

What is the employment relationship for 21st century work, and 21st century workers?

What are the mutual commitments and expectations of employer or employee with regard to effort, ethics, results and rewards?

How does that relationship create the ongoing ability to learn, to be heard and to grow a career?

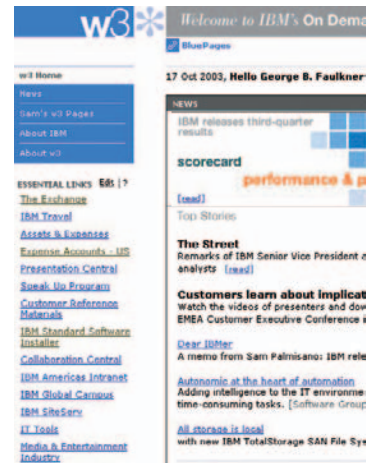
At IBM, we think the answer is simple to state—and tough to accomplish. It's expressed in the recognition that every individual in the company is an adult with the smarts, skills and responsibility to direct his or her own life.

It's premised on the opportunity—available to all employees—to contribute to the upper limits of their potential, and be compensated for it.

We believe it includes the guarantee of a safe, inclusive work environment that rewards excellence, fosters innovation, and values diversity of culture, background and thought, as well as an unflinching commitment to marketplace success.

Only then can a company create the highest level of opportunity, and the broadest employment for the greatest number of people.

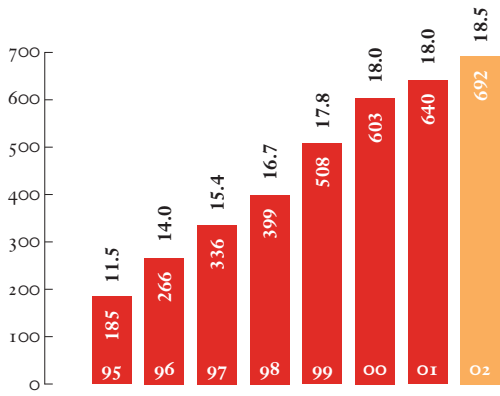
In the three years that
Training Magazine has ranked
top 100
CORPORATE PROGRAMS,
 only IBM has made
 the top five each year



More than half of IBM's
 SENIOR-MOST MANAGEMENT TEAM
 are women,
 U.S. ethnic minorities,
 or non-U.S. born

Nearly 70% OF IBM
 EMPLOYEES view the
 company intranet
 as vital to their jobs

WOMEN EXECUTIVE POPULATION GROWTH
 (percent of total executive workforce)



COMPENSATION AND BENEFITS

The IT industry of the 1960s, '70s, and even the early 1980s had far fewer participants, meaning IBM faced far less competition for marketshare, as well as talent. Our compensation systems reflected that environment — focused more on job security than on continual learning and evolving job opportunity; more on the consistency and predictability of pay than on pay based on individual performance and on the company's overall competitiveness. That was then.

Today, employee compensation and rewards at IBM are designed to drive a culture of high performance. During the last 10 years, the company revamped its reward strategy, focusing far more of its total compensation investment on programs that reward and recognize results, and minimizing rewards based on tenure.

Our overall compensation strategy is designed to:

Pay competitively — based on market rates in the IT industry and within any geography where we compete for talent.

Pay for performance — focused on results, not for effort and years of service, and recognizing the relative contribution of team members.

Differentiate strongly — distributing a proportionately larger share of the rewards to our highest contributors.

This broad-based focus on market-based pay reflects a significant departure from the past compensation investment strategy at IBM.

The pay-for-performance strategy is essential to attract and retain the talent we need to drive marketplace performance, and to re-establish IBM as the agenda setter for the industry, as well as our clients' most expert and capable partner.

Investment in Pay

Business performance directly affects how much money a company can — and should — invest in pay for its people.

During the recent IT industry downturn in many countries, IBM continued to invest in its people, reflecting our generally stronger business performance relative to competitors and the commitment to pay for performance. As a result, IBM was one of the few major IT companies able to provide employee base pay increases in both 2002 and 2003, and to pay employee bonuses in both years, as well.

ADDITIONAL PAY OPPORTUNITY

In addition to competitive base pay, every IBM employee worldwide has additional pay opportunities directly tied to individual and business performance. The type of opportunity depends on an individual's job responsibilities. Consultants in our services business are eligible for performance bonuses; salespeople receive sales commissions; executives are eligible for incentive pay; and everyone else is eligible for a program called "variable pay" that provides the opportunity for additional payments based on business results and individual performance.

Starting in the mid-1990s, IBM has issued approximately \$11 billion in variable pay to employees worldwide. Today, variable pay is designed to deliver between 6 percent and 9 percent of an employee's base pay when business and individual targets are met.

EQUITY OWNERSHIP

In recent years, IBM has also embarked on an aggressive expansion of equity ownership, making changes to align the interests of top contributors at all levels with those of our other shareholders.

As part of this effort, IBM has dramatically expanded the number of nonexecutive employees who are granted equity awards, increasing from fewer than 1,500 non-executive stock option holders at the end of 1995 to more than 78,000 in 2002, a year when about 3,800 executives held options.

GROWTH IN EMPLOYEE STOCK OPTIONS
(total number of nonexecutive employees with stock options)

Year	Total
1995	1,418
1996	1,995
1997	3,256
1998	13,712
1999	36,479
2000	60,136
2001	70,192
2002	78,012

Our approach to equity awards contrasts with the trend at most other IT companies, which typically grant options annually to a broader percentage of employees. IBM (which has a longer history of public ownership than any other IT company) has adopted a strategy that is more selective. While employees at every level are eligible for equity consideration, by design, grants are typically awarded only to top performers, whose skills are most critical to business success.

Employees' options vest 25 percent each year over four years, but remain eligible for exercise for a total of 10 years.

In addition to the global stock option program, IBM also makes a global stock purchase program available, so that IBMers can periodically buy discounted company stock. More than 150,000 employees worldwide participate in this voluntary program.

Today, nonexecutive employees own more than 7 percent of outstanding company shares. Directors and executive officers own just under 1 percent, as disclosed in the financial annual report.

Since 1995, an average of 4.4 percent of all stock option awards at IBM went to the top five company executives. In 2002, the total was less than 1 percent. That compares with an average of 29 percent awarded to the top five executives at the 1,500 largest U.S. companies between 1992 and 2001, according to research conducted at Rutgers University.

EXECUTIVE COMPENSATION

Both employee and executive compensation are built on a fundamental commitment to pay for performance. The differences are primarily of degree — all executives have a much greater share of overall compensation at risk than employees, reflecting their higher levels of direct influence over company results. There is also greater focus on equity ownership for executives, further reflecting their ability to influence business results.

While all executives are eligible for incentive and equity awards, not all executives receive them, in keeping with the broad focus on performance. In 2002, due to business conditions, IBM did not provide merit increases to executives. However, as noted earlier, nonexecutive employees did receive merit increases. In 2003, we took further steps to lower the overall value of executive compensation, leading market trends in this area.

IBM's senior-most leaders — about 300 men and women worldwide — are expected to own defined levels of company stock, linked to their responsibilities and pay levels, and they are not allowed to sell any company stock unless these ownership requirements are met.

Finally, IBM's executive compensation practices and programs are regularly reviewed by a committee of the Board of Directors that is made up solely of independent directors.

OTHER AWARDS AND RECOGNITION

The commitment to pay for performance is complemented by a wide range of other award and recognition programs.

In 2002, 107,180 awards were granted to employees, ranging from gift certificates to cash awards. Also in 2002, 66,838 employees sent a company-provided gift to a peer in recognition of a job well done.

Benefits

Total compensation also includes the value of the IBM benefits programs—an investment that can add as much as 25 percent or more in value to an employee’s pay. Benefits, and the value delivered, vary country by country, due to differences in local customs and laws.

IBM benefits are designed to attract and retain employees in ways that are both sensitive to local customs and competitive within the IT marketplace. Benefits help employees pay for healthcare and set aside money for retirement, and encourage time off and provide support during periods of crisis, such as disability.

To the greatest extent practical, programs provide employees with choices to meet personal needs that may change over time. In many countries around the world, IBM offers employees a flexible menu of benefit options. In Canada and Australia, for example, employees are provided with a core set of benefits plus an allocation of “credits” that they can use at their discretion to choose additional levels of coverage under those programs that matter most to them.

Through “You and IBM,” the company’s global human resources intranet, employees have access to detailed information on benefit plans, along with reminders and features to help employees make the most of the available programs.

HEALTH BENEFITS

IBM defrays the costs of health services for employees, either directly through private employer-sponsored coverage in the United States and Canada; or indirectly through government-required contributions to state-sponsored programs, which are common in Europe and parts of Asia.

In 2003, IBM completed work on a global healthcare strategy that focuses on quality as well as cost, and promotes prevention as a key plank in the overall health benefits platform. We have been actively involved in groups focused on improving healthcare quality while lowering costs in the United States, where the approach to healthcare differs from the approach in many other countries where we do business.

While IBM’s primary commitment is to provide access and to help defray the cost of healthcare for active employees, the company also contributes to post-employment healthcare or provides access to IBM health plans, depending on local practice. In the United States, for example, IBM spends approximately \$600 million annually on retiree healthcare and an additional \$200 million in Medicare taxes to provide health coverage for about 120,000 U.S. retirees, plus family members.

IBM benefits programs can add as much as **25 PERCENT OR MORE** in value to base pay

RETIREMENT BENEFITS

IBM provides retirement benefits to regular employees directly through company-sponsored plans, through contributions to state-sponsored programs, or through a combination of both, depending on local practices. Plans are funded according to country requirements and guidelines.

In most countries, IBM offers either a defined benefit or a defined contribution retirement plan, with both available to at least half our population. In the United States, the company’s 401(k) match is made entirely in cash, with employees free to invest the money among more than 20 different investment options.

In mid-2003, a U.S. federal district court judge ruled that in his view the way IBM’s U.S. pension plan accrues benefits violates the age discrimination provisions of the Employee Retirement Income Security Act (ERISA), as amended. IBM strongly disagrees with the ruling and plans to appeal. The ruling stems from a lawsuit filed in 1999.

Workforce Reductions

As indicated in the profile of IBM's business portfolio in the first section of this report, a workforce—especially in this hyper-competitive and constantly changing industry—is not a static asset. There's an ongoing rebalancing—adding skills that are in high client demand, as well as reducing our presence in areas that no longer fit the strategy to lead in high-value market segments.

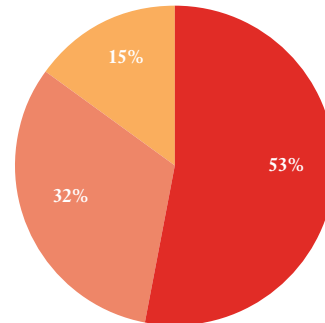
In 2002, for example, IBM hired more than 12,000 people, and about 20,000 IBM employees (roughly 6 percent of IBM's total workforce) lost jobs in resource actions. This was in addition to the changes from acquisitions and divestitures mentioned in the Our Company section of this report.

Having resource actions affect 6 percent of the global workforce in 2002 was atypical. The average for the prior three years was 2 percent each year.

During 2002, a nearly equal number of people left IBM—through divestitures, outsourcing or resource actions—as joined, so that IBM ended the year with about 316,000 employees, compared to roughly 320,000 the year before.

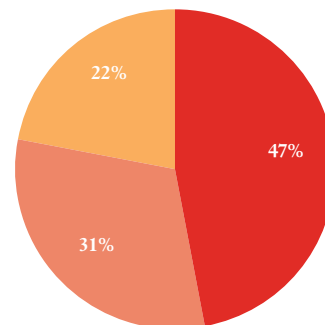
IBM's assistance package for employees affected by resource actions includes a range of benefits to help them through the transition period to their next job. Specifics vary by country. For example, in the United States, this support includes advance notification, so employees have time to look for a new position, supported by an internal job posting system that allows them to see and apply for job openings throughout the company. If they leave IBM, these employees receive severance pay, plus career transition services for 120 days, as well as financial planning services, retraining assistance (\$2,500 to help develop skills for a new career), subsidized post-employment medical benefits plus group life insurance during the period of transition.

2002 GEOGRAPHIC
WORKFORCE DISTRIBUTION



● Americas ● Europe, Middle East, Africa ● Asia

2002 GEOGRAPHIC
REVENUE DISTRIBUTION*



● Americas ● Europe, Middle East, Africa ● Asia

*Excludes OEM revenue, which accounted for 4 percent of IBM's total revenue in 2002.

EMPLOYEE WELL-BEING

The creation and maintenance of a contemporary workplace is about more than an environment that's safe and free of harassment of any kind. IBM's programs to promote employee well-being span proactive wellness initiatives through innovative workplace design.

All these initiatives are directed by IBM's Well-Being Management System (WBMS)—the company's holistic approach to managing the health and safety of employees wherever they work. To achieve that, our management system integrates and centralizes several previously self-standing programs, including occupational medicine, safety, industrial hygiene, employee well-being and ergonomics. This management system has been implemented in manufacturing, development and services organizations across IBM.

Programs include training for employees joining IBM via acquisitions, support for employees working in client locations and initiatives to enhance safety at newly acquired facilities.

While the WBMS is designed to drive improvements consistently around the world, it also accommodates customized programs that meet particular local needs. Examples include accessibility management in Guadalajara, Mexico; online ergonomics training in Japanese, French, German and Spanish; drinking water quality issues in India; injury/illness case management in China and Japan; establishing the foundation for medical Employee Assistance Programs in India and China; Occupational Safety and Health Administration (OSHA) Voluntary Program Protection plan certification in the United States; and work/life balance programs in Germany and Hungary.

Each year, a targeting process considers new global objectives and links them with local well-being activities. IBM identified 14 programs for special emphasis in 2002, including ergonomics, contractor safety, health promotion, indoor air quality, life safety, business transformation, mobility, workplace climate and medical services.

As one example, 34 IBM locations set specific targets for further improving ergonomics programs. These objectives ranged from upgrading chairs and workstations, to increasing ergonomics awareness among laptop users, boosting participation in ergonomics classes and reducing ergonomic-related injuries in manufacturing.

WORKPLACE SAFETY

The commitment to workplace safety was first formalized as a corporate policy in 1967. Today, IBM's safety record continues to be among the best in industry, as documented in continued year-to-year reductions in the rates of illness and injury as measured by the U.S. Occupational Safety and Health Administration. In 2002, IBM recorded a 17 percent drop from 2001 in the OSHA rate.

A number of IBM sites in the United States have received OSHA's highest recognition as Voluntary Protection Program (VPP) Star sites. They include IBM's sites in Rochester, Minn.; San Jose, Calif.; and Yorktown Heights, N.Y. Sites are re-evaluated every three to five years for continual improvement.

The chart below presents IBM U.S. rates, along with the rates for general industry and peer industry sectors. Even as IBM has made the transition from a company with a large manufacturing workforce to a company with a larger number of services professionals, the OSHA rate for this mixed occupation workforce is significantly below the peer computer and semiconductor injury rate, and is below the peer services rate.



These are the rates for total work-related injury/illness cases reported under the U.S. Occupational Safety and Health Act. In addition to lost-time cases, they include cases that required medical treatment or restricted the employee's work activity. Some numbers have been updated from prior years. Industry peer data for 2002 is not yet available.

The table on page 33 details the performance results of IBM's safety programs in a sampling of countries with manufacturing or hardware development operations in 2002. IBM consistently demonstrates low lost workday case rates (a measurement of injury/illness severity and business impact).

When an illness or injury occurs, the objective is threefold: help restore the employee's health as soon as possible, prevent further occurrence, and help support the employee during his or her time off from work. In many countries, IBM employees injured in the workplace are eligible for workers' compensation benefits.

In the United States, the 2002 number of claims per 100 employees decreased by 22 percent from the previous year. The total claims cost rose by 2.5 percent, reflecting factors including increased medical costs and inflation.

IBM's focus on workplace safety extends to contractors working on IBM premises and includes providing information regarding working safely, reviewing potentially high-risk work activities and, where concerns are identified, directing that they be addressed.

CRISIS MANAGEMENT

The IBM emergency planning process has successfully handled the response to numerous emergencies and disasters over many years. However, the events of September 11, 2001, raised both the nature and potential magnitude of these events, creating the need to build on our response processes on a national and global basis.

In order to handle crisis management situations that have companywide implications, IBM added in 2001 a Corporate Crisis Management Team (CCMT) to its existing emergency process.

Structure

The CCMT supports the existing crisis management structures at the country level or at an individual site by providing corporate advice and counsel, and resources as required.

Members

The CCMT is represented by the following primary functions: communications, finance, human resources, global well-being services, legal, security, facilities/real estate, technology, manufacturing and development, and sales and distribution.

Principles of Operation

The executive team members for an affected country or site have the flexibility to act without direct senior executive management approval as long as the actions are appropriate to their immediate responsibilities or to the location(s) they manage.

Corporatewide guidance will be provided by the CCMT or by the appropriate corporate or geographic senior executive using the existing communications infrastructure. Any public statement concerning IBM's response to a crisis must be reviewed by corporate communications.

Crisis management teams in individual locations receive annual training that includes possible responses to hostilities and terrorism, and course materials regarding management of a terrorist event are available to the entire global well-being services community.

WHO'S ON THE local crisis team?

The crisis team includes the location executive or manager and representatives from human resources, communications, finance, legal, security, global well-being services and facilities.

Since September 11, 2001, at least two members of the well-being staff have been assigned to help each local team. They can access experts in ionizing radiation, anthrax, personal protective equipment, heating, ventilation and air conditioning, smallpox, and nerve agents.

These global well-being services experts also stay current with changes in threat potential, detection, remediation and cleanup.

GLOBAL WELLNESS & HEALTH PROMOTION

Health promotion brings preventive health services to all IBM employees. The wellness process is designed to promote behaviors conducive to good health, and allow employees to take full ownership of their well-being with the support of global well-being services and health benefits and their management.

Preventive Health Services

Programs include primary prevention efforts, including immunizations, fitness and nutrition, stress management, weight control, smoking cessation, ergonomics and prevention of injuries. Secondary prevention efforts include programs that focus on early diagnosis and prevention, such as screenings, targeted examinations and disease management.

The objectives of these programs are global, but their program development and implementation are customized to address local issues and cultures.

One of the main portals on IBM's w3 intranet Web site — "Your Health" — enables all IBM employees in the United States to find information about their healthcare benefit options (13 in all, covering medical, dental and mental healthcare), along with material on ergonomics, personal wellness and workplace safety.

Employees also have access to tools for interactive health risk assessments, creating an electronic health record, tracking targeted health improvement programs, analyzing medical symptoms, learning about medical tests and procedures, evaluating potential medication interactions and searching a vast health library.

A Web portal released in 2002 provides well-being professionals with resources and information on organizational contacts, references, forums, professional self-assessment tools, skills and education toolkits, ongoing learning, measurements and best practices.

CLEANROOMS

As noted in last year's IBM Environment and Well-Being Report, questions have been raised about possible adverse health effects associated with chemicals in semiconductor and disk drive cleanrooms. Lawsuits have been filed in New York, California and Minnesota by some current and former IBM employees against chemical suppliers, and in some cases against IBM. While IBM sympathizes with anyone who develops a medical problem, the company does not believe there is a causal relationship between these health issues and the chemicals used in cleanrooms.

The company has programs in place for regular reviews of cleanroom operations. These reviews show that the use of chemicals in cleanrooms and other areas is being properly managed, and that employees are well-informed about both the substances present and the requisite safety procedures.

WORK/LIFE BALANCE

For the last quarter century, a major focus of IBM's efforts to help employees balance the demands of the workplace and the pressure of their private lives has come in the areas of child and eldercare.

In response to the increasing number of dual-income households and working single parents, IBM in 1983 launched the first national corporate childcare initiative, giving employees immediate access to childcare experts. Then, in the late 1980s, issues related to the aging population began to drive a new set of requirements — on individuals and employers.

In 1990, IBM created its Funds for Dependent Care Initiatives (FDICI) to increase the availability and quality of dependent care programs, and provide referrals to senior housing, meal delivery and transportation services. Funded at \$25 million for the first five years, the program enabled IBM to invest in more than 400 child and eldercare projects in more than 50 communities.

LOST WORKDAY CASE RATE PER 100 EMPLOYEES

Country		98	99	00	01	02
Canada	IBM	0.06	0.07	0.11	0.08	0.10
	Available Peer Industry	0.71	0.61	0.61	n/a	0.44
China	IBM	0.00	0.16	0.15	0.12	0.05
	Peer Industry	n/a	n/a	n/a	n/a	n/a
France	IBM	0.36	0.34	0.24	0.25	0.18
	Available Peer Industry	0.93	0.93	0.94	0.87	n/a
Hungary	IBM	0.36	0.50	0.57	0.24	0.19
	Peer Industry	n/a	n/a	n/a	n/a	n/a
Ireland	IBM	0.28	0.23	0.29	0.25	0.11
	Available Peer Industry	n/a	1.29	1.20	1.06	n/a
Japan	IBM	0.01	0.01	0.00	0.01	0.02
	Available Peer Industry	0.02	0.09	0.06	0.04	0.06
Mexico	IBM	0.12	0.00	0.00	0.02	0.00
	Peer Industry	n/a	n/a	n/a	n/a	n/a
Singapore	IBM	0.22	0.11	0.05	0.14	0.43
	Available Peer Industry	0.06	0.12	0.06	0.43	0.39
U.K.	IBM	0.21	0.30	0.19	0.22	0.14
	Available Peer Industry	0.51	0.54	0.56	0.56	n/a
U.S.	IBM	0.34	0.46	0.36	0.36	0.23
	Available Peer Industry	1.85	1.70	1.35	0.80	n/a

n/a = Not Available

The injury rates in this sampling of countries assume an average of 2,000 hours worked per employee per year. The U.K. and Singapore data pertain only to injuries with three or more days lost time. Because of the differences in governmental reporting requirements, a direct comparison between countries is not appropriate. Where available, the peer industry rate is an estimate of the average rate for companies doing a type of work similar to that done by IBM in that country. Some country numbers have been updated from prior years.

During the latter half of the 1990s, the program was expanded to include investments in 1,200 child and elder-care projects in 66 communities, leading to programs that created 61,000 new “spots” for children or seniors in need of care.

In 2001, responding to employee surveys that indicated child and eldercare were increasing concerns worldwide, the program was transformed into the Global Work/Life Fund with a five-year, \$50 million commitment. It was the first fund of its type to address employee issues on a global basis. Among the program’s goals:

- **Global work/life**—providing a complete range of dependent care services, with the specific objective of increasing the number of women in the workforce.
- **Use of IBM technology**—providing IBM computers with age-appropriate educational software to childcare centers and school programs. IBM is a major supporter of SeniorNet, an organization that teaches older adults how to use computers, and the genesis of Generations On Line, a software program that makes it easier for seniors to use the Net.

Since 1983, IBM has committed more than \$200 million to dependent-care programs and services around the world.

ACCESSIBILITY

IBM’s history of leadership in developing accessible solutions for people with disabilities is backed by a corporate instruction that calls for the company to make its information technologies widely available and accessible to people with special needs.

A worldwide Accessibility Center in IBM Research supports IBM’s commitment to accessible software, hardware, documentation and services.

Central to our nondiscrimination policies is a commitment to integrate people with disabilities into the workplace so that they have the necessary access to the facilities and technology to perform their jobs.

In 2002, IBM’s Real Estate Site Operations function enhanced its programs to better prioritize and accelerate appropriate accessibility improvements in our facilities.

Full assessments have been completed for 57 of the highest-priority sites globally (85 percent) and upgrade work has begun. Among identified improvements: constructing or upgrading ramps, modifying door widths, adjusting heights of telephones and elevator controls, installing visual alarm strobe lights and Braille signs, and modifying showers and closets in some IBM residence facilities.

WELLNESS AND HEALTH PROMOTION

	LIFE AT HOME	LIFE IN THE WORKPLACE
Preventive and Wellness Programs	<ul style="list-style-type: none"> • Work/Life Balance Programs • Flexible Work Options • Leaves of Absence <i>Programs that allow employees to work with their managers to modify their work schedules, or to take months off to balance their work and life</i> • Employee Assistance Program <i>Professional counseling for a broad range of concerns, including substance abuse and depression</i> • Health Promotion <i>Tools and information that help employees to take responsibility for their health</i> 	<ul style="list-style-type: none"> • Accident/Illness Prevention <i>Workplace health and safety programs, such as protective equipment and safety training</i> • Quality of Workplace Environment <i>Programs to make the workplace more comfortable, including proper lighting and other ergonomic considerations</i> • Quality of Facilities <i>Building and fire safety, and accessibility for persons with physical disabilities</i>
Healthcare Management Programs	<ul style="list-style-type: none"> • Disability Management <i>Support to help employees obtain appropriate healthcare, and to identify and obtain the accommodations necessary to facilitate their return to work</i> • Disease Management <i>Voluntary, free program to help people with certain conditions take an active role in managing their health</i> 	<ul style="list-style-type: none"> • Temporary Assignment • Progressive Return to Work <i>Accommodations that allow an employee with health-related limitations to continue working or to return to work after an illness leave</i>



WHEN STANDARD HEALTH PLANS ARE NOT ENOUGH

BY GWYNNETH STAPLES

Nurse and Director of IBM's South Africa Medical Center

AIDS CLAIMED more than 3 million lives in 2002. An estimated 5 million people acquired the human immunodeficiency virus (HIV) last year alone.

One of the highest rates of HIV/AIDS in the world is here in my home country, South Africa. In some areas, more than 30 percent of the population is HIV positive.

In the face of this threat, IBM launched an HIV/AIDS education and awareness program for its South African employees and suppliers. Voluntary counseling and testing have been available since the early 1980s.

More recently, we installed two self-service information kiosks in our South African headquarters in Johannesburg, because for many people, lectures or seminars simply don't work. People either don't want to be seen at the lectures, or can't organize their work schedules to fit them in.

With the kiosks and our intranet, people can access this content in their own time and at their own pace, finding the information that is relevant to their own circumstances. In addition to providing self-service access to potentially life-saving information, the local prevention program includes treatment, including Highly Active Anti-Retroviral Therapy (HAART), condom distribution, sexually transmitted infection treatment, and regular monitoring by doctors and counselors.

Since we launched this awareness program, absenteeism for HIV-positive employees dropped from approximately 25 days to three days per year. That's good for the company, but better for our colleagues.

IN JAPAN, IBM'S STRESS MANAGEMENT COURSES ARE
A MODEL AMONG OTHER INFORMATION TECHNOLOGY COMPANIES

IN 2002, MORE THAN 12,500 U.S. EMPLOYEES TOOK ADVANTAGE
OF FREE SCREENINGS FOR CHOLESTEROL, BLOOD PRESSURE, BLOOD SUGAR,
BODY COMPOSITION AND BONE DENSITY.

AFTER SCREENING, AN E-MAIL-BASED PROGRAM PROVIDES
TARGETED INFORMATION AND REFERRALS TO OTHER IBM INTERVENTIONS
BASED ON THE HEALTH RISK PROFILE

1937 *Paid vacation schedule*

1944 *Sickness and accident income plan*

1956 *Leave of absence program*

1966 *Special care for children assistance program*

1972 *Adoption assistance*

1980 *Flexible work schedules*

1983 *Childcare referral service*

1988 *Eldercare consultation and referral service*

1990 *Funding for dependent care initiatives*

1997 *Regular part-time work options*

Leadership accessibility products include:

Home Page Reader, which brings the Internet to blind and low-vision users, applying voice to guide users in exploring the World Wide Web. It enables people with low vision to resize windows and panes; change font size, type and color; and change background colors to make the screen easier to see. In addition, the Voice of Home Page Reader uses the IBM ViaVoice text-to-speech synthesizer to speak Web-based information aloud as it is presented on the computer screen.

WebSphere Voice Server, which includes tools that enable developers to build and deploy voice-enabled e-business solutions, using industry standard technology such as Java technologies and VoiceXML.

Workforce Relations

IBM and its employees continue to maintain strong relationships based on fairness, open communication and mutual respect. The company places a premium on understanding and responding quickly to employee concerns, and has established several formal channels, which are detailed in the Communications Channels discussion beginning on page 42.

Throughout the company's history, IBM has respected the rights of employees to organize, and has made managers at all levels aware of those rights. It is our long-standing belief, however, that the interests of IBM and its employees are best served when managers and employees deal directly with each other. However, IBM complies with legal requirements worldwide regarding employee and third-party involvement.

IBM is committed to acting responsibly with respect to the treatment of employees wherever we do business — either directly or in conjunction with others. IBM does not tolerate child labor or forced labor in its own operations, or in those of its suppliers or contractors.

A SAMPLING OF RECOGNITION

In 2003, IBM received the “Stevie Award” from the American Business Awards for the Best Human Resources Organization, the first time this award was granted.

IBM Colombia was recognized by the Consejo Colombiano de Seguridad from the Secretaria del Trabajo y Prevision Social (equivalent to OSHA) for achieving one of the highest Occupational Health and Safety standards in Colombia.

IBM Singapore received the H.E.A.L.T.H. Award from the Singapore government for its health/wellness programs, policies and safety aspects in the company.

IBM Australia received the National Corporation Award of Employer of the Year recognizing businesses employing people with disabilities. IBM was chosen from more than 230 nominees.

IBM in Belgium, France, Germany, Italy and the U.K. was recognized with awards for its successful prevention of psychosocial risks at work, particularly stress, by the European Agency for Safety and Health at Work.

GLOBAL WORKFORCE DIVERSITY INITIATIVES

We've come a long way over the course of the last century on the issue now called “workforce diversity.” A series of legislative measures, along with enlightened private sector leadership and populist pressure for social change, have opened doors and expanded the dialogue.

But what might have been considered enlightened or progressive as recently as 10 or 15 years ago may not be adequate today, either as business strategy or as social policy.

The reality is that workforce diversity is no longer an issue that can be categorized solely as “ethical” or “social.” The moral imperative never goes away. But now it is joined by a business imperative for enterprises whose fortunes rise or fall based on the quality of their workforce. Increasingly, companies depend on their ability to understand and reflect the range of human characteristics found in any market where they hope to do business.

So, yes, we take our commitment to a diverse and inclusive workforce seriously. And that's why, over nearly a century in business, we've built a reputation as one of the world's most progressive employers. We want it to be obvious to every public that our workforce reflects the values, cultures and differences of race, gender, culture and thought found in markets and communities the world over.

Rather than run our diversity programs from a headquarters organization or centralize them in the human resources function, we've chosen to integrate them into the fabric of our management systems and infuse them into our culture. These workforce policies cut across race, color, religion, gender, gender identity or expression, sexual orientation, national origin, disability, age, veterans' status and human differences such as culture, economic status, lifestyle and marital status.

We manage our diversity commitment—across our workforce and in our perspective on the marketplace—in three principal areas: equal opportunity, affirmative action and work/life balance programs. This management system is governed by a short set of diversity imperatives, which the general manager of each IBM country organization must accept and be held accountable for results. They are: the advancement of women; the diversity of the management team; cultural acceptance and awareness (ethnic minorities, multi-lingualism and individual differences); the integration of gay, lesbian, bisexual and transgender individuals and people with disabilities; work/life balance; and reflecting the global marketplace.

For these reasons, IBM has taken aggressive steps to mirror the demographics of the marketplace.

- Women represent 29% of IBM's global workforce, and 22% of global managers.
- Since 1995, the U.S. Asian executive population has grown 572%, the largest of any of IBM's constituency groups.
- The number of Hispanic employees in the United States has increased 121%, and the Hispanic executive population has grown 211% since 1995.
- The number of IBM gay, lesbian, bisexual and transgender employees enrolled in the company's Domestic Partner Benefits Plan is the largest in the industry.

DIVERSITY TRAINING

Though the company has made significant progress, it continues to promote programs and investments that will drive further improvements.

Diversity training is required for managers and employees, and several recruiting programs focus on hiring under-represented and minority groups.

2002 U.S. EMPLOYMENT DIVERSITY

	Men	Women	All Minorities	Black	Asian	Hispanic	Native American	Total
Officials & Managers	13,027	4,991	2,760	1,095	1,022	565	78	18,018
Professionals	41,420	20,720	15,037	4,765	7,325	2,616	331	62,140
Technicians	11,561	1,507	2,794	1,070	798	852	74	13,068
Marketing	29,077	11,620	9,573	2,975	4,952	1,457	189	40,697
Office & Clerical	1,545	5,125	2,293	1,560	208	466	59	6,670
Craft Workers	1,028	659	342	130	125	83	4	1,687
Operatives	2,053	1,372	1,057	312	496	236	13	3,425
Total	99,711	45,994	33,856	11,907	14,926	6,275	748	145,705
Total	68%	32%	23.2%	8.2%	10.2%	4.3%	0.5%	100%

Note: Table reflects all regular and complementary U.S. employees. The company's complementary workforce includes various workers hired under temporary, part-time and limited-term employment arrangements.

EXECUTIVE TASK FORCES

Eight Executive Task Forces — Asian, Black, Hispanic, Native American, Gay/Lesbian/Bisexual/Transgender, People with Disabilities, Men and Women — were established in 1995.

Each task force is chaired and staffed by executives from that particular constituency. They are charged with looking at IBM from the perspective of these special interests and making recommendations about how:

- IBM can make that group feel welcomed and valued.
- IBM can partner with that group to drive up its productivity.
- IBM can influence buying decisions of that group in the marketplace.

NETWORKS THAT CROSS BORDERS

IBM encourages the formation of internal diversity councils, and has 67 Diversity Councils and 145 Diversity Network Groups that help women and multicultural employees meet, mentor and coach; perform community outreach; implement social, cultural and education events; and develop professional skills.

AFFIRMATIVE ACTION AND EQUAL OPPORTUNITY

The IBM Global Equal Opportunity Project Office assists in assuring full compliance with both the letter and spirit of the law wherever IBM does business.

IBM has successfully responded to letters of compliance for more than 670 government audits. IBM has never failed an equal opportunity audit. When the U.S. Office of Federal Contract Compliance Programs issued its directive for Functional Affirmative Action Programs, permitting compliance by lines of business, IBM received and finalized a compliance agreement.

IBM works with regulatory, governmental and non-governmental agencies to assure full compliance with legal, moral and strategic imperatives of equal opportunity.

GLOBAL EMPLOYMENT DIVERSITY
Women in the IBM Workforce 2002

	Americas	Asia Pacific	Europe Middle East and Africa	Total Worldwide
Total Women	31.0%	23.5%	28.4%	29.0%
Women Managers	27.5%	15.1%	16.6%	22.4%

A SAMPLING OF RECOGNITION

In 2002, members of the National Society for Black Engineers voted IBM the place they would most like to work — for the 12th time in 14 years.

In 2003, IBM was one of only 21 companies to receive a perfect score on the Human Rights Campaign Corporate Equality Index, which specifically recognized progress made on behalf of the gay, lesbian, bisexual and transgender community.

In 2003, *Working Mother Magazine* recognized IBM as a top 100 employer for working mothers and among the top 10 exceptionally progressive companies. IBM has been on both lists for 18 and 16 years respectively, the only company so recognized.

In 2003, the Society of Hispanic Engineers named IBM its Company of the Year.

Since 1998, IBM has been named the top company for women executives by the National Association of Female Executives.

WE HAVE A LOT MORE TO DO

BY TED CHILDS

Vice President, Global Workforce Diversity

MY WORK REQUIRES an unyielding commitment to passion, spirit and integrity. I try to bring all three to the table, and have been fortunate to work for a company that has a heritage of obsession with those traits.

When our founder, Tom Watson, Sr., changed the name of our company to IBM in 1924, he recognized 42 employees with 25 or more years of service. That group included three women and one black man, all hired in 1899—21 years before women's suffrage, 10 years before the NAACP was founded and 36 years after the Emancipation Proclamation.

This year, we mark the 50th anniversary of IBM's first equal opportunity policy letter, authored by Mr. Watson's son, Tom Watson, Jr. When it was written in 1953, its principles were far ahead of their time, the civil rights movement and the legislation that resulted.

After he'd retired, Tom Watson told me the story behind that letter. During negotiations with the governors of two southern U.S. states regarding new IBM plants, he told them there would be no "separate but equal" racial policies at IBM. To make sure they got the point, he wrote a letter to his management team and made it public. Both governors chose investment over bad social policy.

That letter matters to me, and to hundreds of thousands of other people who never heard that story. It did more than express one man's view of the world. It described what his company stood for, his understanding of that institution's place in the world, and its responsibility to use its influence in positive and powerful ways. I don't think he'd be disappointed with the leadership of his successors on issues from marshaling business support for the original Sullivan Principles challenging workplace practices of apartheid in South Africa, to our recent filing of an amicus brief with the U.S. Supreme Court in the University of Michigan affirmative action case.

But here's what disappoints me, and what I believe must change.

We're still not entirely comfortable with all the nuances of race or gender. As a society, we just started to talk about people with disabilities in the last 20 years, and sexual orientation in the last 10. Women represent about 50 percent of the global population, but they're not half of the workforce in IBM.

Domestic partner benefits remain a legitimate issue for discussion. We provide those benefits, and we have invested more than \$200 million in dependent care programs to support women in the workplace and address the needs of working families. But we need to move on to programs that build the pipeline of gay and lesbian leaders; and expand initiatives such as the 33 camps we run in 18 nations to introduce middle school girls, ethnic minorities and children with disabilities to technical professions.

We can describe diversity as a bridge between the workplace and the marketplace, because it is. But in the end, this isn't simply about "good business." It's that, and it's about standing for principles that transcend the goal of reflecting the diversity of the marketplace.

We have a powerful legacy to uphold. And a lot more to do.



LEARNING PROGRAMS

It was once the case that competitive position was defined based on assets such as land, market presence or capital.

Those still matter. But in the information-based economy of the 21st century, the single greatest competitive differentiator — especially in terms of innovation and speed — will be the ability of any organization to *learn*.

IBM currently invests more than \$750 million annually to develop the knowledge and expertise of its workforce. Employees spend an estimated 17 million hours each year (about 55 hours per employee) in formal training—either online, through experiential learning activities or in a traditional classroom. IBM conducts half of all employee training via e-learning, realizing a cost avoidance of nearly \$750 million over the past two years.

These investments are supported by a methodology designed to move people along a development continuum, so that as demand declines for certain skills or for competencies in yesterday's technologies, applications or platforms, our investments in training prepare people with the skills they need now and in the future.

For example, right now, areas like Web services—especially WebSphere and integration services—are in high demand. So are project management, data management and networking expertise. In technical development areas like these, IBM will spend more than \$200 million to upgrade the talents of more than 100,000 employees this year and again in 2004.

Training Magazine again ranked IBM second overall in its Training Top 100 for 2003, and we received the top ranking for a technology company. IBM is the only company that has been rated in the top five in the three years the magazine has compiled the list.

NEWLY BLUE

The learning process for new employees begins with Your IBM—a learning program specifically designed for recent hires and employees who come to IBM via acquisitions. Rather than define learning as something that takes place in a classroom or at the computer, this process identifies a range of opportunities for learning and blends them with a rich mix of Web-based training, collaborative learning, online references and class time. Your IBM received a best practice citation from the American Society of Training and Development.

PROFESSIONAL DEVELOPMENT

All employees create an individual roadmap for learning and development through their Individual Development Plan. Professional development addresses the set of foundational competencies necessary for all employees, as well as the development of skills and competencies within specific career paths. IBM Global Campus, our online educational catalogue, provides more than 11,000 course options.

Focused training is provided to technical and sales professionals so their expertise remains the best in the industry. IBM also provides support for skill certification for the technical and sales workforce.

In addition to internal development opportunities, IBM leverages the best education available externally. Worldwide, there are programs available for employees interested in pursuing outside academic interests, including master's and Ph.D. degrees.

In the United States alone, nearly 6,000 employees participated in the Academic Learning Assistance Program in 2002. The program covers tuition, registration, books and software, and represented an investment of \$30 million in 2002.

MANAGEMENT DEVELOPMENT

In today's matrixed global companies, corporate strategy and direction can be set by a handful of leaders. But for those strategies to be executed with speed and precision requires leadership at all levels and at all times—as people collaborate without regard for organizational or geographic boundaries, and traditional reporting structures are supplemented by ad hoc teams of individuals who come together “virtually” to create, innovate, build and deliver client solutions.

- **Basic Blue:** provides new managers with the skills they need to create the most effective and engaging working environment for employees. Basic Blue won the Sodexo Pass Award for HR Excellence at the World HRD Congress as the most innovative HR practice in the corporate sector.
- **Role of the Manager@IBM:** mobilizes managers into global, virtual teams to identify and resolve business issues. It received an Excellence in Practice citation from the American Society of Training and Development.
- **Shades of Blue:** develops management skills and awareness in managing employees from varied backgrounds. It received Excellence in Practice Citations from ASTD in five categories: Electronic Learning Technologies, Organizational Learning, Performance Improvement, Valuing Differences and Managing Change.
- **Advisor:** a patent-pending, intelligent agent that helps managers assess gaps in their skills and training, and then presents a prescriptive, customized plan to close the gaps. Advisor won a Copper 2003 Axiem Award, which recognizes the best in all forms of electronic media.

EXECUTIVE DEVELOPMENT

Most companies have a program or process for developing leaders, and some are famous for their management training programs. However, few companies have the process of developing leaders as deeply embedded in their business operations as IBM.

In June 2002, *Chief Executive* magazine named IBM the top company for building leaders. The ranking was the first to comprehensively examine the factors that allow companies to build great leadership depth. In announcing the report's findings, Marc Effron, practice leader at Hewitt Associates, said: “Leadership development has become recognized as a critical business tool that has a direct impact on a company's bottom line and future growth. Clearly IBM is using the right tools, the right way, throughout its organization.”

Training Magazine rated IBM
**BEST IN CLASS FOR
TECHNOLOGY COMPANIES**
in 2003

One distinguishing element of IBM's executive training is the rigor applied to experiential development, based on a belief that 80 percent of leadership development happens in the context of real work.

Annually, several hundred IBM executives attend executive education programs and conferences. Designed to reflect the current business challenges faced by participants, each session provides opportunities for the participants to apply their learning directly to their business challenges.

All of IBM's executive development is designed to accelerate the growth of our highest-potential executives and “early-in-career” high-potential employees.

COMMUNICATIONS CHANNELS

Sustainable business transformation occurs only, or occurs most effectively, when it is accompanied by real cultural change in support of new modes of operation, new decision-making constructs, and new ways for work to get done.

IBM's corporate intranet has emerged as both a carrier of communications on the transformation of culture inside IBM, and one of the most tangible manifestations of a company that's faster, more fluid and collaborative. It has become the locus of work and idea movement—in addition to communications—and a tool that nearly 70 percent of our workforce deem critical to their jobs.

In addition to the company intranet, IBM maintains multiple channels and media through which management communicates with the workforce, and employees communicate with management:

“Dear IBMer”: electronic memos from the CEO on business results and topical issues that concern the company, its clients, its partners and its people.

Web and video broadcasts: by the CEO and a variety of executives to provide business updates, address questions raised by employees and other issues affecting IBM and its major business units.

Ideas: a formal program in which managers and employees suggest ways products, operations and programs can be improved. Suggestions can earn awards ranging from \$50 to \$5,000. Since 1992, when the earlier IBM Suggestion Program was modified, employees have submitted 173,000 ideas; more than \$15 million has been awarded; and more than \$731 million has been saved.

Speak Up!: a program implemented in 1962, enables employees to express concerns or ask questions beyond their immediate management chain, or report serious issues such as management misconduct or violations of the IBM Business Conduct Guidelines. Their messages are electronically submitted. At the option of the employee, they can be handled confidentially. They are reviewed by appropriate managers for a decision and the result is confidentially communicated to the employee.

Internal Appeals Process: There are two vehicles in the Internal Appeals Process:

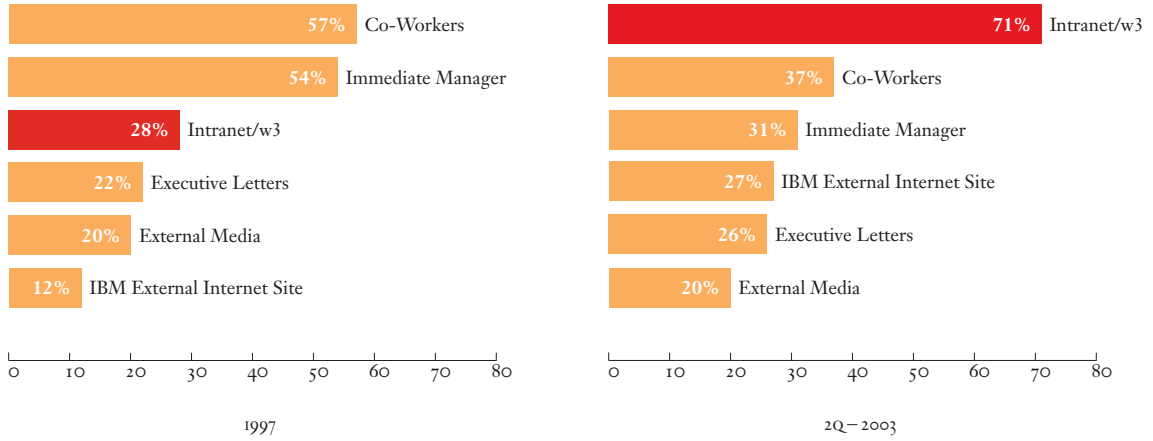
- The Open Door investigation assigns an independent, experienced manager to thoroughly investigate an employee's issue, which is then reviewed by a senior executive for approval.
- The Panel Review is a peer review in which three employees and two managers hear both the employee and the management perspective on an issue and then determine the validity of the issue and the recommended outcome.

GLOBAL PULSE SURVEY

Every eight weeks, this survey goes out to a scientific, random sample of the workforce.

The survey, which can be taken in any of 13 languages, focuses on questions that influence employee satisfaction with the company, their jobs, retention issues and client satisfaction.

CORPORATE INTRANET: FROM ONLINE MAGAZINE TO DYNAMIC WORKPLACE
IBM's intranet has become employees' most trusted source for company information—surpassing even the grapevine.



Survey results are benchmarked with other global companies to identify strengths and areas for improvement.

GLOBAL PULSE SURVEY
(percent responding favorably)

2002	IT Industry Average	IBM
Overall Job Satisfaction	66%	71%
Clarity of Direction	57%	63%
Organizational Teamwork	54%	57%

Recognition

Only half of IBM employees agree that they receive adequate special recognition for excellent work. New management training programs seek to make recognition—above and beyond the standard compensation package—an integral part of our culture.

“New Blue: Focused to Win” is a global recognition program that establishes clear, consistent criteria for awards. The program both simplifies and improves the awards process.

Workload

IBM employees consistently report that work/life balance is critical to their job satisfaction, and that workload issues are among the strongest factors that would prompt them to think about leaving the company. More than one-third of IBM employees say they spend at least 15 percent of their time on unnecessary work related to inefficient processes, inadequate technology or poor planning.

IBM is addressing these concerns by: first, reducing or removing bureaucracy and low-value activities; and second through programs that address issues of work/life balance (page 32), in combination with policies and programs that foster a work environment that gives employees more options to manage and control where, when and how they do their jobs.

More than one-third of IBM employees already work outside a traditional office. This reflects our support for the idea that employees who have more latitude over their schedules and where they work; i.e., from home or at a client location—and are equipped with the right technologies—are able to better manage their business and personal lives, and stay in closer contact with their clients.

By 1995, IBM had equipped 10,000 mobile employees, primarily in the United States. By year-end 2002, flexible work options were implemented in all 18 targeted nations. In 2003, the program was broadened globally, with more than 115,000 employees now considered “mobile” workers.

IBM offers six flexible work options ranging from compressed or part-time schedules to extended leaves. More than 1,100 managers worldwide have been trained on supporting employee use of flexible options as a way of getting work done—not simply as an employee accommodation.





THE RISE OF THE NEW WORKPLACE

BY MARIA ARBUSTO

Director, On Demand Workplace User Experience

NOT TOO LONG AGO the workplace was an office or a factory—some physical location where people could be close to the filing cabinets, the water cooler, and each other. Work happened in specific places within predetermined hours.

But in a company of 316,000 people—one-third of whom work from home or spend most of their time with clients—what is the “workplace”? And when the patterns and nature of work no longer require people to sit side by side, what happens to things like community and corporate culture?

At IBM, all of that—work, information, transactions, even the company grapevine—is migrating to the company intranet, w3.ibm.com. For many of us, w3 isn’t just a source of information on the company—it’s the place where work gets done, where ideas are born, where we meet and collaborate. It’s a tangible, accessible and highly empowering manifestation of a culture that’s premised on innovation, marketplace focus and integrity.

w3 delivers mail, instant messages, industry, company and business unit information—but it is far more than a communications channel, and it does far more than extend the definition and sense of “place” to a den, kitchen table or seat on a commuter train.

With w3, we’ve pioneered the frontiers of online collaboration—from hundreds of online forums run by communities of interest; to massive “jams”—worldwide events where thousands of us capture best practices, generate new learning and connect to colleagues from around the globe.

The material efficiencies are there to be tallied: so far the company has saved billions in expense and is still counting the mounting returns from relocating its core processes to the Web.

Harder to measure—but far more important to us—is a new mentality that’s emerging among employees as they “live” on w3—more responsive, more informed, more competitive and more collaborative. This is about a lot more than efficiency. It’s about redefining the very nature of the workplace, and of work itself.

THREE-QUARTERS OF IBM'S EXPENSE ACCOUNTS WORLDWIDE
FLOW THROUGH THE INTRANET, AND NINE OUT OF 10 U.S. EMPLOYEES
ENROLL FOR HEALTH BENEFITS VIA THE WEB