

# IBM Investor Briefing 2019



# Introduction

IBM  
Investor  
Briefing  
2019

## **Patricia Murphy**

Vice President, Investor Relations  
IBM



# Agenda

## Friday, August 2

### 10AM – 12:15PM

IBM + Red Hat: Strategic Overview

**Ginni Rometty**

Chairman, President and CEO, IBM

IBM + Red Hat: Better Together

**Jim Whitehurst**

Senior Vice President, IBM and CEO, Red Hat

**Arvind Krishna**

Senior Vice President, IBM Cloud & Cognitive Software

**Mark Foster**

Senior Vice President, IBM Services and Global Business Services

**Martin Schroeter**

Senior Vice President, IBM Global Markets

IBM + Red Hat Financial Profile

**James Kavanaugh**

Senior Vice President and Chief Financial Officer, IBM

Q&A

With IBM Senior Executives



# Forward-looking statements and non-GAAP information

Certain comments made in this presentation may be characterized as forward looking under the Private Securities Litigation Reform Act of 1995. Forward-looking statements are based on the company's current assumptions regarding future business and financial performance. Those statements by their nature address matters that are uncertain to different degrees. 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 filings with the SEC. Copies are available from the SEC, from the IBM web site, or from IBM Investor Relations. Any forward-looking statement made during this presentation speaks only as of the date on which it is made. Except as required by law, the company assumes no obligation to update or revise any forward-looking statements. These charts and the associated remarks and comments are integrally related, and are intended to be presented and understood together.

In an effort to provide additional and useful information regarding the company's (IBM's) historical results and forward-looking financial information on a continuing operations basis, as determined by generally accepted accounting principles (GAAP), these materials contain non-GAAP financial measures. Additionally, these materials contain certain non-GAAP financial measures regarding Red Hat's historical financial results.

The company is unable to provide, without unreasonable efforts, certain forward-looking information as determined by GAAP, including expectations for gross profit margin, pre-tax income and diluted earnings per share.

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# IBM + Red Hat: Strategic Overview

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## **Ginni Rometty**

Chairman, President and CEO  
IBM



smart  
is  
open.



open  
is  
smart.

# IBM + Red Hat: Better Together

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## **Jim Whitehurst**

Senior Vice President, IBM and CEO, Red Hat

## **Arvind Krishna**

Senior Vice President, IBM Cloud & Cognitive Software

## **Mark Foster**

Senior Vice President, IBM Services and Global Business Services

## **Martin Schroeter**

Senior Vice President, IBM Global Markets



# Better Together: Red Hat

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## **Jim Whitehurst**

Senior Vice President, IBM  
and CEO, Red Hat





# Value of a platform in open source

Open source **projects** are  
winner takes all



Linux



FreeBSD®



GlassFish

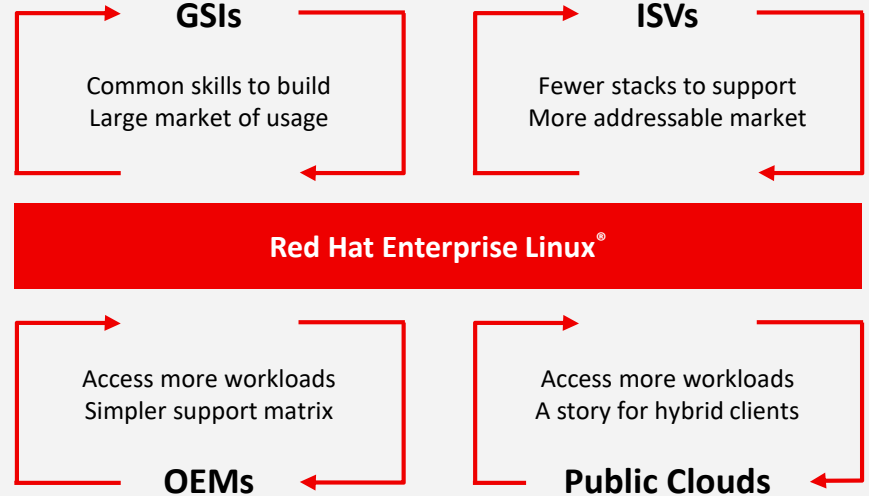


apachecloudstack  
open source cloud computing



Apache  
MESOS™

Successful **product** becomes the  
reference standard (e.g. Linux)



# From servers to hybrid cloud

## LINUX

Red Hat Enterprise Linux =  
default choice for the operating system (OS)



Physical

Physical

Virtual



## CONTAINERS & KUBERNETES

OpenShift =  
default choice for hybrid cloud



Physical

Virtual

Private clouds

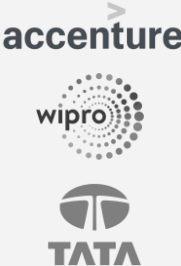
Public clouds

From OS to hybrid cloud = **10x** opportunity

# IBM acceleration of our hybrid, multicloud platform creates opportunity across the ecosystem

### SI/VARs

New **transformation** and **application development** opportunities



### ISVs

Ability to address **new** and **migrating** workloads



### On-premise infrastructure

**New** and **migrated** workloads



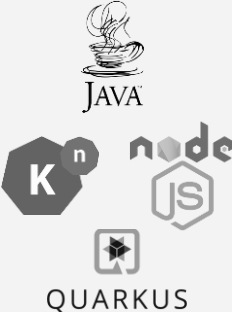
### Public Clouds

Additional workloads, especially **mission critical**



### Developers

Write **once**, run **anywhere**



# Have an early lead, IBM can propel Red Hat

We have early hybrid cloud platform leadership



MODERNIZE APPS

MULTICLOUD



WEB APPS

AI & ML

CLOUD-NATIVE DEV



MOBILE

DATA & ANALYTICS

IoT

IBM brings massive momentum around workloads

**IBM's commercial organizations** drive trial, adoption, marquee customers across its installed base

**IBM software** on OpenShift drives platform adoption and usage

**GBS** migrates and builds new workloads on OpenShift

**GTS** stands up and runs OpenShift at scale

**Systems** drives adoption on IBM platforms

...and will accelerate innovation in the platform



# Better Together: Sell More Software

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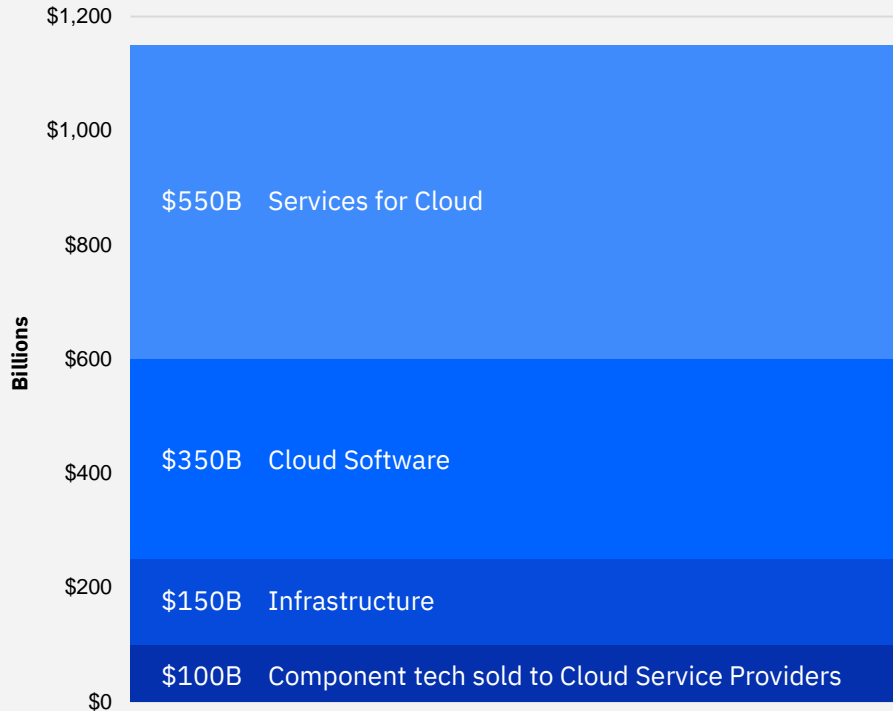
## **Arvind Krishna**

Senior Vice President

IBM Cloud & Cognitive Software



# IBM is the leading provider in a \$1.2 trillion hybrid cloud opportunity



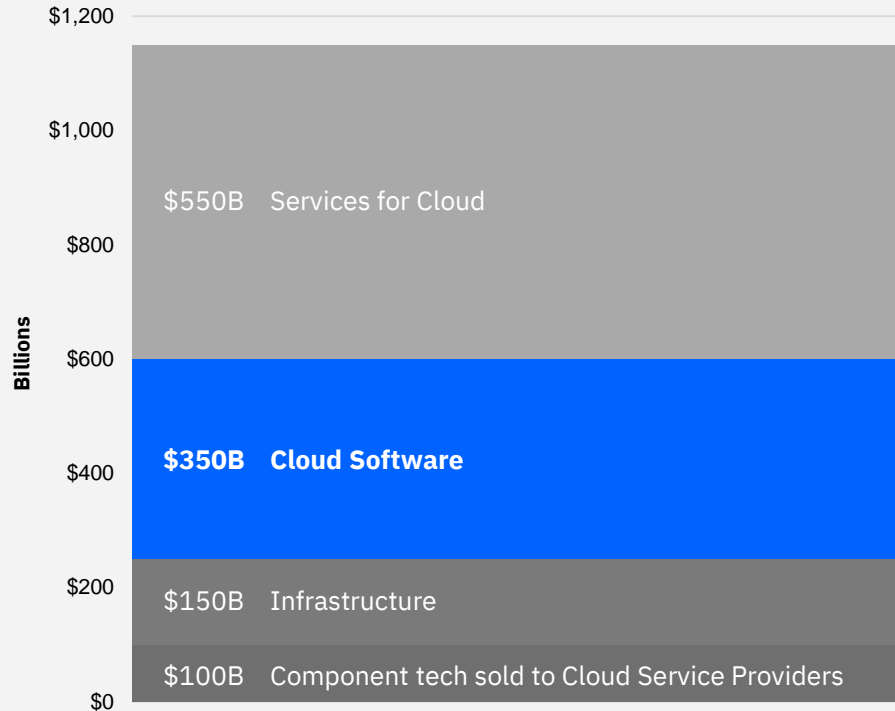
**92%**  
of enterprises have hybrid environments\*

**58%**  
of enterprises have multicloud environments\*

**10%**  
of enterprises with hybrid environments are able to support holistic management and agile movement of applications across environments\*

**50%**  
of enterprises will have moved to 'write once, run anywhere' hybrid and multicloud environments by 2023\*

# IBM Cloud Software becomes the fuel of growth and innovation



## How IBM drives more software revenue:

### Middleware anywhere

Making IBM software cloud native – for private and public clouds

### Preferred destination for mission-critical workloads

Red Hat OpenShift on IBM Cloud is the best end-to-end stack

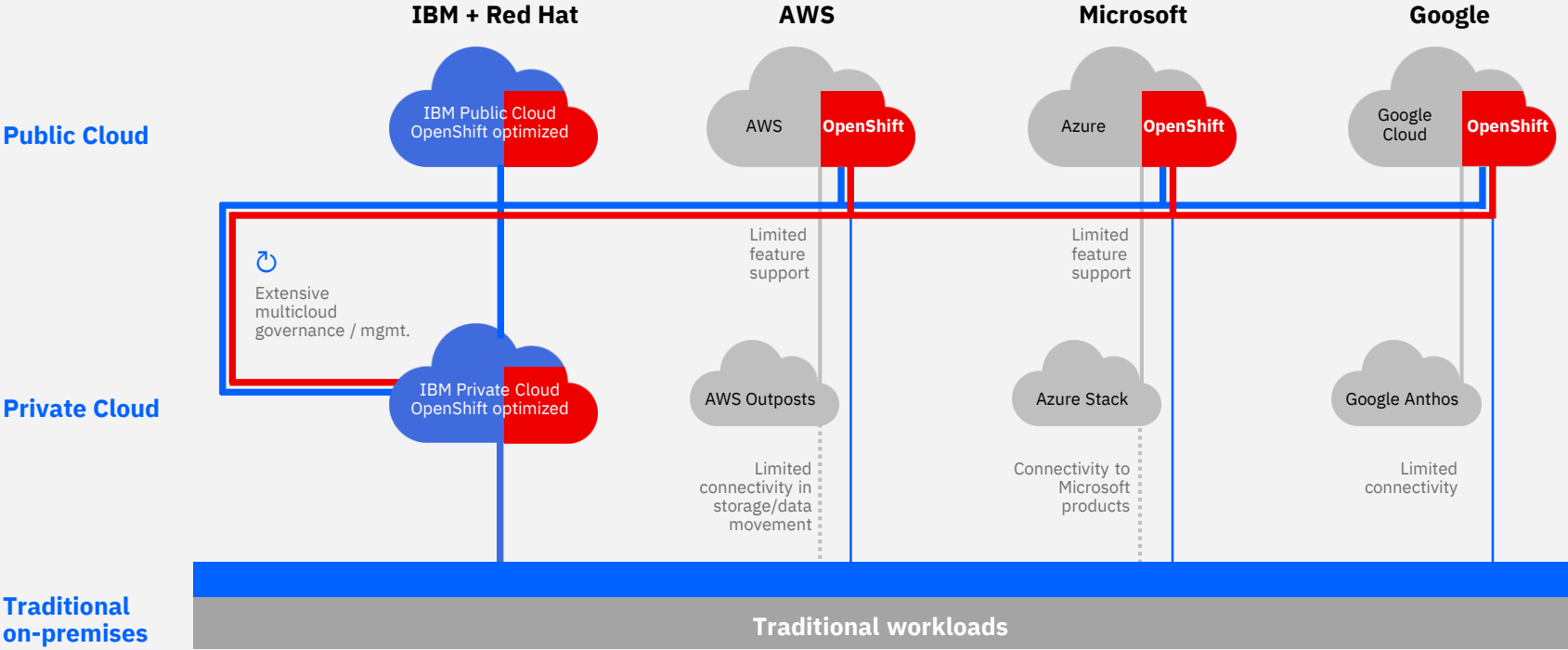
### IBM creates more opportunities for Red Hat

IBM will drive more Red Hat software through strategic solutioning and integration

### New workloads

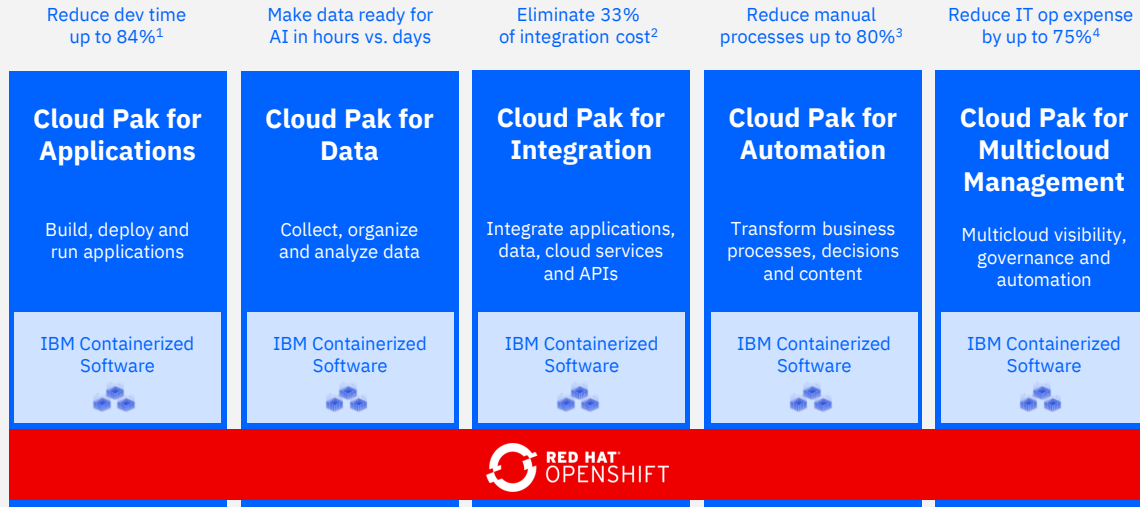
Our hybrid cloud strategy positions us to capture strategic new workloads

# IBM + Red Hat deliver the industry's only true hybrid multicloud platform





# Making IBM's key software products cloud native for all clouds – middleware anywhere



Certifying more than 100 software products on Red Hat

Optimized for Red Hat OpenShift

Instant deployment on IBM Cloud

Consistent management – runs on all public and private clouds

Available on all architectures; coming to IBM Z in 4Q'19



On-premises



Private Cloud



IBM Public Cloud



AWS



Microsoft Azure

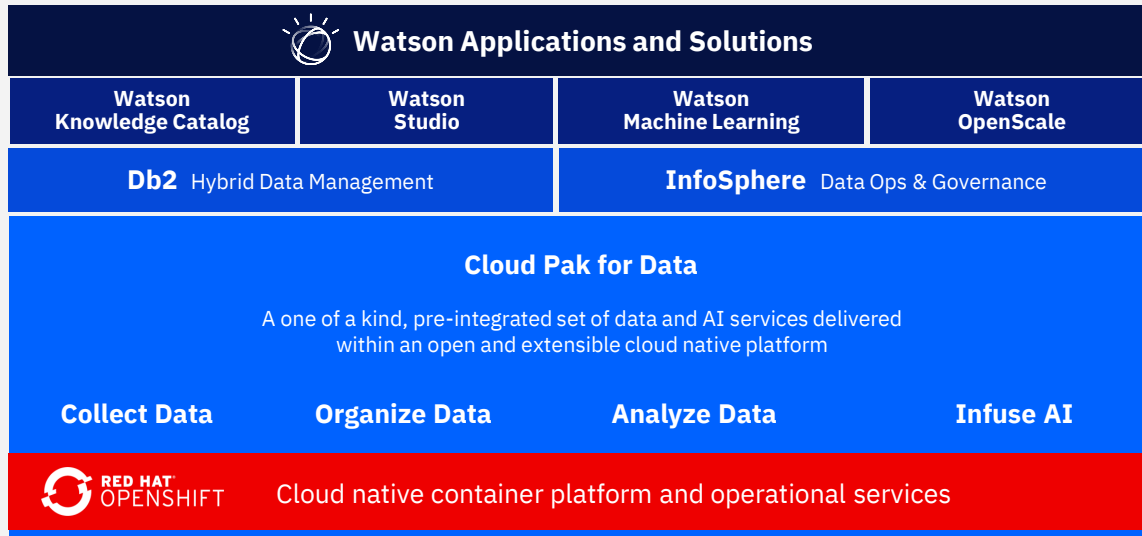


Google Cloud



Edge

# A deeper look: Cloud Pak for Data



## Full data and AI lifecycle platform for hybrid workloads

Allows clients to:

Virtualize their data 500% faster<sup>1</sup>

Reduce data prep time by 80%<sup>2</sup>

Automate 80% of data science effort  
with AutoAI<sup>3</sup>

Deploy where the data resides,  
in hours vs. days<sup>4</sup>



On-premises



Private Cloud



IBM Public Cloud



AWS



Microsoft Azure



Google Cloud



Edge

# The preferred destination for mission-critical workloads is Red Hat OpenShift on IBM Cloud



**IBM Public Cloud**

## **Enterprise proven**

IBM Cloud is only public cloud developed with Kubernetes — fundamental to IBM businesses and used by more than 1,000 clients. Our public cloud manages over 16,000 production Kubernetes clusters today.

## **Secure and compliant**

Built-in container level security, isolation, bare metal support and broad industry compliance (PCI, HIPAA, etc.)

## **Automated global resiliency**

Built-in load balancing and multizone availability for simplified management and resiliency. Available in six global multizone regions and 35 datacenters.

## **Instant deployment**

Cloud Paks are pre-loaded and certified for IBM's public cloud

# IBM's hybrid cloud strategy positions us for >\$50B in strategic new workloads



**AI/Machine Learning**



**Robotic Process Automation**



**5G/Telco**



**IoT**



**Location-based Services**



**Augmented Analytics**



**Blockchain**



**Wearables**

## Cloud Paks



On-premises



Private Cloud



IBM Public Cloud



AWS



Microsoft Azure



Google Cloud



Edge

# Sell More Software: Summary

Making IBM software cloud native – for all private and public clouds

Red Hat OpenShift on IBM Cloud is the best end-to-end stack for mission-critical workloads

IBM will drive more Red Hat software through strategic solutioning and integration

IBM's hybrid cloud strategy positions us to capture new workloads

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**Cloud & Cognitive Software accelerating to double-digit revenue growth in 2020, enhanced by Red Hat**

# Better Together: Sell More Services

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## **Mark Foster**

Senior Vice President

IBM Services and Global Business Services

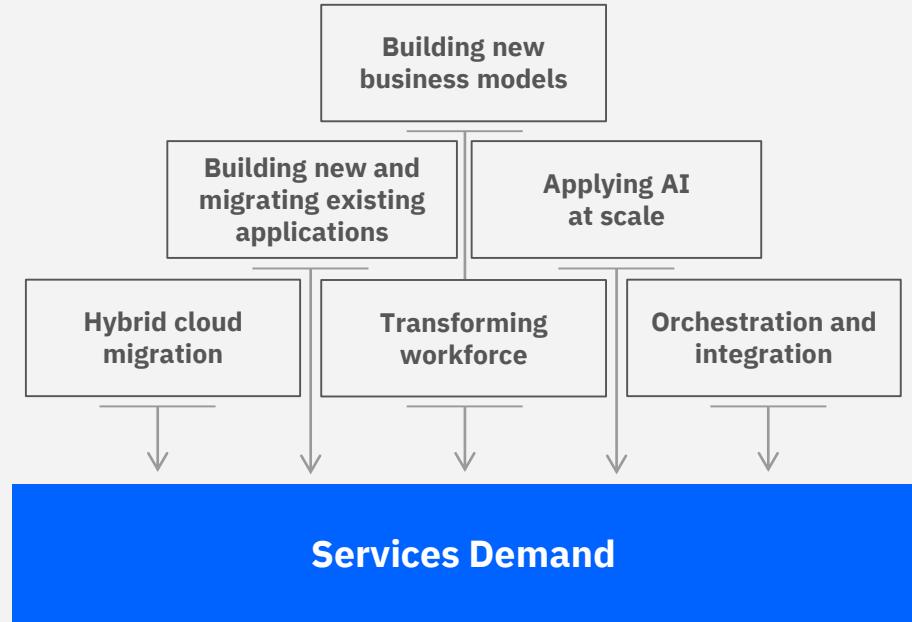


# In Chapter 2, there is significant demand for business and technology services

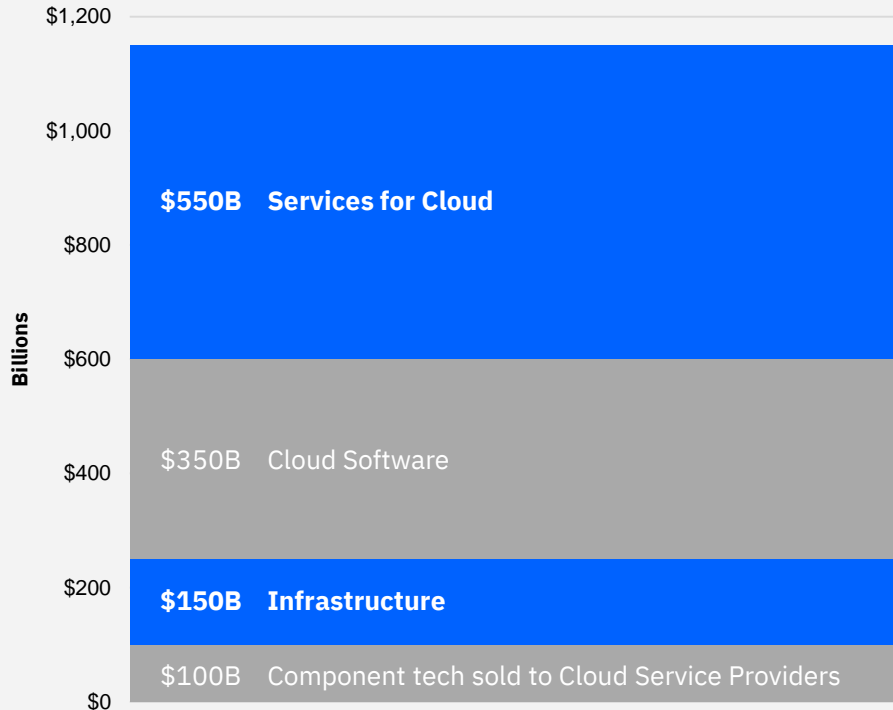
Transforming from the inside-out

Modernizing infrastructure;  
moving mission-critical applications  
to the cloud

Scaling AI across the enterprise



# Red Hat reinforces and accelerates our ability to capture the hybrid cloud services opportunity



## How IBM drives more services revenue:

### Credibility and reach

IBM Services has unique scale, breadth, incumbency and relevance

### Unique Cloud capabilities

Differentiated methods, capabilities and assets to de-risk the client cloud journey

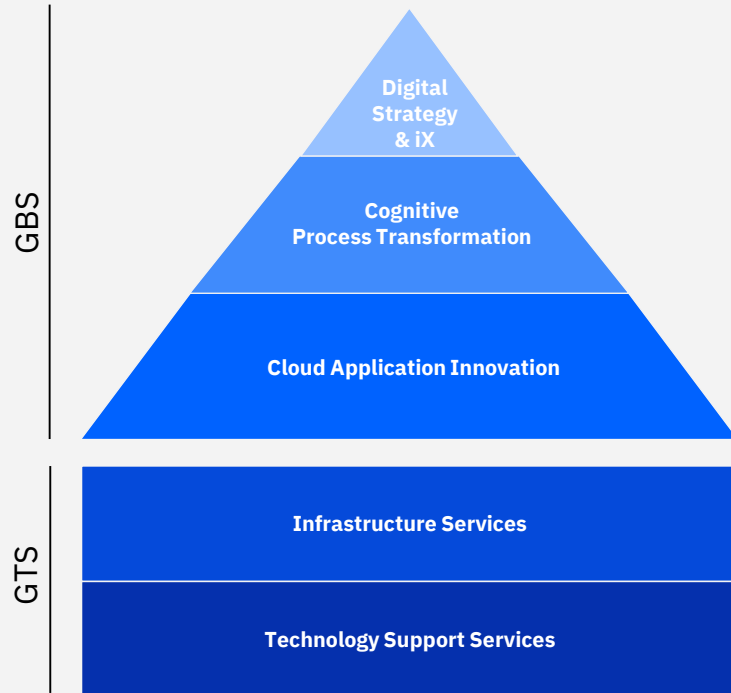
### Fuels OpenShift as “middleware of change”

Accelerate the adoption of OpenShift creating more entry points for IBM Services

**2-5X** For every \$1 spent on public cloud infrastructure, enterprises are projected to spend between \$2 - \$5 on services



# IBM Services has unique scale, breadth, incumbency and relevance



## IBM Services is the digital, cognitive and cloud partner for clients

Largest combined Services player – \$46 billion

250,000 highly-skilled professionals in 170 Countries

Mission-critical incumbency

Largest business design firm in the world

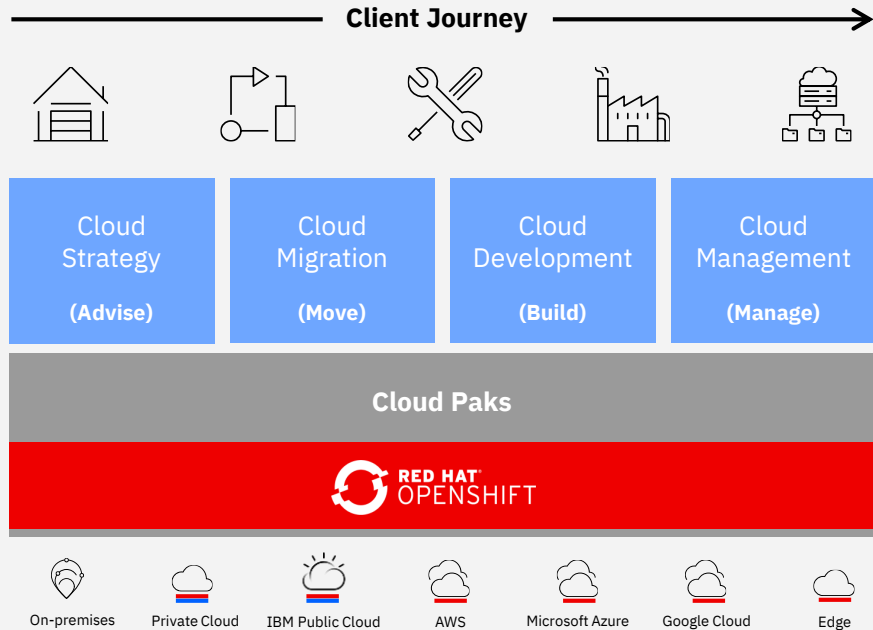
Industry, process and analytics expertise

Global delivery network with deep application and multicloud skills

Leading-edge services orchestration and integration platforms

Market-leading enterprise infrastructure provider

# Differentiated methods, capabilities and assets to de-risk the client cloud journey



## IBM Services is the trusted and credible partner for the open multicloud journey

- Meet clients where they are across Advise, Move, Build and Manage
- 80,000+ Cloud Application Services practitioners

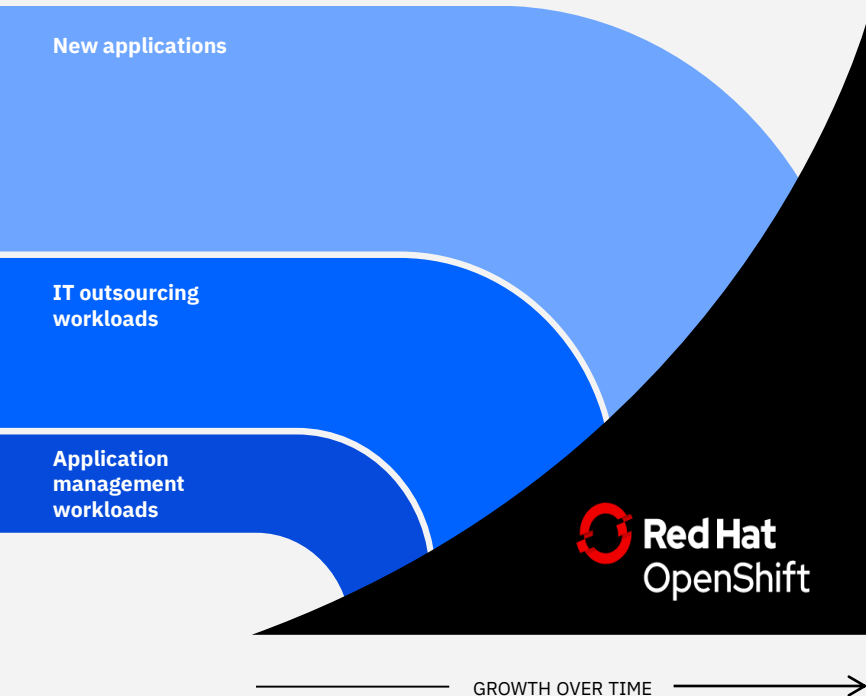
## Unified One IBM hybrid cloud capability delivers differentiated value

- Application Modernization Roadmap, Cloud Migration Factory, Multicloud Management Platform
- Global network of IBM Garages

## Integrated IBM and Red Hat Services and Solutions stack as accelerators

- Largest team of Red Hat services skills
- Fully aligned Red Hat go to market and offering strategy

# IBM Services incumbency will fuel Red Hat and OpenShift as the default hybrid cloud platform, creating more entry points for IBM Services



## Accelerate the adoption of OpenShift

Migrate mission-critical workloads to OpenShift

Build new workloads and applications on OpenShift

Establish and run OpenShift at scale

Set architecture standard with unique IBM Garage Method for Cloud

Deploy Red Hat services skills base

Leverage 5,000 services relationships and channels globally

# Business transformation journey and services opportunity enabled by the cloud journey

← **Intelligent workflows** →



**AI/Machine Learning**



**Robotic Process Automation**



**5G/Telco**



**IoT**



**Location-based Services**



**Augmented Analytics**



**Blockchain**



**Wearables**

**Cloud Paks**



On-premises



Private Cloud



IBM Public Cloud



AWS



Microsoft Azure



Google Cloud



Edge

# Sell More Services: Summary

IBM Services +  
Red Hat = Trusted  
Cloud Journey Partner  
for the Enterprise

IBM Services has  
unique scale, breadth,  
incumbency and  
relevance

Differentiated  
methods, assets and  
capabilities create  
differentiation to  
de-risk the client  
cloud journey

Incumbency will  
accelerate the  
adoption of OpenShift  
creating more entry  
points for IBM  
Services

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**Services improving revenue growth profile with margin expansion**

# Better Together: Sell More Red Hat

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## **Martin Schroeter**

Senior Vice President  
IBM Global Markets



# Our Go-to-Market Priorities

## **Preserve Operating Independence**

Red Hat drives its own go-to-market strategy through independent sales and services organization, management system and compensation plans.

## **Maintain Ecosystem Neutrality**

Red Hat operates a separate partner program and continues to cultivate a distinct developer ecosystem. IBM will be engaged the same way as any other partner.

## **Mobilize IBM and Invest for Scale**

All IBM client-facing teams and ecosystem partners are activated to leverage established relationships, expand reach and create new demand through combined offerings.

# How we will accelerate Red Hat's growth trajectory

## Grow Red Hat with IBM's largest clients

*"We are constantly exploring emerging technology as we transform air travel; IBM + Red Hat will be an essential part of our digital transformation."*

**- Airline CEO, USA**

## Expand Red Hat in ~30 select countries

*"Very bold move that will be critical for us at the bank. Knowing IBM is making the investments to keep us open and safe helps us lose our fear of cloud."*

**- Banking chairman, India**

## Scale Red Hat in all other countries

*"Now that Red Hat has IBM behind it, we are even more confident in carrying out Open Source projects for Argentine banks."*

**- Banking CIO, Argentina**



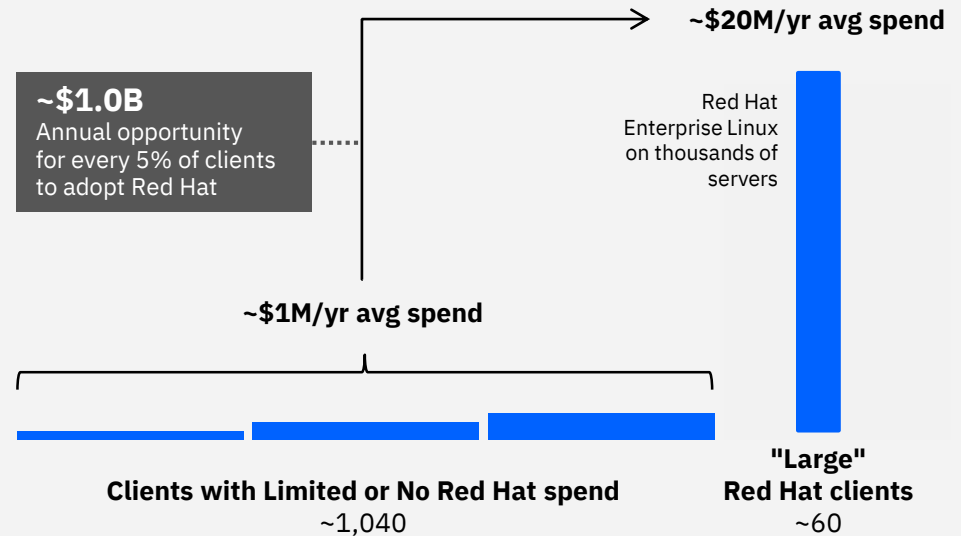
# Leverage relationships at IBM's largest accounts to accelerate open hybrid cloud adoption

## Significant opportunity to accelerate Red Hat adoption in IBM's largest clients

Top accounts are enabled to win:

- Activated joint account planning within 30 days
- Received account-level insight and bespoke sales play recommendations

Indicative Distribution of annual Red Hat spend for IBM's top 1,100 clients



# Expand Red Hat in ~30 select countries with little or no presence

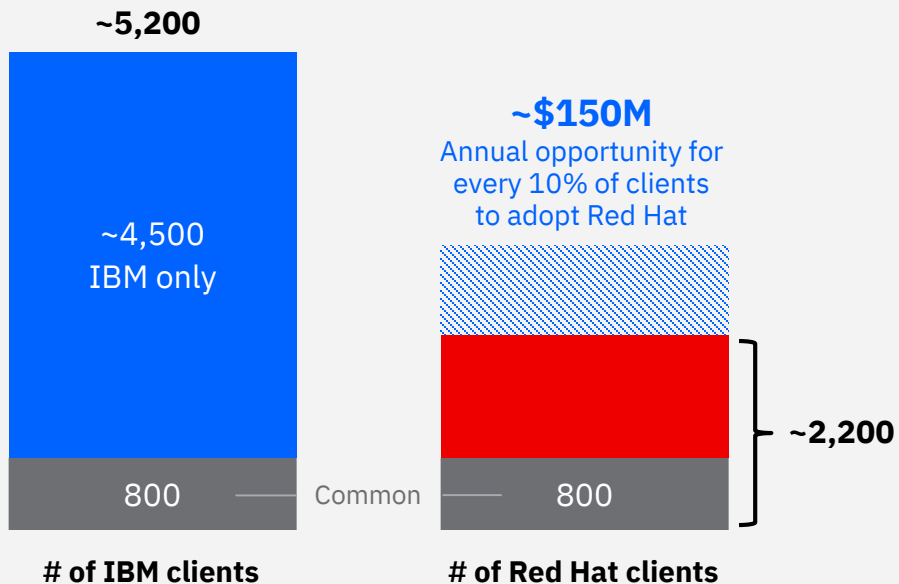
In these ~30 countries, IBM brings:

- 6,000 IBM sellers
- 100,000 services delivery professionals
- 27,000 Ecosystem Partners
- IBM Systems presence and industry expertise

To address opportunity with IBM-only clients:

- ~98% no significant OpenShift presence
- ~90% no significant Red Hat Enterprise Linux deployment

In these countries, Red Hat clients spend \$300K per year, on average

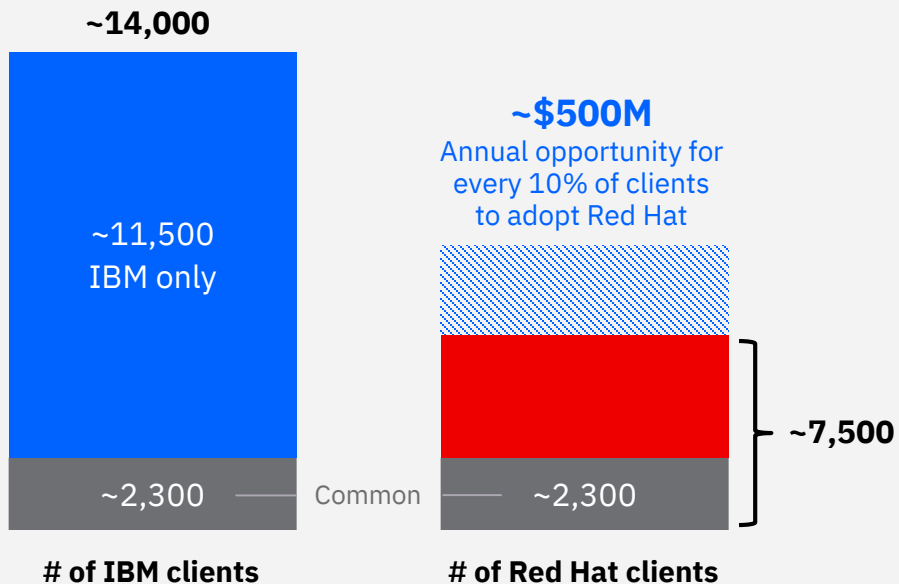


# Scale Red Hat in all other countries and clients

Most IBM clients are not substantial adopters of Red Hat, but when they are, they spend \$450K per year on average

To win the open hybrid cloud mandate in all 175 countries where IBM does business, IBM sellers are incentivized and enabled to drive growth:

- Hybrid multicloud and Red Hat education and sales assets
- Incremental incentives to identify, pass, and help close Red Hat opportunities



# Better Together: Summary

## Red Hat

Accelerate OpenShift adoption

Expand ecosystem

IBM provides scale, expertise and workloads

## Sell More Software

Middleware anywhere

Preferred destination

Capture new workloads

## Sell More Services

Leverage credibility and reach

Unique cloud capabilities

Fuel OpenShift adoption

## Sell More Red Hat

Grow with top clients

Expand geographically

Scale everywhere

---

**Accelerates revenue growth:  
200+ basis points to IBM revenue growth over 5 years**

# IBM + Red Hat: Financial Profile

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**James Kavanaugh**  
Senior Vice President and  
Chief Financial Officer  
IBM



# Red Hat accelerates IBM's revenue growth and shift to higher value

## Value of Red Hat + IBM...

Red Hat is the leading platform for hybrid cloud

IBM brings incumbency, scale and expertise in mission-critical workloads

Together IBM + Red Hat are the leader in client digital reinventions and journeys to cloud

## ...aligns with the hybrid cloud opportunity...

>\$1 Trillion hybrid cloud opportunity

Chapter 2 driven by mission-critical workloads to hybrid cloud

More attractive profit pools in hybrid cloud software

## ...to enhance IBM's financial performance

### **Accelerates revenue growth**

200+ basis points to IBM revenue growth over 5 years

### **Accelerates shift to higher value**

Operating GP margin accretive in Year 1  
Operating EPS accretive by end of Year 2

### **Enhances strong cash flow profile**

Free cash flow accretive in Year 1  
Continued dividend growth

# IBM's 2020-2021 financial performance accelerates across revenue, operating pre-tax income and free cash flow

## IBM 2020 – 2021

Revenue @CC

---

**Mid** Single-digit growth

Operating Pre-tax Income

---

**High** Single-digit growth

Free Cash Flow

---

**>100%** Realization

Leverage Ratio

Consistent with mid to high single A range

### Sustained revenue growth trajectory

- Cloud & Cognitive Software segment accelerating to double-digit revenue growth in 2020, enhanced by Red Hat
- Services improving revenue growth profile with margin expansion
- Systems performance fueled by new innovation

### Continued margin expansion driven by shift to higher value and productivity

Adds ~\$1.5 billion incremental free cash flow by the end of 2021

# Red Hat is the leader in open source platforms with a high value model

Open source technology leader

OpenShift is the platform for hybrid cloud

Hybrid, multicloud platform creates opportunity across the ecosystem

## Red Hat is high-growth, high-value...

### Strong Revenue Growth Profile

\$3.5 billion,  
+16% @ CC

### Strong Subscription Model

~\$3 billion annuity revenue;  
Very high renewal rates

### Strong Margin Profile

~85% GP margin

### Strong Cash Generation

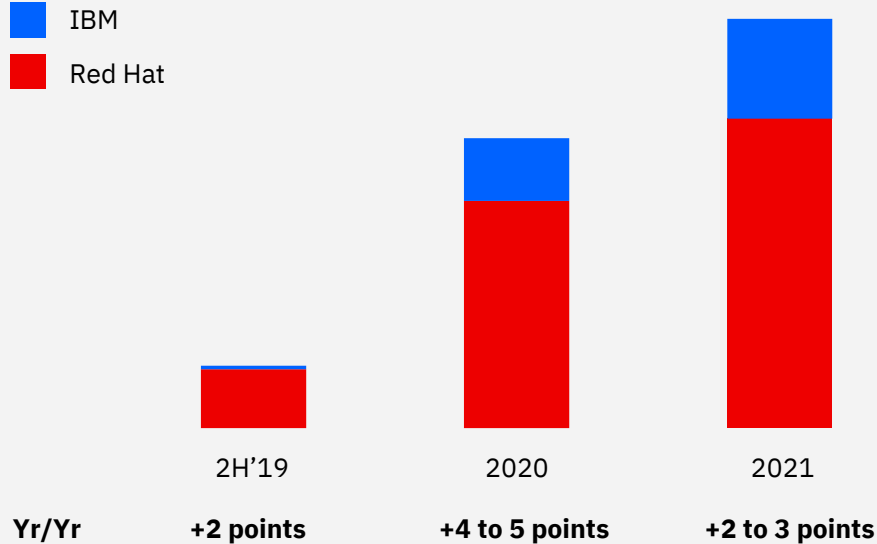
~\$1 billion free cash flow

Reflects reported results for last twelve months



# Red Hat accelerates IBM's revenue growth by 200+ basis points over 5 years

## Revenue contribution to IBM's base business



IBM incremental revenue fueled by shift to hybrid cloud

- Software middleware anywhere
- Services led journey to cloud

Red Hat and IBM incremental revenue contribution over the next 5 years:

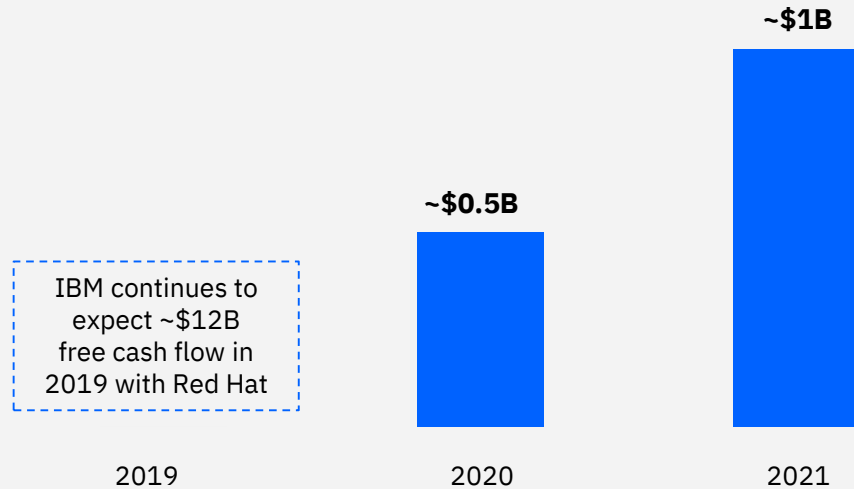
- 2+ points IBM revenue growth
- 8+ points cloud revenue growth

Improves high-value mix of IBM revenue



# Red Hat enhances strong free cash flow and adds ~\$1.5 billion through 2021

## Free cash flow contribution to IBM's base business 2020/2021



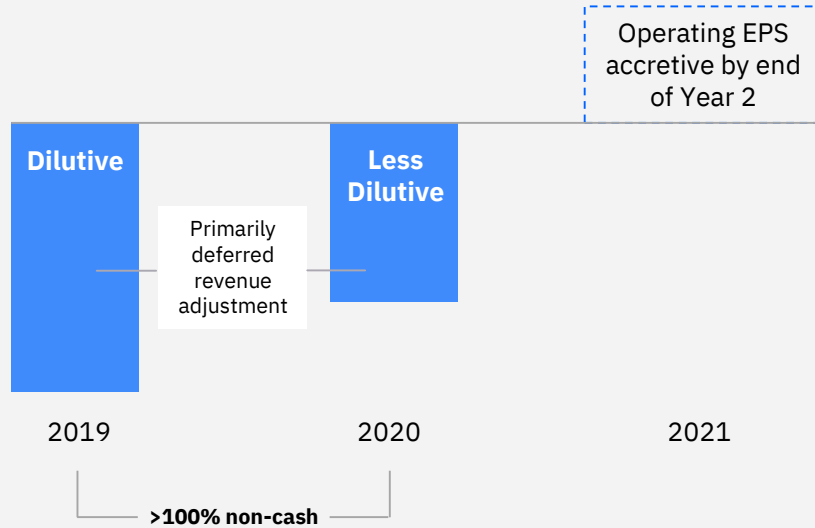
Free cash flow accretive in first twelve months, with nominal dilution in 2H'19

Red Hat increases IBM free cash flow realization

Note: Red Hat net of incremental interest and acquisition-related activity

# Red Hat accretive to operating EPS by end of Year 2

## Impact on total IBM operating (Non-GAAP) EPS

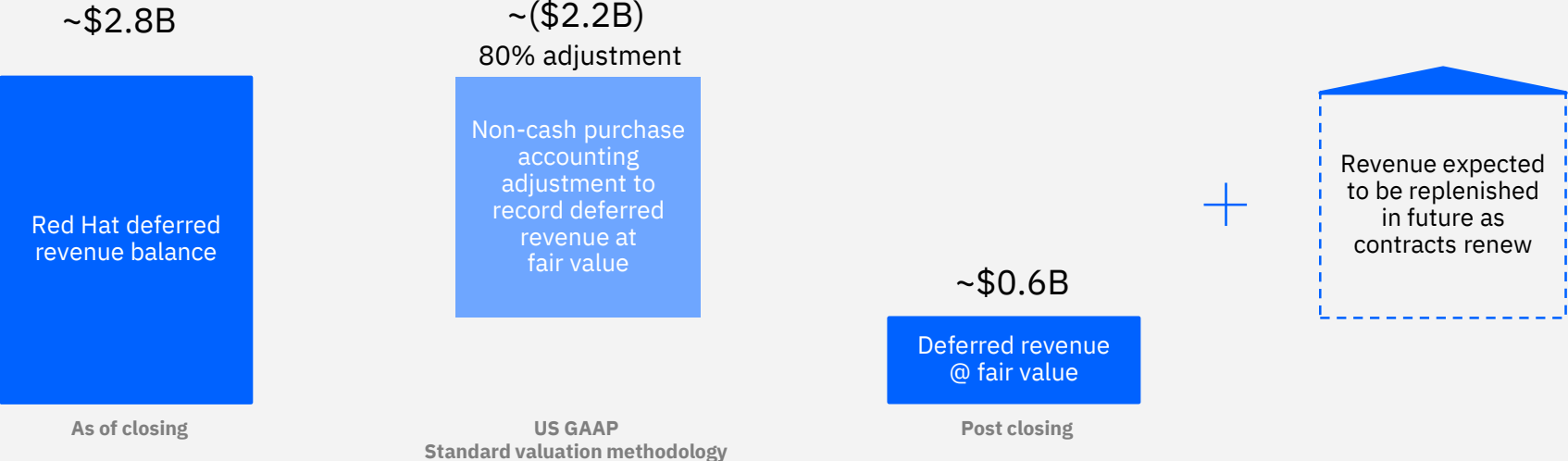


>100% dilution driven by non-cash items

- Deferred revenue adjustment
- Share buyback suspension
- Stock option amortization (equity)

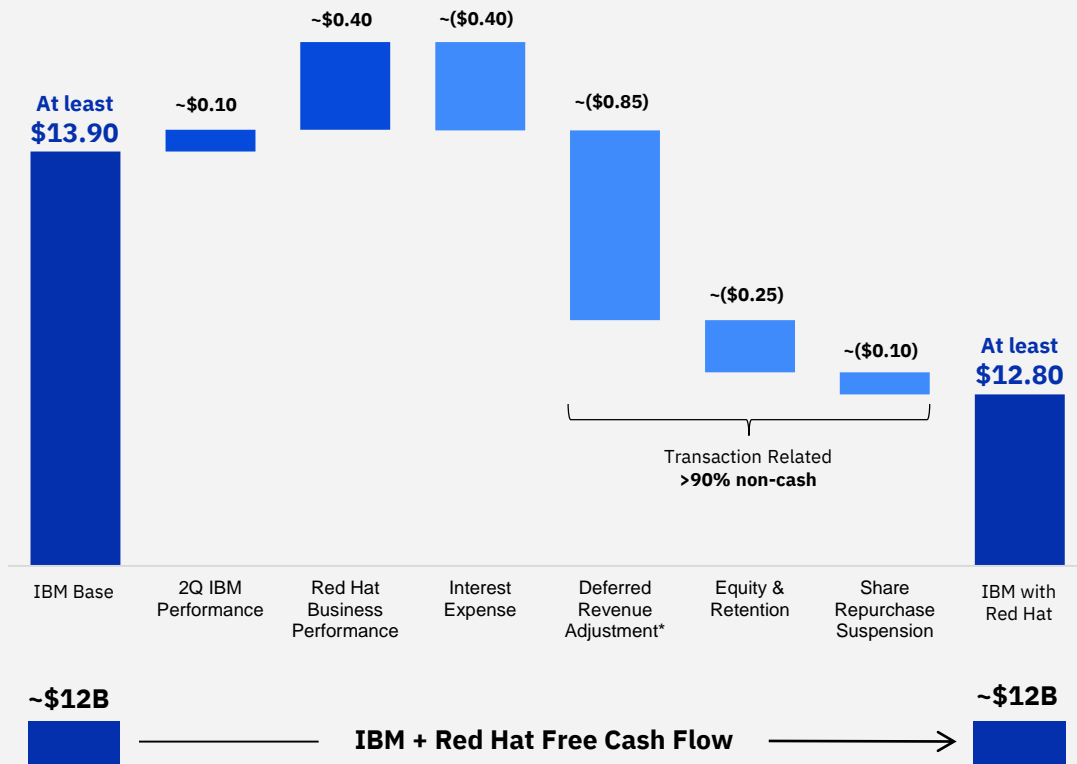
Contributes to IBM growth in 2020

# US GAAP non-cash purchase accounting for deferred revenue



**Pay-in-advance subscription based business**      **High margin business**      **Remaining revenue runoff**      **Very high renewal rates and stable client base**

# IBM + Red Hat: updated 2019 operating EPS expectation



Red Hat standalone business adds to solid IBM base performance

Reduction driven by temporary, non-cash items

Immediately accretive to IBM GP margin

Red Hat-related profit impact and tax rate drives a 2 point tax reduction to IBM rate in 2019

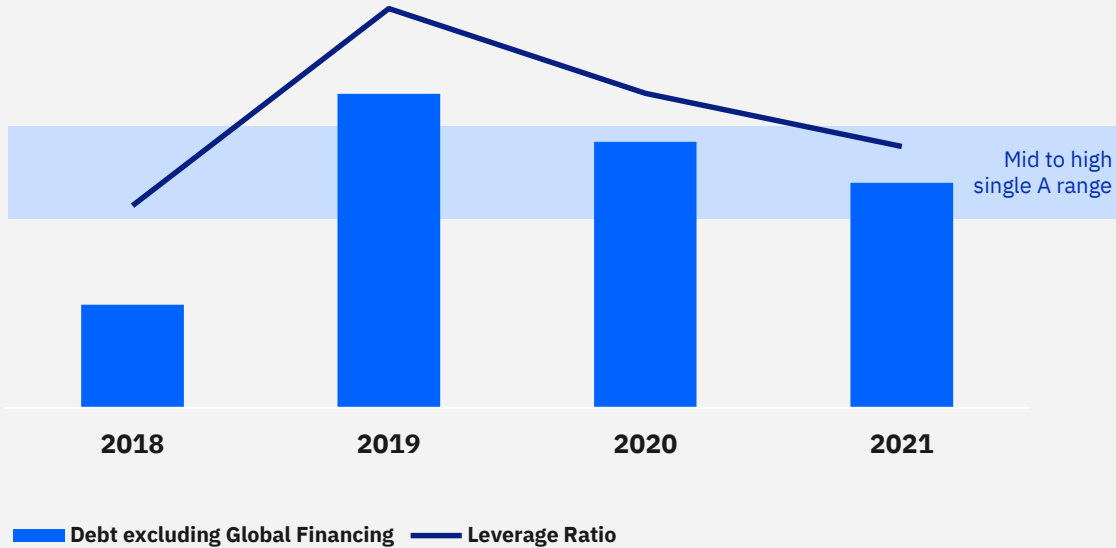
Maintaining ~\$12 billion free cash flow expectation

\*US GAAP purchase accounting adjustment



# Committed to maintaining strong balance sheet

## Debt & Leverage Ratio\*



Suspended share repurchase to focus on debt reduction

Remain committed to continued dividend growth

Expect to achieve targeted leverage ratios within a couple of years

Enables flexibility to continue to invest in the business

\* Leverage Ratio reflects Moody's methodology

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**High** Single-digit growth

Free Cash Flow

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**>100%** Realization

Leverage Ratio

Consistent with mid to high single A range

Sustained revenue growth trajectory

Continued margin expansion driven by shift to higher value and productivity

Adds ~\$1.5 billion incremental free cash flow by the end of 2021

**Ginni Rometty**

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**Jim Whitehurst**

Senior Vice President, IBM  
and CEO, Red Hat

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IBM Global Markets



smart  
is  
open.



open  
is  
smart.

# IBM Investor Briefing 2019



# Forward-looking statements and non-GAAP information

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In an effort to provide additional and useful information regarding the company's (IBM's) historical results and forward-looking financial information on a continuing operations basis, as determined by generally accepted accounting principles (GAAP), these materials contain non-GAAP financial measures, including operating pre-tax income, operating gross profit margin, operating earnings per share, free cash flow, and adjustments for currency.

Additionally, these materials contain certain non-GAAP financial measures regarding Red Hat's historical financial results, including free cash flow and adjustments for currency.

The company is unable to provide, without unreasonable efforts, certain forward-looking information as determined by GAAP, including expectations for gross profit margin, pre-tax income and diluted earnings per share.

The rationale for management's use of non-GAAP information is included in Exhibit 99.2 to the company's Form 8-K furnished with the SEC on August 2, 2019. The reconciliations of non-GAAP information to GAAP on IBM's historical results included in these materials are included on pages 69 and 98 of the company's Form 10-Q filed with the SEC on July 30, 2019. The reconciliations of non-GAAP information to GAAP on Red Hat's historical financial results and IBM's full-year expectation of diluted earnings per share are included on the slides entitled "Non-GAAP Supplemental Materials" in this presentation.

# Notes

**Note 1**

Forward-looking revenue growth rates are provided at the spot rate as of August 2, 2019.

**Note 2**

Growth rate at constant currency is a non-GAAP measure. For additional information on this non-GAAP measure, please refer to Slide 54.

**Note 3**

Operating GP Margin is a non-GAAP measure. For additional information on this non-GAAP measure, please refer to Slide 51.

**Note 4**

Operating Pre-tax Income is a non-GAAP measure. For additional information on this non-GAAP measure, please refer to Slide 51.

**Note 5**

Free Cash Flow is a non-GAAP measure. For additional information on this non-GAAP measure, please refer to Slide 54.

**Note 6**

Free Cash Flow Realization equals Free Cash Flow divided by GAAP Net Income from Continuing Operations.

**Note 7**

Operating EPS is a non-GAAP measure. For additional information on this non-GAAP measure, please refer to Slide 53.

**Note 8**

IBM is unable to provide, without unreasonable efforts, an updated full-year expectation of GAAP diluted earnings per share at this time because it is unable to determine, with reasonable certainty, the purchase accounting valuations that will be utilized to establish the finite-lived intangible assets for the Red Hat acquisition and the expected amortization impact of those acquired intangibles. The operating (non-GAAP) earnings per share full-year expectation can be presented, as it does not include acquired intangible asset amortization. The valuation of acquired intangibles is not yet substantially complete and depends on various factors; as such, the variability in the estimate of the amortization of those intangibles could have a material impact on the GAAP reported results for the guidance period. All other known or estimated factors impacting the GAAP full-year expectations have been presented.

**Note 9**

Within this presentation and speaker materials, all references to "Operating" refers to Non-GAAP metrics

# Non-GAAP Supplemental Materials

## Reconciliation of Operating Earnings Per Share

### Earnings Per Share

### 2019 Full-Year Expectations

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GAAP Diluted EPS*	\$XX.XX
Operating (Non-GAAP) EPS	At least \$12.80
Adjustments	
Acquisition-related Charges	(\$0.96)
Non-Operating Retirement-Related Items	(\$0.45)
Tax Reform Enactment Impacts	(\$0.24)
Amortization of Red Hat Intangibles*	(\$X.XX)

IBM is unable to provide, without unreasonable efforts, an updated full-year expectation of GAAP diluted earnings per share at this time because it is unable to determine, with reasonable certainty, the purchase accounting valuations that will be utilized to establish the finite-lived intangible assets for the Red Hat acquisition and the expected amortization impact of those acquired intangibles. The operating (non-GAAP) earnings per share full-year expectation can be presented, as it does not include acquired intangible asset amortization. The valuation of acquired intangibles is not yet substantially complete and depends on various factors; as such, the variability in the estimate of the amortization of those intangibles could have a material impact on the GAAP reported results for the guidance period. All other known or estimated factors impacting the GAAP full-year expectations have been presented.

The above reconciles the Non-GAAP financial information contained in the “IBM + Red Hat: Financial Profile” presentation of the IBM Investor Briefing. See Exhibit 99.2 included in the company’s first Form 8-K furnished with the SEC on August 2, 2019 for additional information on the use of these non-GAAP financial measures.

# Non-GAAP Supplemental Materials

## Reconciliation of Red Hat Revenue and Free Cash Flow – Last 12 Months

### 12 Months ended May 2019

	GAAP	@ CC
Revenue	14%	16%

### 12 Months ended May 2019

<b>Net Cash from Operations per GAAP</b>	<b>\$1.1</b>
Net Capital Expenditures	(\$0.1)
<b>Free Cash Flow</b>	<b>\$1.0</b>

\$ in billions

The above reconciles the Non-GAAP financial information contained in the “IBM + Red Hat: Financial Profile” presentation of the IBM Investor Briefing. See Exhibit 99.2 included in the company’s first Form 8-K furnished with the SEC on August 2, 2019 for additional information on the use of these non-GAAP financial measures.

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