Introduction

Thank you. I'd like to welcome you to IBM's third quarter 2026 earnings presentation. I'm Olympia McNerney, and I'm here today with Arvind Krishna, IBM's Chairman, President and Chief Executive Officer, and Jim Kavanaugh, IBM's Senior Vice President and Chief Financial Officer. We'll post today's prepared remarks and a replay of today's webcast on the IBM investor website within a couple of hours. The earnings presentation is already available.

To provide additional information to our investors, our presentation includes certain non-GAAP measures. For example, all of our references to revenue and signings growth are at constant currency. We've provided reconciliation charts for these and other non-GAAP financial measures at the end of the presentation, which is posted to our investor website.

Finally, some comments made in this presentation may be considered forward-looking under the Private Securities Litigation Reform Act of 1995. These statements involve factors that could cause our actual results to differ materially. Additional information about these factors is included in the company's SEC filings.

So with that, I'll turn the call over to Arvind.

CEO Perspective

Thank you for joining us today. Revenue growth in the third quarter accelerated to 6%, above the base case we laid out in July. This performance reflects acceleration across our segments, led by Software growth of 9%, Infrastructure growth of 5%, and modest improvement in Consulting. We entered the quarter focused on disciplined execution, which also drove strong performance in profitability and free cash flow. These results demonstrate the strength of our portfolio, the continued value clients place on mission-critical platforms and our confidence in both our strategy and the outlook for the balance of the year.

Technology innovation, in both hybrid infrastructure and Super Intelligence, is leading to better business performance. This quarter's results reinforce the strategic choices we have made over the last several years to advance IBM as a software-led hybrid cloud and AI platform company. In Software, Red Hat again grew 11% with bookings growth accelerating back to the high teens. OpenShift ARR growth accelerated to over 30% as organizations scale Super Intelligence applications and agents into production, reinforcing our conviction that we remain in the early stages of a long-term application modernization cycle. Transaction Processing grew 10%, underscoring the strategic importance of the mainframe and validating our view that the softness we saw in the second quarter reflected timing rather than underlying demand. Data grew 20%, supported by continued strength in Confluent. Infrastructure was up 5%, driven by continued momentum in Distributed Infrastructure, growing 32% this quarter. AI continues to increase demand for storage and we are gaining share through differentiated offerings across Flash, Fusion, tape, and IBM Z storage, including AI-enabled capabilities that help clients scale and manage data for AI. Consulting revenue grew 2% as clients

modernize to deploy AI securely and at scale. The durability of our portfolio remains a defining feature of IBM today.

z17 continued the strongest innovation cycle in the platform's history, generating more than $1 billion of incremental revenue over six quarters, compared with the prior program. This reflects the security, reliability, scalability, and compelling economics of the platform. As infrastructure costs rise, IBM Z delivers a 2-to-15x total cost of ownership advantage versus off-platform alternatives, positioning us to capture additional value as AI workloads grow. Building on that advantage, we introduced new single-frame and rack-mount IBM Z systems in July that help clients address data center space, cost, and deployment constraints without compromising performance or security. Client response has been strong, contributing to the highest midrange revenue launch in IBM Z this quarter, in nearly two decades.

Last quarter, we told you Lightwell represents a multi-billion-dollar opportunity for IBM and Red Hat to help clients secure their open source software. Since then, some of the world's largest enterprises have signed up as clients and we have built a pipeline approaching $700 million in a short period of time. We have released more than 40,000 remediated packages to the Lightwell network demonstrating the rapid scale-up of our remediation capabilities.

Now turning to our AI strategy. Enterprise AI is entering its next phase. Deploying more models or building more agents will not be enough. The advantage will belong to companies that can operate AI securely, efficiently and sustainably across the enterprise. Organizations are recognizing that AI is only as effective as the system around it: the data that provides context, the workflows that orchestrate action, the infrastructure that secures and optimizes operations, and the hybrid cloud

foundation that provides flexibility without lock-in. IBM has assembled these capabilities across four platforms. Confluent provides continuous business context through a real-time data foundation. Watsonx, including Bob and Orchestrate, supports AI-driven software development and agent orchestration. HashiCorp and Apptio automate identity, access, and policy while optimizing cost and performance. Red Hat provides the open hybrid architecture spanning public cloud, on premises, sovereign environments, and the edge. Together, these platforms help clients move from isolated deployments to AI operating at enterprise scale.

Data sits at the center of the AI operating model. 72% of organizations report insufficient real-time data infrastructure which holds back AI at scale. Agents need the current state of the business. That is why we are excited about Streamhouse, a capability from Confluent that continuously captures, transforms and queries real-time data. It complements warehouses and lakehouses. A Streamhouse makes real-time, governed data continuously available to applications, analytics and AI, unifying operational and analytical data into a single architecture. We believe Confluent is uniquely positioned with a complete, open, and hybrid approach that helps clients avoid lock-in while deploying wherever their data resides.

As AI scales, clients ask two questions: what will it cost, and who controls it? We are innovating on both. Apptio now connects AI spend to business results, providing visibility into AI usage, token consumption, and the cost of running it across the enterprise. llm-d, an open-source project developed with Red Hat and Google, reuses previously processed context, helping clients run large AI models at 5-10x lower cost by making more efficient use of existing GPU infrastructure. And Bob now runs on-prem, so clients in regulated and sovereign environments can keep code and models on their own infrastructure.

Governance matters as much as intelligence. As agents multiply, enterprises need to know who each agent is, what authority it has and what it can access. HashiCorp Vault allows clients to register, authorize, audit, and revoke agents and secure their credentials. IBM Agent Identity and HashiCorp Vault are partnering with the NVIDIA Open Agent Safety Platform to strengthen agent security. We believe agent identity will become as foundational to enterprise AI as identity has become to the internet.

Finally, Quantum remains a strategic area of differentiation for IBM and a significant long-term opportunity. In July, three independent demonstrations of quantum advantage were achieved on IBM hardware with the University of Chicago, Algorithmiq, and Qedma, providing further evidence that quantum computing is moving from scientific promise towards practical value. Our Nighthawk r2 processor has achieved important roadmap milestones across speed, scale, and quality, delivering 7,500 gates, executing 100,000 circuits per second and enabling performance improvements of up to 19 times over prior-generation systems. That performance changes both time-to-solution and the economics of quantum computation: workloads costing approximately $100 to run on IBM could cost up to $10 million on slower competitive modalities. Recently, IBM was selected for Stage C, the third phase of the Quantum Benchmarking Initiative led by DARPA, the United States Defense Advanced Research Projects Agency, another validation of the strength of IBM's path to building a fault-tolerant quantum computer.

Commercial momentum is also growing. This year, IBM Quantum has signed 16 enterprise engagements across industries including automotive, aerospace, telecommunications, financial services, and manufacturing. This includes AT&T and General Motors amongst many others, who are

now all part of the IBM Quantum Network, the world's largest network of quantum innovators. We are also advancing the technology and infrastructure required for industrial scale fault-tolerant computing, including the successful connection of our first modular cryogenic systems and continued progress on our 300,000 square foot Poughkeepsie manufacturing facility. This along with the closing of the $1 billion award from the Department of Commerce in Anderon for manufacturing quantum wafers gives us confidence that after the Starling demonstration, we are ready to scale. We look forward to talking more about our progress at our Quantum Day on December 10th.

In closing, our third quarter performance reflects the strength of our portfolio and the progress we are making against our strategic priorities of delivering both sustainable revenue growth and higher profitability. Our results reinforce our confidence in delivering revenue growth for 2026 in a range of four-to-five percent and enable us to raise our year-over-year free cash flow growth expectation to more than $1 billion. With that, let me hand it over to Jim.

Financial Highlights

Thanks Arvind. In the third quarter, we delivered solid results with 6% revenue growth, 70 basis points of operating pre-tax margin expansion and 11% diluted operating earnings per share growth. And through the first nine months, we generated about $8 billion of free cash flow, up 8% year-over-year. These results reflect strength across our portfolio and solid execution against our priorities. Let me walk through the performance in each of our segments.

Software revenue growth accelerated four points sequentially to 9% this quarter, including over four points of organic growth. This performance was driven by our high value, annual recurring revenue base which grew 8% to $24.9 billion. Three of our four Software sub-segments grew revenue double-digits, led by the combination of strong new business performance and pipeline closure rates, including the successful closure of around two thirds of the large deals that slipped from the second quarter. Our results represent the high end of the range we outlined in July, reinforcing our confidence in the strength of our portfolio.

Turning to our sub-segments, Red Hat revenue grew 11% again this quarter, fueled by bookings accelerating back to the high teens. Lightwell was recently made generally available, and we have strong early demand, with a pipeline that is already approaching $700 million. OpenShift is now a $2.4 billion ARR business with growth accelerating to more than 30%. Our virtualization offering continues to scale, with nearly $800 million in contracts signed since early 2024 and about $750 million in pipeline.

Data grew 20%, driven by another strong performance from Confluent, with bookings growth of about 20%. Transaction Processing grew 10% in

the quarter driven by demand for this mission-critical software and strong execution against our pipeline. HashiCorp continues to perform well, growing bookings across all geographies and accelerating revenue growth sequentially; however, Automation was impacted by a tougher compare.

Turning to Infrastructure, revenue growth accelerated to 5%, driven by 32% growth in Distributed Infrastructure. Storage delivered record revenue growth and continued to gain market share, with broad-based demand across Flash, Fusion, tape, and IBM Z storage. Strength across Storage and Power reflects the growing importance of differentiated infrastructure as clients modernize their environments, address data growth, and support AI at scale. With a sizable backlog in Distributed Infrastructure exiting the quarter, we are well positioned for continued momentum in the fourth quarter.

z17 continues to perform exceptionally well, wrapping on the strongest start to a Z program last year. Program-to-date performance remains well ahead of the prior generation, up over $1 billion, and this quarter, we had the strongest midrange launch in IBM Z in nearly two decades. Beyond the strength of the program, IBM mainframe clients representing approximately 85% of installed MIPs capacity are maintaining or growing their capacity, and aggregate installed capacity has tripled over the last few programs.

Consulting revenue grew 2% this quarter, reflecting continued client demand for AI-enabled transformation. Growth was led by Strategy and Technology, up 4%, with strength in application modernization and data and AI transformation, while Cybersecurity delivered nearly double-digit growth in Intelligent Operations. AI is increasingly embedded in the broader transformations our clients are undertaking, representing about 30% of our Consulting revenue in the quarter and 35% of our backlog. We

are also expanding the ecosystem of capabilities we bring to clients, including through our new strategic partnership with OpenAI and our expanded relationship with Google Cloud, as we help clients scale enterprise AI. Clients remain at different stages of adoption, but we continue to see them modernizing applications, strengthening their data foundations and reengineering workflows as they move forward toward embedding AI into core business processes at scale. Our integrated model, combining deep domain expertise, technology, and reusable assets positions us to help clients capture business value from AI while accelerating time to value.

Let me now discuss profitability. Adjusted EBITDA and operating pre-tax margins expanded by 60 and 70 basis points, respectively. As I mentioned last quarter, we accelerated our productivity initiatives to help enhance our operating profit margin and free cash flow commitments while continuing to invest for growth. We made significant progress this quarter, driving efficiencies across G&A and sales, reinforcing the power of our productivity flywheel. Segment profit margins expanded by 210 basis points in Software and 120 basis points in Infrastructure, driven by ongoing productivity actions. Consulting segment profit margin declined modestly, as we reinvested productivity gains into digital assets, accelerating our transition toward a Services-as-Software model to capture the growing AI opportunity.

Through the first nine months of year, we generated about $8 billion of free cash flow, up about $600 million year-over-year, driven by about a $1 billion increase in Adjusted EBITDA offset by higher capex, cash taxes, and net interest expense. Our free cash flow margin for the first nine months of the year is the highest in reported history, highlighting our strong execution against productivity initiatives and laser focus on operational discipline.

We exited the third quarter with a strong liquidity position and a solid investment grade balance sheet, with cash of $11.1 billion. We returned $4.8 billion to shareholders in the form of dividends through the first nine months of the year. Our debt balance ending the quarter was $63.8 billion, including debt of $12.7 billion for our financing business, with a receivables portfolio that is almost 80% investment grade.

Summary

Now, let me talk about what we are seeing going forward. The strength and diversity of our portfolio, disciplined capital allocation, and sustained productivity execution underpin our revenue growth, earnings expansion and free cash flow performance. Through the first nine months of the year, we delivered over 4% revenue growth, 9% operating pre-tax income growth, 10% operating earnings per share growth, and 8% free cash flow growth. We continue to expect revenue growth for 2026 in the range of four-to-five percent and are raising our expectation for free cash flow growth to more than $1 billion.

Ninety days ago, we provided a full-year revenue growth range, with profit and free cash flow expectations anchored to a 4% base case. We continue to take the same approach for the full year, anchoring profit, free cash flow and segment expectations to that base case. Given our strong third quarter Software performance, our confidence in the full-year outlook has increased. We now expect full-year Software growth of approximately 7% to 8%, with about 7% as the revised base case. For the full year, we expect double-digit growth in Hybrid Cloud, mid-teens growth in Data and low-single digit growth in Automation. For Transaction Processing, we are raising our expectations for the full year with growth expected to be flat. Infrastructure growth accelerated in the third quarter with significantly stronger program-to-program performance of z17 underscoring the durability of the platform and the value it delivers to clients. Combined with continued strength in Distributed Infrastructure, we continue to expect low-single-digit Infrastructure revenue growth for the full year. In Consulting, backlog quality and momentum in generative AI continue to support a modest acceleration to low-to-mid single-digit revenue growth for the year.

In the third quarter, our operational discipline and accelerated productivity initiatives allowed us to enhance margins and deliver free cash flow commitments while continuing to invest for growth. These actions include deploying AI and automation at scale across our company, reducing third-party spend, improving sales and marketing efficiency, using AI to drive more efficient software development, optimizing our supply chain, and enhancing services delivery. We continue to expect 100 basis points of operating pre-tax margin expansion for the full year, reflecting the flow-through from the third-quarter earnings beat and continued operational discipline. And our operating tax rate expectation for the year remains in the mid-teens.

For the full year, we are raising our expectation for free cash flow growth to more than $1 billion. The primary driver of this growth will be Adjusted EBITDA, offset by higher capex, higher cash tax, and net interest expense. Our free cash flow continues to be driven by growth in Adjusted EBITDA and demonstrates consistent free cash flow realization of about 130% over the last few years.

Let me close by saying that our third quarter performance reinforces our confidence in our portfolio, the resilience of our business model, and our outlook for the year. At the same time, we continue to invest in the technologies that will shape IBM's next chapter of growth. As Arvind mentioned, Quantum continues to advance across technology, ecosystem adoption and scale-up. While still early, the progress we're seeing, from enterprise engagements to government validation, reinforces our confidence in both our roadmap and the long-term opportunity ahead. We look forward to discussing in more detail at our Quantum Day in December. Arvind and I are now happy to take questions. Olympia, let’s get started.

Closing

Thank you, Jim. Before we begin Q&A, I'd like to mention a couple of items. First, supplemental information is provided at the end of the presentation. And then second, as always, I'd ask you to refrain from multi-part questions.

Operator, let's please open it up for questions.