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<<Unidentified Analyst>>

With that, I really I'm pleased to welcome IBM is being kind of the first company to agree to do these long-term plans for sustainable value creation. And it's often said that, it wouldn't be good if we involved the CFO's, why are they not involved in the conversation. So I think it's fitting, I think it's remarkable that we have the CFO from IBM giving the first presentation. So I'm very esteemed to welcome Martin Schroeter, who is the CFO from IBM.

He's been kind enough to join us, he has a hard stop at 2 O'clock. So we're not going to be able to get to everybody's questions. So point of order is that if anyone has questions that we're not able to get to, you can email sii@cecp.co and we'll get back to you with information very shortly once we compile all that.

So Martin was named Senior Vice President and CFO on January 1, 2014, he's previously General Manager of IBM Global Financing a position he's held since 2011 where he led the world's largest captive IT financer with the total asset base in excess of $37 billion, that's a big number. He also in his spare time served as IBM Treasurer, responsible for the Company's balance sheet, cash flow, capital structures, interest rates, currency risk management and a whole lot of other things that I understand very little about.

So with that, I'm pleased to welcome to the stage, Martin Schroeter.

<<Martin Schroeter, Senior Vice President and Chief Financial Officer>>

Thank you. Thank you very much I have – that was very nice, thank you. Now we're going to do this exactly like we do earnings calls then obviously you have to pretend I'm recorded. And then we don't get to do write-in questions at earning calls, I like that idea. I like the idea of actually writing the questions. I have a few charts that I'm going to refer to and based on this hopefully, we can make sure it all works and everyone can see it. But I wanted to start with the trends, we see in our industry that are fundamentally changing the way our industry is ordered, fundamentally changing the way IBM operates because those that transformation is really probably three transformations at once. And I'll talk more about that.

I'll talk a little bit about then the platforms we've built in order to be successful over the long-term given that industry. I'll talk a little bit about how we've differentiated ourselves and then I'm going to get into a couple of topics that I think are really critical particularly as we think about the long-term. One is how do we bring technology and bring

innovation into our clients in a way that gets accepted and can actually improve the work we do and improve our clients' outcomes.

And secondly, how do we build skills to make sure these systems can run over the long-term, it's a big, big challenge. So I'm going to kind of go through this in an order and presumably will have time left at the end for questions. So first I'm going to talk as I mentioned a little bit about the shifts in our industry and what's happening.

First and foremost and we've been pretty clear about this. We see data as the world's next great natural resource. Now that's not to say that, that we collectively haven't been using data to make decisions for a long, long time, we certainly have. But the creation of data now is at an unprecedented rate by some estimates as much as 80% of all the world's data has been created in the last few years alone.

So the point of the curve we are on is we're headed toward a massive increase in the amount of data and the thing that will transform industries, the element that will transform professions is how we capture that data and how we make better decisions out of it. I'm going to talk a little bit more about our perspective in a moment.

Secondly, there is this thing out there called the cloud. We participate obviously in this market but think about how you can get access to far, far more computing power, far, far more insight into all of the data sources you have. But you don't really buy something and set it up you actually just rent it if you will or you consume it as you need it. And so I'm going to talk a little bit about a cloud because there's obviously there's an economic element to this. But more importantly it's changing the business models that people can deploy and quite frankly, it's changing the agility at which clients have to move.

So the cloud isn't just about economics there are some economics to it but it's really about the agility you get from thinking about and operating in the cloud world. And then finally, as we've all seen over the last few years now almost decade there are fundamentally new ways that our clients engage with their customers. And therefore fundamentally new ways that we have to engage with our clients and that's not only creating again a lot of data, you can see how all these things are intertwined but it's also changing the way that enterprises think about how they interact with their clients.

They are thinking about that experience that the consumer experience if you will and what customers expect and what they're willing to give up in order to get a better experience and we've kind of shorthanded that here. But there are a lot of – an oversimplification to say that you're trading information for access to something and our clients are thinking about how do they use that – our clients are thinking about how do they make sure they understand the most about their customers and are able to serve themselves.

Between this idea that we have all this data, between this idea that we have these new cloud platform is being built and therefore we have access to computers that we never had access to before, and the idea that the world is changing, how it interacts with one

another and the new platforms by which companies interact with their clients. We are really undergoing three transformations at once. And we see it in our business and this is the journey that both IBM and we've been on with our clients.

Now we have a perspective on this, and I'll start by saying that when we take this idea of data and cloud and engagement, we shorthand all of that to say we've got a set of what we call strategic imperatives. And so for our business it's about 41% – last year it's about 41% of our overall revenue, are from these three areas of cognitive cloud and industry perspective businesses.

So we are making this transformation it reflects obviously what we see in our clients which is we are in a productivity business i.e. IT is there to deliver productivity to our clients and then they reinvest that to get new ways of reaching their clientele. So our revenue stream is not surprisingly look a lot like the transformation that our clients are going through, which is I need productivity out a part of my business. And then I'm going to reinvest that to do all these new things to learn new things about my clients to reach them in new ways and to build new platforms.

Our perspective on cognitive and this is a non-technical perspective. So let's just make sure we all understand that you don't have a researcher talking about cognitive to you. But here's my perspective, you can no longer, we can no longer program computers to find relationships in the data that we have. The pools of data are too big and quite frankly you don't really know what you're looking for. So when we think about why is cognitive the next step in analytics, it's because the amount of data that's coming in, in all forms structured and unstructured, it's video, it's sound, it's a lot of unstructured data we couldn't program it to say find the relationship between A and B that's what we used to do, that's what analytics and those are the kinds of programs we've been writing for a long, long time help our clients understand the relationship between one thing and another.

But in a world of cognitive it doesn't work, there's too much data coming in you're not sure of the relationships. So what we really needed to do, what we really have done it with Watson is find a way to interact with your data, find a way to take a pool of data what the researchers would call a corpus and within that corpus then find a way to interact and find insights within the data. That's my non-technical description of cognitive.

And I think in a world where we have not only new data coming in at an astounding rate but we've got a large, large pools of data from within our clients' own shops that is proprietary, large pools of data in their own shops that they want to learn from if these cognitive solutions that are going to drive the next level of insight and solve some of the world's toughest problems, so I'm going to come back to that in a moment. But when we think about for instance healthcare, we created a health business last year Watson Health.

Within that we put, we acquired some businesses that those businesses had their own data. So we now have about 200 million lives worth of healthcare data that our partners

use in order to learn about what they have in their data pools. We added to that about 30 billion images health care images, so that Watson can see and understand what is a certain condition look like and again our partners are accessing all of that data in order to help them diagnose disease.

So the idea of a system that you can program doesn't work you have to ingest data and find a way to interact with it and I think our Watson Health business is a good example of that. Secondly, all of that sits on a cloud again it's not too many companies, it's not too many enterprises in the world that could try to – it could afford to put together the kind of computing power you need to run a Watson. And so the access on the cloud is really done through what the programmers would call a API, Application Programming Interface, it's a way that program share information. So that our developers can write something that accesses Watson's conversation capabilities or Watson's insight capabilities and you don't have to have Watson sitting there, you have it again on the cloud.

Now clouds are important not only because of the cognition that you can get. But the IBM cloud also has the kind of security you would expect and the kind of robust scalability you would expect as well. And then we've added more to that Watson cloud, we have Weather data, we bought the digital assets of the Weather Company as an example. So we keep piling more and more cognition onto that cloud platform but at its very core it's a robust enterprise grade set of cloud capabilities with now data access capabilities to match, so that again, your insights against or in that cloud can provide insights to your business.

All of that gets delivered as you would expect in an industry context. So our experience in talking with our client base, our experience in 105 years now being in businesses that the industry definition, the industry context is really, really important. So the cloud we build for banking is not the same cloud we build for healthcare, for all the obvious reasons. And so when you put all those things together as I mentioned for us, its now 41% of our business but you can see the interplay between cloud and analytics and cognition and industry even though we kind of separate them into three unique things, you can see the interplay.

And so with the differentiation we've built now within our platforms, I think we're ready to take on what we think are the three big questions that our clients will be thinking about and addressing over the next I'd say few years. First and foremost, all of our clients will be thinking about what cloud platform should I be on? Now the answer will likely be more than one.

But our clients – enterprise clients will be thinking about a cloud platform. As I mentioned, we've built not only a scalable robust enterprise base but we have a lot of cognition and data that sits on top of it, so first and foremost what cloud platform.

Secondly, they'll be thinking about what is the AI or the cognitive platform that our clients will be choosing to go with. And these are important decisions because obviously you can't be training a whole lot of data, different pools of data you've got to find

something that works and you have to have a robust set of capabilities. Once you head down that path it's likely you're going to stick with, you're going to stick with that cognitive platform. So you're going to pick a cloud platform probably more than one you're going to pick a cognitive platform probably not more than one.

And then within that you also have to decide on what is your data model over the long – term. And what I mean by that simply is that Watson is built to make sure that your insights from your data will stay with you, stay with the enterprise. It's not ingesting data to make this big graph of data if you will, this big knowledge graph smarter for everybody but Watson is designed to make sure that if you're a bank and you're using Watson to help you navigate the regulatory process. Then you'll get the insights and you'll keep those, you're not making everybody in the banking industry smarter.

And that selection of data platform, you won't make it uniform for every part of your business. Obviously, if you are working on something that doesn't use your own data then you probably would be happy to share it. But for things that work on your own data you're probably happy to keep it yourself.

So we think again we're pretty well positioned to answer which cloud platform, which cognitive platform and what data model as we go – as we head into the next few years. All of that is built on what I would call this relentless focus on innovation and a relentless shift to value. That's the IBM financial model. So I'm going to talk – I'm going to put only one – its not even a numbers chart, I don't have any number other than the – but I'm going to put one financial model chart up there at the end. And you'll see that our revenue growth is fairly, we don't have a high revenue growth model because we really have a high value model.

So first and foremost, we have been investing in R&D for years and years and years, it's always been a big part of – it's always been a big part of how we have created differentiation within the IBM business model. Quite frankly it's the reason that our clients give us the work they give us because we run their most important processes it's the reason that 55 out of 57 of the leading banks run on IBM platform.

So it's the reason that IBM runs the reservation systems of the world and the supply chains of the world and the banking systems of the world because we continue and have always had a fierce dedication to investing in R&D.

Now I didn't put the dollars up but we put the number of patents and IBM last year again for the 24th year lead in the number of U.S. patents created. We broke the 8,000 mark last year for the first time any organization. Now I don't know that this is going to last forever. But what's important I think is that from a business model perspective, we recognize and stay keenly, keenly committed to driving innovation. This is only one measure of that, it's certainly not the only measure of that but our research labs around the world provide a very strong base of innovation.

Secondly, as I mentioned we have a high value model so we're always looking for how do we deliver value to our clients and that means that we have to manage the portfolio of businesses and be willing quite frankly to invest of things that don't have a lot of value in them. And invest in things that we do see a lot of value, so we put in on this chart, we put along the top row, the things that we've invested in of late we are fairly acquisitive, we've purchased roughly 150 companies over the last 10 years.

I don't know that will accelerate I don't know that will slow down in the future but I can tell you that acquisitions have been and will continue to be a big part of our model. And then on offsetting that or reducing the size of IBM in total are the things we divest, things that we don't see a long-term value in. And so while we've probably taken about 8 billion of revenue out of IBM over the last five years probably no impact to profit because none of these things had a lot of value if you will to our clients.

Now they have value in the places that they landed so that the businesses we divested fit nicely into – with some investment fit nicely into their new homes. And therefore our clients get value when they're outside of our model but we couldn't see given our investment choices how we could fuel the investment they needed in order to drive differentiation. So we've continued to divest.

I see now a portfolio that is pretty high value when we look at the segmentation that we work on. And we think about how all of that comes together in front of a client. I think we've divested of things now that it represents those that we couldn't really kind of get our head around and we'll continue to drive investment in the form of acquisitions. So again our base is really built on these really two simple ideas of one we have to continue to innovate for our clients and we have to continue to shift to where value is, where we see it in the marketplace.

That is a little bit of a background on IBM. I wanted to spend just a few minutes on these really two important topics. So I talked a bit about innovation, I talked about how the world – our world is changing rapidly and this idea that you need these cognitive systems in order to engage with your clients and you're going to be collecting and interacting – collecting data and interacting with your clients in a whole new way. So in that world that's changing fairly dramatically, we felt it important that we declare we, IBM declare what are our principles as we head into this cognitive era. And our principles cover the topics that you would expect. They cover the purpose, the transparency and the skills.

So first on purpose, I think it's important that our point of view it's important for our clients to understand. I think it's important for society to understand that we view cognitive systems, we view the purpose of IBM's cognitive systems to augment human intelligence, not to replace human intelligence. And the great – the best example right now it's been out for about a week and a half is what we just announced with H&R Block.

So H&R Block, a big tax preparer here in the U.S. they are going to put – they have now put Watson on the desk of every one of their clients service representatives in the H&R

Block retail shop. So when you go in I don't know if anybody in this room is going to use H&R Block, but if you go to H&R Block, you will be sitting down with someone who has Watson at their fingertips and is making them raising the level if you will and giving the whole inside of the tax code and Watson's ability to navigate the tax code based on tax base. We've raised the level of education that H&R Block has done for their retail store reps, we've raised what I think is the ability for an H&R Block to deliver service to their client base.

Now this was – and again we haven't replaced any of the reps it's just about raising their level. And again this is really for me the real purpose for us, the real purpose of what AI can do, it can augment the intelligence that, that people are delivering within their jobs. I'm going to come back to the idea of jobs in a moment. Secondly, we think it's really been important for IBM to be clear about when is AI being used. How's it being applied, what are the sources of data, how does that system, what's its rank order if you will on what it can provide, so if you were to go for instance and look at some of the health applications, where doctors are using Watson to understand better courses of treatment.

Watson gives that doctor not only what Watson thinks the best course is but it tells the doctor how it got there. It tells the doctor here's what I looked at. Here's where the linkages are and here's my probability that I'm right. Here's my confidence level if you will.

Again all designed to augment the doctor but really clear about the sources it used and I think the transparency. We feel the transparency in how these AI systems are used is really important. Again it's really built around this idea that over the long-term if you're going to use these, if you're going to change your business, if you're going to change the way you interact with the clients, you have to understand both how it's being used, where it's been used and where they're getting their data.

Who trains your data is important so as an example, we are now pushing into deeper into financial services we created another unit called Watson Financial Services, you can see how we name those things. Watson Financial Services is focused on helping our banking clients navigate what is probably one of the biggest challenges they have which is a regulatory environment around the world.

Thousands and thousands of pages of regulations not always consistent, very difficult to navigate and right now done by experts, so we bought the world's leading consulting firm in this called Promontory. And we're going to have Promontory train Watson to help us – help the banks navigate the field it's different, you can't just go search the web try to get all of the regulatory documents and say okay, I'm going to help you now navigate the regulatory environment.

It doesn't work that way and quite frankly we've estimated that as much as 80% of the world's data isn't searchable. You need private data, you need the data that fits within our clients' systems which means you also need to tell them how you're going to use it. And

you can see that again in our transparency, the insights that come from it stay with our clients.

Finally, I wanted to talk about skills, because we see it as one of our biggest challenges we hear it from our clients as one of their biggest challenges. How do you get the skills to run these systems over the long-term and we in IBM have committed to helping students and workers retrain and citizens get the skills they need in order to be relevant and productive in this new cognitive era.

Now the world creates a lot of PhDs not enough maybe but it creates a lot of PhDs and we got research centers full of PhDs. But there's also a lot of work that has to happen from those without a college degree, in fact a lot of our jobs and IBM don't require a college degree, high school yes, associate's degree yes, but not necessarily a college degree. And so we were thinking through how do we address this skills mismatch issue that we have and we've developed a program, a number of years ago back in 2011.

I'll show you how it's evolved in a moment but back in 2011, we developed a program called P-Tech, Pathways in Technology – the Pathways in Technology think about it that way. And what P-Tech is as we take kids traditionally who have been in underserved areas, first when we did it was in Brooklyn. I'll show you the list of where they are now. And in P-Tech, we've created the curriculum and the curriculum is focused on what do we feel based on everyday life in a data center, everyday life in a design studio.

What skills do you need in order to compete and to be successful in those environments and doesn't have to be again a college degree. So we take these kids in there and basically with two years of high school to go 10th, 11th, 12th sometimes we take them in 9th but we take these kids we put them through high school and then they do two years and get an associate's degree and then we hire them.

And we have partners in this who also obviously would love to hire them, we're just getting now the first kids coming out of this program. And we had a number of them with us not long ago and they are the most wonderful inspirational stories these lovely kids from Brooklyn who talk about how their friends now, ask them hey, I'm in college, should I really finish, you did P-Tech, you already working, fascinating story.

So we have in our design studios, they're just starting again now to come into the workforce but P-Tech has been a phenomenal success. Again really on this idea of collaborating between industry who knows what the job they have and an academic environment willing to and government in this case is willing to help create this curriculum.

And we've spread P-Tech now from, it started in Brooklyn, we've now – you can see the list of how it's expanded including Melbourne, Australia we have I think seven schools in Melbourne and now in Morocco as well in Casablanca.

So this is the program, this is an approach not the only one I'm going to come to another one in a moment. This is an approach to how we can scale now and get to what we call not – they're not white collar jobs, they're not blue collar jobs. They are new collar jobs. And it's a scalable approach to help fill the tens of millions of new collar jobs here in America. But these kids need the right skills so this program very well received when we sit down with government, we find that we're pretty much aligned perfectly with what they're trying to get done and we're really excited.

Now at the same time, we also view over the long-term there are going to be some new big labor pools created. In fact by 2040, I think the estimate I saw was that Africa's going to have the largest labor pool in the world by 2040. So we announced a couple of weeks ago based on our discussions with our clients.

Our clients will tell you the number one gap that they see in the labor market is skills, the skills that are coming out of the schools versus the skills that they need. So a few weeks ago, we announced a program called DNA, Digital - Nation Africa and within that we're investing $70 million in order to bring what we call digital skills, things that will make you competitive in a cognitive world, in a cloud world, things that will make you competitive in the labor force. And it'll reach – we think it'll reach 25 million kids over the next five years. That's phenomenal scale.

But again we collectively have to figure out what are we going to do with that big labor pool it's a hugely attractive if we can give them the right skills and if we can get them on a path to being competitive in this new collar world. So between things like P-Tech, between Digital - Nation Africa, there are answers out there to help the skills mismatch that we see. But we have to be willing to jump in with some investment. We have to be willing to jump in with some experience. And we have to be willing to take the lead to take the lead here in order to make it happen.

So between P-Tech and DNA, I think we'll have some pretty good success in there again they scale pretty well. So before I leave, I have to do. I am the CFO I'd be in trouble if I didn't do one financial chart. So very quickly with significant transformation in our industry, we've transformed fairly dramatically over the last 10 years we've divested as I said a fair few number of businesses.

We continue to invest for higher value. We have a model, a financial model that isn't going to produce a ton of growth kind of low single-digit revenue growth. But we do expect within that to continue to expand margins and we do expect that we can continue to both return capital to our shareholders as well as invest.

And in a 105 year old company, we do think about as stewards of this great institution we do think about what do we have to do now to make sure that we've got another 105 years at least ahead of us. So that's all I had from my comments, are we doing questions from?

<<Unidentified Analyst>>

Is the mic on, well thank you for that. I ask that great pivot between the financials to the purpose to the impact of all that. And what I'd like to do is field two questions. We have a hard stop maybe the clock can be reset so that we have and I asked the folks that the investors may have the first crack at the questions. And please avoid statements let's keep questions crisp, so we can end on time I promised to get him out at 2 O'clock. So with that, questions?

Q&A

<Q>: Thank you, absolutely phenomenal presentation. My question is about blockchain, what does it do for trust, what is your vision over the short-term as to how blockchain will evolve?

<A – Martin Schroeter>: Blockchain, it's a great question. So blockchain for us is sort of going to do for transactions what the Internet did for information. It's going to enable a whole new set of transactions between unknown parties in a way that kind of reorders if you will, everything that sits between.

So when you think about a supply chain today and we are spending time with – we have I think 40 or 50 blockchain implementations underway. When you think about supply chain and I'll tell you the one I know the best because it's within IBM, we have we're shipping goods to our distributors and to our business partners. And they're on occasion, they're dispute is not because of the products but because the state is rolling on the tax and both – so the dispute process from start to finish takes 60 to 65 days and obviously there's a whole lot of capital tied up within that process.

So just within global financing now which runs on a blockchain, we shortened the dispute cycle from about 70 days to about two. And so all of that as a CFO, you are looking well, I can get all the capital back now but when you think about not just supply chains when you think about clearing of securities, when you think about – we've got an easy supply chain, think about a global shipping firm that has multiple governments that they're dealing with, multiple importers, multiple bills of lading it's a phenomenally complex process. And blockchain will be the thing that allows you to massively reduce and take out a lot of poorly invested tied up capital to that.

<Q>: Thank you for that. One other question?

<Q – Mark McKeon>: Martin, thank you, those are excellent. Mark McKeon, State Street. ESG factors big data IBM in brief.

<A – Martin Schroeter>: We got a statement or a question. Yeah, so I think for IBM when I think about the investments we're making today. When I think about the path for instance that we've taken on Watson and how we've created a platform, when I think about our relentless shift of capital, when I think about us trying to solve these big problems like how do you fill these jobs, when I think about the kinds of skills we can

bring in quite easily. But we do other ones we have to remix, all of those problems to me are these long-term issues are not going to be solved overnight.

They're not going to be solved without a high conviction approach. Because our choice to divest for instance of our semiconductor manufacturing operations isn't one that's going to pay off – its not going to pay off this year, it's not going to pay off next year in fact I would bet we're not really going to pay off until 2020, 2021 because that's when the cost of building your own semiconductors for a subscale manufacturer like us become too overbearing and we would have had to go to our investors and say we need like $25 billion of capital to do it.

So IBM's culture has always been around managing for the long-term. Our ability to navigate that has improved with things like data, things like big data. So I think we're in an area where - we're in a transformation where we have a lot of change going on in the world, our long-term view though hasn't really wavered. We sit between technology and business if you will and our ability to bring value to our clients is really our ability to help them get value out of those two intersections their business and technology. We're not a consumer business, the closest we get to consumer now is our purchase of the Weather Company. So we're not – it's not like it's a thing we'll never do but we're really still not a consumer business.

We're still business to business and so when we step between those two intersections knowing our client base, knowing how fast they have to respond. We know that we're going to have to think long-term and use the tools the same thing, our clients are asking from us we do those internally as well. So it's quite an exciting I think as a CFO, quite an exciting time to think about how you make better decisions and how you can embed cognitive into everything we do.

<<Unidentified Analyst>>

Well, thank you, Martin. Just like financially timing wise you hit your numbers. So we are ending right at 2 PM. And thank you thank you very much.

<<Martin Schroeter, Senior Vice President and Chief Financial Officer>>

Thank you.