

First quarter 2018 results

23 April 2018

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Check against delivery.

Numbers for slides refer to the first quarter 2018 results presentation.

Sergio P. Ermotti

Slide 1 – Cautionary statement

Thank you, Caroline. Good morning everyone.

Slide 2 – Net profit +19% YoY to 1.5bn

We started 2018 on a positive note with strong net profit growth, higher returns, and a strong capital position. The quarter turned out to be a tale of two halves, with an exuberant start in January that went well beyond typical seasonality, followed by a more muted finish.

Once again, our results showed the power of our diversified business, with strong divisional results in the Investment Bank and Global Wealth Management, and strong regional performances in the Americas and Asia Pacific. Net profit increased by 19% to over 1.5 billion francs and we reported nearly 2 billion francs in pre-tax profit. Our adjusted return on tangible equity ex-DTAs reached a three-year high of almost 18%.

The CET1 leverage ratio, which we currently view as our binding constraint, increased to 3.76%. As anticipated, our CET1 capital ratio is strong at 13.1% and our loss absorbing capacity remained around 80 billion francs.

Slide 3 – Very strong underlying operating performance

Our excellent headline earnings went hand in hand with very strong underlying operating performance, which improved by 20%, or 27% in US dollars – all while continuing to invest for growth and efficiency. Bear in mind that all of our businesses are affected by continued headwinds from higher funding and Swiss franc and euro interest rates.

Slide 4 – 1Q18 highlights and strategic priorities

There are a few highlights of our first quarter performance I'd like to draw out. Global Wealth Management delivered growth across all revenue lines and in all regions. Adjusted pre-tax profit increased 14% in dollars, which I will come back to shortly.

Our Swiss Personal & Corporate business delivered strong underlying results increasing transaction-based and recurring fee income, amid persistent headwinds from low interest rates. I'm also pleased about the continued good net new business volume growth.

With over 30 billion in inflows, Asset Management had another very strong net new money quarter and its invested assets reached a decade-high.

The IB delivered a strong 25% return on attributable equity. The result demonstrates that we are very competitive in all market conditions. The best performances came from our traditional areas of strength: Equities and Corporate Client Solutions, while FRC recovered from last year's challenging second half.

Our businesses' strong performance was partially offset by Group Asset and Liability Management results, which were affected by the widening of US Treasury–OIS spreads on our HQLA, which we report through the P&L rather than OCI, like many of our peers. These market factors are most likely temporary, but we also saw the higher funding costs we have highlighted in the past, and these are likely to remain elevated. Kirt will explain the details later.

Throughout the quarter we continued to invest in technology. In line with our earlier announcement, our spend increased by over 100 million francs year on year.

We also completed the processes necessary to launch our 3 year buyback program, so we will start buying this quarter, with a target of 550 million for the year.

Slide 5 – Global WM – Unique strategic growth drivers

As I mentioned earlier, Global Wealth Management had an excellent first quarter. The results were driven by particularly strong performances in our areas of strategic focus. The Americas and APAC saw double-digit growth to record levels, underlining our unique positioning in these large and fast growing markets. In addition, profit from our unrivaled global Ultra High Net Worth business grew by a third.

Slide 6 – Global WM – driving profitable growth

As well as our strong pre-tax growth, we also saw good momentum in net new money and our cost/income ratio improved. In addition we delivered a further increase in mandate penetration and growth in loans. So overall, we're in a great position to sustain high quality, long-term growth.

We are also pleased with the progress we are making in creating a new organization. In the first 80 days, our focus was on aligning support and control functions, establishing a more global Ultra High Net Worth organization, redesigning our operations in Latin America and streamlining marketing to further increase client acquisition and retention, just to name a few examples. We are also combining technology roadmaps to deliver the best global solutions for our clients, where possible and economically sensible.

There are a number of other areas that we're looking at to support our priorities over the next few years. In a nutshell, with more [efficient] resource usage and by globalizing best in class processes, products and services, we will support the strong growth expectations we have for the business.

So to conclude, I'm very pleased with the first quarter. The business is in good shape. Looking ahead, our momentum is positive. We expect the strengths of our balanced business model to remain evident in the second quarter's performance.

So with this, I'd like to hand over to Kirt.

Kirt Gardner

Thank you, Sergio. Good morning everyone.

Slide 7 – UBS Group AG results (consolidated)

As usual, my comments will compare year-on-year quarters and reference adjusted results unless otherwise stated.

We have adjusted for restructuring expenses of 128 million that relate to our legacy cost reduction programs. In principle, we are not expecting to make adjustments for restructuring expenses related to new cost initiatives. And as you know, we expect our reported and adjusted results to gradually converge, with restructuring cost adjustments declining to about half a billion this year and under 200 million next year.

As of Jan 1st, we adopted IFRS 9, which substantially changes how we calculate credit losses, and classify and measure financial assets. This has resulted in a reduction in our IFRS equity of about 600 million and 300 million in our CET1 capital.

Our taxes this quarter include a 13 million provision for BEAT effects, in line with the 60 million potential impact for 2018 that I referenced last quarter. We are working to mitigate these effects.

Slide 8 – Global Wealth Management

This is the first quarter we've reported results for our combined Global Wealth Management division. I will refer to US dollars, given how significant the foreign currency translation movement was for the business, with roughly 70% of invested assets and revenues based in dollars, as you clearly see on slide 21.

PBT was up a very strong 14%. Our performance was high quality and broad-based, as we saw growth in all regions and all revenue lines, another quarter of loan growth, record mandate penetration, and positive net new money in all regions.

Operating income rose 12%. Recurring net fee income was up 14%, benefiting from higher invested assets and record mandate penetration, which stands at one-third of our invested assets. It is the first time in two years that we've seen growth in recurring fee income outstrip invested assets, as we have put the cross-border effects substantially behind us.

Net interest income improved 11%, on net interest margin and 16% higher loan balances, partly offset by lower net interest from Group ALM, which I'll come to later.

Transaction-based income was 7% higher. We saw increases in all regions outside of the Americas, which had a strong first quarter last year.

Costs increased by 11%, partly on better revenues, but also on higher IT investments, mostly related to migrating our international businesses onto one platform and launching a new digital offering in the Americas, as well as higher regulatory costs.

Despite this, the cost/income ratio improved, in part as we are benefiting from the changes we have made in our Americas' operating model in 2016, and we're confident that we'll see continued efficiency improvements.

Slide 9 – Global Wealth Management – regional performance

The regional split on this slide reflects how Global Wealth Management is managed. I just want to pick out a few highlights here.

We've had record profits in the Americas with a 19% increase. Reducing our reliance on recruiting, while focusing on retention and productivity, is clearly paying off. We saw a 150 million annualized reduction in costs related to recruitment loans versus a year ago. And FA compensation was up in line with revenues, and as we have fully absorbed the increase in pay grids related to our new operating model.

We are also seeing results in our net new money, where same store advisors delivered a record 11 billion. In the second quarter, we're anticipating the typical seasonal outflows for tax payments in the US, which were in the 3 to 4 billion range in previous second quarters.

Our investment in the munis space is showing promising results, as year-to-date sales increased five-fold, along with a significant improvement in our league table position.

APAC profits also reached a new high, up 14%, with record transaction revenues, continued strong mandate sales, and lending growth. We further strengthened our #1 leadership position in Asia as measured by invested assets, where we are 50% larger than the #2 player. Not only that, we delivered higher 1-year and 5-year growth in invested assets than the next 3 competitors.

With cross-border effects largely behind us, we see strong momentum in EMEA that should drive QoQ growth going forward. Loans are up 16% year-on-year, net new money was nearly 5 billion, a 4% annualized growth rate, and we had double-digit transaction-based income growth.

We are also pleased with our consistent performance in Switzerland, where net new money growth was 3% on an annualized basis, and PBT was up a very strong 8% in francs.

In short, a very strong, well-balanced performance for our Global Wealth Management, with positive momentum.

Slide 10 – Personal & Corporate Banking

Personal and Corporate PBT was 393 million Swiss francs, a very solid result, including a number of one-off effects.

We continued to see very strong growth in recurring net fees and transaction-based income on higher referral, FX, custody and mandate fees. Net interest income decreased only slightly, as increased deposit revenues were more than offset by lower GALM allocations, which again, I'll come back to later.

Other income was about 20 million lower, as we booked a one-time gain of 20 million related to the sale of a mortgage portfolio in first quarter '17. Credit loss expense increased by 20 million year over year, as we had a net recovery of 7 million last year versus a build of 13 million in 1Q18. The implementation of IFRS 9 had a minimal impact on provisions for the quarter.

As mentioned last year, we initiated a multi-year program to digitize our Swiss universal bank and expect to see elevated technology investments as a result, with both revenue and cost benefits beginning to accrue in 2019.

Net new business volume growth was very strong at 6.3%, the second best quarter since 2007.

Slide 11 – Asset Management

PBT for Asset Management was 108 million, with the decrease from last year primarily reflecting the sale of our fund administration business in Q4, which contributed around 10 million of profits per quarter. Operating income reflects higher management fees on higher average invested assets, offset by lower performance fees.

Expenses increased on higher personnel costs related to variable compensation accounting.

Once again, Asset Management recorded excellent net new money of 27 billion excluding money markets. At 792 billion, invested assets were at the highest level we've seen for a decade.

Absent any one-time items, we expect PBT to trend around current levels for the next few quarters.

Slide 12 – Investment Bank

Our Investment Bank delivered an excellent quarter, with 20% PBT growth in dollars, a cost/income of 72%, and return on attributed equity of 25%. As with GWM, I'll refer to dollar growth rates.

On a regional basis, we had particularly strong performance in Asia Pacific, where profits more than doubled.

Corporate Client Solutions was up 22%, with strong performance across ECM, DCM, and Advisory, where the global M&A fee pool was down.

Within ICS, Equities increased 25%, with higher revenues across all regions and products, but mostly in Derivatives. This doesn't include corporate derivatives, which we report in CCS. If we were to report them in Equities, like many of our peers do, growth would have been an even stronger 32%. FRC, at 400 million francs, was down from a strong first quarter last year, but recovered from the latter half of 2017.

Costs were up 15%, mostly on higher variable comp, as well as IT investments and regulatory expenses.

Risk-weighted assets increased from the prior quarter, mainly as the spikes in volatility in February led to increased market risk RWA, although from historically low levels. Without any major volatility spikes, we expect market risk RWA to come down.

We keep investing for growth, while managing costs and resources prudently. To name a few examples, we have created scope to grow our M&A business, particularly in the US. In FX, investments into our e-trading platform last year have benefited our clients and we have captured increased volumes. In Equities, we continue to invest in electronic execution. Our goal remains to be the best Investment Bank, not the biggest, by focusing on these areas where we choose to compete, and by delivering sustainable performance over the cycle.

Slide 13 – Corporate Center

The Corporate Center loss before tax was 380 million. Services' PBT improved by 60 million and Group ALM posted a 222 million loss.

Non-core and Legacy Portfolio posted a small loss of 11 million, helped by small one-off items, and its LRD is now down to just 13 billion.

Slide 14 – Workforce management

In the past six months, we have insourced around two thousand jobs, mostly contractors in technology, with the primary objective of improving effectiveness and efficiency. Overall, we've reduced our total workforce by nearly 600.

Looking at costs more generally, we have commenced a number of programs to support improved operating leverage. Aside from general hygiene around headcount, consulting, recruitment and contractor spend, we are more closely aligning Corporate Center with the business divisions they support, and I've created a new team to drive ongoing Group cost management and efficiency. All of this gives us confidence we can take our Group cost/income ratio below 75%.

Slide 15 – Corporate Center – Group ALM

Group Asset and Liability Management results are under pressure from a combination of market and previously highlighted regulatory factors, including the build-out of our legal entity structure.

Revenue lines that are fully allocated to the businesses declined 113 million year-on-year, impacting their net interest income. This was driven by factors we've previously highlighted, such as persistently low or negative interest rates and higher volumes of AT1 and TLAC. In addition, a portfolio of interest rate hedges that expired in 4Q17, contributed to lower banking book income.

We saw a 120 million year-on-year negative variance due to Treasury / OIS basis movements, as you can see on slide 22 in the appendix. During the quarter, the widening of this basis resulted in a roughly 40 million loss reflected in our P&L on our portfolio of US Treasuries that are hedged by OIS instruments. During the first quarter '17, we saw the opposite effect, leading to an 80 million gain. Banks that account for any mark-to-market gains or losses on HQLA through OCI see a direct impact on shareholders' equity, bypassing the P&L, especially to the extent that their HQLA portfolios are unhedged in whole or in part.

Apart from this effect, we also saw an incremental 85 million of losses retained in GALM. Firstly, interest rate expense of 37 million related to FX hedging was reclassified from accounting asymmetries to risk management net income. Secondly, the remainder is driven by increased levels of long-term funding and HQLA held by GALM in response to the build-out of our legal entity structure to meet regulatory requirements, while the business divisions are consuming less.

Given current market conditions and financial resource consumption, we expect that our retained Group ALM negative income will be around 100 million per quarter for the remainder of the year. We are planning and executing a number of optimization actions with the aim of bringing us back towards the negative 50 million a quarter.

Slide 16 – RWA 1Q18

Our risk-weighted assets grew by 16 billion in the quarter to 254 billion.

We had flagged increases in credit and market risk RWA related to the regulatory and methodology changes we expected for the quarter.

As I previously mentioned, the largest increase came from IB Equities market risk.

Of the roughly 11 billion RWA increase we expect from regulatory changes over the next 3 quarters, about 4 billion will come in the second quarter.

Slide 17 – Capital and leverage ratios (fully applied)

Our capital position remains very strong, with TLAC above 79 billion, and our CET1 ratios are comfortably above the 2020 requirements.

Year-over-year, we kept our LRD flat, while increasing CET1 capital by 1.8 billion, which drove the improvement to a 3.76% CET1 leverage ratio.

To wrap up, 2018 started well, the business has good momentum and we are in good shape to deliver on our financial targets.

With that, Sergio and I will open up for questions.

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(xi) the effects on UBS’s cross-border banking business of tax or regulatory developments and of possible changes in UBS’s policies and practices relating to this business; (xii) UBS’s ability to retain and attract the employees necessary to generate revenues and to manage, support and control its businesses, which may be affected by competitive factors including differences in compensation practices; (xiii) changes in accounting or tax standards or policies, and determinations or interpretations affecting the recognition of gain or loss, the valuation of goodwill, the recognition of deferred tax assets and other matters, including from changes to US taxation under the Tax Cuts and Jobs Act; (xiv) UBS’s ability to implement new technologies and business methods, including digital services and technologies and ability to successfully compete with both existing and new financial service providers, some of which may not be regulated to the same extent; (xv) limitations on the effectiveness of UBS’s internal processes for risk management, risk control, measurement and modeling, and of financial models generally; 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Use of adjusted numbers

Unless otherwise indicated, "adjusted" figures exclude the adjustment items listed on the previous slide, to the extent applicable, on a Group and business division level. Adjusted results are a non-GAAP financial measure as defined by SEC regulations. Refer to pages 7-8 of the 1Q18 report which is available in the section "Quarterly reporting" at www.ubs.com/investors for an overview of adjusted numbers.

If applicable for a given adjusted KPI (i.e., adjusted return on tangible equity), adjustment items are calculated on an after-tax basis by applying an indicative tax rate.

Refer to page 14 of the 1Q18 report for more information.

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