

IBM Corporation

In the seven years (since 1994), that Lou Gerstner reigned over IBM, the company's earnings per share increased an average of 27% per year. This remarkable increase in earnings did not go unnoticed by the securities markets. Indeed, the company's market value grew from less than \$30 billion to over \$200 billion during the period.

Use the following financial statement data to:

1. Decompose IBM's ROE (by quarter) and discuss the factors (and trends) that contribute to *Big Blue's* profitability
2. Evaluate IBM's Revenue growth, Receivables, and Gross margins and over the period. Be sure to control for seasonality (e.g., compute the same quarter to same quarter change in these items).
3. Evaluate IBM's Earnings per Share (basic), and Identify the factors most responsible for the increase in IBM's earnings

Write your answers in Standard English. Be specific in your references, provide details of your computations, and be thorough in your explanations – I cannot *read your mind*.

EXHIBIT 1

	IBM				
	Selected Earnings Per Share Data				
	For the Quarters Ended:				
	Jun-00	Mar-00	Dec-99	Sep-99	Jun-99
Earnings Per Share (from continuing operations)	1.06	0.83	1.12	0.90	0.91
Analyst Expected Earnings Per Share	1.00	0.77	1.06	0.90	0.88
Difference	0.06	0.06	0.06	-	0.03
% Surprise	6.00%	7.79%	5.66%	0.00%	3.41%

All of the financial data in the tables that follow (except “per share figures”), are in millions.

EXHIBIT 2

	IBM											
	<u>Earnings per Share*</u>											
	Jun-00	Mar-00	Dec-99	Sep-99	Jun-99	Mar-99	Dec-98	Sep-98	Jun-98	Mar-98	Dec-97	
Earnings per Share of Common Stock - Basic	\$ 1.10	\$ 0.85	\$ 1.16	\$ 0.97	\$ 1.32	\$ 0.80	\$ 1.27	\$ 0.80	\$ 0.77	\$ 0.54	\$ 1.08	
Average Number of Common Shares Outstanding - Basic	1,767.6	1,777.2	1,793.0	1,805.2	1,812.1	1,823.8	1,839.5	1,856.9	1,879.2	1,946.6	1,929.6	
Average Price per Share	\$ 109.34	\$ 111.00	\$ 102.95	\$ 123.61	\$ 116.48	\$ 88.28	\$ 82.91	\$ 62.20	\$ 57.97	\$ 51.12	\$ 52.05	
* All Data are Adjusted to Reflect stock splits					2 for 1 stock split 5/10/99							

EXHIBIT 2 (continued)

	Sep-97	Jun-97	Mar-97	Dec-96	Sep-96
Earnings per Share of Common Stock - Basic	\$ 0.69	\$ 0.73	\$ 0.59	\$ 0.99	\$ 0.62
Average Number of Common Shares Outstanding - Basic	1,956.0	1,973.8	2,006.8	2,053.6	2,087.4
Average Price per Share	\$ 52.13	\$ 42.78	\$ 36.45	\$ 36.61	\$ 31.65
* All Data are Adjusted to Reflect stock splits		2 for 1 stock split 5/9/97			

EXHIBIT 3

IBM										
Consolidated Statements of Income										
For the Quarters Ended:										
	Mar-00	Dec-99	Sep-99	Jun-99	Mar-99	Dec-98	Sep-98	Jun-98	Mar-98	Dec-97
Total Revenues	\$ 19,348	\$ 24,182	\$ 21,144	\$ 21,905	\$ 20,317	\$ 25,131	\$ 20,095	\$ 18,823	\$ 17,618	\$ 23,723
Cost of Sales	12,337	15,299	13,580	13,681	13,059	15,322	12,628	11,677	11,168	14,205
Gross Margin	7,011	8,883	7,564	8,224	7,258	9,809	7,467	7,146	6,450	9,518
Selling, General and Administrative Expenses	3,706	4,445	3,501	2,846	3,937	5,074	4,057	3,812	3,719	5,060
Research and Development	1,172	1,416	1,383	1,293	1,181	1,407	1,240	1,220	1,179	1,425
Total Operating Expenses	4,878	5,861	4,884	4,139	5,118	6,481	5,297	5,032	4,898	6,485
Operating Income	2,133	3,022	2,680	4,085	2,140	3,328	2,170	2,114	1,552	3,033
Other Income (Expense), net	189	134	134	155	134	187	122	130	150	173
Interest Expense	152	171	185	197	174	213	160	161	179	194
Income Before Taxes	2,170	2,985	2,629	4,043	2,100	3,302	2,132	2,083	1,523	3,012
Income Tax Expense	651	896	867	1,652	630	956	638	631	487	919
Net Income	\$ 1,519	\$ 2,089	\$ 1,762	\$ 2,391	\$ 1,470	\$ 2,346	\$ 1,494	\$ 1,452	\$ 1,036	\$ 2,093

EXHIBIT 3 (continued)

	Sep-97	Jun-97	Mar-97	Dec-96	Sep-96
Total Revenues	\$ 18,605	\$ 18,872	\$ 17,308	\$ 23,143	\$ 18,062
Cost of Sales	11,507	11,471	10,716	13,822	10,804
Gross Margin	7,098	7,401	6,592	9,321	7,258
Selling, General and Administrative Expenses	3,932	3,958	3,684	5,093	4,175
Research and Development	1,162	1,221	1,069	1,332	1,115
Total Operating Expenses	5,094	5,179	4,753	6,425	5,290
Operating Income	2,004	2,222	1,839	2,896	1,968
Other Income (Expense), net	162	137	185	181	183
Interest Expense	183	179	172	190	172
Income Before Taxes	1,983	2,180	1,852	2,887	1,979
Income Tax Expense	624	734	657	864	694
Net Income	\$ 1,359	\$ 1,446	\$ 1,195	\$ 2,023	\$ 1,285

EXHIBIT 4

IBM				
Consolidated Statements of Income				
For the Years Ended:				
	<u>1999</u>	<u>1998</u>	<u>1997</u>	<u>1996</u>
Sales	\$ 87,548	\$ 81,667	\$ 78,508	\$ 75,947
Cost of Goods Sold	55,619	50,795	47,899	45,408
Gross Margin	31,929	30,872	30,609	30,539
Research and Development Expense	5,273	5,046	4,877	4,654
Other Selling, General & Administrative Expense	14,729	16,662	16,634	16,854
Total Operating Expenses	20,002	21,708	21,511	21,508
Total Operating Income	11,927	9,164	9,098	9,031
Other Income (Expense) net	557	589	657	707
Interest Expense	727	713	728	716
EBT	11,757	9,040	9,027	9,022
Tax on EBT	4,045	2,712	2,934	3,158
Net Income	7,712	6,328	6,093	5,864

EXHIBIT 5

IBM				
Common Size Statements of Income				
For the Years Ended:				
	<u>1999</u>	<u>1998</u>	<u>1997</u>	<u>1996</u>
Sales	1.00	1.00	1.00	1.00
Cost of Goods Sold	0.64	0.62	0.61	0.60
Gross Margin	0.36	0.38	0.39	0.40
Research and Development Expense	0.06	0.06	0.06	0.06
Other Selling, General & Administrative Expense	0.17	0.20	0.21	0.22
Total Operating Expenses	0.23	0.27	0.27	0.28
Total Operating Income	0.14	0.11	0.12	0.12
Other Income (Expense) net	0.01	0.01	0.01	0.01
Interest Expense	0.01	0.01	0.01	0.01
EBT	0.13	0.11	0.11	0.12
Tax on EBT	0.05	0.03	0.04	0.04
Net Income	0.09	0.08	0.08	0.08

EXHIBIT 6

IBM
Consolidated Balance
For the Quarters

	Mar-00	Dec-99	Sep-99	Jun-99	Mar-99	Dec-98	Sep-98	Jun-98	Mar-98	Dec-97
Assets										
Cash	3606	5,831	\$ 6,026	\$ 7,241	\$ 5,356	\$ 5,768	\$ 5,869	\$ 5,471	\$ 5,889	\$ 7,553
Receivables, Inventory and Pre-Paid	35533	37,324	36,851	36,211	34,445	36,592	32,933	31,541	31,682	32,865
Total Current Assets	\$ 39,139	\$ 43,155	\$ 42,877	\$ 43,452	\$ 39,801	\$ 42,360	\$ 38,802	\$ 37,012	\$ 37,571	\$ 40,418
Property & Equipment (net)	16959	17,590	17,463	17,253	18,866	19,631	19,005	18,453	18,223	18,347
Investments and Other Assets	26666	26,750	25,035	22,642	23,084	24,109	21,912	21,647	22,150	22,734
Total Assets	\$ 82,764	\$ 87,495	\$ 85,375	\$ 83,347	\$ 81,751	\$ 86,100	\$ 79,719	\$ 77,112	\$ 77,944	\$ 81,499
Liabilities and Shareholders' Equity										
Accounts Payable, Taxes & Accruals	21767	25,348	\$ 23,682	\$ 21,248	\$ 19,753	\$ 22,922	\$ 18,275	\$ 16,779	\$ 17,325	\$ 20,277
Debt Maturing within One Year	13844	14,230	14,096	14,713	13,708	13,905	13,237	13,271	12,667	13,230
Total Current Liabilities	\$ 35,611	\$ 39,578	\$ 37,778	\$ 35,961	\$ 33,281	\$ 36,827	\$ 31,512	\$ 30,050	\$ 29,992	\$ 33,507
Long Term Debt	14295	14124	13,807	14,330	16285	15,508	15,239	14,590	15,029	13,696
Other Liabilities & Deferred Taxes	13340	13282	13,722	13,898	13,879	14,332	14,333	13,895	14,058	14,480
Total Liabilities	\$ 63,246	\$ 66,984	\$ 65,307	\$ 64,189	\$ 63,445	\$ 66,667	\$ 61,084	\$ 58,535	\$ 59,079	\$ 61,683
Total Shareholders Equity	19518	20,511	\$ 20,068	\$ 19,158	\$ 18,306	\$ 19,433	\$ 18,635	\$ 18,577	\$ 18,865	\$ 19,816
Total Liabilities and Shareholders' Equity	\$ 82,764	\$ 87,495	\$ 85,375	\$ 83,347	\$ 81,751	\$ 86,100	\$ 79,719	\$ 77,112	\$ 77,944	\$ 81,499

EXHIBIT 6 (continued)

	Sep-97	Jun-97	Mar-97	Dec-96
Assets				
Cash	\$ 6,486	\$ 6,861	\$ 6,463	\$ 8,137
Receivables, Inventory and Pre-Paid	31,704	31,778	30,857	32,558
Total Current Assets	\$ 38,190	\$ 38,639	\$ 37,320	\$ 40,695
Property & Equipment (net)	17,921	17,647	17,062	17,407
Investments and Other Assets	22,182	22,533	22,145	23,030
Total Assets	\$ 78,293	\$ 78,819	\$ 76,527	\$ 81,132
Liabilities and Shareholders' Equity				
Accounts Payable, Taxes & Accruals	\$ 18,072	\$ 18,531	\$ 17,998	\$ 21,043
Debt Maturing within One Year	12,518	14,028	13,243	12,957
Total Current Liabilities	\$ 30,590	\$ 32,559	\$ 31,241	\$ 34,000
Long Term Debt	13,623	11,675	10,402	9,872
Other Liabilities & Deferred Taxes	14,324	14,476	14,933	15,632
Total Liabilities	\$ 58,537	\$ 58,710	\$ 56,576	\$ 59,504
Total Shareholders Equity	\$ 19,756	\$ 20,109	\$ 19,951	\$ 21,628
Total Liabilities and Shareholders' Equity	\$ 78,293	\$ 78,819	\$ 76,527	\$ 81,132

Chart 1

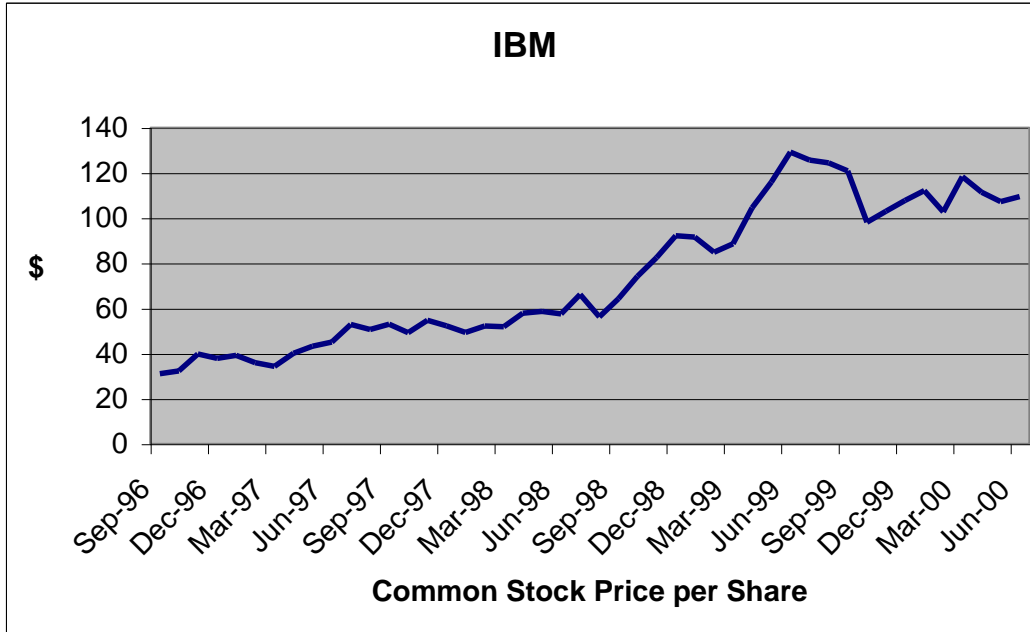


Chart 2

