UBS

Letter to Shareholders Half-Year Report 1999

24 August 1999

Dear Shareholder

Two items distinguish the first half of 1999: a net profit after taxes and minority interests of CHF 3,962 million – which translates into diluted earnings per share of CHF 18.84, an increase of 14% over the previous period – and the successful integration of the information technology (IT) platforms in Switzerland. Group results were driven by good developments at Warburg Dillon Read, higher-than-expected results from Private and Corporate Clients as well as gains from various divestments in the first half. Assets under management in Private Banking also developed positively. These results are testament to UBS's ability to maintain the vast majority of its client franchise through the merger. In Switzerland, UBS completed the highly complex task of integrating 2.5 million master client accounts by June 1999, and internationally we had already finalized the merger by year-end 1998. All this was realized as planned within one year of the legal merger.

UBS chose and successfully executed a rapid integration, despite the challenge thus created for growing the normal business in the short term. By doing so, we have put ourselves in a position as quickly as possible to concentrate on further building the franchise and accelerating its growth.

While first-half 1999 total operating income increased five percent to CHF 15,240 million, total operating expenses increased only one percent to CHF 10,001 million. First-half 1999 revenues also include pre-tax gains of CHF 1,490 million associated with the sale of the 25% stake in Swiss Life/Rentenanstalt, CHF 110 million from the divestment of Julius Baer, as well as CHF 200 million from the disposal of the international operations of the Global Trade Finance business. In the corresponding period of the previous year, UBS realized a pre-tax CHF 1,058 million gain from the sale of BSI-Banca della Svizzera Italiana and Bank Adler.

Adjusted for the impact of gains on major divestments, the related operating income and expenses associated with these divestments, and the associated taxes on these items, net profit after tax increased 13%.

The one percent increase in operating expenses was driven by higher performance-related expenses due to good results in the first half of 1999. Additionally, accrual of performance-related compensation in 1998 was on a linear basis. This was due to the complexity and speed of the merger and the anticipated impact on full year results, whereas in 1999, accrual is on a non-linear basis and reflects strong year-to-date results. Excluding performance-related expenses, personnel costs decreased slightly. Perhaps the clearest indicator of the success of the merger was the decrease in general and administrative expenses of 13%, excluding the CHF 544 million provision for the US class action suit from half-year 1998 results.

Divisional results lie generally within – and to some extent clearly above – expectations. Over the past year, integration has presented a challenging environment for the Private Banking and Private and Corporate Clients divisions. However, the loss of assets under management from clients leaving UBS was significantly lower than assumed at the announcement of the merger. Furthermore, during first-half 1999, we are particularly pleased that, in the Private Banking Division, assets under management associated with new clients clearly outstripped those of clients leaving the bank. With the integration completed, the inevitable inconvenience to our clients should come to an end, and we thank them for their patience during this time.

The UBS Group that is the product of the merger is a global integrated investment services firm and the leading bank in Switzerland. Across the UBS Group, we provide a complete range of investment, financial and advisory services to individual, corporate, institutional and sovereign clients based on a highly efficient infrastructure.

We recognize trends in our industry such as globalization, consolidation and scale, the increased importance of disciplined risk management, the impact of technology on the delivery of complex and flexible solutions, and demographic shifts towards more sophisticated clientele and aging populations in industrialized countries. The UBS Group has the positioning, financial strength, unique franchise, strong earnings-generating ability and now the developing culture which enable us to benefit from these trends to an exceptional degree. This translates directly into increased shareholder value.

With the merger behind UBS, we will harness the significant resources freed up by its completion to build upon our position as a leading global financial institution.

We wish to thank our employees for their dedication and hard work in making the merger a true success and also thank our shareholders for their trust. We are confident for 1999 as a whole.

Sincerely

UBS AG

Alex Krauer
Chairman of the Board of Directors

Marcel Ospel
President and Group CEO

Review of the divisions

Private Banking posted a pre-tax profit of CHF 1,388 million. Last year's interim result of CHF 2,736 million is not directly comparable, however, because the first half of 1998 included the proceeds from the sale of BSI-Banca della Svizzera Italiana and the net operating income from this business. The comparable pre-tax profit figure would have been around CHF 1.5 billion. The slight drop in profit can be attributed to lower trading volumes in the Swiss stock market and to the negative impact of the integration process, which was expected. Now that this phase has been successfully concluded, it will be possible to channel all our energies into expanding the business further. The growth of onshore private banking operations outside Switzerland was encouraging, with new branch offices being opened in Spain, Italy, France and Germany. The units in London, New York, Singapore and Hong Kong were also strengthened. As of the end of June, Private Banking had assets under management totalling CHF 659 billion, which was 8.6% more than at the beginning of the year. UBS Investment Funds enjoy a commanding position in Europe and in Switzerland, and the assets under management in this segment amount to CHF 190 billion. This represents a 8.6% increase thus far in 1999.

Warburg Dillon Read, our investment banking division, has built on its excellent first-quarter result. At CHF 1,543 million, pre-tax profit is up 37% on last year's interim figure, which was in itself a good result. Excluding the extraordinary gain on the sale of the Global Trade Finance business, the increase comes to 19%. The equities and the fixed-income businesses performed extremely well. Advisory business recorded good results, whereas primary equity business was weaker versus last year's strong performance. Warburg Dillon Read is a leading player in e-commerce. Through focused investments in human resources and technologies, we seek to further expand our client base and exploit new business opportunities. The large number of high-profile international awards received by the division in the first half of 1999 testify to the high quality of our investment banking services.

For the *Private and Corporate Clients* Division the first six months of 1999 were dominated by the practical logistics of the merger process. Some 2.5 million master client accounts were transferred to a new, joint IT platform, and this migration placed the most strenuous demands on our staff and our technological resources. The successful completion of this extremely complex project a mere twelve months after the legal conclusion of the merger is an outstanding achievement, and one we can be proud of. Further progress has also been made in streamlining the branch network, with branch closures completed in 130 of 150 locations in Switzerland where two UBS branches were previously present.

Pre-tax profit climbed 24% to CHF 582 million, while assets under management increased by 2% to CHF 443 billion. The merger-related projects inevitably made banking relationships more difficult, and in certain instances unfortunately meant that our clients were inconvenienced. Nevertheless, the assets of new clients acquired outstripped those of clients leaving the bank. A particular focus of our

Key data

Annualized return on equity:
21.1% (17.2% in the first six months of 1998)

Cost/income ratio:
63% (67%)

Group assets under management:
CHF 1,665 billion (+5.9% compared with 31 December 1998)

Number of staff:
48,066 (48,011 at end-December 1998)

Total assets:
CHF 904,573 million
(CHF 944,116 million as of 31 December 1998)

Shareholders' equity:
CHF 32,487 million
(CHF 32,395 million as of 31 December 1998)

Treasury stock:
7,832,697 (3.6% of total shares)

efforts is on the continued expansion of alternative products, services and distribution channels. Telebanking and Internet banking are both developing at a mercurial pace. At the end of June, there were some 180,000 users, and around 2,000 more join every week. In this field, as indeed in the private and corporate clients business generally, UBS is the leading bank in Switzerland.
UBS Brinson (institutional asset management) reported a pre-tax profit of CHF 153 million, roughly a third lower than in the first six months of 1998. While investment performance within the UBS Brinson area remains generally good, US equity portfolios and certain balanced portfolios have under-performed relevant benchmarks on a short-term basis, causing some client detections in Europe. These particular short-term challenges aside, our investment philosophy has clearly demonstrated itself to be a sound one upon which to add long-term value to our clients and shareholders. The beginning of the year and now stand at CHF 563 billion.
UBS Capital, the private equity division, is currently in an expansion phase marked by an increased number of investments and fewer disposals. At CHF 56 million, pre-tax profit for the first half of 1999 was well down on the excellent CHF 276 million figure reported last year. However, lower earnings are not uncommon in such a portfolio-building phase. Investments are generally held for a few years with a view to exiting at a profit when a suitable opportunity arises. A number of different funds were set up to address the demand from clients for private equity investment vehicles. This business will be expanded further in future.

Development of individual income components

Net interest income rose 1% to CHF 3.4 billion, despite the loss of earnings from the subsidiary banks that were sold and the ongoing reduction in the international credit portfolio. The aforementioned divestments also reduced net fee and commission income, which fell 6% overall to CHF 6.2 billion. This drop was primarily due to weaker trading volumes in a number of stock markets and lower income from new issues, 1998 having been a bumper year in this regard. Net trading income recorded a 26% rise to CHF 4 billion. While the equities, fixed-income and precious metals business areas all posted encouraging growth rates, income from foreign currency and banknote trading was down.
The sharp rise in "Other income" is primarily due to the sale of investments in associates (Swiss Life/Rentenanstalt, Julius Baer, Global Trade Finance business), which resulted in an aggregate pre-tax profit of CHF 1.8 billion.

Credit costs in line with expectations

Credit risk expense totalling CHF 635 million was charged to income in the first half-year, marking a sharp increase over the CHF 310 million in credit costs for the same period last year. This rise is not attributable to any deterioration in the risk situation, however, which has in fact eased somewhat, especially in Switzerland. The very low level recorded last year is due to the fact that a significant portion of the risk costs were charged against the allowances created for this purpose, and as such were not reflected in the income statement.
The allowances for credit risks represent a coverage ratio of 103.5% of non-performing loans, which now account for 4.4% of the overall credit portfolio, compared with 4.7% last year.

A detailed report on the first half-year is available in English on the Internet (www.ubs.com). It can also be obtained in printed form from: UBS AG, RM0W-ISU, P.O. Box, CH-8098 Zurich.

UBS Group Income Statement

CHF million For the 6-month period ended	**30.6.1999**	30.6.1998	Change	%
Operating income				
Interest income	**8,149**	11,492	(3,343)	(29)
Less: Interest expense	**4,784**	8,156	(3,372)	(41)
Net interest income	**3,365**	3,336	29	1
Less: Credit loss expense	**635**	310	325	105
Total	**2,730**	3,026	(296)	(10)
Net fee and commission income	**6,184**	6,597	(413)	(6)
Net trading income	**3,986**	3,176	810	26
Other income, including income from associates	**2,340**	1,707	633	37
Total	**15,240**	14,506	734	5
Operating expenses				
Personnel	**6,819**	5,780	1,039	18
General and administrative	**2,318**	3,211	(893)	(28)
Depreciation and amortization	**864**	910	(46)	(5)
Total	**10,001**	9,901	100	1
Operating profit before tax	**5,239**	4,605	634	14
Tax expense	**1,256**	1,094	162	15
Group profit	**3,983**	3,511	472	13
Less: Minority interests	**21**	0	21	–
Net profit	**3,962**	3,511	451	13
Basic earnings per share (CHF)	**18.95**	16.55	2.40	14
Diluted earnings per share (CHF)	**18.84**	16.48	2.36	14

Segment Reporting by Business Division

For the 6-month period ended 30 June 1999

CHF million	Private Banking	Warburg Dillon Read [2]	Private & Corp. Clients	UBS Brinson	UBS Capital	Corporate Center [2]	Group total
Operating income	2,910	7,100	3,600	541	119	1,605	15,875
Less: Credit loss expenses [1]	6	171	554	0	0	(96)	635
Total	2,904	6,929	3,046	541	119	1,701	15,240
Personnel, general and administrative expenses	1,442	4,983	2,174	324	60	154	9,137
Depreciation and amortization	74	403	290	64	3	30	864
Total	1,516	5,386	2,464	388	63	184	10,001
Segment performance before tax	**1,388**	**1,543**	**582**	**153**	**56**	**1,517**	**5,239**
Tax expense							1,256
Group profit							**3,983**
Less: Minority interests							21
Net profit							**3,962**

[1] In order to show the relevant divisional performance over time, adjusted expected loss figures rather than the net credit loss expense are reported for all business divisions. The statistically derived adjusted expected losses reflect the inherent counterparty and country risks in the respective portfolios. The difference between the statistically derived adjusted expected loss figures to the financially booked net credit loss expenses at Group level is reported in the Corporate Center. The divisional breakdown of the net credit loss expense of CHF 635 million as of 30 June 1999 is as follows: Private Banking CHF 14 million, Warburg Dillon Read CHF 14 million, Private and Corporate Clients CHF 603 million, Corporate Center CHF 4 million. [2] Warburg Dillon Read: the first half of 1999 includes pre-tax CHF 200 million gain from divestment of the Global Trade Finance business. Corporate Center: the first half of 1999 includes pre-tax CHF 1,600 million gain from divestments of investments in Julius Baer and Swiss Life/Rentenanstalt.