I.  INTRODUCTION

Good evening. It's a pleasure to be with you. I recall very well my first meeting with Cybernet.

[September 1969 - recall]

But I'm not here to reminisce -- this is a time to look ahead. So let's do that.

II.  CORPORATE POSITION & OUTLOOK

Control Data, whatever our problems might be, is a fascinating company. I know -- and I'm glad -- that you've been so focused on Cybernet and your problems and opportunities, there is not much time left over for knowing about the opportunities much less the problems of your colleagues in other groups. So, I'll talk about that for a bit before we get down to the business at hand for you.
First of all, as I said in my letter to employees back in December, in the somewhat gloomy light cast over us all by our collective financial performance in 1984, it's difficult for many people to see the strengths we have and the significant steps we have taken to get us back on track. Not the least of those strengths is to face up to problems and fix them -- whether they happen to be in the category of strategy, products, processes, or people. Strategy decisions, by the way, are far and away the most painful -- they involve the most dislocation and affect everything else -- employees, products and customers. The decision with regard to "plugs" for example or with regard to the financial services business -- Commercial Credit. Fixing people problems probably requires the most skill. Control Data, believe me, is in a league far above most.

The thing that seems to be hardest for us is "process. Although you are probably not as affected by shortcomings in that regard as many other groups, it is a problem demanding attention by all of us. In my Direction '85 remarks, I dwell on that at some length. Basically, it is a matter of quality -- a quality result in everything we do. Anyway, I'll leave my comments in that regard for you to hear on the tape.
I mentioned Commercial Credit so let me cover that part of the business first. First of all, having started two years ago in their part of the business to get at this question of process -- of effective operation -- Commercial Credit made great progress in 1984 in improving their performance -- by far the best of any of the four businesses -- i.e. Systems, Peripherals, Services, and Financial Services. And 1985 looks even better for them.

The decision to offer Commercial Credit for sale is a matter of strategy, not of operating problems. We have dug into the critical corporate strategic issues over the past two years using teams of top executives and in some cases outside consultants. In both 1983 and 1984, various parts of Commercial Credit were among the strategic issues being studied. In a somewhat oversimplified way, this is what it comes down to:

**CDC:** good at applying microelectronics and computer technology

**CCC:** finance for business, finance for consumers (banking), insurance -- some of both

Investment in non-synergetic businesses

**Options:**

(1) do nothing
(2) retrench
(3) sell it all.
Emphasize it is not absolutely necessary to sell CCC. It is necessary to free management and financial resources to invest in parts of the business with greater potential -- e.g. Peripherals. Management -- L. Perlman plus seven other key staff and line executives -- were assigned to CCC in 1982-83 to address the problems. That's a lot of resource, almost all of which will be freed to attack other problems.

And as you know from recent announcements, some of that has already happened.

**SYSTEMS**

Computer Systems is where it all started in Control Data. Although the scientific and engineering segment of the commercial market is and has been our particular niche, special purpose military computers have also always played an important role. This latter business has experienced particularly solid growth in the last year. It will have record revenue and profits this year. And the outlook for 1985 is more of the same. We have an excellent mix of long term production programs and advanced technology development contracts. That's what you need in the military business. The two major production programs are the standard airborne computer for the Navy, called the AYK-14, and an on-board ballistic computer system for the M1 tank. Both are yielding good results. The Navy has also given us a product improvement contract that will extend production life of the AYK-14 well into the 1990s, and production on the tank program is also expected to continue through that period.
On the more familiar side of the computer mainframe business, let me talk about super computers. Applications for this high performance segment of the mainframe business are increasing rapidly as a result compared to a limp growth rate of zero to 15 percent over the past ten years in terms of numbers of units. The market will grow by a factor of five between now and 1990. One important rising application area is computer-aided engineering design, especially advanced electronic circuit design.

The successor machine to the 205 is, of course, being designed by ETA Systems. There continues to be speculation that because ETA is designing super computers Control Data is no longer in the business. That's about the same as saying that because MPI builds peripherals Control Data is out of the OEM business.

In order to get ETA started, the architecture, VLSI technology, and software that Control Data had been developing were transferred to them. So the technology today flows from Control Data to ETA. Later on, of course, the flow will reverse.
One of the major benefits of super computer development at Control Data over the years has been the ultimate flow of technology from those developments to the main computer product line. Through cross-licensing arrangements with ETA, we will continue to enjoy such benefits while fostering the very special environment needed for super computer development. Ultimately, the beneficiaries of ETA will be all of Control Data's customers, present and future, from super computers on down.

Control Data's newest computer product family -- the 180/800 -- introduced last year -- is enjoying good marketplace acceptance. In total, some 280 systems were shipped in 1984 -- approximately 28 percent more than the number of units shipped in 1983.

I should add that although we shipped about 28 percent more in terms of units, revenues actually remained the same. Perhaps you can guess that the price erosion implicit in that statement is very closely related to the transformation/restructuring going on in the data services marketplace.

The absolute key risk factor in Systems is the size of the technical investment required. For Peripherals in total, that investment is 7.2 percent of revenue. For Services, it's 11 to 14 percent. But in Systems, nearly one-fourth of every revenue dollar must be spent for technical effort -- that, then, is two or even three times as much as some of our other businesses.
Secondly, as opposed to the significant market share many of our services or the OEM business enjoy, Systems must deal in a competitive world where they have a share of one to two percent -- or roughly ten times less. In broad terms, then, it takes twice the technical investment for one-tenth the market share. So when we talk about the need to seek special market niches in Systems, you know that is not just idle talk. And when we talk about the favored position from a strategic basics point of view Services enjoy, it isn't just some blue sky wishful thinking.

PERIPHERALS

Anyway, I mentioned Peripherals a moment ago regarding technical effort. Let me turn to that part of the business. As you look back at Control Data's history, it is clear that one of the key factors in our growth and success was the development of the OEM peripherals business and like many such things -- it was pure serendipity. No one envisioned a billion-and-a-half-dollar business back there at the beginning. Really, when you get down to it, it was just plain common sense that started us in OEM. Control Data needed high performance peripherals for high performance computers. Those peripherals were hard to come by and they were very expensive.
On the other hand, Control Data, as a $40 million a year company, wasn't exactly a huge customer for the products either -- much less could it justify the R&D investment. So selling OEM -- the computer folks said you mean "selling to our competitors?" -- was, as I say, a common sense way of attacking the problem.

But what we got was a source of stability -- another leg, if you will, in the stool to support the business and its ever lasting struggle in the face of IBM's dominance.

So OEM and the peripherals business in total rapidly became and is today an integral part of our strategy. There is no doubt that as we have moved in the last year or two into the new technologies of the XMD, FSD, and WREN, the underlying weaknesses were exposed of a peripherals organization ill-prepared to be a billion dollar company, much less one capable of producing the yields and therefore costs essential to competing in that higher technology/performance arena. Creativity and market response never have been lacking in Peripherals. Operations is another story.

We are fixing that. We have been fixing that. It isn't going to get done in a day or even a year. But it is going to improve a lot this year.
COMPUTER SERVICES

By the middle-sixties, our strategic limitations due to IBM's dominance on the computer systems business were clear. And so if we wanted to have over the long term a true value-added business in which market and applications knowledge could be combined with basic computer and peripheral products technology, then we should move into services. This was done and it was a time consuming and expensive long term move, but by the mid-seventies, Computer Services was a relatively mature and solid business.

During the last half of the 70s, rapid growth in revenues and profitability in services continued. As opposed to the previous ten years, however, there was little in the way of brand new services start ups other than CBE.

Although by 1981 some more serious looks at renewed investment in Services began to be taken, by that time the wave of distributed computing had hit and the basic network services found themselves behind the power curve, even though the full force of that wave didn't hit until 1983 and 1984. Now through all this, large parts of the Services business -- in particular the industry/application specific services such as Arbitron and Ticketron -- continued their steady growth.
Meanwhile, new market focused groups, such as Healthcare Services, the CIM division, and Small Business Services, have made good progress during 1984. In 1985 and 1986, these businesses should grow significantly in size as well as profitability.

Just as in hardware businesses -- although with longer time cycles -- the Services business must prepare for the next wave of technology. We were slow in doing this with regard to distributed computing. Excess negativism in that regard is, however, misplaced. Looking ahead, one critical strategic issue in the technical area is to prepare to utilize to advantage artificial intelligence technology and the special subset of that technology known as expert systems.

Computer Services, in many people's minds, is equated to one special niche of that business known as time-sharing. Time-sharing did not amount to more than 20 percent of Control Data's total Computer Services revenues. Most of it, of course, was in SBC/NIS. This portion of the business was the most vulnerable to the individual personal computer -- in particular where the time-sharing application amounted to essentially a spread sheet calculation. But contrary to what most people would guess, this is still a significant source of revenue. Better things may be available technologically but customers change slowly -- especially if you have creative sales people!
II. ORGANIZATION

I know from talking to Greg, Chuck Nies, and Bob Nierman, both before the fact and afterward, that the organization changes we announced last August were difficult for many people in USM. You just don't change something as firmly established as USM without causing a good bit of turmoil. Perhaps first of all there may be some small comfort in knowing that there have been changes equally as dramatic in years gone by.

[Go back over OEM, Cybernet, GSM, International changes.]

So don't go around feeling like you've been singled out by history. But the important thing is not that. It is that the overriding need in the systems and network services parts of Control Data's mainstream business was to make them marketing oriented operations -- not just "market focused" -- a term which is somewhat overworked in Control Data these days -- but market driven. And no place was this more true than in Cybernet. In the competition for management attention and focus, the changing needs of the network services market place were not receiving adequate priority -- from about 1980 onward. The results didn't really surface until three years later or so -- but surface they did.
Of all the sales people involved in that change, the ones of you who chose or "were chosen" for Cybernet are the most fortunate. I'm not joking. I know there's been some feeling around -- "how do I get out of this c-s outfit?!" -- that's not only wrong -- it's not very smart. Why?

III. CYBERNET

Let's look at fundamentals.


(2) Competitive basics. Cover UIS. Others, UCC, Boeing, Computer Sciences, McAuto.

(3) Product strategy. That's where we fell down. Why? Because we were not responsive to the basic change going on in the market place. Workstations -- absolutely -- but more. Cost of systems went through another cycle where dedicated application mainframes have become economically viable.

But you have it altogether -- you can do whatever you want to do. Seriously. Well, maybe if you ask for one-half billion dollars, I might be hard pressed. But I believe in you and in the opportunities we have in Services. You know, I suggested to Rick and Harold we might think about changing the name "Cybernet." I like that name -- always have -- but the reason I said that was if it causes us to look back instead of forward, then to hell with it.

[1970 organization change story]
Greg told me a while back that all my theorizing was great but he had a few more day-to-day pragmatic problems. Like people having reasonable, realistic opportunities for compensation and incentive earnings in a time of transition. That's a combination of new and better product/service strategies and a realistic market place appraisal. Although the past two years have been painful, it seems to me we have done that and 1985 is a year to go out and make it all happen.

IV. CLOSE

In my Direction '85 remarks, I discuss "Services" in terms of the challenge facing them in 1985.

[Go over 4 categories, Cybernet, statement "I believe in you," "Control Data believes in you"]

You have opportunity few others have in Control Data. I have been there where you are -- where those around you -- who don't understand or believe in your future -- far outnumber those who do. Bill Norris took me to financial analyst meetings for seven years. Two, three, four, even five times a year I explained over and over what we were doing. It was like talking to the mountain. The proof was in the doing. It always was and it always will be. So do it. There isn't any reason you can't!

Thank you.