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International Business Machines Corporation and Subsidiary Companies

- Approximately 60 percent of our annual revenue is in recurring revenue streams;
- Our balance sheet remains strong with ample liquidity and access to capital.

All of this provides some level of stability, not only in our revenue, but also in profit and cash, as we continue to manage through these challenging times. However, in this macroeconomic environment, clients balanced near-term needs and opportunities for transformation. Their near-term priorities were focused on operational stability, flexibility and cash preservation, and as such, in 2020, we experienced some disruptions in transactional performance, shorter duration software transactions and delays in some services projects.

At the same time, this environment has only reinforced the need for clients to modernize their businesses to succeed in this new normal, with hybrid cloud and AI at the core of their digital transformations. While the current environment poses certain short-term challenges, it also presents long-term opportunities that IBM will seize as our open hybrid platform and AI-driven model delivers greater innovation, higher productivity and more strategic optionality to our clients.

Financial Performance Summary

In 2020, we reported \$73.6 billion in revenue and income from continuing operations of \$5.5 billion, which included a \$2.0 billion pre-tax charge for structural actions (primarily workforce rebalancing) in the fourth quarter to simplify and optimize our operating model. Operating (non-GAAP) earnings in 2020 were \$7.8 billion, which also included the charge for workforce rebalancing. Diluted earnings per share from continuing operations was \$6.13 as reported and \$8.67 on an operating (non-GAAP) basis. We also generated \$18.2 billion in cash from operations, \$10.8 billion in free cash flow and delivered shareholder returns of \$5.8 billion in dividends. With the unprecedented COVID-19 pandemic and macroeconomic uncertainty beginning in March 2020, client priorities shifted to maintaining operational stability, flexibility and preservation of cash. While there was continued demand for offerings that support their digital transformation, clients moved to shorter term duration engagements and prioritized operational expenditures over capital expenditures, which impacted the company's performance in 2020. However, our results reflect strong performance in hybrid cloud led by Red Hat, gross margin expansion and solid cash generation. We also continued to strengthen our position as a hybrid cloud platform and AI company through strategic organic investments and acquisitions.

Total consolidated revenue decreased 4.6 percent as reported and 4.7 percent adjusted for currency compared to the prior year. Excluding divested businesses and adjusted for currency, revenue decreased 3.5 percent. Cloud & Cognitive Software increased 2.1 percent as reported and 2 percent adjusted for currency, with strong performance from Red Hat, offset by declines in transactional performance in other areas of the portfolio. Within Cloud & Cognitive Software, Cloud & Data Platforms, which includes Red Hat, grew 20.9 percent as reported (20 percent adjusted for currency), while Cognitive Applications decreased 3.0 percent as reported (3 percent adjusted for currency), and Transaction Processing Platforms declined 16.8 percent as reported (17 percent adjusted for currency) reflecting the impacts of the macroeconomic uncertainty, with purchase deferrals and clients opting for shorter duration contracts. Global Business Services decreased 3.8 percent as reported and 4 percent adjusted for currency with declines across all lines of business due to project delays and less discretionary spending by clients. Global Technology Services decreased 5.7 percent as reported and 5 percent adjusted for currency with declines in Infrastructure & Cloud Services and Technology Support Services driven by lower business volumes primarily with clients in industries more impacted by the macroeconomic environment. Systems decreased 8.2 percent year to year as reported and 9 percent adjusted for currency due to product cycle dynamics. Across the segments, total IBM cloud revenue of \$25.1 billion in 2020 grew 19 percent as reported (18 percent adjusted for currency) and 20 percent excluding divested businesses and adjusted for currency.

From a geographic perspective, Americas revenue declined 6.0 percent year to year as reported (4 percent excluding divested businesses and adjusted for currency). Europe/Middle East/Africa (EMEA) decreased 3.3 percent (4 percent excluding divested businesses and adjusted for currency). Asia Pacific declined 3.5 percent (4 percent excluding divested businesses and adjusted for currency).

The consolidated gross margin of 48.3 percent increased 1.0 points year to year, and the operating (non-GAAP) gross margin of 49.3 percent increased 1.3 points versus the prior year, reflecting portfolio