

**As Prepared**

**Ginni Rometty  
Chairman, President and Chief Executive Officer  
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I will now provide a report on your company.

For more than a century, IBM has distinguished itself by creating leading-edge information technology and applying it to change business and society. In this way, we become essential to our clients, generate attractive returns for our investors, and provide meaningful and rewarding careers for our people.

This also compels us to continuously reinvent IBM – our products and services, as well as our operations, workforce and culture. Dozens and dozens of competitors have come and gone throughout our history. Your company is alone in having emerged as a leader, era after era.

As you know, over the past several years we have undertaken a top-to-bottom transformation – arguably the most extensive in our history.

Years ago, we came to believe that the IT industry would radically re-order, driven by the phenomenon of data... the maturation of cloud computing... and the emergence of what many call artificial intelligence, or AI.

We were convinced that the source of value – for our clients and for you, our owners – would shift. So, over the past three years...

- We got out of commoditizing businesses – which trimmed \$8 billion from our top-line (and nothing from our bottom line).
- We reinvented our core hardware, software and services franchises.
- And we invested to create and grow new businesses – our strategic imperatives of cloud, data, cognitive and security.

As a result of this transformation, we made substantial progress last year. Our strategic imperatives have reached critical mass. At \$33 billion, they contribute 41 percent of IBM's revenue. They continue to show double-digit growth, and we're on pace to achieve our goal of growing these businesses to \$40 billion by 2018.

In 2016, our cloud business grew at 35 percent, to \$13.7 billion. Cloud by itself is now more than 17 percent of our total revenues. Our as-a-Service exit run-rate was \$8.6 billion, up 61 percent for the year.

For the 24th year in a row, IBM led in U.S. patents earned, becoming the first company ever to break the 8,000 mark.

And we returned \$8.8 billion to you, including dividends of \$5.3 billion and \$3.5 billion in gross share repurchases. With today's announcement of an increase in our quarterly dividend from \$1.40 to \$1.50 – an increase of 7 percent – we marked our 22nd consecutive year of raising our dividend and our 102nd year of paying one.

Our goal throughout was to build the integrated capability that our clients would need for a new era of technology and business. And we worked just as hard to transform our operations and culture for

a marketplace where speed, innovation and agility determine winners and losers.

A strong foundation is now in place.

Of course, as our history has taught us, transformation is a way of life in our industry, and we know what it takes.

Most of all, it takes perseverance and unwavering confidence in your strategy. We have both. We know our business and our clients intimately, and we know that they are with us on this journey. As the leader of this great company and its nearly 380,000 employees, I am confident that the investments we have been making will yield superior rewards for you, our shareholders, for many years to come. Our transformation will succeed.

Here's why.

**First, as I said, we have built a strong foundation.**

We continue to transform IBM's core businesses.

- Global Technology Services continues to be the market leader in IT services, because it continues to reinvent what it offers to clients and how it manages and delivers technology services.
- Global Business Services continues to reinvent itself, and is growing robustly where we have created new practices.
- Our mainframe business continues to inject new technology into the platform – from Linux to machine learning. This is why installed mainframe capacity has increased 20 times in the past 20 years – and is still growing. I call mainframe our youngest oldest business.

At the same time, we have created a powerful new platform – the IBM Cloud. There’s nothing else like it in our industry. It is “enterprise strong” – from its global footprint and unmatched security to its support for regulated industries like financial services and healthcare. But what truly differentiates the IBM Cloud is that it’s optimized for data and artificial intelligence.

I have often said that data is the world’s new natural resource and the new basis for competitive advantage. This is why, in addition to a cloud that is enterprise-strong, the IBM Cloud has a ‘data-first’ architecture and is cognitive at its core.

No other cloud has Watson, which has become the AI platform for business. By the end of this year, Watson will touch one billion people in some way.

What we started off with one function – Watson’s ability to answer questions – has become a broad and expanding range of capabilities:

Watson can “see” better than any other AI system: It can automatically describe the contents of an image – e.g., recognizing melanoma from skin lesion images with 95% accuracy.

- Watson can “hear,” understanding speech almost as well as humans.
- Watson can “read” 12 languages (90% of the global internet population).
- Watson can “feel” impulses from sensors in elevators, buildings, autos and even ball bearings.

And we continue to add new capabilities to the IBM Cloud.

- One is Blockchain, which will do for trusted transactions what the Internet has done for information. Blockchain facilitates the transfer of any asset – whether a physical asset like a shipping container, a financial asset like a bond, or a digital asset like music – by creating a secure digital ledger that can be shared across any business network. IBM has already worked with more than 400 clients to pioneer blockchain for business.
- And looking farther ahead, IBM Q is the first commercially available quantum computing capability, which will be delivered only on the IBM Cloud. Quantum holds the promise of exponentially increasing computing power – and it will only be accessible via the cloud. Why? It operates 1,000 times colder than outer space. A company would find that tough to put on-premises!

**Now, on this powerful new platform, we, our clients and our partners are building new solutions and businesses – which is my second reason for confidence in our transformation.**

Our own company has in recent years built new businesses focused on industries and professions -- IBM Watson Health, IBM Watson IoT, IBM Watson Financial Services.

And our clients are using our platform to innovate in world-changing ways.

- They are transforming the treatment of disease.
  - At the University of North Carolina, Watson found diagnoses and treatments expert oncologists had not spotted for 30 percent of cancer patients.

- Barrow Neurological Institute in Phoenix, Arizona used Watson for a breakthrough in ALS – aka Lou Gehrig's Disease. They identified five genes that had never been linked to this complex and deadly disease.
- They are transforming financial services...
  - From currency exchange, where CLS is using IBM Blockchain to take friction out of the world's largest financial market, at \$5 trillion daily...
  - ... to individual tax preparation, where H&R Block is using Watson to help their 70,000 tax advisors get maximum refunds for customers.
- They are optimizing global supply chains.
  - WalMart is using IBM Blockchain to track the movement of pork in China to ensure food safety.
  - Maersk is using IBM Blockchain to largely eliminate paperwork – which today costs as much as the actual shipping of, say, flowers, from Africa to Rotterdam.
- They are transforming transportation.
  - GM is integrating Watson into OnStar to make every car a cognitive information system.
  - BMW is working on new intelligent driver assistant technologies.
- And a new generation of entrepreneurs is innovating in amazing ways.

- For example, Stanford student Josh Barrow created an app called DoNotPay, which identified legal precedents to save motorists about \$5 million in parking fines.

All of this momentum – with clients, developers and startups -- is possible because these solutions are built upon our core franchises in systems, software and services. We could not scale without them.

**But something else is needed for the promise of this new era to be realized... and this leads to my third and final reason for confidence in our transformation.**

As IBM has done with every new era of innovation, we take seriously our responsibility to ensure that the new technology is adopted in ways that are both ethical and enduring.

This is why, in January, we issued “Principles for Transparency and Trust in the Cognitive Era.” Its core tenets are:

- IBM believes AI’s purpose is to augment human intelligence.
- IBM will be transparent about when and where AI is being applied, and about the data and training that went into its recommendations. Core to this is our staunch belief that our clients’ data will not be shared or monetized – except by them. Their data is their data.
- Finally, IBM is committed to helping students, workers and citizens acquire the skills to engage safely, securely and effectively with cognitive systems, and to do the new kinds of work that will emerge in a cognitive economy.

Our breakthrough P-TECH schools are a great example of leading the development of what we call “new collar” skills, essential for the jobs of the future. What began as one school in Brooklyn six years ago will soon be 100 around the U.S. and abroad – with plans to expand significantly. Thousands of lives have been transformed – including those of ten bright graduates whom we’ve already hired at IBM.

Going forward, these principles will be the touchstone for everything we do to build this new world – a world that is not about machines replacing humans... but about the new capabilities that are enabling every professional and every enterprise to realize their aspirations and do their life’s work.

Today, tens of thousands of entrepreneurs, innovators and other leaders from business, government, healthcare and civil society are working with Watson to transform their industries and sectors.

As IBM has done throughout its history, we remain dedicated to creating a world that is healthier, more secure and less wasteful; more productive, more personalized and more sustainable; more diverse, more tolerant and more just.

I hope you share our optimism about your company. And I am deeply grateful to the entire IBM team for bringing us to this point, and to you, our shareholders, for your support.