Report of Management 50

Report of Independent Accountants 51

Management Discussion 52

Consolidated Financial Statements
- EARNINGS 64
- FINANCIAL POSITION 65
- STOCKHOLDERS' EQUITY 66
- CASH FLOWS 68

Notes to Consolidated Financial Statements
- A SIGNIFICANT ACCOUNTING POLICIES 69
- B ACCOUNTING CHANGES 71
- C COMMON STOCK SPLIT 72
- D ACQUISITIONS/DIVESTITURES 72
- E INVENTORIES 74
- F FINANCING RECEIVABLES 74
- G PLANT, RENTAL MACHINES AND OTHER PROPERTY 74
- H INVESTMENTS AND SUNDRY ASSETS 74
- I SALE AND SECURITIZATION OF RECEIVABLES 74
- J BORROWINGS 75
- K FINANCIAL INSTRUMENTS 76
- L OTHER LIABILITIES 78
- M STOCKHOLDERS' EQUITY ACTIVITY 79
- N CONTINGENCIES 79
- O TAXES 80
- P ADVERTISING 81
- Q 1999 ACTIONS 81
- R RESEARCH, DEVELOPMENT AND ENGINEERING 82
- S EARNINGS PER SHARE OF COMMON STOCK 83
- T RENTAL EXPENSE AND LEASE COMMITMENTS 83
- U STOCK-BASED COMPENSATION PLANS 84
- V RETIREMENT PLANS 85
- W NONPENSION POSTRETIREMENT BENEFITS 88
- X SEGMENT INFORMATION 89

Five-Year Comparison of Selected Financial Data 94

Selected Quarterly Data 94

Stockholder Information 95

Board of Directors and Senior Management 96

Responsibility for the integrity and objectivity of the financial information presented in this Annual Report rests with IBM management. The accompanying financial statements have been prepared in conformity with generally accepted accounting principles, applying certain estimates and judgments as required.

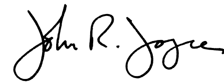
IBM maintains an effective internal control structure. It consists, in part, of organizational arrangements with clearly defined lines of responsibility and delegation of authority, and comprehensive systems and control procedures. We believe this structure provides reasonable assurance that transactions are executed in accordance with management authorization, and that they are appropriately recorded in order to permit preparation of financial statements in conformity with generally accepted accounting principles and to adequately safeguard, verify and maintain accountability of assets. An important element of the control environment is an ongoing internal audit program.

To assure the effective administration of internal control, we carefully select and train our employees, develop and disseminate written policies and procedures, provide appropriate communication channels, and foster an environment conducive to the effective functioning of controls. We believe that it is essential for the company to conduct its business affairs in accordance with the highest ethical standards, as set forth in the IBM Business Conduct Guidelines. These guidelines, translated into numerous languages, are distributed to employees throughout the world, and reemphasized through internal programs to assure that they are understood and followed.

PricewaterhouseCoopers LLP, independent accountants, is retained to examine IBM's financial statements. Its accompanying report is based on an examination conducted in accordance with generally accepted auditing standards, including a review of the internal control structure and tests of accounting procedures and records.

The Audit Committee of the Board of Directors is composed solely of outside directors, and is responsible for recommending to the Board the independent accounting firm to be retained for the coming year, subject to stockholder approval. The Audit Committee meets periodically and privately with the independent accountants, with our internal auditors, as well as with IBM management, to review accounting, auditing, internal control structure and financial reporting matters.

Louis V. Gerstner, Jr.
Chairman of the Board and
Chief Executive Officer



John R. Joyce
Senior Vice President and
Chief Financial Officer

To the Stockholders and Board of Directors of
International Business Machines Corporation:

In our opinion, the accompanying consolidated financial statements, appearing on pages 64 through 93, present fairly, in all material respects, the financial position of International Business Machines Corporation and subsidiary companies at December 31, 2000 and 1999, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2000, in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the company's management; our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America, which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

PricewaterhouseCoopers LLP

PricewaterhouseCoopers LLP
New York, New York
January 17, 2001

OVERVIEW OF 2000

IBM finished the year 2000 with a strong fourth quarter performance after three challenging quarters. The company's revenue, net income and earnings per share again reached record levels and cash flow was strong. In many respects, the full-year financial performance reflects momentum that had been building steadily all year, momentum that is an affirmation of the strategies adopted over the last several years: a focus on services and solutions; powerful, scalable servers; and open-source platforms. The company also had solid full-year results in the strategic high-growth areas of services, middleware software and technology. In addition, Global Services ended the year with a strong backlog of services contracts totaling $85 billion, up from $60 billion at year-end 1999.

The company reported revenue of $88.4 billion, net income of $8.1 billion and $4.44 diluted earnings per common share. The effects of adverse currency movements lowered year-to-year revenue growth from approximately 4 percent at constant currency to 1 percent on an as reported basis. In Europe/Middle East/Africa, revenue declined 5 percent (up 6 percent at constant currency). Asia Pacific revenue grew 16 percent (15 percent at constant currency). In the Americas, revenue decreased 0.5 percent (flat at constant currency).

In 2000, aggressive focus on cost and expense management improved the company's gross profit margin (despite a changing mix of business) and net income margin. The company continued to use technology and other productivity improvements to enhance the efficiency of its operations, particularly by increasing the revenue generation and customer service capabilities of ibm.com and significantly increasing electronic processing within the procurement function.

The company ended 2000 with cash and cash equivalents and current marketable securities of $3.7 billion, after funding investments of over $18 billion in capital expenditures; research, development and engineering; strategic acquisitions; and repurchases of common stock. During 2000, the company announced a multi-year, $5 billion program to build an advanced chip-making facility and to expand operations at its worldwide technology facilities. Share repurchases resulted in common shares outstanding at year-end 2000 of 1.74 billion, down 2 percent compared with 1.78 billion last year. During 2000, the company's non-global financing related debt was reduced while Global Financing debt increased in line with the asset growth of the Global Financing business.

CHALLENGES

The company's broad portfolio and geographic diversification position it well relative to its competitors in 2001. The company's top priority is to build on the momentum of last year, driven, for the most part, by business strategies taking hold; the marketplace moving in the company's direction; demand increasing for IBM's products and services (particularly e-business applications and services); and the company's improved execution.

In 2001, the company faces concerns that economic softness in the United States could worsen and expand into non-U.S. markets. Increasingly aggressive price competition and the potential effects of ongoing adverse currency movements are other areas of volatility.

Yet, even against a backdrop of uncertainty, the company is in a unique competitive position. Its traditional customer base—essentially large, global institutions—requires the technology and services of the company to improve competitiveness, in both good times and bad. The company's ability to integrate complex technologies across the full range of computing platforms sets it apart from competitors.

FORWARD-LOOKING AND CAUTIONARY STATEMENTS

Certain statements contained in this Annual Report may constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These statements involve a number of risks, uncertainties and other factors that could cause actual results to be materially different, as discussed more fully elsewhere in this Annual Report and in the company's filings with the Securities and Exchange Commission, including the company's 2000 Form 10-K to be filed on or about March 12, 2001.

RESULTS OF OPERATIONS

(dollars in millions except per share amounts)	*2000*	*1999*	*1998*
Revenue	$ 88,396	$ 87,548	$ 81,667
Cost	55,972	55,619	50,795
Gross profit	32,424	31,929	30,872
Gross profit margin	36.7%	36.4%	37.8%
Total expense	20,890	20,172	21,832
Income before income taxes	$ 11,534	$ 11,757	$ 9,040
Net income	$ 8,093	$ 7,712	$ 6,328
Earnings per share of common stock:			
Assuming dilution	$ 4.44	$ 4.12	$ 3.29
Basic	$ 4.58	$ 4.25	$ 3.38

The average number of common shares outstanding assuming dilution was lower by 59.0 million shares in 2000 versus 1999 and 49.1 million shares in 1999 versus 1998, primarily as a result of the company's common share repurchase program. The average number of shares outstanding assuming dilution was 1,812.1 million, 1,871.1 million and 1,920.1 million, respectively, at December 31, 2000, 1999 and 1998.

The following table identifies the company's percentage of revenue by segment:

	2000	1999*	1998*
Hardware	42.7%	43.3%	44.2%
Global Services	37.5	36.7	35.4
Software	14.3	14.5	14.5
Global Financing	3.9	3.6	3.5
Enterprise Investments/ Other	1.6	1.9	2.4
Total	100.0%	100.0%	100.0%

**Reclassified to conform with 2000 presentation.*

The overall gross profit margin of 36.7 percent increased 0.3 points from 1999, following a 1.4 point decline in 1999 versus 1998. The increase in gross profit margin was primarily driven by improvement in the hardware margin associated with microelectronics and personal computer products. This increase was partially offset by a lower Global Services margin and the company's continued shift in revenue to Global Services, which has a lower gross profit margin than the company's server products. The decline in 1999 versus 1998 was primarily due to the company's changing mix of revenue toward Global Services and away from server products.

In the Americas, full-year 2000 revenue was $38.6 billion, down 0.5 percent (flat at constant currency) from the 1999 period. Revenue from Europe/Middle East/Africa was $24.3 billion, a decrease of 5.3 percent (up 6 percent at constant currency). Asia Pacific revenue grew 16.4 percent (15 percent at constant currency) to $17.7 billion. Original equipment manufacturer (OEM) revenue decreased 0.9 percent (1 percent decrease at constant currency) to $7.8 billion.

Information about the company's operating segments can be found in note X, "Segment Information," on pages 89 through 93. Note X provides additional information, including a description of the products and services of each segment, as well as financial data pertaining to each segment.

The following discussion is based on the Consolidated Financial Statements on pages 64 through 68, which reflect, in all material respects, the company's segment results on an external basis.

Hardware

(dollars in millions)	2000	1999*	1998*
Revenue	$ 37,777	$ 37,888	$ 36,096
Cost	27,038	27,591	24,653
Gross profit	$ 10,739	$ 10,297	$ 11,443
Gross profit margin	28.4%	27.2%	31.7%

**Reclassified to conform with 2000 presentation.*

Hardware revenue was essentially flat (up 2 percent at constant currency) in 2000 versus 1999 and increased 5.0 percent (5 percent at constant currency) in 1999 compared with 1998.

In January 2000, the company reorganized the Server segment and renamed it the Enterprise Systems segment. In accordance with that organizational change, the company transferred system-level product businesses from the Technology segment to the Enterprise Systems segment. Those system-level product businesses are the company's disk storage products, which include the Enterprise Storage Server known as "Shark," tape subsystems and the company's storage area networking program, and networking products. Also, in January 2000, the company transferred the Retail Store Solutions business, a leader in providing point-of-sale solutions, to the Personal Systems segment from the Enterprise Investments segment. All amounts disclosed herein for all years presented have been reclassified to conform with these changes.

Technology revenue increased 4.0 percent when compared with 1999, following an increase of 13.0 percent in 1999 versus 1998. The increase in 2000 revenue was driven by strong growth in custom logic, networking and pervasive computing products, partially offset by lower hard disk drive (HDD) revenue. Although HDD revenue declined for the full year due primarily to delays in the 10K RPM drive, revenue sequentially improved each quarter in 2000 and from the 1999 fourth quarter to the 2000 fourth quarter.

The Technology segment results were also affected by supply constraints of wafers and ceramic substrates in the second half of 2000. In both cases, strong demand for these items from internal users and external OEM customers exceeded the company's ability to supply these components. The company improved its ability to manage this challenge toward the end of the year through short-term and strategic actions. In addition, on October 10, 2000, the company announced plans to invest $5.0 billion in the following projects: (1) building an advanced chip-making facility in East Fishkill, New York; (2) expanding its chip-making capacity in Burlington, Vermont and Yasu, Japan, as well as at a joint venture in Essonnes, France; and (3) expanding its organic and ceramic chip-packaging operations worldwide.

The company took actions in 1999 in the microelectronics and storage areas that were aimed at strengthening the Technology segment over the long term. Those actions were intended to shift the focus of the Technology segment to higher margin businesses and more efficient operations. To further achieve these goals, the company sold its MiCRUS semiconductor business in June 2000. (See note Q, "1999 Actions," on pages 81 and 82 for additional information.)

Strong growth in OEM technology, primarily custom logic and high-performance static random access memory (SRAM) revenue drove the increase in 1999 revenue. A slower growth rate in HDD storage revenue in 1999 versus 1998 reflected pricing pressures.

Personal Systems revenue grew 0.8 percent in 2000 from 1999, following an increase of 20.1 percent in 1999 versus 1998. The change in 2000 revenue was driven by increased revenue in xSeries servers and mobile products, partially offset by lower desktop personal computer and retail store solutions revenue. The decline in desktop revenue was driven by consumer products, as the company decided in 1999 to exit retail channels in the United States and Europe. The Personal Systems segment has benefited from the company-wide focus on building a competitive cost and expense structure, which has been crucial in enabling the company to price personal computers competitively. The segment was profitable for the second half of 2000 despite a challenging industry environment. The increase in 1999 revenue versus 1998 was primarily driven by strong revenue growth in Netfinity servers and mobile products. Mobile revenue was constrained due to a shortage of flat-panel displays in the second half of 1999.

In October 2000, the company announced IBM eServers to manage the unprecedented demands of e-business. This new generation of servers features mainframe-class reliability and scalability, broad support of open standards for the development of new applications, and capacity on demand. The new servers feature technology from the company's high-end server brands and share the best attributes of all mainframe-class computing. The entire IBM eServer family uses Tivoli e-infrastructure management software which manages all components of a heterogeneous e-business infrastructure.

IBM zSeries mainframe servers are at the heart of the e-business infrastructure for mission-critical data and transaction processing.

IBM pSeries servers are the most powerful, technologically advanced UNIX servers.

IBM iSeries mid-range servers are integrated mid-range business servers that run sophisticated business applications.

IBM xSeries servers are Intel-based servers.

In 2000, Enterprise Systems revenue declined 1.4 percent from 1999, following a decrease of 16.9 percent in 1999 versus 1998. Revenue grew for the pSeries UNIX servers with particular strength in the mid-range and high-end Web servers in 2000 versus 1999. This increase was more than offset by revenue declines for the mid-range iSeries servers and the zSeries servers in 2000 as compared to 1999. Although zSeries servers revenue declined, total deliveries of computing power increased more than 20 percent as measured in MIPS (millions of instructions per second) versus 1999. In addition, revenue from the company's storage systems products, which include "Shark," increased year over year, while revenue from networking products declined, consistent with the company's divestment strategy.

In 1999, lower revenue primarily from S/390, AS/400 and RS/6000 servers drove the revenue decline versus 1998. These declines were primarily driven by Y2K-related issues that affected the second-half results. Many of the company's large customers locked down their systems and technology purchases heading into the Y2K transition. In addition, the storage networking product decreases resulted, in part, from the sale of routing and switching intellectual property to Cisco Systems, Inc.

Hardware gross profit dollars increased 4.3 percent in 2000 from 1999, following a 10.0 percent decline in 1999 versus 1998. The increase in gross profit dollars was primarily driven by increased revenue and improvements in the gross profit margin for microelectronics and personal computers. The decline in gross profit dollars in 1999 resulted from a shift in the company's revenue away from servers, pricing pressures associated with HDDs, and memory chip price declines.

The hardware gross profit margin increased in 2000 by 1.2 points versus 1999 and declined 4.5 points in 1999 compared to 1998. The increase in 2000 was primarily driven by improved margins in microelectronics and personal computers. The decrease in 1999 was driven by the shift in the company's revenue away from servers to lower gross profit products, such as personal computers, OEM chip technology and HDDs, as well as price pressures.

Global Services

(dollars in millions)	*2000*	*1999*	*1998*
Revenue	$ 33,152	$ 32,172	$ 28,916
Cost	24,309	23,304	21,125
Gross profit	$ 8,843	$ 8,868	$ 7,791
Gross profit margin	26.7%	27.6%	26.9%

Global Services revenue increased 3.0 percent (6 percent at constant currency) in 2000 over 1999 and 11.3 percent (11 percent at constant currency) in 1999 over 1998. Revenue comparisons in 2000 were adversely affected by two events: the sale of the Global Network to AT&T in 1999 and the decline in Y2K services activity year over year. After adjusting for those two factors, Global Services revenue (excluding maintenance) increased 9 percent in 2000 and 17 percent in 1999. (See note D, "Acquisitions/Divestitures," on pages 72 through 74 for additional information about the Global Network sale.) Maintenance revenue was flat in 2000 when compared to 1999 and declined 1 percent in 1999 versus 1998.

Strategic Outsourcing Services and Integrated Technology Services were the major contributors to the revenue growth in 2000 and 1999. Strategic Outsourcing Services continued to demonstrate good revenue growth in 2000 as compared to 1999, with particularly strong growth in Asia Pacific. Integrated Technology Services benefited from growth in OEM alliance revenue, especially as related to Cisco Systems products. These increases were partially offset by the loss of revenue due to the sale of the Global Network and lower revenue growth from Business Innovation Services primarily resulting from the decline in Y2K activity. Business Innovation Services recovered in the second half of 2000 as customers shifted from mature offerings such as custom systems integration and Y2K remediation to the company's e-business offerings. Business Innovation Services revenue, exclusive of Y2K and custom systems integration, experienced strong growth in 2000.

e-business spans many of the Global Services offerings and contributed significantly to 2000 performance. The company's total discrete e-business revenue grew more than 70 percent to approximately $5 billion in 2000. This increase was driven by e-commerce consulting, e-business enablement and e-hosting services.

In 2000, the company signed contracts totaling $55 billion, including 60 contracts in excess of $100 million, 6 of which exceeded $1 billion. These transactions contributed to a services backlog at December 31, 2000, of $85 billion compared with $60 billion at December 31, 1999. The company continued to meet the demand for its services by hiring more than 19,000 employees in 2000 and 17,000 employees in 1999.

Global Services gross profit dollars were essentially flat in 2000 compared to 1999 and increased 13.8 percent in 1999 versus 1998. The decline in gross profit margin in 2000 of 0.9 points was driven by lower utilization rates in Business Innovation Services and Integrated Technology Services due to rapid hiring and retraining associated with rebalancing skills toward e-business services. Also contributing to the decline was a revenue shift to OEM alliances, which have a lower gross profit margin. The maintenance gross profit margin improved 0.6 points in 2000 versus 1999 due to continued productivity improvements and effective cost management.

Global Services gross profit dollars and gross profit margins improved in 1999 as compared with 1998 due to significant productivity improvements that more than offset competitive pressures and the negative effect of the changing mix of services and maintenance within the Global Services portfolio.

Software

(dollars in millions)	*2000*	*1999*	*1998*
Revenue	$ 12,598	$ 12,662	$ 11,863
Cost	2,283	2,240	2,260
Gross profit	$ 10,315	$ 10,422	$ 9,603
Gross profit margin	81.9%	82.3%	80.9%

Software revenue declined 0.5 percent (up 4 percent at constant currency) in 2000 from 1999, following an increase of 6.7 percent (8 percent at constant currency) from 1998. The company's middleware products had revenue growth of 3 percent in 2000 and 12 percent in 1999. Middleware comprises data management, transaction processing, Tivoli systems management and Lotus Notes messaging and collaboration for both IBM and non-IBM platforms. This growth was driven by the company's key products on UNIX and Windows NT platforms, led by WebSphere (Web application server software), MQSeries (business integration software) and DB2 (data management) offerings. These increases in middleware revenue were partially offset by revenue declines for Tivoli products as they were affected by a transition in the systems management software marketplace. The company continues to focus on helping customers use its software to transform their businesses to e-businesses, particularly in collaboration with the company's Global Services offerings, Independent Software Vendors, Web integrators and other service providers.

Operating systems software revenue declined 9 percent in 2000 and 4 percent in 1999 when compared with the previous period. The decline in 2000 was driven by lower revenue associated with eSeries servers and legacy products. The 1999 decline was driven by lower AS/400 revenue.

Software gross profit dollars decreased 1.0 percent in 2000 from 1999, following an increase of 8.5 percent in 1999 from 1998. The decline in gross profit dollars in 2000 was primarily because of lower revenue, higher costs for purchased vendor software and higher vendor royalty payments, partially offset by lower amortization and services costs. Increased revenue and lower amortization costs associated with previously capitalized software development spending drove the 1999 improvement, partially offset by higher vendor royalty payments primarily due to increased volumes.

Global Financing

(dollars in millions)	*2000*	*1999*	*1998*
Revenue	$ 3,465	$ 3,137	$ 2,877
Cost	1,595	1,446	1,494
Gross profit	$ 1,870	$ 1,691	$ 1,383
Gross profit margin	54.0%	53.9%	48.1%

Global Financing revenue increased 10.4 percent (13 percent at constant currency) in 2000 from 1999, following an increase of 9.0 percent (10 percent at constant currency) in 1999 versus 1998. Growth in sales of used equipment and in commercial financing drove the revenue increase in 2000. The revenue increase in 1999 over 1998 was due to growth in commercial financing and in financing of software and services.

Gross profit dollars increased 10.6 percent in 2000 versus 1999, following an increase of 22.3 percent in 1999 over 1998. The increase in 2000 was primarily driven by higher sales of used equipment and an improving gross profit margin on these sales. The increase in 1999, as well as in 2000, reflects the company's ongoing strategy to increase its use of the Global Treasury Centers rather than have the Global Financing business directly access external funding sources. This strategy minimizes the company's overall cost of borrowing via an efficient and economical centralized funding strategy that enables the company to access the global capital markets. This results in a shift of some costs within the Consolidated Statement of Earnings from Cost of Global Financing to Interest expense. (See the Debt/Equity section of the Management Discussion on page 60 for additional discussion of Global Financing debt and note J, "Borrowings," on page 75 for additional discussion of the company's interest expense.)

Enterprise Investments/Other

(dollars in millions)	*2000*	*1999**	*1998**
Revenue	$ 1,404	$ 1,689	$ 1,915
Cost	747	1,038	1,263
Gross profit	$ 657	$ 651	$ 652
Gross profit margin	46.8%	38.5%	34.0%

**Reclassified to conform with 2000 presentation.*

Enterprise Investments/Other revenue decreased 16.9 percent (13 percent at constant currency) from 1999, following a decrease of 11.8 percent (12 percent at constant currency) in 1999 from 1998. The decrease in both years was driven by lower revenue associated with the company's decision in 1999 to discontinue certain product lines, such as automated teller machines (ATMs), partially offset by growth in computer-aided three-dimensional interactive application (CATIA) software.

The gross profit dollars from Enterprise Investments/Other increased 0.9 percent in 2000 versus 1999, and were flat in 1999 versus 1998. The increase in 2000 gross profit dollars and gross profit margin was primarily due to a shift in the mix of revenue to software products that have a higher gross profit margin than the hardware product lines the company discontinued in 1999.

Expenses

(dollars in millions)	*2000*	*1999*	*1998*
Selling, general and administrative	$ 15,639	$ 14,729	$ 16,662
Percentage of revenue	17.7%	16.8%	20.4%
Research, development and engineering	$ 5,151	$ 5,273	$ 5,046
Percentage of revenue	5.8%	6.0%	6.2%

Selling, general and administrative (SG&A) expense increased 6.2 percent in 2000 versus 1999, following a decline of 11.6 percent in 1999 compared with 1998. The increase in 2000 was primarily driven by the 1999 net pre-tax benefit of $2,107 million associated with the sale of the Global Network, actions taken by the company in 1999 to improve its competitiveness and to strengthen the company's overall business portfolio, and implementation of a change in personal computers' depreciable lives. (See note D, "Acquisitions/Divestitures," on pages 72 through 74, and note Q, "1999 Actions," on pages 81 and 82 for further information.) Excluding the 1999 actions and sale of the Global Network, 2000 SG&A expense would have declined 7.1 percent versus 1999 and increased 1.0 percent in 1999 compared with 1998. In addition, its percentage of revenue would have been 17.7 percent for 2000, 19.2 percent for 1999 and 20.4 percent for 1998.

This improved expense-to-revenue ratio in 2000 results from the company's aggressive management of its infrastructure expense and discretionary spending, and improvements in its productivity through the use of technology and other productivity tools. Examples include revenue generation and customer services capabilities of ibm.com and a significant increase in electronic processing within the procurement function. The company also continues to benefit from growth in its licensing of intellectual property. In addition, the company has lower expenses as a result of the sale of the Global Network and actions taken in 1999 to exit such businesses as networking hardware and DRAM (dynamic random access memory) manufacturing. SG&A expense also benefited from the effects of currency and asset sales, excluding securities, in 2000.

The increase in 1999 compared to 1998, excluding the benefit from the action taken by the company in 1999, was primarily driven by the company's ongoing investments in software marketing and major marketing campaigns including the e-business campaign. These expenditures were consistent with the company's objective of growing revenue while improving the expense-to-revenue ratio over time.

Research, development and engineering (RD&E) expense declined 2.3 percent in 2000 from 1999, following an increase of 4.5 percent in 1999 from 1998. The decline in 2000 is primarily due to a $111 million pre-tax charge taken in 1999 for acquired in-process research and development (IPR&D) associated with the acquisition of Sequent Computer Systems, Inc., Mylex Corporation and DASCOM, Inc. See note D, "Acquisitions/Divestitures," on pages 72 through 74 for further detail about the IPR&D charge. Overall, the company continues to invest in high-growth opportunities such as e-business, Tivoli software products and initiatives to support Linux.

As a result of its ongoing research and development efforts, the company received 2,886 patents in 2000, placing it number one in patents granted in the United States for the eighth consecutive year. The application of these technological advances transforms the company's research and development into new products.

Recent advances include high-quality inductors and transformers that can be integrated into silicon chips without consuming excess chip area, enhancing miniaturization. These high-speed circuits are used in wireless communications applications and can operate at high frequencies, which extends the use of circuits in many applications, such as cell phones and personal digital assistants.

Included in the company's cost and expense is $327 million of benefit for retirement-related plans, including pension plans and nonpension postretirement benefits, for the year ended December 31, 2000. The comparable amounts for the years ended December 31, 1999 and 1998, were additional costs of $83 million and $286 million, respectively. See note V, "Retirement Plans," on pages 85 through 88 and note W, "Nonpension Postretirement Benefits," on pages 88 and 89 for the benefit and cost amounts for the major pension and nonpension postretirement plans.

For the year ended December 31, 2000, the company realized cost and expense reductions of $1,171 million due to the funded status of its pension plans. Of the total 2000 reductions, the change in actuarial assumptions for the primary U.S. plan contributed an estimated $221 million.

For the year ended December 31, 1999, the company realized cost and expense reductions of $694 million due to the funded status of its pension plans. Of the total 1999 reductions, the amendment to the U.S. plan, as more fully discussed in note V, "Retirement Plans," on pages 85 through 88, contributed an estimated $167 million. The impact in 1999 of changes in actuarial assumptions for the U.S. Plan was approximately $143 million of additional cost. This amount is included in the $694 million cost and expense reduction amount previously noted.

The change in the discount rate from 7.75 percent to 7.25 percent, effective December 31, 2000, is not expected to have a material effect on the company's 2001 results of operations. Effective January 1, 2001, the company increased pension benefits to recipients who retired before January 1, 1997. The increases ranged from 2.5 percent to 25 percent, and are based on the year of retirement and the pension benefit currently being received. This improvement is expected to result in an additional cost to the company of approximately $100 million in 2001.

The company does not expect to provide additional funding for the U.S. plan in 2001 because of the aforementioned items. Future effects of pension plans, including the changes noted above, on the operating results of the company depend on economic conditions, employee demographics, mortality rates and investment performance.

See note X, "Segment Information," on pages 89 through 93 for additional information about the pre-tax income of each segment, as well as the methodologies employed by the company to allocate shared expenses to the segments.

Other income increased 10.9 percent in 2000 from 1999 and declined 5.5 percent in 1999 from 1998. The increase was primarily a result of gains from sales of available-for-sale securities held by the company, partially offset by lower interest income. The decline in 1999 versus 1998 was primarily due to lower interest income.

Provision for Income Taxes

The provision for income taxes resulted in an effective tax rate of 29.8 percent for 2000, compared with the 1999 effective tax rate of 34.4 percent and a 1998 effective tax rate of 30.0 percent. The 4.6 point decrease in the 2000 rate from the 1999 rate and the 4.4 point increase in the 1999 rate from the 1998 rate were primarily the result of the company's 1999 sale of its Global Network business and various other actions implemented during 1999.

As reflected in the reconciliation of the company's effective tax rate in note O, "Taxes," on pages 80 and 81, the increased benefit on the company's tax rate of the foreign tax differential in 2000 was principally due to the U.S. tax benefit from the repatriation of profits previously subject to foreign taxes, partially offset by a less favorable mix of profits arising in markets with lower effective tax rates. The decreased benefit of the foreign tax differential from 1998 to 1999 primarily reflects a less favorable mix of profits arising in markets with lower effective tax rates.

FOURTH QUARTER

The company's fourth-quarter results reflect the momentum that has been building steadily all year. For the quarter ended December 31, 2000, the company had revenue of $25.6 billion, an increase of 5.9 percent (12 percent at constant currency) compared with the fourth quarter of 1999. Fourth quarter 2000 net income was $2.7 billion ($1.48 per diluted common share), compared with net income of $2.1 billion ($1.12 per diluted common share) in the fourth quarter of 1999.

In the Americas, fourth-quarter revenue was $10.8 billion, an increase of 3.3 percent (4 percent at constant currency) from the 1999 period. Revenue from Europe/Middle East/Africa was $7.4 billion, up 3.0 percent (18 percent at constant currency). Asia Pacific revenue increased 13.3 percent (20 percent at constant currency) to $5.0 billion. OEM revenue increased 13.4 percent (14 percent at constant currency) to $2.4 billion compared with the fourth quarter of 1999.

Hardware revenue increased 9.7 percent (15 percent at constant currency) to $11.4 billion from the fourth quarter of 1999, with revenue growth across all server, storage and technology hardware categories. The company began shipping its new z900 server in mid-December, contributing to a greater than 100 percent increase in shipments of mainframe computing capacity in the fourth quarter, as measured in MIPS. Revenue grew strongly for the pSeries UNIX servers, with particular strength in the mid-range and high-end Web server models. Revenues for the mid-range iSeries servers also increased, with growth across all geographic areas. Personal Systems revenue grew significantly and the unit was profitable in the quarter. Microelectronics revenue also increased strongly, principally due to continued acceleration in growth of sophisticated, leading-edge custom chips. Revenue for HDDs increased as well. Excluding networking products, storage revenue increased, driven by Shark and shipment of its advanced functions.

Revenue from Global Services, including maintenance, grew 5.2 percent (12 percent at constant currency) in the fourth quarter to $9.2 billion, reflecting revenue growth across all services categories. e-business services revenue grew more than 70 percent year over year. Revenue comparisons for Global Services were adversely affected by a year-over-year decline in the Y2K services business and the sale of the Global Network in 1999. After adjusting for these factors, Global Services revenue (excluding maintenance) increased 10.1 percent (17 percent at constant currency). The company signed more than $12.5 billion in services contracts in the quarter.

Software revenue totaled $3.6 billion, decreasing 1.0 percent (up 6 percent at constant currency) versus the fourth quarter of 1999. Revenues continued to grow strongly in the company's middleware segment, with significant growth in database and Web-management software. Tivoli revenues declined in the quarter, reflecting an ongoing transition in this product area.

Global Financing revenue increased 6.2 percent (10 percent at constant currency) in the fourth quarter to $1.0 billion, primarily as a result of increased sales of used equipment.

Revenue from the Enterprise Investments/Other area, which includes custom hardware and software products for specialized customer uses, declined 10.7 percent (3 percent at constant currency) year over year to $425 million.

The company's total gross profit margin was 37.7 percent in the fourth quarter of 2000 compared with 36.7 percent in the fourth quarter of 1999. The increase was driven by a 3.5 point improvement in the hardware gross profit margin as eServer, personal computer and HDD gross profit margins improved year over year. In addition, the Global Financing gross profit margin increased 6.1 points, primarily as a result of higher margins for hardware remarketing. These increases were partially offset by a decline in the Global Services gross profit margin of 0.9 points. This decline was primarily driven by lower Business Innovation Services revenue, which benefited from Y2K services in 1999, partially offset by an improvement in the Strategic Outsourcing Services gross profit margin.

Total fourth-quarter 2000 expense declined 0.3 percent when compared with the fourth quarter of 1999. SG&A expense decreased 2.4 percent, primarily driven by the effects of currency, while RD&E expense increased 2.4 percent year over year. The expense-to-revenue ratio in the fourth quarter of 2000 was 23.0 percent, compared with 24.4 percent in 1999.

The company's tax rate was 29.5 percent in the fourth quarter, down slightly as compared with 30.0 percent in the fourth quarter of last year.

The company spent approximately $1.4 billion on common share repurchases in the fourth quarter. The average number of common shares outstanding assuming dilution was lower by 57.2 million shares in fourth quarter 2000 versus fourth quarter 1999, primarily as a result of these repurchases. The average number of shares assuming dilution was 1,790.6 million in fourth quarter 2000 versus 1,847.8 million in fourth quarter 1999.

FINANCIAL CONDITION

During 2000, the company continued to demonstrate strong financial performance, enabling it to make significant investments to fund future growth and increase shareholder value without increasing its non-global financing debt. The company spent $5,645 million for research, development and engineering, excluding $9 million of IPR&D; $4,360 million for plant and other property, including machines used in strategic outsourcing contracts; $1,256 million for machines on operating leases with customers; and $6,659 million for the repurchase of the company's common shares. In addition, of the company's nine acquisitions in 2000, the company paid cash totaling approximately $300 million of the aggregate $511 million purchase price. The company had $3,722 million in cash and cash equivalents and current marketable securities at December 31, 2000. The company's debt levels remained essentially flat with a small increase in Global Financing debt, offset by a decline in non-global financing debt.

The company maintains a $10 billion committed global credit facility that expires in February 2002. As of December 31, 2000 and 1999, $9.1 billion and $8.6 billion were unused and available, respectively. In addition, the company had outstanding other committed and uncommitted lines of credit of approximately $4.7 billion and $5.5 billion as of December 31, 2000 and 1999, respectively. As of December 31, 2000 and 1999, $4.1 billion and $4.5 billion were unused and available, respectively.

The company managed assets of $136 million and $273 million at December 31, 2000 and 1999, respectively, from the securitization of loans, leases and trade receivables. For additional information, see note I, "Sale and Securitization of Receivables," on page 74.

The changes in the company's U.S. pension plan, including the increased benefits for retirees and the 1999 amendment to the plan, are not expected to have a material effect on the company's financial condition.

The major rating agencies' ratings of the company's debt securities and preferred stock as of December 31, 2000, appear in the table below:

	Standard and Poor's	*Moody's Investors Service*	*Fitch, Inc.*
Senior long-term debt	A+	A1	AA-
Commercial paper	A-1	Prime-1	F-1+
Preferred stock	A	a1	A+

Cash Flows

The company's cash flows from operating, investing and financing activities, as reflected in the Consolidated Statement of Cash Flows on page 68, are summarized in the following table:

(dollars in millions)	*2000*	*1999*	*1998*
Net cash provided from/ (used in):			
Operating activities	$ 9,274	$ 10,111	$ 9,273
Investing activities	(4,248)	(1,669)	(6,131)
Financing activities	(6,359)	(8,625)	(4,993)
Effect of exchange rate changes on cash and cash equivalents	(147)	(149)	120
Net change in cash and cash equivalents	$ (1,480)	$ (332)	$ (1,731)

Working Capital

(dollars in millions) AT DECEMBER 31:	*2000*	*1999*
Current assets	$ 43,880	$ 43,155
Current liabilities	36,406	39,578
Working capital	$ 7,474	$ 3,577
Current ratio	1.21:1	1.09:1

Current assets increased $725 million due primarily to an increase in accounts receivable of $3,108 million, offset by decreases of $2,109 million in cash and cash equivalents and current marketable securities, and $206 million in deferred taxes. The increase in accounts receivable was due to strong year-end business volumes and global financing activity in the software and services businesses across all geographies. The decrease in cash and cash equivalents and current marketable securities resulted primarily from stock repurchases and capital expenditures, partially offset by cash generated from operations.

The company ended 2000 with inventories of $4,765 million, the lowest level since 1983, primarily a result of lower inventory levels within Enterprise Systems segment and Microelectronics Division, and currency translation on inventories outside the United States. The company's inventory turnover ratio improved to 6.3 in 2000 from 5.9 in 1999.

Current liabilities declined $3,172 million from year-end 1999, primarily due to decreases of $4,025 million in short-term debt and $922 million in other accrued expenses and liabilities, offset by an increase in accounts payable of $1,792 million. The increase was primarily due to strong year-end business volumes, primarily in the Enterprise Systems segment, across all geographies.

Investments

The company's investments for plant, rental machines and other property were $5,616 million for 2000, a decrease of $343 million from 1999.

In addition to software development expenses included in research, development and engineering, the company capitalized $565 million of software costs during 2000, an increase of $101 million from the 1999 period. The increase resulted, in part, from the adoption of Emerging Issues Task Force Issue No. 00-2, "Accounting for Web Site Development Costs." In 2000 the company capitalized $81 million of certain Web site development costs.

Investments and sundry assets were $14,447 million at the end of 2000, an increase of $775 million from 1999, primarily the result of increases in prepaid pension assets and deferred taxes, offset by declines in alliance investments and goodwill. See note H, "Investments and Sundry Assets," on page 74 for additional information.

The company continues to invest significantly in its rapidly growing services business, primarily in the management of customers' information technology and in manufacturing capacity for microelectronics. The company has announced plans to redirect approximately $1 billion in 2001 to the open-source Linux operating system including hardware and software development, the operation of its Linux Technology Center, and various marketing initiatives across the country. Additionally, the company plans to invest $4 billion over the next three years in the information technology outsourcing sector.

On October 10, 2000, the company announced plans to invest $5.0 billion in the following projects: (1) building an advanced chip-making facility in East Fishkill, New York; (2) expanding its chip-making capacity in Burlington, Vermont and Yasu, Japan, as well as at a joint venture in Essonnes, France; and (3) expanding its organic and ceramic chip packaging operations worldwide. The company anticipates these actions to be completed over the next four years.

The company has remaining authorization as of December 31, 2000, to purchase $2,870 million of IBM common shares in the open market from time to time, based on market conditions.

The company expects to fund these investments primarily with cash from ongoing operations.

Debt and Equity

The majority of the company's funding is executed by Corporate Treasury in support of the Global Financing segment. A process has been established for monitoring the Global Financing funding requirements and executing strategies to manage the company's overall asset and liability profile. Additionally, the company maintains sufficient flexibility to access global funding sources as needed. During 2000, the company issued debt denominated in U.S. dollars, Japanese yen, Euros and Swiss francs to meet existing financing needs.

The company's total debt increased $222 million to $28,576 million. Financing businesses have different capital structures than non-financing businesses, and therefore the analysis of this change and certain ratios are discussed below on both a Global Financing and a non-global financing basis.

GLOBAL FINANCING

(dollars in millions)

AT DECEMBER 31:	*2000*	*1999*
Assets*	$ 40,822	$ 39,686
Debt**	27,514	26,799
Equity	4,142	4,864
Debt/Equity	6.6x	5.5x

* *Global Financing assets include cash, financing receivables (see note F, "Financing Receivables," on page 74), intercompany amounts, rental machine fixed assets and other assets.*

** *Global Financing debt includes external debt of the Global Financing business that generates the interest expense included in Cost of Global Financing on the Consolidated Statement of Earnings. Global Financing debt also includes intercompany borrowings from other company units. The total interest expense related to Global Financing debt is presented in note X, "Segment Information," on pages 89 through 93.*

The Global Financing segment is a financial services business and is, therefore, more debt dependent than the company's other businesses. At December 31, 2000, more than 95 percent of the company's total debt was attributable to this business, and supported almost half of the company's total assets. In 2000, Global Financing debt to equity ratio increased to 6.6x, which is within management's acceptable target range. Typically, a financial services business has a higher leverage than an industrial or technology business given its low return on asset characteristics.

NON-GLOBAL FINANCING

(dollars in millions)

AT DECEMBER 31:	*2000*	*1999*
Debt*	$ 1,062	$ 1,555
Debt/Capitalization	6.1%	9.0%
EBITDA/Interest Expense**	24x	19x

* *Non-global financing debt is the company's total external debt less the Global Financing debt described in the Global Financing table above.*

** *EBITDA is earnings before interest and taxes, plus depreciation and amortization, adjusted for minimum rental commitments and for one-time items such as the 1999 actions and the sale of the Global Network. The interest expense used in the denominator represents the company's total interest expense less the Global Financing interest expense disclosed in note X, "Segment Information," on pages 89 through 93.*

The company's non-global financing businesses generate significant cash from ongoing operations and therefore generally do not require a significant amount of debt. Cash flows from operations are these businesses' primary source of funds for future investments.

The company's total consolidated stockholders' equity increased $113 million to $20,624 million at December 31, 2000, primarily due to the increase in retained earnings, partially offset by the company's ongoing stock repurchase program and Accumulated gains and losses not affecting retained earnings. (See note M, "Stockholders' Equity Activity," on page 79).

Currency Rate Fluctuations

Changes in the relative values of non-U.S. currencies to the U.S. dollar affect the company's results. At December 31, 2000, currency changes resulted in assets and liabilities denominated in local currencies being translated into fewer dollars than at year-end 1999. The currency rate changes had an unfavorable effect on revenue growth of approximately 3 percent in 2000, minimal effect in 1999 and an unfavorable effect of approximately 2 percent in 1998.

For non-U.S. subsidiaries and branches that operate in U.S. dollars or whose economic environment is highly inflationary, translation adjustments are reflected in results of operations, as required by Statement of Financial Accounting Standards (SFAS) No. 52, "Foreign Currency Translation." Generally, the company manages currency risk in these entities by linking prices and contracts to U.S. dollars and entering into foreign currency hedge contracts.

The company uses a variety of financial hedging instruments to limit specific currency risks related to financing transactions and other foreign currency-based transactions. Further discussion of currency and hedging appears in note K, "Financial Instruments," on pages 76 and 77.

On January 1, 2001, the company adopted SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities." The company does not expect this standard to have a significant impact on the Consolidated Statement of Earnings. This standard will result in an incremental gross-up of certain assets and liabilities, including fair value adjustments to the company's portfolio of fixed-rate debt. In addition, the standard may result in increased volatility within the stockholders' equity section of the Consolidated Statement of Financial Position (Accumulated gains and losses not affecting retained earnings). See note B, "Accounting Changes," on pages 71 and 72 for additional information regarding SFAS No. 133.

Market Risk

In the normal course of business, the financial position of the company routinely is subject to a variety of risks. In addition to the market risk associated with interest rate and currency movements on outstanding debt and non-U.S. dollar denominated assets and liabilities, other examples of risk include collectibility of accounts receivable and recoverability of residual values on leased assets.

The company regularly assesses all of these risks and has established policies and business practices to protect against the adverse effects of these and other potential exposures. As a result, the company does not anticipate any material losses from these risks.

The company's debt in support of the Global Financing business and the geographic breadth of the company's operations include an element of market risk from changes in interest and currency rates. The company manages this risk, in part, through the use of a variety of financial instruments including derivatives, as explained in note K, "Financial Instruments," on pages 76 and 77.

To meet disclosure requirements, the company performs sensitivity analysis to determine the effects that market risk exposures may have on the fair values of the company's debt and other financial instruments.

The financial instruments that are included in the sensitivity analysis comprise all of the company's cash and cash equivalents, marketable securities, long-term non-lease receivables, investments, long-term and short-term debt and all derivative financial instruments. The company's portfolio of derivative financial instruments includes interest rate swaps, interest rate options, foreign currency swaps, forward contracts and foreign currency option contracts.

To perform sensitivity analysis, the company assesses the risk of loss in fair values from the effect of hypothetical changes in interest rates and foreign currency exchange rates on market-sensitive instruments. The market values for interest and foreign currency exchange risk are computed based on the present value of future cash flows as affected by the changes in rates that are attributable to the market risk that is being measured. The company selected the discount rates that it used for the present value computations based on market interest and foreign currency exchange rates in effect at December 31, 2000 and 1999. The differences in this comparison are the hypothetical gains or losses associated with each type of risk.

Information provided by the sensitivity analysis does not necessarily represent the actual changes in fair value that the company would incur under normal market conditions because, due to practical limitations, all variables other than the specific market risk factor are held constant. In addition, the results of the model are constrained by the fact that certain items are specifically excluded from the analysis, while the financial instruments that relate to the financing or hedging of those items are included by definition. Excluded items include leased assets, forecasted foreign currency cash flows, and the company's net investment in foreign operations. As a consequence, the reported changes in the values of some financial instruments that affect the results of the sensitivity analysis are not matched with the offsetting changes in the values of the items that those instruments are designed to finance or hedge.

The results of the sensitivity analysis at December 31, 2000, and December 31, 1999, are as follows:

INTEREST RATE RISK

As of December 31, 2000, a 10 percent decrease in the levels of interest rates with all other variables held constant would result in a decrease in the fair value of the company's financial instruments of $99 million as compared with a decrease of $164 million as of December 31, 1999. A 10 percent increase in the levels of interest rates with all other variables held constant would result in an increase in the fair value of the company's financial instruments of $83 million as of December 31, 2000, as compared with an increase of $145 million as of December 31, 1999. Changes in the relative sensitivity of the fair value of the company's financial instrument portfolio for these theoretical changes in the level of interest rates primarily are driven by changes in the company's debt maturity and interest rate profile and amount. In 2000 versus 1999, the reported decline in interest rate sensitivity primarily is due to adjustments in the company's "receive fixed/pay floating" interest rate swap portfolio to more closely match the maturity profile of the company's fixed rate debt.

FOREIGN CURRENCY EXCHANGE RATE RISK

As of December 31, 2000, a 10 percent decrease or increase in the levels of foreign currency exchange rates against the U.S. dollar with all other variables held constant would result in a decrease in the fair value of the company's financial instruments of $1,352 million or an increase in the fair value of the company's financial instruments of $1,435 million, respectively, compared with a decrease of $1,319 million or an increase of $1,340 million, respectively, as of December 31, 1999. The change in the relative sensitivity of the fair value of the company's financial instrument portfolio to the level of foreign currency exchange rates was primarily driven by increased hedging activity of foreign currency transactions in accordance with the company's established risk management practices. As the effect of offsetting changes in the fair market value of the company's anticipated foreign currency cash flows are not included in the sensitivity model, the results of the analysis are not indicative of an increase in the company's actual exposure to foreign currency exchange rate risk.

Financing Risks

Global Financing is an integral part of the company's total worldwide offerings. Inherent in Global Financing are certain risks, including credit, interest rate, currency and residual value. The company manages credit risk through comprehensive credit evaluations and pricing practices. To manage the risks associated with an uncertain interest rate environment, the company pursues a funding strategy of substantially matching the interest rate profile of its debt with the interest rate profile of its assets. Currency risks are managed by denominating liabilities in the same currency as the assets.

Residual value risk is managed by developing projections of future equipment values at lease inception, reevaluating these projections periodically, and effectively deploying remarketing capabilities to recover residual values and potentially earn a profit. The following table presents the recorded amount of unguaranteed residual values for sales-type and operating leases as of December 31, 1998, 1999 and 2000. In addition, the table presents the run out of the unguaranteed residual value over the remaining lives of these leases as of December 31, 2000. The following table excludes approximately $34 million of estimated residual value associated with non-information technology equipment. There was no significant change in the ratio of the unguaranteed residual value to total net investment in sales-type leases from December 31, 1999 to December 31, 2000.

	Total			*Run out of 2000 Balance*			
(dollars in millions)	*1998*	*1999*	*2000*	*2001*	*2002*	*2003*	*2004 and beyond*
Sales-type leases	$ 685	$ 737	$ 751	$ 275	$ 273	$ 174	$ 29
Operating leases	731	609	396	230	124	37	5
Total residual value	$ 1,416	$ 1,346	$ 1,147	$ 505	$ 397	$ 211	$ 34

EMPLOYEES AND RELATED WORKFORCE

				Percentage Changes	
	2000	*1999*	*1998*	*2000-99*	*1999-98*
IBM/wholly owned subsidiaries	316,303	307,401	291,067	2.9	5.6
Less than wholly owned subsidiaries	21,886	17,176	21,704	27.4	(20.9)
Complementary	25,500	29,800	36,900	(14.4)	(19.2)

In 2000, the number of IBM employees, including employees in wholly owned subsidiaries, increased nearly 9,000 year over year. The company's strategic growth areas—services, software and technology—continue to drive the increase; Global Services hired in excess of 19,000 people in 2000. Acquisitions, such as the LGS Group Inc. in Canada, contributed to the increase, as well. The company continues to reduce its infrastructure and to withdraw from certain businesses, offsetting some of the growth.

The increase in employees in the less than wholly owned subsidiaries over 1999 reflects growth primarily in subsidiaries within the company's storage, personal computer and microelectronics businesses in China, and services in Japan and Australia.

The company's complementary workforce is an approximation of equivalent full-time employees hired under temporary, part-time and limited-term employment arrangements to meet specific business needs in a flexible and cost-effective manner.

CONSOLIDATED STATEMENT *of* EARNINGS

INTERNATIONAL BUSINESS MACHINES CORPORATION

and Subsidiary Companies

(dollars in millions except per share amounts)

FOR THE YEAR ENDED DECEMBER 31:	*Notes*	*2000*	*1999**	*1998**
Revenue:				
Hardware		$ 37,777	$ 37,888	$ 36,096
Global Services		33,152	32,172	28,916
Software		12,598	12,662	11,863
Global Financing		3,465	3,137	2,877
Enterprise Investments/Other		1,404	1,689	1,915
Total revenue		88,396	87,548	81,667
Cost:				
Hardware		27,038	27,591	24,653
Global Services		24,309	23,304	21,125
Software		2,283	2,240	2,260
Global Financing	J	1,595	1,446	1,494
Enterprise Investments/Other		747	1,038	1,263
Total cost		55,972	55,619	50,795
Gross profit		32,424	31,929	30,872
Expense:				
Selling, general and administrative	P	15,639	14,729	16,662
Research, development and engineering	R	5,151	5,273	5,046
Other income		(617)	(557)	(589)
Interest expense	J & K	717	727	713
Total expense		20,890	20,172	21,832
Income before income taxes		11,534	11,757	9,040
Provision for income taxes	O	3,441	4,045	2,712
Net income		8,093	7,712	6,328
Preferred stock dividends		20	20	20
Net income applicable to common stockholders		$ 8,073	$ 7,692	$ 6,308
Earnings per share of common stock:				
Assuming dilution	S	$ 4.44	$ 4.12	$ 3.29
Basic	S	$ 4.58	$ 4.25	$ 3.38

Average number of common shares outstanding:
Assuming dilution: 2000—1,812,118,422; 1999—1,871,073,912; 1998—1,920,130,470
Basic: 2000—1,763,037,049; 1999—1,808,538,346; 1998—1,869,005,570

**Reclassified to conform with 2000 presentation.*
The accompanying notes on pages 69 through 93 are an integral part of the financial statements.

CONSOLIDATED STATEMENT *of* FINANCIAL POSITION

INTERNATIONAL BUSINESS MACHINES CORPORATION

and Subsidiary Companies

(dollars in millions except per share amounts)

AT DECEMBER 31:	Notes	2000	1999*
Assets			
Current assets:			
Cash and cash equivalents		$ 3,563	$ 5,043
Marketable securities	K	159	788
Notes and accounts receivable—trade, net of allowances		10,447	9,103
Short-term financing receivables	F	18,705	17,156
Other accounts receivable		1,574	1,359
Inventories	E	4,765	4,868
Deferred taxes	O	2,701	2,907
Prepaid expenses and other current assets		1,966	1,931
Total current assets		43,880	43,155
Plant, rental machines and other property	G	38,455	39,616
Less: Accumulated depreciation		21,741	22,026
Plant, rental machines and other property—net		16,714	17,590
Long-term financing receivables	F	13,308	13,078
Investments and sundry assets	H	14,447	13,672
Total assets		$ 88,349	$ 87,495
Liabilities and Stockholders' Equity			
Current liabilities:			
Taxes	O	$ 4,827	$ 4,792
Short-term debt	J & K	10,205	14,230
Accounts payable		8,192	6,400
Compensation and benefits		3,801	3,840
Deferred income		4,516	4,529
Other accrued expenses and liabilities		4,865	5,787
Total current liabilities		36,406	39,578
Long-term debt	J & K	18,371	14,124
Other liabilities	L	12,948	13,282
Total liabilities		67,725	66,984
Contingencies	N		
Stockholders' equity:	M		
Preferred stock, par value $.01 per share		247	247
Shares authorized: 150,000,000			
Shares issued and outstanding (2000 and 1999—2,546,011)			
Common stock, par value $.20 per share	C	12,400	11,762
Shares authorized: 4,687,500,000			
Shares issued (2000—1,893,940,595; 1999—1,876,665,245)			
Retained earnings		23,784	16,878
Treasury stock, at cost (shares: 2000—131,041,411; 1999—72,449,015)		(13,800)	(7,375)
Employee benefits trust (shares: 2000 and 1999—20,000,000)		(1,712)	(2,162)
Accumulated gains and losses not affecting retained earnings		(295)	1,161
Total stockholders' equity		20,624	20,511
Total liabilities and stockholders' equity		$ 88,349	$ 87,495

**Reclassified to conform with 2000 presentation.*

The accompanying notes on pages 69 through 93 are an integral part of the financial statements.

CONSOLIDATED STATEMENT *of* STOCKHOLDERS' EQUITY

INTERNATIONAL BUSINESS MACHINES CORPORATION

and Subsidiary Companies

(dollars in millions)	*Preferred Stock*	*Common Stock*	*Retained Earnings*	*Treasury Stock*	*Employee Benefits Trust*	*Accumulated Gains and Losses Not Affecting Retained Earnings*	*Total*
1998							
Stockholders' equity, January 1, 1998	$ 252	$ 8,601	$ 11,010	$ (86)	$ (860)	$ 899	$ 19,816
Net income plus gains and losses not affecting retained earnings:							
Net income			6,328				$ 6,328
Gains and losses not affecting retained earnings (net of tax):							
Foreign currency translation adjustments (net of tax benefit of $45)						69	69
Net unrealized losses on marketable securities (net of tax benefit of $36)						(57)	(57)
Total gains and losses not affecting retained earnings							12
Subtotal: Net income plus gains and losses not affecting retained earnings							$ 6,340
Cash dividends declared—common stock			(814)				(814)
Cash dividends declared—preferred stock			(20)				(20)
Common stock purchased and retired (113,993,636 shares)		(556)	(6,291)				(6,847)
Preferred stock purchased and retired (51,250 shares)	(5)						(5)
Common stock issued under employee plans (29,701,038 shares)		709	(1)				708
Purchases (9,100,678 shares) and sales (9,024,296 shares) of treasury stock under employee plans—net			(71)	(47)			(118)
Fair value adjustment of employee benefits trust		1,002			(994)		8
Tax effect—stock transactions		365					365
Stockholders' equity, December 31, 1998	$ 247	$ 10,121	$ 10,141	$ (133)	$ (1,854)	$ 911	$ 19,433
1999							
Net income plus gains and losses not affecting retained earnings:							
Net income			7,712				$ 7,712
Gains and losses not affecting retained earnings (net of tax):							
Foreign currency translation adjustments (net of tax expense of $180)						(546)	(546)
Net unrealized gains on marketable securities (net of tax expense of $456)						796	796
Total gains and losses not affecting retained earnings							250
Subtotal: Net income plus gains and losses not affecting retained earnings							$ 7,962
Cash dividends declared—common stock			(859)				(859)
Cash dividends declared—preferred stock			(20)				(20)
Treasury shares purchased, not retired (70,711,971 shares)				(7,192)			(7,192)
Common stock issued under employee plans (22,927,141 shares)		741	(1)				740
Purchases (6,418,975 shares) and sales (6,606,223 shares) of treasury stock under employee plans—net			(95)	(50)			(145)
Fair value adjustment of employee benefits trust		318			(308)		10
Increase due to shares issued by subsidiary		37					37
Tax effect—stock transactions		545					545
Stockholders' equity, December 31, 1999	$ 247	$ 11,762	$ 16,878	$ (7,375)	$ (2,162)	$ 1,161	$ 20,511

CONSOLIDATED STATEMENT *of* STOCKHOLDERS' EQUITY

INTERNATIONAL BUSINESS MACHINES CORPORATION

and Subsidiary Companies

(dollars in millions)	*Preferred Stock*	*Common Stock*	*Retained Earnings*	*Treasury Stock*	*Employee Benefits Trust*	*Accumulated Gains and Losses Not Affecting Retained Earnings*	*Total*
2000							
Stockholders' equity, December 31, 1999	$ 247	$ 11,762	$ 16,878	$ (7,375)	$ (2,162)	$ 1,161	$ 20,511
Net income plus gains and losses not affecting retained earnings:							
Net income			8,093				$ 8,093
Gains and losses not affecting retained earnings (net of tax):							
Foreign currency translation adjustments (net of tax expense of $289)						(531)	(531)
Net unrealized losses on marketable securities (net of tax benefit of $506)						(925)	(925)
Total gains and losses not affecting retained earnings							(1,456)
Subtotal: Net income plus gains and losses not affecting retained earnings							$ 6,637
Cash dividends declared—common stock			(909)				(909)
Cash dividends declared—preferred stock			(20)				(20)
Treasury shares purchased, not retired (58,867,226 shares)				(6,431)			(6,431)
Common stock issued under employee plans (17,275,350 shares)		615	1				616
Purchases (8,799,382 shares) and sales (9,074,212 shares) of treasury stock under employee plans—net			(259)	6			(253)
Fair value adjustment of employee benefits trust		(439)			450		11
Increase due to shares remaining to be issued in acquisition		40					40
Tax effect—stock transactions		422					422
Stockholders' equity, December 31, 2000	$ 247	$ 12,400	$ 23,784	$ (13,800)	$ (1,712)	$ (295)	$ 20,624

The accompanying notes on pages 69 through 93 are an integral part of the financial statements.

CONSOLIDATED STATEMENT *of* CASH FLOWS

INTERNATIONAL BUSINESS MACHINES CORPORATION

and Subsidiary Companies

(dollars in millions) AT DECEMBER 31:	*2000*	*1999*	*1998*
Cash flow from operating activities:			
Net income	$ 8,093	$ 7,712	$ 6,328
Adjustments to reconcile net income to net cash provided from operating activities:			
Depreciation	4,513	6,159	4,475
Amortization of software	482	426	517
Deferred income taxes	29	(713)	(606)
Gain on disposition of fixed and other assets	(792)	(4,791)	(261)
Other changes that (used)/provided cash:			
Receivables	(4,720)	(1,677)	(2,736)
Inventories	(55)	301	73
Other assets	(643)	(130)	219
Accounts payable	2,245	(3)	362
Other liabilities	122	2,827	902
Net cash provided from operating activities	9,274	10,111	9,273
Cash flow from investing activities:			
Payments for plant, rental machines and other property	(5,616)	(5,959)	(6,520)
Proceeds from disposition of plant, rental machines and other property	1,619	1,207	905
Investment in software	(565)	(464)	(250)
Purchases of marketable securities and other investments	(1,079)	(3,949)	(4,211)
Proceeds from marketable securities and other investments	1,393	2,616	3,945
Proceeds from sale of the Global Network	—	4,880	—
Net cash used in investing activities	(4,248)	(1,669)	(6,131)
Cash flow from financing activities:			
Proceeds from new debt	9,604	6,133	7,567
Short-term (repayments)/borrowings less than 90 days—net	(1,400)	276	499
Payments to settle debt	(7,561)	(7,510)	(5,942)
Preferred stock transactions—net	—	—	(5)
Common stock transactions—net	(6,073)	(6,645)	(6,278)
Cash dividends paid	(929)	(879)	(834)
Net cash used in financing activities	(6,359)	(8,625)	(4,993)
Effect of exchange rate changes on cash and cash equivalents	(147)	(149)	120
Net change in cash and cash equivalents	(1,480)	(332)	(1,731)
Cash and cash equivalents at January 1	5,043	5,375	7,106
Cash and cash equivalents at December 31	$ 3,563	$ 5,043	$ 5,375
Supplemental data:			
Cash paid during the year for:			
Income taxes	$ 2,697	$ 1,904	$ 1,929
Interest	$ 1,447	$ 1,574	$ 1,605

The accompanying notes on pages 69 through 93 are an integral part of the financial statements.