

Section Four

Promoting Social Responsibility with our Suppliers

OUR CHALLENGES

Extending supply chain social responsibility across a global supply chain

Improving our suppliers' ability to meet social responsibility requirements in our sourcing strategies

OUR OPPORTUNITIES

Assisting suppliers in emerging markets to develop into world-class providers

Raising the management systems capabilities of suppliers and sharing best practices

Contributing to the sustainable economic development of emerging markets

OUR STRATEGY

Identifying patterns of compliance and noncompliance through audits conducted in supplier locations globally

Facilitating learning and capacity building programs

Chairing the Electronic Industry Citizenship Coalition to promote collaboration within the industry

Including Supplier Code of Conduct in pre-sourcing activities

For an enterprise like IBM to consistently provide innovative products and services on a global basis, it must maintain a strong supply chain—especially today, with markets so diverse and dispersed. We currently have about 30,000 supplier locations in more than 60 countries.

At IBM, we understand that our supply chain is only as good as the relationship we have with our suppliers. We believe in the value of establishing long-term supplier relationships which facilitate sustained growth and opportunities for both IBM and our suppliers. To help define the parameters of the relationship, we have developed a comprehensive Supply Chain Social Responsibility initiative that underscores our belief that values define business relationships just as much as economic necessities do. This includes:

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What We Expect of Our Suppliers

“Over the past decade, companies in many sectors have begun to address issues within their supply chains both individually and collectively. Initial efforts have resulted in some level of improved factory labor and environmental conditions through auditing procedures and subsequent remediation plans to improve compliance. However, it is time for companies to move to the next step of factory engagement in order to effect change.

Despite a decade of good intent and dedicated resource commitment, programs based on the traditional audit model have not brought sustained workplace improvement in the global supply chain. Leadership companies like IBM have begun to focus on improved capacity building and collaboration as a means of furthering on-the-ground change.

The technology sector has been one of the first to proactively address supplier issues in a consistent and collaborative way through the efforts of the EICC. Looking ahead, the industry will also need to consider:

- › Stronger consistency and shared processes to reduce duplicate efforts with suppliers
- › Improved communication between buyers and suppliers in order to incorporate suppliers’ needs, including those related to incentives, in a more sustained manner
- › Stronger engagement with local government, industry participants and NGOs to help address systemic issues, such as excessive working hours and full payment of wages and social benefits”

Wei dong Zhou,
Business for Social Responsibility
China Director

The foundation of our Supply Chain Social Responsibility program is a set of Supplier Conduct Principles that outlines our expectations in regards to working hours, wages and benefits, employee health and safety, nondiscrimination, communications, the environment and ethics.

Our Supplier Conduct Principles are integrated into new and existing contracts and relationships with suppliers. We have also undertaken hundreds of on-location supplier assessments to the Code of Conduct, focusing on suppliers in emerging markets where noncompliance may be likely to occur.

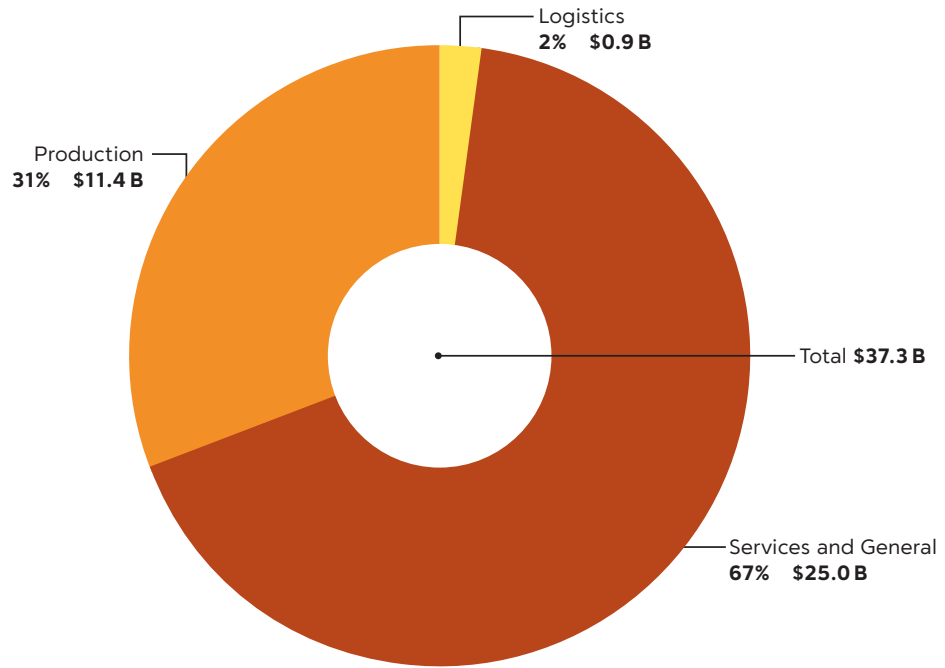
By the end of 2007 we had conducted more than 450 audits with suppliers in 12 countries. Audits were conducted by third-party agencies with local personnel who specialize in social responsibility and are well versed in local law, practices, culture and customs.

Our supplier audit program encompasses both manufacturing (production) and distribution (logistics) suppliers—which are historically where social audits are focused—as well as services and general procurement suppliers. With IBM’s growth in services offerings, we believe it is important to include all of these in our program and also monitor trends specific to these categories of suppliers.

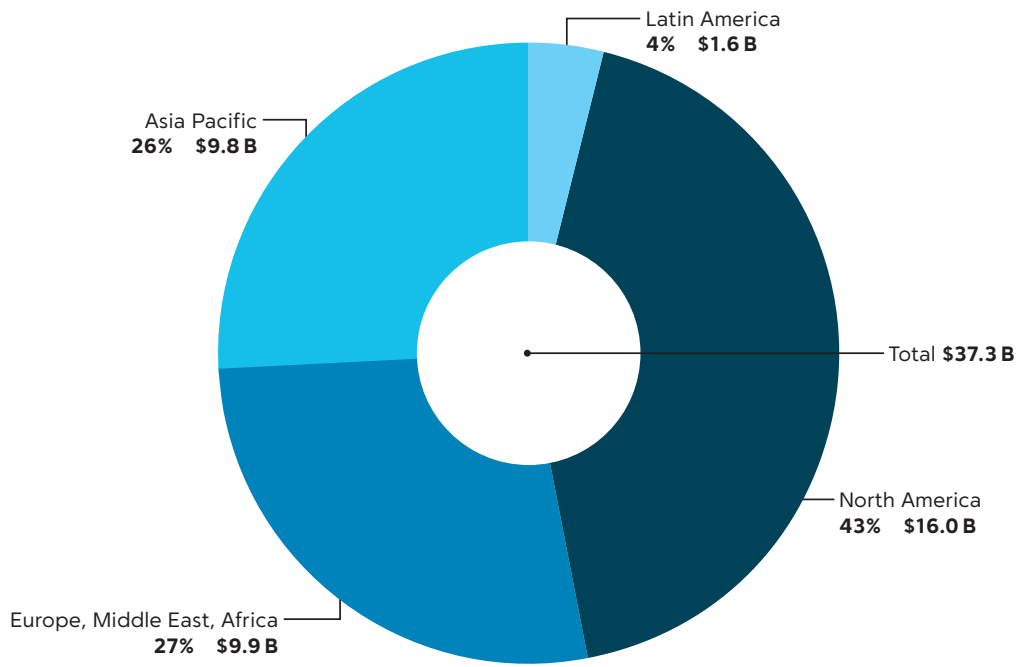
It is important to recognize the efforts of the many suppliers that are compliant with all or most of the provisions in our Code of Conduct. During our audits we strive to identify “best practices” and we commend our suppliers for demonstrating many of the following over the past year:

- › Senior management directly involved in social responsibility
- › Open management/worker communication channels
- › Written policies on human resources, health and safety, nondiscrimination and ethics
- › Frequent health and safety worker retraining
- › Detailed pay stubs with full disclosure of calculations
- › On-location worker recreational and educational programs
- › Active environmental conservation programs

2007 SUPPLIER SPENDING
By Category



2007 SUPPLIER SPENDING
By IBM Location

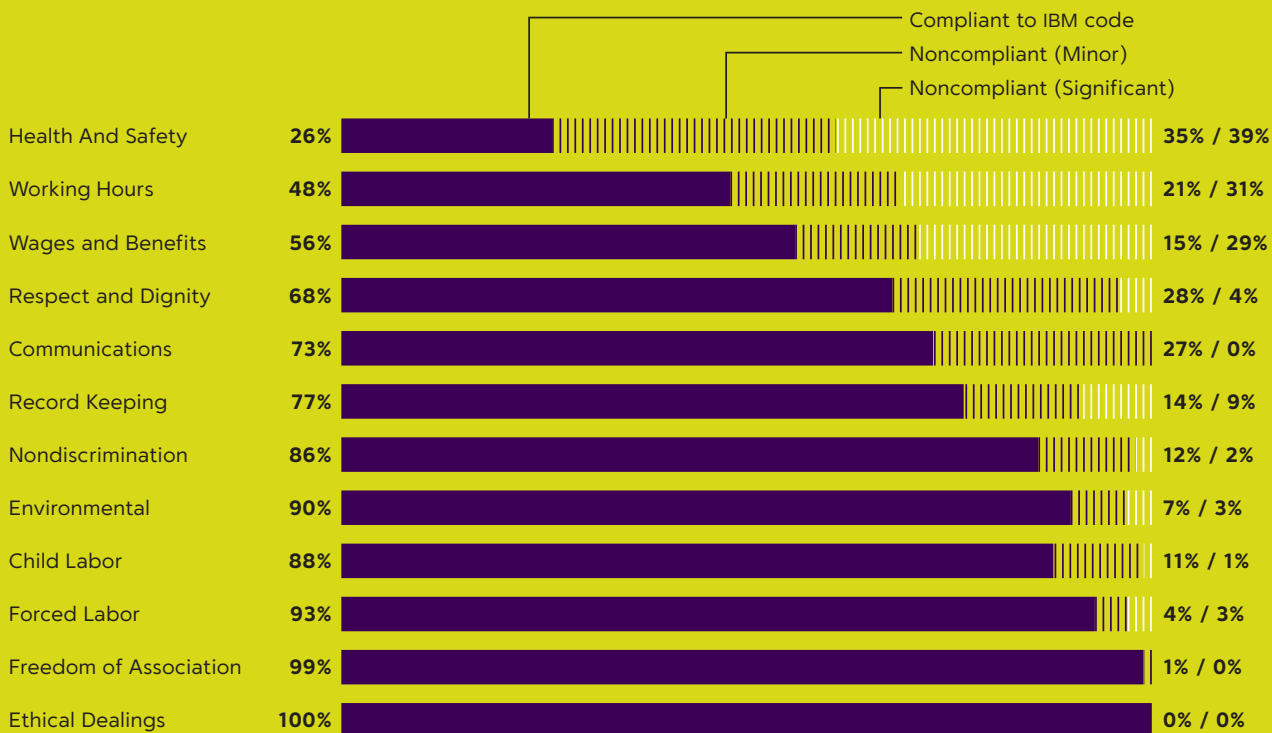


KEY PERFORMANCE INDICATOR

Supply Chain Social Responsibility Audits

SUPPLIER INITIAL AUDIT RESULTS

(2004-2007)



Commentary: By the end of 2007 we had conducted over 450 audits with suppliers in 12 emerging market countries. Audits were conducted by third-party agencies with local personnel who specialize in social responsibility and are well versed in local law, practices, culture and customs. * Overall, these audits have provided a number of insights:

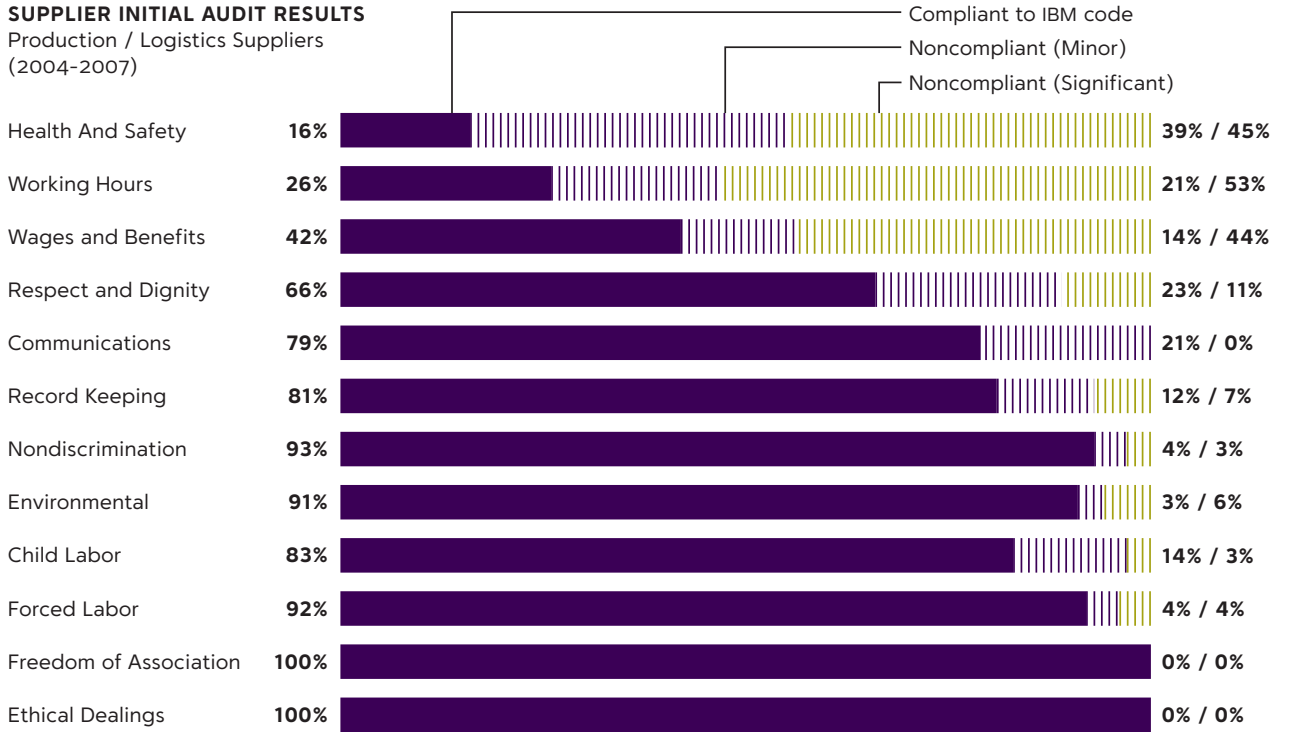
- › Suppliers in emerging markets generally need to further develop their management systems in non-operational areas such as human resources, health and safety, compliance and communications.
- › Local culture is a strong influencer of compliance with Codes of Conduct.

- › Manufacturing and Distribution suppliers generally were found to have a larger number of non-compliances than services and general procurement suppliers.
- › Our findings are similar to other companies performing supplier audits, both inside and outside the electronic sector.

Note: The graph shows the cumulative findings of assessments, including suppliers of both manufactured products and services in Brazil, China, Czech Republic, Hungary, India, Mexico, Philippines, Poland, Romania, Slovakia, Taiwan and Thailand.

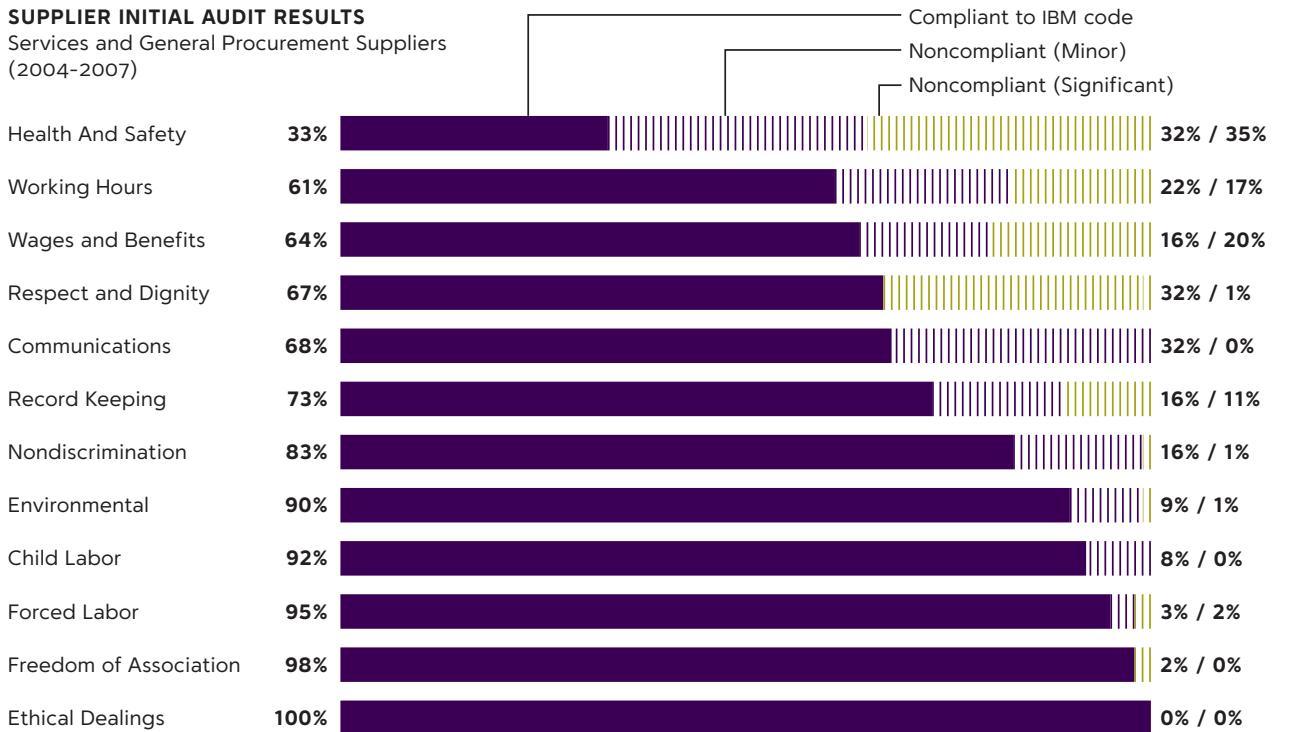
SUPPLIER INITIAL AUDIT RESULTS

Production / Logistics Suppliers
(2004-2007)



SUPPLIER INITIAL AUDIT RESULTS

Services and General Procurement Suppliers
(2004-2007)



2**Continuous Improvement**

We share audit results with our suppliers so that they are aware of any noncompliance with IBM's Supplier Conduct Principles. When audit findings reveal noncompliances, we require that our suppliers submit root cause and corrective action plans for our approval. We believe that this encourages them to take ownership over their own progress and devise realistic solutions that work for them. During 2007, we reviewed and accepted over 90 supplier improvement plans resulting from audits conducted during the year.

Our objective is to work with our suppliers to foster full compliance as they, in turn, apply these to the parts of their supply chain that are engaged in the production of goods and services for IBM. This interchange of audit information and improvement plans helps emphasize to our suppliers that continuous improvement is a requirement for their global supply chain as well as ours. The exchange also helps foster our suppliers' efforts to establish social responsibility as part of their own branding and daily operations.

We have also created an educational program to help our internal procurement teams become knowledgeable about IBM's Supply Chain Social Responsibility requirements as they conduct business with our suppliers on an ongoing basis. Over 700 buyers, engineers and interested employees have taken this Supply Chain Social Responsibility course since it was made available in 2005.

3**Industry Collaboration:
Electronic Industry Citizenship Coalition**

While we continue to advance our own IBM internal supply chain programs and trainings, we strongly believe in the value of industry collaboration. For example, we were one of the original companies to adopt the Electronic Industry Citizenship Coalition's (EICC) Code of Conduct (CoC) in 2004.

The EICC is the combined effort of more than 40 companies focused on improving industry-wide social and environmental performance through the adoption of a standardized industry code of conduct as well as consistent use of effective implementation tools and methods.

The creation and acceptance of a single common code of standards and consistent auditing and reporting procedures for the electronics industry make compliance more straightforward and efficient for all parties involved. The EICC Code covers expectations for performance across a range of issues including labor practices, health and safety, ethics and management systems, and environmental practices. And we accept the EICC Code as an equivalent to the IBM Supplier Conduct Principles.

In the three years since the EICC's inception, it has largely focused on establishing the Code of Conduct and developing implementation tools—building a foundation from which we expect to see tangible results during the next phase of implementation. The EICC offers great value in fostering peer learning and enabling access to responsible suppliers. We believe that aligning and incorporating different approaches, increasing dialogue and combining resources will lead to greater success in improved standards and consistent evaluation and performance for all.

In 2007, IBM's Manager of Supply Chain Social Responsibility, John Gabriel, assumed a post as Chair of the EICC, deepening our commitment to leadership of this initiative.

Looking Forward

A major priority will be to actively use the IBM Supplier Conduct Principles and the EICC Code of Conduct in pre-sourcing activities in emerging market countries as a means to better understand the environment and suppliers' readiness to assume social responsibility prior to conducting business. To achieve this, we will conduct pilot audits with high-potential suppliers in emerging market countries where our sourcing is in its infancy. This is a significant proactive step in moving our initiative to the forefront of sector activities in emerging markets.

Finally, we look forward to using the EICC's learning and capability training applications, joint audit activity, and database for the controlled exchange of audit reports.

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Supply Chain Diversity

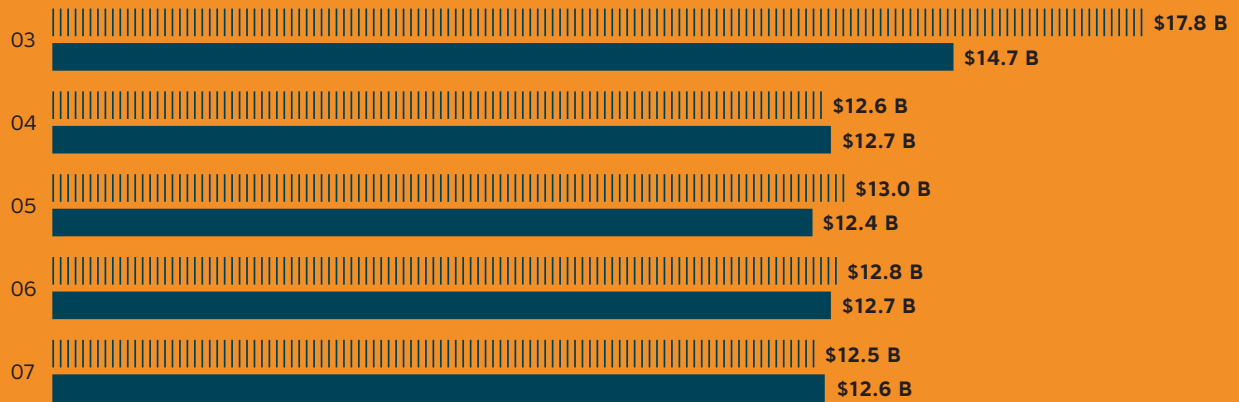
Through our sourcing practices we support a variety of diverse suppliers, including companies owned by minorities, women, people with disabilities and GLBT. In 2007 alone, we spent \$1.4 billion with such first-tier suppliers in the U.S. and \$2.4 billion worldwide (first and second tier diverse spend).

We have also established relationships with a number of organizations around the world that focus on supplier diversity programs for minority- and women-owned businesses. These organizations include, but are not limited to:

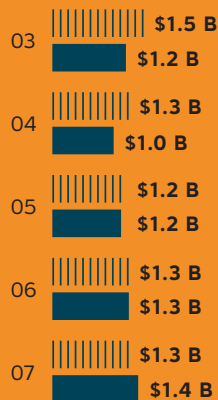
- › **NATIONAL MINORITY SUPPLIER DEVELOPMENT COUNCIL (NMSDC's)**
International Committee
- › **CANADIAN, ABORIGINAL AND MINORITY SUPPLIER COUNCIL (CAMSC)**
in Canada
- › **MINORITY SUPPLIER DIVERSITY UNITED KINGDOM (MSDUK)**
- › **ASSOCIATION OF ADVANCED KNOWLEDGE PROMOTION IN ETHNIC REGIONS (AKPRO)**
- › **WOMEN'S BUSINESS ENTERPRISE NATIONAL COUNCIL (WBENC)**
- › **THE U.S. NATIONAL GAY AND LESBIAN CHAMBER OF COMMERCE (NGLCC)**

KEY PERFORMANCE INDICATOR Supplier Diversity

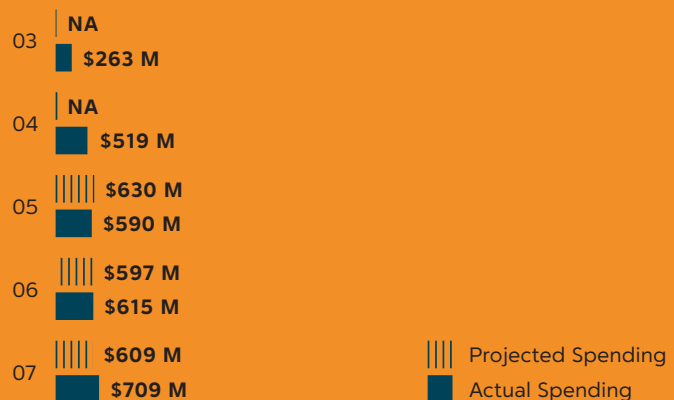
TOTAL U.S. SPENDING (First Tier)



DIVERSE U.S. SPENDING (First Tier)



DIVERSE NON-U.S. SPENDING (First Tier)



Projected Spending
Actual Spending

Commentary: IBM has established relationships with a number of organizations around the world that focus on supplier diversity programs for minority- and women-owned businesses. In addition to ensuring that certified U.S.-owned diverse businesses are given the opportunity to participate in the supply chain process worldwide, IBM understands the need to provide opportunities for in-country diverse owned businesses. This demonstrates IBM's commitment to the communities in which we operate around the world.

Short-Term Goals: Provide supplier diversity education to all non-U.S. members of the Global Procurement organization * Participate with NMSDC in the establishment of MSD-China * Identify high-quality diversity suppliers based in non-U.S. geographies

Long-Term Goals:

- › Achieve \$1 billion in supplier diversity spend outside the U.S. * Mirror our U.S. supplier development programs in non-U.S. geographies
- › Key programs include our Regional Town Meetings, Mentor Program, and Matchmakers
- › Establish diverse supplier relationships in Australia and South Africa