



The Silver Word

## **International Business Machines Corporation**

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A mixed prognosis lies ahead for Big Blue. International Business Machines has top class abilities in computing expertise and their ecommerce solutions are the best in the business. However, the company is laden with debt and can't seem to move fast enough like the other lean and mean machines of the New Economy.

Established in 1911, IBM uses advanced information technology to provide customer solutions. The company is segmented into five divisions: Hardware (technology, personal systems and servers), Global Services, Software, Global Financing and Enterprise Investments. In 1999, the hardware division represented the bulk of their business: 42% of revenues and 49% of gross profits. Headquartered in Armonk, New York, IBM is located in 165 countries and its employee count as of December 1999 was 307,401.

When Louis V. Gerstner became Chairman and CEO in 1993, the company was in need of a strategic turnaround. Despite mounting pressure to split IBM into separate independent units, Gerstner kept it together. One of IBM's strengths was in its ability to provide integrated solutions for customers and with the rise of the Internet and network computing, IBM was ahead of the pack. In 1995 IBM acquired Lotus Development Corporation and a year later, acquired Tivoli Systems Inc. Services became the fastest growing segment of the company with growth of more than 20 percent per year. From 1993 to 1996, the market value of the company increased by more than \$50 billion. In May 1997, IBM demonstrated Deep Blue, a 32-node IBM RS/6000 commuter, programmed to play chess on a world-class level. Deep Blue's calculating power, accessing 200 million chess moves per second, had a wide range of applications from weather forecasting to financial modeling.

Today, IBM delivers a full range of innovative, integrated ebusiness solutions to a variety of industries, education, healthcare and government organizations. The company manufactures over 40,000 products including desktop computers, notebooks, workstations, servers, software and networks.

IBM's ecommerce services incorporate assessments and strategy workshops to the planning and implementation of specific business solutions. Ecommerce includes web application development, procurement services, knowledge management, custom systems Integration, enterprise resource planning, supply chain management, business intelligence and customer relationship management.

In February of this year, IBM joined Cisco Systems to provide their customers with IBM's host integration software which enables web access to applications and data that reside on host computers. In April, S1 Corporation and IBM announced a global strategic alliance to deliver ebusiness solutions to assist financial institutions that offer Internet based corporate banking. The S1 Corporate Suite on the IBM platform enables banks to offer their clients a wide range of online cash and asset management services.

June was busy month for the company. IBM, Siebel Systems, Intenia International and Mercury Systems aligned to develop and market a comprehensive set of integrated ebusiness airline applications. Secondly, IBM and nine other companies created e2open.com, a global business-to-business emarket place for the computer, electronics and telecommunications industries. The nine other companies are Hitachi, LG Electronics, Matsushita Electronic, Nortel Networks, Seagate Technology, Solectron, Toshiba, Ariba and i2. e2open.com's electronic marketplace brings together thousands of companies to plan, manage and execute supply-chain transactions over the Internet.

Year-end revenues increased by only 7% in 1999 to \$87.5 billion from \$81.7 billion in 1998. However net income increased 22% to \$7.7 billion and earnings per share increased by \$0.87 per share from 1998 to \$4.25 per share in 1999. It was a record year for net income and earnings, as ebusiness services revenues grew at an extraordinary 60% from a year ago. Moreover, IBM generated strong cash flows and completed 17 acquisitions.

However the company's capital structure is rather irksome: debt levels were close to 60% in 1998 and 1999. In addition, the long-term debt to equity ratio was close to 80% in 1998 and 70% in 1999. The company can obviously handle the debt as times interest earned, an indication of solvency, increased from 12.9 in 1998 to 16.4 in 1999. More to the fact, two inventory measures in particular look worrisome. Inventory turnover, an indication of the number times dollars invested in inventory are completely recovered through sales, increased from 9.8 in 1998 to 11.1 in 1999. This means more dollars are being invested in inventory. Days to Turn Over Inventory decreased from 37.4 in 1998 to 33.0 in 1999. This implies that inventories are being converted to account receivables at a slower rate in 1999 versus 1998. On other words, IBM is investing more in inventories in order to maintain sales. Again, not a good sign.

So it is a mixed bag for IBM. First quarter revenues declined by 5% from the year ago quarter to \$19.3 billion and net income increased a meager 3%. Lately the stock has come back, closing at 116 13/16 as of the June 15<sup>th</sup> close. But until more solid financial indications are apparent, cautious optimism reigns for Big Blue.

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