Translation of the German audit opinion concerning the audit of the financial statements and management report prepared in German

Audit opinion

We have audited the annual financial statements, comprising the balance sheet, the income statement and the notes to the financial statements, together with the bookkeeping system, and the management report of UBS Europe SE, Frankfurt am Main, for the fiscal year from 1 January 2016 to 31 December 2016. The maintenance of the books and records and the preparation of the annual financial statements and management report in accordance with German commercial law are the responsibility of the Institution's management. Our responsibility is to express an opinion on the annual financial statements, together with the bookkeeping system, and the management report based on our audit.

We conducted our audit of the annual financial statements in accordance with Sec. 317 HGB ["Handelsgesetzbuch": German Commercial Code] and German generally accepted standards for the audit of financial statements promulgated by the Institut der Wirtschaftsprüfer [Institute of Public Auditors in Germany] (IDW). Those standards require that we plan and perform the audit such that misstatements materially affecting the presentation of the net assets, financial position and results of operations in the annual financial statements in accordance with [German] principles of proper accounting and in the management report are detected with reasonable assurance. Knowledge of the business activities and the economic and legal environment of the Institution and expectations as to possible misstatements are taken into account in the determination of audit procedures. The effectiveness of the accountting-related internal control system and the evidence supporting the disclosures in the books and records, the annual financial statements and the management report are examined primarily on a test basis within the framework of the audit. The audit includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the annual financial statements and management report. We believe that our audit provides a reasonable basis for our opinion.

Translation of the German audit opinion concerning the audit of the financial statements and management report prepared in German

Our audit has not led to any reservations.

In our opinion, based on the findings of our audit, the annual financial statements comply with the legal requirements and give a true and fair view of the net assets, financial position and results of operations of the Institution in accordance with [German] principles of proper accounting. The management report is consistent with the annual financial statements, complies with the legal requirements and as a whole provides a suitable view of the Institution's position and suitably presents the opportunities and risks of future development.

Eschborn/Frankfurt am Main, 18 May 2017

Ernst & Young GmbH
Wirtschaftsprüfungsgesellschaft

signed	signed
Müller-Tronnier	Kuhlmann
Wirtschaftsprüfer	Wirtschaftsprüferin
[German Public Auditor]	[German Public Auditor]

UBS

Balance Sheet as of 31 December 2016
UBS Europe SE
Bockenheimer Landstraße 2-4
60306 Frankfurt am Main

Assets

			31. December 2016	31. December 2015
	EUR	EUR	EUR	EUR k
1. Cash reserve				
a) Cash on hand		**1.731.357,40**		626
b) Balances at central banks		**4.056.216.579,48**		908.060
thereof: at Deutsche Bundesbank Euro 3.913.227.062,86 (prior year: EUR k 908.060)			**4.057.947.936,88**	**908.686**
3. Due from banks				
a) Payable on demand		**11.459.859.169,63**		1.329.568
b) Other amounts due		**5.134.769.357,97**		1.899.709
			16.594.628.527,60	**3.229.277**
4. Due from customers			**5.207.362.588,44**	**1.196.225**
thereof: secured by real estate property liens Euro 208.696.301,97 (prior year: EUR k 201.913)				
5. Debt securities and other fixed-income securities				
a) Money market securities				
aa) Issued by the public sector	175.035.101,28			0
thereof: eligible as collateral with Deutsche Bundesbank Euro 0,00 (prior year: EUR k 0)				
ab) Issued by other borrowers	542.434.428,39	**717.469.529,67**		0
thereof: eligible as collateral with Deutsche Bundesbank Euro 47.167.510,85 (prior year: EUR k 0)				
b) Bonds and debt securities				
ba) Issued by the public sector	1.074.628.968,75			204.889
thereof: eligible as collateral with Deutsche Bundesbank Euro 0,00 (prior year: EUR k 204.889)				
bb) Issued by other borrowers	572.960.085,84	**1.647.589.054,59**		0
thereof: eligible as collateral with Deutsche Bundesbank Euro 58.673.209,75 (prior year: EUR k 0)			**2.365.058.584,26**	**204.889**
6. Shares and other variable-yield securities			**5.124.611,80**	**359.410**
7. Equity investments			**11.155,00**	**163**
thereof: in banks Euro 0,00 (prior year: EUR k 0)				
thereof: in financial services institutions Euro 0,00 (prior year: EUR k 0)				
8. Shares in affiliates			**11.477.917,74**	**69**
thereof: in banks Euro 0,00 (prior year: EUR k 0)				
thereof: in financial services institutions Euro 0,00 (prior year: EUR k 0)				
9. Trust assets			**71.821.821,00**	**93.425**
thereof: trust loans Euro 0,00 (prior year: EUR k 0)				
11. Intangible assets			**0,00**	**0**
b) Purchased franchises, industrial and similar rights and assets and licenses in such rights and assets		**2.156.255,07**		85
c) Goodwill		**26.314.319,46**		0
			28.470.574,53	**85**
12. Property and equipment			**21.828.395,79**	**4.886**
14. Other assets			**670.278.950,62**	**52.753**
15. Prepaid expenses			**5.325.868,65**	**3.234**
16. Deferred tax assets			**0,00**	**0**
		Total assets	**29.039.336.932,31**	**6.053.102**

UBS

Balance Sheet as of 31 December 2016
UBS Europe SE
Bockenheimer Landstraße 2-4
60306 Frankfurt am Main

Liabilities and equity

			31. December 2016	31. December 2015
	EUR	EUR	EUR	EUR k
1. Liabilities to banks				
a) Payable on demand		**6.583.217.264,71**		613.309
b) With an agreed term of period of notice		**4.333.197.108,29**		1.136.940
			10.916.414.373,00	**1.750.249**
2. Liabilities to customers				
b) Other liabilities				
ba) Payable on demand		**14.864.790.504,72**		2.188.235
bb) with an agreed term of period of notice		**862.687.858,36**		508.053
			15.727.478.363,08	**2.696.288**
3. Securitized liabilities				
a) Debt securities issued		**5.093.841,93**		676.988
b) Other securitized liabilities		**0,00**		0
thereof: own acceptances and promissory notes outstanding Euro 0,00 (prior year: EUR k 0)			**5.093.841,93**	**676.988**
4. Trust liabilities			**71.821.821,00**	**93.425**
thereof: trust loans Euro 0,00 (prior year: EUR k 0)				
5. Other liabilities			**530.118.777,26**	**93.982**
6. Deferred income			**3.449.396,06**	**2.955**
6a. Deferrred tax liabilities			**0,00**	**0**
7. Provisions				
a) Provisions for pensions and similar obligations		**218.974.069,74**		215.290
b) Tax provisions		**23.409.221,03**		0
c) Other provisions		**164.717.711,36**		80.085
			407.101.002,13	**295.375**
9. Subordinated liabilities			**0,00**	**0**
10. Participation certificate capital			**0,00**	**0**
thereof: due within two years Euro 0,00 (prior year: EUR k 0)				
11. Fund for general banking risks			**24.900,00**	**25**
thereof: special reserve pursuant to Sec. 340e (4) HGB Euro 24.900,00 (prior year: EUR k 25)				
12. Equity				
a) Subscribed capital		**176.001.000,00**		176.001
b) Capital reserves		**986.404.601,10**		221.386
c) Revenue reserves				
cd) Other revenue reserves	46.428.856,75	**46.428.856,75**		46.428
d) Net retained profit/accumulated loss		**169.000.000,00**		0
			1.377.834.457,85	**443.815**
		Total liabilities and equity	**29.039.336.932,31**	**6.053.102**
1. Contingent liabilities				
b) Guarantees		**146.918.668,49**		**57.312**
			146.918.668,49	**57.312**
2. Other obligations				
c) Irrevocable loan commitments		**184.388.136,08**		**13.814**
			184.388.136,08	**13.814**

UBS

Income statement

UBS Europe SE
Bockenheimer Landstraße 2-4
60306 Frankfurt am Main

for the period from 1 January 2016 to 31 December 2016

			31. December 2016	31. December 2015
	EUR	EUR	EUR	EUR k
1. Interest income from				
a) Lending and money market transactions	54.012.035,53			54.496
b) Fixed-Income securities and government-inscribed debt	4.310.892,13	58.322.927,66		0
2. Interest expenses		20.350.641,99		38.023
			37.972.285,67	16.473
3. Current income from				
a) Shares and other variable-yield securities		0,00		0
b) Equity investments		169.647,59		544
			169.647,59	544
5. Commission income		408.773.511,24		241.849
6. Commission expense		49.123.816,34		40.766
			359.649.694,90	201.083
7. Net income or net expense from trading book positions			0,00	51
thereof: Allocation to the special item/income from the reversal of the special item "Fund for general banking risks" Euro 0,00 (prior year: EUR k 51)				
8. Other operating income			62.187.910,09	58.079
10. General administrative expenses				
a) Personnel expenses				
aa) wages and salaries	232.741.580,00			118.649
ab) Social security, pension and other benefit costs	35.345.773,21	268.087.353,21		27.894
thereof: for pensions Euro 7.759.784,13 (prior year: EUR k 17.775)				
b) Other administrative expenses		179.837.252,02		116.380
			447.924.605,23	262.923
11. Amortization, depreciation and write-downs of intangible assets and property and equipment			8.239.240,66	2.432
12. Other operating expenses			33.372.466,13	16.731
13. Write-downs of and allowances on amounts due and certain securities as well as allocations to provisions for possible loan losses			981.034,34	68
14. Income from the write-up of amounts due and certain securities as well as from the reversal of provisions for possible loan losses			84.158,94	468
15. Write-downs of and allowances on equity investments, shares in affiliates and securities classified as fixed assets			1.552.960,07	481
16. Income from write-ups on equity investments, shares in affiliates and securities classified as fixed assets			18.689,82	293
19. Results from ordinary activities			-31.987.919,42	-5.644
20. Extraordinary income			0,00	0
21. Extraordinary expenses			0,00	0
22. Extraordinary result			0,00	0
23. Income taxes			16.147.116,04	0
thereof: Deferred taxes Euro 0,00 (2015: Euro '000 0)				
24. Other taxes not disclosed under item 12			0,00	0
25. Income from loss absorption			0,00	5.644
26. Profits transferred under profit pooling, profit transfer or partial profit transfer agreements			0,00	0
27. Net income/net loss for the year			-48.135.035,46	0
28. Profit/loss carryforward from the prior year			0,00	0
29. Withdrawals from the capital reserve			217.135.035,46	0
34. Net retained profit/accumulated loss			169.000.000,00	0

General information

UBS Europe SE emerged from a cross-border combination involving the merger of UBS Italia S.P.A., Milan/Italy, UBS Bank S.A., Madrid/Spain, UBS (Luxembourg) S.A., Luxembourg and its branches in Austria, Denmark and Sweden, and UBS Bank (Netherlands) B.V., Amsterdam (transferring entities) into UBS Deutschland AG, Frankfurt/Main (absorbing entity) accompanied by the adoption of the legal form of a European stock corporation (SE) within the meaning of Regulation (EU) No. 2157/2001. The company was entered in the commercial register of Frankfurt/Main Local Court under HRB 107046 on 1 December 2016.

This means that UBS Europe SE is the legal successor of UBS Deutschland AG. The absorption of the assets and liabilities of the transferring entities took the form of the book value method. Under this method, all the assets and liabilities from the closing balance sheet of the transferring entities are assumed at their carrying amount under local accounting regulations. The measurement of provisions for pensions and similar obligations and general loan loss allowances on loans and advances were adjusted to reflect German accounting law. Deferred taxes were also remeasured under German accounting law, whereby deferred taxes are not recognized by the bank. The assets and liabilities were transferred for accounting purposes for UBS Italia S.P.A., UBS Bank S.A. and UBS Bank (Netherlands) B.V. with effect from 1 January 2016 and for UBS (Luxembourg) S.A. and its branches in Austria, Denmark and Sweden with effect from 1 December 2016.

Accounting principles

The annual financial statements for the 2016 financial year were prepared in line with the provisions of the German Commercial Code (HGB), the German Stock Corporation Act (AktG) and the supplementary provisions for banks set out in the German Bank Accounting Directive (RechKredV). Accounting is based on the principles of the former UBS Deutschland AG, which remained unchanged as against the previous year with the exception of the necessary amendments due to the German Accounting Directive Implementation Act (BilRUG).

UBS Europe SE is not capital market-oriented in accordance with section 264d HGB and therefore refrains from preparing a cash flow statement and a statement of changes in equity.

The corresponding prior-year values of UBS Deutschland AG are used for comparison purposes. As the income statement of UBS Europe SE includes all the branches, there is no direct comparability with the prior-year amounts. The merger of UBS Luxemburg SA with effect from 1 December 2016 means that the income statement of UBS Europe SE contains only the earnings contribution for December 2016.

The items in the **cash reserve** are reported at their notional amount.

Loans and advances to banks and customers are reported at their nominal amount, with differences between the issuing amount and the nominal amount deferred over the respective term.
Sufficient provisions were recognised for identifiable and general banking risks. General banking risks were recognised adequately in the form of a general loan loss allowance calculated in accordance with the letter from the Federal Ministry of Finance dated 10 January 1994.

Securities held in the liquidity reserve were measured on the basis of the lower of cost or market value, while other securities were measured on the basis of the moderated principle of the lower of cost or market.

Securities lending transactions do not involve the derecognition of securities loaned or the recognition of securities borrowed, as the risk arising from the security and the corresponding economic ownership remains with the lender.

Equity interests and **shares in affiliated companies** are recognised at the lower of cost or fair value.

Trust assets and liabilities result from interests in private equity funds held in trust. They are recognised at the lower of cost or market.

Intangible assets, goodwill and property, plant and equipment are recognised at cost and depreciated or amortised on a straight-line basis over their expected useful life.
Low-value assets are written off in the year of acquisition if their net cost is less than or equal to EUR 150 or are written down on a straight-line basis of 20% per year if their net cost is between EUR 150 and EUR 1,000.

Deferred income and prepaid expenses contain payments relating to future financial years. This primarily relates to premiums paid and received and advance payments of non-labour operating costs.

Liabilities are carried at their settlement amount as a matter of principle.

In the financial years prior to 2016, the Bank did not calculate any **deferred taxes** as it was a member of an income tax entity with UBS Beteiligungs-GmbH & Co. KG. The income tax entity was dissolved with effect from 31 December 2015.
The option provided by section 274 (1) sentence 2 HGB is applied, meaning that no deferred tax assets are recognised.
The excess of deferred tax assets primarily results from tax loss carryforwards in various tax jurisdictions and deductible temporary differences in the balance sheet items "Provisions for pensions and similar obligations", "Other assets", "Property, plant and equipment" and "Intangible assets" in various tax jurisdictions that are not offset by material taxable temporary differences on the liability side.
Deferred taxes are measured using the respective national and company-specific tax rates at the expected realisation date. The applicable tax rates are 31.93% in Germany (comprising corporation tax of 15.83% plus the solidarity surcharge), 25.00% in Austria and the Netherlands, 27.50% in Italy (IRES tax rate plus 5.57% IRAP), 29.22% in Luxembourg, 30.00% in Spain and 22.00% in Denmark and Sweden.

Pension provisions and similar obligations are calculated using actuarial principles (accrued benefit method) based on the 2005 G mortality tables published by Dr. Heubeck. They are discounted using the average market interest rate for the past ten financial years. Freely available reserves were recognised for the profit arising in comparison with discounting using the average market interest rate for the last seven financial years.

Provisions were recognised for all identifiable risks and uncertain obligations on the basis of cautious business judgement.
The settlement amount of **other provisions** was calculated taking into account future price and cost increases. Provisions with a remaining term of more than one year were discounted using the average market interest rate for the past ten financial years corresponding to their term as calculated by Deutsche Bundesbank. Any repayment arrangements are taken into account in measuring provisions (net reporting).

Forward and other derivative transactions in indices and interest rate contracts are recognised at the prices and interest rates at the respective balance sheet date.

Fair value measurement of interest-based transactions in the banking book
All interest-based financial instruments in the banking book are subject to the principle of German commercial law that a provision for expected losses in accordance with section 340a in conjunction with section 249 (1) sentence 1 alt. 2 HGB is recognised for any excess obligation resulting from the measurement of the interest component of the entire interest rate position of the banking book. As of 31 December 2016, the Bank applies the comment issued by the IDW under RS BFA 3 "Individual questions relating to the fair value measurement of interest-based transactions in the banking book (interest rate book)" dated 30 August 2012 to the fair value measurement of interest-based transactions in the banking book. Under this method, the present value of the net interest income from these transactions is compared with the corresponding administrative and risk costs. There was no negative excess obligation at the reporting date. As such, no provision was recognised.

Assets and liabilities in foreign currency were translated at the middle ECB exchange rates at the reporting date. Where the ECB did not publish middle rates, the items were translated using the respective market exchange rates. Unsettled spot and forward exchange contracts were translated at the respective spot and forward exchange rates at the reporting date. All transactions in foreign currency were subject to special cover in the same currency in the form of countertrades. Income and expenses from foreign currency translation were treated in accordance with the requirements of section 340h HGB. The resulting net income is reported in the income statement under "Other operating income".

Balance sheet disclosures

Maturities

Receivables due from credit institutions	2016 EUR k	Previous year EUR k
Other receivables with maturities of		
up to three months	1.786.410	698.375
more than three months up to one year	2.980.397	620.915
more than one year up to five years	217.546	243.251
more than five years	150.416	337.169

Receivables due from customers	2016 EUR k	Previous year EUR k
with maturities of		
up to three months	2.465.259	457.940
more than three months up to one year	1.655.007	296.738
more than one year up to five years	487.533	219.596
more than five years	67.795	42.863
with an indefinite term	531.769	179.087

Liabilities to credit institutions	2016 EUR k	Previous year EUR k
with agreed term or period of notice of		
up to three months	2.648.327	600.245
more than three months up to one year	1.181.576	292.727
more than one year up to five years	471.702	205.257
more than five years	31.592	38.711

Liabilities to customers	2016 EUR k	Previous year EUR k
with agreed term or period of notice of		
up to three months	471.093	24.838
more than three months up to one year	39.243	1.021
more than one year up to five years	206.159	225.480
more than five years	146.192	256.713

Receivables from associated companies

	2016 EUR k	Previous year EUR k
Receivables due from credit institutions	8.312.483	2.727.809
Thereof: Receivables due from UBS AG	*8.271.823*	*2.694.756*
Receivables due from customers	10.874	1.455

Liabilities to associated companies

	2016 EUR k	Previous year EUR k
Liabilities to credit institutions	10.880.203	1.707.935
Thereof: Liabilities to UBS AG	*10.477.327*	*1.472.523*
Liabilities to customers	264.323	44.769
Subordinated liabilities	0	0

Receivables due from companies in which participations are held

	2016 EUR k	Previous year EUR k
Receivables due from customers	10.018	16

Liabilities to companies in which participations are held

	2016 EUR k	Previous year EUR k
Liabilities to customers	31.489	71

Shares and other variable-yield securities

Marketable:	EUR k	5.125
Listed:	EUR k	-

Bonds and other fixed-income securities

Repayable in the subsequent year:	EUR k	1.700.357
Marketable:	EUR k	2.365.059
Listed:	EUR k	2.365.059

Issued bonds

Repayable in the subsequent year:	EUR k	5.094

The item "**Equities and other non-fixed income securities**" contains shares in a real estate fund and non-fixed income securities that are not held in the trading portfolio. The decrease is primarily due to derecognitions of non-fixed income securities (EUR 354.0 million) used to secure repayment obligations for securities issued by the Bank. The non-fixed income securities were replaced by corresponding countertrades with UBS AG, London branch, as part of a restructuring.
The fair value amounts to EUR 5.1 million.

Statement of changes in fixed assets

in EUR thousand	Cost					
	Opening balance	Addition	of which capitalised borrowing costs	Disposals	Reclassifications	Closing balance
Equities and other non-fixed-income securities	362,005	3		354,039		7,969
Investments	163			119		44
Shares in affiliated companies	69	12,780		100		12,749
Goodwill		28,892				28,892
Other intangible assets	19,074	3,159				22,233
Property, plant and equipment	80,090	21,539		1,897		99,732

in EUR thousand	Depreciation, amortization and write-downs						Carrying amounts	
	Opening balance	Addition	Reversals of write-downs	Disposal	Reclassifications	Closing balance	Opening balance	Closing balance
Equities and other non-fixed-income securities	2,595	249				2,844	359,410	5,125
Investments		33				33	163	11
Shares in affiliated companies		1,271				1,271	69	11,478
Goodwill		2,578				2,578		26,314
Other intangible assets	18,989	1,087				20,076	85	2,157
Property, plant and equipment	75,204	4,574		1,874		77,904	4,886	21,828

Shareholdings in accordance with section 285 no. 11 HGB

Company	Suscribed capital		Share of capital	Result 2016	
Trustee VermogensParaplu B.V., Amsterdam	EUR	18.000,00	100%	EUR	0,00
UBS Custody Services Netherlands B.V., Amsterdam	EUR	125.000,00	100%	EUR	0,00
VermogensParaplu Beheer B.V., Amsterdam	EUR	18.000,00	100%	EUR	1.843.215,00
UBS Fiduciaria SpA, Mailand	EUR	200.000,00	100%	EUR	180.512,00
UBS Gestión Sociedad Gestora de Instituciones de Inversión Colectiva SA, Madrid	EUR	8.333.250,00	100%	EUR	5.125.097,11

Company	Suscribed capital		Share of capital	Result 2015 *	
UBS Private Equity Komplementär GmbH, Frankfurt am Main	EUR	25.000,00	100%	EUR	7.061,47

*The result for the year 2016 of UBS Private Equity

The **goodwill** relates to the acquisition of ETRA SIM S.p.A in 2005 and Santander Private Banking Unit (SPB Unit Italia) in June 2016 by the former UBS Italia S.p.A. and was assumed at its carrying amount in the course of the merger. The straight-line amortisation of the goodwill arising from the acquisition of ETRA SIM S.p.A is based on the original useful life of the Italian branch, which amounted to around nine years at the reporting date. The goodwill arising in connection with the acquisition of SPB Unit Italia is amortised over a period of seven years. This corresponds to the expected useful life of the other intangible assets arising from the acquisition, which relate solely to the customer base.

Other intangible assets consist solely of purchased software.

Property, plant and equipment at year-end 2016 consisted solely of office and operating equipment.

Other assets

"Other assets" primarily comprise receivables from intragroup settlements (EUR 37.5 million), receivables from the tax office (EUR 67.7 million) and variation/initial margins (EUR 201.9 million). In addition, derivative financial instruments with a carrying amount of EUR 307.2 million as of 31 December 2016 were assumed in the course of the merger.

Prepaid expenses

"Prepaid expenses" contain premiums paid in the amount of EUR 2.3 million and advance payments of non-labour operating costs in the amount of EUR 3.0 million.

Other liabilities

"Other liabilities" primarily comprise liabilities from intragroup settlements (EUR 37.8 million), liabilities to the tax office (EUR 28.4 million) and liabilities for litigation (EUR 64.8 million). In addition, derivative financial instruments with a carrying amount of EUR 306.5 million as of 31 December 2016 were assumed in the course of the merger.

Deferred income

"Deferred income" primarily contains premiums received for the issuance of promissory note loans (EUR 2.3 million), non-recurring rental subsidies of EUR 0.6 million recognised over the term of the respective rental agreement, and income received in advance in the amount of EUR 0.5 million.

Provisions for pensions and similar obligations

The provisions recognised relate almost exclusively to obligations for employees of the parent company in Germany.
The following assumptions were applied in measuring provisions for pensions:

- Actuarial interest rate:	4.01%
- Income and assessment threshold trend:	2.50%
- Pension trend:	1.5% for old commitments (issued prior to 1 January 1999) 1% for new commitments
- Fluctuation:	average 12.00%

In accordance with section 253 (6) HGB, the difference between discounting using a ten-year average interest rate and a seven-year average interest rate is required to be calculated as of the reporting date. The seven-year average discount rate published by Deutsche Bundesbank with a remaining term of 15 years in the amount of 3.24% is applied in presenting the comparative amounts for the purpose of calculating this difference. The resulting pension provision and deferred compensation provision amount to EUR 148.9 million and EUR 92.6 million respectively. Applying the corresponding ten-year average interest rate with a remaining term of 15 years in the amount of 4.01%, the pension provision and the deferred compensation provision would amount to EUR 135.0 million and EUR 83.7 million respectively. This results in a difference for pensions and deferred compensation of EUR 22.8 million, which may not be distributed or transferred.

Other provisions

"Other provisions" primarily comprise the following items:

Bonus	EUR	55.2 million
Early retirement obligations	EUR	10.1 million
Restructuring	EUR	43.1 million
Claims for damages	EUR	30.3 million
Claims for repayment of retrocession charges	EUR	2.0 million

Subscribed capital and shares

The subscribed capital of EUR 176,001,000 (previous year: EUR 176,000,500) is divided into 35,200,200 bearer shares that are wholly owned by UBS AG. The EUR 500 increase in subscribed capital compared with the previous year was due to the merger by absorption of the former UBS (Luxembourg) S.A.

Capital and revenue reserves

The net assets of UBS Italy, UBS Spain and UBS Netherlands based on the respective closing balance sheet, which totalled EUR 394.0 million at the absorption date, was added to the equity of UBS Europe SE as an increase in capital reserves in accordance with section 272 (2) no. 4 HGB.

The net assets of UBS Luxembourg based on the respective closing balance sheet in excess of EUR 500.00 at the absorption date (EUR 563.1 million) was added to the equity of UBS Europe SE as an increase in capital reserves in accordance with section 272 (2) no. 1 HGB.

Under Luxembourg tax law, a reduction in the wealth tax due is permitted if a special reserve that is non-distributable for a period of five years is recognised in the amount of five times the respective wealth tax liability. The non-distributable reserve forms part of the reported capital reserves in accordance with section 272 (2) no. 1 HGB in the equity of UBS Europe SE and amounted to EUR 124.5 million as of 31 December 2016.

Of the capital reserves in accordance with section 272 (2) no. 4 HGB, EUR 22.8 million related to the difference resulting from the adjustment of the discount rate in accordance with section 253 (6) HGB (see the notes on pension provisions).

EUR 217.1 million was withdrawn from capital reserves in accordance with section 272 (2) no. 4 and taken to the unappropriated surplus.

Revenue reserves remain unchanged at EUR 46.4 million.

Trust receivables and liabilities

Trust assets

	2016 EUR k	Previous year EUR k
Shares and other variable-yield securities	-	16.940
Participations	71.822	76.485

Trust liabilities

	2016 EUR k	Previous year EUR k
Liabilities to customers	71.822	93.425

The Bank provides its customers with the opportunity to invest in private equity funds. To allow them to also invest smaller amounts, the Bank enters into trust agreements with customers. This results in trust investments of EUR 71.8 million, which corresponds to the amount of the trust agreements entered into. The Bank does not hold any loans in trust.

Contingent liabilities and other obligations

Contingent liabilities relate solely to guarantees issued. Other obligations relate solely to irrevocable loan commitments. There is no material call risk.

Assets and liabilities denominated in foreign currency

Assets denominated in foreign currency totalled EUR 7,114.4 million (previous year: EUR 1,713.5 million), while liabilities denominated in foreign currency amounted to EUR 7,097.1 million (previous year: EUR 1,702.5 million).

Income statement disclosures

Net interest income

Net interest income contains EUR 29.3 million in negative interest paid and EUR 22.6 million in negative interest received. The net expense is primarily attributable to an investment with Deutsche Bundesbank. Negative interest of EUR 21.9 million was paid to Deutsche Bundesbank as a result of euro clearing, while negative interest of EUR 21.9 million was collected by the parent company UBS AG.

Net commission income

Portfolio management	EUR	33,7 m
Asset management	EUR	141,2 m
Brokerage of funds	EUR	61,7 m
Consultancy in Mergers and Acquisitions	EUR	22,1 m
Sales Income (shares, pensions and certificates)	EUR	31,5 m
Securities settlement	EUR	32,2 m
Other commission income	EUR	37,2 m
Total net commission income	**EUR**	**359,6 m**

Breakdown according to geographical source		
in EUR k	**Net Interest Income**	**Net Commission Income**
Denmark	-	135
Germany	11.849	166.606
Netherlands	-31	6.296
Italy	16.682	137.549
Luxembourg	2.175	8.671
Austria	220	1.696
Sweden	-	86
Spain	7.077	38.611
Total UBS Europe SE	**37.972**	**359.650**

The other disclosure for the financial year 2016 is contained in the country-specific reporting in accordance with section 26a of the German Banking Act (KWG).

Other operating income

This item primarily contains intragroup settlements (EUR 45.3 million), reversals of provisions (EUR 6.1 million), VAT refund claims (EUR 8.2 million) and currency translation income (EUR 0.9 million).

Other operating expenses

This item primarily contains payments and provisions in connection with customer complaints resulting in litigation (EUR 17.8 million) and expenses of EUR 9.3 million from unwinding discounts on provisions as of 31 December 2016 (including EUR 8.3 million for pension obligations).

Other disclosures

Proposal on the appropriation of net profit

The closing balance sheet of UBS Europe SE for the financial year 2016 contains an unappropriated surplus of EUR 169.0 million.

The Management Board proposes to pay out the unappropriated surplus as of 31 December 2016 to the shareholder in full. This corresponds to a dividend of EUR 4.80 per share based on a total of 35,200,200 shares.

Other financial commitments

Other financial commitments exist in the form of rental obligations for the premises of the head office and the branches. The rental agreement for the head office (Opernturm, Frankfurt/Main) expires in 2025. The rental obligations to 2025 for all premises total EUR 152.8 million, of which EUR 77.3 million relates to the Opernturm building (UBS Group).

Derivative financial instruments:

At the reporting date, the Bank had pending transactions in the following forward and option contracts

- Forward exchange contracts in foreign currency
  - Currency futures

- Transactions with other price risks
  - Equity/index option contracts
  - Swaps

Structured financial instruments were issued by the Bank in the past in the form of certificates and promissory note loans. The repayment amount for these instruments is directly dependent on the development of equity indices, foreign currencies or other values contained in the instrument as an embedded derivative alongside the underlying instrument. Until March 2016, the market risk of these issues was fully hedged by countertrades with UBS AG, London branch, and notes issued by Star Compass PLC. The Bank restructured its hedging operations in March 2016. The notes issued by Star Compass PLC were sold in full and replaced by countertrades with UBS AG, London branch. The Bank has formed hedges comprising the countertrades with UBS AG, London branch, used to hedge the repayment claims and the underlying issues. The underlying instrument and the embedded derivative are reported uniformly under securitised liabilities (certificates) or liabilities to customers and other banks (promissory note loans/registered bonds). Accounting for the existing hedges recognised on the basis of the net hedge presentation method takes account of deferred interest and discounts to the issue price. In March 2016, the issue price for certificates whose hedging was converted from notes issued by Star Compass Ltd to countertrades with UBS AG, London branch, was adjusted to the respective market value. The countertrades were capitalised in the same amount.

Hedges

The Bank is an issuer of structured financial instruments that are offered in the form of certificates and promissory note loans. The Bank also issues plain vanilla products that are offered to customers as promissory note loans and registered bonds. The repayment amount of the structured products depends on the change in the value of the underlying instruments. The Bank pays a fixed interest rate for its plain vanilla products. The Bank has concluded countertrades with UBS AG, London branch, to hedge its repayment obligations and the individual payment obligations arising from the financial instruments issued. These countertrades serve to hedge all the market, foreign currency and interest rate risks arising from all its issues. The issues and the countertrades form hedges. The corresponding hedging volume has a carrying amount of EUR 410.2 million. The hedges solely take the form of micro-hedges.
Foreign currency risk in the amount of EUR 6.9 million (market value) is hedged. In addition, interest rate risk of EUR 435 million (market value) is hedged.
The critical terms match method is applied for the micro-hedges. This is aimed at matching value components such as nominal amounts, payment currency, maturity and payment deadlines, and the repayment structure of the underlying and the hedging instrument. The formation of hedges mean that changes in market value do not represent a risk to the Bank and its results of operations are not affected.
The corresponding hedges are recognised at their carrying amount and the countertrades are capitalised at identical amounts.

Volume of derivatives and forward exchange contracts:

Derivatives for hedging issues:

	Par value	Market value	
		pos.	neg.
	in EUR m	*in EUR m*	*in EUR m*
Swaps on equities / indices	44,0	45,0	0,0

Derivatives and forward exchange contracts from brokerage:

	Par value	Market value	
		pos.	neg.
	in EUR m	*in EUR m*	*in EUR m*
Currency-related transactions	31.991,9	399,7	398,2
Interest-related transactions	7.875,5	44,3	44,3
Equity-/Index-related transactions	6.936,1	141,0	141,0
Other transactions	81,6	0,1	0,1

Accounting models and accounting policies

Option positions are measured using the Black-Scholes method. The market parameters are updated on a daily basis within the risk management systems.
Equity and index swaps, which constitute the majority of the hedging instruments for the alternative investment products issued by the Bank, are measured using the discounted cash flow method for the cash flows of equity/index performance and interest.
In line with Group policy, all the financial instruments are hedged with intragroup banks.

Contingent liabilities

There were no contingent liabilities as of 31 December 2016.

Auditor's fee

There is no disclosure of the auditor's fee as this is contained in the consolidated financial statements of UBS AG, Zurich.

Related party disclosures

The related companies of UBS Europe SE are defined as our parent company, UBS AG, Zurich, UBS Group AG and all unconsolidated companies, joint ventures and associates of the UBS Group.
The related persons are defined as the key members of management (Management Board, managing directors, Supervisory Board) of the UBS Group, UBS AG, Zurich, and UBS SE.

The following financial transactions are conducted with related parties (solely Group companies):

- Money market transactions, investments and borrowings
- Forward exchange contracts in equities, currencies, bonds and structured products
- Options in equities, bonds and currencies
- Equity and interest rate swaps
- Securities lending
- Warranties and guarantees
- Procurement/performance of intragroup services

All transactions are concluded at arm's-length conditions.

Significant events after the reporting date

The Bank is not aware of any significant events after the end of the financial year that have not already been reported in the income statement and the balance sheet.

Liquidity

Total liquidity, which is defined as the ratio of realisable holdings (asset items from cash in hand to receivables from customers with a term of less than three months) to liabilities to other banks and customers with a term of less than three months, amounted to 83.07% at the reporting date.

Group affiliation

As of 31 December 2015, UBS Group AG, Zurich, held all the share capital of the Bank via its subsidiary UBS Beteiligungs-GmbH & Co. KG, Frankfurt/Main. A control and profit and loss transfer agreement in accordance with section 291 AktG was in place with the sole shareholder until 31 December 2015.
As of midnight on 1 January 2016, UBS Beteiligungs-GmbH & Co. KG sold and transferred all its shares in the Bank to UBS AG, Zurich. The control and profit and loss transfer agreement was unanimously cancelled with effect from midnight on 31 December 2015.

UBS Europe SE is included in the consolidated group of UBS Group AG, Zurich. In line with the Regulation on Exempting Consolidated Financial Statements (Konzernabschlussbefreiungsverordnung), UBS Europe SE therefore refrains from preparing subgroup financial statements.
UBS Group AG, Zurich, prepares exempting consolidated financial statements. The consolidated financial statements are prepared in accordance with the International Financial Reporting Standards (IFRS) as published by the International Accounting Standards Board (IASB). These are the consolidated financial statements for the largest group of consolidated entities. The 2016 consolidated financial statements of UBS Group AG, Zurich, can be obtained on the UBS website and are published in German in the electronic Federal Gazette (Bundesanzeiger) by UBS Beteiligungs-GmbH & Co. KG, Frankfurt/Main.

Disclosure

The disclosure report for the year ended 31 December 2016 is published on the UBS website at https://www.ubs.com/de/de/ubsgermany/finanzberichteundmitteilungen.html.

Executive bodies of the company

Supervisory Board

-	Roland Koch, Chairman Independent attorney, Former Prime Minister of the State of Hesse, Frankfurt	
-	Jakob Stott, Deputy Chairman, Divisional Vice Chairman Wealth Management, UBS Switzerland AG, Zurich	from 1 December 2016
-	Silke Alberts*, Chair of the Works Council, UBS Europe SE, Frankfurt	
-	Andrea Dech*, Security Specialist, Frankfurt	until 30 November 2016
-	Univ.-Prof. Dr. Armin Heinzl, Faculty of Business Administration and Business Informatics, University of Mannheim	until 30 November 2016
-	Dr. Ulrich Körner, President Asset Management and President Europe, Middle East and Africa, UBS AG, Zurich	
-	Jean-Marc Lehnertz*, Business Risk and Regulatory Management, UBS Europe SE, Luxembourg	from 13 December 2016
-	Emma Molvidson, Chief of Staff President Investment Bank, UBS AG, Zurich	from 1 December 2016
-	Piero Novelli, Chairman of Global M&A, UBS AG, Zurich	until 30 November 2016
-	Francesco Stumpo*, Wealth Management IT Application Delivery, UBS Europe SE, Milan	from 1 December 2016
-	Tanja Weiher, Chief of Staff to the Group CEO, UBS AG, Zurich	from 13 December 2016
-	Dr. Martin Wittig, managing director and CEO mcw Management Services AG, Silvaplana	from 13 December 2016

*Employee representative

In accordance with the resolution by the Annual General Meeting on 27 April 2016, total remuneration of EUR 30 thousand was paid to the employee representatives on the Supervisory Board and total remuneration of EUR 309 thousand was paid to the independent Supervisory Board members in the year under review.

Management Board

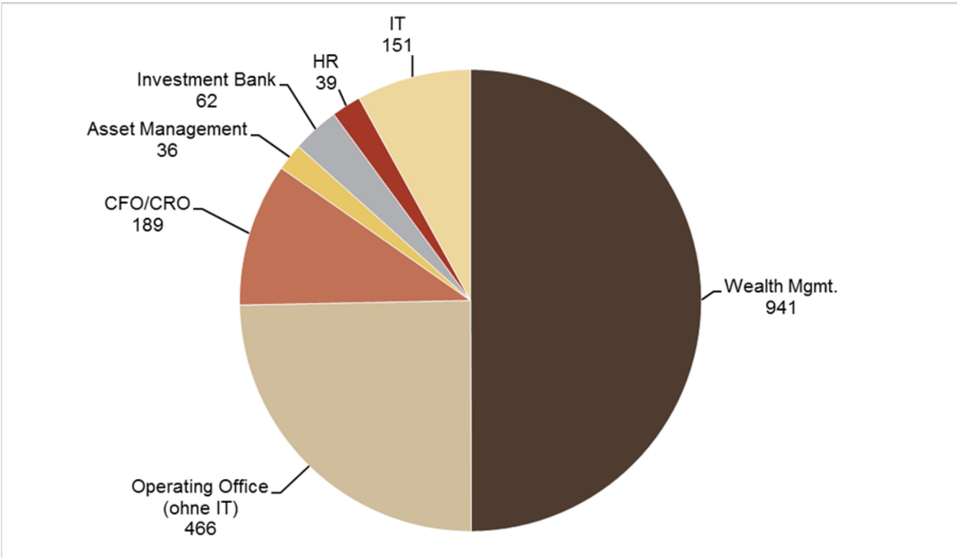
-	Thomas Rodermann, Spokesman of the Board, Market Head Germany and Austria	
-	Carsten Dentler, Investment Bank, Head Corporate Client Solutions	until 30 November 2016
-	Birgit Dietl-Benzin, Chief Risk Officer (Chief Risk Officer and Chief Financial Officer until 30 November 2017)	from 1 January 2016
-	Fabio Innocenzi, Market Head Italy and Iberia	from 1 December 2016
-	René Mottas, Market Head Benelux and Nordics	from 1 December 2016
-	Dr. Andreas Przewloka, Operating Head and Chief Financial Officer	
-	Matthias Schellenberg, Head Asset Management Germany	until 30 June 2016
-	Stefan M. Winter, Head Corporate Client Solutions and Investor Client Services	

The remuneration paid to the members of the Management Board in the year under review totalled EUR 5.3 million. This figure comprised the basic salary, variable remuneration and other remuneration components.
We paid EUR 2.5 million to former members of the Management Board, i.e. members of the former UBS Deutschland AG, and their surviving dependants; the pension provisions for these individuals amounted to EUR 33,079 thousand as of 31 December 2016.

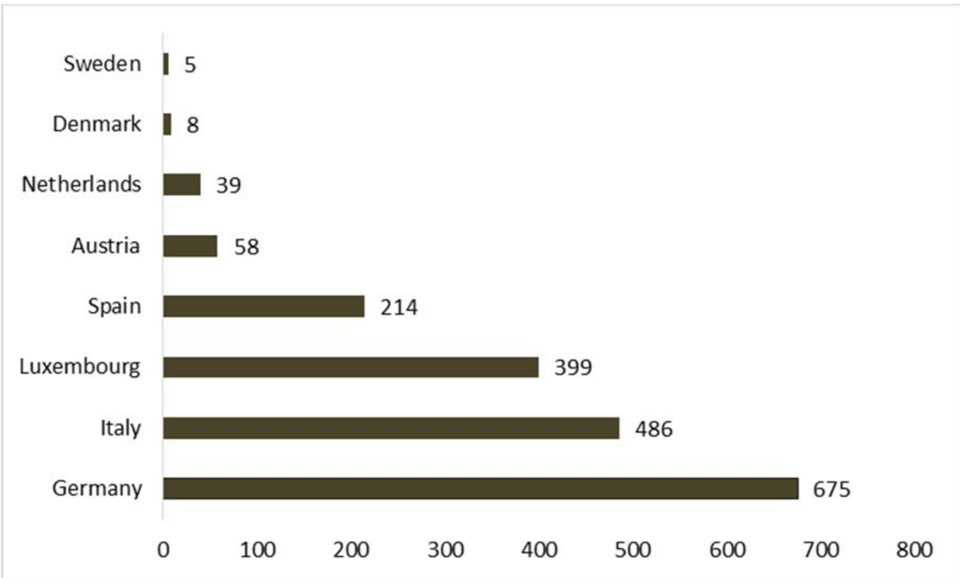
Employees

The Bank had a total of 1,884 employees as of 31 December 2016. The average number of employees for 2016 was 1.525. A total of 41 employees were on parental leave as of 31 December 2016.

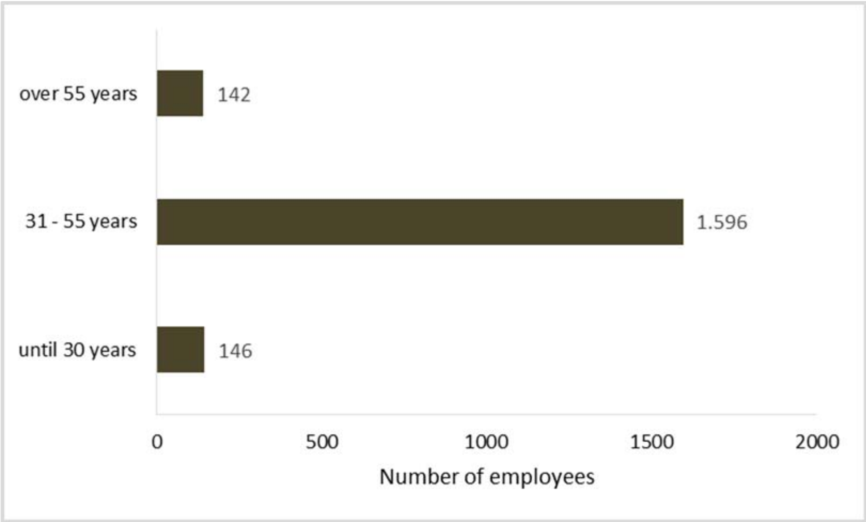
- Breakdown by division



- Breakdown by location

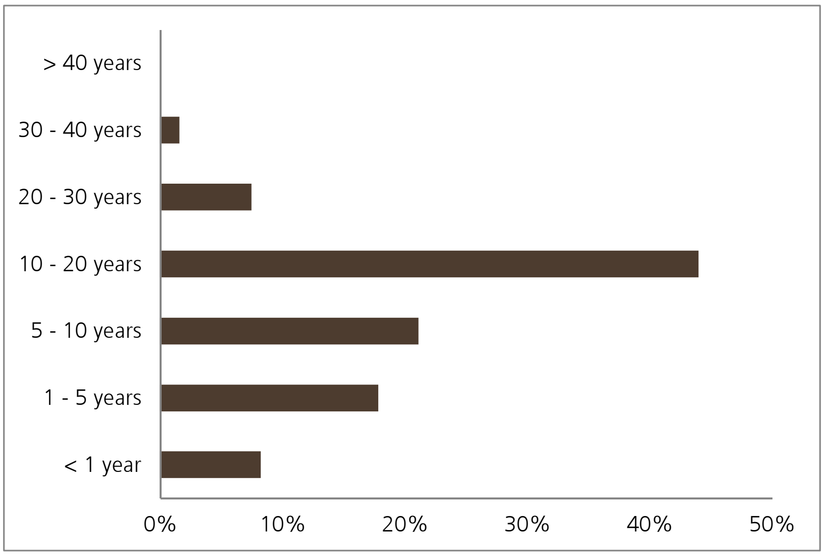


- Age structure



- Breakdown by gender

- Breakdown by length of service



Frankfurt/Main, 16 May 2017

UBS Europe SE

Thomas Rodermann	Birgit Dietl-Benzin	Fabio Innocenzi
René Mottas	Dr. Andreas Przewloka	Stefan M. Winter

Other disclosures in accordance with Sec. 26a (1) Sentences 2 and 4 KWG ("Kreditwesengesetz": German Banking Act) for fiscal year 2016 (Arts. 89 and 90 of Directive 2013/36/EU)

Counrty-by-Country Reporting (Sec. 26a (1) Sentence 2 KWG))

1. UBS Europe SE is included in the scope of consolidation of UBS Group AG, Zurich.
UBS Group AG, Zurich, prepared exempting consolidated financial statements. These are available at UBS Europe SE and are published by UBS Beteiligungs-GmbH & Co. KG, Frankfurt am Main, in German language in the Electronic Federal Gazette ("elektronischer Bundesanzeiger").
The consolidated financial statements have been prepared in accordance with International Financial Reporting Standar as published by the International Accounting Standards Board (IASB).

2. UBS Europe SE has forreign branches in the following locations:

- Copenhagen, Denmark
- Amsterdam, Netherlands
- Milan, Italy
- Luxembourg, Luxembourg
- Vienna, Austria
- Stockholm, Sweden
- Madrid, Spain

3. UBS Europe SE offers the following key services:

- Wealth Management und -advice for private customers
- Custody Business (including its custodian bank function)
- Distribution of funds
- Consultancy in Mergers and Acquistions
- Research for German equities
- Issuance of certificates, promissory note loans and registered bonds

4. UBS Europe SE generated a revenue of EUR 459.980 k. This amount includes the following components:

- Net interest income
- Net commission income
- Current income
- Trading income
- Other operting income

Country-by-Country information is provided on a gross basis (i.e. before the expensing of borrowing costs between bra

Revenue	in EUR k
Denmark	143
Germany	222.032
Netherlands	9.067
Italy	163.141
Luxembourg	12.572
Austria	2.016
Sweden	105
Spain	51.128
Total UBS Europe SE	**460.204**

5. The average number of employees in full-time equivalents was 1.816 in 2016.
The merger of UBS Luxembourg S.A. (including its branches in Denmark, Austria and Sweden) into UBS Europe SE took place on 01.12.2016. The average for these branches was calculated on an annual basis for reasons of comparability.

Number of employees	
Denmark	7
Germany	644
Netherlands	40
Italy	469
Luxembourg	386
Austria	57
Sweden	5
Spain	208
Total UBS Europe SE	**1.816**

6. Net loss before taxes amounts to EUR 31.988 k and the taxes on profit and loss were EUR 16.147 k.

in EUR k	Result before taxes	Taxes on profit and loss	**Result after taxes**
Denmark	-686	0	**-686**
Germany	-70.758	0	**-70.758**
Netherlands	-604	0	**-604**
Italy	38.084	15.835	**22.249**
Luxembourg	1.693	1.377	**316**
Austria	-18	57	**-75**
Sweden	-86	0	**-86**
Spain	387	-1.122	**1.509**
Total UBS Europe SE	**-31.988**	**16.147**	**-48.135**

7. UBS Europe SE did not receive any public subsidies in the reporting year.

Disclosure of return on capital (Sec. 26a (1) Sentence 4 KWG)

Return on capital (as the ratio of net profit by total assets) for UBS Europe SE is – 0,17%.

UBS Europe SE
Annual Report 2016 – Management Report

I. Business Report

Divisions and organization

Throughout 2016 UBS Group developed its European strategy and implemented significant measures to consolidate and simplify its legal structures and regulatory regime in Europe, optimize the capital structure and create a uniform operational model to utilize economies of scale. As part of that strategy, UBS Bank (Netherlands) B.V., UBS Italia S.p.A., UBS Bank (Spain) S.A., UBS (Luxembourg) S.A. with its branches in Austria, Denmark and Sweden and UBS Deutschland AG executed joint draft terms of merger on 10th of February 2016, setting out the terms under which the mentioned entities would be merged into one European Company.

This resulted in the creation of UBS Europe Societas Europea (UBS Europe SE), which was formed on 1st of December 2016 through a parallel side-stream merger of these seven European Wealth Management units into UBS Deutschland AG.

All assets and liabilities of the listed entities were transferred with their book values to the accounts of UBS Europe SE as of 1st of December 2016 in the case of UBS (Luxembourg) S.A. and as of 1st of January 2016 in the case of all other entities. The formerly independent bank subsidiaries became branches of UBS Europe SE.

The bank is a direct, one hundred percent subsidiary of UBS AG, Zurich. Its organizational structure is based on the former structure of UBS Deutschland AG, comprising the three divisions Wealth Management, Investment Bank and Asset Management with its sales function. The business activities of the Investment Banking and Asset Management divisions are essentially limited to Germany. As a universal bank within the meaning of the German Banking Act (KWG) and as an SE under European law, its administrative bodies are the Management Board, Supervisory Board and Annual General Meeting. The Management Board autonomously controls the business activities of Wealth Management, Investment Bank and Asset Management, in addition to the Corporate Center units which support them.

Throughout 2016 the Management Board of the former UBS Deutschland AG experienced some notable changes. The former members of the Management Board Matthias Schellenberg and Carsten Dentler, who had been valuable assets for UBS in Germany throughout the years, left the company on 30th of June and 30th of November 2016, respectively. Birgit Dietl-Benzin (Chief Risk Officer) joined the Board as of 1st of January 2016; Fabio Innocenzi (Market Head Italy & Iberia) and René Mottas (Market Head Benelux) as of 1st of December. The Management Board of UBS Europe SE further consists of: Andreas Przewloka (Chief Operating Officer, Chief Financial Officer), Thomas Rodermann (Spokesman, Market Head Germany & Austria) and Stefan Winter (Head Investment Bank Germany). The Supervisory Board is chaired by Roland Koch and further consists of Jakob Stott (Deputy), Dr. Ulrich Körner, Emma Molvidson, Tanja Weiher, Dr. Martin Wittig, Silke Alberts, Jean-Marc Lehnertz and Francesco Stumpo.

Organizationally, 2016 also saw some changes to the structure of UBS Deutschland AG before its transformation into UBS Europe SE. As part of long-term strategic efforts to streamline our cross-divisional business activities, the accounting and reporting service provider Inter-Concern-Revisions GmbH (ICR), previously owned by UBS Deutschland AG through BV Beteiligungsverwaltungsgesellschaft mbH (BV), was sold to the Hamburg based consulting firm Spudy Invest GmbH on 1st of September 2016 alongside the BV through which it was owned.

The newly created UBS Europe SE has its core business in **Wealth Management** for Ultra High Net Worth (UHNW) clients including Family Offices, High Net Worth (HNW) and Affluent client segments within the European Union. The Financial Intermediaries (FIM) client segment supports UBS Europe SE's business by providing access to markets and clients beyond the bank's client advisor network. Geographically, the Wealth Management division encompasses eight countries with a total of 23 branches in Europe. In Germany, Luxembourg, Spain and Italy UBS Europe SE also acts as a strategic business partner for financial intermediaries.

The **Investment Bank** structure of UBS Europe SE is based on the former Investment Bank structure of UBS Deutschland AG. At its core, the Investment Bank is divided into two independent and aligned business units: Corporate Client Solutions (CCS) and Investor Client Services (ICS).

CCS comprises the entire business in consulting and financing solutions, origination, structuring and clearing, including capital markets (equities and bonds as well as leveraged finance) for corporate clients, financial institutions and sponsors, as well as Family Offices and Institutional Wealth Management clients. It also incorporates Mergers and Acquisitions.

Investor Client Services (ICS) includes clearing, distribution and trading for institutional investors, supporting both Corporate Client Solutions and the Wealth Management business of UBS. This unit also involves other business activities in the field of equities, including cash, derivatives and research expertise covering various asset classes, along with our Foreign Exchange, Rates and Credit (FRC) business. FRC focuses on institutional clients, from the fund and insurance sector to other financial institutions.

In addition to the two core units of the Investment Bank division, Corporate and Institutional Clients (CIC) is responsible for maintaining and expanding the local product offering for Cash Management Solutions and, by cooperating closely with other CIC teams across the international UBS network, allowing UBS to offer its global expertise to clients in Europe.
Overall, the Investment Bank division assumes a sales-and distribution function for the mentioned services and products. For UBS Europe SE no risks arise from these transactions as new business is reflected comprehensively on the balance sheet of UBS AG. For its sales activities the bank receives its proportionate share of income.

The **Asset Management** structure of UBS Europe SE is based on the former Asset Management structure of UBS Deutschland AG. In Germany we offer asset management for I. Institutional investors such as insurance companies, pension funds, companies, pension insurance carriers, church institutions and foundations, II. wholesale clients (banks, savings banks and other financial service providers) and III. UBS Wealth Management clients.

Value proposition

UBS Wealth Management's vision is "We want to create superior value for our clients, shareholders and employees. And we want to stand out as a winner in our industry: for our expertise, advice and execution, our contribution to society, our work environment, and our business success." We aim to expand our presence in Europe as the UBS home market over the long term. In all of our business activities we want to be one of the market leaders and the first choice among our target clients based on our 4-pillar UBS Europe SE value proposition: (I) Global strength, (II) local roots, (III) cross-divisional collaboration and (IV) superior investment advice & research.

Strategy

The merger of UBS Europe SE underlines our commitment to the European market and our ambition to further strengthen our leading position as an international financial service provider. We strive to offer best in class client service and optimize the use of capital through a simplified legal entity structure and an integrated operating platform, all with a clear ambition for sustainable growth in mind.

When defining its strategy, UBS Europe SE was building on the fundamental basic principles established by UBS Group AG for all of its global businesses and their respective strengths, while also leveraging its insight into specific local markets and adjusting to the needs of its European client base. On a mid to long-term perspective we have determined three division-overarching strategic priorities: I. Expanding Wealth Management Europe as the home market of UBS Europe SE, II. increasing revenues and generating new business through the improvement of our client advisor performance and ultimately, III. intensifying our cross-divisional collaboration to provide clients with the full range of the group's expertise.

As part of our revenue boosting effort (strategic priority II) we are focusing on the increased recruiting of client advisors and a structured lead generation process.

Cross-divisional collaboration between the various segments and markets in Wealth Management, and the business divisions of the Investment Bank and Asset Management is essential. In order to determine the optimal solution for our clients, we make use of the expertise from all three divisions, selecting the most suitable products and services from each. Owing to our size, we are able to scale the services in all divisions of the company and offer them not only to institutional, but also to our private clients, especially in the UHNW segment.

Across all divisions and hierarchical levels **efficiency and cost management** are integral parts of our strategy, in particular against the background of the ever-increasing pressure on margins. We will focus on cost initiatives that won't compromise our customers' experience, but help us to improve our service quality and make internal processes more efficient.

In the field of **Wealth Management**, we have defined a clear growth strategy based on the following six pillars: (I) seizing of growth opportunities, (II) process standardization and digitalization, (III) specialized segment strategies, (IV) brand communication, (V) cross-divisional collaboration and (VI) global access to our services.

Beyond the mere **standardization** of processes and services, **digitalization** is taking on major significance as part of our growth strategy. Above all, this is justified by changed client behavior and an increased demand for digital banking services. Based on our strong platform, we are investing, in particular, in the expansion of our online offers within the context of the WM Online project (WMO), Straight Through Contract Processing (STCP) as one of the future leading platforms in the world for the management of investment mandates and the expansion of client access through mobile devices via client-friendly apps in order to achieve differentiation in the market and address new client groups.

The investment and advisory business will become a high-tech, high-touch industry, one in which clients choose the touch-points or channels through which they want to receive our services – as in other areas of everyday life. Clients expect us to select from the abundance of available information, interpret the information that is relevant for them and matches their individual risk-return-profile and, on this basis, provide them with meaningful proposals on how to manage their wealth in a compliant manner. This requires taking both the relevant regulations and a client's individual investment profile into account. Combining the use of human expertise and technology to give clients better advice is at the core of delivering our client promise to a larger audience, mainly in the Affluent segment.

For that purpose UBS in Germany has launched its novel service model UBS [Access] which addresses clients willing to invest up from 100,000 EUR to access or test our capabilities. The remote advice model is offered in a convenient, engaging way by fully leveraging the digital capabilities of UBS Wealth Management Online. It targets the digital-savvy clients who seek wealth management that is constantly accessible both online and via personal contact by phone. Upon launch in October 2016, UBS [Access] provided the "UBS Vermögensverwaltungsmandat" UBS Manage [Access] with a simple, asset based, all-in fee model. This was followed by the introduction of UBS Systematic Allocation [Access] in April 2017.

The support model in Wealth Management provides for a **segment-specific orientation** of the product and service range. By aligning our organization with our customer segments more stringently, we can streamline our services towards the specific needs of our heterogeneous client base. For that purpose we have differentiated several client segments: Ultra High Net Worth, High Net Worth and Affluent for our private clients and the Financial Intermediary (FIM) segment for our institutional clients.

In terms of **brand communication** and as part of UBS Wealth Management's pursuit of additional market share, the marketing strategy has been streamlined and sharpened with focus on the following three core objectives: (I) Communicating the WM Client Promise consistently and with clarity, (II) improving Client Experience and finally, (III) generating prospects. The overarching objective of the 2017 marketing strategy is to contribute tangible and measurable growth, expressed in quality contact inquiries through a consistent lead management funnel. These objectives will be accompanied by specific initiatives focusing on the main growth levers for the UBS Wealth Management: Increased female participation, entrepreneurship and next generation acquisitions. In the European markets the global Wealth Management Marketing Strategy will be applied, building on the established regional strategy and a set of successful pilots and marketing projects – examples include Investor Watch, UBS Forum Event Series or UBS Forum Digital, a streamlined and increasingly growth-oriented event landscape.

We want to offer our clients in the European market **global access to our services** through the different booking centers – taking into account all directives governing cross-border business. In this collaboration we take advantage of synergy effects, in particular with respect to joint activities and projects.

Within the framework of the UBS Group strategy in Europe, the **Investment Bank** division has selectively withdrawn from products and business activities which are excessively complex and do not generate any stable, risk-adjusted returns under the Basel III rules or are associated with the intensive use of risk-weighted assets and capital. Since 2012 we have been focusing on our traditional strengths in the consulting business for Mergers and Acquisitions, transactions in the equity and debt capital markets, leveraged finance as well as the equity and foreign exchange sector. Proprietary trading has been discontinued. The Investment Bank, Wealth Management and Asset Management divisions are not authorized to take market risks either actively or passively or generate proprietary trading profits or losses, unless these are margin allocations. Instead our Investment Banking division will be focusing on clients with particularly high levels of income and potential in order to ensure sustainable growth, on the core activities of consulting and our leading position in the equity and foreign exchange field. As an integral part of the overall strategy of UBS Europe SE, the Investment Bank will be further expanding its collaboration with Wealth Management and Asset Management and help us to position ourselves in the market through the active communication of our comparative strengths. The collaboration within the various areas of the Investment Bank, as well as with Asset Management and Wealth Management, is crucial to identify and realize new business opportunities and synergy effects.

The strategic priorities of our **Asset Management** division are aligned with the overall goals of UBS Europe SE and aim to support our core business activities. In order to distinguish ourselves in the market and strengthen our position as one of the leading international Asset Managers in Europe, we have decided to focus more distinctly on promising client segments and offer tailored products and solutions. UBS Asset Management also seeks to intensify its collaboration with selected partners, especially high-potential institutional clients.

Management systems

The Bank's management systems comprise planning and reporting systems.

Planning systems are used mainly for the annual strategic planning (for a period of three to five years) and the rolling forecast (quarterly forecasting for the current and following year).

In the scope of the top-down strategic planning, the targets for UBS Europe SE are discussed and agreed with the parent company, UBS AG. The planning horizon is longer term. The agreed target is broken down by sales unit/segment and agreed with the relevant party (region or segment). Strategic planning relates chiefly to key performance indicators, such as targets for net new money, income, direct costs and the number of front office and support staff.

Local planning is based on the rolling forecast, which is prepared by the divisions on a quarterly basis and is based on anticipated business developments in the subordinated units (branches, segments) over the next six quarters (bottom-up approach).

The consolidated results of the local rolling forecast are compared to the top-down plan. Deviations are analyzed by the Controlling department and reported to management.

The key **reporting system** is the cost center accounting system (web-based standard reporting system "DOMINO"). The DOMINO reporting system focuses on the following figures for the last three (up to 23) months of the current year and the same prior-year period: Managed assets, net inflows/outflows of customer funds, costs, income broken down by type and product, margins, number of front office and support staff and number of customers. The above mentioned indicators are also reported in relative terms such as income per customer advisor or cost-income ratio.

II. Economic Report

Financial performance indicators

Our key financial performance indicators (KPIs) are aligned with our business objectives, focusing on the drivers of direct increases in efficiency and profitability. Hence, all levels of divisions’ functional organizational structure (segment, location and team level) are covered. The following performance indicators, among others, are analyzed on a monthly basis: Across all divisions attention is paid to the cost/income ratio, which compares the direct cost of sale with net income. In the Wealth Management and Asset Management divisions additional KPIs are of relevance: Net inflows of funds (net new money), revenue, number of new customers and managed (invested) assets per client advisor (CA). Additionally, the return on assets (margin on managed assets) and the ratio of front/support staff represent important performance indicators.

Non-financial performance indicators

The performance of UBS Europe SE cannot be measured using financial indicators alone. Our competitiveness and target achievement are largely – as with every service company – dependent on the quality of our employees. Therefore we actively promote staff commitment, qualification and performance. Employee satisfaction is measured in group-wide employee surveys on a regular basis. In Germany, following the employment protection act (Arbeitsschutzgesetz (ArbSchG)); a mandatory vulnerability analysis has been conducted. The results hereof as well as the results of the employee satisfaction survey which are of relevance for the German head office and the branches, are analyzed by the senior management; staff is informed of positive aspects and areas in need of improvement. Corresponding measures are developed and implemented.

In the course of the group-wide cost efficiency effort – mainly in the mid and back offices – new restructuring measures have been defined and implemented throughout the predecessors of UBS Europe SE during the year. When defining the related personnel measures, available resources in the units were reviewed and adapted to the relevant volumes and core areas. The level of staff turnover at UBS Europe SE was 8.4 % overall and varied between 0 % in Sweden and approximately 15 % in the Netherlands. The average length of service of permanent employees is approximately 10.6 years, showing the shortest length of service in Denmark with 1.7 years and the longest in Germany with 11.6 years. To avoid a high level of staff turnover among top performers, individual staff retention measures have been agreed and implemented.

Disregarding the mentioned efficiency measures, our strategic focus was geared towards the hiring of client advisors. Recruiting first-class professionals in all areas of the entity as well as hiring and developing young talents enables us to strengthen our organization and increase the diversity of our workforce. UBS is particularly concerned with the promotion of women in management positions both globally and locally. To support these efforts the focus lies on:

- Working towards an inclusive and diverse organizational culture as a general means of achieving sustainable performance.
- Fostering meritocracy, performance and objective and fair assessments.

UBS Europe SE addresses diversity goals by local measures. Italy, for example, has developed a Diversity and Inclusion (D&I) program that includes both training plans and specific initiatives aimed at creating an inclusive corporate culture. Dedicated D&I Ambassadors have been nominated to support the bank in the design of the D&I strategic initiatives. The awareness and training initiatives are directed towards line managers and employees, likewise and focus on "The value of diversity"

and the management of "Unconscious bias". The latter is a group-wide initiative that will also be rolled out in other locations throughout 2017.
The branch in Luxembourg, as another example, is a member of the Diversity Working Group of Luxembourg's Banking Association (ABBL) and the former UBS (Luxembourg) S.A. signed the "Charte de la diversité Lëtzebuerg".
The above mentioned goals have also been incorporated into human resource processes. In this context, UBS Europe SE in particular supports work-family balance through (depending on location) promoting part-time work, bank funding of childcare provided in association with cooperation partners and occupational reintegration management. The latter consists in that employees on long-term absence (e.g. maternity leave) enjoy maintenance of their roles and coverage with the current workforce, fix-term contracts or secondments. Furthermore, an integrated local occupational health management program (e.g. health checks, preferred conditions for fitness centers) is in place to foster the long-term performance of employees in an ever-changing working environment. In 2016 UBS Group conducted for the first time a worldwide health day on November 9th.
In an effort to adapt even more to today's environment, Italy developed a pilot with regards to "agile work", that allows employees to work in a more flexible and innovative way from home. This is having a positive impact on work-life balance, an index that UBS is regularly monitoring in the internal employees survey.
Pursuant to Article 76 (4) and 111 (4) AktG ("Aktiengesetz": German Stock Cooperation Act) in conjunction with the FührposGleichberG ("German Act on the Equal Participation of Women and Men in Management Positions"), in 2015 the predecessor of UBS Europe SE (UBS Deutschland AG) defined targets for the ratio of female employees on the Supervisory Board, the Management Board and in the two management levels below the Management Board. The Supervisory Board defined a target quota for women in the Management Board of 20%, the quota of women in the Supervisory Board, which was set at 33% before was kept at this level. The Management Board has maintained the former quota of 27% for women in the first management level below Management Board, regarding the second management level an increase from 7% to 20% has been agreed. The defined targets shall be achieved until 30th of June 2017.
Currently UBS Europe SE has a ratio of women to men in the Supervisory Board of one third to two thirds. Management Board representation is 1 to 5 but it is envisaged to increase this ratio to 2 to 5 in the next year.

In recognition of its Corporate Social Responsibility (CSR), UBS Europe SE also actively engages in local community work. One example of such is the Community Affairs Working Group in Italy. The latter has developed a convincing program that achieved excellent results in the local community, in particular in the fields of education, employability and social inclusion. The UBS teams involved have used their collective expertise to select partners, recruit volunteers among UBS employees and tackle some of the current major educational, employment and social issues. The community affairs activity is recognized both at country level and at international UBS level, among others in the form of specific awards. Germany also conducted several initiatives in the fields of youth / education (e.g.

professional orientation program for pupils), social entrepreneurship as well as charity runs with more than 220 volunteers and more than 800 volunteer hours.

Overall economic environment

Recent data suggest that the Eurozone economy ended 2016 on a bright note, despite the uncertainties created by various political developments, finishing the year with an overall real GDP growth rate of 1.8 %.

As labor markets improve and continue to drive up consumption, economic output has been growing for almost four consecutive years since the recovery began in 2013. Although the recovery has been gradual, recent data indicates that it is becoming more broadly based across different countries and sectors.

Apart from rising consumption levels across the Eurozone, which are seen as the main driver of growth, survey indicators signal improvements in foreign demand and new export orders. In addition, the depreciation of the effective exchange rate of the Euro since the third quarter of 2016 should provide some gains in competitiveness for key European exporters. However, any emergence of protectionist tendencies around the world could deteriorate the outlook for foreign demand in the longer term.

Overall, credit conditions in the Eurozone and across Europe remained very supportive as borrowing costs for firms continued to decline and bank lending growth further strengthened, also reflecting the continuingly expansive monetary policy measures put in place by the European Central Bank since mid-2014.

Furthermore, throughout 2016, most countries in Western Europe have seen appreciable equity-market performance, such as Italy with 15 %. Countries like Spain and Portugal that had been in substantial difficulties in 2013 experience continuous growth of private wealth of 4 %, driven largely by a rising bond market (12 % in Spain and 9 % in Portugal). The expansion of Western European private wealth is supported mainly by modest gains in bonds, driven in part by the European Central Bank's monetary policy. Growth in private wealth is highest in countries with a relatively high share of bonds, such as Denmark (wealth growth of 10 %, bond share of 45 %) and Italy (wealth growth of 6 %, bond share of 48 %).

The developments on the financial markets and positive effects caused by continuously rising trade demand can also be attributed to the stable trajectory of the global economic recovery. Although the first half of 2016 did not pick up significantly from the relatively weak trend of 2015, the global performance for the second half of the year showed stable growth in developed economies and slight improvements in the emerging markets.

Over the last two years many developed economies in Europe and North America have seen historically low levels of inflation, with lower oil prices regarded one of the drivers of that development due to their crucial role in the Consumer Price Index (CPI).

After a prolonged period of cheap crude oil in late 2015 and early 2016, with Brent crude oil prices dropping under 30 U.S. Dollar in January 2016, oil prices started to rally throughout the second half

of 2016 and stabilized towards the end of the year after a deal between OPEC and other oil producing nations had been reached. The deal is expected to support the rebalancing of the oil market over the coming months.
The Euro Area's harmonized inflation came in at 1.1 % in December, which was above November's 0.6 % and marked the highest reading since August 2013. Inflation climbed in December as the effect of low energy prices dissipated and a weaker Euro fueled price pressures. As a result, inflation is now out of what European Central Bank President Mario Draghi has called the "danger zone" of below 1.0 %. Despite rising prices, the ECB made no considerable changes in its monetary policy throughout the year and has signaled no intention of changing its course. The ECB stressed that a high degree of accommodation was still needed and that they would evaluate price pressures on an aggregate level going forward, ignoring quicker inflation in certain core countries.

Business in 2016

The European Wealth Management market is undergoing fundamental structural changes with significant implications for the bank (e.g. customer protection, MiFID II, regulatory changes, pressure from local regulators, technological change). As the internationally divided entity structure was likely to limit inorganic growth opportunities and the possibility to gain cross-divisional efficiencies, the decision to consolidate and optimize our entity structure allowed us to focus on delivering an "onshore" experience to our WM clients, combined with easy market access for all businesses across all the European Economic Area (EEA) countries.

For UBS in Europe the year 2016 was dominated by our decision to adopt to the changing needs of our client base and shift to a more internationally positioned approach to **Wealth Management** by planning and implementing the transition to UBS Europe SE as a pan-European Wealth Manager. Despite the increasingly competitive business environment, UBS Europe SE, with its EUR 113 bn of assets under management remains one of the top internationally positioned Wealth Managers in the region. In accordance with our expectations, the bank was therefore able to increase the assets under management in its main business of Wealth Management and therefore strengthen its revenue base through the acquisition of new customers and additions to stocked assets by existing customers.

In the light of the merger to UBS Europe SE previous forecasts regarding the generation of new business and customer acquisition are not directly comparable to the actual business performance of the year. In general terms however, the bank recorded a growth in business and was therefore able to meet its goals.

A successful strategic transformation secured a strong market position for the **Investment Bank** division. In Cash Equities, we have a clear competitive advantage over foreign banks due to our local presence with sales specialists, supported by local research experts in Frankfurt, while at the same time being able to access the global expertise of UBS Investment Bank. In Equity Derivatives, we focus on high potential institutional clients, in particular pension funds and insurers with an interest

in fund linked product solutions and long-term options which we consider to have attractive growth potential.
We have integrated Debt Capital Markets (DCM) more strongly into structured solutions business and are expanding the rate flow business using structured derivatives, private placements (callable / plain), new issues and priority transactions which do not have a significant impact on our balance sheet. The collaboration between Foreign Exchange, Rates and Credit (FRC) and Equity Derivatives resulted in the first multi issuer risk premia certificate in Germany. Furthermore, throughout the course of 2016, the solution team has successfully completed a few significant structured finance transactions.
Revenues in the area of IB fell in the year 2016, negatively affecting the cost-income ratio despite the downsizing of costs.

In Mergers & Acquisitions (M&A), UBS in Germany was involved in a number of high profile transactions in 2016, such as being the defense advisor to Deutsche Wohnen AG in relation to the unsuccessful EUR 10bn unsolicited public exchange offer made by Vonovia SE. On the Equity Capital Markets (ECM) side, UBS was involved as joint bookrunner in the IPO of Innogy SE, the largest German IPO since Deutsche Post AG in November 2000. In Debt Capital Markets (DCM), UBS was involved as joint bookrunner in the placement of a corporate bond for Commerzbank AG. Total volumes in M&A increased by 40.0 % to EUR 112 bn in the year 2016. Nonetheless the targets in terms of revenue could not be met completely.

In spite of the demanding market environment, the **Asset Management** division achieved a very good result in 2016. Over the course of the year, positive net inflows of EUR 0.5 bn were recorded across various asset classes with strong inflows by Wholesale Distribution (including ETFs) and Wealth Management Distribution. As of the end of 2016, assets in excess of EUR 17 bn were managed for institutional investors and in the retail fund business in the Asset Management division in Germany.
As predicted by the forecast, managed assets grew moderately.

Rating

UBS Europe SE was not rated on a stand-alone basis as the parent company UBS AG is rated by the three major rating agencies.

Financial position

The financial position of UBS Europe SE for the year 2016 cannot be directly compared to the previous year as the financial statements for 2016 included the assets and liabilities of all foreign branches of UBS Europe SE. Prior year figures relate to UBS Deutschland AG only.

Net assets

The bank's net assets are in order.

The balance sheet total increased to EUR 29.04 bn for the current year (prior year UBS Deutschland AG: EUR 6.05 bn) as a result of the aggregation of all branches' assets and liabilities and the centralization of the liquidity management. It is also partly based on the increase in surplus of EUR 3.1 bn derived from the Euro-Clearing of UBS AG which remains on the account of UBS Europe SE held at Deutsche Bundesbank.

Key items were receivables from credit institutions (57 % of total assets), customer receivables (18 %) and reserves with central banks (14 %). Further items affecting net assets are described below.

Cash reserve

As of the balance sheet date 2016, the credit balance with central banks was EUR 4.1 bn, thereof 3.9 bn with Deutsche Bundesbank. This represents an increase of EUR 3.1 bn with regard to the cash reserve as of 31st of December 2015 for the former UBS Deutschland AG.

Receivables from credit institutions and customers

Total receivables increased by EUR 17.4 bn compared to the prior-year value for UBS Deutschland AG.

	31/12/2016	31/12/2015	Change	
	m. EUR	m. EUR	m. EUR	%
Receivables from credit institutions	16,595	3,229	13,366	413.9%
Receivables from customers	5,207	1,196	4,011	335.4%
Total receivables	**21,802**	**4,425**	**17,377**	**392.7%**

Liabilities to credit institutions and customers

Total liabilities increased by EUR 21.5 bn compared to the prior-year value for UBS Deutschland AG.

Liabilities due from credit institutions and customers rose according to the overall increase of liabilities. Due to the decrease in issue volumes and various maturing certificates, the bank´s securitized liabilities fell by EUR 672 m to EUR 5 m.

	31/12/2016	31/12/2015	Change	
	m. EUR	m. EUR	m. EUR	%
Liabilities to credit institutions	10,916	1,750	9,166	523.8%
Liabilities to customers	15,727	2,696	13,031	483.3%
Securitized liabilities	5	677	-672	-99.3%
Total liabilities	**26,648**	**5,123**	**21,525**	**420.2%**

Receivables and liabilities according to geographical source

in m. EUR 31/12/2016	Total	Austria	Denmark	Germany	Italy	Luxembourg	Netherlands	Spain	Sweden
Receivables from credit institutions	**16,595**	29	1	13,214	61	3,261	1	28	-
Receivables from customers	**5,207**	254	-	1,212	1,882	932	2	925	-
Liabilities to credit institutions	**10,916**	-	-	7,488	1,813	680	-	935	-
Liabilities to customers	**15,727**	355	-	3,774	3,819	6,747	4	1,028	-

Securities

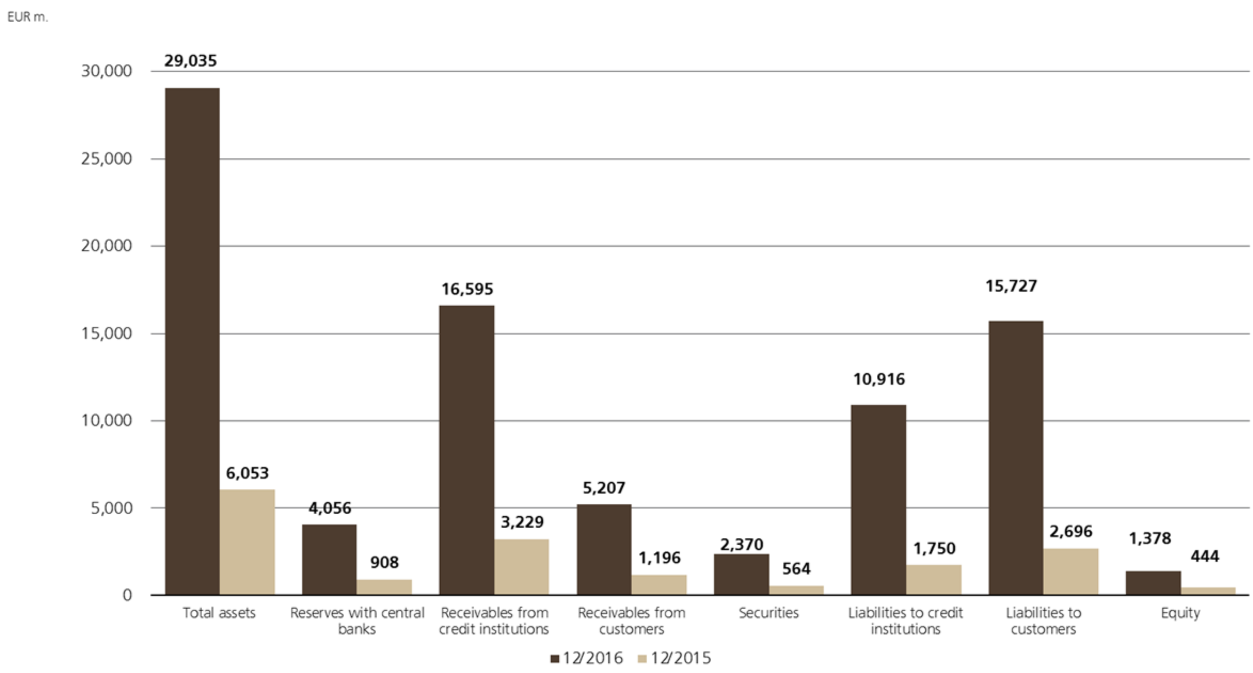
Following the merger, a Local Liquidity Portfolio (LLP) was established on UBS Europe SE level, while all branches sold their locally held securities. The LLP is a diversified pool of high-quality assets which is available as a first-line liquidity shock absorber. Consequently, securities increased by EUR 1.8 bn to EUR 2.4 bn.

	31/12/2016	31/12/2015	Change	
	m. EUR	m. EUR	m. EUR	%
Money market instruments, bonds and debt securities from public issuers	1,250	205	1,045	509.8%
Money market instruments, bonds and debt securities from other issuers	1,115	0	1,115	-
Debt and other fixed-income securities	**2,365**	**205**	**2,160**	**1053.7%**
Shares and other variable-yield securities	**5**	**359**	**-354**	**-98.6%**
Total securities	**2,370**	**564**	**1,806**	**320.2%**

Equity

The bank's subscribed capital amounted to EUR 176.001.000 and is divided into 35.200.200 bearer shares. The capital and profit reserves totaled EUR 986.4 m and EUR 46.4 m, respectively.
The Common Equity Tier 1 (CET 1) ratio according to Article 92 CRR was 16.77 %.

Summary of key balance sheet items



Valuation of interest rate transactions in the Banking Book at net realizable value

There was no net obligation as of 31st of December 2016. Therefore provisions were not recognized.

Results of operations

The values for the year 2016 are not directly comparable to those of the previous year as they included the results of all foreign branches of UBS Europe SE – and the result of the former UBS (Luxembourg) S.A. including its branches for December 2016 – rather than UBS Deutschland AG only. The former UBS (Luxembourg) S.A. recorded a profit of 41.8 m for the period from 1st of January until 30th of November, which has been transferred to the capital reserves of UBS Europe SE. From an economic point of view, considering the result of the former UBS (Luxembourg) S.A. for the complete year 2016, the bank's net loss of EUR 48.1 m would be reduced to EUR 6.3 m.

Net interest income totaled approximately EUR 38 m, burdened by net negative interest amounting to EUR 6.8 m. Net commission income amounted to EUR 360 m.

Regarding the cost side, the most significant items were personnel expenses with EUR 268.1 m including restructuring costs. Other administrative expenses amount to EUR 179.8 m. Of the other administrative expense, 36 % represent intra group charges, particularly for IT and management services.

The result of UBS Europe SE also includes the result of the German Investment Bank division. The latter recorded a sales decline which can be attributed to a reduced trading volume in the market as well as the reduced engagement in the area of Corporate Client Solutions.

In 2016 the bank has defined and implemented measures aimed at increasing revenue and scale down costs. Growth measures focus on hiring additional client advisors as a means of customer

acquisition and investments in digitalization. On the cost side, the Bank is working to foster efficiency to recuperate the economic result. For instance, the German location realized a personnel cost cutting program. The economic result for UBS Europe SE would have been significantly more positive without these costs related to restructuring.
Our performance for the year 2016 in terms of revenue therefore corresponds to our expectations.

Liquidity

UBS Europe SE was solvent at all times during the fiscal year. The liquidity principle stipulated by BaFin ["Bundesanstalt für Finanzdienstleistungsaufsicht": German Federal Financial Supervisory Authority] in accordance with Article 11 KWG was complied with at all times. The minimum ratio required by the supervisory authority is 1.00. As of 31st of December 2016, it amounted to 1.92 for UBS Europe SE (prior year UBS Deutschland AG: 1.23).
Since 1st of October 2015, the minimum requirements for the Liquidity Coverage Ratio (LCR) have to be fulfilled. During a phase-in period, the minimum ratio will increase stepwise from 70 % to 100 % until 2019. For 2016 the minimum requirement was set at 70 % according to the Delegated Regulation 2015/61 as of 10th of October 2014. As of 31st of December 2016, the LCR for UBS Europe SE amounted to 121.87 % (prior year UBS Deutschland AG: 237.4 %).

Investments

In June 2016 the Italian UBS branch acquired Santander's private banking unit in Italy (SPB Italia), taking over the asset portfolio under management. This created goodwill of EUR 21.5 m and other intangible assets of EUR 7 m, which are solely based on customer relations.

III. Opportunities and Risk Report

Key challenges in the European banking market continue to be the implementation of regulatory changes on an ongoing basis, the setting up of a cost-efficient organization to compensate for falling income and the recovery of customer confidence on a lasting basis. Through targeted investment in the area of digitalization among others we aim to generate further growth and increase our market share.

Implementation of regulatory requirements

The financial services industry is subject to continuing regulatory challenges. In this context the directive on markets for financial instruments and the corresponding regulation in the European Union (MiFID II / MiFIR) play a key role as such requirements are having a significant impact on our business. More precisely, their implementation and the ongoing fulfilment of additional requirements imply the commitment of resources which negatively affects our margins. In addition, the leverage ratio induced capital constraints reduce our net new money growth potential.

In recent years we have worked persistently and diligently to comply with regulatory requirements. Efficiently carrying out regulatory projects such as MiFID II has been a priority, as we believe that this allows us to strengthen our competitive advantage and represents the best interests of our stakeholders.

Efficiency considerations in the light of shrinking margins

The demanding earnings situation in the financial services industry remains a challenge for the bank. Apart from limited growth potential due to stricter regulatory provisions – particularly relating to equity capital and liquidity standards – net interest margins and earnings have also been negatively affected by the macroeconomic environment. This is marked by the continuingly low interest rate environment with its flat interest rate curve and restrained client activity.

It follows that a key challenge in the European banking market is to ensure a cost-effective line-up and the sustainable recovery of client confidence to compensate for declining revenues.

However, one promising opportunity that we see is the growing client demand for digital services as the introduction of increasingly advanced digital offers can not only intensify the client relationship, but also lead to efficiency savings through processes-automation and standardization.

Opportunities through technological innovations

While new technologies have already resulted in profound changes in various industries, the pressure on the financial services industry to adjust to the new digital reality continues to grow. The reason for this is in particular the rapidly changing needs of clients and the increasing demand for digital services as well as the emerging competition from non-Wealth Management players.

The WM business model is traditionally based on direct client interactions and has not seen the same level of digitalization as other financial services. But due to clients' increasing interest in approaching digital players with high technical and security standards and a normalization of digital interactions throughout the business environment, digitalization is swiftly becoming a clear opportunity in the WM business.

Additionally, developments in business process automation have increasingly shown to be financially viable and continue to become more and more approachable. By automating simple and repetitive business tasks, many business support functions can be made more efficient and reliable. As more sophisticated tools are developed, UBS will have to assess the opportunities of optimizing its existing processes from both an organizational and technological point of view.

IT Risks

The growing digitalization und interconnection comes along with the risks of new vulnerabilities and potential intruders accessing confidential information, sabotaging business and administrative processes or enriching themselves at the expense of others by other criminal means.

In 2016 a dedicated Location Cyber Threat Business Risk Assessment has analyzed, classified and presented the remaining risks and their proposed handling to the Management Board.
The digital vulnerabilities of our society will continue to suppose a challenge as there is no "one size fits all" solution for effective cyber-security. We aim to meet this challenge in the coming years by combining technology, processes and people skills in the right way. Further developing regulations such as "BAIT", "NIS Richtlinie" and "IT Sicherheitsgesetz" as well as safeguarding data security and integrity in the systematic assembling of data will represent the core of prudential regulation.

Market and competitive risks

Due to its multinational and multicultural nature the banking business in Europe is highly heterogeneous. Given this fragmentation of the market, regional players have emerged in the various European nations and became well established in the financial services market of their selected region. As one of the top brands in the business, the UBS branches face vigorous competition from well-established financial service providers on a national and regional level. Examples of such players include Deutsche Bank and Commerzbank in Germany, Nordea and Danske in Denmark or Intesa Sanpaolo and Unicredit in Italy. More recently, some Swiss banks such as Julius Bär and Pictet have been trying to establish themselves across Europe, further increasing competition.
While growth projections for the European banking sector are moderate and competition is high, UBS Europe SE is well positioned to differentiate itself from its competitors. As the only competitor in the market with a pan-European Wealth Management setup, UBS Europe SE can develop a sustainable competitive advantage by balancing the comprehensive local and global expertise of its various business units.

On European soil Germany is the most fiercely competed market for **Investment Bank** services. In addition to the presence of strong German banks, major foreign banks have been established in Germany for many years. However, some US banks among other major foreign banks have been partly withdrawing from Europe, shifting their focus towards growing markets such as Asia. Across all products and services, Deutsche Bank, Goldman Sachs and JP Morgan are the Investment Bank's main competition in Germany. Competitors in specific segments include Commerzbank, HSBC Trinkhaus, Morgan Stanley and Citigroup.

Our competitors in **Asset Management** mainly include major national asset managers such as Deutsche Asset Management, Allianz Global Investors, Deka Bank Asset Management and Union Investment, foreign asset managers such as BlackRock, Fidelity Investments, JP Morgan and Franklin Templeton as well as boutiques such as Flossbach von Storch.

Risk management and methods

UBS Europe SE uses a risk management and risk control approach that is both qualitative and quantitative in nature.

The concrete application of quantitative or qualitative measures is dependent on the nature of the respective risk and whether it is managed as part of the day to day business (operational level) or on a strategic level. While operational risk is limited qualitatively by policies and process descriptions, the bank's primary risks are mainly steered by quantitative operational limits.
The overall principles of risk management and risk control, including the limit setting on qualitative and quantitative level are defined within the Risk Appetite Framework of UBS Europe SE.
A more strategic quantitative view of the Bank's risk taking activities is provided by the Bank's ICAAP (Internal Capital Adequacy Assessment Process) concept. The ICAAP concept serves as a steering tool at UBS Europe SE entity level, taking on a one year forward looking perspective.
The concept defines the overall ICAAP methodology, outlines how the bank quantifies its material risks and how it proves that the material risks derived from risk taking activities are covered by available financials ("Risikotragfähigkeitsberechnung"). As a preferred management approach for the ICAAP, UBS Europe SE applies a "going concern" approach, including a baseline as well as a stress scenario. A "gone concern" view completes the overall ICAAP concept.
As a result of the establishment of UBS Europe SE, the ICAAP framework has been enhanced, especially with regard to the modelling of the different risk exposures. Since the fourth quarter of 2016 UBS Europe SE uses the so called "Combined Stress Test" (CST) and the underlying risk models developed by UBS AG. The CST applies a predefined macroeconomic stress scenario consistently to all material risk categories of the bank. In order to cater to the specific aspects of UBS Europe SE's risk profile as well, the CST is complemented by local analyses. By this it can be ensured that overall the UBS Europe SE ICAAP covers both macro-economic as well as idiosyncratic components and therefore is able to reflect the individual risk profile of UBS Europe SE comprehensively. The CST with all of its components is part of the comprehensive UBS Europe SE outsourcing framework.
Another significant enhancement of the risk management and control framework has been achieved in the Asset Liability Management (ALM). The newly introduced Treasury AML unit is dedicated to the proper management of the bank's balance sheet, including liquidity management in line with the agreed risk appetite. A dedicated Market and Treasury Risk Control unit supervises the activities of Treasury AML as an independent party and escalates to the Management Board if required.
The overall risk management and control framework will be subject to further modifications along the progressing risk profile of the bank in 2017. All changes and enhancements are considered within the Risk Appetite Framework keeping the risk exposures in line with internal as well as external limits.

Other major risks

Counterparty Default Risk

Customer lending business

Counterparty default risks are mainly associated with UBS Europe SE's lending business, which primarily consists of collateralized loans for Wealth Management customers. Key eligible collateral types for this business are marketable securities as well as first ranking mortgages over residential properties in Germany and Italy. The large cap corporate lending and trading activities of the Investment Bank division do not form part of the key credit activities of UBS Europe SE and remained dormant throughout the entire fiscal year. The trading business of the Investment Bank division still relates to transactions without counterparty default risk only, i.e. securities transactions are settled on a delivery against payment basis.

UBS Europe SE's credit business focused on the traditional securities-backed Lombard loan business in Wealth Management throughout the fiscal year 2016. In line with the credit risk strategy of UBS Europe SE, the collateralized Lombard loan business continued to be the credit activity designed to support relationships with private customers, private investment companies and, to a limited extent, with corporate clients. In addition, the bank continued to offer collateralized hedging facilities and short term redemption bridge facilities within the assets servicing business maintained in Luxembourg. This collateralized loan business relates to the custodian bank function of the bank for regulated funds and is offered as a supplementary offering to support the asset servicing / custody business of the bank. Real estate lending to wealth management clientele secured by first ranking mortgages mainly over eligible residential mortgages is only supported in Italy and Germany. The latter mortgage business in Germany is in the process of being phased out, i.e. no new business was taken on since 2014 with the incumbent loan book being repaid along legacy maturity profile. In Italy, the selective mortgage lending business of the bank was launched a few years ago only. Despite the Santander acquisition step up of the Italian mortgage book, the overall mortgage lending activity of UBS Europe SE including Germany and Italy represents less than 5 % of the overall loan book and is therefore not material from a credit risk standpoint.

Other than that, the bank maintains the restricted Corporate & Institutional Clients business in Germany only. This offering focuses on payment products, intra-day overdraft limits and direct debit limits for selected subsidiaries of Swiss Corporate Groups, in turn maintaining banking relationships with UBS Switzerland AG. This activity continued to remain immaterial from a credit risk and limit notional amount perspective (less than 0.2 % of the overall book).

In terms of volume split, the wealth management related collateralized Lombard lending business shows a balanced split across countries with the Italy branch embracing 32 %, Luxembourg branch 31 % (including Austrian and Nordic clientele), Germany 23 % (including the Latin America offshore business) and Spain branch 14 %.

During the fiscal year 2016, the bank's credit risk control function focused on the review of Lombard lending underwriting as well as monitoring practice across locations, among others to safeguard MaRisk compliance as well as proper reporting on credit risk aspects regarding the credit portfolio. Overall alignment activities benefited from common lending, collateral valuation and methodology principles maintained by UBS Group, which in turn result in key credit quality commonalities being in place across all UBS Europe SE locations. Also, no material risk concentrations, neither on credit relationship level nor on collateral level were identified. Having said that, no new material loan defaults were identified / reported in the context of UBS Europe SE collateralized loan business during the fiscal year 2016.

Loans to UBS AG Switzerland/UBS Group

Most of the receivables due from credit institutions arise from transactions with the parent company, UBS AG, Switzerland. The bank closely monitors this concentration risk and reports on it in its daily large exposure report. Monitoring activities include the review of financial information and related internal analyses regarding UBS AG as well as market information such as rating agency assessments and the status and development of credit default swap spreads compared to other banks. The bank also received collateral in the form of securities for the exposures to UBS AG, Switzerland, and concluded a netting agreement with UBS AG and UBS Switzerland AG, respectively, that reduces group exposure to a level below liable capital.

Market Risk

Market Risk is the risk of loss resulting from adverse movements in market variables such as interest rates, foreign exchange rates, equity prices, credit spreads and commodity prices.
Investment Risk, as the consequential risk of operational risk (especially suitability risk) for UBS Europe SE, is a sub-category of market risk. It occurs if the bank has to take shares onto the own book due to operational errors or litigations.

UBS Europe SE does not engage in proprietary trading book activities. Non-trading (Banking Book) market risk arises largely from client deposits and lending products in our Wealth Management business. Interest rate risk related to non-maturing client deposits is modelled by means of replication portfolios. Treasury ALM is authorized to run market risk arising from the interest rate duration mismatch inherent in Wealth Management´s balance sheet. Treasury ALM also manages a local liquidity portfolio, which is maintained to fulfil the entity's regulatory liquidity requirements and to invest excess cash. It contains high quality liquid assets (government, supranational, government agency issuers rated AA or better).

Foreign exchange risk arises from client transactions which are hedged with UBS Group entities and foreign currency profit and loss converted to Euro on a regular basis.

Market risk is monitored by Market and Treasury Risk Control using standard risk metrics (such as value at risk).

Liquidity Risk

Liquidity risk is the risk that the institution is not able to fund increases in assets and meet obligations as they come due, without incurring unacceptable losses.
Our liquidity risk management aims to maintain a sound liquidity position to meet all of our liabilities when due and to provide adequate time and financial flexibility to respond to a firm specific liquidity crisis in a generally stressed market environment, without incurring unacceptable losses or risking

sustained damage to our various businesses. The Liquidity and Funding Framework & Management Policy of UBS Europe SE defines the processes, roles and responsibilities that ensure that UBS Europe SE’s exposure to liquidity risk is monitored, efficiently structured and managed in accordance with regulatory requirements and the risk appetite set by the UBS Europe SE Management Board.

Operational Risk

Operational risk arises naturally from all areas of UBS Europe SE’s activities, and is defined as the risk resulting from inadequate or failed internal processes, people and systems, or from external causes (deliberate, accidental or natural) which have an impact (either financial or non-financial) on UBS, its clients or the markets in which it operates. Operational risk may result in direct financial losses or indirect losses in the form of revenue forgone as a result of business suspension. It may also result in damages to our reputation and to our franchise, implying longer term financial consequences.

Conduct risk is a subset of operational risk. The group-wide definition of conduct risk is “The risk that the conduct of the firm or its individuals unfairly impacts clients or counterparties undermines the integrity of the financial system or impairs effective competition to the detriment of consumers”. Together, these definitions provide a complete view of the impact of operational risks, issues and failures both internally and externally.

UBS Europe SE’s operational risk exposure is systematically monitored, assessed and reported by the Compliance and Operational Risk Control departments. The monitoring and assessment of operational risk processes are based on a holistic control framework of quantitative and qualitative risk indicators, and on the approved risk appetite. Monitoring, assessment and reporting are managed on enterprise level, considering the aggregated UBS Europe SE network of branches and subsidiaries, and acting on individual entity level if required. UBS Europe SE’s governance bodies are fully updated on the operational risk exposure in accordance with the approved UBS Europe SE Risk Governance structure.

In 2016, the majority of the operational risk's events nature was aligned with UBS Europe SE's key activities as Wealth Management services provider and the most relevant registered amount related to operational risk financial events was allocated to financial provisions.
To ensure operational continuity in case of system failure, emergency plans for each of the business centers are in place. Furthermore these centers are technologically independent.
The pre-existing Recovery Plan has been upgraded to serve the needs of the newly created UBS Europe SE in the supervision of potential recovery situations and their respective escalation process. These elements are integrated into the existing risk management and control system, the corresponding monitoring of recovery indicators and their utilization are an integral part of the monthly risk reporting. The plan is subject to further merger-induced enhancements and will be provided to regulators upon request in 2017.

Outsourcing Risk

Outsourcing risk as the aggregate outsourcing risk of branches' and subsidiaries' exposures is managed, assessed and controlled primarily at enterprise level and complementary acting on individual basis if required.

The intragroup outsourcing risk is subject to ongoing evaluation in accordance with the Circular 10/2012 Minimum Requirements for Risk Management (MaRisk). The results of this evaluation process are being managed to ensure full compliance with MaRisk requirements. Final results are expected by the second half of 2017.

UBS Europe SE's operational strategy is designed to leverage the group's strengths to gain on efficiency and scalability. This strategy will gradually increase the intragroup outsourcing framework and the contract structure standardization across the entire UBS Europe SE network.

The external outsourcing framework and risk are equally subject to ongoing evaluation in light of the MaRisk requirements. In general terms, UBS Europe SE's outsourcing framework management model is the successor of the former UBS Deutschland AG's model. The latter used to be audited by the German Federal Financial Supervisory Authority (BaFin) and by the Deutsche Bundesbank in previous years.

For the efficient outsourcing management UBS Europe SE has set up teams and governance (1st and 2nd line) to ensure early and effective implementation of any new regulatory requirements. Additionally all staff of UBS Europe SE responsible for contracting were trained to fulfill MaRisk requirements in their daily business. The major part of the Corporate Center services will be provided by the newly established UBS Business Solutions AG in the future, a one hundred percent subsidiary of UBS AG. The contractual framework of the agreed services of the UBS Business Solutions AG fully complies with the MaRisk removal requirements.

Reputational Risks

In the following only the material reputational risks will be outlined.

With regards to Italy, the following substantial developments can have a reputational impact:

In June 2016 UBS (Italia) S.p.A. acquired Santander Private Banking business in Italy. Strong efforts have been put in place for the integration of the Santander business in terms of operational aspects. UBS SE Italy branch is still working on the integration through constant monitoring activity by local management and dedicated working groups.

Concentration of issues in the division of Financial Intermediaries (FIM) drove UBS (Italia) S.p.A to the decision to carry out specific risk mitigation plans over I) customer onboarding, II) order processing and III) payment process.

From the beginning of 2016 as of the end of November the Bank has received 137 client complaints in its Italy branch. The significant growth in the number of complaints compared to 2015 is due to the acquisition of the Santander business in Italy which most of these (99 out of 137) are related to.

From 1st of December as of today the bank received 17 complaints, eleven of which are linked to the Santander acquisition.
Overall, 30 complaints have been filed during the fiscal year 2016 in Luxembourg, which fall in various categories with currently no concentration on a topic and therefore no indication of a systematic failure of a process.
Likewise, there was no concentration of issues and therefore no indication of systematic failure in UBS branches in Germany, Austria, Sweden and Denmark.
UBS Europe SE, Spain Branch, S.A. is expecting a fine from the local market regulator related to the distribution of certain Mutual Funds Classes which allegedly had not been suitable due to higher fees. The entity has provisioned EUR 650.000 to cover for this risk.

Litigation

In the following only the material litigation cases will be outlined.
A significant proportion of the value in dispute for UBS Europe SE, as legal successor of UBS (Luxembourg) S.A. and UBS Deutschland AG is attributable to the consequences of the Madoff investment fraud. As a result of the fraud, two third-party funds established under Luxembourg law, substantially all the assets invested via by Bernard L Madoff Investment Securities LLC ("BMIS"), as well as certain funds established in offshore jurisdictions, directly or indirectly affected by the Madoff fraud, face severe losses. Both of the Luxembourg funds are in liquidation. The documentation establishing these funds identified UBS entities in various roles including custodian, administrator, manager, distributor and promoter and indicates that UBS employees served as board members. UBS Europe SE (as successor of UBS (Luxembourg) S.A.) is involved in various claims in different jurisdictions brought by investors in funds affected by the Madoff fraud, as well as claims by the liquidators of the two Luxembourg funds and the Trustee for the liquidation of BMIS. The majority of these claims are pending in Luxembourg. UBS Europe SE, its Luxembourg branch and certain other UBS subsidiaries are also responding to inquiries by Luxembourg investigating authorities without, however, being named as parties in those investigations. UBS Europe SE (as successor to UBS Deutschland AG) is involved in a small number of claims brought by certain clients who invested through third-party funds and funds administered by UBS entities in Germany that were affected by the Madoff fraud. UBS Europe SE also faces two claims brought against it as the legal successor of Dresdner Bank Lateinamerika AG; one brought by the liquidators of an offshore fund and the other, by the Trustee. UBS Europe SE continues to defend itself vigorously in all pending claims, as the bank firmly believes that it has done nothing that provides any basis for claims with respect to losses caused by the Madoff fraud.
UBS Europe SE is indemnified by UBS AG up to a contractually defined maximum amount for Madoff-related liabilities that might arise as a result of having become the successor to UBS (Luxembourg) S.A.
With the indemnity agreement in place UBS Europe SE has transferred the original litigation risk to a counterparty risk towards UBS AG, which as a consequence increases the concentration risk towards UBS group. In order to appropriately monitor the enhanced concentration an "collateral posting

process” has been implemented in addition to the already existing monitoring processes. According to the collateral posting process UBS AG needs to provide additional collateral in case its long term credit rating falls below a pre-defined threshold. The specific litigation risk is furthermore monitored by the Legal department on a permanent basis.

Apart from those cases related to the Madoff investment fraud, UBS Europe SE was involved in a high double digit number of litigation cases with a total alleged amount of approximately EUR 125 m. UBS Europe SE has established provisions in a lower double-digit million amount for these cases. The most significant cases within this category are described hereinafter:

Nearly half of the amount in dispute in Germany, relates to cases in which customers in the Latin America segment primarily claim damages resulting from option trades. One of these customers is suing for payment of an amount above EUR 60 m. This customer's claim was dismissed in first instance and is now under appeal.

In a credit-related case in Luxembourg the plaintiff claims damages in a low double-digit million amount alleging in particular lack of suitability. This customer's claim was dismissed in first instance. Following an appeal, the case has been referred back to the first instance (with a change in the court's composition).

The majority of the cases in Spain are related to products MiFID classified as "complex" (basically structured products) and is based on suitability topics (previous experience and knowledge, lack of information). Some cases are also related to families' disputes and Lombard agreements.

In a credit-related Spanish case, in which plaintiff claims damages amounting to a high single-digit million amount, the customer's claim was dismissed in first instance and is now under appeal.

In Germany, cases in a single-digit million amount are still pending, relating to a business line, which has been closed in 2011 (Sauerborn). The claims mainly allege the non-disclosure of certain information and claim compensation for losses incurred in the 2008 financial crisis.

Legal proceedings related to closed end funds make up the largest amount in number of cases in Germany. In more than 20 cases clients mainly allege that certain information was not disclosed. The total value in dispute at the end of 2016 for these cases amounts to approximately EUR 5 m.

In 2016 a client in Italy filed a claim amounting to a single-digit million amount, claiming for damages and losses coming from a contractual and extra-contractual liability and alleging the infringement of contractual obligations by UBS Italy in the execution of certain bank transfers.

In a case related to the former branch of UBS (Luxembourg) S.A. in Belgium the plaintiff claims damages amounting to a single-digit million amount. The claim is based on suitability concerns by the client. This customer's claim was dismissed in first instance and is now under appeal.

In a case related to the revocation of a line of credit a customer in Italy claims a single-digit million amount. This customer's claim was dismissed in first instance and is now under appeal.

In another low single-digit million case in Spain regarding a structured product, the court of appeal dismissed the claim by the plaintiff, who now appealed to the Spanish Supreme Court.

The bank will continue to be subject to litigation risks in the future.

Internal and external Investigations

In Germany the ongoing investigations by the public prosecutor’s office in Mannheim continue to represent a potential reputational risk for the bank. During the reporting period the bank did not become aware of any suspicions relating to staff at UBS Deutschland AG, the legal predecessor of UBS Europe SE.

In Belgium, UBS has been notified by the Belgian investigating judge that it is under formal investigation (“inculpé”) regarding the laundering of proceeds of tax fraud and of banking, financial solicitation by unauthorized persons and serious tax fraud. The case stems from the former Belgian branch of UBS (Luxembourg) S.A. and was closed in December 2015.

A special audit in Germany was instructed by the Bundesanstalt für Finanzdienstleistungsaufsicht (BaFin) in follow up of Project CETUS. The subject of the audit in particular referred to outsourcing compliance regarding the CETUS platform. BaFin/ Bundesbank issued findings in the areas of business strategy, outsourcing framework, provider management and test framework regarding certain remaining local applications. Remediation is scheduled for June 2017.

BaFin further ordered a special audit in Germany on the participation of the former UBS Deutschland AG Investment Banking division in the bidding auction at Finanzagentur GmbH. The scope of the audit was to assess compliance of the business organization with the requirements of Article 25a (1) KWG. The onsite audit is closed and discussions for clarification of facts have taken place. The audit report with finding ratings was submitted in the first quarter of 2017.

The transfer of the reviewed auction process to UBS Limited as of January 2017 has taken place and was communicated to BaFin.

After a “not effective” rating of an Internal Audit report on the WM suitability framework in 2015, a task force was established to track remediation actions. In 2016 an Internal Audit follow-up audit was rated “effective”. Also, the Audit of the securities services business in 2016 shows significant progress compared to last year report.

On 7th of December 2016 BaFin announced to perform a special audit relating to AML and KnowYourCustomer (KYC) processes, focusing on the specifications the bank has made in the context of the "Panama Papers" market survey. The review will be performed in the format of a special audit pursuant to Article 44 of the Banking Act, which is expected to start in the course of 2017. In Luxembourg, the Commission de Surveillance du Secteur Financier undertook a review on offshore accounts further to the publication of the “Panama Papers”.

A Bank of Italy AntiMoneyLaundering (AML) inspection over the evaluation of suspicious transactions carried out by UBS (Italia) S.p.A. started in May 2016 (audit closed in October 2016).

Bank of Italy started an on-site inspection over transparency law and client complaints management on 14th November 2016. The inspection is still in course.

Risk Mitigation

Legal risks are curtailed at various stages of work processes by measures put in place by Legal and Compliance among other departments. Main preventive measures include the operational framework as well as the involvement of Legal in the drafting of standard forms and contracts. Non-standardized contracts and/or disclaimers require review and sign-off by the Legal department. Outside legal counsel may only be retained by the Legal department or a unit authorized by the Legal department. During the processing of legal proceedings, the bank regularly reviews whether a provision needs to be recognized or adjusted for specific events. Legal reports on significant developments in existing and new litigation cases are reported to the Risk and Capital Committee of UBS Europe SE on a monthly basis.

Overall, no material legal risks in connection with the abovementioned legal matters beyond the individual case level were identified for the bank in the reporting period. In individual cases the Legal department and the Compliance department have provided information and specific recommendations on how to lower the risk with regard to operational processes, documentation or product design based on experience gained from processing complaints, actions filed and other events.

Risk Position

The bank's own funds pursuant to Article 72 CRR amounted to EUR 1,314 m (prior year UBS Deutschland AG: 437 m), which corresponds to an overall ratio of 16.77 % (prior year UBS Deutschland AG: 23.67 %).. The capital requirements according to Regulation (EU) No 575/2013 (Capital Requirements Regulation – CRR) have been fulfilled at all times during the fiscal year.

The bank's risk-weighted assets as of the balance sheet date break down as follows:

Risk-weighted assets in EUR m	31st of December 2016
Credit risk	6,400
Market risk	51
Operational risk	1,239
Credit value adjustments	149
Total risk-weighted assets	7,839

Summarizing presentation of the risk position

UBS Europe SE carries out a risk inventory on a yearly basis and calculates an overall bank risk profile on the basis of this risk inventory. Based on the business activities of UBS Europe SE the operational as well as the business/earnings risks are the most significant risks at the overall bank level.

Within the scope of the risk-bearing capacity concept, risk potentials for business/ income, operational, counterparty default and market price risks including the relevant sub-categories, are determined quarterly. The identified risk potentials are compared with the risk cover potential available on the respective reporting date.

In conceptual terms, a Going Concern approach has been defined as a preferred management approach. This is divided into a basic scenario and a stress scenario, whereof the basis scenario was defined as primary control-relevant. In addition, the bank determines a Gone Concern perspective on the risk-bearing capacity, which is intended to comply with the creditor protection in particular. The consideration of liquidity risks in terms of insolvency risk within the risk-bearing capacity concept is omitted since this risk can not be reasonably covered with equity. Depending on the further development of the business model, in particular the expansion of the treasury ALM activities, the bank is already pointing out that it intends to take account of refinancing risks within the risk-bearing capacity concept. In addition, pension risk have also been included as of 31st of March 2017.

The overview below shows the utilization of the individual scenarios for the risk-bearing capacity calculation as of 31st of December 2016:

31/12/2016 in m. EUR	**Capital limits**	**Capital use – Going Concern Basis-scenario**	**Capital use – Going Concern stress scenario**	**Capital use - Gone Concern scenario**
Total capital	-	1355	1355	1355
(./.) capital requirements according to CRR (pillar I)	-	862	862	-
Ytd P&L (HGB)		-41	-41	-41
planned P&L (HGB)	-	59	59	-
(./.) hidden losses (HGB)	-	-	-	8
Risk cover potential for covering of pillar II risks	-	**511**	**511**	**1306**
Business-/ Income Risk	150	37	134	153
Operational Risk	100	42	66	88
Counterparty Default Risk	40	6	6	11
Market Risk	40	7	13	13
Total	**330**	**92**	**219**	**266**
Risk-free capital	**-**	**419**	**292**	**1040**

IV. Forecast Report

UBS Europe SE has its core business in Wealth Management and is set up as a pan-European Wealth Manager, with supporting business divisions providing other services on a regional level.

We aim to expand all of our business activities in Europe, being the UBS home market, over the long term and to be one of the market leaders and the first choice among our target clients. We aspire to further develop our market position and to safeguard and improve our reputation. To achieve that, we have defined a clear strategy for active customer acquisition. By supporting and developing the cooperation between different markets, segments and divisions we want to ensure that our clients have access to the entire set of capabilities and skills our company has to offer. The key challenges to achieve this are notably the continuous implementation of new regulatory requirements, a cost-efficient positioning to compensate for falling income and a sustainable approach to rebuild customer confidence across all divisions and markets.

The European **Wealth Management** market is undergoing fundamental structural changes with significant implications for the bank (e.g. customer protection, MiFID II, regulatory requirements, technological change), leading us to the decision to consolidate and optimize our entity structure. This will allow us to deliver an "onshore" experience to our WM clients, combined with easy market access for all businesses across the European Economic Area (EEA).
After the North American Region, Europe, with an estimated market size of EUR 5,600 bn in our targeted markets and client segments, is the second most important market for our global Wealth Management business. With private wealth across Western Europe expected to grow by approximately 4 % p.a. until 2019, we expect to outperform the market with regard to the increase in earnings by capturing additional market share in the coming year. The main driver of this growth will be the segment of the extremely wealthy Ultra High Net Worth (UHNW) clients with assets of over EUR 30 m. Based on these forecasts, the bank expects to expand its assets under management, especially in this segment, strengthen its client-specific return on assets and improve its cost-income ratio through increased revenues in the year 2016 and ongoing cost discipline. Furthermore we see additional potential for growth due to an increasing willingness of clients to switch to new service providers, the growing tendency to have accounts with multiple banks and UBS Europe SE's ability to transcend borders and cater to our clients' cosmopolitan lifestyle.
By hiring additional customer advisors, we expect to improve the ratio of front and support staff.

The **Investment Bank** division is positioning itself on the basis of expert consulting services, innovative solutions, excellent execution and extensive access to the global capital markets.
As the regulatory reforms and the structural transformation of the market of Investment Banking are continuing, just like other market players, UBS is focusing on its core activities and abandoning products and services that are deemed overly complex, don't generate stable risk-adjusted returns, or are accompanied with an intensive strain on either risk-weighted assets or capital.
By intensifying our relationships with all relevant online brokers, in particular, we plan to further expand our market share in public distribution business, and by this strengthen our revenue base.

The outlook for the German equity market is more positive for 2017 than it was in the prior year with volatility indices being near to all-time lows and other markets reaching record highs. This has naturally benefited ECM markets across Europe with increased primary issuance volumes compared to 2016. In this environment investors continue to welcome the liquidity events that the ECM market can provide creating a positive backdrop against which issuers and vendors can come to market.

. We expect our Mergers and Acquisitions business to generate an improved result in the next year and gain in importance for private and public acquisitions in Germany.

Within UBS Europe SE the **Asset Management** division specializes in offering services to institutional investors, distribution of investment funds through various financial service providers and support for Wealth Management in distributing UBS investment funds or investment management expertise.
With approximately EUR 17 bn under management at the end of 2016, the Asset Management division is well positioned to further strengthen its position as one of the leading international asset managers in Germany. The continuing trend towards passive funds (e.g. the so called Exchange Traded Funds or ETFs) and Alternative Investment gives the UBS Asset Management division a unique opportunity to further focus on these core products, in which we have already developed highly competitive advantages throughout recent years. Despite increasing regulatory requirements, moderate but continuous growth with the aforementioned products and an increase in the assets under management is expected for the global asset management business in 2017.

From a division overarching perspective, we have initiated several projects that will bring the balance sheet closer to our target structure after the successful setup of the entity. Among others, we will implement approaches leading to a better reflection of our risks in terms of RWA. Subject to the successful delivery of these initiatives~~,~~ and under the careful consideration of relevant business developments and market circumstances, adjustments to UBS Europe SE's capital structure, including a possible material capital reduction may follow. In anticipation of such a measure, a resolution by the general meeting to increase share capital by EUR 400 m via a transfer of the corresponding amount from capital reserve referred to in Article 272 (2) No 1 of German Commercial Code is due. Prerequisite for any such change will be for UBS Europe SE to maintain its strong capital position, well above existing regulatory requirements.

Dependency Report according to Article 312 AktG (3) sentence 3

The Management Board of UBS Europe SE has provided a report on the relations with affiliated companies for the year 2016 which ends with the following declaration:
"For all known legal relationships with the obligation to be reported in the Dependency Report according to § 312 with related parties and affiliated entities, UBS Europe SE received appropriate compensation in return. The company has not been prejudiced by any act or omission".

Frankfurt/Main, 16 May 2017

UBS Europe SE
- The Management Board –

Thomas Rodermann	Birgit Dietl-Benzin	Fabio Innocenzi
René Mottas	Dr. Andreas Przewloka	Stefan M. Winter