2

TOTAL PERIPHERAL PRODUCTS COMPANY REVENUE OF $715 MILLION IS $111 MILLION AHEAD OF BUDGET AND 34 PERCENT HIGHER THAN THE COMPARABLE PERIOD LAST YEAR. THIS INCREASE CONTINUES TO REFLECT VERY STRONG DEMAND FOR DISK PRODUCTS AND RELATED MEDIA.

BOTH OEM AND BUSINESS PRODUCTS ARE FORECASTING A STRONG FOURTH QUARTER WITH ORDERS AND BACKLOGS REMAINING VERY STRONG. RECENT FACILITY EXPANSION IS HELPING TO ALLEVIATE SOME OF THE CUSTOMER ORDER PRESSURE AND IMPROVE OUR PRODUCTION CAPACITY.
RC-5

NET PROFIT BEFORE TAX OF $70 MILLION WAS AHEAD OF LAST YEAR BY $26 MILLION. OEM AND BUSINESS PRODUCTS ARE BOTH HAVING EXCELLENT RESULTS. ALSO, PERIPHERAL SYSTEMS IS HAVING A GOOD YEAR IN PLUGS -- PROFIT OF $9.7 MILLION ON REVENUE OF $69.3 MILLION. BUT THE OMEGA PROGRAM WITH INVENTORY DEVALUATION AND BAD DEBT PROVISIONS AS WELL AS AN OPERATING LOSS MORE THAN OFFSETS THAT WITH A TOTAL LOSS OF $5.5 MILLION.

EDUCATION

RC-2

THE TOTAL EDUCATION REVENUES THROUGH OCTOBER WERE $49 MILLION AND REFLECT SIGNIFICANT PROGRESS IN MOST OF THE BUSINESS UNITS. REVENUE PERFORMANCE HAS INCREASED 32 PERCENT COMPARED TO LAST YEAR; HOWEVER, THERE IS A SHORTFALL FROM THIS YEAR'S BUDGET APPROXIMATING 10 PERCENT DUE TO THE LOSS OF THE IRAN PROGRAM REVENUE AND OUT-RIGHT BUDGET CANCELLATION. THE U.S. CONTROL DATA INSTITUTES WERE 18 PERCENT FAVORABLE COMPARED TO BUDGET AND MONTHLY SALES ARE UP 24 PERCENT OVER JANUARY 1979. LEARNING CENTERS, SEMINARS AND CDI INTERNATIONAL ALSO REFLECT IMPROVED PERFORMANCE. MONTHLY SUBSCRIPTION REVENUES REFLECT A BETTER THAN 50 PERCENT INCREASE SINCE THE END OF LAST YEAR.
RC-5

FOR TEN MONTHS THE EDUCATION SHORTFALL FROM BUDGET WAS $2.8 MILLION. OFFSETTING THE IRAN AND EDUCATION SYSTEMS SALES SHORTFALL IS IMPROVED PERFORMANCE BY CDI WORLDWIDE AND LEARNING CENTERS WHERE A $3.3 MILLION BETTER-THAN-BUDGET CONDITION EXISTS.

GENERAL COMMENTS

WITH THAT BRIEF OVERVIEW, LET ME TURN NOW TO A Couple OF LONGER-RANGE SUBJECTS.

PROFITABILITY.

FIRST OF ALL, THE OUTLOOK FOR 1979 IS OBVIOUSLY EXCELLENT, AND WHILE THE OUTLOOK FOR 1980 IS ALSO GOOD ALL OF THIS MUST BE VIEWED AGAINST THE BACKGROUND OF GENERAL AND INCREASING DISSARRAY IN THE U.S. ECONOMY AND IN THAT OF MOST OF THE REST OF THE WORLD AS WELL. THE DEGREE OF UNCERTAINTY ABOUT WHAT SIMULTANEOUSLY HIGH INTEREST, TIGHT MONEY AND INFLATION WILL MEAN TO OUR BUSINESS IS VERY GREAT. AS YOU WILL RECALL FROM THE PRESENTATION IN SEPTEMBER, OUR PLANS FOR 1980 ARE AGGRESSIVELY STRETCHED AND, IN THAT SENSE, THERE IS A GREATER RISK OF SHORTFALL FROM BUDGET THAN ANY OF THE PLANS PRESENTED IN RECENT YEARS. I STRONGLY BELIEVE THAT THAT IS THE RIGHT THING TO DO -- AND THAT WE ARE DOING THE RIGHT THINGS, BUT IT IS IMPORTANT TO GO FORWARD WITH OUR EYES OPEN.
MOREOVER, BENEATH THE ROSY NUMBERS WE HAVE JUST SEEN, THERE ARE SIGNS OF PROBLEMS. TAKE ASSETS. WHILE FOR YEAR-TO-DATE WE ARE STILL INCREASING ASSET EFFICIENCY -- I.E. ATTAINING A 20 PERCENT INCREASE IN REVENUE WITH A 15 PERCENT INCREASE IN ASSETS, THIS IS NOT AS ROBUST AS THE 21 PERCENT INCREASE IN REVENUE ON A 12 PERCENT INCREASE IN ASSETS THAT I REPORTED FOR THE FIRST SIX MONTHS OF THIS YEAR.

I MENTIONED A MOMENT AGO THAT ADMINISTRATIVE EXPENSE IS RISING AT THE SAME RATE OF REVENUE. THE LACK OF PRODUCTIVITY IMPROVEMENT IN THIS AREA IS FRUSTRATING. IT IS A VEXING PROBLEM THAT HAS NOT YIELDED IN THE WAY I WANTED TO VARIOUS PROGRAMS OVER THE PAST FEW YEARS. WHILE AS A PERCENT OF REVENUE ADMINISTRATIVE EXPENSE HAS DECLINED -- FROM 1977 7.1, TO 1979 5.7 -- AND WILL BE BUDGETED AT 5.3 NEXT YEAR, THE BEST THAT CAN BE SAID IS THAT PROGRESS IS GLACIALLY SLOW AND, AS NOTED, ALL BUT AT A STANDSTILL AT THE MOMENT. SIMULTANEOUSLY, REVENUE PER EMPLOYEE IS NOT GROWING AS IT HAS. THE AVERAGE WILL BE $45,800 COMPARED TO $45,000 IN 1978.

THese things are reflected in our debt profile where in the last few months short-term bank borrowings have gone from zero to some $25 million at the end of October. Suffice to say that while a few months of negative cash flow is no big deal it sure couldn't have occurred at a less favorable time in terms of cost.
LOOKING AHEAD, I EXPECT THE 1980 BUDGETS TO SHOW FURTHER IMPROVEMENT IN DEBT TO EQUITY, RETURN ON INVESTED CAPITAL AND SO ON EVEN THOUGH THERE WILL BE A NEGATIVE CASH FLOW IN TOTAL FOR THE YEAR -- JUST AS THERE HAS BEEN THIS YEAR. AFTER BUILDING UP IN THE SECOND HALF OF THIS YEAR AND EARLY NEXT YEAR, WE WILL HAVE ACHIEVED A CAPACITY LEVEL WHICH WILL SUPPORT A LARGER BUSINESS. SO THE IMPROVEMENT IN PROFITABILITY ASSUMES A VOLUME INCREASE WHICH STILL HAS TO BE MADE TO HAPPEN.

TO SUMMARIZE -- THE THINGS WE HAVE TO DO TO CONTINUE THE IMPROVEMENT IN PROFITABILITY ARE JUST PLAIN HARDER THAN THE THINGS WE DID TWO, THREE AND FOUR YEARS AGO THAT ARE YIELDING THIS YEAR'S IMPROVEMENT. CONTINUED PROGRESS IN PERIPHERALS, FOR EXAMPLE, WILL REQUIRE LARGE INVESTMENTS IN TIME AND MONEY IN MORE AUTOMATED MANUFACTURING.

WE HAVE A FEW BUSINESSES THAT ARE OF DOUBTFUL LONG-RANGE STRATEGIC IMPORTANCE. WE WILL BE TALKING ABOUT BUSINESS FORMS LATER THIS MORNING. WE ARE WORKING ON A PLAN FOR ELECTROFACT AND A SMALL COMPANY WITH WHICH IT WOULD FIT. IT WILL STILL BE A MONTH OR SO BEFORE WE KNOW IF THIS WILL WORK.

MARKETING PRODUCTIVITY IN THE LONG RUN MEANS INVESTMENT NOW IN NEW DISTRIBUTION CHANNELS SUCH AS THE VARIOUS KINDS OF BUSINESS CENTERS FOR SELLING TO SMALL BUSINESS.
FURTHER IMPROVEMENT IN USE OF WORKING CAPITAL -- MOST NOTABLY IMPROVING RECEIVABLES COLLECTIONS AND INVENTORY MANAGEMENT -- CAN ONLY BE ACHIEVED BY MAKING THE INVESTMENT IN NEW INFORMATION SYSTEMS. AND SO ON.

IN BRIEF, THEN, WHEREAS IMPROVEMENT OVER THE PAST FIVE YEARS HAS COME FROM "CLEANING UP OUR ACT" SO TO SPEAK, FOR THE NEXT FIVE YEARS IT WILL COME FROM INVESTING IN NEW METHODS -- AND THAT CLEARLY IS COSTLIER, MORE TIME CONSUMING AND JUST PLAIN HARDER.

SEMI CONDUCTOR TECHNOLOGY

A SECOND LONGER-RANGE SUBJECT HAS TO DO WITH THE FUTURE OUTLOOK FOR SEMI-CONDUCTOR TECHNOLOGY -- SPECIFICALLY OUR ACCESS TO THE VERY LARGE-SCALE INTEGRATED CIRCUITS NECESSARY TO CONTINUE PRICE/PERFORMANCE PROGRESS.

FIRST OF ALL, THE COST OF GOING FORWARD IS ENORMOUS. NOT ONLY IS IT BEYOND THE RESOURCES OF CONTROL DATA IT IS BEYOND THE RESOURCES OF ALMOST EVERYONE. THERE ARE EXCEPTIONS: IBM, JAPAN INC. AND TI. IBM MADE IT CLEAR IN THEIR NEW COMPUTER ANNOUNCEMENT EARLIER THIS YEAR JUST HOW FAR THEY HAVE WIDENED THE GAP BETWEEN THEIR TECHNOLOGY AND THE REST OF THE INDUSTRY. IN FACT, FRANK CARY RECENTLY OPINED AT A DINNER PARTY THAT THERE COULD WELL BE NEW CASUALTIES IN THE COMPUTER FIELD IN THE COMING YEARS. (HE EXCLUDED CONTROL DATA, BY THE WAY.)
THE INCREASED COSTS ARE TO COVER THE WHOLE SPECTRUM OF ACTIVITY. IN RESEARCH, THE LABORATORY EQUIPMENT INVESTMENT IS BEYOND WHAT MOST UNIVERSITIES -- OR COMPANIES OUTSIDE IBM AND TI -- CAN AFFORD. AUTOMATED PRODUCTION FACILITIES ARE EVEN MORE EXPENSIVE. AND MOST CRITICALLY -- THE SIMULATION AND AUTOMATED DESIGN TOOLS NECESSARY FOR THE DESIGN ENGINEER TO WORK EFFICIENTLY WITH LSI WILL BE AN ENORMOUS ONGOING DEVELOPMENT EFFORT AND EXPENSE.

SO IT IS CLEAR THAT COOPERATION IS THE ONLY ANSWER. AND, WITH THIS IN MIND, WE HAVE STARTED DISCUSSIONS WITH SEVERAL ORGANIZATIONS INCLUDING HONEYWELL, MOTOROLA AND THE UNIVERSITY OF MINNESOTA ON VARIOUS POSSIBLE FORMS OF COOPERATION. WITH THE UNIVERSITY WE ARE HELPING THEM PUT TOGETHER A PROPOSAL TO NSF FOR A LARGE REGIONAL RESEARCH FACILITY THAT WOULD BE SUPPORTED BY INDUSTRY, THE NSF AND INVOLVE OTHER UNIVERSITIES -- WE HAVE TALKED TO THE UNIVERSITY OF MICHIGAN -- AS WELL. ALTHOUGH THERE IS MUCH WORK TO BE DONE TO MAKE THIS A REALITY, WE WILL PROBABLY ANNOUNCE A SIZEABLE GIFT -- $2 MILLION OR MORE -- TO THE UNIVERSITY OF MINNESOTA RESEARCH FOUNDATION BEFORE YEAR END.

WITH HONEYWELL, WE ARE PROPOSING A JOINT COMPANY DEVOTED TO THE DEVELOPMENT AND OPERATION OF LSI DESIGN TOOLS AND SERVICES. AS USUAL, WE ARE MORE OR LESS DRAGGING THEM KICKING AND SCREAMING...
INTO A BENEFICIAL UNDERTAKING. IT IS HARD WORK AND AT THIS POINT THE OUTCOME IS MOST UNCERTAIN, BUT WE'LL BE GLAD AFTERWARD IF WE CAN CONVINCE THEM.

WE HAVE A SMALL, TWO-MAN PROJECT WITH MOTOROLA AND WILL BE PROPOSING THAT THEY SUPPORT THE MINNESOTA RESEARCH INSTITUTE AND PERHAPS JOIN US IN THE HONEYWELL VENTURE AS WELL.

ALL THIS IS JUST BEGINNING AND I WILL REPORT TO YOU AT FUTURE MEETINGS AS THINGS DEVELOP. MEANWHILE, I WOULD BE GLAD TO DISCUSS IT WITH ANY OF YOU INDIVIDUALLY AND WOULD APPRECIATE ANY COMMENTS OR SUGGESTIONS.

CDBAI

FINALLY, LET ME CLOSE ON A DIFFERENT NOTE -- THE FORMATION OF A NEW BUSINESS IN CONTROL DATA. CONTROL DATA BUSINESS ADVISORS, INC., WILL OPERATE AS AN INDEPENDENT CONSULTING ORGANIZATION REPORTING TO ITS OWN BOARD OF DIRECTORS. IT WILL UTILIZE CONTROL DATA SERVICES AND PERSONNEL AND SPECIAL EXPERTISE AS NEEDED. CDBAI WILL SPECIALIZE IN SERVING SMALL BUSINESS, AN AREA NOT EFFECTIVELY SERVED BY EXISTING MANAGEMENT CONSULTING COMPANIES. THE RESOURCES OF CDBAI WILL ALSO BE AVAILABLE TO DO INTERNAL CONSULTING. SEVERAL KEY STAFF APPOINTMENTS HAVE ALREADY BEEN MADE TO PROVIDE CDBAI WITH A BROAD RANGE OF FUNCTIONAL MANAGEMENT DISCIPLINES, AND IT WILL BE DEVELOPING
NEW AND UNIQUE TECHNIQUES TO DELIVER COST-EFFECTIVE EXPERTISE TO THE GROWING SMALL BUSINESS MARKET AS A PROFIT MAKING MANAGEMENT CONSULTING FIRM.

SECONDLY, IT IS AN EFFECTIVE VEHICLE FOR KEY MANAGEMENT PERSONNEL TO BROADEN THEIR PROBLEM SOLVING CAPABILITY BY EXPERIENCE OF A DIVERSE RANGE OF PRACTICAL BUSINESS PROBLEMS. THE CONSULTING ORGANIZATION WILL PROVIDE THOSE CHALLENGES IN A UNIQUE BUSINESS ENVIRONMENT.

I CAN'T RECALL A NEW PROJECT IN CONTROL DATA WHICH HAS BEEN GREETED WITH MORE INTEREST AND ENTHUSIASM. PETER BAILEY HAS BEEN SELECTED TO BE THE FIRST PRESIDENT OF CDBAI AND I AM CONFIDENT HE WILL DO AN EXCELLENT JOB.

CONCLUSION
FINALLY, LET ME SAY THAT 1979 HAS BEEN AN EXCELLENT YEAR. OUR PROGRESS HAS CERTAINLY EXCEEDED THE EXPECTATIONS I HAD THIS TIME LAST YEAR. THERE IS JUST NO QUESTION THAT IN 1980 IT WILL BE HARDER TO SUSTAIN OUR PROGRESS BUT WE WILL BE WORKING AT IT.

THANK YOU.

QUESTIONS?