



IBM 2Q 2005
Earnings Presentation

July 2005

Certain comments made in this presentation may be characterized as forward looking under the Private Securities Litigation Reform Act of 1995.

Those statements involve a number of factors that could cause actual results to differ materially.

Additional information concerning these factors is contained in the Company's filing with the SEC. Copies are available from the SEC, from the IBM web site, or from IBM Investor Relations.

OPENING REMARKS

■ Key Accomplishments

- Operational Performance
- PC Sale
- Restructuring Actions
- Microsoft Settlement

■ 2Q Performance Highlights

- Services Signings
- Power5-based Servers and Storage
- Key Middleware
- Growth Initiatives
- Cash & Balance Sheet

IBM FINANCIAL SUMMARY

Continuing Operations (\$B except EPS)	Non-Recurring Items				IBM Results without Non-Recurring Items
	IBM As Rptd	PC Gain	Incremental Restructuring Charge	Microsoft Settlement	
Revenue	22.3				22.3
Yr/Yr%	(4%)				(4%)
Yr/Yr% excl. PC	6%				6%
Cost	13.5				13.5
GP%	39.4%				39.4%
Expense	6.0	(1.1)	1.7	(0.8)	6.2
PTI	2.7	1.1	(1.7)	0.8	2.6
Tax Rate	32.3%	33.1%	32.4%	39.0%	30.0%
Net Income	1.9	0.7	(1.2)	0.5	1.8
EPS	\$1.14	\$0.45	(\$0.72)	\$0.29	\$1.12
Yr/Yr%	13%				11%

May not add due to rounding

IBM FINANCIAL SUMMARY EXCLUDING PC RESULTS

(\$B except EPS)	IBM Results without Non-Recurring <u>Items</u>	Less: <u>PC Results</u>	IBM Results on an <u>Ongoing Basis</u>
Revenue	22.3	0.6	21.7
Yr/Yr%	(4%)		6%
Yr/Yr% @CC	(6%)		4%
Cost	13.5	0.6	12.9
GP%	39.4%	(9%)	40.6%
Expense	6.2	0.1	6.1
PTI	2.6	(0.1)	2.7
Net Income	1.8		1.9
EPS	\$1.12		\$1.18
Yr/Yr%	11%		18%

May not add due to rounding

IBM REVENUE

(\$B)	<u>B/(W) Yr/Yr</u>			<u>B/(W) Yr/Yr</u>		
	<u>1Q05</u>	<u>Rptd</u>	<u>@CC</u>	<u>2Q05</u>	<u>Rptd</u>	<u>@CC</u>
Global Services	11.7	6%	3%	12.0	6%	4%
Hardware	6.7	--	(2%)	5.6	(25%)	(27%)
w/o PC	4.4	2%	(1%)	5.0	5%	4%
Software	3.6	2%	--	3.8	10%	7%
Global Financing	0.6	(12%)	(15%)	0.6	(4%)	(7%)
Enterprise Inv./Other	0.3	15%	12%	0.3	(3%)	(5%)
IBM	22.9	3%	1%	22.3	(4%)	(6%)
w/o PC	20.6	4%	1%	21.7	6%	4%

IBM GEOGRAPHIC REVENUE

(\$B)	<u>B/(W) Yr/Yr</u>			<u>B/(W) Yr/Yr</u>			
	<u>1Q05</u>	<u>Rptd</u>	<u>@CC</u>	<u>2Q05</u>	<u>Rptd</u>	<u>@CC</u>	<u>@CC</u> <u>w/o PC</u>
Americas	9.3	2%	1%	9.4	(3%)	(4%)	5%
Europe/ME/A	7.7	7%	2%	7.5	--	(4%)	4%
Asia Pacific	5.2	1%	(2%)	4.6	(10%)	(13%)	2%
OEM	0.7	3%	3%	0.7	--	--	--
IBM	22.9	3%	1%	22.3	(4%)	(6%)	4%

- Continued strong growth in emerging countries without PC

IBM REVENUE - KEY INDUSTRY SALES UNITS

(\$B)	<u>B/(W) Yr/Yr</u>			<u>B/(W) Yr/Yr</u>			w/o PC
	<u>1Q05</u>	<u>Rptd</u>	<u>@CC</u>	<u>2Q05</u>	<u>Rptd</u>	<u>@CC</u>	<u>Yr/Yr</u>
Financial Services	5.7	4%	1%	5.8	(3%)	(5%)	1%
Public	3.4	4%	1%	3.5	2%	--	12%
Industrial	3.0	(1%)	(4%)	2.9	(5%)	(8%)	1%
Distribution	2.2	5%	2%	2.2	7%	4%	14%
Communications	2.1	1%	(1%)	2.1	--	(3%)	4%
Small / Medium	5.1	7%	4%	4.3	(14%)	(16%)	12%
All Sectors	22.3	3%	1%	21.7	(3%)	(6%)	7%

IBM GROSS PROFIT MARGIN

	<u>1Q05</u>	<u>B/(W)</u> <u>Yr/Yr Pts</u>	<u>2Q05</u>	<u>B/(W)</u> <u>Yr/Yr Pts</u>
Global Services	24.3%	0.6 pts	26.1%	1.7 pts
Hardware	27.5%	1.0 pts	33.9%	4.9 pts
w/o PC	35.3%	0.1 pts	38.7%	(0.5 pts)
Software	86.4%	0.5 pts	86.7%	0.5 pts
Global Financing	54.2%	(6.3 pts)	52.6%	(6.8 pts)
Enterprise Inv./Other	52.5%	13.0 pts	43.8%	(2.6 pts)
IBM	36.0%	0.4 pts	39.4%	3.0 pts
w/o PC	38.7%	0.1 pts	40.6%	0.9 pts

NON-RECURRING ITEMS

	Pre-Tax <u>(\$B)</u>
PC Sale Gain	1.1
Incremental Restructuring Action	(1.7)
■ Workforce Reduction	\$1.5B
Real Estate	0.2B
■ Approx. 14,500 resources, over 70% in Europe	
■ About 50% exits as of July 15	
■ Cost / Expense Savings	
➤ 2H 2005 = \$500M	
➤ FY 2006 = \$1.3B	
➤ Improves competitiveness	
Microsoft Settlement	0.8
■ \$75M credit for future use	

IBM EXPENSE SUMMARY

(\$B)	<u>As Reported</u>		Non- Recurring Items	<u>w/o Non- Recurring Items</u>	
	<u>2Q05</u>	<u>B/(W) Yr/Yr</u>		<u>2Q05</u>	<u>B/(W) Yr/Yr</u>
SG&A	6.5	(35%)	1.5	5.0	(4%)
RD&E	1.5	--	--	1.5	--
IP and Custom Dev. Income	(0.3)	(33%)	--	(0.3)	(33%)
Other Income and Expense	(1.7)	nm	(1.6)	(0.1)	nm
Interest Expense	0.1	nm	--	0.1	nm
Total Expense and Other Income	6.0	(2%)	(0.1)	6.2	(4%)
w/o PCs	6.0	(5%)		6.1	(7%)
E/R%	27.1%	(1.5 pts)		27.7%	(2.1 pts)
w/o PCs	27.4%	0.4 pts		28.0%	(0.2 pts)

nm = not meaningful

May not add due to rounding

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IBM CASH FLOW ANALYSIS

(\$B)	<u>1H04</u>	<u>FY04</u>	<u>1H05</u>
Net Cash from Operations (Cont. Ops.)	7.4	15.3	5.2
Less: GF Accounts Receivable	<u>4.0</u>	<u>2.5</u>	<u>3.8</u>
Net Cash from Operations (Cont. Ops.), excl. GF Rec.	3.5	12.9	1.5
Investing Activities			
Capital Expenditures, Net	(1.7)	(3.7)	(2.0)
GF A/R	4.0	2.5	3.8
GF Debt	<u>(1.5)</u>	<u>(1.7)</u>	<u>(0.5)</u>
Net GF Debt to A/R	2.4	0.7	3.3
Acquisitions	(0.8)	(1.7)	(1.1)
Divestitures	0.0	0.0	0.5
Return to Shareholders			
Share Repurchase	(3.1)	(7.1)	(5.2)
Dividends	(0.6)	(1.2)	(0.6)
Change in Non-GF Debt	0.1	0.7	1.7
Other	0.8	2.5	0.0
Discontinued Operations	<u>(0.1)</u>	<u>(0.1)</u>	<u>0.0</u>
Change in Cash & Marketable Securities	0.5	2.9	(1.9)

May not add due to rounding

IBM BALANCE SHEET

(\$B)	June <u>2004</u>	Dec <u>2004</u>	June <u>2005</u>
Cash & Marketable Securities	8.2	10.6	8.7
Non-GF Assets*	62.9	66.7	66.8
Global Fin. Assets*	<u>30.2</u>	<u>33.7</u>	<u>27.9</u>
Total Assets	101.3	111.0	103.4
Other Liabilities	48.7	56.4	49.5
Non-GF Debt	0.6	0.6	2.8
Global Financing Debt	<u>21.3</u>	<u>22.3</u>	<u>20.9</u>
Total Debt	<u>21.9</u>	<u>22.9</u>	<u>23.7</u>
Total Liabilities	70.6	79.3	73.3
Equity	30.7	31.7	30.1
Non-GF Debt/Cap	2%	2%	10%
Global Fin. Leverage	7.0	7.0	6.7

* Excluding Cash & Marketable Securities

May not add due to rounding

IBM SEGMENT RESULTS

(\$B)	<u>Global Svcs</u>	<u>Sys & Tech</u>	<u>Pers Comp</u>	<u>Soft-ware</u>	<u>Global Fin</u>	<u>Ent Invest</u>	<u>Total IBM*</u>
Revenue							
External	12.0	4.9	0.6	3.8	0.6	0.3	22.3
Internal	0.8	0.3	--	0.5	0.3	--	0.0
Total Revenue	12.8	5.1	0.6	4.3	0.9	0.3	22.3
PTI	(0.1)	0.3	(0.1)	1.0	0.3	(0.1)	2.7
PTI Margin	(0.7%)	5.7%	(26.4%)	22.2%	37.8%	(22.0%)	12.3%
Incr Restructuring	1.2	0.1	0.0	0.1	0.0	0.0	1.7
PC Sale/MSFT Settlement							(1.9)
PTI w/o Non-Recurring	1.1	0.4	(0.1)	1.0	0.3	(0.1)	2.6
PTI Margin w/o Non-Recurring	8.5%	8.2%	(26.4%)	24.4%	38.9%	(20.4%)	11.7%

Segment results include:

- Equity compensation
- Organizational change – Retail Store Solutions and Printing Systems to S&TG
- BAU restructuring

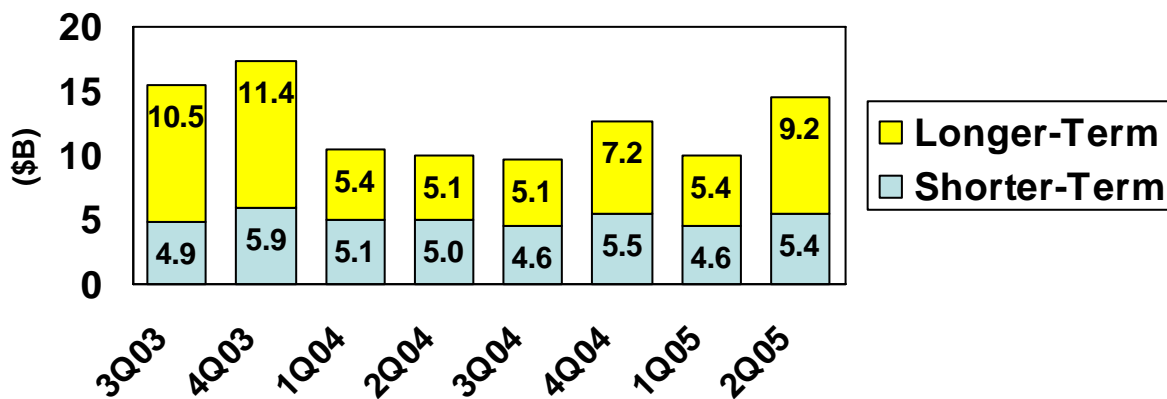
* Total IBM includes activity recorded above segments

GLOBAL SERVICES

Revenue \$12.0B, +6%; 4% @CC

(\$B)	2Q05	Yr/Yr	Yr/Yr @CC
Revenue	12.0	6%	4%
PTI Margin w/o Incr Restructuring	8.5%	0.8 pts	
PTI Margin As Reported	(0.7%)	(8.4 pts)	
Revenue			
Strategic Outsourcing		5%	2%
Business Consulting Services		9%	7%
Integrated Tech Services		5%	2%
Maintenance		5%	2%

IGS WW Contract Signings



2Q05 Signings	Yr/Yr
SO	80%
ITS	6%
BCS	30%
C&SI	4%
BTO	192%

SYSTEMS & TECHNOLOGY

Revenue \$4.9B, +5%; 3% @CC

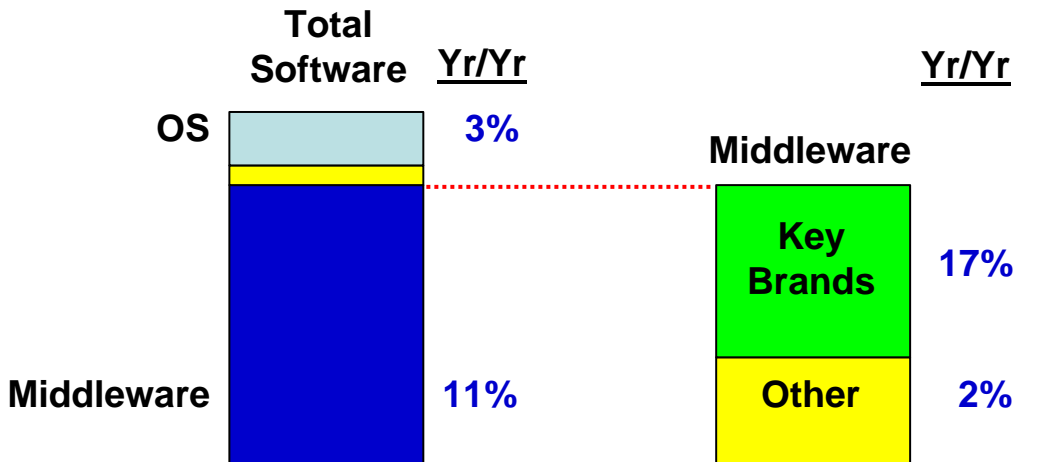
2Q05 Revenue

As Rptd @CC GP% Share

zSeries	(24%)	(25%)	+	-	3Q product announcement
iSeries	10%	9%	-	+	Growth in all geos, Strength in high-end
pSeries	36%	34%	+	+	Double-digit growth in all geos
xSeries Servers	11%	8%	-	=	Continued blade leadership
Total Storage	19%	17%	-	+	Double-digit disk & tape growth
Microelectronics	(5%)	(5%)	+		Product transition to gaming
E&TS	37%	36%	+		7 th quarter of double-digit growth
Printing Systems	(3%)	(5%)	+		Maintenance decline
Retail Store Sols	(19%)	(20%)	-		Large customer deferrals

SOFTWARE

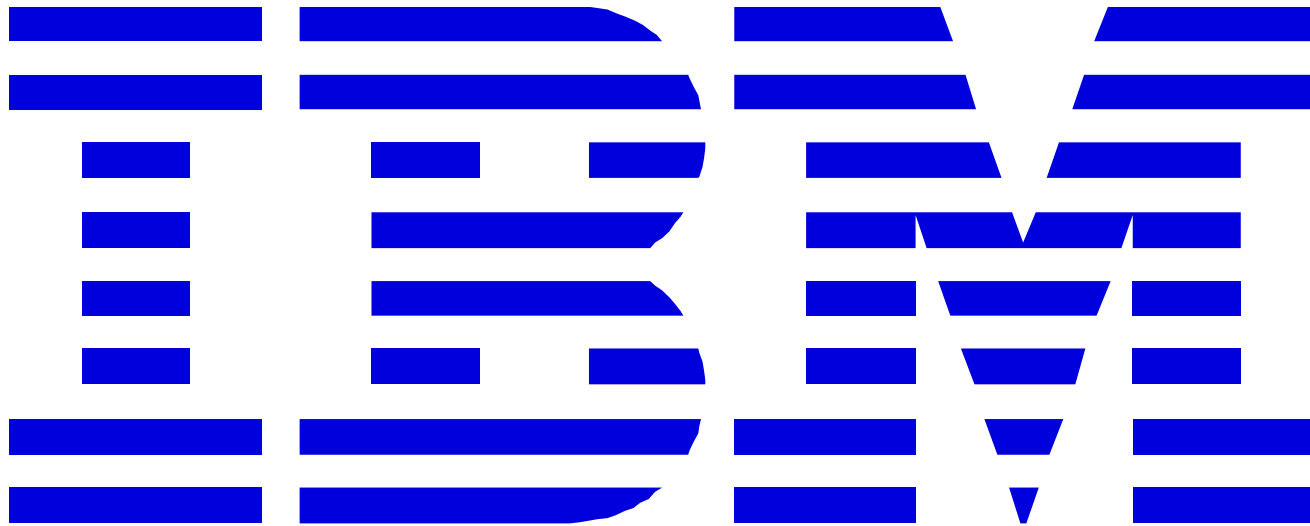
Revenue \$3.8B, +10%; 7% @CC



Brand	Yr/Yr	Yr/Yr @CC
WebSphere Family	18%	14%
Information Mgmt	15%	11%
Lotus	17%	14%
Tivoli	28%	25%
Rational	8%	5%
Other Middleware	2%	(1%)

	2Q05	Yr/Yr
GP Margin	86.7%	+0.5 pts

- Strength in Americas and Asia
- Gained or held market share in key segments



-S1-

PC RESULTS

	<u>PC Business As Reported</u>	<u>Internal Rev / GP*</u>	<u>Internal IT Uplift*</u>	<u>Net Allocations**</u>	<u>Est PC Direct</u>
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2Q04

Revenue

External	2679				2679
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Internal	31	(31)			
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PTI	(10)	(6)	24	37	45
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2Q05

Revenue

External	557				557
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Internal	7	(7)			
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PTI	(149)	(2)	8	7	(136)
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* Intercompany sales and profits eliminated in consolidation

** Allocations in support of PC operations which are not contractually recoverable under Lenovo relationship and effectively remain with IBM

See non-GAAP reconciliation for additional description, chart S8

-S2-

EQUITY-BASED COMPENSATION

Pre-Tax (\$M)	<u>1Q04</u>	<u>1Q05</u>	<u>B/(W) Yr/Yr</u>	<u>2Q04</u>	<u>2Q05</u>	<u>B/(W) Yr/Yr</u>
Stock Options*	291	228	63	303	221	82
Empl. Stock Purchase Plan*	<u>49</u>	<u>18</u>	<u>31</u>	<u>54</u>	<u>0</u>	<u>54</u>
Sub-Total	340	246	94	357	221	136
RSUs / Performance Units	57	41	16	38	42	(4)
Total w/o Non-Recurring	396	286	110	394	263	131
Non-Recurring**					(12)	12
Total Equity Comp	396	286	110	394	251	143

* Expensed beginning 1Q05. Employee Stock Purchase Plan rendered non-compensatory in 2Q05

** Forfeitures credited to PC sale (\$12M) and incremental restructuring (\$3M) for stock options; forfeitures credited to incremental restructuring (\$1M) and award modification charges to PC sale of \$4M for RSUs / Performance Units

May not add due to rounding

CURRENCY: YEAR-TO-YEAR COMPARISON

QUARTERLY AVERAGES PER US\$

	<u>1Q05</u>	<u>2Q05</u>	<u>7/15/05 Spot</u>	<u>@ 7/15/05 Spot</u>	
				<u>3Q05</u>	<u>4Q05</u>
Euro	0.76	0.79	0.83		
Yr/Yr	5%	4%		-1%	-7%
Pound	0.53	0.54	0.57		
Yr/Yr	3%	3%		-3%	-6%
Yen	105	108	112		
Yr/Yr	2%	2%		-2%	-6%
IBM Revenue Impact	3 pts	2 pts		0 pts	-3 pts

Negative Yr/Yr growth signifies a translation hurt

-S4-

IBM CASH FLOW (FAS 95)

(\$B)	<u>1H04</u>	<u>FY04</u>	<u>1H05</u>
Net Cash from Continuing Operations	3.1	7.5	3.3
Depreciation / Amortization	2.4	4.9	2.6
Stock-based Compensation Expense	0.8	1.6	0.5
Working Capital / Other	(2.8)	(1.1)	(5.0)
GF A/R	<u>4.0</u>	<u>2.5</u>	<u>3.8</u>
Net Cash provided by operating activities	7.4	15.3	5.2
Cash Expenditures, Net	(1.7)	(3.7)	(2.0)
Divestitures	0.0	0.0	0.5
Acquisitions	(0.8)	(1.7)	(1.1)
Other Investing	<u>(0.1)</u>	<u>0.1</u>	<u>0.6</u>
Net cash used in investing activities	(2.6)	(5.3)	(2.0)
GF Debt	(1.5)	(1.7)	(0.5)
Non-GF Debt	0.1	0.7	1.7
Dividends	(0.6)	(1.2)	(0.6)
Share Repurchase	(3.1)	(7.1)	(5.2)
Other	<u>0.9</u>	<u>1.8</u>	<u>0.5</u>
Net cash used in financing activities	(4.2)	(7.6)	(3.9)
Effect of exchange rate changes on cash	(0.1)	0.4	(0.7)
Discontinued Operations	(0.1)	(0.1)	0.0
Net Change in Cash & Cash Equivalents (Cont. Ops.)	0.4	2.8	(1.4)

May not add due to rounding

IBM CASH FLOW (FAS 95) - QUARTER

(\$B)	<u>2Q04</u>	<u>2Q05</u>
Net Cash from Continuing Operations	1.7	1.9
Depreciation / Amortization	1.2	1.3
Stock-based Compensation Expense	0.4	0.3
Working Capital / Other	(0.3)	(1.1)
GF A/R	<u>0.8</u>	<u>0.7</u>
Net Cash provided by operating activities	3.8	3.1
Cash Expenditures, Net	(0.8)	(1.1)
Divestitures	0.0	0.5
Acquisitions	(0.8)	(0.9)
Other Investing	<u>0.6</u>	<u>0.1</u>
Net cash used in investing activities	(0.9)	(1.3)
GF Debt	(1.3)	(0.5)
Non-GF Debt	0.1	0.9
Dividends	(0.3)	(0.3)
Share Repurchase	(1.3)	(1.6)
Other	<u>0.3</u>	<u>0.2</u>
Net cash used in financing activities	(2.5)	(1.3)
Effect of exchange rate changes on cash	(0.1)	(0.4)
Discontinued Operations	0.0	0.0
Net Change in Cash & Cash Equivalents (Cont. Ops.)	0.3	0.0

May not add due to rounding

-S6- IBM CASH FLOW ANALYSIS - QUARTER

(\$B)	<u>2Q04</u>	<u>2Q05</u>
Net Cash from Operations (Cont. Ops.)	3.8	3.1
Less: GF Accounts Receivable	<u>0.8</u>	<u>0.7</u>
Net Cash from Operations (Cont. Ops.), excl. GF Rec.	3.0	2.4
Investing Activities		
Capital Expenditures, Net	(0.8)	(1.1)
GF A/R	0.8	0.7
GF Debt	<u>(1.3)</u>	<u>(0.5)</u>
Net GF Debt to A/R	(0.5)	0.2
Acquisitions	(0.8)	(0.9)
Divestitures	0.0	0.5
Return to Shareholders		
Share Repurchase	(1.3)	(1.6)
Dividends	(0.3)	(0.3)
Change in Non-GF Debt	0.1	0.9
Other	0.3	(0.1)
Discontinued Operations	<u>0.0</u>	<u>0.0</u>
Change in Cash & Marketable Securities	(0.3)	0.0

May not add due to rounding

NON-GAAP FINANCIAL MEASURES

- **In an effort to provide investors with additional information regarding the Company's results as determined by generally accepted accounting principles (GAAP), the Company also discloses the following non-GAAP information which management believes provides useful information to investors:**
 - **Management has presented certain financial results excluding the effects of (1) the gain on the sale of the company's PC business, (2) a gain related to a settlement agreement reached with Microsoft and (3) charges related to the company's restructuring initiatives. Given the unique and non-recurring nature of these items, management believes that presenting certain financial information without these items is more representative of the company's operational performance and provides additional insight into, and clarifies the basis for, historical and/or future performance, which may be more useful for investors.**

NON-GAAP FINANCIAL MEASURES (cont.)

- **On April 30, 2005, IBM sold its PC business. IBM's reported results include operational performance of the company's PC business for (a) one month in the quarter ended June 30, 2005, as compared to three months in comparable period of the prior year and (b) four months in the six month period ended June 30, 2005, as compared to six months in the comparable period of the prior year. Management believes that it is important to investors to understand the financial results of the company adjusted for the impact of its divested PC operations in order to show IBM's results on a comparable basis year-to-year, and to best present ongoing operational performance. Accordingly, management has presented certain financial results excluding the effects of the PC business.**

In accordance with segment reporting, revenues and pre-tax income include transactions between segments that are intended to reflect an arm's-length transfer price and include intercompany profit. Management believes that a more appropriate measure of the financial impacts that the divestiture of the PC business has on IBM's consolidated financial results should exclude any revenues associated with internal sales and intercompany profits, which are eliminated in consolidation. Accordingly, the results of the PC business have been adjusted from the reported PC segment. The basis for these adjustments are to give effect to intercompany and certain allocated expenses and the adjusted results are intended to display the impact on the IBM consolidated results on a basis comparable to which the company operates post-PC divestiture which management believes is meaningful and useful to investors.

NON-GAAP FINANCIAL MEASURES (cont.)

- **Management includes a presentation of cash flows that excludes the effect of Global Financing Receivables and subtracts net capital investments from Net Cash from Operations. For a financing business, increasing receivables is the basis for growth. Receivables are viewed as an investment and an income-producing asset. Capital investments are necessary to grow and sustain the business. Therefore, management presents financing receivables as an investing activity, which has the effect of lowering cash from operations, and net capital investments as a reduction of Net cash from Operations. Management's view is that this presentation gives the investor the best perspective of cash available for investment or for distribution to shareholders.**
- **Management refers to growth rates at constant currency or adjusting for currency so that the business results can be viewed without the impact of changing foreign currency exchange rates, thereby facilitating period-to-period comparisons of the Company's businesses performance. Generally, when the dollar either strengthens or weakens against other currencies, the growth at constant currency rates or adjusting for currency will be higher or lower than growth reported at actual exchange rates.**

NON-GAAP FINANCIAL MEASURES (cont.)

- **The complexity and volatility associated with the accounting and financial reporting for pension plans has been a major focus of the Company's management and investors. To help investors better understand the estimates, judgments and performance of the plans, in the 2004 Annual Report, the Company provided significant disclosures. Management has presented forecasted pension expense excluding a one-time charge recorded in 2004 for the partial settlement of certain legal claims related to IBM's pension plan. Given the unique and non-recurring nature of this charge, management believes that presenting such financial items without the charge is useful to investors in better understanding the Company's business performance. The Company believes the magnitude of these impacts can affect investors' understanding of the Company's overall business performance. Management further believes that investors' understanding is enhanced when the year-to-year dynamics associated with pension cost is rendered explicit in the discussion of the Company's earnings and cash flows. Therefore, while giving appropriate prominence to the GAAP based financial measures in presenting earnings and cash flows, the Company believes it is appropriate and useful to investors to include certain non-GAAP measures.**

RECONCILIATION TO NET CASH FROM OPERATIONS EXCLUDING GF RECEIVABLES AND INCLUDING NET CAPITAL INVESTMENTS

(\$B)	<u>1H05</u>	<u>Yr/Yr</u>
Net Cash from Operations (Cont. Ops.), excl GF Rec, incl Net Capital Investments	<u>(0.6)</u>	<u>(2.3)</u>
Less: Net Capital Investments	<u>(2.0)</u>	<u>(0.3)</u>
Net Cash from Operations (Cont. Ops.), excl GF Rec	1.5	(2.0)
Plus: GF Accounts Receivable	<u>3.8</u>	<u>(0.2)</u>
Net Cash from Operations (Cont. Ops.)	5.2	(2.2)

May not add due to rounding

-S12-

RECONCILIATION OF INCREASE IN PENSION EXPENSE

(\$M)

2004-2005
Estimated

Increase in Pension Expense

707

One-time Pension Settlement Charge (2004)

320

Increase in Pension Expense, excluding
One-time Pension Settlement Charge

1027

RECONCILIATION OF GROWTH IN EMERGING COUNTRIES

	<u>2Q05</u>
Revenue growth in Emerging Countries, as reported	(5%)
Effects of sale of PC business	<u>28%</u>
Revenue growth in Emerging Countries, without PC business	23%

