Is Control Data in Trouble?

The rumor mills have it that fast-stepping Control Data has hit the skids; its stock dropped by 60%. Here's what the company says about the pessimistic reports.

It was only eight years ago that a small group of discontented Univac men, headed by William C. Norris and with a bankroll of $600,000, left Sperry Rand to form Control Data Corp.* It shrewdly stuck to highly sophisticated scientific computers rather than mixing in the general business computer market dominated by International Business Machines. Thus did little CDC succeed spectacularly while far richer outfits like RCA, General Electric and Honeywell continued to lose money or barely break even. Control Data is still the only company besides IBM ever to show a computer profit. It netted 5% on revenues, 11% on equity last year. Since 1957 its revenues have shot from $625,000 to $160 million, its profit from a 4-cent deficit to $1.06 per share.

Late last year, though, unpleasant rumors began to fly that relatively small CDC might be getting in over its head. It was getting deeper into the business computer field to keep up its growth rather than sticking to the science field. It was cutting prices. It was trying to digest no less than 14 acquisitions in 25 months in a crash effort to broaden its somewhat limited product line.

What's more, its customers were starting to prefer leases to outright purchases. Since leases require far more capital, CDC might be spread too thin to raise the necessary cash. Finally, some company officers (including Chairman and President Norris himself) and mutual funds were unloading CDC shares, which plunged a sickening 60%—from 75 to 30—between mid-1964 and this summer.

Last month, CDC reported for the year ended June 30, 1965. Revenues were up from $131 million to $160 million. But profits—after taking away some 46 cents a share gained from changing its depreciation policy and its manner of writing off costs of leased equipment—had fallen from 84 cents to 60 cents a share, the first drop in eight years.

To get Control Data's side of the story, late last month FORBES' Associate Editor Stephen Quickel flew to Minneapolis to interview Norris. Below are highlights of the interview:

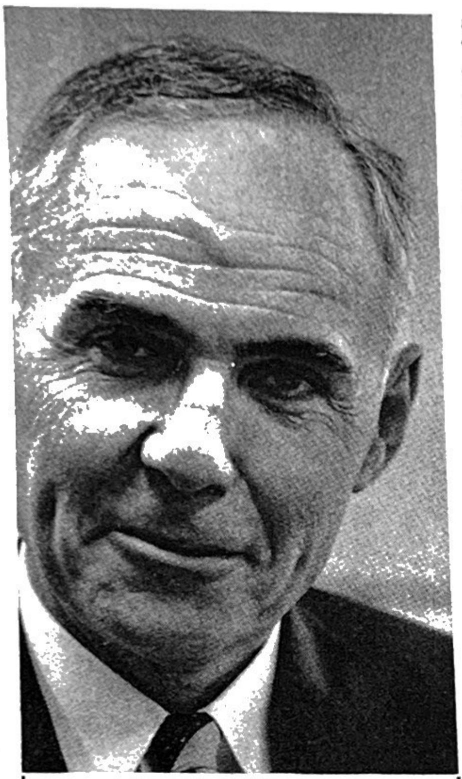
"Naturally competition has increased for us as we have grown," Norris began. "It's not because we've changed our orientation. It's just that the computers we make are penetrating more into the business world.

"This is not a simple overlapping of functions. Rather, it is a matter of business data processing becoming more scientific, if you will. The emphasis is shifting from record-keeping computers to ones that can be used in the science of management."

• *Did increased competition cause the drop in earnings?*

"The major factor," Norris replied somewhat indirectly, "was that customers more or less suddenly shifted from outright purchases of equipment to leasing." Since lease income is spread over several years, the profit is spread, too, instead of coming in one fell swoop. A few years ago, CDC got over 90% of its revenues from direct sales; now the percentage is down to about 80%.

Norris does, however, attribute the shift toward leasing to the stepped-up competition, especially IBM's new 360 which was announced more than a year before the first deliveries. "This created uncertainty among customers. With all the new models and changes, they want to avoid locking themselves in."



CDC's Norris *declines to predict 1965-66 results. Says he: "If a couple of buyers suddenly decide to lease, bang, there go your predictions right out the window."*

• *Why shift to less conservative accounting procedures at a time when competition is getting stiffer?*

Norris argued that the much-criticized accounting changes were dictated by the shift in the sales-lease mix. "We wanted to get rid of the wide fluctuations in earnings due to shifting from sales to lease." Under a lease, income is received over a period of time, not all at once as in a sale. By spacing out depreciation and expense write-offs, he explained, the company evened out some of the effects of the trend toward leasing.

"An accounting system should reflect the true condition of a business at a given point in time. In the early stages of this company we deemed it best to adopt a very conservative accounting system. We wanted to avoid an overstatement of earnings that might be dangerous to us and misleading to the public. It was good accounting not to take any chances. Now today, it would be just as wrong *not* to shift from the overly conservative system."

Norris said that in depreciation CDC is still fairly conservative. It

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*Control Data Corp. Traded NYSE.
Recent price: 36. 1965 Range: 64¼–30¼.
Dividend (fiscal 1965): none. Ind. fiscal 1966: none.
Earnings per share (fiscal 1965): $1.05.
Common shares: 7,331,000.
Total assets: $208 million.
Ticker symbol: CDA.