YOU'RE ONE PAGE AWAY

from the NO-HOLDS-BARRED STORY

of ONE YEAR

in THE LIFE OF A COMPANY.

It's the story of

BIG BATTLES, STINGING DEFEATS & GRITTY COMEBACKS.

UNEXPECTED ALLIANCES, DARING FORAYS & GAME-CHANGING DISCOVERIES.

In many ways,
IT'S A STORY ABOUT THE FUTURE,
AS WELL AS THE RECENT PAST,
AND ABOUT ALL BUSINESS TODAY.
WHICH MEANS IT'S ABOUT E-BUSINESS.
AND ONE IN PARTICULAR.

ANNUAL REPORT 2000

THE STORY OF IBM is really many stories.

We're opening up new markets and extending our lead in others. We're fighting back in businesses we pioneered and changing ourselves in some fundamental ways. Last year, we absorbed our share of hits, too. But we won more than we lost. And closed the year on a high note.

All the while, we've kept working, inventing and partnering to write the next chapter of the story we started five years ago. The story of e-business.

So, while this year's report is not a simple narrative, it does yield one singular theme. It's ultimately the story of hundreds of thousands of people tackling scores of the toughest business and technological challenges over 12 intensely challenging months.

It's one story we're proud to tell.

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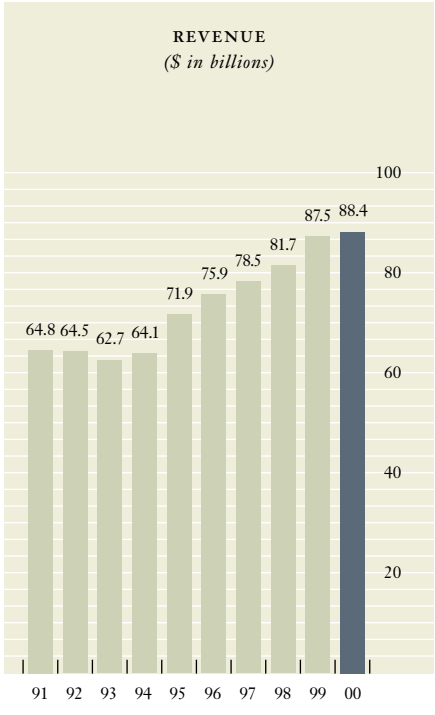
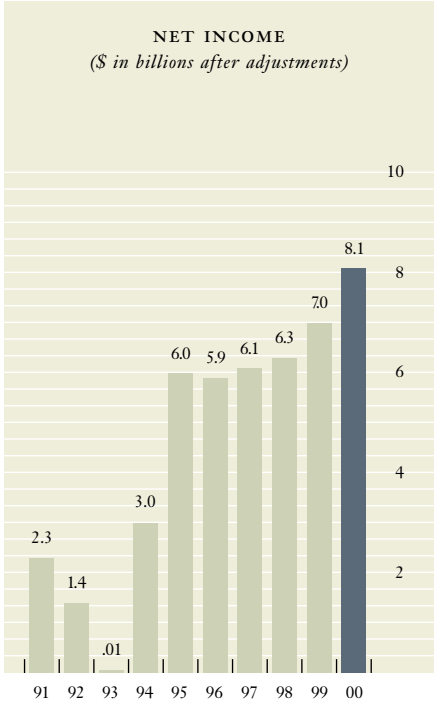
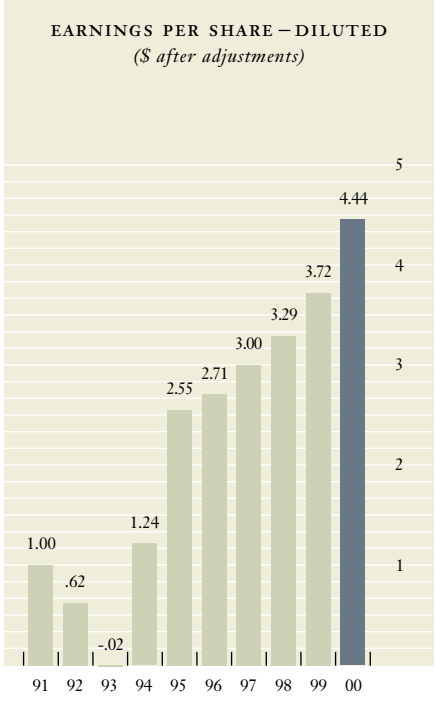
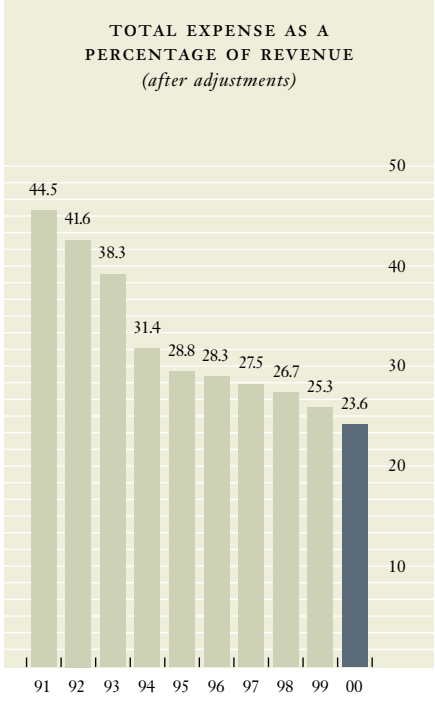

REVENUE
($ in billions)
64.8
64.5
62.7
64.1
71.9
75.9
78.5
81.7
87.5
88.4
100
80
60
40
20
91 92 93 94 95 96 97 98 99 00


NET INCOME
($ in billions after adjustments)
2.3
1.4
.01
3.0
6.0
5.9
6.1
6.3
7.0
8.1
10
8
6
4
2
91 92 93 94 95 96 97 98 99 00


EARNINGS PER SHARE—DILUTED
($ after adjustments)
1.00
.62
-.02
1.24
2.55
2.71
3.00
3.29
3.72
4.44
5
4
3
2
1
91 92 93 94 95 96 97 98 99 00


TOTAL EXPENSE AS A
PERCENTAGE OF REVENUE
(after adjustments)
44.5
41.6
38.3
31.4
28.8
28.3
27.5
26.7
25.3
23.6
50
40
30
20
10
91 92 93 94 95 96 97 98 99 00

DEAR FELLOW INVESTOR,

Last year at this time, I said 2000 looked to be a year of great promise for IBM—as well as a year of great uncertainty. I said that, based on the way things were playing out in our

industry—and in business in general—and because IBM, more perhaps than any other company in information technology, was vulnerable to customer wariness over "Y2K problems."

It turned out that last year was, in a word, unique. As you may remember, our company entered the year facing a severe drop-off in customer demand because of Y2K. Many of our largest customers had frozen big-ticket technology purchases heading into the new millennium, and that persisted until almost the middle of 2000.

Then, in a flip-flop the likes of which I have never seen, demand went through the roof. Within a 30-day period last summer, orders for some of our products tripled. We couldn't build fast enough to fill orders and, to make matters worse, we had shortages of some key components. Thanks to the determined, round-the-clock work of literally hundreds of thousands of IBMers, we got supply and demand into better balance in the final quarter of the year, and we finished strong. But, I don't need to describe to you the frustration of not being able to satisfy customer demand, particularly in view of the drought we had endured. I am determined that's not going to happen again.

But, add it all up—the highs, lows and sideways moves of 2000—and IBM had a solid year. For the sixth straight year we reported record revenue—$88.4 billion. Our earnings rose to $8.1 billion, a 16 percent increase, resulting in another record in earnings per diluted common share. After making substantial investments—$5.6 billion in research and development, $5.6 billion in capital expenditures and more than $500 million in strategic acquisitions that strengthened our business portfolio—we had enough cash to increase our dividend to shareholders and to buy back $6.7 billion of common shares.

The most disappointing note was that our year-to-year stock price went down for the first time since I joined the company—to $85 from $108, a decline of 21 percent. Of course, just about all information technology stocks dropped, in what might be called a NASDAQ crash, and IBM fared better than most. Also, over the past eight years IBM's share price has increased nearly 800 percent. Even so, we can do better.

What about 2001? Can the recent trend continue? Whether or not there is a softening of the U.S. economy, IBM should be in reasonably good

LOUIS V. GERSTNER, JR.
Chairman of the Board and
Chief Executive Officer

JOHN M. THOMPSON
Vice Chairman of the Board

SAMUEL J. PALMISANO
President and
Chief Operating Officer

competitive shape. Of course, we all hope such a downturn doesn't occur. But if it does, the ebbing tide may not beach all boats. For one thing, services offerings like outsourcing and hosting are cost-saving propositions for our customers. Services, in this regard, is a countercyclical business. And in a tightening economic environment, customers are going to invest in projects that deliver rock-solid, tangible, near-term payoffs, not in speculative, exploratory schemes. As a result, this may be a prime opportunity for IBM to improve its market position.

THE DOT-COM CRASH: WHAT IT MEANS

That's not the way things seemed a year ago. Back then, it looked as though Internet start-ups were taking over and traditional bricks-and-mortar enterprises had better jump with both feet into "e-tailing" or get steamrolled.

Well, as we all know today, it didn't happen. The crash brought out the usual pundits and weathervanes—the same ones who a year earlier had declared that dot-coms were taking over the world. Only now they were saying, "This e-business was mostly hype anyway. E-nough!"

Since, in many ways, IBM gave birth to all things "e" five years ago, I'd like to offer a perspective.

The collapse of the dot-coms was not a failure of e-business. It was the failure of an overly narrow approach to e-business. For all the proclamations we have been hearing about a "new economy," the problem with most dot-coms was that their business model—win customers through lower prices—wasn't anything new, not to mention transformative.

IBM has always said that e-business involves more than transforming one part of a company, such as selling directly over the Net. We said the real action, the real work—and the ultimate payoff—involved the transformation and the integration of the *entire enterprise*, from the customer all the way through the supply chain. Things have played out pretty much that way—and that may have been a bucket of cold water for some. For IBM, it was a tough but ultimately heartening reaffirmation of the strategic direction we set in place several years ago.

So, if there is a lesson to be extracted from the dot-com crash, it may be this: There is no short-cut to e-business. And if 2000 comes to be seen as a watershed (and I think it will), that will be because this was the year the world's established enterprises awoke to the true possibilities of e-business. I believe a broad consensus has emerged that e-business is just…business, real business. And real business is serious work.

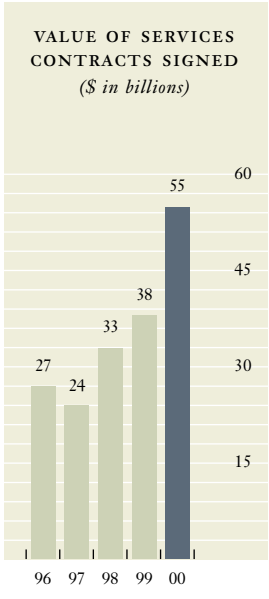
THE GAME TODAY

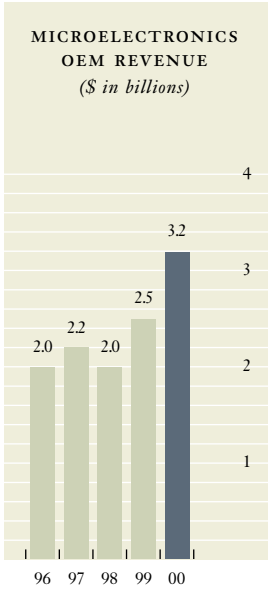
One word you heard a lot last year was "buzz." It's what the cooler members of our industry were supposed to create to get all their constituencies excited about what they were doing. Unfortunately for them, this isn't a very buzz-y period for our industry. In fact, it's downright boring, but oh so important for the future.

Customers tell us the battleground has shifted to computing infrastructure. Of course, IBM is no longer alone in saying that the PC era is over, nor in pointing to the explosion in personal access devices (as well as an even wider array of *things* with embedded intelligence, such as appliances and cars). Most of our competitors today are saying that enterprise servers, storage and software are key, and that they must be bulletproof, robust, scalable, never-go-down. But I'm not sure we all agree on what "infrastructure" actually means.

Businesses are coming to see that their computing infrastructure cannot be designed or built around any one product—or even any particular *type* of technology, whether databases, or servers, or storage. None of those tails can wag this entire dog. For one thing, the pieces all have to work with one another. For another, in order to function in the real world—where there is a hodgepodge of existing systems within any company and among its customers, suppliers and trading partners—they have to take a broad view of the full spectrum of infrastructure elements.

The point is, no company's systems are an island. They're part of a new, emerging, *global* infrastructure that is made possible by the emergence of the Internet, and that no one enterprise can—or wants to—own. It's *collectively* owned, accessed and relied upon by every business, government, school, hospital and neighborhood.





In that respect, computing infrastructure is rapidly becoming like all the other kinds of infrastructure we take for granted in the world—the telephone system, the highways, the power grid.

This has been a long time coming. The main obstacle has been a lack of standards in our industry. Simply put, without standards, computing systems cannot work with each other. And if your computer can't work with all the other computers in the world, then you're limited in how you can buy and sell, trade stock, book a vacation, receive health care and cast a vote over the Net. And in the same way, your company is limited in how it can work with its trading partners, its suppliers, its customers—and you.

The Internet, of course, began to change all that by bringing common standards to network connectivity. Now, the astounding adoption of the Linux operating system—and the broader Open Source movement of which it is a part—are pushing standards over the top (which is why IBM has made such a huge commitment to Linux). Standards are a reality of our industry today. There's no going back.

This is wonderful for customers and users of computing. But for many technology companies, it is an earthquake. No longer will the battle be won or lost over computing technology controlled by one company. Success going forward will require open platforms, and tech companies that rely on closed, proprietary technologies will dry up. In fact, some of the players riding high today may never, without major strategic adjustments, see their current growth rates again.

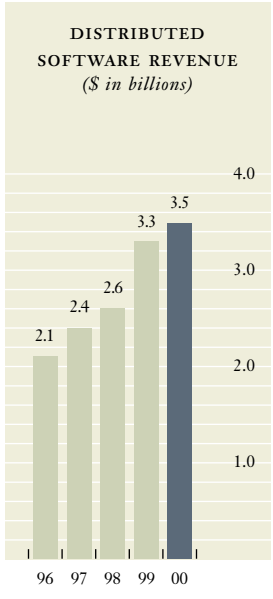
Now, some people assert that standards-based computing will commoditize information technology. And certainly, many are asking: Where will the value be? The profits? Who will set the agenda? What will matter most to customers?

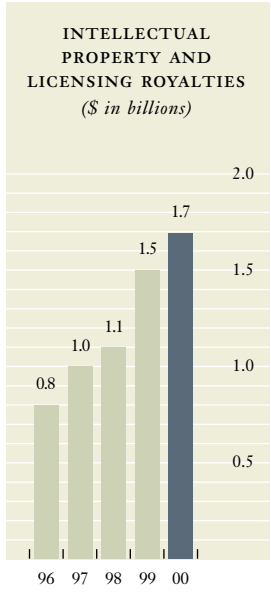
We ask ourselves these questions all the time. I think we can now see clearly that competitive advantage in the future will rest essentially on three things: technological innovation, the ability to help customers integrate technology with their business, and the capability to make information technology easy to acquire and manage.

Each of these capacities takes a long time to build, and the barriers to entry are daunting. These are not things you can simply buy your way into. Step back from the array of all the things IBM is and does today, and what you'll see is a company strengthening its position in these three fundamental areas.

1. Technology Innovation. Make no mistake. A world of standard computing technology increases, not decreases, the value and competitive advantage of innovation. And that requires real science. Not just software developers, but also quantum physicists. Not just storage specialists, but computational biologists. Not just people who move data, but people who move atoms—one at a time. We have all of that.

This ability to invent is IBM's ace in the hole. The scope and impact of what our researchers have invented in just the past eight years—during which they have continually set record after record in patents—is remarkable. We are in the midst of a Golden Age at IBM Research. Equally important is how rapidly we've moved those innovations into the marketplace. From silicon germanium to copper chips, from silicon-on-insulator to WebSphere,





from self-managing servers to microdrives—IBM's technology business has become a multibillion-dollar juggernaut.

That's important. If the first age of e-business was an age of supply—a seemingly endless abundance of Web sites, new businesses, new business models and capital—then the second age of e-business will be an age of *demand*. Before long, we'll see Internet traffic grow a thousandfold, propelled by, among other things, an explosion in the number of client and embedded networked devices that will reach into the trillions. That's a lot of bits and bytes that businesses are going to have to capture, manage, store, access, analyze and use. And no matter how much more efficient we make our current computing infrastructure, no matter how many more bright young people go into computer science, it won't be enough. We're going to need whole new levels of scientific and technological discovery, much of it aimed at creating *self-managing* e-business infrastructure. Who would you bet on to create and patent the lion's share?

2. Business Innovation. So, new technology is essential. But let me tell you, when I was a customer, I never turned to IBM because of a piece of technology; I took that for granted. Instead, I turned to IBM because they helped me apply all their amazing technology to my business. I valued IBM's *applied* intelligence, its ability to understand my problems and help fix them.

This capability will be even more important as e-business moves into the realm of serious business transformation. All of the decisions that customers need to make—technology decisions, product decisions and process decisions—derive from some much more basic, strategic choices. So the first thing a customer needs is a partner with a deep, experience-based understanding of their business, of business in general, of e-business in particular.

Of course, a "solution" isn't truly a solution unless your customer can implement it quickly and affordably. Business transformation doesn't mean much if you can't then enable applications and get the infrastructure in place. One of IBM's key competitive advantages is our experience in actually building and integrating e-business systems and e-business infrastructure for our customers (and for ourselves).

3. Managing Technology's Cost and Complexity. And then there's the question of how a company should acquire and manage information technology. This is not trivial, especially when you understand the vast, sophisticated computing infrastructure that will be required to support real e-business.

There's traditional purchase, of course. And outsourcing—where a partner like IBM Global Services takes on the operation of a customer's existing I/T systems and staff. IBM is already the world leader in strategic outsourcing, including more than 50 deals signed in 2000 that were valued at more than $100 million each. But now, we have bigger ideas about how to help our customers.

How about moving infrastructure out of the corporate data center, and onto the Net? Don't own it. Rent it as a service, on an as-needed, as-used basis. This is what we call "e-sourcing," and it will vastly increase companies' access to computing

power, expertise and innovation. IBM is already one of the world's largest hosting companies, with revenue that doubled in 2000. And we are working rapidly with telecom partners to build new IBM e-business hosting centers worldwide.

Finally, often overlooked in IBM's portfolio is a capability our customers and business partners value highly, because it makes e-business real and financially manageable. IBM Global Financing is the world's largest provider of I/T financing—a $4 billion business managing over $40 billion in assets.

UNDER THE HOOD

When you look at these industry trends, at our strategies and at what's happening "under the hood" within IBM, not only did our company have a good year in 2000, but prospects for 2001 are even better.

As I've reported here, not only is the marketplace ready for IBM, but we're ready for it. A whole lot of hard, disciplined work turning our strategic plans into reality is now coming to fruition. And in helping our customers build their computing infrastructure, we have the advantage of having a strong position in all its major parts—middleware, enterprise servers, component technology and enterprise storage. In every one of those fields, we've made major gains.

• In software, value continues to shift from the operating system to middleware, which links all kinds of servers and all the applications with every kind of client device. A few years ago, IBM set out to build a software business focused on middleware. It wasn't glamorous. We just quietly invested billions of dollars to create a set of open products that work with every industry-leading platform. And what's happening? Explosive growth. Our DB2 database revenue was up more than 70 percent on UNIX and Windows NT platforms in 2000. MQ Series messaging software was up more than 60 percent. And WebSphere, our e-commerce middleware, tripled year over year. Industry analysts estimate that the middleware market—already $77 billion today—is growing at a 14 percent annual clip.

• In servers, after years of investment and invention, we transformed our products from the inside out, integrating our offerings with common technologies, common chip architecture, a common development platform in Linux, interoperability with dozens of leading applications—and took them to market as the IBM eServer family. Customer reaction has been swift and enthusiastic.

• After deciding a couple of years ago to exit the enterprise application software business, we have put into place a powerful set of partnerships. In 2000, we established strategic alliances with 50 leading independent software companies, most of whom had previously been going to market mainly with some of our top competitors.

• In component technology, we are getting our innovations to market not just inside our own products, but inside the products of other high-tech companies. At the same time, we made a key shift from increasingly commoditized, general-purpose DRAM chips to high-end microprocessors for servers, chips for pervasive computing devices and chips for networking equipment. It's taken us time to build up our technology portfolio, but now we have it, and demand is white-hot. In the market for pervasive device chips alone, our revenue increased 80 percent last year. Revenue from networking infrastructure chips grew 137 percent.

• The list goes on. We reanimated our enterprise storage business with a product we call Shark; restructured our PC unit and returned it to profitability in the second half of the year; drove the growth of Linux inside and outside IBM; and staked out new ground in emerging markets, such as life sciences.

• Finally, there's services, which in many ways is our trump card. We provide consulting, implementation services, outsourcing and now e-sourcing, aimed at the heart of the hosting and service provider opportunity. After years of hard work, we've got the most capable services business in the world. In fact, IBM is now the largest business and technology consultancy. We have 50,000 consultants who billed more than $10 billion in revenue in 2000. We have

FINANCIAL HIGHLIGHTS—*International Business Machines Corporation and Subsidiary Companies*

ONE-YEAR PERFORMANCE

(dollars in millions except per share amounts)	*2000*	*1999*	*Percent Increase*	*Percent Increase Normalized*
FOR THE YEAR				
Revenue	$ 88,396	$ 87,548	1%	1%
Net income	$ 8,093	$ 7,712*	5%*	16%
Per share of common stock:				
Assuming dilution	$ 4.44	$ 4.12*	8%*	19%
Basic	$ 4.58	$ 4.25*	8%*	19%
Cash dividends paid on common stock	$ 909	$ 859	6%	6%
Per share of common stock	$ 0.51	$ 0.47	9%	9%
AT YEAR END				
Total assets	$ 88,349	$ 87,495	1%	1%
Total debt	$ 28,576	$ 28,354	1%	1%
Stockholders' equity	$ 20,624	$ 20,511	1%	1%

**Includes a net benefit from the 1999 sale of the IBM Global Network and other 1999 actions.*

SIX-YEAR PERFORMANCE

(dollars in millions except per share amounts)	*2000*	*1994*	*6-Year CAGR***
FOR THE YEAR			
Revenue	$ 88,396	$ 64,052	6%
Net income	$ 8,093	$ 3,021	18%
Per share of common stock:			
Assuming dilution	$ 4.44	$ 1.24	24%
Basic	$ 4.58	$ 1.26	24%
Cash dividends paid on common stock	$ 909	$ 585	8%
Per share of common stock	$ 0.51	$ 0.25	13%
AT YEAR END			
Total assets	$ 88,349	$ 81,091	1%
Total debt	$ 28,576	$ 22,118	4%
Stockholders' equity	$ 20,624	$ 23,413	-2%

*** Compound Annual Growth Rate*

created a network of Business Innovation Centers, offering customers everything from front-end Web design to the heavy lifting at the back end. And just as important, we have built a field force that includes thousands of experienced industry specialists—many of them former professionals in their respective domains, from manufacturing to consumer products, from health care to government.

* * *

When I look back on the past five years, I think that, for a lot of people, the "e" in e-business came to mean "easy" or "escape"—e-business represented a kind of magical way of *avoiding* everything traditionally associated with "business." All the planning. All the process. All the relationship building. All the checks and cross-checks and safeguards. Boring stuff like accounting. Gut-wrenching stuff like accountability and responsible public policy. The magic "e" seemed to offer the prospect of leapfrogging right over all that, achieving wealth overnight—in a sprint, rather than a marathon.

Some of us, though, actually enjoy business. We enjoy the competition. Our adrenaline kicks in at the prospect of a long-distance race. We accept—we relish—the pragmatic, tactical, roll-up-your-sleeves-and-dive-in aspects of planning, and process creation, and management systems. It doesn't feel boring. It feels like building something important and significant.

The soaring fantasies of the era we're now leaving were, perhaps, inevitable—and, in their own way, inspiring. Big shifts in history usually begin with a romantic revolution. Whenever people set out for the unknown, they do so in a spirit of adventure. But, when they arrive there, they put down roots. They build something that lasts.

So arguably, the most striking thing about this moment in e-business's short, eventful life is the people who are now at the front of the march. The era we're now entering calls for a new breed of adventurer. The veterans have joined the crusade—with vigor. Indeed, we've never felt so energized. In the pages that follow, we hope to communicate our excitement about what we are doing.

For me personally, I experience this time with a mixture of satisfaction, confidence and hope. Satisfaction at IBM having stuck to its guns—and gotten things pretty much right. Confidence in our ability going forward to deliver on our promise, and to deliver on our customers' needs. And hope about the genuinely transformative future that is opening up before all of us—businesses, schools, governments, entire societies.

And there's something else, too. This is fun. I find myself relishing this work as never before. There's simply nothing like working as hard as you can with an extraordinary group of people to hit your targets, to prove yourself against tough odds, to build something entirely new, even to change the world. For me, it's the most satisfying feeling there is.

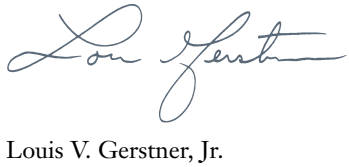
We'd better not blink. These next couple of years are going to go by in a flash.

* * *

I want to introduce two people to you who are very important to the future of IBM.

• Sam Palmisano was named president, chief operating officer and a director of IBM in September. He has a stellar record of achievement in the 27 years he has worked at IBM, including stints as head of our services, PC and server businesses. His primary responsibility is making sure that we execute well and that all our business units work as one team. Our fourth quarter results are, in part, evidence of Sam's expertise.

• John Thompson, elected vice chairman and a director in September, is responsible for research, new business opportunities, new technology, new directions. While everyone's focused on the ball, John is focused on the fences.



Louis V. Gerstner, Jr.
Chairman and Chief Executive Officer

AND SO OUR STORY BEGINS

CHAPTER I

REPORTS OF OUR DEMISE

IN MARKETS WE ONCE LED (OR SHOULD HAVE)—HIGH-END STORAGE, UNIX SERVERS AND DATABASE SOFTWARE—WE'RE BATTLING BACK AND MAKING UP LOST GROUND.

DATABASE SOFTWARE

When the world's information ran on IBM mainframes, IBM databases managed it all. But when the world shifted to smaller computers and the model known as client-server, we ceded major portions of that database leadership. The methodical comeback that has put us back within striking distance of the lead in the data management marketplace started in the mid-'90s, with massive investments in the product itself; then we built marketing and mindshare; and finally we put in place a dedicated sales force. Through the course of 2000, DB2 grew three times faster than the industry on Windows NT and UNIX platforms.

IBM DB2 **SOFTWARE** REVENUE
ON UNIX AND WINDOWS NT
PLATFORMS GREW 73% IN 2000.

IN THE PAST 18 MONTHS, APPROXIMATELY 1,000
companies have either replaced or chosen
IBM'S DB2 DATABASE PRODUCTS OVER ORACLE.

MAJOR SOFTWARE VENDORS LIKE
SIEBEL, SAP AND **PEOPLESOFT**
HAVE SELECTED DB2 AS THEIR
PREFERRED DATABASE.

"We've come all the way back. Now it's time for each of us to look in the mirror and say, 'This is personal. There's no way I'm going to sit back and let any competitor encroach on my account.'"

SHERRY YAZDI
Data Management Sales Team Leader

"We penetrated half of our chief competitor's key accounts even before we had all the advanced function for Shark. Okay, in December we shipped it. Now things are really going to get fun."

JOHN POWER
Worldwide Marketing Manager, Shark

ENTERPRISE **STORAGE**

Take your eye off the ball in this industry, and the penalties are severe. In the marketplace for storage, we've patented more technology than any other company, and in 2000, IBM received the U.S. National Medal of Technology in recognition of decades of leadership in storage. But for most of the 1990s, we labored at a substantial disadvantage in the marketplace for storage subsystems. Enter the IBM Enterprise Storage Server code named "Shark." In 2000, the first year after its launch, we shipped nearly 4,000 Sharks, and revenue for high-end disk storage increased 21 percent for the year.

IN 2000, IBM SHIPPED 73% MORE TERABYTES OF STORAGE THAN THE PREVIOUS YEAR – **INCREASING** SHIPPED DISK STORAGE TO MORE THAN **11,000 TERABYTES** IN 12 MONTHS.

60% OF GLOBAL 100 COMPANIES HAVE *already purchased and installed* A SHARK ENTERPRISE STORAGE SERVER.

COMBINED, ALL SHARK ENTERPRISE STORAGE SERVERS WORLDWIDE HOLD MORE THAN 7 PETABYTES OF DATA, *roughly equal to the printed text of* 700 U.S. LIBRARIES OF CONGRESS.

CINDY GALLO
Shark Testing Manager

VINCENT HSU
Microcode Development

BARRY RUDOLPH
Vice President, Disk Storage Systems and Software

UNIX SERVERS

The painful irony of our history in Web servers is that we invented the RISC chip—the basic building block of the UNIX marketplace. But rather than exploit that technical head start, we watched as a handful of competitors did—and built advantages so significant some considered them insurmountable. Some, but not us. We made the decision in the late '90s to stay in the market, invest, mobilize and compete. Today, behind IBM-invented technologies like silicon-on-insulator and copper-based microprocessors, our pSeries eServer is the price/performance leader. The S80 is the fastest-selling UNIX server in history, and our overall UNIX server revenues were up 28 percent for the year, 49 percent in the last quarter.

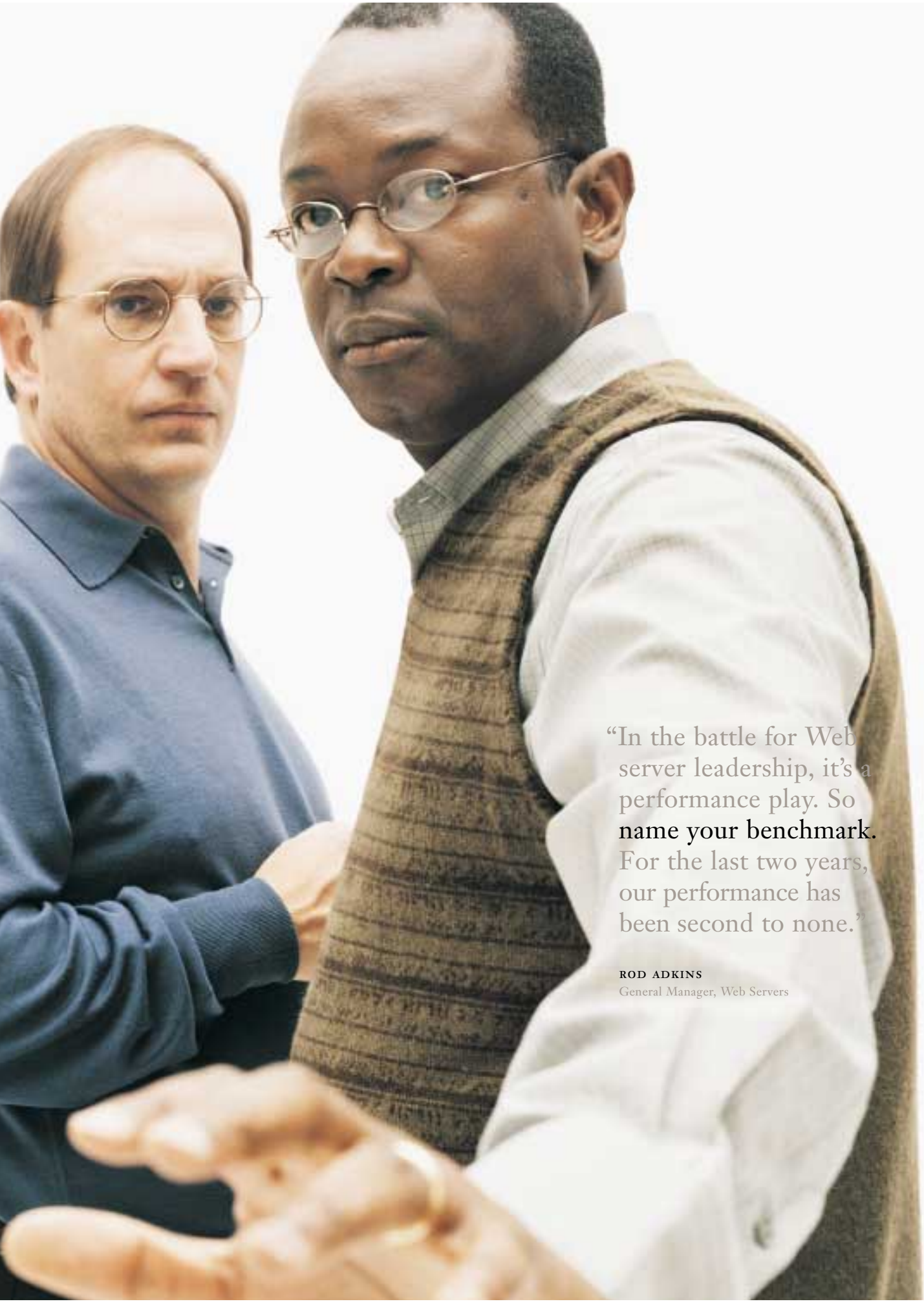
IN 2000, IBM UNIX SERVERS HELD
MORE INDUSTRY *performance benchmarks*
THAN ANY OTHER VENDOR.

NUMBER ONE
IN
SUPERCOMPUTING

IBM LEADS THE TOP500 LIST OF SUPERCOMPUTERS,
WITH 215 OF THE WORLD'S 500
FASTEST, MOST *powerful supercomputers.*

ACCORDING TO IDC, IBM IS THE
NUMBER ONE WORLDWIDE
SERVER VENDOR
WHEN MEASURED BY REVENUE.

DAVE TUREK
Vice President, Scientific and Technical Computing Offerings, Web Servers



"In the battle for Web server leadership, it's a performance play. So **name your benchmark.** For the last two years, our performance has been second to none."

ROD ADKINS
General Manager, Web Servers

CHAPTER 2

THE LEADER'S DILEMMA

OUR STORY CONTINUES WITH A VICTORY AND A LESSON: THAT BEING TOP OF THE CHARTS MAY BEGET ITS OWN KIND OF CHALLENGE, AS WHEN MARKET DEMAND RACES AHEAD OF SUPPLY, OR WHEN SUCCESS SERVES TO DAMPEN THE COMPETITIVE FIRE.

If they were running self-standing enterprises, John Kelly, Doug Elix and Steve Mills would be Fortune 150 CEOs. They're not. Instead, they run IBM's technology, services and software businesses, respectively—businesses that generated more than 60 percent of IBM's revenue last year. They plan competitive strategy, lead vast workforces, make decisions about where to invest and when to divest—and stand accountable for their results. And in 2000, they all had to adjust on the fly to changing market conditions.

JOHN KELLY, III
Senior Vice President, IBM Technology Group

DOUG ELIX
Senior Vice President, IBM Global Services

In the early days of 2001, **JOHN KELLY, DOUG ELIX AND STEVE MILLS** sat down to talk about the wild ride of the year past and the opportunities of the year ahead.

LESSONS LEARNED

Kelly: For us, the big lesson of 2000 was that if you have leadership technology, "build it and they will come." In the first quarter, I'm sitting near 70 percent utilization—which is death in my business—but we knew what was coming, and just kept building. In the third quarter, it popped. We thought we were in a high-growth business; what we didn't realize was we were in a hypergrowth business. Even that's an understatement.

Elix: Tell me about it. In services, we worked through a transition that spanned three quarters. We'd had great business in systems integration and even doing Y2K work, and then suddenly we had to transition all of those services completely to e-business-oriented services, hire thousands of people and retrain thousands of our own people. It wasn't until the fourth quarter that we saw the momentum return to the business.

Kelly: But in any one of our cases, we've got to continue to have confidence that the business is going to grow.

STEVE MILLS
Senior Vice President, IBM Software Group

Mills: The thing I like about what you've been doing in the OEM business is getting more utilization, more customers, across more industry segments, and that gives you some cushion against the ups and downs. It's the single-customer phenomenon that can kill you.

Kelly: Right. Customers and segments. But we came from a background of doing too many things. And we've finally focused on the top segments and key customers. The trick now is to keep the team focused, because there's always the temptation to go for the high-volume opportunity in lower-margin products. We've made the decision that's not our game.

Mills: I think this was a year that taught many people that no tree is going to grow straight to heaven. In software, we'd had a number of very good years, and a lot of growth, and in retrospect, I don't think the reasons for that success were as well understood as they have become this year.

MAKING THE CALL

Mills: You can't study things to death. There are development opportunities where you don't have a lot of time to do long, complicated business cases. You have to incubate a number of them, pilot them and see whether they're successful. The ones that aren't, you've got to be prepared to terminate quickly and efficiently, and the ones that do take off, you nurture them and grow them.

Kelly: A vendor in Japan built a packaging plant to support our growth, on a handshake. We shook hands, and they literally started digging the hole in August. By the end of the year, the plant was online.

Elix: In almost every one of our big growth businesses, we've started based as much on management judgment as on business cases. I mean, conversion to the customer relationship management services, to e-procurement, to supply chain: we didn't spend a lot of time doing complicated business cases to get those off the ground.

Having said that, we do still have to make the case for capital investment. To build the Web hosting business required a tremendous commitment of capital—$4 billion so far. And we also have huge investments in bringing people on board to meet the increasing demand in the professional services business. We're hiring more than 19,000 people a year. That's a tremendous investment, as well, which we now do almost as a matter of course.

Kelly: For me, well, there aren't a lot of companies in the semiconductor business prepared to put $5 billion on the table for big fabricators. We can. We did. Somebody asked me what you feel like when the company says, "Okay, here's $5 billion. Don't let us down!"

Mills: And I bet you said, "I didn't blink an eye!"

Kelly: Actually, I said I felt relieved, because I'd already started the project. In fact, I had Lou Gerstner up in Fishkill a few weeks after I got the approvals. We're driving in, and a lot of progress is already visible. The cranes were there, and there must have been several hundred construction workers at the site. And Lou looked at me and he said, "John, you started this before I approved it." So, back to the question: The day I got the funding, I was relieved.

THE ADVANTAGE OF SCALE

Kelly: There are challenges built into being one company with a portfolio of businesses, as opposed to being a pure play, self-standing, single-minded operation. The challenges are dwarfed by the advantages, but they're still there to be managed.

One of them is this balance you have to strike: Make sure you capitalize on the assets of the rest of the company, be an asset yourself, and balance that with the focus you need to succeed within your market segment.

Elix: Exactly. We're the biggest, most capable services organization in the world, but we can't and won't go in front of a customer without the right alignment across the corporation. When we start to put together a solution, being hardwired to colleagues who have great customer relationships at one end and who are actually building the products and technologies at the other end is a trump card we play again and again and again.

COMPETE? COOPERATE? YES.

Kelly: A lot of my best customers are some of IBM's biggest competitors in the server and box business, and no one has ever constrained me from selling our great technology to them. So I just keep driving.

Mills: Yeah, us too. It's a diverse world. We have to coexist with, support and sell to companies that other parts of the product or services organization compete with. But we certainly jump on opportunities where we can leverage another part of IBM, because we know software can pull hardware and services into a sale.

Elix: Right. We made this decision many years ago. We are a multi-faceted company that is in many product areas, as well as many service areas.

Kelly: I mean, some parts of the business have tough challenges in this—some of the product houses. But there are lots of areas where it's positive synergy. One of my biggest customers is somebody that Doug calls on, so the better Doug does, the more components I sell.

MANAGING THE FUTURE

Mills: Thinking customers today understand that you can't implement a transformed e-business enterprise unless you get the infrastructure underneath it running. They also know they need a partner that can look across all these processes and see how to put them together. Infrastructure is going to be a winning play for us this year.

Elix: For us, outsourcing is back strong. We cracked the market in Asia—in a way, we *created* the market in Asia. Then there's e-sourcing (see page 33), and the business transformation that underpins all of the infrastructure and hardware and software changes. That holds tremendous opportunities for growth.

Kelly: We've planted ourselves in an incredibly fast-growing segment. So whether it's chips for servers, chips for infrastructure for the Internet, or chips for pervasive devices, we're parked in the sweet spot. And we have a broad spectrum of customers in each segment. We're ready to go wherever this thing is going to go.

You can't live through a year like 2000 and not learn a lot. One of the advantages that the three of us have had is that we grew up in our businesses. We have a gut instinct for it, so we can make decisions—even big ones—faster.

services

market opportunity

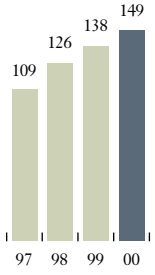
IDC projects spending on I/T to grow 11 percent over the next five years, with the fastest growth coming in services, microelectronics and software—the areas on which IBM has been focusing.

$470

BILLION MARKET FOR INFORMATION TECHNOLOGY SERVICES

Estimates show the market for I/T services will grow 14 percent annually to $470 billion by 2003.

investments



EMPLOYEES AT IBM GLOBAL SERVICES

(in thousands)

In 2000, IBM Global Services hired more than 19,000 people. It invested $400 million in professional development and knowledge tools, and $50 million in e-business training.

semiconductors

market opportunity

$69

BILLION MARKET FOR NON-PC CHIPS

Analysts estimate a $69 billion market for chips used in networking infrastructure, pervasive computing devices and enterprise information technology—three of the fastest growing segments of this industry.

investments

$5

BILLION INVESTED

IBM is investing $5 billion over the next four years to expand chip manufacturing and packaging capacity. This includes a $2.5 billion facility in East Fishkill, N.Y.—the first to integrate IBM's leading chip-making technologies into larger, 300mm wafers.

software

market opportunity

$77

BILLION OPPORTUNITY FOR MIDDLEWARE

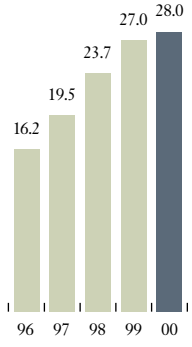
Analysts estimate that today's $77 billion market for middleware is growing 14 percent annually.

investments

50

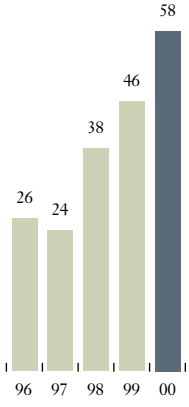
MAJOR ALLIANCES

IBM forged 50 strategic alliances with business software specialists to increase sales of hardware, services, database software and other middleware. IBM is investing heavily in WebSphere—including a $1 billion investment in 2000 for marketing, partner development and sales programs.



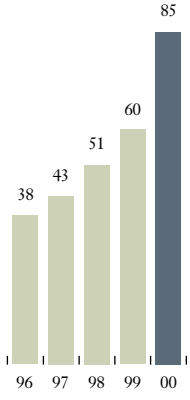
SERVICES REVENUE

($ in billions)



OUTSOURCING

Total number of signed strategic outsourcing contracts valued at more than $100 million



BACKLOG

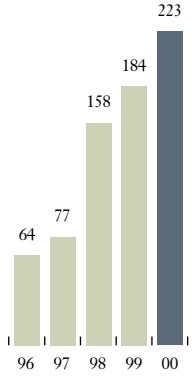
($ in billions) Backlog represents the total amount of revenue remaining on signed contracts

REVENUE from e-business services—which include e-commerce consulting, e-business enablement and e-hosting services—grew more than 70 percent in 2000.

IBM SIGNED $10 billion in outsourcing contracts in the Asia Pacific region in 2000—more than twice the value of contracts signed there in 1999.

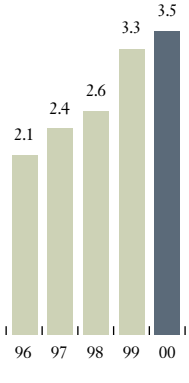
28%

MICROELECTRONICS OEM REVENUE GROWTH IN 2000



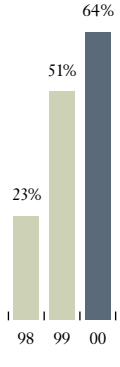
NUMBER OF NEW CUSTOM MICROCHIP DESIGNS FOR CUSTOMERS

REVENUE from logic chips grew 50 percent in 2000. ASICs, the most prevalent form of custom logic chip, are used in all types of electronic products where functions and performance requirements can't be met by off-the-shelf processors. In 1999, IBM became the number-one supplier of ASICs, and continued this leadership in 2000.



DISTRIBUTED SOFTWARE REVENUE

($ in billions)



DB2 DISTRIBUTED SOFTWARE REVENUE GROWTH

(year over year)

221%

WEBSPHERE REVENUE GROWTH IN 2000 ON UNIX AND WINDOWS NT

Nearly 35,000 customers are using IBM WebSphere as e-infrastructure software, including most of the world's top commercial banks, telecommunications, health care and Wall Street brokerage companies.

CHAPTER 3

THE PLOT THICKENS

WHOLE NEW FRONTS OPEN THAT PROMISE
TO DWARF TODAY'S MARKET BATTLES.
INTRODUCING LINUX AND E-SOURCING.
VICTORY WILL GO TO THE FIRST ONE
WITH THE RESOURCES, VISION AND COMMITMENT
TO SEIZE THE MOMENT.

Why I believe Linux will fundamentally change the information technology industry.

AN OPINION

by

IRVING WLADAWSKY-BERGER, Vice President, Technology and Strategy, IBM Server Group

If Linux were just another operating system, we wouldn't be all that high on it. But that's what's so interesting. Linux *is* an operating system, but it's also radically different from anything that has come before it. It changes the way software is created and delivered.

Linux is like the Internet itself—it's unowned, and unownable. Anyone can propose software changes, as long as those changes are returned to a loose-knit network of developers known as the Open Source community. It's a highly selective, disciplined process that serves two purposes: It throws technical innovation into perpetual fast-forward; and it guarantees the world that Linux will always remain beyond the control of any single vendor.

In my mind, then, Linux is a phenomenon that holds the potential to change the game along two important dimensions.

1. It fulfills a big promise: all hardware, software and applications working together. Linux is a wonderful thing because it is the first operating system to run on any hardware platform. That means it can do for business applications what the Internet did for networking and communications—deliver on the promise of truly open, interoperable, any-to-any computing.

In a world where a billion people using a trillion devices are all interconnected, can you imagine that software and hardware that hasn't even been invented yet will have to coexist? Of course! Linux will make that possible, and that's one reason it's going to grow a lot faster than any other operating system over the next several years.

It's interesting to me that some people are surprised that IBM is embracing Linux, while other large technology companies are trying to act as though Linux weren't happening. This shouldn't be a surprise. Linux is bringing the game back into our zone, precisely because we saw the world moving to open standards and fundamentally reconfigured our products, our strategy and our culture toward open systems, common standards and collaborative business practices.

2. It alters the way our industry delivers value to its customers (which is very good news for IBM). A lot of people who have played by one set of rules in this industry are going to find out they're now playing a different game. The widespread adoption of Linux is going to neutralize any vendor's ability to exercise control—over customers or software developers—based on that vendor's proprietary operating system. When applications are no longer lashed to a specific operating platform, control and choice shift away from the technology company, and into the hands of customers. This makes possible an equally seismic shift in the way value is delivered—through services, through middleware, through servers.

So, we're going to invest $1 billion in Linux, and we've dedicated 1,500 programmers to enable every IBM hardware and software product for Linux. Our strategy is to accelerate its adoption as a platform that can support heavy-duty, enterprise workloads—such as those already in production with customers like weather.com, Shell International Exploration and Production in the Netherlands, and Telia, Scandinavia's largest telecommunications company.

We think that, at the end of the day, the operating system that provides the most flexibility to customers is the one that is going to end up winning. We're voting with our customers on this one. We're betting a big part of IBM's future on Linux.

IBM IS A

FOUNDING **MEMBER**

AND CONTRIBUTOR TO THE
OPEN SOURCE DEVELOPMENT LAB.

OVER THE NEXT THREE YEARS,
IBM WILL INVEST MORE THAN

$300 **MILLION** TO DEVELOP

LINUX CONSULTING, IMPLEMENTATION
AND SUPPORT SERVICES.

IBM IS INVESTING

$4 BILLION

OVER THE NEXT 3 YEARS TO BUILD OUT ITS E-BUSINESS HOSTING INFRASTRUCTURE.

WITH

230 DATA CENTERS

WORLDWIDE, IBM IS WORKING WITH PARTNERS SUCH AS AT&T, QWEST, TELECOM ITALIA AND NTT TO OPEN NEW IBM E-BUSINESS HOSTING CENTERS AROUND THE WORLD IN 2001.

Why I BELIEVE e-sourcing WILL FUNDAMENTALLY change THE INFORMATION TECHNOLOGY industry.

AN OPINION

by

GINNI ROMETTY, General Manager, Strategy and Marketing, IBM Global Services

The initial idea of outsourcing is simple enough. An enterprise decides to turn over its information technology department—both equipment and staff—to an I/T partner. The physical assets switch owners, and the people running the systems switch ID badges.

The logic is compelling: an improved balance sheet; relief from the headaches of technology ownership and maintenance; and much greater flexibility in meeting the infrastructure demands of doing real e-business.

Now, take that idea and surround it with the networked world. Very soon, it won't be necessary for an enterprise physically to own, install, manage—or even house—any aspect of a traditional computing environment. The processing, the storage, the applications, the systems management, the security, the load balancing—all of it can be provided over the Internet as a service. Customers don't have to own it. They can rent it, and pay as they need it, as they use it.

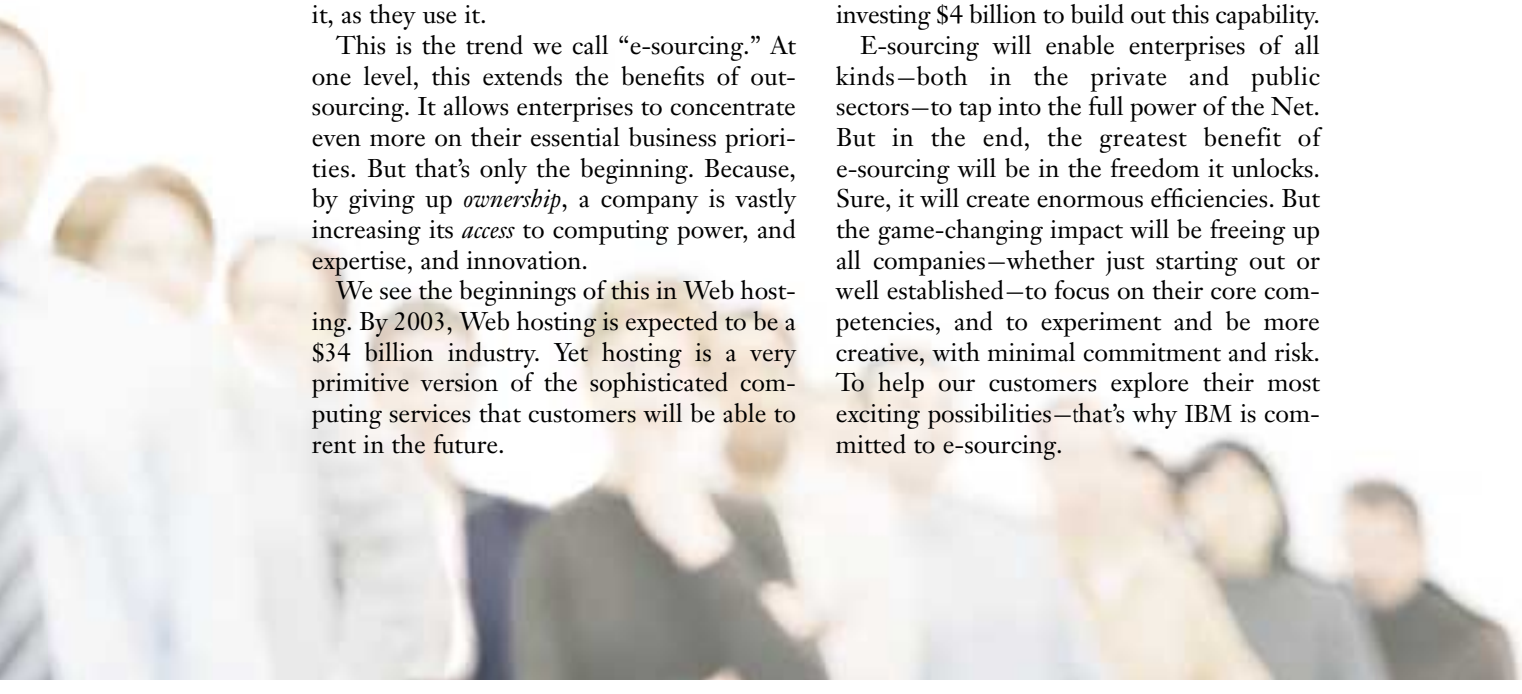
This is the trend we call "e-sourcing." At one level, this extends the benefits of outsourcing. It allows enterprises to concentrate even more on their essential business priorities. But that's only the beginning. Because, by giving up *ownership*, a company is vastly increasing its *access* to computing power, and expertise, and innovation.

We see the beginnings of this in Web hosting. By 2003, Web hosting is expected to be a $34 billion industry. Yet hosting is a very primitive version of the sophisticated computing services that customers will be able to rent in the future.

For IBM and the rest of our industry, this has profound implications. It changes who our customers are and what we will sell to them. Individual businesses may no longer be the primary decision makers when it comes to I/T purchases. Instead, those decisions may eventually be aggregated to a small number of mammoth computing "service providers," like telecommunications companies and today's hosting companies.

We intend to provide the infrastructure technologies that all of these service providers will require. And we'll provide many of these services ourselves. We're already one of the world's largest hosting businesses, and we're investing $4 billion to build out this capability.

E-sourcing will enable enterprises of all kinds—both in the private and public sectors—to tap into the full power of the Net. But in the end, the greatest benefit of e-sourcing will be in the freedom it unlocks. Sure, it will create enormous efficiencies. But the game-changing impact will be freeing up all companies—whether just starting out or well established—to focus on their core competencies, and to experiment and be more creative, with minimal commitment and risk. To help our customers explore their most exciting possibilities—that's why IBM is committed to e-sourcing.



IBM'S E-BUSINESS
HOSTING REVENUE
DOUBLED IN 2000.

CHAPTER 4

INTO THE WILD

ON THE HORIZON, NEW WORLDS SHIMMER IN THE MORNING LIGHT. WHO WILL GET THERE FIRST AND DEVELOP THEIR POTENTIAL? AT NIGHT, WE DREAM OF NEW TECHNOLOGIES. AT DAYBREAK, WE CONCEIVE NEW BUSINESS MODELS.

GERD BINNIG
Nobel Laureate and IBM Fellow,
Micromechanics and Nanomechanics
REAL JOB: *Finding the atomic tipping po*

ETTE BURTON
ıior Consultant, Knowledge
l Content Management Solutions

AL JOB: *Understanding the anic life of ideas and conversations*

SAY THE WORD "innovation" in the context of the information technology industry, and it's easy to make the mental connection to the world of R&D, physical sciences, algorithms and invention.

And for a lot of people, all that makes for a very natural connection to IBM. But for us, that kind of innovation is only half the story.

There's another kind of innovation—requiring its own special kind of ingenuity. It's equally demanding and every bit as important to our customers. This is about the invention of new business models and market structures, in every industry—from retail and financial services to education, governance and the delivery of health care.

Tucked inside IBM Global Services is the world's largest business and information technology consultancy. IBM Business Innovation Services is populated by 50,000 consultants, each of them specialized by industry, or in such disciplines as customer relationship management, supply chain, business intelligence, digital branding, and security and privacy practices.

Of course, technological innovation *is* the genetic code of IBM. The record of achievement here reaches from prototypes of quantum computers and holographic storage to technologies for specialized chips—including chips that consume very little energy—that will power the next generation of Net-access devices. Our research stretches from the most powerful supercomputer technology on the planet to the software and servers that power the most heavily trafficked sites on the Web.

For the eighth straight year, IBM earned more patents than any other company (more, in fact, than our eight closest competitors combined). By year end, fully one third of those patents had made their way from the lab to the marketplace—and were at work powering our own products or licensed to others. IBM's total intellectual property portfolio generated more than $1.5 billion in income in 2000.

There are some companies that excel at technical innovation. There are others that specialize in consulting. Our ability to do both is a unique combination and strength, because customers who commit to make a real transformation require both—the new idea, and the technologies to implement it.

So what mental image should come to mind when you apply the word "innovation" to IBM? It has two closely related, but exceptionally distinct faces. And thousands of names.

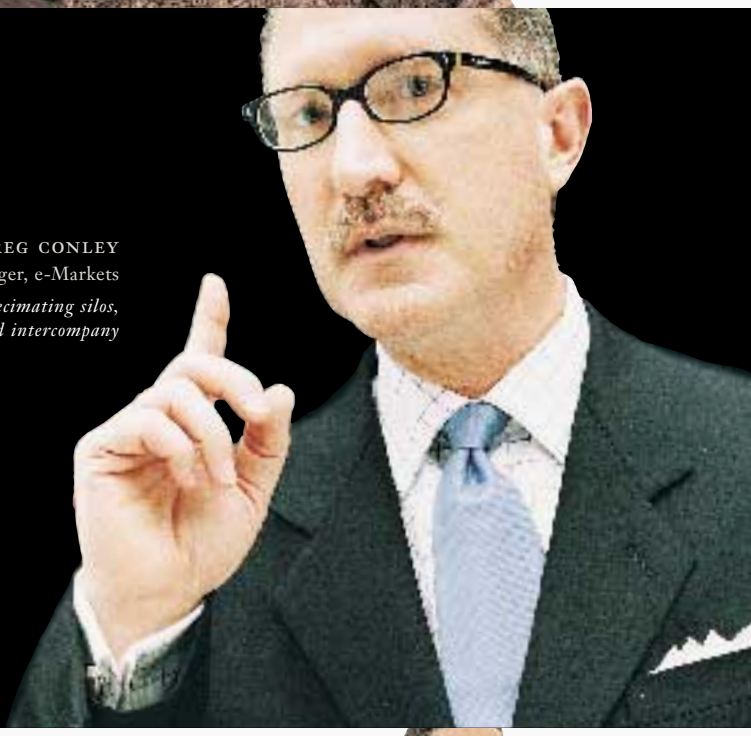
Meet just a few of them.

MARK DEAN
IBM Fellow and Vice President, Systems Research
REAL JOB: *Taking computing beyond the computer*

SHOUHENG SUN
Researcher, Materials Chemist
REAL JOB: *Self-assembling magnetic materials*

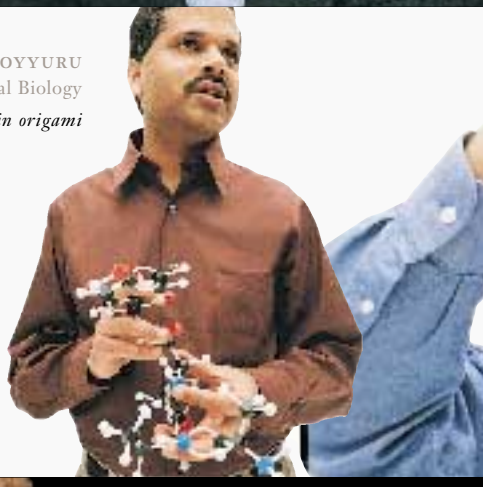
. LEPPANEN
er, Mobile Internet Solutions
JOB: *Obsoleting the office*

GREG CONLEY
General Manager, e-Markets
REAL JOB: *Decimating silos, intracompany and intercompany*



CHERIE KAGAN
Researcher, Electronic and Optical Organic Materials and Devices
REAL JOB: *Free-range components*

AJAY ROYYURU
Manager, Structural Biology
REAL JOB: *Protein origami*



MICHAEL HEIDEMAN
Vice President, Global Services—Communications Sector
REAL JOB: *Turning showbiz and phone biz into e-biz*

JANET CALDOW
Director, Institute for Electronic Government
REAL JOB: *Government at the speed of business*

RUSSELL LANGE
IBM Fellow and Chief
Technologist, Microelectronics
REAL JOB: *Semiconductor seismology*

GIAN-LUCA BONA
Manager, Photonic Networks
REAL JOB: *Data at light speed*

HARRIET PEARSON
Chief Privacy Officer
REAL JOB: *That is her real job*

MICHAEL V. LITTLEJOHN
General Manager, IBM
Learning Services, Americas
REAL JOB: *Raising organizational IQ*

STEVE WHITE
Senior Manager, Massively
Distributed Systems Group
REAL JOB: *Discovering the physics of market ecosystems*

STUART PARKIN
IBM Fellow, Project Leader,
Magnetoelectronics
REAL JOB: *Instant-on computing*

DR. RUSSELL RICCI
General Manager,
Healthcare Industry
REAL JOB:
Tender loving e-care

CAROLINE KOVAC
Vice President,
Life Science Solutions
REAL JOB: *What makes us tick*

The Wizard of Oz ©1939 Turner Entertainment Co.

CHAPTER 5

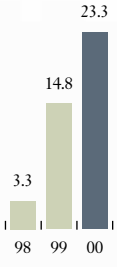
COMING HOME

HOW THE WORLD'S LARGEST PROPONENT OF E-BUSINESS IS TRANSFORMING ITS PROCESSES AND CULTURE TO BECOME THE WORLD'S LARGEST E-BUSINESS. AND SO IT BEGINS.

When does a business become an e-business? Until recently, the answer seemed to be: when you can buy something over its Web site. Today, we know better. It's when you work with your customers, take and fulfill orders, provide services, procure billions of dollars in goods and services, interlock with your suppliers—and support thousands of employees in scores of countries around the world to learn, collaborate and work in real time…on the Web. That's how we're helping our customers become e-businesses. And it all starts at home.

"Customers need fast and easy ways to do business with IBM. Our integrated Web-and-call-center channel, ibm.com—providing direct sales, service and support—does that. Today, customers can access more than 14,000 IBM products and solutions. And at $47,000 in sales per minute on an average business day, we're IBM's lowest-cost channel. IBM's PC business now does about a third of its business direct, one of the reasons it's returned to profitability."

DOUG MAINE
General Manager, ibm.com



TOTAL E-COMMERCE REVENUE GENERATED WITH BUSINESS PARTNERS, OEM PARTNERS AND THROUGH IBM.COM

($ in billions)

IBM e-commerce revenue grew sevenfold over the last three years to $23.3 billion.

In 2000, e-commerce revenue through ibm.com grew 143 percent. And revenue generated by e-commerce with business partners and OEM partners each grew 50 percent.

e-commerce

e-learning

"We saved a lot of money last year by moving 36 percent of our employee training to an online environment. But that's not the best reason to make the shift. With a mobile workforce like IBM's, and the increasing complexity of our customers' businesses, we're able to provide just-in-time learning for people who need to be with their clients and not sitting in a classroom. And we are providing these same types of e-learning solutions to customers around the world."

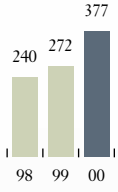
NANCY DEVINEY
General Manager, Learning Services

More than 200,000 employees have received education and training online.

New IBM managers are trained through an award-winning program that blends 75 percent e-learning with 25 percent classroom training.

"IBM's global purchasing activity is enormous and, therefore, complicated. To improve efficiency and effectiveness, we've applied e-business across the entire buying process, including the ability to select suppliers, place orders and handle payments online. What once took 30 days now takes one."

PATRICE KNIGHT
Vice President, Procurement Strategy and Transformation



COST AVOIDANCE FROM E-PROCUREMENT
($ in millions)

In 2000, IBM "e-procured" more than $43 billion in goods and services—up 60 percent from 1999—with 24,000 suppliers worldwide.

94%

OF GOODS AND SERVICES ARE NOW PURCHASED ELECTRONICALLY

e-procurement

MORE THAN

$350 MILLION

IN ANNUAL COST AVOIDANCE THROUGH THE USE OF DISTRIBUTED E-LEARNING

"Let's talk innovation. Today, U.S. health care enrollment is available via the intranet. Now, employees have access to personalized decision-making tools, such as a plan finder that helps them make health care choices; nearly 42,000 employees used the tool in 2000. Now, let's talk convenience and control. More information is available than ever before, and transactions can be conducted at any time. Employees are tracking the value of their HR programs and making charitable contributions online, all without the use of paper forms."

BARBARA BRICKMEIER
Director, Global Benefits

e-workforce

Since 1998, IBM Human Resources has been a leader in the creation of Web-based tools and information to transform its employee relationships.

Today, IBM employees use the intranet to access information, enroll and manage:
• 401K Plans • Career Planning
• Employee Stock Purchase Plans
• Health Care Options • Pension Plans
• Stock Options • Sales Commissions

IBM has also launched a Web resource for retired employees.

83%

of U.S. employees reviewed and enrolled in their annual health care options via the intranet in 2000.

"We're using some of the best solutions from our alliance partners to transform and integrate our own systems and operations. The payoffs: stronger customer relationships, greater marketplace agility to reach new customers, and a wealth of experience we can put to work helping customers who are transforming themselves. To be CIO of one of the world's largest e-businesses, you need to see the complementary relationship between external business strategy and internal technology strategy."

PHIL THOMPSON
Vice President, Business Transformation and CIO

IBM has avoided $4 billion in cost since 1998 through business process transformation of procurement, customer support and employee education.

Today, IBM is working with its software alliance partners to implement "best-of-class" e-business capabilities inside the company to reduce cost in areas such as enterprise resource planning, customer relationship management and supply chain management.

e-transformation

e-corporat culture

"Don't think of intranets as one-way communication channels. They're much more—productivity tools, workflow managers, places to collaborate, virtual workspaces. We're adding all that functionality to make IBM's intranet a platform for some key e-business goals: to integrate IBM's processes; redefine our culture and our brand; and empower individual employees, so they can access the company's collective knowledge—and contribute their own. The payoff is a smarter collective organism."

MIKE WING
Director, Worldwide Intranet
Strategy and Programs

In 2000, IBM's intranet surpassed nearly all channels—internal or external—as the most credible, preferred and useful source of information about the company in the IBM Global Employee Survey. All but one…it was tied by the grapevine.

2.5

MILLION VISITS BY
EMPLOYEES PER WEEK

REINVENTING EDUCATION
Scoil Mhuire Senior Primary School, Blakestown, Ireland; and Tran Quoc Toan Primary School, Hanoi, Vietnam

what DOES IT mean TO lead?

In our business, there's technical leadership, thought leadership, financial leadership, marketplace leadership—all the things documented in this report. But any company that aspires to make a lasting contribution to the world must lead in ways that spread far beyond the confines of the marketplace, and winning, and profit.

It's leadership by serving; leadership by caring; leadership in the community. It's the kind of leadership we think about when we think about the world our work will leave for our children. At IBM, it's how we apply our financial strength, resources and minds—more than 300,000 of the most talented people in any industry, and one of the most storied and aspirational of business enterprises—to change things, to make our planet a better place.

That's true now more than ever. The arrival of a networked world brings with it the requirement for enterprises, governments and entire societies to establish new frameworks on virtually every vital public policy issue—not simply to foster the development of an important new platform for our economy, but to take responsibility for how its consequences will affect people and the planet.

Of special urgency with the rise of the Net are protections of the individual's right to privacy. In 2000, we appointed IBM's first chief privacy officer—a senior executive charged with guiding all our policies and practices in this area, and with working across the public and private sectors to advance workable protections of consumer and citizen privacy.

Our largest ongoing corporate commitment remains the $45 million grant program Reinventing Education—which has the potential to touch one in five children in U.S. public schools, as well as children in seven other countries, including Singapore, site of our latest grant.

Independent evaluations tell us that our Reinventing Education efforts are doing what we set out to do—drive higher student achievement. In West Virginia, high school students using standards-based math lessons, created via online technology developed through the grant partnership, scored significantly higher on statewide exams. And in Houston, first-graders using an innovative speech-recognition technology called Watch-me!-Read scored significantly higher on comprehension and word recognition.

Underlying it all, IBM is perennially among the world's most generous corporations. In 2000, we contributed more than $126 million to programs around the world that help people in need. Individual employees added another $49 million through matching grants and donations to nonprofit organizations and educational institutions. And of incalculable value was the more than 4 million hours of their time and expertise IBMers volunteered to a broad range of local causes.

IBM continued its longstanding commitment to environmental leadership last year, ensuring that its operations and products provide ever greater value to society while minimizing their potential impact on the environment. Our participation in voluntary initiatives to address global climate change and our latest offering to facilitate the reuse and recycling of PCs are just two examples of environmental efforts that contributed to the significant recognition the company received in 2000 for environmental excellence.

We do all this because we know that people have high expectations of leaders. High, but appropriate. We understand that if we aspire to lead in the creation of the networked world, we have to demonstrate the courage and wisdom to step up to the grand societal challenges it raises—both those as new as today's headlines, and those as timeless as human society.

Because that's what it really means to lead.

COMPANY MISSION

At IBM, we strive to lead in the creation, development and manufacture of the industry's most advanced information technologies, including computer systems, software, networking systems, storage devices and microelectronics.

We translate these advanced technologies into value for our customers through our professional solutions and services businesses worldwide.