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Management Discussion

International Business Machines Corporation and Subsidiary Companies

response we have received from our client outreach demonstrates the confidence our clients have in NewCo's long-term value proposition to manage and modernize their mission-critical infrastructures.

Technology Support Services revenue of \$1,562 million declined 6.3 percent as reported (7 percent adjusted for currency), driven primarily by lower services due to Systems product cycles and lower volumes due to hardware consolidation and shift to cloud.

Within GTS, cloud revenue of \$2.5 billion grew 4 percent year to year as reported (1 percent adjusted for currency).

GTS gross profit margin of 35.9 percent improved 0.7 points in the fourth quarter of 2020 compared to the prior-year period. This improvement was driven by the restructuring of certain existing contracts and reduced activity in lower value offerings. GTS reported a pre-tax loss of \$353 million in the fourth quarter of 2020 compared to pre-tax income of \$645 million in the prior-year period. The pre-tax margin decreased 14.1 points year to year to (5.1) percent. The pre-tax loss and decline in pre-tax margin reflect the workforce rebalancing charge taken in the fourth quarter of 2020, which had 12.5 points of impact on the pre-tax margin. Through these workforce rebalancing actions, we are optimizing the NewCo business to have a leaner and more efficient operating model.

Systems

Systems revenue of \$2,501 million decreased 17.8 percent as reported (19 percent adjusted for currency) in the fourth quarter of 2020 compared to the same period in 2019. Systems Hardware revenue of \$2,077 million decreased 18.8 percent as reported (20 percent adjusted for currency), driven by product cycle dynamics in IBM Z, Power Systems and Storage Systems.

Within Systems Hardware, IBM Z revenue decreased 22.9 percent year to year as reported (24 percent adjusted for currency), compared to the fourth quarter of 2019, which was the first full quarter of shipments of the z15 mainframe. Clients in sectors such as banking and financial markets made purchases early in the cycle to manage through robust market volatility. However, clients in some other industries focused on cash preservation due to the current macroeconomic environment, delayed their purchases elongating the z15 adoption cycle. Our fourth-quarter 2020 performance reflected improved adoption of z15 in some of these industries.

Power Systems revenue declined 14.5 percent as reported (16 percent adjusted for currency) in the fourth-quarter 2020 compared to the prior-year period, driven primarily by declines in low-end and high-end systems reflecting the product cycles.

Storage Systems revenue decreased 14.9 percent as reported (17 percent adjusted for currency), driven primarily by declines in high-end storage systems, partially offset by growth in SAN. In the fourth-quarter 2019, we launched the DS8900 high-end system that is tightly integrated with the z15 mainframe, which drove strong performance in the prior-year period.

In the fourth quarter, Operating Systems Software revenue of \$423 million decreased 12.1 percent as reported (14 percent adjusted for currency) driven primarily by the IBM Z and Power Systems product cycles.

Within Systems, cloud revenue of \$1.1 billion decreased 18 percent as reported (19 percent adjusted for currency) in the fourth quarter of 2020 compared to the same period in 2019.

The Systems gross profit margin increased 3.8 points to 59.9 percent in the fourth-quarter 2020 compared to the prior year. Pre-tax income of \$455 million decreased 43.2 percent and the pre-tax margin decreased 7.9 points year to year to 16.9 percent. The gross profit margin expansion was driven primarily by improvements in IBM Z and Power Systems margins, partially offset by a mix within the hardware portfolio. The decline in pre-tax income and margin reflects the workforce rebalancing charge taken in the fourth-quarter 2020, which had 6.0 points of impact on the pre-tax margin.

Global Financing

Global Financing revenue of \$286 million decreased 4.8 percent year to year, primarily driven by declines in financing revenue partially offset by an increase in used equipment sales. Global Financing fourth-quarter pre-tax income decreased 22.6 percent to \$195 million and the pre-tax margin of 37.6