1998 Annual Report UnionBanCal Corporation

Our mission is to enhance shareholder value by establishing UnionBanCal Corporation as the premier financial services company headquartered on the West Coast. We will achieve this mission by providing quality products and personalized services that satisfy the needs of our customers.

Serving targeted market segments on the West Coast, throughout the U.S. and in selected international markets, particularly the Pacific Rim, we will create value through high-quality, responsive service and a combination of active relationship management and internal collaboration, which will enable us to respond to customer needs quickly.

We will maintain a clear focus on asset quality and risk management. We will extend and strengthen our support to the communities we serve. We will provide opportunity for professional and financial growth for our employees, by nurturing a collaborative culture that rewards teamwork and performance.

San Francisco-based UnionBanCal Corporation is a bank holding company. Its primary subsidiary is Union Bank of California, N.A., the third-largest commercial bank in California, based on total assets and total deposits in California, and one of the 30 largest commercial banks in the country.

We provide a comprehensive array of personal and commercial financial products and services to individuals, businesses and government agencies, and are differentiated from our competitors by providing personalized, high-quality and responsive service.

At year-end 1998, we had 250 full-service domestic branches, including 49 in-store branches. Additionally, we had another 41 limited service branches; 15 Cash & Save facilities; 15 Private Bank offices and 18 overseas offices.

Common stock of UnionBanCal Corporation is traded on the Nasdaq National Market under the symbol UNBC. Capital securities were issued in February 1999, and are listed on the New York Stock Exchange under the symbol UBT.

Community Banking

Commercial Financial Services

International Banking

Trust & Private Financial Services

Pacific Rim Corporate

Global Markets

Systems Technology and Item Processing

Operations and Services

Selected Financial Highlights

(In thousands, except per share data)

For the Year Ended:	1997	**1998**
Net income	$ 411,296	$ 466,461
Net income applicable to common stock	403,696	466,461
Net income per common share — basic	2.31	2.66
Net income per common share — diluted	2.30	2.65
Dividends per common share	0.51	0.61
Weighted average common shares outstanding — basic	174,683	175,127
Weighted average common shares outstanding — diluted	175,189	175,737
Return on average assets	1.39%	1.53%
Return on average common equity	16.05%	16.39%
Net interest margin[1]	4.70%	4.81%
Efficiency ratio	61.53%	61.31%
At Year End:		
Total loans (gross)	$22,741,408	$24,296,111
Allowance for credit losses	451,692	459,328
Total assets	30,585,265	32,276,316
Total deposits	23,296,374	24,507,879
Shareholders' equity	2,679,299	3,058,244
Book value per common share	15.32	17.45
Risk-based capital ratios		
Tier 1	8.96%	9.64%
Total	11.05%	11.61%
Tangible common equity to assets	8.54%	9.30%
Nonperforming assets to total assets	0.42%	0.28%

[1] Taxable equivalent

To our Shareholders, Customers and Staff

The year 1998 was a watershed year for UnionBanCal Corporation, with a performance record that earned a place on the FORBES Magazine "Platinum List" of the country's top 20 banks.

Net income for 1998 was $466.5 million, 13 percent more than 1997's $411.3 million. Net income per diluted share for 1998 was $2.65, up from $2.30 the year earlier.

Return on average assets rose to 1.53 percent in 1998 from 1.39 percent in 1997. The 1998 return on average common equity was 16.39 percent, compared with 16.05 percent for the previous year.

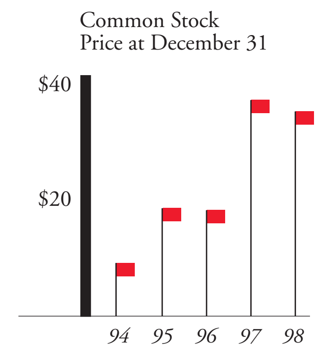
The continued decline of nonperforming assets as a percent of total assets, from an already stellar 0.42 percent at year-end 1997 to 0.28 percent at the close of 1998, demonstrates our commitment to place asset quality above quantity, a philosophy that will serve us well in a less robust economy.

We still have room for improvement; for example, our 1998 efficiency ratio — 61.31 percent — is not acceptable. We are attacking this issue through *Mission Excel,* an intensive, company-wide initiative to increase revenue, improve our business mix, simplify and streamline our processes, reduce or redeploy expenses, and leverage our competitive advantages.

In 1998, a time of dramatic industry consolidation, our strategy was to refine our line of products and services, expanding in high-opportunity areas in which we have industry expertise and in-depth knowledge of the market, and adding value for our customers through outstanding ideas, effort and service.

Our acquisition of DCI Corporation, which provides software for bankruptcy trustees, for example, was a small but strategically important step in serving the banking needs of a narrow but significant market. To provide more flexibility in meeting the needs of customers and to increase the visibility of our highly successful mutual funds, we converted our investment-management operation

The UnionBanCal Corporation Executive Management Team, from left: Kaoru Hayama, Chairman of the Board; Robert M. Walker, Vice Chairman of the Board; Takahiro Moriguchi, President and Chief Executive Officer; Richard C. Hartnack, Vice Chairman of the Board; and Yoshihiko Someya, Deputy Chairman of the Board.



into a separate subsidiary — HighMark Capital Management, Inc. Conversely, we withdrew from the credit card issuance business, in order to redirect assets into more strategic endeavors with potential for greater returns. Abroad, we became sub-advisors on U.S. equities for pensions managed in Japan by Tokyo-Mitsubishi Asset Management.

In 1998, we continued to expand our distribution channels, most notably through the Internet. Through our expanded website (www.uboc.com), we offer personal banking, information services for commercial clients, cash management services, trust and investment services and a wide range of information about Union Bank of California. While maintaining traditional service through an expanding branch system and telephone-supported banking, we plan more website-based service offerings in the near future.

Our share of household banking accounts grew at a rate of nearly five percent. We experienced double-digit growth in small-business relationships. Our service to government agencies expanded. We increased our influence in commercial and investment banking to certain specialty industries, moving beyond bank debt by further establishing ourselves as a resource for complex leasing and private capital products. Union Bank of California also became a greater force for such services as cash vault, cash management and item processing. Despite economic turmoil in Asia, we maintained profitability in our international operations. Our Global Markets Group, organized during 1998, strengthened foreign exchange and other market-product capabilities to service the bank's customers across the board, while providing a consolidated structure for managing bank-wide market, interest rate and liquidity risks.

Going forward, we will continue to look for ways to enhance the value of our franchise. Part of our challenge is to increase fee-based revenue, particularly from our Trust and Private Financial Services and International Banking businesses. We also see opportunities to leverage our relationship with The Bank of Tokyo-Mitsubishi to gain access to the Japanese market for asset-management services.

The year was also notable for several initiatives to enhance shareholder value. In December, we split our stock three for one and increased our dividend by 36 percent. In March 1999, we repurchased more than $311 million of common stock in our holding company, financed by a highly successful issuance of capital securities, which trade on the New York Stock Exchange (NYSE: UBT).

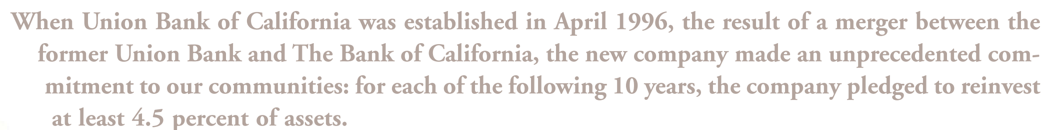
Our majority shareholder, The Bank of Tokyo-Mitsubishi, Ltd., supported our capital-management effort through a secondary offering of 28.75 million shares of UnionBanCal Corporation stock in February 1999, reducing its stake in UnionBanCal Corporation to 64.1 percent from 81.5 percent.

The expected effects of these measures include an increase in earnings per share, return on common equity, and public float in UnionBanCal common stock.

We also made progress in addressing the "Millennium Bug" — the possibility that computers won't be able to tell the difference between the year "1900" and the year "2000." By December 1998, our core computer systems passed rigorous compliance testing, and we are confident that our operations are well prepared for the year 2000 and beyond.

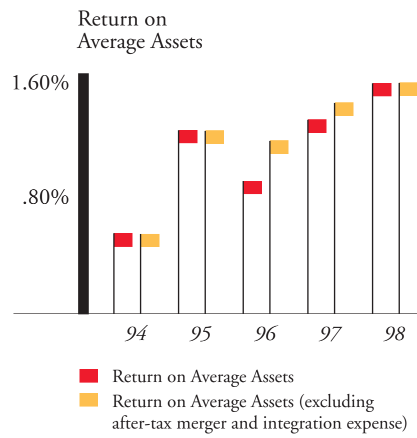
Commitment to community

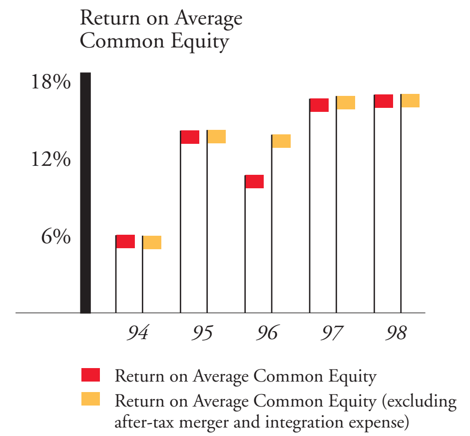
When Union Bank of California was established in April 1996, the result of a merger between the former Union Bank and The Bank of California, the new company made an unprecedented commitment to our communities: for each of the following 10 years, the company pledged to reinvest at least 4.5 percent of assets.



We direct these funds to three broad categories: affordable housing, enterprise development, and grants to nonprofit organizations serving a number of interests.

Our efforts earned a rating in September 1998 of "satisfactory" under the Office of the Comptroller of Currency's new rating system. We are pleased with this rating, the second-highest available, and pledge to continue to work hard to identify and manage reinvestment opportunities throughout our communities. "Community," a publication that details our community-reinvestment activities, is available through our branch offices and by writing to Public Relations & Government Affairs Department, Union Bank of California, N.A; 400 California Street, San Francisco 94104 (MC 1-001-17).





Our Year-2000 effort, although initially remedial in nature, will yield competitive advantages; for example, we are replacing the International Banking Group's network — several older networks patched together — with a powerful, fully integrated platform that promises quantum leaps in service quality.

We are also replacing internal networks and computers with a new desktop platform, sophisticated "shareware" and an "intranet" computer environment, which will facilitate customer service and product development throughout the company.

In 1998, we bade farewell to Tamotsu Yamaguchi, who served as Chairman of the Board, Minoru Noda, Deputy Chairman of the Board and Chief Financial Officer and Chief Credit Officer, and Directors Charles R. Scott and Tetsuo Shimura. Their counsel and guidance over the years have contributed to the success of our enterprise.

We welcomed Kaoru Hayama as Mr. Yamaguchi's successor, Yoshihiko Someya as Deputy Chairman of the Board and head of Credit and Administration and Trust and Private Financial Services, and Hiroshi Watanabe, Managing Director and CEO of Headquarters for the Americas of The Bank of Tokyo-Mitsubishi, Ltd.

In summary, 1998 was a great year. We established all-important momentum for the company. By nurturing that momentum, maintaining our niche-market strategy of personalized service, maintaining high asset quality, aggressively managing capital resources, and improving the efficiency of our operations, we believe we will continue to enhance the value of our franchise long into the future.

KAORU HAYAMA
Chairman
March 24, 1999

TAKAHIRO MORIGUCHI
President and Chief Executive Officer
March 24, 1999

Adrian Vandenakker
PK, Inc.
Chula Vista, California
Satisfied Customer

“I’ve relied on Union Bank of California for 10 years. For my small business, manufacturing outdoor sports equipment, I use the bank’s Fast-Step℠ credit line and merchant services. I also use Signature Banking℠ for my personal banking needs. I’m an ‘early adapter’ of the bank’s electronic banking program, Bank@Home℠, and a big fan of my investment specialist.”

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Value begins with ideas, and at Union Bank of California ideas grow from customer needs.

It was to meet the space needs of **Remec,** Inc., a publicly traded microwave electronics company in San Diego, that we structured a "synthetic lease agreement" covering several buildings Remec was occupying.

Our innovative staff cooked up a full menu of cash-management products that helped the San Francisco landmark **Clift Hotel** earn more and spend less.

With creativity and persistence, we met the need for bank statements for customers of **Nigro, Karlin & Segal**, public accountants in the entertainment industry, before the standard cutoff, for more than 800 accounts instead of the usual handful.

Our wake-up call turned an idle asset — a long-term holding in Coca Cola stock — into a paid-off mortgage, $900 of monthly income, and a charitable remainder trust that minimized tax exposure for a **San Diego couple.**

Our hands-on approach and responsiveness hit sweet notes, but "**Jazz in the City,**" the San Francisco Jazz Festival, was most impressed by the ability of Union Bank of California Investment Services to tailor investment strategies within risk tolerances.

Through cross -border presentations, Union Bank of California, with The Bank of Tokyo-Mitsubishi, played to win the credit and overall banking needs of **Square Electronic Arts,** a new venture between giant video game industry developers from Japan and the U.S., Square Co., Ltd., from Tokyo, and Electronic Arts from San Mateo.

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Lowell W. Paxson
Chairman and Founder
Paxson Communications Corporation
Satisfied Customer

"When we were launching PAX TV, the nation's newest TV network, we thought the high-yield bond market was our best financing alternative. However, in four weeks, Union Bank of California structured, underwrote and syndicated a $122 million bank financing that not only reduced our cost of capital but increased our financial flexibility."

But ideas aren't always enough. Sometimes it takes Herculean effort to add value.

After **Lion Raisins,** a Fresno-based raisin packager and distributor, gave our letters of credit, direct collections and foreign-exchange services a try, our high-quality service led the company to entrust all its international business to us.

Tapping into our longstanding entertainment-industry capabilities, **Beacon Communications** is using a $145 million syndicated credit facility we underwrote to produce two films, one of which is "End of Days," the largest independently bank-financed film ever.

Our **Cash & Save** offices are helping people without bank accounts make the transition to traditional banking products. Almost 40 percent of repeat check-cashing customers are making the move now, up from 8 percent when we began testing the concept in 1996.

In two weeks, including one 40-hour marathon with lawyers, we underwrote, committed, documented and funded a $45 million capitalization for client **Fountain View, Inc.,** a Southern California provider of long-term nursing, rehabilitation and therapy services.

Our government services and electronic banking staff worked through the New Years holiday to complete an implementation of a contract with the **State of California Treasurer's Office** for a process by which six state agencies can collect tax revenues electronically.

His flight cancelled, our officer drove all night so **Stadtlander Drug Distribution Company** of Pennsylvania could meet a three-day deadline for $120 million for recapitalization and acquisition financing.

For **small businesses,** our Fast-Step℠ loan and lease program conserves effort; with a one-page application available from any of our branches, entrepreneurs can get from $5,000 to $50,000 for almost any commercial purpose, like a business computer for a Y2K upgrade, delivery vehicles, or a line of credit to consolidate personal loans used for business.

Terri Bostater
Assistant Treasurer, Hexcel
Satisfied Customer

"We had several orders for our honeycomb composite materials ready for shipping to India when our existing banking relationship could not negotiate the letters of credit we needed. Thankfully, Union Bank of California stepped in and, with its solid network of correspondent banks, negotiated new letters of credit and got our product moving in a hurry."

Our high standards for service set us apart, enhancing the value we created through our ideas, effort and products.

Safeway Inc., one of the largest national supermarket chains, awarded Union Bank of California the check processing for its Southern California Vons stores. Safeway's long relationship with us and Vons' positive experience with our cash vault collections services were the factors in winning the business.

Our A-team of professional banking officers provide white-glove service through our **Priority Banking**SM program to affluent individuals and service-firm clientele who require personal attention and a full array of financial products, from basic ATM access to individually tailored commercial loans.

When **JD Power & Associates** needed cash overnight for focus group costs in a small Georgia town, we saved the day with a wire transfer after overcoming time differences and searching the area for a local bank to act as correspondent.

Our chance to land **Documentum** arrived one Saturday when the CFO of this publicly traded company called with an urgent need for a medallion guarantee. We delivered the sophisticated product Monday morning, winning the full relationship.

Our depository services passed muster in a two-month pilot test of eight warehouses by quality-focused **Costco Wholesale.** The big challenge was to bring another 18 warehouses on line within the following 30 days. We pulled it off, and four more warehouses followed a few months later.

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Ideas plus a Herculean effort and white-glove service can still go for naught, without a strong product platform, and few can match the product array Union Bank of California has to offer.

Operations and Services Complete suite of cash-management services, including lockbox, account reconciliation and controlled disbursement. Cash-handling services through five West Coast cash vaults. ACH and tax payment services to businesses and public agencies. Telephone banking services for consumers, investors and entrepreneurs through Teleservices and Private Service Line.

Systems Technology and Item Processing Direct check-deposit services, coded or not, via office or customer courier through one of five service centers; pre-sorted deposits, post-processing adjustments; return items, collections, check-image products, photocopies of checks and more. On the way: a new "image proof" system resulting in images of deposited items for clients.

Global Markets Market makers for the bank's clients in various global market products and services including foreign exchange, capital and money market securities, interest rate risk management products, and bank- and holding company-issued products like certificates of deposit, bankers acceptances, commercial paper and euro deposits.

Pacific Rim Corporate Products and services for Japanese and Korean companies with operations in the U.S. Resource for interest-rate swaps, asset-backed financing, development bond financing, cash management, trust, equipment leasing, and assistance with reorganizations and mergers and acquisitions, as well as information and advice about local and regional business conditions and practices.

Milton D. Johnson
Administrator, Pipe Trades
Los Angeles

“Since 1959, Union Bank of California has helped us manage retirement programs for workers in the plumbing and pipe-fitting trades industry. Services include custody of assets, funds transfer, lockbox services and fully bundled 401(k) services — and the service has always been excellent.”

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Trust & Private Financial Services Comprehensive investment services, trust and estate planning, corporate retirement plans including bundled daily valuation 401(k) services — *SelectBENEFIT*®, custody and securities lending services, corporate trust services, custom credit capabilities including commercial and residential real estate lending.

International Banking Export bill collections; opening, advising, confirming and negotiating letters of credit; bank-to-bank reimbursements; international and third-party payments, trade and clean financing, money-market transactions, foreign exchange, bankers acceptances, cash letters, collections, deposit and cash management services.

Commercial Financial Services Credit and deposit services for middle market, corporate, and specialized industries clients, including cash management products, check processing and cash vault services, lines of credit, accounts receivable and inventory financing, term loans, construction loans, commercial mortgages and industrial development bonds, leasing, structured financing, project finance, syndications and private capital.

Community Banking For individuals, checking, savings and investment services. Lines of credit, car loans, mortgages, online banking and retirement programs. For businesses, merchant credit card, payroll and online banking. Lines of credit, accounts receivable and inventory financing, leasing, term loans, commercial mortgages, SBA 504 and 7A loans. Services tailored for agriculture, government services, not-for-profits and small and midsize businesses.

Union
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Page

Page	Section
16.	Management's Discussion and Analysis of Financial Condition and Results of Operations
52.	Consolidated Statements of Income
53.	Consolidated Balance Sheets
54.	Consolidated Statements of Changes in Shareholders' Equity
55.	Consolidated Statements of Cash Flows
56.	Notes to Consolidated Financial Statements
85.	Independent Auditors' Report
86.	Boards of Directors and Executive Officers
88.	Bank Directory
89.	Shareholder Information

Management's Discussion and Analysis of Financial Condition and Results of Operations

Selected Financial Data

As of and for the Years Ended December 31,	1994	1995	1996	1997	**1998**
(Dollars in thousands, except per share data)					
Results of operations:					
Net interest income[1]	$ 1,007,789	$ 1,152,777	$ 1,175,302	$ 1,237,010	**$ 1,322,655**
Provision for credit losses	73,000	53,250	40,000	—	**45,000**
Noninterest income	359,831	395,319	418,676	463,001	**533,531**
Noninterest expense	1,036,349	978,101	1,134,904	1,044,665	**1,135,218**
Income before income taxes[1]	258,271	516,745	419,074	655,346	**675,968**
Taxable-equivalent adjustment	12,566	10,444	6,724	5,328	**4,432**
Income tax expense	120,356	193,359	162,892	238,722	**205,075**
Net income	$ 125,349	$ 312,942	$ 249,458	$ 411,296	**$ 466,461**
Net income applicable to common stock	$ 114,045	$ 301,637	$ 238,152	$ 403,696	**$ 466,461**
Per common share:					
Net income—basic	$ 0.67	$ 1.74	$ 1.37	$ 2.31	**$ 2.66**
Net income—diluted	0.67	1.73	1.36	2.30	**2.65**
Dividends[2]	0.47	0.47	0.47	0.51	**0.61**
Book value (end of period)	11.88	13.49	13.53	15.32	**17.45**
Common shares outstanding (end of period)	172,043,617	174,180,493	174,457,603	174,917,674	**175,259,919**
Weighted average common shares outstanding—basic	171,089,311	173,806,300	174,391,048	174,683,338	**175,127,487**
Weighted average common shares outstanding—diluted	171,149,731	174,099,241	174,783,565	175,189,078	**175,737,303**
Balance sheet (end of period):					
Total assets	$24,569,042	$27,546,859	$29,234,059	$30,585,265	**$32,276,316**
Total loans	18,065,650	20,431,683	21,049,787	22,741,408	**24,296,111**
Nonperforming assets	421,227	246,871	156,784	129,809	**89,850**
Total deposits	17,409,737	19,655,043	21,532,960	23,296,374	**24,507,879**
Subordinated capital notes	655,859	501,369	382,000	348,000	**298,000**
Preferred stock	135,000	135,000	135,000	—	**—**
Common equity	2,044,202	2,349,092	2,359,933	2,679,299	**3,058,244**

Management's Discussion and Analysis of Financial Condition and Results of Operations

Selected Financial Data (continued)

As of and for the Years Ended December 31,	1994	1995	1996	1997	**1998**
(Dollars in thousands, except per share data)					
Balance sheet (period average):					
Total assets	$23,692,560	$25,564,843	$27,899,734	$29,692,992	**$30,523,806**
Total loans	17,616,002	18,974,540	20,727,577	21,855,911	**23,215,504**
Earning assets	21,046,600	22,849,129	24,717,326	26,291,822	**27,487,390**
Total deposits	16,826,443	17,969,972	20,101,544	22,067,155	**22,654,714**
Common equity	1,980,577	2,197,476	2,325,437	2,514,610	**2,845,964**
Financial ratios:					
Return on average assets	0.53%	1.22%	0.89%	1.39%	**1.53%**
Return on average common equity	5.76	13.73	10.24	16.05	**16.39**
Efficiency ratio[3]	70.39	63.39	71.02	61.53	**61.31**
Net interest margin[1]	4.79	5.05	4.75	4.70	**4.81**
Dividend payout ratio	70.15	27.01	34.31	22.08	**22.93**
Tangible equity ratio	7.91	8.20	7.80	8.54	**9.30**
Tier 1 risk-based capital ratio	9.24	9.35	9.08	8.96	**9.64**
Total risk-based capital ratio	12.03	11.70	11.17	11.05	**11.61**
Leverage ratio	8.67	8.70	8.41	8.53	**9.38**
Allowance for credit losses to total loans	3.12	2.72	2.49	1.99	**1.89**
Allowance for credit losses to nonaccrual loans	161.08	266.56	408.48	413.12	**585.50**
Net loans charged off to average total loans	1.15	0.32	0.34	0.33	**0.15**
Nonperforming assets to total loans and foreclosed assets	2.32	1.21	0.74	0.57	**0.37**
Nonperforming assets to total assets	1.71	0.90	0.54	0.42	**0.28**

(1) Amounts are on a taxable-equivalent basis using the federal statutory tax rate of 35 percent.

(2) Dividends per share reflect dividends declared on UnionBanCal Corporation's common stock outstanding as of the declaration date. Amounts prior to the merger are based on Union Bank only and do not include the dividend of $145 million paid to The Mitsubishi Bank, Limited in the first quarter of 1996 by BanCal Tri-State Corporation and The Bank of California, N.A.

(3) The efficiency ratio is noninterest expense, excluding foreclosed asset expense (income), as a percentage of net interest income (taxable-equivalent) and noninterest income. Foreclosed asset expense (income) was $73.7 million, $(3.2) million, $2.9 million, $(1.3) million, and $(2.8) million for 1994 through 1998, respectively.

Management's Discussion and Analysis of Financial Condition and Results of Operations

This document may contain forward-looking statements that are subject to risks and uncertainties that could cause actual results to differ materially from those indicated. For a discussion of factors that could cause actual results to differ, please see the discussion contained herein and in our publicly available Securities and Exchange Commission filings and press releases.

You should read the following discussion and analysis of our consolidated financial position and the results of our operations for the years ended December 31, 1996, 1997 and 1998 together with our Consolidated Financial Statements and the Notes to Consolidated Financial Statements. Averages as presented in the following tables are substantially all based upon daily average balances.

Introduction

We are a California-based, commercial bank holding company with consolidated assets of $32.3 billion at December 31, 1998. Union Bank of California, N.A. was the third largest commercial bank in California, based on total assets and total deposits in California, and one of the 30 largest commercial banks in the United States.

UnionBanCal Corporation and its banking subsidiary, Union Bank of California, N.A., was created on April 1, 1996 by the combination of Union Bank with BanCal Tri-State Corporation and its banking subsidiary, The Bank of California, N.A. The combination was accounted for as a reorganization of entities under common control, similar to a pooling of interests. Accordingly, all historical financial information has been restated as if the combination had been in effect for all periods presented.

Overview

Net income in 1997 was $411 million, compared to $466 million in 1998. Net income applicable to common stock was $404 million, or $2.30 per diluted common share, in 1997, compared with $466 million, or $2.65 per diluted common share, in 1998. This increase in diluted earnings per share of 15 percent over 1997 was due to a 7 percent increase in net interest income, a 15 percent increase in noninterest income, and a 6 percent decrease in the effective income tax rate, partially offset by a $45 million increase in the provision for credit losses and a 9 percent increase in noninterest expense. Excluding an after-tax refund of $25 million from the California Franchise Tax Board (FTB) received in the third quarter of 1997, net income applicable to common stock was $379 million, or $2.16 per diluted common share, in 1997. Excluding a state tax reduction of $60 million, net of federal tax, as described below, net income applicable to common stock in 1998 was $406 million, or $2.31 per diluted common share. Other highlights for 1998 include:

- Net interest income, on a taxable-equivalent basis, was $1.3 billion in 1998, an increase of $86 million, or 7 percent, over 1997. Net interest margin in 1998 was 4.81 percent, an increase of 11 basis points over 1997.
- No provision for credit losses was recorded in 1997, compared with $45 million in 1998. This resulted from management's regular assessment of overall credit quality, loan growth and economic conditions in relation to the level of the allowance for credit losses. The allowance for credit losses was $452 million, or 413% of total nonaccrual loans, at December 31, 1997, compared with $459 million, or 586% of total nonaccrual loans, at December 31, 1998. Net loans charged off for 1998 were $36 million.
- Nonperforming assets declined $40 million, or 31 percent, from December 31, 1997 to $90 million at December 31, 1998. Nonperforming assets as a percent of total assets declined to 0.28 percent at December 31, 1998, compared with 0.42 percent a year earlier. Total nonaccrual loans were $109 million at December 31, 1997, compared with $78 million at year-end 1998, resulting in a reduction in the ratio of nonaccrual and renegotiated loans to total loans from 0.48 percent at December 31, 1997 to 0.32 percent at year-end 1998.
- Noninterest income was $534 million in 1998, an increase of $71 million, or 15 percent, over 1997. This increase includes the $17 million gain from the sale of the credit card portfolio in the second quarter of 1998. Service

Management's Discussion and Analysis of Financial Condition and Results of Operations

charges on deposit accounts grew $24 million, or 21 percent; trust and investment management fees increased $14 million, or 13 percent; international commissions and fees increased $6 million, or 9 percent; merchant banking fees increased $6 million, or 26 percent; and securities gains, net, increased $3 million.

- Noninterest expense was $1.1 billion in 1998, an increase of $91 million, or 9 percent, over 1997. Personnel-related expense increased $46 million, or 8 percent; other non-interest expense increased $22 million, or 29 percent; and professional services increased $9 million, or 31 percent.
- The effective tax rate for 1997 was 37 percent, compared with 31 percent for 1998. The effective tax rate for 1997 was favorably affected by an after-tax refund of $25 million from the FTB for tax years 1975-1987. The primary reason for the lower 1998 effective tax rate was the filing of our 1997, and our intention to file our 1998, California franchise tax returns on a worldwide unitary basis, which incorporates the results of The Bank of Tokyo-Mitsubishi, Ltd. and its worldwide affiliates. Excluding the FTB refund in 1997 and the $60 million state tax reduction in 1998, the effective tax rates would have been 41 percent and 40 percent, respectively.
- The return on average assets for 1998 increased to 1.53 percent, compared to 1.39 percent for 1997. The return on average common equity for 1998 increased to 16.39 percent, compared to 16.05 percent for 1997.
- Total loans at December 31, 1998 were $24.3 billion, an increase of $1.6 billion, or 7 percent, over year-end 1997.
- At December 31, 1998, our Tier 1 risk-based capital ratio was 9.64 percent and our total risk-based capital ratio was 11.61 percent, exceeding the minimum regulatory guidelines for bank holding companies of 4 percent and 8 percent, respectively. The Tier 1 and total risk-based capital ratios for Union Bank of California, N.A. at December 31, 1998 exceeded the regulatory guidelines for "well-capitalized" banks. Our leverage ratio was 9.38 percent at December 31, 1998, exceeding the minimum regulatory guideline for bank holding companies.

Business Segments

We segregate our operations into five primary business units for the purpose of management reporting, as shown in the table on the following page. The results show the financial performance of our major business units.

The information reflects the condensed income statements, balance sheet items and a selected financial ratio by business unit. The information presented does not necessarily represent the business units' financial condition and results of operations as if they were independent entities. Unlike financial accounting, there is no authoritative body of guidance for management accounting equivalent to generally accepted accounting principles. Consequently, reported results are not necessarily comparable with those presented by other companies.

Business unit results are based on an internal management reporting system used by management to measure the performance of the units and the company as a whole. The management reporting system assigns balance sheet and income statement items to each business unit based on internal management accounting policies. Net interest income is determined using our internal funds transfer pricing system, which assigns a cost of funds or a credit for funds to assets or liabilities based on their type, maturity or repricing characteristics. Noninterest income and expense directly attributable to a business unit are assigned to that business. Indirect costs, such as overhead, operation, and technology expense, are allocated to the business units based on studies of billable unit costs for product or data processing. The provision for credit losses is allocated based on the formula and specific reserves and the net chargeoffs for each respective business unit. Equity is allocated based on a combination of regulatory requirements and management's assessment of economic risk factors, primarily credit, operating, foreign exchange and interest rate risk.

The Company is in the process of developing a model for measuring profitability on a risk adjusted return on equity basis. When fully implemented, this methodology will be adopted and all prior periods will be restated.

Management's Discussion and Analysis of Financial Condition and Results of Operations

Years Ended December 31,	Community Banking Group 1997	Community Banking Group 1998	Commercial Financial Services Group 1997	Commercial Financial Services Group 1998	International Banking Group 1997	International Banking Group 1998
Results of operations (dollars in thousands):						
Net interest income	$682,782	**$673,463**	$440,804	**$494,713**	$ 49,405	**$ 55,741**
Noninterest income	142,944	**178,208**	100,316	**109,520**	62,238	**65,834**
Total revenue	825,726	**851,671**	541,120	**604,233**	111,643	**121,575**
Noninterest expense	568,031	**596,714**	231,906	**257,124**	64,874	**66,967**
Credit expense (income)	57,870	**4,300**	18,872	**21,316**	234	**11,304**
Income (loss) before income tax expense (benefit) and performance center earnings (expense)[1]	199,825	**250,657**	290,342	**325,793**	46,535	**43,304**
Performance center earnings (expense)[1]	10,040	**7,769**	3,926	**2,270**	(3,759)	**(4,087)**
Income (loss) before income tax expense (benefit)	209,865	**258,426**	294,268	**328,063**	42,776	**39,217**
Income tax expense (benefit)	86,063	**102,138**	120,676	**127,854**	17,542	**14,773**
Net income	$123,802	**$156,288**	$173,592	**$200,209**	$ 25,234	**$ 24,444**
Average balances (dollars in millions):						
Total loans before performance centers[2]	$ 9,672	**$ 9,328**	$ 9,336	**$ 11,164**	$ 1,631	**$ 1,356**
Total assets	10,626	**10,270**	10,513	**12,414**	2,631	**2,070**
Total deposits before performance centers[2]	11,757	**12,444**	4,875	**5,985**	959	**851**
Financial ratio:						
Return on average assets[3]	1.17%	**1.52%**	1.65%	**1.61%**	0.96%	**1.18%**

Years Ended December 31,	Trust and Private Financial Services Group 1997	Trust and Private Financial Services Group 1998	Global Markets Group 1997	Global Markets Group 1998	Other 1997	Other 1998
Results of operations (dollars in thousands):						
Net interest income	$ 20,995	**$ 22,979**	$ 25,348	**$35,472**	$ 12,348	**$ 35,855**
Noninterest income	128,100	**145,593**	21,189	**29,854**	8,214	**4,522**
Total revenue	149,095	**168,572**	46,537	**65,326**	20,562	**40,377**
Noninterest expense	123,102	**134,977**	22,574	**26,718**	34,178	**52,718**
Credit expense (income)	155	**345**	—	**—**	(77,131)	**7,735**
Income (loss) before income tax expense (benefit) and performance center earnings (expense)[1]	25,838	**33,250**	23,963	**38,608**	63,515	**(20,076)**
Performance center earnings (expense)[1]	(1,472)	**122**	(10,194)	**(9,231)**	1,459	**3,157**
Income (loss) before income tax expense (benefit)	24,366	**33,372**	13,769	**29,377**	64,974	**(16,919)**
Income tax expense (benefit)	9,992	**13,133**	5,647	**11,608**	(1,198)	**(64,431)**
Net income	$ 14,374	**$ 20,239**	$ 8,122	**$17,769**	$ 66,172	**$ 47,512**
Average balances (dollars in millions):						
Total loans before performance centers[2]	$ 229	**$ 258**	$ —	**$ —**	$ 988	**$ 1,110**
Total assets	303	**315**	4,078	**4,090**	1,542	**1,365**
Total deposits before performance centers[2]	708	**675**	3,783	**2,662**	(15)	**38**
Financial ratio:						
Return on average assets[3]	4.74%	**6.43%**	0.20%	**0.43%**	na	**na**

(1) Performance center earnings (expense) represent the allocation of net interest income, noninterest income and noninterest expense between the business segments for products and services originated in one segment but managed by another.

(2) Represents loans and deposits for each business segment before allocation between the segments of loans and deposits originated in one segment but managed by another.

(3) The increase in 1998 over the prior year for the Community Banking Group was due to the sale of the credit card portfolio as discussed on page 31.

Management's Discussion and Analysis of Financial Condition and Results of Operations

Community Banking Group

The Community Banking Group provides its customers with a full line of checking and savings, investment, loan and fee-based banking products. In 1998, average assets in this group were $10.3 billion, and average deposits were $12.4 billion. The increase in the group's net income over 1997 was primarily attributable to the decline in the provision for credit losses, resulting from the sale of the credit card portfolio that is discussed on page 31.

The group focuses on four major markets:

- consumers,
- businesses with sales under $3 million,
- businesses with sales between $3 million and $20 million, and
- middle market companies, including agricultural firms, in central California and in selected parts of Oregon and Washington.

The group serves over one million consumer households and businesses through its 244 branches in California, six branches in Oregon and Washington and its network of over 380 proprietary ATMs. Customers may also access our services 24 hours a day by telephone or personal computer. In addition, the group offers automated teller and point-of-sale debit services through our founding membership in the Star System, the largest shared ATM network in the Western United States.

The group is organized by service delivery method, by markets and by geography. The primary sub-units of the group are:

- community banking branches, which serve consumers, businesses and, in certain locations, affluent individuals,
- business banking centers, which serve businesses with sales between $3 million and $20 million,
- in-store branches, which also serve consumers and businesses,
- middle market and agricultural lending offices, and
- the Consumer Asset Management division, which is responsible for indirect auto finance, auto leasing, and residential real estate lending.

Through alliances with other financial institutions, the group offers additional products and services, such as credit cards, leasing, and asset-based and leveraged financing.

The group competes with larger banks by providing service quality superior to that of its major competitors. We are recognized as among the highest rated banks in California for customer service quality and satisfaction.

The group's primary means of competing with community banks include its large and convenient branch network and its reputation for innovative use of technology to deliver banking services. We have the fifth largest branch network among depository institutions in California. We also offer convenient banking hours to consumers through our drive-through banking locations and selected branches that are open seven days a week.

The group's strategies include continuing to build upon the more than one million households and businesses it serves and broadening the range of financial products and services it provides to existing customers. The group uses direct mail marketing methods targeted at specific consumers to supplement its traditional mass media advertising. We are also introducing a new computer- driven sales system designed to foster cross-selling of our products. The new system uses improved software to prompt sales staff to offer customers additional products and services, based on a customer profile. We have installed the new system in 40 of our branches, and we anticipate full implementation within 18 months.

The group will continue to use varied pricing strategies to encourage customers to use lower-cost methods of delivery to receive our products and services. The group is emphasizing further development of existing lower-cost product and service delivery methods, such as the Internet, video kiosks and loans-by-phone, and is expanding its Direct Banking Center, which offers products, services, and technical support for home banking via the telephone and computer.

The group competes with a number of commercial banks, savings associations and credit unions, as well as more specialized financial service providers, such as investment brokerage companies, consumer finance companies, and residential real estate lenders. The group's primary competitors are other major depository institutions such as Bank of America, California Federal, Washington Mutual and Wells Fargo, as well as smaller community banks in the markets in which we operate.

Commercial Financial Services Group

The Commercial Financial Services Group offers a variety of commercial financial services, including:

- commercial and project loans,
- real estate financing,
- commercial financing based on accounts receivable, inventory, or other short term assets,
- trade financing, which is the short-term extension of credit to support export/import transactions, including letters of credit,
- lease financing,
- customized cash management services, and
- selected capital markets products.

The group's customers provide a significant source of opportunities for us to sell products and services of other units of the bank, including treasury, trust, and retail banking services. In 1998, average assets in this group were $12.4 billion, and average deposits were $6.0 billion. The increase in the group's net income over 1997 was primarily due to

Management's Discussion and Analysis of Financial Condition and Results of Operations

the growth in commercial, financial and industrial loans as further discussed on page 31.

The group is divided into the following business units, which serve specific markets and industries:

- the Commercial Banking Group, which serves California middle-market companies and larger companies most often headquartered in the Western United States,
- the Real Estate Industries Group, which serves real estate developers and real estate investment trusts,
- the Specialized Lending Group, which serves companies operating in various industries, including oil and gas, utilities, media, communications, healthcare, finance, and retailing, and
- the Institutional and Deposit Markets Group, which serves title and escrow companies, financial institutions, retailers, bankruptcy trustees, and other customers with large pools of deposits.

The Commercial Customer Service Unit supports these business units by providing centralized customer service support.

The group competes with other banks primarily on the basis of its reputation as a "business bank", the quality of its relationship managers, and the delivery of superior customer service. We are recognized in California as having a superior "business banking" reputation relative to other large banks. We are also highly rated among financial institutions for our cash management services and systems.

The group's main strategy is to target industries and companies for which the group can reasonably expect to be one of a customer's primary banks. Consistent with its strategy, the group attempts to serve a large part of its targeted customers' credit and depository needs.

The group competes with a variety of other financial services companies. Competitors include other major California banks, as well as regional, national and international banks. In addition, we compete with investment banks, commercial finance companies, leasing companies, and insurance companies.

International Banking Group

The International Banking Group primarily provides correspondent banking and trade finance-related products and services to financial institutions worldwide, particularly in Brazil, Hong Kong, Japan, Korea, and Taiwan. This includes the provision of products and services that facilitate trade finance transactions, including payments, collection and the extension of short-term credit. The group also serves selected foreign firms and U.S. corporate clients in selected countries worldwide, particularly in Asia. In the U.S., the group serves subsidiaries and affiliates of non-Japanese Asian companies and U.S. branches and agencies of foreign banks. The group also provides international services to domestic corporate clients along the West Coast. The group's revenue predominately relates to foreign customers. In 1998, average assets in this group were $2.1 billion and average deposits were $851 million.

The group has a long and stable history of providing correspondent and trade- related services to international financial institutions. We believe that we have achieved a leading market position and strong customer loyalty in the Asia/Pacific correspondent banking market because we provide high quality, customized products, and services at competitive prices. The group maintains branches in Tokyo, Taipei, Seoul, Manila and Hong Kong, representative offices in other parts of Asia and Latin America, and an international banking subsidiary in New York.

One of the group's primary services is international trade finance. Trade finance is typically short-term, which means it generally has a lower credit risk. Despite this relatively lower credit risk compared to some other forms of commercial credit, we have reduced the amount of credit we have extended to our customers and the average maturity of this portfolio in response to recent instability in global markets.

The group's strategy is to improve its global operations by reducing costs and improving productivity. It competes with both U.S. and foreign banks. Approximately 25 U.S. banks compete with the group to provide correspondent banking and trade-related services to Asian banks. The group's primary competitors include First Union, Bank of New York, Chase Manhattan, Citibank, Bank of America, and Bank of Hawaii.

Trust and Private Financial Services Group

The Trust and Private Financial Services Group offers investment management and administration services for a broad range of individuals and institutions. The group:

- services individual client needs through its trust and private banking, investment management and brokerage products and services,
- services institutional client needs through traditional employee benefit and 401(k) programs, global and domestic securities custody programs, securities lending programs and corporate trust products, and
- provides investment management services for both individual and institutional clients through HighMark Capital Management, Inc. and its family of proprietary HighMark mutual funds.

As of December 31, 1998, the group had over $97.4 billion in assets under administration.

The group is organized into five business divisions:

- The Private Bank division focuses primarily on delivering integrated and customized financial services to high net worth individuals with sophisticated financial needs. Specific products and services include trust and estate services,

Management's Discussion and Analysis of Financial Condition and Results of Operations

investment account management services, offshore trust services and customized deposit and credit products. The Private Bank's strategy is to expand its business by increasing its geographic market coverage and the breadth of its products and services. To support that strategy, The Private Bank expanded from 9 offices to 15 offices during 1998. In addition, it has shifted sales staff training efforts toward increased cross-selling of all of the bank's available products and services.

- HighMark Capital Management, Inc., a registered investment advisor, manages our proprietary HighMark family of mutual funds. It also provides investment management services to institutions, pension plans and individuals, including to clients of other divisions. HighMark Capital Management's strategy is to expand distribution of its mutual funds by targeting its marketing efforts at registered investment advisors and regional broker/dealers. In addition, HighMark is working with The Bank of Tokyo-Mitsubishi, Ltd. and other third parties to establish mutual funds offshore that Highmark will advise and which will be offered to non-U.S. investors. HighMark also serves as a sub-advisor for funds managed by Tokyo-Mitsubishi Asset Management, Ltd. in Japan.
- The Business Trust division provides businesses, government agencies, unions and non-profit organizations with trustee services, investment management and 401(k) valuation and record keeping services. Business Trust's strategy is to expand its third-party distribution network to include insurance companies, investment managers, brokers and mutual funds.
- The Investment Services division consists of Union Bank of California, N.A. Insurance Services and Union Bank of California, N.A. Investment Services, Inc., a registered broker/dealer offering a full line of investment products to individuals and institutional clients. The division's primary strategy is to further penetrate our existing client base.
- The Securities Services division is engaged in domestic and global securities custody, safekeeping, mutual fund accounting, securities lending, and corporate trust services. Its client base includes financial institutions, businesses, government agencies, unions, investment managers and non-profit organizations. Securities Services is the only West Coast based provider of a full range of institutional financial services.

Global Markets Group

The Global Markets Group conducts business activities primarily to support the previously described business groups and their customers. This group offers a broad range of risk management products, such as foreign exchange and interest rate swaps, caps and floors. Additionally, it originates debt instruments for bank eligible issuers, places debt securities, including Union Bank of California, N.A.'s own liabilities, with institutional investors and trades debt instruments in the secondary market. This group also manages our market-related risks as part of its responsibilities for asset/liability management. The group is also responsible for maintaining Union Bank of California, N.A.'s investment securities portfolio. In 1998, average assets in this group were $4.1 billion and average deposits were $2.7 billion.

The group manages our securities portfolio, trading operations, wholesale funding needs, and interest rate and liquidity risk. The group includes products that support corporate lending, customer interest rate risk management needs and foreign exchange.

Other

"Other" includes the following items, none of which, on an individual basis, are significant to our business:

- Corporate activities that are not directly attributable to one of the five major business units. Included in this category are goodwill, merger and integration expense, certain parent company non-bank subsidiaries, and the elimination of the fully taxable-equivalent amounts.
- The unallocated allowance and related provision for credit losses, the net impact of transfer pricing, and earnings associated with unallocated equity capital.
- The Credit and Compliance Group, which includes $193 million of average nonperforming assets.
- The Pacific Rim Corporate Group, which offers a range of credit, deposit, and investment management products and services to companies in the U.S. which are affiliated with companies headquartered outside the U.S., mostly in Japan.
- The residual costs of support groups.

Strategic Initiatives

In connection with our strategic repositioning, we have developed long-term financial performance goals. These goals will serve as a tool for measuring the long-term success of our operating strategies, based on normal business operations, without including nonrecurring events that may occur from time to time. Our long-term financial performance goals include:

Performance Ratio	Goal
• Return on average common equity	15% to 17%
• Earnings per share growth	10% to 12%
• Efficiency ratio	54% to 56%
• Tangible common equity to assets	7.5% to 8.5%

Although we believe these goals are realizable given our proposed operating strategies and our current asset quality, we cannot assure you that we will attain these long-term financial performance goals at any particular time. See paragraph on forward-looking statements on page 18.

Management's Discussion and Analysis of Financial Condition and Results of Operations

Net Interest Income

The table below shows the major components of net interest income and net interest margin.

Years Ended December 31,	1996 Average Balance	1996 Interest Income/ Expense[1]	1996 Average Yield/ Rate[1]	1997 Average Balance	1997 Interest Income/ Expense[1]	1997 Average Yield/ Rate[1]	**1998 Average Balance**	**1998 Interest Income/ Expense[1]**	**1998 Average Yield/ Rate[1]**
(Dollars in thousands)									
Assets									
Loans:[2]									
Domestic	$19,328,752	$1,604,799	8.30%	$20,332,494	$1,672,006	8.22%	**$21,890,350**	**$1,736,847**	**7.93%**
Foreign[3]	1,398,825	84,693	6.05	1,523,417	92,420	6.07	**1,325,154**	**90,011**	**6.79**
Securities—taxable[4]	2,138,282	133,170	6.23	2,521,339	158,950	6.30	**3,056,152**	**192,404**	**6.30**
Securities—tax-exempt[4]	151,970	15,451	10.17	124,174	12,669	10.20	**103,097**	**11,384**	**11.04**
Interest bearing deposits in banks	911,575	52,709	5.78	968,966	56,748	5.86	**260,720**	**17,080**	**6.55**
Federal funds sold and securities purchased under resale agreements	547,547	30,246	5.52	466,321	26,079	5.59	**296,285**	**16,056**	**5.42**
Trading account assets	240,375	12,960	5.39	355,111	19,917	5.61	**555,632**	**25,829**	**4.65**
Total earning assets	24,717,326	1,934,028	7.82	26,291,822	2,038,789	7.75	**27,487,390**	**2,089,611**	**7.60**
Allowance for credit losses	(544,806)			(503,126)			**(471,113)**		
Cash and due from banks	1,926,050			2,006,038			**1,919,714**		
Premises and equipment, net	425,943			411,302			**405,562**		
Other assets	1,375,221			1,486,956			**1,182,253**		
Total assets	$27,899,734			$29,692,992			**$30,523,806**		
Liabilities									
Domestic deposits:									
Interest bearing	$ 5,001,060	135,821	2.72	$ 5,340,661	151,768	2.84	**$ 5,482,257**	**$ 153,805**	**2.81**
Savings and consumer time	2,837,198	105,350	3.71	2,970,370	112,808	3.80	**3,205,823**	**120,778**	**3.77**
Large time	4,095,222	218,959	5.35	4,652,293	256,007	5.50	**3,644,732**	**194,324**	**5.33**
Foreign deposits[3]	1,504,067	71,437	4.75	1,589,303	75,398	4.74	**1,704,027**	**86,221**	**5.06**
Total interest bearing deposits	13,437,547	531,567	3.96	14,552,627	595,981	4.10	**14,036,839**	**555,128**	**3.95**
Federal funds purchased and securities sold under repurchase agreements	933,433	47,095	5.05	1,097,707	58,544	5.33	**1,604,675**	**84,440**	**5.26**
Subordinated capital notes	458,966	30,104	6.56	354,575	22,850	6.44	**325,808**	**20,347**	**6.24**
Commercial paper	1,620,087	87,411	5.40	1,637,070	89,912	5.49	**1,631,216**	**88,358**	**5.42**
Other borrowed funds	1,119,051	62,549	5.59	635,900	34,492	5.42	**328,872**	**18,683**	**5.68**
Total borrowed funds	4,131,537	227,159	5.50	3,725,252	205,798	5.52	**3,890,571**	**211,828**	**5.44**
Total interest bearing liabilities	17,569,084	758,726	4.32	18,277,879	801,779	4.39	**17,927,410**	**766,956**	**4.28**
Noninterest bearing deposits	6,663,997			7,514,528			**8,617,875**		
Other liabilities	1,206,216			1,295,728			**1,132,557**		
Total liabilities	25,439,297			27,088,135			**27,677,842**		
Shareholders' Equity									
Preferred stock	135,000			90,247			**—**		
Common equity	2,325,437			2,514,610			**2,845,964**		
Total shareholders' equity	2,460,437			2,604,857			**2,845,964**		
Total liabilities and shareholders' equity	$27,899,734			$29,692,992			**$30,523,806**		
Net interest income/margin (taxable-equivalent basis)		1,175,302	4.75%		1,237,010	4.70%		**1,322,655**	**4.81%**
Less: taxable-equivalent adjustment		6,724			5,328			**4,432**	
Net interest income		$1,168,578			$1,231,682			**$1,318,223**	

(1) Yields and interest income are presented on a taxable-equivalent basis using the federal statutory tax rate of 35 percent.

(2) Average balances on loans outstanding include all nonperforming and renegotiated loans. The amortized portion of net loan origination fees (costs) is included in interest income on loans, representing an adjustment to the yield.

(3) Foreign loans and deposits are those loans and deposits originated in foreign branches.

(4) Yields on securities available for sale are based on fair value. The difference between these yields and those based on amortized cost was not significant.

Management's Discussion and Analysis of Financial Condition and Results of Operations

Net interest income is interest earned on loans and investments less interest expense on deposit accounts and borrowings. Primary factors affecting the level of net interest income include the margin between the yield earned on interest earning assets and the rate paid on interest bearing liabilities, as well as the volume and composition of average interest earning assets and average interest bearing liabilities.

Net interest income, on a taxable-equivalent basis, was $1.2 billion in 1997, compared with $1.3 billion in 1998. The increase of $86 million, or 7 percent, was primarily attributable to a $1.2 billion, or 5 percent, increase in average earning assets largely funded by a $1.1 billion, or 15 percent, increase in average noninterest bearing deposits. In addition, net interest margin increased 11 basis points to 4.81 percent. Although the differential between the decrease in the yield on average earning assets and the decrease in the rate on average interest bearing liabilities was a negative 4 basis points, resulting from a 75 basis point decrease in the Federal Funds rate in the fourth quarter of 1998, the negative impact on the net interest margin of these two factors was more than offset by the increase in the proportion of funding provided by average noninterest bearing deposits, thereby lowering the overall cost of funds.

Average earning assets were $26.3 billion in 1997, compared with $27.5 billion in 1998. This growth was primarily attributable to a $1.4 billion, or 6 percent, increase in average loans and a $514 million, or 19 percent, increase in average securities, partially offset by a $708 million decrease in average interest bearing deposits in banks. The growth in average loans was attributable to the increase in average commercial, financial and industrial loans of $1.8 billion, partially offset by the decrease in average consumer loans of $389 million, primarily related to the sale of the credit card portfolio. See "Loans" on page 30 for additional commentary on growth in the loan portfolio. The increase in primarily fixed rate securities reflected interest rate risk management actions to reduce our exposure to declines in interest rates.

The $1.2 billion, or 5 percent, growth in average earning assets over 1997 was primarily funded by a $1.1 billion increase in average noninterest bearing deposits. The increase in average noninterest bearing deposits in 1998 was partially due to an influx of new customer relationships, arising from the merger and acquisition activities of other financial institutions in the California market during the past year.

Management's Discussion and Analysis of Financial Condition and Results of Operations

Analysis of Changes in Net Interest Income

The following table shows the changes in the components of net interest income on a taxable-equivalent basis. The changes in net interest income between periods have been reflected as attributable either to volume or to rate changes. For purposes of this table, changes that are not solely due to volume or rate changes are allocated to rate.

	Increase (decrease) due to change in			Increase (decrease) due to change in		
	Average Volume	Average Rate	Net Change	Average Volume	Average Rate	Net Change
Years Ended December 31,		1997 Versus 1996			1998 Versus 1997	
(Dollars in thousands)						
Changes in Interest Income						
Loans:						
Domestic	$ 83,311	$(16,104)	$ 67,207	$128,056	$(63,215)	$ 64,841
Foreign[1]	7,538	189	7,727	(12,035)	9,626	(2,409)
Securities—taxable	23,856	1,924	25,780	33,693	(239)	33,454
Securities—tax-exempt	(2,826)	44	(2,782)	(2,150)	865	(1,285)
Interest bearing deposits in banks	3,317	722	4,039	(41,503)	1,835	(39,668)
Federal funds sold and securities purchased under resale agreements	(4,484)	317	(4,167)	(9,505)	(518)	(10,023)
Trading account assets	6,184	773	6,957	11,249	(5,337)	5,912
Total earning assets	116,896	(12,135)	104,761	107,805	(56,983)	50,822
Changes in Interest Expense						
Domestic deposits:						
Interest bearing	$ 9,237	$ 6,710	15,947	$ 4,021	$ (1,984)	$ 2,037
Savings and consumer time	4,941	2,517	7,458	8,947	(977)	7,970
Large time	29,803	7,245	37,048	(55,416)	(6,267)	(61,683)
Foreign deposits[1]	4,049	(88)	3,961	5,438	5,385	10,823
Total interest bearing deposits	48,030	16,384	64,414	(37,010)	(3,843)	(40,853)
Federal funds purchased and securities sold under repurchase agreements	8,296	3,153	11,449	27,021	(1,125)	25,896
Subordinated capital notes	(6,848)	(406)	(7,254)	(1,853)	(650)	(2,503)
Commercial paper	916	1,585	2,501	(321)	(1,233)	(1,554)
Other borrowed funds	(27,006)	(1,051)	(28,057)	(16,641)	832	(15,809)
Total borrowed funds	(24,642)	3,281	(21,361)	8,206	(2,176)	6,030
Total interest bearing liabilities	23,388	19,665	43,053	(28,804)	(6,019)	(34,823)
Changes in net interest income	$ 93,508	$(31,800)	$ 61,708	$136,609	$(50,964)	$ 85,645

[1] Foreign loans and deposits are those loans and deposits originated in foreign branches.

Management's Discussion and Analysis of Financial Condition and Results of Operations

Interest income on a taxable-equivalent basis increased $51 million in 1998, primarily due to growth in interest income from average domestic loans and average taxable securities of $65 million and $33 million, respectively, partially offset by lower interest income from average interest bearing deposits in banks of $40 million. These changes reflected higher average balances outstanding on average domestic loans and average taxable securities, partially offset by a lower average yield on average domestic loans and a lower average balance outstanding on average interest bearing deposits in banks.

Interest expense decreased $35 million in 1998 due to lower interest expense on average interest bearing deposits, primarily reflecting lower average deposit balances and lower average rates. Interest expense on borrowed funds increased $6 million in 1998, reflecting higher volumes, offset by an 8 basis point decrease in the average rate paid.

Noninterest Income

				Increase (Decrease)			
				Amount	Percent	Amount	Percent
Years Ended December 31,	1996	1997	**1998**	1997 Versus 1996		1998 Versus 1997	
(Dollars in thousands)							
Service charges on deposit accounts	$101,975	$114,647	**$138,847**	$12,672	12%	$24,200	21%
Trust and investment management fees	93,479	107,527	**121,226**	14,048	15	13,699	13
International commissions and fees	66,108	66,122	**72,036**	14	—	5,914	9
Merchant transaction processing fees	49,778	57,128	**56,929**	7,350	15	(199)	—
Merchant banking fees	23,929	24,924	**31,402**	995	4	6,478	26
Foreign exchange trading gains, net	13,255	16,268	**19,527**	3,013	23	3,259	20
Brokerage commissions and fees	12,932	15,569	**19,085**	2,637	20	3,516	23
Gain on sale of credit card portfolio	—	—	**17,056**	—	—	17,056	nm
Securities gains, net	4,502	2,711	**5,686**	(1,791)	(40)	2,975	110
Other	52,718	58,105	**51,737**	5,387	10	(6,368)	(11)
Total noninterest income	$418,676	$463,001	**$533,531**	$44,325	11%	$70,530	15%

nm = not meaningful

Noninterest income in 1998 was $534 million, an increase of $71 million, or 15 percent, over 1997. This included a $24 million increase in service charges on deposit accounts, a $14 million increase in trust and investment management fees, a $6 million increase in both international commissions and fees and merchant banking fees, a $3 million increase in net foreign exchange trading gains, a $4 million increase in brokerage commissions and fees, a $17 million gain from the sale of the credit card portfolio in the second quarter of 1998 (see "Consumer Loans" on page 31), and a $3 million increase in net securities gains, partially offset by a $6 million decrease in other noninterest income.

Revenue from service charges on deposit accounts was $139 million, an increase of 21 percent over 1997. The increase was primarily attributable to a 3 percent increase in average deposits coupled with the expansion of several products and services.

Trust and investment management fees were $121 million, an increase of 13 percent over 1997. The increase was due to strong growth in trust accounts and assets under management, which resulted in higher mutual fund management fees.

International commissions and fees were $72 million, an increase of 9 percent over 1997. The increase was due to increases in export and import related short-term trade transactions.

Merchant banking fees were $31 million, an increase of 26 percent over 1997. The increase was due to the expansion of loan syndication activities by the Commercial Financial Services Group.

Net foreign exchange trading gains were $20 million, an increase of 20 percent over 1997, primarily due to more volatility in the foreign exchange markets in 1998.

Brokerage commissions and fees were $19 million, an increase of 23 percent over 1997. The increase was primarily attributable to brokerage commissions on non-proprietary mutual fund sales.

Management's Discussion and Analysis of Financial Condition and Results of Operations

Net securities gains were $6 million, an increase of 110 percent over 1997, primarily due to sales of securities available for sale.

Other noninterest income was $52 million, a decrease of 11 percent from 1997. The decrease was due to a $8 million nonrecurring gain recognized in 1997 related to a real estate joint venture and a $3 million trading loss recognized in the third quarter of 1998, arising from the decline in interest rates, partially offset by a $5 million gain recognized in the second quarter of 1998 from the sale of commercial real estate loans.

Noninterest Expense

				Increase (Decrease)			
				Amount	Percent	Amount	Percent
Years Ended December 31,	1996	1997	1998	1997 Versus 1996		1998 Versus 1997	
(Dollars in thousands)							
Salaries and other compensation	$ 448,793	$ 461,915	**$ 501,220**	$ 13,122	3%	$39,305	9%
Employee benefits	108,454	109,729	**116,344**	1,275	1	6,615	6
Personnel-related expense	557,247	571,644	**617,564**	14,397	3	45,920	8
Net occupancy	103,335	85,630	**90,917**	(17,705)	(17)	5,287	6
Equipment	55,942	56,137	**56,252**	195	—	115	—
Merchant transaction processing	37,091	42,274	**43,926**	5,183	14	1,652	4
Communications	40,133	42,372	**41,710**	2,239	6	(662)	(2)
Professional services	24,342	28,075	**36,748**	3,733	15	8,673	31
Advertising and public relations	28,788	28,664	**31,897**	(124)	—	3,233	11
Data processing	22,140	25,973	**28,091**	3,833	17	2,118	8
Printing and office supplies	27,085	24,098	**26,716**	(2,987)	(11)	2,618	11
Software	15,895	16,562	**20,969**	667	4	4,407	27
Travel	14,936	15,763	**18,080**	827	6	2,317	15
Intangible asset amortization	13,335	13,352	**13,581**	17	—	229	2
Armored car	13,296	12,209	**12,231**	(1,087)	(8)	22	—
Foreclosed asset expense (income)	2,889	(1,268)	**(2,821)**	(4,157)	nm	(1,553)	nm
Merger and integration expense	117,464	6,037	**—**	(111,427)	(95)	(6,037)	nm
Other	60,986	77,143	**99,357**	16,157	26	22,214	29
Total noninterest expense	$1,134,904	$1,044,665	**$1,135,218**	$ (90,239)	(8)%	$90,553	9%

nm = not meaningful

Noninterest expense in 1998 was $1.1 billion, an increase of $91 million, or 9 percent, over 1997. The increase was mostly due to a $46 million increase in personnel-related expense, a $5 million increase in net occupancy expense, a $9 million increase in professional services expense, a $4 million increase in software expense, and a $22 million increase in other noninterest expense, partially offset by a $6 million decrease in merger and integration expense.

Personnel-related expense was $618 million, an increase of 8 percent over 1997. This increase was due to a $22 million increase in performance- based incentive compensation and a $22 million increase in exempt base pay, due to regular merit increases and a 3 percent increase in workforce to support increased revenue growth.

Net occupancy expense was $91 million, an increase of 6 percent over 1997, primarily due to expenses related to lease terminations on several properties.

Professional services expense was $37 million, an increase of 31 percent over 1997, primarily due to consultant fees related to the year 2000 effort.

Software expense was $21 million, an increase of 27 percent over 1997, primarily due to increased software maintenance contracts and increased purchases of computer software products related to system upgrades at Union Bank of California, N.A.

Other noninterest expense was $99 million, an increase of 29 percent from 1997, primarily attributable to an increase of $8.3 million in expenses incurred to support

Management's Discussion and Analysis of Financial Condition and Results of Operations

higher deposit volumes and an increase of $8.2 million in other outside service expenses.

Merger and integration expense of $6 million was recorded in 1997, compared to no merger and integration expense in 1998. The merger resulted in the recording of $124 million in total merger and integration expense. The remaining liability balance at December 31, 1997 was $23 million, compared to $11 million at December 31, 1998. The remaining liability balance included amounts primarily for operating lease payments related to redundant banking facilities that are continuing over the expected term of the leases. See Note 7 to our Consolidated Financial Statements for further information.

We continue to make preparations for the year 2000. (See "Year 2000" on page 49 for a detailed discussion of the year 2000 program). We estimate that the total cost of our year 2000 project will be approximately $50 million, of which $10 million relates to capital expenditures which we will capitalize and depreciate over their useful lives. We will include the remaining $40 million in noninterest expense in the period incurred. As of December 31, 1998, we have spent $24 million on our year 2000 project, $2 million in 1997 and $22 million in 1998. Of the $24 million spent as of December 31, 1998, $6 million related to capital expenditures, $1 million in 1997 and $5 million in 1998. Of the estimated $26 million remaining to be spent, an estimated $4 million is expected to be for capital expenditures and $22 million is expected to be included in noninterest expense over the next two years. Of the $22 million to be included in noninterest expense, we have assumed that approximately $14 million will be spent on salaries and contract labor. This assumes that the current mix of internal staff and contract labor remains the same, the hours and the person-days needed to complete the projects are not materially exceeded, and that preparations for the year 2000 remain on schedule. The remaining $8 million is expected to relate to other operating expenses. We are funding the cost of our year 2000 project with normal operating cash and are staffing it with external resources as well as internal staff re-deployed from less time-sensitive assignments. Estimated total cost could change further as analysis continues.

Euro Conversion

On January 1, 1999, 11 European countries who joined the Economic and Monetary Union transitioned into a single currency (the Euro) and a single central bank, the European Central Bank. Beginning on that date, the exchange rates of the national currencies of the 11 countries became fixed and all financial transactions can now be settled in Euros.

We have completed our analysis of the bank-wide impact and have implemented a project plan that addresses the Euro conversion. We are now fully operational to settle transactions in the Euro.

Income Tax Expense

Years Ended December 31,	1996	1997	**1998**
(Dollars in thousands)			
Income before income taxes	$412,350	$650,018	**$671,536**
Income tax expense	162,892	238,722	**205,075**
Effective tax rate	40%	37%	**31%**

Our effective tax rate in 1997 was 37 percent compared with 31 percent in 1998. The lower 1998 effective tax rate was due to our ability to file our 1997 and 1998 California franchise tax returns on a worldwide unitary basis, incorporating the financial results of The Bank of Tokyo-Mitsubishi, Ltd. and its worldwide affiliates. As a result, we reduced our state income tax liabilities by $29 million, net of federal tax, for previously accrued 1997 state tax liabilities, and lowered our 1998 state tax provision by $31 million, net of federal tax. In 1997, we received an after-tax refund from the FTB of $25 million to settle litigation, administration, and audit disputes covering the years 1975-1987. In 1996, we recognized a $5 million after-tax benefit from a settlement with the FTB for 1985 and 1986. Excluding the income tax reductions and FTB refunds, the effective tax rates were 41 percent in 1996 and 1997, and 40 percent in 1998.

Credit Risk Management

Our principal business activity is the extension of credit in the form of loans or other credit substitutes to individuals and businesses. Our policies and applicable laws and regulations, governing the extension of credit, require risk analysis as well as ongoing portfolio and credit management through loan product diversification, lending limit constraints, credit review and approval policies, and extensive internal monitoring.

We manage and control credit risk through diversification of the portfolio by type of loan, industry concentration, dollar limits on multiple loans to the same borrower, geographic distribution and type of borrower. Geographic diversification of loans originated through our branch network is generally within California, Oregon and Washington, which we consider to be our principal markets. In addition, we will continue to originate and participate in lending activities outside these states, as well as internationally.

Management's Discussion and Analysis of Financial Condition and Results of Operations

In analyzing our existing loan portfolios, we apply specific monitoring policies and procedures that vary according to the relative risk profile and other characteristics of the loans within the various portfolios. Our residential and consumer loans are relatively homogeneous and no single loan is individually significant in terms of its size or potential risk of loss. Therefore, we review our residential and consumer portfolios by analyzing their performance as a pool of loans. In contrast, our monitoring process for the commercial, financial and industrial, construction, commercial mortgage, and foreign loan portfolios includes a periodic review of individual loans. Loans that are performing but have shown some signs of weakness are subjected to more stringent reporting and oversight. We review these loans to assess the ability of the borrowing entity to continue to service all of its interest and principal obligations and as a result may adjust the risk grade accordingly. In the event that we believe that full collection of principal and interest is not reasonably assured, the loan will be appropriately downgraded and, if warranted, placed on nonaccrual status, even though the loan may be current as to principal and interest payments.

We have a Credit Policy Forum, composed of the Chief Credit Officer, senior credit officers, and appropriate line officers, that establishes policy, credit quality criteria, portfolio guidelines and other controls. Credit Administration, together with a series of loan committees, have the responsibility for administering the credit approval process, as well as the implementation and administration of our credit policies and lending practices and procedures. These policies require an extensive evaluation of credit requests and continuing review of existing credits in order to promptly identify, monitor, and quantify evidence of deterioration of asset credit quality or potential loss.

As another part of the control process, an independent internal credit review and examination function provides quality assurance that loans and commitments are made and maintained as prescribed by our credit policies and that the assets are appropriately and timely risk graded. This includes a review of compliance with our underwriting policies when the loan is initially extended and subsequent on-site examinations to ensure continued compliance.

Loans

The following table shows loans outstanding by loan type and as a percentage of total loans for 1996 through 1998.

December 31,	1996		1997		**1998**	
(Dollars in millions)						
Domestic:						
Commercial, financial and industrial	$ 9,496	45%	$10,747	47%	**$13,120**	**54%**
Construction	358	2	293	1	**440**	**2**
Mortgage:						
Residential	2,961	14	2,961	13	**2,628**	**11**
Commercial	2,598	12	2,952	13	**2,975**	**12**
Total mortgage	5,559	26	5,913	26	**5,603**	**23**
Consumer:						
Installment	2,063	10	2,091	9	**1,985**	**8**
Home equity	1,113	5	993	5	**818**	**4**
Credit card and other lines of credit	303	1	270	1	**—**	**—**
Total consumer	3,479	16	3,354	15	**2,803**	**12**
Lease financing	800	4	875	4	**1,032**	**4**
Total loans in domestic offices	19,692	93	21,182	93	**22,998**	**95**
Loans originated in foreign branches	1,358	7	1,559	7	**1,298**	**5**
Total loans	$21,050	100%	$22,741	100%	**$24,296**	**100%**

Management's Discussion and Analysis of Financial Condition and Results of Operations

Our lending activities are predominantly domestic, with such loans comprising approximately 95 percent of the total loan portfolio at December 31, 1998. Total loans at December 31, 1998 were $24.3 billion, an increase of $1.6 billion, or 7 percent, from one year earlier. The increase from 1997 was primarily attributable to growth in the commercial, financial and industrial loan portfolio, which increased $2.4 billion, partially offset by the residential mortgage loan portfolio, which decreased $333 million, and by the consumer loan portfolio, which decreased $551 million.

Commercial, Financial and Industrial Loans

Commercial, financial and industrial loans represent the largest category in the loan portfolio. These loans are extended principally to major corporations, middle market businesses, and small businesses, with no industry concentration exceeding 10 percent of total commercial, financial and industrial loans.

Our commercial market lending originates primarily through our banking office network. These offices, which rely extensively on relationship-oriented banking, provide many services including cash management services, lines of credit, accounts receivable and inventory financing. Separately, we originate or participate in a wide variety of financial services to major corporations. These services include traditional commercial banking and specialized financing tailored to the needs of each customer's specific industry. Presently, we are active in the communications, media and entertainment, energy capital services, technology, healthcare, agribusiness, retailing and financial services industries.

At December 31, 1998, the commercial, financial and industrial loan portfolio was $13.1 billion, or 54 percent of the total loan portfolio. The increase of $2.4 billion, or 22 percent, from the previous year-end was primarily attributable to loans extended to businesses with revenues exceeding $20 million. The growth continued to reflect the results of initiatives to increase participation in larger syndicated loan positions as lead manager and as agent, especially in the communications, media, and entertainment and energy capital services industries in which we have developed specialized lending expertise. The increase in the communications, media, and entertainment business units over 1997 was $469 million, or 30 percent, and the increase over 1997 in the energy capital services units was $312 million, or 24 percent.

Construction and Commercial Mortgage Loans

We engage in non-residential real estate lending that includes commercial mortgage loans and construction loans secured by deeds of trust. Construction loans are made primarily to commercial property developers and to residential builders.

At December 31, 1998, the commercial real estate mortgage loan portfolio was $3.0 billion, or 12 percent of the total loan portfolio. Despite the sale of $123 million in commercial real estate mortgages during the second quarter of 1998, commercial mortgage loans slightly increased by $23 million, or 1 percent, from December 31, 1997, reflecting both the favorable California real estate market and the continued improvement in the West Coast economy.

At December 31, 1998, construction loans were $440 million, or 2 percent of the total loan portfolio. The increase of $147 million, or 50 percent, from the previous year-end was primarily attributable to the favorable California real estate market coupled with the continuing improvement in the West Coast economy.

Residential Mortgage Loans

We originate residential loans, secured by one-to-four family residential properties, through our branch network in California, Oregon and Washington, and periodically purchase loans in our market area.

At December 31, 1998, residential mortgage loans were $2.6 billion, or 11 percent of the total loan portfolio. The decrease of $333 million, or 11 percent, from December 31, 1997 was principally due to prepayments arising from the lower interest rate environment.

Consumer Loans

Through our auto dealer relationships and our branch network, we originate consumer loans, such as indirect and direct vehicle-secured installment loans, and home equity lines where advances are generally secured by second deeds of trust on residential real estate. In the second quarter of 1998, we sold our $253 million credit card portfolio to First National Bank of Omaha located in Nebraska.

At December 31, 1998, consumer loans were $2.8 billion, or 12 percent of the total loan portfolio. The decrease of $551 million, or 16 percent, from the previous year-end was attributable to the sale of the credit card portfolio and to a reduction in home equity loans as customers refinanced to take advantage of favorable long-term, fixed mortgage rates.

Lease Financing

We enter into direct financing and leveraged leases through an agreement with a subsidiary of The Bank of Tokyo-Mitsubishi, Ltd. In addition, we originate auto leases through

Management's Discussion and Analysis of Financial Condition and Results of Operations

our Consumer Asset Management division, a part of the Community Banking Group.

At December 31, 1998, lease financing outstandings were $1.0 billion, or 4 percent of the total loan portfolio. During 1998, management created new initiatives for lending, especially in the lease financing segment. This refocus on leasing resulted in a $157 million, or 18 percent, increase in lease financing over the prior year.

Loans Originated in Foreign Branches

Our loans originated in foreign branches consist primarily of short-term extensions of credit to financial institutions located primarily in Asia and to corporations in Japan, Korea and Taiwan.

At December 31, 1998, loans originated in foreign branches totaled $1.3 billion, or 5 percent of the total loan portfolio. The decrease of $261 million, or 17 percent, is attributable to the contraction of our exposure to key Asian markets, primarily Japan, Korea, Indonesia and Thailand, in response to the Asian economic crisis.

Cross-Border Outstandings

Our cross-border outstandings reflect certain additional economic and political risks that are not reflected in domestic outstandings. These risks include those arising from exchange rate fluctuations and restrictions on the transfer of funds. The following table sets forth our cross-border outstandings as of December 31, 1996, 1997 and 1998 for each country where such outstandings exceeded 1 percent of total assets. The cross-border outstandings were compiled based upon category and domicile of ultimate risk and are comprised of balances with banks, trading account assets, securities available for sale, securities purchased under resale agreements, loans, accrued interest receivable, acceptances outstanding and investments with foreign entities. The amounts outstanding for each country exclude local currency outstandings. For those individual countries shown in the table below, we do not have significant local currency outstandings that are not hedged or are not funded by local currency borrowings.

(Dollars in millions)	Financial Institutions	Public Sector Entities	Corporations and Other Borrowers	Total Outstandings
December 31, 1996				
Japan	$1,373	$—	$452	$1,825
Korea	574	8	330	912
December 31, 1997				
Japan	401	—	438	839
Korea	561	10	257	828
Thailand	320	—	—	320
December 31, 1998				
Japan	173	—	464	637
Korea	448	1	117	566

The economic condition and the ability of some countries, to which we have cross-border exposure, to manage their external debt obligations have been impacted by the Asian economic crisis that began in the second half of 1997. The Asian economic crisis appears to have stabilized somewhat, though the impact of the crisis on other global markets is still uncertain. Our exposure in all affected countries continues to be primarily short-term in nature and substantially related to the finance of trade. For further discussion on the actions taken by management to reduce our credit exposure in Asia and Latin America, see "Allowance for Credit Losses" on the following page.

Provision for Credit Losses

We recorded a $40 million provision for credit losses in 1996, compared with no provision for credit losses in 1997 and a $45 million provision for credit losses in 1998. Provisions for credit losses are charged to income to bring our allowance for credit losses to a level deemed appropriate by management based on the factors discussed under "Allowance for Credit Losses" on the following page. No provision for credit losses was recorded in 1997 because, based on our review of such factors, management believed that the allowance for credit losses was adequate to cover probable losses inherent in the loan portfolio and firm

Management's Discussion and Analysis of Financial Condition and Results of Operations

commitments at each quarter end, including December 31, 1997. We resumed recording provisions in 1998 in order to bring our allowance for credit losses to a level deemed appropriate by management based upon management's application of the allowance methodology.

Allowance for Credit Losses

The following table reflects the allowance allocated to each respective loan category at period end and as a percentage of the total period end balance of that loan category, as set forth in the "Loans" table on page 30.

December 31,	1996		1997		**1998**	
(Dollars in millions)						
Domestic:						
Commercial, financial, and industrial	$166,100	1.75%	$123,610	1.15%	**$145,100**	**1.11%**
Construction	5,700	1.59	3,221	1.10	**5,500**	**1.25**
Mortgage:						
Residential	4,000	0.14	2,700	0.09	**1,100**	**0.04**
Commercial	39,000	1.50	60,680	2.06	**17,500**	**0.59**
Total mortgage	43,000	0.77	63,380	1.07	**18,600**	**0.33**
Consumer:						
Installment	10,400	0.50	11,400	0.55	**20,900**	**1.05**
Home equity	4,900	0.44	3,600	0.36	**3,800**	**0.46**
Credit card and other lines of credit	34,000	11.22	30,500	11.30	**—**	**—**
Total consumer	49,300	1.42	45,500	1.36	**24,700**	**0.88**
Lease financing	5,300	0.66	4,862	0.56	**3,800**	**0.37**
Total domestic allowance	269,400	1.37	240,573	1.14	**197,700**	**0.86**
Foreign allowance	9,394	0.69	39,313	2.52	**47,000**	**3.62**
Unallocated	245,152		171,806		**214,628**	
Total allowance for credit losses	$523,946	2.49%	$451,692	1.99%	**$459,328**	**1.89%**

Reserve Policy and Methodology

We maintain an allowance for credit losses to absorb losses inherent in the loan portfolio. The allowance is based on ongoing, quarterly assessments of the probable estimated losses inherent in the loan portfolio, and to a lesser extent, unused commitments to provide financing. Our methodology for assessing the appropriateness of the allowance consists of several key elements, which include the formula allowance, specific allowances for identified problem loans and portfolio segments and the unallocated allowance.

The formula allowance is calculated by applying loss factors to outstanding loans and certain unused commitments, in each case based on the internal risk grade of such loans, pools of loans, leases or commitments. Changes in risk grades of both performing and nonperforming loans affect the amount of the formula allowance. Loss factors are based on our historical loss experience and may be adjusted for significant factors that, in management's judgment, affect the collectibility of the portfolio as of the evaluation date. Loss factors are described as follows:

- Problem graded loan loss factors are derived from a migration model that tracks four years of historical loss experience. We are exploring changes to the migration model to track historical loss experience over an eight-year period, which management believes approximates a business cycle.
- Pass graded loan loss factors are based on the average annual net chargeoff rate over an eight-year period.
- Pooled loan loss factors (not individually graded loans) are based on expected net chargeoffs for one year. Pooled loans are loans that are homogeneous in nature, such as consumer installment and residential mortgage loans and automobile leases.

Specific allowances are established in cases where management has identified significant conditions or circumstances related to a credit that management believes

Management's Discussion and Analysis of Financial Condition and Results of Operations

indicate the probability that a loss has been incurred in excess of the amount determined by the application of the formula allowance.

The unallocated allowance is composed of two elements. The first element, which is based on our credit policy, consists of an amount that is at least 20 percent to 25 percent of the formula allowance and the specific allowance. This element recognizes the model and estimation risk associated with the formula and specific allowances. The second element is based upon management's evaluation of various conditions, the effects of which are not directly measured in the determination of the formula and specific allowances. The evaluation of the inherent loss with respect to these conditions is subject to a higher degree of uncertainty because they are not identified with specific problem credits or portfolio segments. The conditions evaluated in connection with the unallocated allowance include the following conditions that existed as of the balance sheet date:

- general economic and business conditions affecting our key lending areas,
- credit quality trends (including trends in nonperforming loans expected to result from existing conditions),
- collateral values,
- loan volumes and concentrations,
- seasoning of the loan portfolio,
- specific industry conditions within portfolio segments,
- recent loss experience in particular segments of the portfolio,
- duration of the current business cycle,
- bank regulatory examination results, and
- findings of our internal credit examiners.

Executive management reviews these conditions quarterly in discussion with our senior credit officers. To the extent that any of these conditions is evidenced by a specifically identifiable problem credit or portfolio segment as of the evaluation date, management's estimate of the effect of such condition may be reflected as a specific allowance applicable to such credit or portfolio segment. Where any of these conditions is not evidenced by a specifically identifiable problem credit or portfolio segment as of the evaluation date, management's evaluation of the probable loss related to such condition is reflected in the unallocated allowance.

The allowance for credit losses is based upon estimates of probable losses inherent in the loan portfolio. The amount actually observed in respect of these losses can vary significantly from the estimated amounts. Our methodology includes several features that are intended to reduce the differences between estimated and actual losses. The loss migration model that is used to establish the loan loss factors for problem graded loans is designed to be self-correcting by taking into account our recent loss experience. Similarly, by basing the pass graded loan loss factors on loss experience over the last eight years, the methodology is designed to take our recent loss experience into account. Pooled loan loss factors are adjusted quarterly based upon the level of net chargeoffs expected by management in the next twelve months. Furthermore, our methodology permits adjustments to any loss factor used in the computation of the formula allowance in the event that, in management's judgment, significant factors which affect the collectibility of the portfolio as of the evaluation date are not reflected in the loss factors. By assessing the probable estimated losses inherent in the loan portfolio on a quarterly basis, we are able to adjust specific and inherent loss estimates based upon any more recent information that has become available.

Comparison of the Total Allowance and Related Provision for Credit Losses

At December 31, 1996, our allowance for credit losses was $524 million, or 2.49 percent of the total loan portfolio, and 408 percent of total nonaccrual loans. This compares with an allowance for credit losses of $452 million, or 1.99 percent of the total loan portfolio, and 413 percent of total nonaccrual loans at December 31, 1997, and an allowance for credit losses of $459 million, or 1.89 percent of the total loan portfolio, and 586 percent of total nonaccrual loans at December 31, 1998.

In 1998, we reclassified a $1.9 million previously established allowance for credit losses related to interest rate derivatives and foreign exchange contracts from the unallocated portion of the allowance for credit losses. The reserve for derivative and foreign exchange contracts is presented as an offset to trading account assets. Future changes in that reserve as a result of changes in the positive replacement cost of those contracts will be provided as an offset to trading gains and losses.

In addition, the allowance incorporates the results of measuring impaired loans as provided in Statement of Financial Accounting Standards (SFAS) No. 114, "Accounting by Creditors for Impairment of a Loan" and SFAS No. 118, "Accounting by Creditors for Impairment of a Loan—Income

Management's Discussion and Analysis of Financial Condition and Results of Operations

Recognition and Disclosures". These accounting standards prescribe the measurement methods, income recognition and disclosures related to impaired loans. At December 31, 1996, total impaired loans were $114 million and the associated impairment allowance was $21 million, compared with $108 million and $9 million, respectively, at December 31, 1997, and $78 million and $11 million, respectively, at December 31, 1998.

During 1997 and 1998, there were no changes in estimation methods or assumptions that affected our methodology for assessing the appropriateness of the allowance for credit losses, except that we extended the average annual net chargeoff rate for pass graded loans from 4.75 years in 1996 to 6 years in 1997 and to 8 years in 1998. The impact of these changes resulted in an increase of approximately $13 million and $19 million in the formula allowance in 1997 and 1998, respectively. We extended the average annual net chargeoff rate to better reflect the business cycle. Changes in assumptions regarding the effects of economic and business conditions on borrowers and other factors, which are described below, affected the assessment of the unallocated allowance. In addition, as described below, we allocated a portion of the unallocated allowance to foreign loans amid concerns that the Asian financial turmoil had adversely impacted companies and financial institutions in Asian markets in which we operate.

We did not record a provision for credit losses during 1997. The decision not to record a provision was based upon management's application of the allowance methodology as previously described and other factors, particularly the level of net chargeoffs and the decline in the level of nonperforming loans. Although management determined that no provision for credit losses was necessary in 1997, it noted that certain factors could necessitate the resumption of provisioning in the future. In particular, management noted that although net chargeoffs were relatively stable from 1996 to 1997, net chargeoffs steadily increased in each of the last three quarters of 1997. Furthermore, management noted that although the level of net chargeoffs and the decline in nonperforming loans favorably impacted our asset quality ratios, the total portfolio of commercial, financial and industrial loans and commercial mortgage loans was increasing. Losses inherent in both of these types of credits are more difficult to assess because historically they have been more volatile than losses from other credits.

Management also considered the effect on global economic conditions of the Asian financial crisis. At December 31, 1997, cross-border loans and acceptances to Japan, Korea, Malaysia, Thailand, Vietnam, Singapore, Indonesia, the Philippines, China, Taiwan and Hong Kong totaled $2.1 billion. Although at December 31, 1997, we had not identified any specific losses related to our Asia/Pacific exposures, management believed that it was probable that the Asian financial turmoil had adversely impacted companies and financial institutions in Asia/Pacific markets in which we operate. In light of this concern, we allocated $29 million from the unallocated portion of the allowance at December 31, 1997 to foreign loans. The allocated amount was based upon the total amount of foreign loans to corporate borrowers in Asian countries, and management's assessment of the quantified losses inherent in the Asia/Pacific portfolio segment. In addition, we believed that the historical loss factors for the Asia/Pacific exposures failed to estimate the total probable inherent losses because we had not suffered any credit losses in the foreign loan portfolio during the four-year historical loss cycle used to establish the problem loan loss factors. Based upon this concern, as well as the magnitude of our exposure to the Asia/Pacific segment, management did not believe that the $29 million allocated to foreign loans was sufficient to cover all of the losses inherent in the foreign loan portfolio and, accordingly, these factors were considered by management in its overall assessment of the unallocated allowance at December 31, 1997. During the first quarter of 1998, we changed the method of determining the quantified losses on Asia/Pacific loans from one based on total corporate exposure in the segment to one based on total country exposure to countries receiving assistance from the International Monetary Fund. This change resulted in a $9 million decrease in the allowance allocated to foreign loans.

In addition to the impact of the Asian financial turmoil on companies and financial institutions in Asian markets in which we operate, management considered the effects of the Asian turmoil on companies and financial institutions in the domestic (primarily California) and foreign (other than Asia/Pacific) markets in which we operate. As of December 31, 1997, management believed that the impact of the Asian financial turmoil on the collectibility of loans to domestic and foreign (non-Asia/Pacific) borrowers was not generally reflected in the level of nonperforming loans or in the internal risk grading process with respect to such loans.

Management's Discussion and Analysis of Financial Condition and Results of Operations

Accordingly, our evaluation of these probable losses was reflected in the unallocated allowance at December 31, 1997. The evaluations of these inherent losses were subject to higher degrees of uncertainty because they were not identified with specific problem credits.

In our assessment as of December 31, 1998, management focused, in particular, on factors affecting elements of the oil and gas, agriculture and technology industries, as well as the continued effects of the global financial turmoil on companies and financial institutions in domestic and foreign markets in which we operate and the growth in, and changes in the composition of, the loan portfolio.

- With respect to the oil and gas industry, where we had $719 million of loans outstanding at December 31, 1998, management considered the effects of the decline in oil prices on the cash flows of borrowers in the oil and gas industry.
- With respect to the agriculture industry, where we had $541 million of loans outstanding at December 31, 1998, management considered the effects of abnormal weather conditions (commonly referred to as "El Nino") and export market conditions on agricultural borrowers.
- With respect to the technology industry, where we had $913 million of loans outstanding at December 31, 1998, management considered the effects of export market conditions and cyclical over-capacity on borrowers in the chip and semiconductor industries.
- With respect to cross-border loans and acceptances to Japan, Korea, Malaysia, Thailand, Singapore, Indonesia, the Philippines, China, Taiwan and Hong Kong, where we had outstandings of $1.7 billion at December 31, 1998, management considered the continued effects of the global financial turmoil.
- With respect to cross-border loans and acceptances to Latin American countries, where we had outstandings of $255 million at December 31, 1998, management considered the continued effects of the global financial turmoil.

Although in certain instances the downgrading of a loan resulting from these effects was reflected in the formula allowance, management believed that in most instances the impact of these events on the collectibility of the applicable loans was not reflected in the level of nonperforming loans or in the internal risk grading process with respect to such loans. Accordingly, our evaluation of the probable losses related to these factors was reflected in the unallocated allowance. The evaluations of the inherent losses with respect to these factors were subject to higher degrees of uncertainty because they were not identified with specific problem credits.

Changes in the Formula, Specific and Unallocated Allowances

The following table sets forth the composition of the allowance for credit losses.

December 31,	1996	1997	**1998**
(Dollars in millions)			
Allocated allowance:			
Formula	$237	$212	**$206**
Specific	42	68	**38**
Total allocated allowance	279	280	**244**
Unallocated allowance	245	172	**215**
Total allowance	$524	$452	**$459**

At December 31, 1997, the formula allowance decreased by $25 million from the prior year, primarily due to a reduction in the level of criticized loans and the reflection of lower historical losses in the loss factors, partially offset by loan growth, by changes to conform the various risk grade definitions after the combination of Bank of California and Union Bank, and by the extension of the average annual net chargeoff rate for pass graded loans as previously described. At December 31, 1998, the formula allowance decreased by $6 million from the prior year, primarily due to a decline in criticized credits, offset by the extension of the average annual net chargeoff rate for pass graded loans as previously described.

At December 31, 1997, the specific allowance increased by $26 million over the prior year, primarily due to the reallocation for the Asian exposure as previously described. At December 31, 1998, the specific allowance decreased by $30 million from the prior year due to the sale of real estate notes and the change related to foreign loans as previously described.

At December 31, 1996, the allocated portion of the allowance for credit losses included $134 million related to special mention and classified credits, compared to $108 million at December 31, 1997 and $76 million at December 31, 1998. Special mention and classified credits are those that are internally risk graded as "special mention", "substandard" or "doubtful". Special mention credits are potentially weak, as the borrower has begun to exhibit deteriorating trends which, if not corrected, could jeopardize repayment of the loan and result in further downgrade. Substandard credits have well-defined weaknesses which, if not corrected, could jeopardize the full satisfaction of the debt. A credit classified as "doubtful" has critical weaknesses that make full collection improbable.

Management's Discussion and Analysis of Financial Condition and Results of Operations

At December 31, 1997, the unallocated allowance decreased by $73 million from the previous year-end because management believed that the inherent losses related to certain conditions considered in its evaluation of the unallocated allowance at December 31, 1996 had been recognized through chargeoffs, had been reflected in the formula or specific allowance or had declined. From December 31, 1996 to December 31, 1997, there was no change in the component of the unallocated allowance related to the 20 percent to 25 percent margin for model and estimation risk prescribed by our credit policy. Included among those conditions that management believed gave rise to lower inherent losses at December 31, 1997 compared to December 31, 1996 were:

- reduced concerns regarding the lingering effects of the California recession on, and the sustainability of the recovery in, the California commercial real estate and construction market,
- reduced concerns regarding consumer debt burdens and rising levels of consumer bankruptcies,
- resolution of uncertainties related to assimilating data for the formula allowance that resulted from combining the loan portfolios of Bank of California and Union Bank and inconsistencies in the risk grading systems of our predecessor banks,
- reduced concerns related to consolidation and restructuring in the retail industry, and
- reduced concerns regarding the sustainability of perceived improvements in economic conditions.

We do not weight the unallocated allowance among segments of the portfolio. At December 31, 1996, we had a $245 million unallocated allowance in our allowance for credit losses. In evaluating the appropriateness of the unallocated allowance, we considered the following factors:

- the approximately $56 million to $70 million margin for model and estimation risk prescribed by our credit policy,
- the lingering effects of the California recession on, and the sustainability of the recovery in, the California commercial real estate and construction market, which could be in the range of $45 million to $70 million,
- the effects of consumer debt burdens and rising levels of consumer bankruptcies, which could be in the range of $25 million to $40 million,
- the effects of uncertainties related to assimilating data for the formula allowance that resulted from combining the loan portfolios of Bank of California and Union Bank and inconsistencies in the risk grading systems of our predecessor banks, which could be in the range of $15 million to $30 million,
- the effects of consolidation and restructuring in the retail industry, which could be in the range of $5 million to $10 million, and
- the effects of adverse economic and business conditions in Japan, which could be in the range of $5 million to $10 million.

At December 31, 1997, we had a $172 million unallocated allowance in our allowance for credit losses. The following factors were reflected in management's estimate of the unallocated allowance:

- the approximately $56 million to $70 million margin for model and estimation risk prescribed by our credit policy and
- our estimate that the adverse impact of the Asian financial turmoil on us could be in the range of $100 million to $105 million.

At December 31, 1998, we had a $215 million unallocated allowance in our allowance for credit losses. The following factors were reflected in management's estimate of the unallocated allowance:

- the approximately $49 million to $61 million margin for model and estimation risk prescribed by our credit policy,
- the effects of the decline in oil prices on borrowers in the oil and gas industry, which could be in the range of $14 million to $22 million,
- the effects of abnormal weather conditions and export market conditions on agricultural borrowers, which could be in the range of $11 million to $16 million,
- the effects of export market conditions and cyclical over-capacity on borrowers in the technology industry, which could be in the range of $18 million to $27 million,
- the continued effects of the global financial turmoil on borrowers in Asia/Pacific countries, which could be in the range of $55 million to $80 million, and
- the continued effects of the global financial turmoil on borrowers in Latin American countries, which could be in the range of $10 million to $15 million.

There can be no assurance that the adverse impact of any of these conditions on us will not be in excess of the range set forth above. See paragraph on forward-looking statements on page 18.

Despite the foregoing factors, management reduced the size of the provision in each of the quarters of 1998 based upon certain mitigating factors, including the continued decline in the level of nonperforming loans, the lower levels of net chargeoffs, the sale of the credit card portfolio in the second quarter of 1998, the real estate note sales and the results of our efforts to limit our exposure and counterparty risk in Asia.

Management's Discussion and Analysis of Financial Condition and Results of Operations

Change in the Total Allowance for Credit Losses

The following table sets forth a reconciliation of changes in our allowance for credit losses.

Years Ended December 31,	1996	1997	**1998**
(Dollars in thousands)			
Balance, beginning of period	$555,149	$523,946	**$451,692**
Loans charged off:			
Commercial, financial and industrial	42,134	58,664	**38,219**
Construction	3,249	120	**3**
Mortgage	13,483	5,058	**6,547**
Consumer	56,361	55,336	**29,312**
Lease financing	2,623	3,601	**2,709**
Foreign[1]	1,250	—	**—**
Total loans charged off	119,100	122,779	**76,790**
Recoveries of loans previously charged off:			
Commercial, financial and industrial	22,341	23,371	**23,762**
Construction	132	9,054	**3**
Mortgage	12,277	3,292	**2,857**
Consumer	12,906	14,946	**14,021**
Lease financing	368	351	**501**
Foreign[1]	—	—	**—**
Total recoveries of loans previously charged off	48,024	51,014	**41,144**
Net loans charged off	71,076	71,765	**35,646**
Provision for credit losses	40,000	—	**45,000**
Transfer of reserve for trading account assets	—	—	**(1,911)**
Foreign translation adjustment and other net additions (deductions)	(127)	(489)	**193**
Balance, end of period	$523,946	$451,692	**$459,328**
Allowance for credit losses to total loans	2.49%	1.99%	**1.89%**
Provision for credit losses to net loans charged off	56.28	nm	**126.24**
Recoveries of loans to loans charged off in the previous year	35.95	42.83	**33.51**
Net loans charged off to average loans outstanding	0.34	0.33	**0.15**

[1] Foreign loans are those loans originated in foreign branches.

nm = not meaningful

Loans charged off in 1997 increased by $4 million over 1996, primarily due to a $17 million increase in commercial, financial and industrial loans charged off, partially offset by an $8 million decrease in mortgage loans charged off. Loans charged off in 1998 decreased by $46 million, primarily due to a $20 million decrease in commercial, financial and industrial loans charged off as portfolio quality improved, and a $26 million decrease in consumer loans charged off, primarily due to the sale of the credit card portfolio in the second quarter of 1998. Chargeoffs reflect the realization of losses in the portfolio that were recognized previously through provisions for credit losses. Recoveries of loans previously charged off in 1997 increased by $3 million over 1996, and the percentage of current year recoveries to loans charged off in the previous year increased from 35.95 percent in 1996 to 42.83 percent in 1997. Recoveries of loans previously charged off in 1998 decreased by $10 million from 1997, and the percentage of current year recoveries to loans charged off in the previous year decreased from 42.83 percent in 1997 to 33.51 percent in 1998. At December 31, 1998, the allowance for credit losses exceeded the net loans charged off during 1998, reflecting management's belief, based on the foregoing analysis, that there were additional losses inherent in the portfolio.

At December 31, 1996, our average annual net chargeoffs for the past five years were $166 million, compared with $131 million at December 31, 1997 and $88 million at December 31, 1998. These net chargeoffs represent 3.1 years, 3.4 years

Management's Discussion and Analysis of Financial Condition and Results of Operations

and 5.2 years of losses based on the level of the allowance for credit losses at December 31, 1996, 1997 and 1998, respectively. Historical net chargeoffs are not necessarily indicative of the amount of net chargeoffs that we will realize in the future.

Nonperforming Assets

Nonperforming assets consist of nonaccrual loans, renegotiated loans, and foreclosed assets. Nonaccrual loans are those for which management has discontinued accrual of interest because there exists significant uncertainty as to the full and timely collection of either principal or interest or such loans have become contractually past due 90 days with respect to principal or interest. For a more detailed discussion of the accounting for nonaccrual loans, see Note 1 to our Consolidated Financial Statements.

Renegotiated loans are those accruing loans for which, for reasons related to the borrower's financial difficulties, we have amended the terms of the original loan agreement and the borrower is performing according to the renegotiated terms.

Foreclosed assets include property where we acquired title through foreclosure or "deed in lieu" of foreclosure. On an ongoing basis, foreclosed asset values are reviewed and any decline in value is recognized as noninterest expense in the current period.

The following table sets forth an analysis of nonperforming assets.

December 31,	1996	1997	**1998**
(Dollars in thousands)			
Commercial, financial and industrial	$ 56,864	$ 46,392	**$ 60,703**
Construction	7,349	4,071	**4,359**
Mortgage:			
Residential	11,214	954	**—**
Commercial	52,593	57,921	**8,254**
Total mortgage	63,807	58,875	**8,254**
Other	247	—	**5,134**
Total nonaccrual loans	128,267	109,338	**78,450**
Renegotiated loans	—	—	**—**
Foreclosed assets	28,517	20,471	**11,400**
Total nonperforming assets	156,784	129,809	**89,850**
Allowance for credit losses	$523,946	$451,692	**$459,328**
Nonaccrual and renegotiated loans to total loans	0.61%	0.48%	**0.32%**
Allowance for credit losses to nonaccrual loans	408.48	413.12	**585.50**
Nonperforming assets to total loans and foreclosed assets	0.74	0.57	**0.37**
Nonperforming assets to total assets	0.54	0.42	**0.28**

The following table sets forth an analysis of loans contractually past due 90 days or more as to interest or principal, but not included in nonaccrual loans above.

December 31,	1996	1997	**1998**
(Dollars in thousands)			
Commercial, financial and industrial	$ 4,527	$ 450	**$ 913**
Construction	—	—	**—**
Mortgage:			
Residential	8,969	10,170	**9,338**
Commercial	168	1,660	**13,955**
Total mortgage	9,137	11,830	**23,293**
Consumer and other	10,028	7,712	**7,292**
Total loans 90 days or more past due and still accruing	$23,692	$19,992	**$31,498**

Management's Discussion and Analysis of Financial Condition and Results of Operations

At December 31, 1998, nonperforming loans totaled $90 million, a decrease of $40 million, or 31 percent, from year-end 1997. The decrease was primarily the result of reductions of $50 million in nonaccrual commercial mortgage loans, due to third quarter 1998 note sales totaling $30 million, repayments and restorations to accrual status, and $9 million in foreclosed assets, due to sales of individual assets, partially offset by a $14 million increase in nonaccrual commercial, financial and industrial loans, due to the placement on nonaccrual status of a few large loans made to upper-middle market and large businesses. The decline in nonaccrual loans was reflected in an improvement in the overall risk grades of the portfolio, which contributed to a reduction in the formula allowance.

Nonaccrual and renegotiated loans as a percentage of total loans were 0.48 percent at December 31, 1997 compared with 0.32 percent at December 31, 1998. Nonperforming assets as a percentage of total loans and foreclosed assets improved to 0.37 percent at year-end 1998 from 0.57 percent at December 31, 1997. At December 31, 1998, approximately 77 percent of nonaccrual loans were related to commercial, financial and industrial.

Total loans 90 days or more past due and still accruing were $20 million at December 31, 1997 compared with $31 million at December 31, 1998.

Interest Foregone

Interest foregone during 1997 and 1998 for loans that were on nonaccrual status at December 31, 1997 and 1998 was $6 million and $4 million, respectively. We recognized interest income of $3 million during 1997 for loans that were on nonaccrual status at December 31, 1997. We recognized no interest income during 1998 for loans that were on nonaccrual status at December 31, 1998.

Securities

The following tables summarize the composition of the securities portfolio and the gross unrealized gains and losses within the portfolio.

Securities Available for Sale

December 31,	1996	1997				1998			
	Fair Value	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	**Amortized Cost**	**Gross Unrealized Gains**	**Gross Unrealized Losses**	**Fair Value**
(Dollars in thousands)									
U.S. Treasury	$1,141,052	$ 987,374	$10,793	$ 170	$ 997,997	**$ 753,991**	**$16,341**	**$ —**	**$ 770,332**
Other U.S. government	691,931	709,536	6,005	67	715,474	**856,463**	**12,364**	**—**	**868,827**
Mortgage-backed securities	193,657	679,692	3,331	265	682,758	**1,875,141**	**9,271**	**2,634**	**1,881,778**
State and municipal	114,755	90,937	13,236	—	104,173	**72,777**	**11,469**	**—**	**84,246**
Corporate debt securities	—	2,698	311	1	3,008	**8,069**	**—**	**—**	**8,069**
Equity securities	21,594	28,881	1,596	672	29,805	**18,149**	**252**	**—**	**18,401**
Foreign securities	1,208	5,132	39	—	5,171	**6,799**	**121**	**41**	**6,879**
Total securities available for sale	$2,164,197	$2,504,250	$35,311	$1,175	$2,538,386	**$3,591,389**	**$49,818**	**$2,675**	**$3,638,532**

Securities Held to Maturity

December 31,	1996	1997				1998			
	Amortized Cost	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	**Amortized Cost**	**Gross Unrealized Gains**	**Gross Unrealized Losses**	**Fair Value**
(Dollars in thousands)									
U.S. Treasury	$ 50,109	$ 40,092	$1,333	$ —	$ 41,425	**$ 40,047**	**$1,050**	**$ —**	**$ 41,097**
Other U.S. government	139,188	99,520	2,568	—	102,088	**89,783**	**1,392**	**—**	**91,175**
Mortgage-backed securities	41,985	24,477	1,745	14	26,208	**15,247**	**1,178**	**—**	**16,425**
State and municipal	36,914	24,686	75	1,367	23,394	**15,436**	**4**	**893**	**14,547**
Total securities held to maturity	$268,196	$188,775	$5,721	$1,381	$193,115	**$160,513**	**$3,624**	**$893**	**$163,244**

Management's Discussion and Analysis of Financial Condition and Results of Operations

Management of the securities portfolio involves the maximization of return while maintaining prudent levels of quality and liquidity. At December 31, 1998, approximately 99 percent of total securities were investment grade.

Analysis of Securities Portfolio

The following tables show the remaining contractual maturities and expected yields of the securities portfolio at December 31, 1998.

Securities Available for Sale

	Maturity									
	One Year or Less		Over One Year Through Five Years		Over Five Years Through Ten Years		Over Ten Years		Total Amortized Cost	
(Dollars in thousands)	Amount	Yield[4]	Amount	Yield[4]	Amount	Yield[4]	Amount	Yield[4]	Amount	Yield[4]
U.S. Treasury	$328,946	6.24%	$ 425,045	6.47%	$ —	—%	$ —	—%	$ 753,991	6.37%
Other U.S. government	315,010	6.25	491,453	6.19	50,000	5.50	—	—	856,463	6.17
Mortgage-backed securities[1]	1,287	6.23	99,193	6.36	269,879	6.24	1,504,782	6.05	1,875,141	6.09
State and municipal[2]	12,085	9.10	15,209	10.13	15,052	10.86	30,431	11.40	72,777	10.64
Corporate debt securities	—	—	1,189	17.37	6,880	15.32	—	—	8,069	15.62
Equity securities[3]	—	—	—	—	—	—	—	—	18,149	—
Foreign securities	—	—	5,106	0.21	1,693	6.04	—	—	6,799	1.66
Total securities available for sale	$657,328	6.30%	$1,037,195	6.36%	$343,504	6.52%	$1,535,213	6.16%	$3,591,389	6.28%

Securities Held to Maturity

	Maturity									
	One Year or Less		Over One Year Through Five Years		Over Five Years Through Ten Years		Over Ten Years		Total Amortized Cost	
(Dollars in thousands)	Amount	Yield[4]	Amount	Yield[4]	Amount	Yield[4]	Amount	Yield[4]	Amount	Yield[4]
U.S. Treasury	$ 40,047	7.56%	$ —	—%	$ —	—%	$ —	—%	$ 40,047	7.56%
Other U.S. government	69,782	7.74	20,001	7.68	—	—	—	—	89,783	7.73
Mortgage-backed securities[1]	—	—	1,162	9.08	5,759	9.00	8,326	9.05	15,247	9.03
State and municipal[2]	—	—	930	7.31	2,990	5.71	11,516	5.76	15,436	5.84
Total securities held to maturity	$109,829	7.67%	$22,093	7.74%	$8,749	7.88%	$19,842	7.14%	$160,513	7.63%

(1) The remaining contractual maturities of mortgage-backed securities were allocated assuming no prepayments. The contractual maturity of these securities is not a reliable indicator of their expected life because borrowers have the right to repay their obligations at any time.

(2) Yields on tax-exempt municipal securities are presented on a taxable- equivalent basis using the current federal statutory rate of 35 percent.

(3) Equity securities do not have a stated maturity and are included in the total column only.

(4) Yields are based on amortized cost.

Management's Discussion and Analysis of Financial Condition and Results of Operations

Loan Maturities

The following table presents our loans by maturity.

December 31, 1998	One Year or Less	Over One Year Through Five Years	Over Five Years	Total
(Dollars in thousands)				
Domestic:				
Commercial, financial and industrial	$5,924,641	$5,790,572	$1,404,321	$13,119,534
Construction	255,840	178,424	5,542	439,806
Mortgage:				
Residential	60,126	261,155	2,306,387	2,627,668
Commercial	644,536	1,395,649	935,299	2,975,484
Total mortgage	704,662	1,656,804	3,241,686	5,603,152
Consumer:				
Installment	509,602	1,040,794	434,545	1,984,941
Home equity	106,964	415,048	296,187	818,199
Total consumer	616,566	1,455,842	730,732	2,803,140
Lease financing	383,105	649,043	—	1,032,148
Total loans in domestic offices	7,884,814	9,730,685	5,382,281	22,997,780
Loans originated in foreign branches	1,229,554	67,264	1,513	1,298,331
Total loans	$9,114,368	$9,797,949	$5,383,794	$24,296,111
Allowance for credit losses				459,328
Loans, net				$23,836,783
Total fixed rate loans due after one year				$ 5,060,580
Total variable rate loans due after one year				10,121,163
Total loans due after one year				$15,181,743

Certificates of Deposit of $100,000 and Over

The following table presents domestic certificates of deposit of $100,000 and over by maturity.

December 31,	1998
(Dollars in thousands)	
Three months or less	$2,543,176
Over three months through six months	961,179
Over six months through twelve months	211,750
Over twelve months	109,603
Total domestic certificates of deposit of $100,000 and over	$3,825,708

We offer certificates of deposit of $100,000 and over at market rates of interest. Many of these certificates are issued to customers, both public and private, who have done business with us for an extended period. We expect that as these deposits come due, the majority will continue to be renewed at market rates of interest.

Substantially all of our deposits in foreign branches are certificates of deposit of $100,000 and over and mature in less than one year.

Management's Discussion and Analysis of Financial Condition and Results of Operations

Borrowed Funds

The following table presents information on our borrowed funds.

December 31,	1996	1997	**1998**
(Dollars in thousands)			
Federal funds purchased and securities sold under repurchase agreements with weighted average interest rates of 5.09%, 5.38% and 4.88% at December 31, 1996, 1997 and 1998, respectively	$1,322,654	$1,335,884	**$1,307,744**
Commercial paper, with weighted average interest rates of 5.34%, 5.64% and 5.01% at December 31, 1996, 1997 and 1998, respectively	1,495,463	966,575	**1,444,745**
Other borrowed funds, with weighted average interest rates of 5.66%, 6.23% and 5.35% at December 31, 1996, 1997 and 1998, respectively	749,422	476,010	**331,165**
Total borrowed funds	$3,567,539	$2,778,469	**$3,083,654**
Federal funds purchased and securities sold under repurchase agreements:			
Maximum outstanding at any month end	$1,322,654	$1,575,930	**$2,058,610**
Average balance during the year	933,433	1,097,707	**1,604,675**
Weighted average interest rate during the year	5.05%	5.33%	**5.26%**
Commercial paper:			
Maximum outstanding at any month end	$1,854,576	$1,876,135	**$1,918,700**
Average balance during the year	1,620,087	1,637,070	**1,631,216**
Weighted average interest rate during the year	5.40%	5.49%	**5.42%**
Other borrowed funds:			
Maximum outstanding at any month end	$1,697,236	$ 851,694	**$ 438,151**
Average balance during the year	1,119,051	635,900	**328,872**
Weighted average interest rate during the year	5.59%	5.42%	**5.68%**

Capital Adequacy and Dividends

Our principal capital objectives are to support future growth, to protect depositors, to absorb any unanticipated losses and to comply with various regulatory requirements. Management believes that we have retained our capital at a level that supports our risk structure, as well as providing for anticipated growth of current business activities and strategic expansion.

Total shareholders' equity was $3.1 billion at December 31, 1998, an increase of $379 million from year-end 1997. This change was primarily a result of $466 million of net income for 1998, offset by dividends on common stock of $107 million.

We offer a dividend reinvestment plan that allows shareholders to reinvest dividends in our common stock at 5 percent below the market price. During 1998, The Bank of Tokyo-Mitsubishi, Ltd. did not participate in the plan.

Capital adequacy depends on a variety of factors including asset quality and risk profile, liquidity, earnings stability, competitive and economic conditions, and management. We believe that the current level of profitability, coupled with a prudent dividend policy, is adequate to support normal growth in operations while meeting regulatory capital guidelines.

Management's Discussion and Analysis of Financial Condition and Results of Operations

The following table summarizes our risk-based capital, risk-weighted assets, and risk-based capital ratios.

December 31,	1996	1997	**1998**	Minimum Regulatory Requirement
(Dollars in thousands)				
Capital Components				
Tier 1 capital	$ 2,395,580	$ 2,587,071	**$ 2,965,865**	
Tier 2 capital	551,074	601,102	**604,938**	
Total risk-based capital	$ 2,946,654	$ 3,188,173	**$ 3,570,803**	
Risk-weighted assets	$26,390,288	$28,862,340	**$30,753,030**	
Quarterly average assets	$28,496,355	$30,334,507	**$31,627,022**	
Capital Ratios				
Total risk-based capital	11.17%	11.05%	**11.61%**	8.0%
Tier 1 risk-based capital	9.08	8.96	**9.64**	4.0
Leverage ratio[1]	8.41	8.53	**9.38**	4.0

[1] Tier 1 capital divided by quarterly average assets (excluding certain intangible assets).

We and Union Bank of California, N.A. are subject to various regulations issued by federal banking agencies, including minimum capital requirements. We and Union Bank of California, N.A. are required to maintain minimum ratios of total and Tier 1 capital to risk-weighted assets and of Tier 1 capital to quarterly average assets (the leverage ratio).

Compared with December 31, 1997, our Tier 1 risk-based capital ratio at December 31, 1998 increased 68 basis points to 9.64 percent, our total risk-based capital ratio increased 56 basis points to 11.61 percent, and our leverage ratio increased 85 basis points to 9.38 percent. The increase in our capital ratios was primarily attributable to retained earnings growing faster than both risk-weighted assets and average assets, partly offset by the reduction of $50 million in subordinated capital notes.

As of December 31, 1998, management believed the capital ratios of Union Bank of California, N.A. met all regulatory minimums of a "well-capitalized" institution.

Comparison of 1996 to 1997

Net income in 1996 was $249 million, compared to $411 million in 1997. Net income applicable to common stock was $238 million, or $1.36 per diluted common share, in 1996, compared with $404 million, or $2.30 per diluted common share, in 1997. This increase in diluted earnings per share of 69 percent over 1996 was due to a 5 percent increase in net interest income, an 11 percent increase in noninterest income, a 8 percent decrease in noninterest expense, a decrease in the effective income tax rate, and a $40 million reduction in the provision for credit losses. Other highlights for 1997 include:

- Net interest income, on a taxable-equivalent basis, was $1.2 billion in 1997, an increase of $62 million, or 5 percent, over 1996 primarily due to a $1.6 billion, or 6 percent, increase in average earning assets, resulting primarily from a $1.1 billion, or 5 percent, increase in average loans and largely funded by an $851 million, or 13 percent, increase in average demand deposits. Partially offsetting the positive impact of the growth in earning assets and demand deposits on net interest income was a 5 basis point decline in the net interest margin to 4.70 percent. The decline in net interest margin was primarily due to a 14 basis point decrease in the spread between the average yield on average earning assets and the average rate paid on average interest bearing liabilities.
- A $40 million provision for credit losses was recorded in 1996, compared with no provision for credit losses in 1997, reflecting improvement in the quality of our loan portfolio and a reduction in nonaccrual loans. Nonperforming assets declined $27 million, or 17 percent, from December 31, 1996 to $130 million at December 31, 1997. Nonperforming assets as a percent of total assets declined from 0.54 percent at December 31, 1996 to 0.42 percent at December 31, 1997. Total nonaccrual loans were $128 million at December 31, 1996, compared with $109 million at year-end 1997, resulting in a reduction in the ratio of nonaccrual and renegotiated loans to total loans from 0.61 percent at December 31, 1996 to 0.48 percent at year-end 1997. The allowance for credit losses was $524 million, or

Management's Discussion and Analysis of Financial Condition and Results of Operations

408 percent of total nonaccrual loans, at December 31, 1996, compared with $452 million, or 413 percent of total nonaccrual loans, at December 31, 1997.

- Noninterest income was $463 million in 1997, an increase of $44 million, or 11 percent, over 1996. Service charges on deposit accounts grew $13 million, or 12 percent, reflecting growth in deposit balances while trust and investment management fees increased $14 million, or 15 percent, on growth in trust accounts and assets under management.
- Noninterest expense was $1.0 billion in 1997, a decrease of $90 million, or 8 percent, from 1996. This decrease was primarily attributable to a decrease of $111 million in merger and integration expense and a decrease of $18 million in net occupancy expense, reflecting a $12 million charge recorded in 1996 related to former banking facilities, as well as merger efficiencies realized in 1997. These decreases were partially offset by an increase of $14 million, or 3 percent, in personnel-related expense, a significant portion of which was due to severance payments related to realignment of departments and to higher performance-related incentive compensation, and an increase of $16 million, or 26 percent, in other expenses. Excluding the $12 million charge in 1996 and merger and integration expense, noninterest expense increased $33 million over 1996.
- The effective tax rate for 1996 was 40 percent, compared with 37 percent for 1997. Excluding a $5 million after-tax benefit from the settlement of a unitary tax issue with the FTB, the effective tax rate in 1996 was 41 percent. Excluding the $25 million after-tax refund from the FTB, the effective tax rate in 1997 was 41 percent.
- The return on average assets for 1997 increased to 1.39 percent, compared to 0.89 percent for 1996. The return on average common equity for 1997 increased to 16.05 percent, compared to 10.24 percent for 1996.
- Total loans at December 31, 1997 were $22.7 billion, an increase of $1.7 billion, or 8 percent, over year-end 1996, primarily from growth in the commercial, financial and industrial loan portfolio.
- At December 31, 1997, our Tier 1 risk-based capital ratio was 8.96 percent and our total risk-based capital ratio was 11.05 percent, exceeding the minimum regulatory guidelines for bank holding companies of 4 percent and 8 percent, respectively. The Tier 1 and total risk-based capital ratios for Union Bank of California, N.A. at December 31, 1997 exceeded the regulatory guidelines for "well-capitalized" banks. Our leverage ratio was 8.53 percent at December 31, 1997, exceeding the minimum regulatory guideline for bank holding companies.

Quantitative and Qualitative Disclosures About Market Risk

General

Market risk is the risk of loss to future earnings, to fair values, or to future cash flows that may result from changes in the price of a financial instrument. The value of a financial instrument may change as a result of changes in interest rates, foreign currency exchange rates, commodity prices, equity prices, and other market changes that affect market risk sensitive instruments. Market risk is attributed to all market risk sensitive financial instruments, including securities, loans, deposits, borrowings, as well as derivative instruments. Our exposure to market risk is a function of our asset and liability management activities, our trading activities for our own account, and our role as a financial intermediary in customer-related transactions. The objective of market risk management is to avoid excessive exposure of our earnings and equity to loss and to reduce the volatility inherent in certain financial instruments.

The management of market risk is governed by policies reviewed and approved annually by our Board of Directors (Board). The Board delegates responsibility for market risk management to the Asset & Liability Management Committee (ALCO), which reports quarterly to the Finance and Capital Committee of the Board on activities related to the management of market risk. As part of the management of our market risk, ALCO may direct changes in the mix of assets and liabilities and the use of derivative instruments such as interest rate swaps, caps and floors. ALCO also reviews and approves market risk-management programs and market risk limits. The ALCO Chairman is responsible for the company-wide management of market risk. The Treasurer is responsible for implementing funding, investment, and hedging strategies designed to manage this risk. On a day-to-day basis, the oversight of market risk management takes place at a centralized level within the Risk Monitoring Unit (RMU). The RMU is responsible for measuring risks to ensure compliance with all market risk limits and guidelines incorporated within the policies and procedures established by ALCO. The RMU reports monthly to ALCO on the effectiveness of our hedging activities, on trading risk exposures, and on compliance with policy limits. In addition, periodic reviews by internal audit, regulators and independent accountants provide further evaluation of controls over the risk management process.

We have separate and distinct methods for managing the market risk associated with our trading activities and our asset and liability management activities, as described below.

Management's Discussion and Analysis of Financial Condition and Results of Operations

Interest Rate Risk Management (Other Than Trading)

We engage in asset and liability management activities with the objective of reducing adverse changes in earnings as a result of changes in interest rates. The management of interest rate risk relates to the timing and magnitude of the repricing of assets compared to liabilities and has, as its objective, the control of risks associated with movements in interest rates.

The Asset & Liability Management (ALM) Policy approved by the Board requires monthly monitoring of interest rate risk by ALCO. As part of the management of our interest rate risk, ALCO may direct changes in the composition of the balance sheet and the extent to which we utilize off-balance sheet derivative instruments such as interest rate swaps, floors, and caps.

Our unhedged balance sheet is inherently "asset-sensitive", which means that assets generally reprice more often than liabilities. Since an asset-sensitive balance sheet tends to reduce net interest income when interest rates decline and to increase net interest income when interest rates rise, off-balance sheet hedges and the securities portfolio are used to manage this interest rate risk.

One method of measuring interest rate risk is by measuring the interest rate sensitivity gap, which is the difference between earning assets and liabilities maturing or repricing within specified periods. The table on page 48 presents such an analysis, which reflects certain assumptions as to the rate sensitivity of deposits without contractual maturities or repricing dates. These include demand deposits, money market demand accounts, and savings deposits. Additional assumptions such as prepayment estimates for residential mortgages and mortgage-backed securities are made to reflect the probable behavior of those assets. The section of the table on page 48 entitled "Interest Rate Risk Management Positions" presents the effects of the securities portfolio and of derivatives used for hedging, such as interest rate swaps and floors, in reducing the interest rate sensitivity gap primarily for LIBOR-based loans.

The table on page 48 shows that assets that are rate sensitive within one year exceeded liabilities within that same period by $5.0 billion at December 31, 1998. Adjusted for the effects of the securities portfolio and derivatives used for hedging, this cumulative gap was reduced to $3.7 billion. At December 31, 1997, our assets that were rate sensitive within one year exceeded liabilities within that same period by $4.9 billion. Adjusted for the effects of the securities portfolio and derivatives used for hedging, this cumulative gap was reduced to $2.5 billion.

Gap analysis has significant limitations as a method for measuring interest rate risk since changes in interest rates do not affect all categories of assets and liabilities in the same way. To address these limitations, we use a simulation model to quantify the impact of changing interest rates on net interest income (NII). A frequency distribution of simulated 12-month NII outcomes based on rate scenarios produced through a Monte Carlo rate generation process is prepared monthly to determine statistically the mean NII. The amount of Earnings at Risk (EaR), defined as the potential negative change in NII, is measured at a 97.5 percent confidence level and is managed within the limit established in the Board's ALM Policy at 5 percent of mean NII. The following table summarizes our EaR and EaR as a percentage of NII.

December 31,	1997	**1998**
(Dollars in millions)		
EaR	$23.0	**$25.5**
EaR as a percentage of mean NII	1.80%	**1.97%**

An additional limit established by the Board's ALM Policy is that under single interest rate shock scenarios, up or down 200 basis points, the difference between the lower simulated NII and the mean NII must be no more than 8 percent of the mean NII. The following table sets forth the change in simulated NII for both an upward and downward shock scenario of 200 basis points.

December 31,	1997	**1998**
(Dollars in millions)		
+200 basis points	$63.9	**$23.4**
as a percentage of mean NII	5.00%	**1.81%**
–200 basis points	$(51.8)	**$(52.2)**
as a percentage of mean NII	4.05%	**4.03%**

Management's Discussion and Analysis of Financial Condition and Results of Operations

Trading Activities

We enter into trading account activities primarily as a financial intermediary for customers, and, to a lesser extent, for our own account. By acting as a financial intermediary, we are able to provide our customers with access to a wide range of products from the securities, foreign exchange, and derivatives markets. In acting for our own account, we may take positions in some of these instruments with the objective of generating trading profits. These activities expose us to two primary types of market risk: interest rate and foreign currency exchange risk.

In order to manage interest rate and foreign currency exchange risk associated with our trading activities, we utilize a variety of non-statistical methods including: position limits for each trading activity, daily marking of all positions to market, daily profit and loss statements, position reports, and independent verification of all inventory pricing. Additionally, the RMU reports positions and profits and losses daily to the Treasurer and trading managers and weekly to the ALCO Chairman. ALCO is provided reports on a monthly basis. We believe that these procedures, which stress timely communication between the RMU and senior management, are the most important elements of the risk management process.

We use a form of Value at Risk (VaR) methodology to measure the overall market risk inherent in our trading account activities. Under this methodology, management statistically calculates, with 97.5 percent confidence, the potential loss in fair value that we might experience if an adverse shift in market prices were to occur within a period of 5 business days. The amount of VaR is managed within limits well below the maximum limit established by Board policy at 0.5 percent of shareholders' equity. The VaR model incorporates a number of key assumptions, including assumed holding period and historical volatility based on 3 years of historical market data updated quarterly. The following table sets forth the average, high and low VaR during the year for our trading activities.

	Average VaR	High VaR	Low VaR	**Average VaR**	**High VaR**	**Low VaR**
December 31,		1997			**1998**	
(Dollars in thousands)						
Foreign exchange	$ 73	$147	$ 32	**$103**	**$389**	**$ 20**
Securities	558	717	439	**410**	**873**	**222**

Our interest rate derivative contracts include $2.3 billion of derivative contracts entered into as an accommodation for customers. We act as an intermediary and match these contracts at a profit with contracts with The Bank of Tokyo-Mitsubishi, Ltd. or other dealers, thus neutralizing the related market risk. We maintain responsibility for the credit risk associated with these contracts.

Liquidity Risk

Liquidity risk represents the potential for loss as a result of limitations on our ability to adjust our future cash flows to meet the needs of depositors and borrowers and to fund operations on a timely and cost-effective basis. The ALM Policy approved by the Board requires quarterly reviews of our liquidity by the ALCO, which is composed of bank senior executives. Our liquidity management draws upon the strengths of our extensive retail and commercial market business franchise, coupled with the ability to obtain funds for various terms in a variety of domestic and international money markets. Liquidity is managed through the funding and investment functions of the Global Markets Group.

Core deposits provide us with a sizable source of relatively stable and low-cost funds. Our average core deposits, which include demand deposits, money market demand accounts, and savings and consumer time deposits, combined with average common shareholders' equity, funded 66 percent of average total assets of $30.5 billion for the year ended December 31, 1998. Most of the remaining funding was provided by short-term borrowings in the form of negotiable certificates of deposit, foreign deposits, federal funds purchased and securities sold under repurchase agreements, commercial paper and other borrowings. In 1998, we increased our Commercial Paper program by $100 million.

Liquidity may also be provided by the sale or maturity of assets. Such assets include interest bearing deposits in banks, federal funds sold and securities purchased under resale agreements, and trading account securities. The aggregate of these assets averaged $1.1 billion during 1998. Additional liquidity may be provided by investment securities available for sale that amounted to $3.6 billion at December 31, 1998, and by loan maturities. At December 31, 1998, $9.1 billion of loans were scheduled to mature within one year.

Management's Discussion and Analysis of Financial Condition and Results of Operations

The following table summarizes our interest rate sensitivity based on expected repricings in the time frames indicated for the balance sheet and interest rate derivatives as of December 31, 1998.

	Amounts Maturing or Repricing In			
December 31, 1998	0–12 Months	>1–5 Years	After 5 years	Total
(Dollars in thousands)				
Assets				
Federal funds sold and securities purchased under resale agreements	$ 333,530	$ —	$ —	$ 333,530
Interest bearing deposits in banks	209,568	—	—	209,568
Trading account assets	267,718	—	—	267,718
Loans	18,917,483	3,825,925	1,552,703	24,296,111
Other assets[(1)(2)]	571,793	1,492,820	1,305,731	3,370,344
Total assets (except securities)	$20,300,092	$ 5,318,745	$ 2,858,434	$28,477,271
Liabilities and Shareholders' Equity				
Interest bearing deposits:				
Interest bearing checking[(1)(3)]	$ 192,599	$ 1,348,190	$ —	$ 1,540,789
Money market demand accounts[(1)(3)]	1,331,227	2,674,582	—	4,005,809
Savings[(1)(3)]	189,998	1,329,985	—	1,519,983
Other time deposits[(1)]	6,889,618	365,434	6,841	7,261,893
Federal funds purchased and securities sold under repurchase agreements	1,307,744	—	—	1,307,744
Other borrowed funds[(1)]	1,771,306	4,027	577	1,775,910
Subordinated capital notes	298,000	—	—	298,000
Noninterest bearing deposit accounts[(4)]	3,053,825	7,125,580	—	10,179,405
Other liabilities[(1)(2)]	288,500	—	1,040,039	1,328,539
Shareholders' equity[(2)]	—	—	3,058,244	3,058,244
Total liabilities and shareholders' equity	$15,322,817	$12,847,798	$ 4,105,701	$32,276,316
Gap before risk management positions	$ 4,977,275	$ (7,529,053)	$(1,247,267)	$ (3,799,045)
Cumulative gap before risk management positions	$ 4,977,275	$ (2,551,778)	$(3,799,045)	
Interest rate risk management positions				
Securities[(1)]	1,244,866	2,239,073	315,106	3,799,045
Interest rate swaps	(500,000)	500,000	—	—
Interest rate floors[(5)]	(2,000,000)	2,000,000	—	—
Gap adjusted for risk management positions	$ 3,722,141	$ (2,789,980)	$ (932,161)	$ —
Cumulative gap adjusted for risk management positions	$ 3,722,141	$ 932,161	$ —	$ —

(1) Certain balance sheet classifications used for interest rate sensitivity analysis do not conform to the Consolidated Balance Sheets on page 53.

(2) Items that neither reprice nor mature are included in the "After 5 years" column.

(3) Interest rate sensitivity of non-maturity deposit accounts are based on assumptions for a declining interest rate scenario since the Company's balance sheet is asset-sensitive.

(4) 70 percent of the demand deposit account balance is assumed to be "core" deposits, which are not sensitive to interest rate changes.

(5) Floors purchased affect interest rate sensitivity in a declining interest rate scenario.

Management's Discussion and Analysis of Financial Condition and Results of Operations

Year 2000

The year 2000 problem exists because many computer programs use only the last two digits to refer to a year. This convention could affect date-sensitive calculations that treat "00" as the year 1900, rather than as the year 2000. Another issue is that the year 2000 is a leap year and some programs may not properly provide for February 29, 2000.

This discussion of the implications of the year 2000 problem for us contains numerous forward-looking statements based on inherently uncertain information. The cost of the project and the date on which we plan to complete the internal year 2000 modifications are based on management's best estimates of future events. See details with respect to costs for year 2000 on page 29. The material assumptions underlying the estimated cost are:

- the continued availability of internal and external resources,
- the cost of these resources,
- the time required to accomplish the tasks, and
- the cost of needed equipment.

We cannot guarantee, however, these estimates, and actual results could differ. Moreover, although management believes it will be able to make the necessary modifications in advance, failure to modify the systems may have a material adverse effect on us.

In addition, we place a high degree of reliance on computer systems of third parties, such as customers, vendors, and other financial and governmental institutions. Although we are assessing the readiness of these third parties and preparing contingency plans, the failure of these third parties to modify their systems in advance of December 31, 1999, may have a material adverse effect on us.

Readiness Preparation

Resolution of the year 2000 problem is among our highest priorities, and we are preparing for the century change with a comprehensive enterprise-wide year 2000 program. We have identified all of the major systems and have sought external and internal resources to renovate and test the systems. We are testing purchased software, internally developed systems and systems supported by external parties as part of the program. We are evaluating customers and vendors that have significant relationships with us to determine whether they are adequately preparing for the year 2000. In addition, we are developing contingency plans to reduce the impact of some potential events that may occur. We cannot guarantee, however, that the systems of vendors or customers with whom we do business will be completed on a timely basis, or that contingency plans will shield operations from failures that may occur.

Our year 2000 program is comprised of numerous individual projects that address the following broad areas:

- data processing systems,
- telecommunications and data networks,
- building facilities and security systems,
- vendor risk,
- customer risk,
- contingency planning, and
- communications.

We have identified over 2,000 individual projects. The projects vary in size, importance and materiality, from large undertakings, such as remediating complicated data systems, to smaller, but still important, projects such as installing compliant computer utility systems or assuring that building equipment will perform properly. The program continues to evolve as we identify new projects to keep up with increased understanding of year 2000 implications and evolving external requirements. Virtually all of the projects currently identified have begun, and approximately two-thirds have been completed.

We assign projects a priority, indicating the importance of the function to our continuing operation. This prioritization facilitates reporting on projects based on their relative importance. We have prioritized projects as "Critical" and "Non-Critical". Critical projects are further prioritized as "Mission Critical" and "Other Critical".

"Mission Critical" projects are defined as:

- systems vital to the continuance of a broad core business activity;
- functions, the interruption of which for longer than 3 days would threaten our viability; or
- functions that provide the environment and infrastructure necessary to continue the broad core business activities.

"Other Critical" projects are defined as:

- other customer and accounting systems;
- functions supporting delivery of information and service to customers;
- administrative systems, the interruption of which for longer than two weeks would cause severe business impact; or
- functions that provide the environment and infrastructure necessary for delivery of the above systems and functions.

We plan to complete all projects currently identified prior to the year 2000, with special emphasis placed on those prioritized as "Mission Critical" or "Other Critical". Failure to complete an "Other Critical" project would not necessarily have a material adverse effect on us.

The most important projects are the "Mission Critical" application systems upon which we rely for our principal

Management's Discussion and Analysis of Financial Condition and Results of Operations

business functions. We have renovated and tested all of these systems. However, outside servicers operate three of them. The outside servicers have renovated and tested each of these systems, but we still need to validate them.

The following table presents actual and estimated progress with "Mission Critical" projects.

Mission Critical Application Completion

	% Completed
Actual:	
June 1998	10%
September 1998	38
December 1998	90
Estimated:	
March 1999	100%

We have also achieved substantial progress with systems prioritized as "Other Critical". As of December 31, 1998, 63 percent of these systems were complete. Substantially all are expected to be complete by March 31, 1999.

In addition to testing individual systems, we have begun integrated contingency testing of our "Mission Critical" and many other systems in a separate computer environment where dates are set forward in order to identify and correct problems that might not otherwise become evident until the actual end of the century.

We do not significantly rely on "embedded technology" in our critical processes. "Embedded technology", which means microprocessor-controlled devices as opposed to multi-purpose computers, does control some building security and operations, such as power management, ventilation, and building access. All building facilities are presently being evaluated, and we expect all systems using embedded technology to be confirmed as year 2000 ready by June 1999.

We rely on vendors and customers, and we are addressing year 2000 issues with both groups. We have identified over 300 vendors and have made inquiries about their year 2000 readiness plans and status. Approximately 35 percent of these vendors are rated as critical. We have completed risk assessments on the critical and non-critical vendors, and we are undertaking appropriate measures to minimize risk as much as possible for those vendors that we have assigned a risk rating of medium or high. Among the critical vendors, presently 72 percent are rated as low risk, 19 percent as medium risk, and 9 percent as high risk.

We plan to have the medium and high risk vendor situations resolved in June 1999. We have, however, no viable alternatives for some suppliers, such as power distribution and local telephone companies. We are still evaluating these companies, and we will use the results as information for system-wide contingency planning. As with all financial institutions, we place a high degree of reliance on the systems of other institutions, including governmental agencies, to settle transactions. We will test principal settlement methods associated with major payment systems as part of their associated system projects.

We also rely on our customers to make necessary preparations for the year 2000 so that their business operations will not be interrupted, thus threatening their ability to honor their financial commitments. We have identified over 2,500 borrowers, capital market counterparties, funding sources, and large depositors that constitute our customers as having financial volumes sufficiently large to warrant our inquiry and assessment of their year 2000 preparation. The financial volumes included loans and unused commitments, collected deposit balances, automated clearing house transactions, foreign exchange, and derivatives. We have completed inquiries and initial written assessments for 97 percent of the identified financial volumes.

Our borrowers, the population of customers with loans and unused commitments outstanding, pose the highest level of concern. As of December 31, 1998, our assessment of these borrowers resulted in the following assignments of risk: 79 percent low risk, 18 percent medium risk and 3 percent high risk. We have established individual risk mitigation plans for substantially all of the customers rated as high risk. The risk mitigation plans evaluate whether year 2000 issues will materially affect the customer's cash flow, asset values, and collateral pledged to us. The risk mitigation plans use the normal credit process that we employ to manage credit risk and require the concurrence of a credit administrator.

We will make ongoing assessments of customers at all levels of risk. Those with low risk will be reassessed semi-annually, while customers with medium and high risk will be reassessed quarterly.

Risks

The principal risks associated with the year 2000 problem can be grouped into three categories:

- we do not successfully ready our operations for the next century,
- disruption of our operations due to operational failures of third parties, and

Management's Discussion and Analysis of Financial Condition and Results of Operations

- business interruption among fund providers and obligors such that expected funding and repayment does not take place.

The only risk largely under our control is preparing our internal operations for the year 2000. We, like other financial institutions, are heavily dependent on our computer systems. The complexity of these systems and their interdependence make it impractical to convert to alternative systems without interruptions if necessary modifications are not completed on schedule. Management believes we will be able to make the necessary modifications on schedule.

Failure of third parties may jeopardize our operations, but the seriousness of this risk depends on the nature and duration of the failures. The most serious impact on our operations from vendors would result if basic services such as telecommunications, electric power, and services provided by other financial institutions and governmental agencies were disrupted. Some public disclosure about readiness preparation among basic infrastructure and other suppliers is now available. We are unable, however, to estimate the likelihood of significant disruptions among our basic infrastructure suppliers. In view of the unknown probability of occurrence and impact on operations, we consider the loss of basic infrastructure services to be the most reasonably likely worst case year 2000 scenario.

Operational failures among our customers could affect their ability to continue to provide funding or meet obligations when due. The information we develop in the customer assessments described earlier allows us to identify those customers that exhibit a risk of not making adequate preparations for the century change. We are taking appropriate actions to manage these risks.

Program Assessment

The year 2000 program office reports on progress monthly to our Executive Management Committee and quarterly to the Audit and Examination Committee of the Board. The Internal Audit Division and the National Bank Examiners regularly assess our year 2000 preparations and report quarterly to the Audit and Examination Committee.

Contingency Plans

We are developing year 2000 remediation contingency plans and business resumption contingency plans specific to the year 2000. Remediation contingency plans address the actions we would take if the current approach to remediating a system is falling behind schedule or otherwise appears in jeopardy of failing to deliver a year 2000-ready system when needed. Business resumption contingency plans address the actions that we would take if critical business functions cannot be carried out in the normal manner upon entering the next century due to system or supplier failure.

Our business resumption contingency planning is following a four-phase process:

- Organizational Planning Guidelines,
- Business Impact Analysis,
- Plan Development, and
- Validation of Plans

During the first two phases, which have been completed, we assigned responsibilities, specified scenarios and determined which scenarios were significant for each critical business unit. The second two phases call for the development of plans to meet the significant scenarios and testing the effectiveness of the plans.

We are developing plans for system-wide or regional failures and for individual critical operating units where necessary. We expect to complete development of plans for the operating units and their validation in June 1999. We expect to complete development of plans to address system-wide or regional failures, and their validation, in September 1999.

To determine where plans are necessary for individual operating units, we identified the following areas of concern, assigned to each a level of potential risk and a probability of occurrence. The areas of concern are:

- telecommunications or data network outage,
- enterprise information systems failure,
- operational disruptions,
- vendor or service provider failure,
- staff unavailability,
- utility or facility failure, and
- personal computer or local area network failure.

We rated the level of potential risk as high, moderate or low, and we rated the probability of occurrence as high, moderate or low. Critical operating units with a low or moderate level of potential risk and a low probability of occurrence do not require a contingency plan for the area of concern. For any other combination, the development of a contingency plan is required.

Other Related Disclosures

HighMark Capital Management, Inc. is a registered investment advisor and Union Bank of California Investment Services, Inc. is a broker-dealer. Each of these subsidiaries makes publicly available separate year 2000 reports. You can find additional year 2000 information in those reports.

Consolidated Statements of Income

(Amounts in thousands, except per share data)

Years Ended December 31,	1996	1997	**1998**
Interest Income			
Loans	$1,687,977	$1,763,277	**$1,826,096**
Securities	143,412	167,440	**200,337**
Interest bearing deposits in banks	52,709	56,748	**17,080**
Federal funds sold and securities purchased under resale agreements	30,246	26,079	**16,056**
Trading account assets	12,960	19,917	**25,610**
Total interest income	1,927,304	2,033,461	**2,085,179**
Interest Expense			
Domestic deposits	460,130	520,583	**468,907**
Foreign deposits	71,437	75,398	**86,221**
Federal funds purchased and securities sold under repurchase agreements	47,095	58,544	**84,440**
Commercial paper	87,411	89,912	**88,358**
Subordinated capital notes	30,104	22,850	**20,347**
Other borrowed funds	62,549	34,492	**18,683**
Total interest expense	758,726	801,779	**766,956**
Net Interest Income	1,168,578	1,231,682	**1,318,223**
Provision for credit losses	40,000	—	**45,000**
Net interest income after provision for credit losses	1,128,578	1,231,682	**1,273,223**
Noninterest Income			
Service charges on deposit accounts	101,975	114,647	**138,847**
Trust and investment management fees	93,479	107,527	**121,226**
International commissions and fees	66,108	66,122	**72,036**
Merchant transaction processing fees	49,778	57,128	**56,929**
Merchant banking fees	23,929	24,924	**31,402**
Securities gains, net	4,502	2,711	**5,686**
Other	78,905	89,942	**107,405**
Total noninterest income	418,676	463,001	**533,531**
Noninterest Expense			
Salaries and employee benefits	557,247	571,644	**617,564**
Net occupancy	103,335	85,630	**90,917**
Equipment	55,942	56,137	**56,252**
Foreclosed asset expense (income)	2,889	(1,268)	**(2,821)**
Merger and integration	117,464	6,037	**—**
Other	298,027	326,485	**373,306**
Total noninterest expense	1,134,904	1,044,665	**1,135,218**
Income before income taxes	412,350	650,018	**671,536**
Income tax expense	162,892	238,722	**205,075**
Net Income	$ 249,458	$ 411,296	**$ 466,461**
Net income applicable to common stock	$ 238,152	$ 403,696	**$ 466,461**
Net income per common share—basic	$ 1.37	$ 2.31	**$ 2.66**
Net income per common share—diluted	$ 1.36	$ 2.30	**$ 2.65**
Weighted average common shares outstanding—basic	174,391	174,683	**175,127**
Weighted average common shares outstanding—diluted	174,784	175,189	**175,737**

See accompanying notes to consolidated financial statements.

Consolidated Balance Sheets

(Dollars in thousands, except share data)

December 31,	1997	**1998**
Assets		
Cash and due from banks	$ 2,541,699	**$ 2,135,380**
Interest bearing deposits in banks	633,421	**209,568**
Federal funds sold and securities purchased under resale agreements	24,335	**333,530**
Total cash and cash equivalents	3,199,455	**2,678,478**
Trading account assets	394,313	**267,718**
Securities available for sale	2,538,386	**3,638,532**
Securities held to maturity (market value: 1997, $193,115; 1998, $163,244)	188,775	**160,513**
Loans (net of allowance for credit losses: 1997, $451,692; 1998, $459,328)	22,289,716	**23,836,783**
Due from customers on acceptances	773,339	**489,480**
Premises and equipment, net	406,299	**421,091**
Other assets	794,982	**783,721**
Total assets	$30,585,265	**$32,276,316**
Liabilities		
Domestic deposits:		
Noninterest bearing	$ 8,574,515	**$ 9,919,316**
Interest bearing	12,666,458	**12,609,565**
Foreign deposits:		
Noninterest bearing	275,029	**260,089**
Interest bearing	1,780,372	**1,718,909**
Total deposits	23,296,374	**24,507,879**
Federal funds purchased and securities sold under repurchase agreements	1,335,884	**1,307,744**
Commercial paper	966,575	**1,444,745**
Other borrowed funds	476,010	**331,165**
Acceptances outstanding	773,339	**489,480**
Other liabilities	709,784	**839,059**
Subordinated capital notes	348,000	**298,000**
Total liabilities	27,905,966	**29,218,072**
Commitments and contingencies		
Shareholders' Equity		
Preferred stock:		
Authorized 5,000,000 shares, no shares issued or outstanding at December 31, 1997 or 1998	—	**—**
Common stock—no stated value:		
Authorized 300,000,000 shares, issued 174,917,674 shares in 1997 and 175,259,919 shares in 1998	1,714,209	**1,725,619**
Retained earnings	957,662	**1,314,915**
Accumulated other comprehensive income	7,428	**17,710**
Total shareholders' equity	2,679,299	**3,058,244**
Total liabilities and shareholders' equity	$30,585,265	**$32,276,316**

See accompanying notes to consolidated financial statements.

Consolidated Statements of Changes in Shareholders' Equity

(Dollars in thousands)

Years Ended December 31,	1996		1997		**1998**	
Preferred Stock						
Balance, beginning of year	$ 135,000		$ 135,000		**$ —**	
Redemption of preferred stock	—		(135,000)		**—**	
Balance, end of year	$ 135,000		$ —		**$ —**	
Common Stock						
Balance, beginning of year	$1,699,260		$1,703,838		**$1,714,209**	
Dividend reinvestment plan	1,162		(37)		**28**	
Deferred compensation—restricted stock awards	2,355		3,757		**5,744**	
Stock options exercised	1,061		6,651		**5,638**	
Balance, end of year	$1,703,838		$1,714,209		**$1,725,619**	
Retained Earnings						
Balance, beginning of year	$ 626,172		$ 645,214		**$ 957,662**	
Net income(1)	249,458	$249,458	411,296	$411,296	**466,461**	**$466,461**
Dividends on common stock(2)(3)	(73,932)		(89,848)		**(106,932)**	
Dividends on preferred stock	(11,306)		(7,600)		**—**	
Dividend to The Mitsubishi Bank, Ltd.	(144,890)		—		**—**	
Deferred compensation—restricted stock awards	(288)		(1,400)		**(2,276)**	
Balance, end of year	$ 645,214		$ 957,662		**$1,314,915**	
Accumulated Other Comprehensive Income						
Balance, beginning of year	$ 23,660		$ 10,881		**$ 7,428**	
Unrealized holding gains (losses) arising during the year on securities available for sale, net of tax expense (benefit) of $(5,297) in 1996, $4,370 in 1997, and $6,672 in 1998		(8,112)		7,538		**12,734**
Less: reclassification adjustment for gains on securities available for sale included in net income, net of tax expense of $1,778 in 1996, $995 in 1997, and $2,175 in 1998		(2,724)		(1,716)		**(3,511)**
Net unrealized gains (losses) on securities available for sale		(10,836)		5,822		**9,223**
Foreign currency translation adjustment, net of tax expense (benefit) of $(1,269) in 1996, $(5,377) in 1997, and $1,739 in 1998		(1,943)		(9,275)		**2,807**
Minimum pension liability adjustment, net of tax benefit of $1,083 in 1998		—		—		**(1,748)**
Other comprehensive income	(12,779)	(12,779)	(3,453)	(3,453)	**10,282**	**10,282**
Total comprehensive income		$236,679		$407,843		**$476,743**
Balance, end of year	$ 10,881		$ 7,428		**$ 17,710**	
Total Shareholders' Equity	$2,494,933		$2,679,299		**$3,058,244**	

(1) Includes dividends applicable to preferred shareholders of $11.3 million in 1996 and $7.6 million in 1997.

(2) Dividends per share in 1996 were based on historical Union Bank common cash dividends declared and did not include the $145 million dividend paid to The Mitsubishi Bank, Limited in the first quarter of 1996 by BanCal Tri-State Corporation and The Bank of California, N.A.

(3) Dividends per share were $0.47 in 1996, $0.51 in 1997, and $0.61 in 1998, and are based on UnionBanCal Corporation's shares outstanding as of the declaration date.

See accompanying notes to consolidated financial statements.

Consolidated Statements of Cash Flows

(Dollars in thousands)

Years Ended December 31,	1996	1997	**1998**
Cash Flows from Operating Activities:			
Net income	$ 249,458	$ 411,296	**$ 466,461**
Adjustments to reconcile net income to net cash provided by operating activities:			
Provision for credit losses	40,000	—	**45,000**
Depreciation, amortization and accretion	65,092	65,469	**67,640**
Provision for deferred income taxes	50,658	59,814	**28,097**
Gain on sales of securities available for sale	(4,502)	(2,711)	**(5,686)**
Merger and integration costs in excess of (less than) cash utilized	54,344	(31,414)	**(12,388)**
Net (increase) decrease in trading account assets	(359,234)	52,743	**126,595**
Other, net	52,101	173,706	**(117,258)**
Total adjustments	(101,541)	317,607	**132,000**
Net cash provided by operating activities	147,917	728,903	**598,461**
Cash Flows from Investing Activities:			
Proceeds from sales of securities available for sale	19,536	171,629	**418,477**
Proceeds from matured and called securities available for sale	757,463	587,034	**259,465**
Purchases of securities available for sale	(995,479)	(1,112,080)	**(1,528,281)**
Proceeds from matured and called securities held to maturity	95,829	79,828	**28,540**
Purchases of premises and equipment	(69,047)	(60,829)	**(82,880)**
Net increase in loans	(741,335)	(1,788,179)	**(1,625,149)**
Other, net	14,927	4,245	**12,466**
Net cash used by investing activities	(918,106)	(2,118,352)	**(2,517,362)**
Cash Flows from Financing Activities:			
Net increase in deposits	1,877,917	1,763,414	**1,211,505**
Net increase (decrease) in federal funds purchased and securities sold under repurchase agreements	127,596	13,230	**(28,140)**
Net increase (decrease) in commercial paper and other borrowed funds	(201,214)	(797,464)	**333,325**
Maturity and redemption of subordinated debt	(119,369)	(234,000)	**(50,000)**
Proceeds from issuance of subordinated debt	—	200,000	**—**
Payments of cash dividends	(222,533)	(93,303)	**(98,160)**
Redemption of preferred stock	—	(135,000)	**—**
Repayment of borrowing to support corporate owned life insurance	(95,475)	—	**—**
Other, net	(882)	(2,661)	**8,473**
Net cash provided by financing activities	1,366,040	714,216	**1,377,003**
Net increase (decrease) in cash and cash equivalents	595,851	(675,233)	**(541,898)**
Cash and cash equivalents at beginning of year	3,352,423	3,937,697	**3,199,455**
Effect of exchange rate changes on cash and cash equivalents	(10,577)	(63,009)	**20,921**
Cash and cash equivalents at end of year	$3,937,697	$3,199,455	**$2,678,478**
Cash Paid During the Year For:			
Interest	$ 764,327	$ 820,355	**$ 784,023**
Income taxes	172,451	113,588	**234,895**
Supplemental Schedule of Noncash Investing and Financing Activities:			
Loans transferred to foreclosed assets (OREO)	$ 44,557	$ 23,114	**$ 17,260**
Dividends declared but unpaid	20,383	24,528	**33,300**

See accompanying notes to consolidated financial statements.

Notes to Consolidated Financial Statements

December 31, 1996, 1997, and 1998

Note 1.

Summary of Significant Accounting Policies and Nature of Operations

Introduction

UnionBanCal Corporation, a commercial bank holding company, and subsidiaries (the Company) was created on April 1, 1996 by the combination of Union Bank with BanCal Tri-State Corporation and its banking subsidiary, The Bank of California, N.A. (the Bank). The combination was accounted for as a reorganization of entities under common control (similar to a business combination under the pooling of interests method). Accordingly, all historical financial information has been restated as if the combination had been in effect for all periods presented. The merger was effected by the issuance of 54.4 million shares of Union Bank common stock in exchange for all the outstanding common shares of BanCal Tri-State Corporation. Information pertaining to merger and integration expense is presented in Note 7. Prior to the March 3, 1999 transaction discussed below, the Company was 82 percent owned by The Bank of Tokyo-Mitsubishi, Ltd. (BTM) and 18 percent owned by other shareholders.

On August 10, 1998, the Company exchanged 10.2 million shares of its Common Stock for the 7.2 million shares of the Bank's Common Stock owned directly by BTM. This share exchange provided the Company with a 100 percent ownership interest in the Bank. In addition, on that date, it increased BTM's ownership percentage of the Company to 82 percent from 81 percent.

The exchange of shares was accounted for as a reorganization of entities under common control. Accordingly, amounts previously reported as Parent Direct Interest in Bank Subsidiary, including the proportionate share of net income, dividends, and other comprehensive income, have been reclassified to combine them with the corresponding amounts attributable to the Company's common shareholders for all periods presented.

On November 18, 1998, the Board of Directors approved the declaration of a 3-for-1 common stock split effective for shareholders of record on December 7, 1998. Accordingly, all historical financial information has been restated as if the stock split had been in effect for all periods presented.

Also on November 18, 1998, the Board of Directors approved a change in the stated value of the Company's Common Stock to no stated value from $1.67 per share effective as of December 7, 1998. Accordingly, amounts previously reported as Additional Paid-in Capital have been reclassified to combine them with Common Stock.

On March 3, 1999, the Company completed a secondary offering of 28.75 million shares of its Common Stock owned by BTM. The Company received no proceeds from this transaction. Concurrent with the secondary offering, the Company repurchased 8.6 million shares of its outstanding Common Stock from BTM and 2.1 million shares owned by Meiji Life Insurance Company with $311 million of the net proceeds from the issuance of $350 million of 7⅜ percent capital securities that occurred on February 19, 1999. After the secondary offering and the repurchase, BTM owns 64 percent of the Company, or 105.6 million shares, compared with 82 percent prior to the transactions.

The Company provides a wide range of financial services to consumers, small businesses, middle market companies and major corporations, primarily in California, Oregon, and Washington, but also nationally and internationally.

Basis of Financial Statement Presentation

The accounting and reporting policies of the Company conform to generally accepted accounting principles (GAAP) and general practice within the banking industry. Those policies that materially affect the determination of financial position, results of operations, and cash flows are summarized below.

The Consolidated Financial Statements include the accounts of the Company. All material intercompany transactions and balances have been eliminated. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Certain amounts for prior periods have been reclassified to conform with current financial statement presentation.

Cash and Cash Equivalents

For purposes of reporting cash flows, cash and cash equivalents include cash and due from banks, interest bearing deposits in banks, and federal funds sold and securities purchased under resale agreements, substantially all of which have maturities less than 90 days.

Trading Account Assets

Trading account assets are those financial instruments that management acquires with the intent to hold for short periods of time in order to take advantage of anticipated changes in market values. Substantially all of these assets are securities with a high degree of liquidity and a readily determinable

Notes to Consolidated Financial Statements

December 31, 1996, 1997, and 1998

market value. Interest earned, paid, or accrued on trading account assets is included in interest income using a method that generally produces a level yield. Realized gains and losses from the closeout of trading account positions and unrealized market value adjustments are recognized in noninterest income.

Securities Available for Sale and Securities Held to Maturity

The Company's securities portfolios consist of debt and equity securities that are classified either as securities available for sale or securities held to maturity.

Debt securities for which the Company has the positive intent and ability to hold until maturity are classified as securities held to maturity and carried at amortized cost.

Debt securities and equity securities with readily determinable market values that are not classified as either securities held to maturity or trading account assets are classified as securities available for sale and carried at fair value, with the unrealized gains or losses reported net of taxes as a component of accumulated other comprehensive income in shareholders' equity until realized.

Realized gains and losses arising from the sale of securities are based upon the specific identification method and included in noninterest income as securities gains (losses), net.

Interest income on debt securities includes the amortization of premiums and the accretion of discounts using the effective interest method and is included in interest income on securities. Dividend income on equity securities is included in noninterest income.

Loans

Loans are reported at the principal amounts outstanding, net of unamortized nonrefundable loan fees and related direct loan origination costs. Deferred net fees and costs are recognized in interest income over the loan term using a method that generally produces a level yield on the unpaid loan balance. Nonrefundable fees and direct loan origination costs related to loans held for sale are deferred and recognized as a component of the gain or loss on sale. Interest income is accrued principally on a simple interest basis.

Nonaccrual loans are those for which management has discontinued accrual of interest because there exists significant uncertainty as to the full and timely collection of either principal or interest or such loans have become contractually past due 90 days with respect to principal or interest.

Interest accruals are continued for certain small business loans that are processed centrally, consumer loans, and one-to-four family residential mortgage loans. These loans are charged off or written down to their net realizable value based on delinquency time frames that range from 120 to 270 days, depending on the type of credit that has been extended. Interest accruals are also continued for loans that are both well-secured and in the process of collection. For this purpose, loans are considered well-secured if they are collateralized by property having a net realizable value in excess of the amount of principal and accrued interest outstanding or are guaranteed by a financially responsible and willing party. Loans are considered "in the process of collection" if collection is proceeding in due course either through legal action or other actions that are reasonably expected to result in the prompt repayment of the debt or in its restoration to current status.

When a loan is placed on nonaccrual, all previously accrued but uncollected interest is reversed against current period operating results. All subsequent payments received are first applied to unpaid principal and then to uncollected interest. Interest income is accrued at such time as the loan is brought fully current as to both principal and interest, and, in management's judgment, such loans are considered to be fully collectible. However, Company policy also allows management to continue the recognition of interest income on certain loans designated as nonaccrual. This portion of the nonaccrual portfolio is referred to as "Cash Basis Nonaccrual" loans. This policy only applies to loans that are well secured and in management's judgment are considered to be fully collectible. Although the accrual of interest is suspended, any payments received may be applied to the loan according to its contractual terms and interest income recognized when cash is received.

Loans are considered impaired when, based on current information, it is probable that the Company will be unable to collect all amounts due according to the contractual terms of the loan agreement, including interest payments. Impaired loans are carried at the lower of the recorded investment in the loan, the estimated present value of total expected future cash flows, discounted at the loan's effective rate, or the fair value of the collateral, if the loan is collateral dependent. Additionally, some impaired loans with commitments of less than $1 million are aggregated for the purpose of measuring impairment using historical loss factors as a means of measurement. Excluded from the impairment analysis are large groups of smaller balance homogeneous loans such as consumer, installment, residential mortgage loans, and automobile leases.

Renegotiated loans are those in which the Company has formally restructured a significant portion of the loan. The remaining portion is normally charged off, with a concession either in the form of below market rate financing, or debt forgiveness on the charged off portion. Loans that have

Notes to Consolidated Financial Statements

December 31, 1996, 1997, and 1998

been renegotiated and have not met specific performance standards for payment are classified as renegotiated loans within the classification of nonperforming assets. Upon payment performance, such loans may be transferred from nonperforming status to accrual status.

The Company offers primarily two types of leases to customers: 1) direct financing leases where the assets leased are acquired without additional financing from other sources, and 2) leveraged leases where a substantial portion of the financing is provided by debt with no recourse to us. Direct financing leases are carried net of unearned income, unamortized nonrefundable fees and related direct costs associated with the origination or purchase of leases. Leveraged leases are carried net of nonrecourse debt.

Allowance for Credit Losses

The Company maintains an allowance for credit losses to absorb losses inherent in the loan portfolio. The allowance is based on ongoing, quarterly assessments of the probable estimated losses inherent in the loan portfolio, and to a lesser extent, unused commitments to provide financing. The allowance is increased by the provision for credit losses, which is charged against current period operating results and decreased by the amount of chargeoffs, net of recoveries. The Company's methodology for assessing the appropriateness of the allowance consists of several key elements, which include the formula allowance, specific allowances and the unallocated allowance.

The formula allowance is calculated by applying loss factors to outstanding loans and certain unused commitments. Loss factors are based on the Company's historical loss experience and may be adjusted for significant factors that, in management's judgment, affect the collectibility of the portfolio as of the evaluation date. The Company derives the loss factors for problem graded loans from a loss migration model, for pass graded loans by using historical average net chargeoffs during a business cycle, and for pooled loans by using expected net chargeoffs for one year. Pooled loans are homogenous in nature and include consumer installment, residential mortgage, automobile leases and other loans and leases.

Specific allowances are established in cases where management has identified significant conditions or circumstances related to a credit that management believes indicate the probability that a loss has been incurred in excess of the amount determined by the application of the formula allowance.

The unallocated allowance is composed of two elements. The first element recognizes the model and estimation risk associated with the formula and specific allowances. The second element is based upon management's evaluation of various conditions that are not directly measured in the determination of the formula and specific allowances. The conditions evaluated in connection with the unallocated allowance may include existing general economic and business conditions affecting the key lending areas of the Company, credit quality trends, collateral values, loan volumes and concentrations, seasoning of the loan portfolio, specific industry conditions within portfolio segments, recent loss experience in particular segments of the portfolio, duration of the current business cycle, bank regulatory examination results and findings of the Company's internal credit examiners.

The allowance also incorporates the results of measuring impaired loans as provided in Statement of Financial Accounting Standards (SFAS) No. 114, "Accounting by Creditors for Impairment of a Loan" and SFAS No. 118, "Accounting by Creditors for Impairment of a Loan—Income Recognition and Disclosures". These accounting standards prescribe the measurement methods, income recognition and disclosures related to impaired loans. A loan is considered impaired when management determines that it is probable that the Company will be unable to collect all amounts due according to the original contractual terms of the loan agreement. Impairment is measured by the difference between the recorded investment in the loan (including accrued interest, net deferred loan fees or costs and unamortized premium or discount) and the estimated present value of total expected future cash flows, discounted at the loan's effective rate, or the fair value of the collateral, if the loan is collateral dependent. Impairment is recognized by adjusting an allocation of the existing allowance for credit losses.

Premises and Equipment

Premises and equipment are carried at cost, less accumulated depreciation and amortization. Depreciation and amortization are calculated using the straight-line method over the estimated useful life of each asset. Lives of premises range from ten to forty years; lives of furniture, fixtures and equipment range from three to eight years. Leasehold improvements are amortized over the term of the respective lease or 10 years, whichever is shorter.

Other Assets

Goodwill represents the excess of purchase price over the fair value of identifiable net assets of acquired companies and is reported as intangible assets. Goodwill is amortized using the straight-line method, generally over 15 years.

Notes to Consolidated Financial Statements

December 31, 1996, 1997, and 1998

Other real estate owned (OREO) represents the collateral acquired through foreclosure in full or partial satisfaction of the related loan. OREO is recorded at the lower of the loan's unpaid principal balance or its fair value as established by a current appraisal, adjusted for disposition costs. Any write-down at the date of transfer is charged to the allowance for credit losses. OREO values, recorded in other assets, are reviewed annually and any decline in value is recognized as foreclosed asset expense in the current period. The net operating results from these assets are included in the current period in noninterest expense as foreclosed asset expense (income).

Derivative Instruments Held for Trading or Customer Accommodation

The Company enters into a variety of interest rate derivative contracts, primarily swaps, options and foreign exchange contracts, either for trading purposes, based on management's intent at inception, or as an accommodation to customers.

Derivatives held or issued for trading or customer accommodation are carried at fair value, with realized and unrealized changes in fair values on contracts included in noninterest income in the period in which the changes occur. Unrealized gains and losses are reported gross and included in trading account assets and other liabilities, respectively. Cash flows are reported net as operating activities.

Derivative Instruments Held for Purposes Other Than Trading

The Company enters into a variety of derivative contracts as a means of reducing the Company's interest rate and foreign exchange exposures. At inception these contracts are evaluated in order to determine if they qualify for hedge accounting treatment and are accounted for either on a deferral, accrual or market value basis, depending on the nature of the Company's hedge strategy and the method used to account for the hedged item. Hedge criteria include demonstrating the manner in which the hedge will reduce risk, identifying the specific asset, liability or firm commitment being hedged, and citing the time horizon being hedged. A monthly evaluation is performed to ensure that continuing correlation exists between the hedge and the item being hedged.

Net interest settlements on interest rate swap, cap and floor agreements are recognized on an accrual basis as interest income or interest expense of the related asset or liability over the lives of the agreements. Premiums paid or received for interest rate caps and floors are amortized either to interest income or to interest expense of the related asset or liability over the lives of the agreements. If an agreement is terminated early, any resulting gain or loss is deferred and amortized as interest income or interest expense of the related asset or liability over the remaining life of the original agreement. Net settlement amounts are reported gross as other assets and other liabilities. Cash flows are reported net as operating activities.

Foreign Currency Translation

Assets, liabilities and results of operations for foreign branches are recorded based on the functional currency of each branch. Since the functional currency of the branches is the local currency, the net assets are remeasured into U.S. dollars using a combination of current and historical exchange rates. The resulting gains or losses are included in shareholders' equity, as a component of accumulated other comprehensive income, on a net of tax basis.

Transfers and Servicing of Financial Assets and Extinguishment of Liabilities

On January 1, 1997, the Company adopted SFAS No. 125, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities". The Statement establishes standards for when transfers of financial assets, including those with continuing involvement by the transferor, should be considered a sale. SFAS No. 125 also establishes standards for when a liability should be considered extinguished. This Statement is effective for transfers of assets and extinguishments of liabilities occurring after December 31, 1996 and has been applied prospectively. In December 1996, the Financial Accounting Standards Board (FASB) reconsidered certain provisions of SFAS No. 125 and issued SFAS No. 127, "Deferral of the Effective Date of Certain Provisions of FASB Statement No. 125", to defer for one year the effective date of implementation for transactions related to repurchase agreements, dollar-roll repurchase agreements, securities lending and similar transactions. Management determined that the effect of adoption of SFAS No. 125 and SFAS No. 127 on the Company's financial statements was not material.

Income Taxes

The Company files consolidated federal and combined state income tax returns. Amounts provided for income tax expense are based on income reported for financial statement purposes and do not necessarily represent amounts currently payable under tax laws. Deferred taxes, which arise principally from temporary differences between the period in which certain income and expenses are recognized for financial accounting purposes and the period in which they affect taxable income, are included in the amounts provided for income taxes. Under this method, the computation of the net deferred tax liability or asset gives current recognition to changes in the tax laws.

Notes to Consolidated Financial Statements

December 31, 1996, 1997, and 1998

Net Income Per Common Share

Basic earnings per share (EPS) is computed by dividing net income after preferred dividends by the weighted average number of common shares outstanding during the period. Diluted EPS incorporates the dilutive effect of common stock equivalents outstanding on an average basis during the period. Stock options (see Note 12) are a common stock equivalent. Also see Note 17.

Comprehensive Income

On January 1, 1998, the Company adopted SFAS No. 130, "Reporting Comprehensive Income", which requires that an enterprise report and display, by major components and as a single total, the change in its net assets during the period from non-owner sources. The adoption of this Statement resulted in a change in the financial statement presentation, but did not have an impact on the Company's consolidated financial position, results of operations or cash flows. As required by the provisions of SFAS No. 130, all prior period data presented has been restated. Also see Note 18.

Employee Benefit and Incentive Plans and Other Postretirement Benefits

The Company provides a variety of benefit and incentive compensation plans for eligible employees and retirees. Provisions for the costs of these employee benefit and incentive plans and postretirement benefit plans are accrued and charged to expense when the benefit is earned.

During 1998, the Company adopted SFAS No. 132, "Employers' Disclosures about Pensions and Other Post-retirement Benefits", and, accordingly, has revised the disclosures for pensions and other postretirement benefits. Adoption of this Statement did not impact the Company's consolidated financial position, results of operations, or cash flows, and any effect was limited to the form and content of its disclosures. As required by the provisions of SFAS No. 132, all prior period data presented has been restated. Also see Note 6.

Stock-Based Compensation

As allowed under the provisions of SFAS No. 123, "Accounting for Stock-Based Compensation", the Company has chosen to continue to recognize compensation expense using the intrinsic value-based method of valuing stock options prescribed in Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" and related Interpretations. Under the intrinsic value-based method, compensation cost is measured as the amount by which the quoted market price of the Company's stock at the date of grant exceeds the stock option exercise price.

Compensation cost associated with the Company's unvested restricted stock issued under the management stock plan is measured based on the market price of the stock at the grant date and is expensed over the vesting period.

Segment Reporting

During 1998, the Company adopted SFAS No. 131, "Disclosures about Segments of an Enterprise and Related Information". SFAS No. 131 establishes annual and interim reporting standards for an enterprise's operating segments and related disclosures about its products, services, geographic areas, and major customers. Adoption of this Statement did not impact the Company's consolidated financial position, results of operations, or cash flows, and any effect was limited to the form and content of its disclosures.

Pending Accounting Pronouncements

In June 1998, the FASB issued SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities". The Statement will require the Company to recognize all derivatives on the balance sheet at fair value. SFAS No. 133 requires that derivative instruments used to hedge be identified specifically to assets, liabilities, firm commitments or anticipated transactions and measured as to effectiveness and ineffectiveness when hedging changes in fair value or cash flows. Derivative instruments that do not qualify as either a fair value or cash flow hedge will be valued at fair value with the resultant gain or loss recognized in current earnings. Changes in the effective portion of fair value hedges will be recognized in current earnings along with the change in fair value of the hedged item. Changes in the effective portion of the fair value of cash flow hedges will be recognized in other comprehensive income until realization of the cash flows of the hedged item through current earnings. Any ineffective portion of hedges will be recognized in current earnings. Management believes that, depending upon the accumulated net gain or loss of the effective portion of cash flow hedges at the date of adoption, the impact of SFAS No. 133 could have a material impact on other comprehensive income. However, management believes that any ineffective portion of cash flow hedges or any other

Notes to Consolidated Financial Statements

December 31, 1996, 1997, and 1998

hedges will not have a material impact on the Company's financial position or results of operations. This Statement is effective for fiscal years beginning after June 15, 1999, with earlier application encouraged. The Company expects to adopt SFAS No. 133 as of January 1, 2000.

In October 1998, the FASB issued SFAS No. 134, "Accounting for Mortgage-Backed Securities Retained after the Securitization of Mortgage Loans Held for Sale by a Mortgage Banking Enterprise". This Statement amends SFAS No. 65, "Accounting for Certain Mortgage Banking Activities", which established accounting and reporting standards for certain activities of mortgage banking and other similar enterprises. After securitization of mortgage loans held for sale, SFAS No. 134 requires an entity to classify the resulting mortgage-backed securities or other retained interests based on its ability or intent to sell or hold those investments. Management believes that the adoption of SFAS No. 134 will have no impact on the Company's financial position or results of operations. This Statement is effective for fiscal years beginning after December 15, 1998, with earlier application permitted. The Company expects to adopt SFAS No. 134 on January 1, 1999.

In March 1998, the American Institute of Certified Public Accountants (AICPA) issued Statement of Position (SOP) 98-1, "Accounting for the Costs of Computer Software Developed or Obtained for Internal Use". SOP 98-1 requires the capitalization of eligible costs of specified activities related to computer software developed or obtained for internal use. Management believes that the adoption of SOP 98-1 will not have a material effect on the Company's financial position or results of operations. The Statement is effective for fiscal years beginning after December 15, 1998, with earlier adoption encouraged. The Company expects to adopt SOP 98-1 on January 1, 1999.

In April 1998, the AICPA issued SOP 98-5, "Reporting on the Costs of Start-Up Activities". SOP 98-5 requires that entities expense start-up costs and organization costs as they are incurred. Management believes that the adoption of SOP 98-5 will not have a material effect on the Company's financial position or results of operations. The Statement is effective for fiscal years beginning after December 15, 1998, with earlier adoption encouraged. The Company expects to adopt SOP 98-5 on January 1, 1999.

Note 2.

Securities

The amortized cost, gross unrealized gains, gross unrealized losses, and fair values of securities are presented below.

Securities Available for Sale

December 31,	1997				**1998**			
(Dollars in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	**Amortized Cost**	**Gross Unrealized Gains**	**Gross Unrealized Losses**	**Fair Value**
U.S. Treasury	$ 987,374	$10,793	$ 170	$ 997,997	**$ 753,991**	**$16,341**	**$ —**	**$ 770,332**
Other U.S. government	709,536	6,005	67	715,474	**856,463**	**12,364**	**—**	**868,827**
Mortgage-backed securities	679,692	3,331	265	682,758	**1,875,141**	**9,271**	**2,634**	**1,881,778**
State and municipal	90,937	13,236	—	104,173	**72,777**	**11,469**	**—**	**84,246**
Corporate debt securities	2,698	311	1	3,008	**8,069**	**—**	**—**	**8,069**
Equity securities	28,881	1,596	672	29,805	**18,149**	**252**	**—**	**18,401**
Foreign securities	5,132	39	—	5,171	**6,799**	**121**	**41**	**6,879**
Total securities available for sale	$2,504,250	$35,311	$1,175	$2,538,386	**$3,591,389**	**$49,818**	**$2,675**	**$3,638,532**

Notes to Consolidated Financial Statements

December 31, 1996, 1997, and 1998

Securities Held to Maturity

December 31,	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	1997				1998			
(Dollars in thousands)								
U.S. Treasury	$ 40,092	$1,333	$ —	$ 41,425	$ 40,047	$1,050	$ —	$ 41,097
Other U.S. government	99,520	2,568	—	102,088	89,783	1,392	—	91,175
Mortgage-backed securities	24,477	1,745	14	26,208	15,247	1,178	—	16,425
State and municipal	24,686	75	1,367	23,394	15,436	4	893	14,547
Total securities held to maturity	$188,775	$5,721	$1,381	$193,115	$160,513	$3,624	$893	$163,244

The amortized cost and fair value of securities, by contractual maturity, are shown below. Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations, with or without call or prepayment penalties.

Maturity Schedule of Securities

December 31, 1998	Securities Available for Sale[1]		Securities Held to Maturity[1]	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
(Dollars in thousands)				
Due in one year or less	$ 657,328	$ 662,332	$109,829	$111,688
Due after one year through five years	1,037,195	1,063,390	22,093	22,711
Due after five years through ten years	343,504	348,998	8,749	9,129
Due after ten years	1,535,213	1,545,411	19,842	19,716
Equity securities	18,149	18,401	—	—
Total securities	$3,591,389	$3,638,532	$160,513	$163,244

[1] The remaining contractual maturities of mortgage-backed securities were allocated assuming no prepayments. The contractual maturity of these securities is not a reliable indicator of their expected life because borrowers have the right to repay their obligations at any time.

During the years ended 1996, 1997 and 1998, there were no sales or transfers from the securities held to maturity portfolio.

In 1996, proceeds from sales of securities available for sale were $20 million with gross realized gains of $5 million and no gross realized losses. In 1997, proceeds from sales of securities available for sale were $172 million with gross realized gains of $3 million and no gross realized losses. In 1998, proceeds from sales of securities available for sale were $418 million with gross realized gains of $6 million and no gross realized losses.

Notes to Consolidated Financial Statements

December 31, 1996, 1997, and 1998

Note 3.

Loans and Allowance for Credit Losses

A summary of loans net of unearned interest and fees of $128 million and $126 million at December 31, 1997 and 1998, respectively, is as follows:

December 31,	1997	**1998**
(Dollars in thousands)		
Domestic:		
Commercial, financial and industrial	$10,747,179	**$13,119,534**
Construction	293,333	**439,806**
Mortgage:		
Residential	2,961,233	**2,627,668**
Commercial	2,951,807	**2,975,484**
Total mortgage	5,913,040	**5,603,152**
Consumer:		
Installment	2,090,752	**1,984,941**
Home equity	992,916	**818,199**
Credit card and other lines of credit	270,097	**—**
Total consumer	3,353,765	**2,803,140**
Lease financing	874,860	**1,032,148**
Total loans in domestic offices	21,182,177	**22,997,780**
Loans originated in foreign branches	1,559,231	**1,298,331**
Total loans	22,741,408	**24,296,111**
Allowance for credit losses	451,692	**459,328**
Loans, net	$22,289,716	**$23,836,783**

Changes in the allowance for credit losses were as follows:

Years Ended December 31,	1996	1997	**1998**
(Dollars in thousands)			
Balance, beginning of year	$555,149	$523,946	**$451,692**
Loans charged off	(119,100)	(122,779)	**(76,790)**
Recoveries of loans previously charged off	48,024	51,014	**41,144**
Total net loans charged off	(71,076)	(71,765)	**(35,646)**
Provision for credit losses	40,000	—	**45,000**
Transfer of reserve for trading account assets	—	—	**(1,911)**
Foreign translation adjustment and other net deductions	(127)	(489)	**193**
Balance, end of year	$523,946	$451,692	**$459,328**

In 1998, the Company reclassified a $1.9 million previously established reserve for credit losses related to interest rate derivatives and foreign exchange contracts from the unallocated portion of the allowance for credit losses. The reserve for derivative and foreign exchange contracts is presented as an offset to trading account assets. Future changes in the reserve as a result of changes in the positive replacement cost of those contracts will be provided as an offset to trading gains and losses.

Nonaccrual loans totaled $109 million and $78 million at December 31, 1997 and 1998, respectively. There were no renegotiated loans at December 31, 1997 and 1998. Interest foregone on loans designated as nonaccrual at December 31, 1996, 1997 and 1998 was $9 million, $6 million and $4 million, respectively.

Loan Impairment

Impaired loans of the Company include commercial, financial and industrial, construction and commercial mortgage loans designated as nonaccrual. When the value of an impaired loan is less than the recorded investment in the loan, a portion of the Company's allowance for credit losses is allocated as an impairment allowance.

The Company's policy for recognition of interest income, chargeoffs of loans, and application of payments on impaired loans is the same as the policy applied to nonaccrual loans.

The following table sets forth information about the Company's impaired loans.

December 31,	1996	1997	**1998**
(Dollars in thousands)			
Impaired loans with an allowance	$ 69,886	$ 59,351	**$49,741**
Impaired loans without an allowance[1]	43,962	49,033	**28,709**
Total impaired loans[2]	$113,848	$108,384	**$78,450**
Allowance for impaired loans	$ 21,260	$ 9,418	**$11,219**
Average balance of impaired loans during the year	$145,351	$120,096	**$91,233**
Interest income recognized on nonaccrual loans during the year	$ 4,795	$ 2,506	**$ 274**

(1) These loans do not require an allowance for credit losses since the fair values of the impaired loans equal or exceed the recorded investments in the loans.

(2) This amount was evaluated for impairment using three measurement methods as follows: $38 million, $27 million, and $53 million was evaluated using the present value of the expected future cash flows at December 31, 1996, 1997 and 1998, respectively; $45 million, $53 million, and $8 million was evaluated using the fair value of the collateral at December 31, 1996, 1997 and 1998, respectively; and $31 million, $28 million, and $17 million was evaluated using historical loss factors at December 31, 1996, 1997 and 1998, respectively.

Notes to Consolidated Financial Statements

December 31, 1996, 1997, and 1998

Related Party Loans

In some cases, the Company makes loans to related parties including its directors, executive officers, and their affiliated companies. At December 31, 1997, related party loans outstanding to individuals who served as directors or executive officers at anytime during the year totaled $38 million, as compared to $138 million at December 31, 1998. In the opinion of management, these related party loans were made on substantially the same terms, including interest rates and collateral requirements, as those terms prevailing at the date these loans were made. During 1997 and 1998, there were no loans to related parties which were charged off. Additionally, at December 31, 1997 and 1998, there were no loans to related parties which were nonperforming.

Note 4.

Premises and Equipment

Premises and equipment are carried at cost, less accumulated depreciation and amortization. As of December 31, 1997 and 1998, the amounts were:

December 31,	Cost	Accumulated Depreciation and Amortization	Net Book Value	**Cost**	**Accumulated Depreciation and Amortization**	**Net Book Value**
		1997			**1998**	
(Dollars in thousands)						
Land	$ 69,290	$ —	$ 69,290	**$ 68,598**	**$ —**	**$ 68,598**
Premises	253,752	101,997	151,755	**261,271**	**108,114**	**153,157**
Leasehold improvements	135,609	80,019	55,590	**143,810**	**84,767**	**59,043**
Furniture, fixtures and equipment	400,774	271,110	129,664	**442,914**	**302,621**	**140,293**
Total	$859,425	$453,126	$406,299	**$916,593**	**$495,502**	**$421,091**

Rental and depreciation and amortization expenses were as follows:

Years Ended December 31,	1996	1997	**1998**
(Dollars in thousands)			
Rental expense of premises	$66,189	$46,556	**$51,695**
Less: rental income	11,904	11,049	**12,161**
Net rental expense	$54,285	$35,507	**$39,534**
Other net rental expense (income), primarily for equipment	$ 2,218	$ 298	**$ (374)**
Depreciation and amortization of premises and equipment	$51,821	$53,652	**$56,490**

Future minimum lease payments are as follows:

(Dollars in thousands)	**December 31, 1998**
Years ending December 31,	
1999	**$ 49,473**
2000	**45,214**
2001	**42,314**
2002	**34,594**
2003	**29,857**
Later years	**120,319**
Total minimum operating lease payments	**$321,771**
Minimum rental income due in the future under noncancellable subleases	**$ 45,880**

Included in other liabilities in the accompanying December 31, 1998 Consolidated Balance Sheet is $11 million of future operating lease payments accrued in connection with the merger (also see Note 7).

A majority of the leases provide for the payment of taxes, maintenance, insurance, and certain other expenses applicable to the leased premises. Many of the leases contain extension provisions, escalation clauses, and purchase options. There are no restrictions on paying dividends, incurring additional debt or negotiating additional leases under the terms of the present lease agreements.

Note 5.

Deposits

At December 31, 1998, the Company had $393 million in domestic interest bearing time deposits with a remaining term of greater than one year, of which $110 million exceeded $100,000. Maturity information for all domestic interest bearing time deposits with a remaining term of greater than one year is summarized below.

(Dollars in thousands)	**December 31, 1998**
Due after one year through two years	**$189,863**
Due after two years through three years	**96,836**
Due after three years through four years	**67,830**
Due after four years through five years	**31,523**
Due after five years	**6,870**
Total	**$392,922**

Notes to Consolidated Financial Statements

December 31, 1996, 1997, and 1998

Substantially all of the foreign interest bearing time deposits exceeding $100,000 mature in less than one year.

Note 6.

Employee Benefit and Incentive Plans and Other Postretirement Benefits

Retirement Plans

The Company maintains the Union Bank of California, N.A. Retirement Plan (the Plan), which is a noncontributory defined benefit plan covering substantially all of the employees of the Company. The plan provides retirement benefits based on years of credited service and the final average compensation amount, as defined in the Plan. Employees become eligible for this plan after one year of service and become fully vested after five years of service. The Company's funding policy is to make contributions equal to the maximum deductible amount as allowed by the Internal Revenue Code. Contributions are intended to provide not only for benefits attributed to services to date, but also for those expected to be earned in the future. Plan assets are invested in U.S. government securities, corporate bonds, and commingled investment funds.

In 1996, the Company maintained a second plan for former BanCal Tri-State Corporation employees. The former plan, which was terminated effective January 1, 1997, was a defined contribution plan. The Company's expense for pension contributions for the year ended December 31, 1996 was $5 million.

Other Postretirement Benefits

The Company provides certain health care and life insurance benefits for its retired employees. The health care cost is shared between the Company and the retiree. The life insurance plan is noncontributory. The accounting for the health care plan anticipates future cost-sharing changes to the written plan that are consistent with the Company's intent to maintain a level of cost-sharing at approximately 25 percent. Assets set aside to cover such obligations are primarily invested in mutual funds.

The following table sets forth the funded status of the Company's defined benefit pension plan and its other postretirement benefit plans.

	Pension Benefits		Other Benefits	
Years Ended December 31,	1997	**1998**	1997	**1998**
(Dollars in thousands)				
Change in benefit obligation				
Benefit obligation, beginning of year	$323,646	**$400,958**	$ 80,274	**$ 79,308**
Service cost	20,667	**22,697**	3,123	**3,067**
Interest cost	25,049	**28,475**	5,150	**5,067**
Plan participants' contributions	—	**—**	570	**919**
Amendments	10,926	**—**	—	**—**
Actuarial (gain) loss	31,588	**49,432**	(5,452)	**(258)**
Benefits paid	(10,918)	**(12,185)**	(4,357)	**(5,075)**
Benefit obligation, end of year	400,958	**489,377**	79,308	**83,028**
Change in plan assets				
Fair value of plan assets, beginning of year	381,194	**460,501**	21,703	**31,136**
Actual return on plan assets	66,765	**65,537**	4,445	**3,428**
Employer contribution	23,460	**23,234**	8,775	**9,060**
Plan participants' contributions	—	**—**	570	**919**
Benefits paid	(10,918)	**(12,185)**	(4,357)	**(5,075)**
Fair value of plan assets, end of year	460,501	**537,087**	31,136	**39,468**
Funded status	59,543	**47,710**	(48,172)	**(43,560)**
Unrecognized transition amount	(210)	**(61)**	59,813	**55,825**
Unrecognized net actuarial gain	(37,717)	**(23,505)**	(21,119)	**(20,314)**
Unrecognized prior service cost	12,915	**9,740**	—	**—**
Prepaid (accrued) benefit cost	$ 34,531	**$ 33,884**	$ (9,478)	**$ (8,049)**

Notes to Consolidated Financial Statements

December 31, 1996, 1997, and 1998

The following table summarizes the assumptions used in computing the present value of the projected benefit obligation and the net pension expense.

	Pension Benefits			Other Benefits		
Years Ended December 31,	1996	1997	**1998**	1996	1997	**1998**
Discount rate in determining expense	7.50%	7.50%	**7.00%**	7.50%	7.00%	**6.50%**
Discount rate in determining benefit obligations at year end	7.50	7.00	**6.50**	7.50	7.00	**6.50**
Rate of increase in future compensation levels for determining expense	5.50	5.50	**5.00**	—	—	**—**
Rate of increase in future compensation levels for determining benefit obligations at year end	5.50	5.00	**5.00**	—	—	**—**
Expected return on plan assets	8.25	8.25	**8.25**	8.00	8.00	**8.00**

The following table sets forth the components of postretirement benefit expense.

	Pension Benefits			Other Benefits		
Years Ended December 31,	1996	1997	**1998**	1996	1997	**1998**
(Dollars in thousands)						
Components of net periodic benefit cost						
Service cost	$ 12,651	$ 20,667	**$ 22,697**	$ 1,741	$ 3,123	**$ 3,067**
Interest cost	22,043	25,049	**28,475**	5,581	5,150	**5,067**
Expected return on plan assets	(23,877)	(27,119)	**(31,648)**	(1,335)	(1,736)	**(2,491)**
Amortization of prior service cost	2,108	3,175	**3,175**	—	—	**—**
Amortization of transition amount	(149)	(149)	**(149)**	3,988	3,987	**3,988**
Recognized net actuarial (gain) loss	—	—	**1,330**	(846)	(1,870)	**(2,000)**
Net periodic benefit cost	$ 12,776	$ 21,623	**$ 23,880**	$ 9,129	$ 8,654	**$ 7,631**

For 1996, the Company assumed a 9 percent annual rate of increase in the per capita cost of postretirement medical benefits for the indemnity plan and a 4 percent annual rate of increase was assumed for the health maintenance organization (HMO) plan. For future periods, the assumed rate for the indemnity plan gradually decreased from 9 percent to 5.5 percent in 2007 and remained level thereafter. The assumed rate of change on the HMO plan increased to 7 percent in 1997 and then gradually decreased to 5.5 percent in 2007 and thereafter.

For 1997, the Company assumed a 9 percent annual rate of increase in the per capita cost of postretirement medical benefits for the indemnity plan and a 4 percent annual rate of increase was assumed for the HMO plan. For future periods, the rate for the indemnity plan was expected to gradually decrease from 9 percent to 5.5 percent in 2007 and remain at that level thereafter. The rate for the HMO plan was expected to increase after one year of being at a low rate and then gradually decrease to 5.5 percent in 2007 and thereafter.

For 1998, the Company assumed a 9 percent annual rate of increase in the per capita cost of postretirement medical benefits for the indemnity plan and a 7 percent annual rate of increase was assumed for the HMO plan. For future periods, the rate for the indemnity plan was expected to gradually decrease from 9 percent to 5.5 percent in 2007 and remain at that level thereafter. The rate for the HMO plan was expected to gradually decrease to 5.5 percent in 2007 and remain at that level thereafter.

Notes to Consolidated Financial Statements

December 31, 1996, 1997, and 1998

The healthcare cost trend rate assumption has a significant effect on the amounts reported for the health care plans. A one-percentage-point change in assumed health care cost trend rates would have the following effects.

	1-Percentage-Point Increase	1-Percentage-Point Decrease
(Dollars in thousands)		
Effect on total of service and interest cost components	$1,131	$ (932)
Effect on postretirement benefit obligation	9,757	(8,176)

Executive Supplemental Benefit Plans

The Company has several Executive Supplemental Benefit Plans (ESBP) which provide eligible employees with supplemental retirement benefits. The plans are unfunded. The accrued liability for ESBP's included in other liabilities in the Consolidated Balance Sheets was $25 million at December 31, 1997 and $28 million at December 31, 1998. The Company's expense relating to the ESBP's was $3 million for each of the years ended December 31, 1996, 1997 and 1998.

Section 401(k) Savings Plans

The Company has a defined contribution plan authorized under Section 401(k) of the Internal Revenue Code. All benefits-eligible employees with at least one year of service are eligible to participate in the plan. Employees may contribute up to 16 percent of their pre-tax covered compensation or up to 10 percent of their after-tax covered compensation through salary deductions. The Company contributes 50 percent of every pre-tax dollar an employee contributes up to the first 6 percent of the employee's pre-tax covered compensation. Effective January 1, 1997, employees are fully vested in the employer's contributions immediately. In addition, the Company may make a discretionary annual profit-sharing contribution up to 2.5 percent of an employee's pay. This profit-sharing contribution is for all eligible employees, regardless of whether an employee is participating in the 401(k) plan, and depends on the Bank's annual financial performance. All employer contributions are tax deductible by the Company. The Company's combined matching contribution expense was $9 million, $13 million and $12 million for the years ended December 31, 1996, 1997 and 1998, respectively.

Note 7.

Other Expenses

The detail of other expenses is as follows:

Years Ended December 31,	1996	1997	**1998**
(Dollars in thousands)			
Merchant transaction processing	$ 37,091	$ 42,274	**$ 43,926**
Communications	40,133	42,372	**41,710**
Professional services	24,342	28,075	**36,748**
Advertising and public relations	28,788	28,664	**31,897**
Data processing	22,140	25,973	**28,091**
Printing and office supplies	27,085	24,098	**26,716**
Other	118,448	135,029	**164,218**
Total other expenses	$298,027	$326,485	**$373,306**

In connection with the merger, the Company incurred merger and integration expense of $117 million and $6 million for the years ended 1996 and 1997 and none for the year ended 1998, as summarized in the following table.

Years Ended December 31,	1996	1997	**1998**
(Dollars in thousands)			
Balance, accrued merger and integration expense, beginning of year	$ —	$54,344	**$22,930**
Provision for merger and integration costs	117,464	6,037	**—**
Utilization:			
Cash	40,155	35,809	**2,890**
Noncash	22,965	1,642	**9,498**
Total utilization	63,120	37,451	**12,388**
Balance, accrued merger and integration expense, end of year	$ 54,344	$22,930	**$10,542**

Total merger and integration expense of $124 million was recorded to cover $38 million of personnel expense for severance, retention, and other employee related costs, $54 million for facilities expense related to redundant banking facilities, and $32 million in professional services and other expense. At December 31, 1998, the liability balance included amounts primarily for operating lease payments related to redundant banking facilities that are continuing over the expected term of the leases.

Notes to Consolidated Financial Statements

December 31, 1996, 1997, and 1998

Note 8.

Income Taxes

The components of income tax expense were as follows:

Years Ended December 31,	1996	1997	**1998**
(Dollars in thousands)			
Taxes currently payable:			
Federal	$ 86,159	$168,375	**$218,949**
State	23,180	8,441	**(44,731)**
Foreign	2,895	2,092	**2,760**
Total currently payable	112,234	178,908	**176,978**
Taxes deferred:			
Federal	47,575	49,437	**25,458**
State	3,455	10,499	**2,152**
Foreign	(372)	(122)	**487**
Total deferred	50,658	59,814	**28,097**
Total income tax expense	$162,892	$238,722	**$205,075**

The components of the net deferred tax balances of the Company were as follows:

December 31,	1997	**1998**
(Dollars in thousands)		
Deferred tax assets:		
Allowance for credit losses	$169,769	**$178,161**
Accrued income and expense	21,987	**33,434**
Accrued merger expense	15,641	**10,410**
Deferred state taxes	21,063	**4,910**
Net operating loss carryforwards	—	**14,974**
Other	7,585	**4,861**
Valuation allowance	—	**(14,974)**
Total deferred tax assets	236,045	**231,776**
Deferred tax liabilities:		
Leasing	297,891	**329,263**
Depreciation	17,192	**11,108**
Unrealized gain on securities available for sale	13,536	**18,033**
Total deferred tax liabilities	328,619	**358,404**
Net deferred tax liability	$ 92,574	**$126,628**

During 1998, a valuation allowance was established to offset deferred tax assets related to state income tax net operating loss carryforwards. The carryforwards expire on December 31, 2002, and are subject to various conditions and limitations. In the opinion of management, the Company may not meet the conditions necessary to realize the benefits of such carryforwards.

The following table is an analysis of the effective tax rate:

Years Ended December 31,	1996	1997	**1998**
Federal income tax rate	35%	35%	**35%**
Net tax effects of:			
State income taxes, net of federal income tax benefit	4	2	**(4)**
Tax-exempt interest income	(1)	(1)	**—**
Amortization of intangibles	1	1	**1**
Other	1	—	**(1)**
Effective tax rate	40%	37%	**31%**

During 1997, the Company received a refund from the State of California Franchise Tax Board of approximately $25 million, net of federal tax, in settlement of litigation, administration, and audit disputes covering the years 1975–1987. The refund was recorded as a reduction to state income tax expense.

The Company has filed its 1997, and intends to file its 1998, California franchise tax return on a worldwide unitary basis, incorporating the financial results of BTM and its worldwide affiliates. As a result, during 1998, the Company reduced its state income tax liabilities by $29 million, net of federal tax, for previously accrued 1997 state tax liabilities and lowered its 1998 state tax provision by $31 million, net of federal tax.

Federal and state tax returns for several years are under or subject to examination by the respective taxing authorities. Although the ultimate outcome of such examinations cannot be determined at this time, management believes that the resolution of issues that have been or may be raised will not have a material adverse effect on the Company's consolidated financial position or results of operations.

Notes to Consolidated Financial Statements

December 31, 1996, 1997, and 1998

Note 9.

Borrowed Funds

The following is a summary of the major categories of borrowed funds:

December 31,	1997	**1998**
(Dollars in thousands)		
Federal funds purchased and securities sold under repurchase agreements with weighted average interest rates of 5.38% and 4.88% at December 31, 1997 and 1998, respectively	$1,335,884	**$1,307,744**
Commercial paper, with weighted average interest rates of 5.64% and 5.01% at December 31, 1997 and 1998, respectively	966,575	**1,444,745**
Other borrowed funds, with weighted average interest rates of 6.23% and 5.35% at December 31, 1997 and 1998, respectively	476,010	**331,165**
Total borrowed funds	$2,778,469	**$3,083,654**
Federal funds purchased and securities sold under repurchase agreements:		
Maximum outstanding at any month end	$1,575,930	**$2,058,610**
Average balance during the year	1,097,707	**1,604,675**
Weighted average interest rate during the year	5.33%	**5.26%**
Commercial paper:		
Maximum outstanding at any month end	$1,876,135	**$1,918,700**
Average balance during the year	1,637,070	**1,631,216**
Weighted average interest rate during the year	5.49%	**5.42%**
Other borrowed funds:		
Maximum outstanding at any month end	$ 851,694	**$ 438,151**
Average balance during the year	635,900	**328,872**
Weighted average interest rate during the year	5.42%	**5.68%**

Note 10.

Subordinated Capital Notes and Preferred Stock

The following is a summary of capital notes that are subordinated to other obligations of the Company.

December 31,	1997	**1998**
(Dollars in thousands)		
Floating rate notes due June 2007. These notes bear interest at 0.325% above 3-month London Interbank Offered Rate (LIBOR) and are payable to BTM	$200,000	**$200,000**
Floating rate notes due July 2000. These notes bear interest at 0.30% above 3-month LIBOR	98,000	**98,000**
Floating rate notes due July 1998. These notes bear interest at 0.25% above 3-month LIBOR and are payable to BTM	50,000	**—**
Total subordinated capital notes	$348,000	**$298,000**

All of the above notes qualify as Tier 2 risk-based capital under the Federal Reserve guidelines for assessing regulatory capital. For the total risk-based capital ratio, the amount of notes that qualify as capital is reduced as the notes approach maturity. At December 31, 1997 and 1998, $239 million and $220 million, respectively, of the notes qualified as risk-based capital.

Provisions of several of the notes restrict the use of the Company's property as security for borrowings, and place limitations on leases, indebtedness, distributions to shareholders, mergers, sales of certain assets, transactions with affiliates, and changes in majority stock ownership of the Company.

The following table presents the maturities of subordinated capital notes.

(Dollars in thousands)	**December 31, 1998**
Years ending December 31, 2000	**$ 98,000**
Years after 2003	**200,000**
Total	**$298,000**

Notes to Consolidated Financial Statements

December 31, 1996, 1997, and 1998

At December 31, 1996, the Company had outstanding 1.35 million shares (or 5.4 million depositary shares) of 8⅜ percent Noncumulative Preferred Stock, Series A (Preferred Stock) totaling $135 million. On September 3, 1997, the Company redeemed all 1.35 million outstanding shares of its Preferred Stock, reducing shareholders' equity by $135 million. The redemption price was equal to the stated value of $100 per share of Preferred Stock (equivalent to $25 per depositary share), plus $2 million in accrued and unpaid dividends to the redemption date. The redemption was funded by proceeds from the issuance of $200 million in subordinated capital notes in June 1997.

Note 11.

Dividend Reinvestment and Stock Purchase Plan

The Company has a dividend reinvestment and stock purchase plan for shareholders. The plan allows shareholders to automatically reinvest all or part of their dividends in additional shares of the Company's common stock at a cost of 5 percent below the market price. Participating shareholders also have the option of purchasing additional shares at the full market price with cash payments of $25 to $3,000 per quarter. The Company obtains shares required for reinvestment through open market purchases or through the issuance of new shares from its authorized but unissued stock. During 1996, 1997 and 1998, 155,724, 131,127 and 83,727 shares, respectively, were required for dividend reinvestment purposes, of which 71,706, 3,687 and 5,166 shares were considered new issuances during 1996, 1997 and 1998, respectively. BTM did not participate in the plan in 1997 and 1998.

Note 12.

Management Stock Plan

The Company has a management stock plan (the Stock Plan) which has 6.6 million shares of the Company's common stock authorized to be awarded to key employees and outside directors of the Company and its subsidiaries at the discretion of the Executive Compensation and Benefits Committee of the Board of Directors (the Committee). Committee members and employees on rotational assignment from BTM are not eligible for stock awards.

The Committee determines the term of each stock option grant, up to a maximum of ten years from the date of grant. The exercise price of the options issued under the Stock Plan shall not be less than the fair market value on the date the option is granted. Unvested restricted stock issued under the Stock Plan is shown as a reduction to retained earnings. The value of the restricted shares at the date of grant is amortized to compensation expense over its vesting period. All cancelled or forfeited options and restricted stock become available for future grants.

In 1996, 1997 and 1998, the Company granted options to various key employees, including principal officers, under the Stock Plan. The stock options vest pro rata on each anniversary of the grant date and become fully exercisable three years from the grant date, provided that the employee has completed the specified continuous service requirement. They vest earlier if the employee dies, is permanently and totally disabled, or retires under certain grant, age, and service conditions.

The following is a summary of stock option transactions under the Stock Plan.

	Number of Shares	Weighted-Average Exercise Price	Number of Shares	Weighted-Average Exercise Price	**Number of Shares**	**Weighted-Average Exercise Price**
Years Ended December 31,	1996		1997		**1998**	
Options outstanding, beginning of year	1,082,106	$10.42	1,263,807	$12.13	**1,397,178**	**$15.41**
Granted	277,200	18.29	441,900	22.13	**533,850**	**35.08**
Exercised	(80,496)	10.69	(289,029)	10.84	**(169,995)**	**13.34**
Forfeited	(15,003)	10.47	(19,500)	22.13	**(20,952)**	**30.63**
Options outstanding, end of year	1,263,807	$12.13	1,397,178	$15.41	**1,740,081**	**$21.47**
Options exercisable, end of year	686,145	$10.38	712,107	$11.50	**894,432**	**$13.77**

The weighted-average fair value of options granted was $6.00 during 1996, $6.94 during 1997, and $11.99 during 1998.

Notes to Consolidated Financial Statements

December 31, 1996, 1997, and 1998

The following table summarizes information about stock options outstanding.

	Options Outstanding at December 31, 1998			Options Exercisable at December 31, 1998	
Range of Exercise Prices	Number Outstanding	Weighted-Average Remaining Contractual Life	Weighted-Average Exercise Price	Number Exercisable	Weighted-Average Exercise Price
$ 6.67–9.08	214,008	4.4 years	$ 8.51	214,008	$ 8.51
11.25–12.83	398,253	5.3	11.79	398,253	11.79
18.29–22.13	608,220	7.7	20.73	274,371	20.15
35.08	519,600	9.2	35.08	7,800	35.08
	1,740,081			894,432	

In 1996, 1997 and 1998, the Company also granted 133,440, 178,320 and 184,935 shares, respectively, of restricted stock to key officers, including executive officers, under the Stock Plan. The awards of restricted stock vest pro rata on each anniversary of the grant date and become fully vested four years from the grant date, provided that the employee has completed the specified continuous service requirement. They vest earlier if the employee dies, is permanently and totally disabled, or retires under certain grant, age, and service conditions. Restricted shareholders have the right to vote their restricted shares and receive dividends.

The following is a summary of restricted stock transactions under the Stock Plan.

	Number of Shares	Weighted-Average Grant Date Fair Value	Number of Shares	Weighted-Average Grant Date Fair Value	**Number of Shares**	**Weighted-Average Grant Date Fair Value**
Years Ended December 31,	1996		1997		**1998**	
Restricted stock awards outstanding, beginning of year	1,044,951	$ 8.99	1,166,820	$10.04	**1,337,217**	**$11.59**
Granted	133,440	18.29	178,320	22.18	**184,935**	**33.43**
Cancelled	(11,571)	10.78	(7,923)	20.08	**(17,850)**	**24.58**
Restricted stock awards outstanding, end of year	1,166,820	$10.04	1,337,217	$11.59	**1,504,302**	**$14.12**
Restricted stock awards vested, end of year	764,670	$ 8.35	942,738	$ 9.17	**1,115,229**	**$10.18**

At December 31, 1996, 1997 and 1998, 958,383, 3,365,586 and 2,685,603 shares, respectively, were available for future grants as either stock options or restricted stock under the Stock Plan.

The Company follows the intrinsic value based method in accounting for its employee stock-based compensation plan. Accordingly, no compensation cost has been recognized for its stock option grants. Had compensation cost for the Company's stock-based plan been determined based on the fair value at the grant dates for awards under that plan consistent with the method of SFAS No. 123, "Accounting for Stock-Based Compensation", the Company's net income and net income per share would have decreased to the pro forma amounts indicated in the following table. Options that

Notes to Consolidated Financial Statements

December 31, 1996, 1997, and 1998

were granted prior to January 1, 1995 with vesting periods in 1995 and later are excluded from the pro forma results indicated for 1996 in the following table.

Years Ended December 31,	1996	1997	**1998**
(Dollars in thousands, except per share data)			
Net income			
As reported	$249,458	$411,296	**$466,461**
Pro forma	248,874	410,068	**463,998**
Net income applicable to common stock			
As reported	$238,152	$403,696	**$466,461**
Pro forma	237,568	402,468	**463,998**
Net income per share—basic			
As reported	$ 1.37	$ 2.31	**$ 2.66**
Pro forma	1.36	2.30	**2.65**
Net income per share—diluted			
As reported	$ 1.36	$ 2.30	**$ 2.65**
Pro forma	1.36	2.30	**2.64**

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option pricing model with the following weighted-average assumptions used for grants made in 1996, 1997 and 1998: risk-free interest rates of 6.3 percent in 1996, 6.6 percent in 1997, and 5.8 percent in 1998; expected volatility of 28 percent in 1996, 26 percent in 1997, and 29 percent in 1998; expected lives of 7, 6 and 6 years for 1996, 1997 and 1998, respectively; and expected dividend yields of 2.6 percent in 1996, 2.1 percent in 1997, and 1.5 percent in 1998.

Effective January 1, 1997, the Company established a Performance Share Plan. Eligible participants may earn performance share awards to be redeemed in cash three years after the date of grant. Performance shares are linked to shareholder value in two ways: (1) the market price of the Company's common stock, and (2) return on assets, a performance measure closely linked to value creation. Eligible participants generally receive grants of performance shares annually. The total number of performance shares granted under the plan cannot exceed 600,000. The Company granted 14,400 shares in 1997 and 24,900 shares in 1998. In 1998, 2,400 performance shares were forfeited. The value of a performance share is equal to the market price of the Company's common stock. All cancelled or forfeited performance shares become available for future grants.

Note 13.

Fair Value of Financial Instruments

The fair value of a financial instrument is the amount at which the instrument could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale. All of the fair values presented below are as of their respective period ends and have been made under this definition of fair value unless otherwise disclosed.

It is management's belief that the fair values presented below are reasonable based on the valuation techniques and data available to the Company as of December 31, 1997 and 1998, as more fully described below. It should be noted that the operations of the Company are managed on a going concern basis and not on a liquidation basis. As a result, the ultimate value realized for the financial instruments presented could be substantially different when actually recognized over time through the normal course of operations. Additionally, a substantial portion of an institution's inherent value is its capitalization and franchise value. Neither of these components has been given consideration in the presentation of fair values that follow.

Notes to Consolidated Financial Statements

December 31, 1996, 1997, and 1998

The table below presents the carrying value and fair value of the specified assets and liabilities held by the Company.

December 31,	Carrying Value 1997	Fair Value 1997	**Carrying Value 1998**	**Fair Value 1998**
(Dollars in thousands)				
Assets				
Cash and cash equivalents	$ 3,199,455	$ 3,199,455	**$ 2,678,478**	**$ 2,678,478**
Trading account assets	394,313	394,313	**267,718**	**267,718**
Securities available for sale	2,538,386	2,538,386	**3,638,532**	**3,638,532**
Securities held to maturity	188,775	193,115	**160,513**	**163,244**
Loans, net of allowance for credit losses[1]	21,419,718	21,189,820	**22,808,435**	**22,568,873**
Liabilities				
Deposits:				
Noninterest bearing	8,849,544	8,849,544	**10,179,405**	**10,179,405**
Interest bearing	14,446,830	14,453,029	**14,328,474**	**14,343,972**
Total deposits	23,296,374	23,302,573	**24,507,879**	**24,523,377**
Borrowed funds	2,778,469	2,775,531	**3,083,654**	**3,081,418**
Subordinated capital notes	348,000	348,000	**298,000**	**298,000**

(1) Excludes lease financing.

The Company is also a party to financial instruments that are not reflected on the balance sheet but represent obligations of the Company in the normal course of business. For information regarding the fair value of off-balance sheet financial instruments, see Note 14.

The following methods and assumptions were used to estimate fair value of each class of financial instruments for which it is practicable to estimate that value.

Cash and cash equivalents: The book value of cash and cash equivalents is considered a reasonable estimate of fair value.

Trading account assets: Trading account assets are short term in nature and valued at market based on quoted market prices or dealer quotes. If a quoted market price is not available, the recorded amounts are estimated using quoted market prices for similar securities. Thus, carrying value is considered a reasonable estimate of fair value for these financial instruments.

Securities: The fair value of securities is based on quoted market prices or dealer quotes. If a quoted market price is not available, fair value is estimated using quoted market prices for similar securities. Securities available for sale are carried at their aggregate fair value, while securities held to maturity are carried at amortized cost.

Loans: The fair value for performing fixed and non-reference rate loans was estimated by discounting the future cash flows using the current rates at which similar loans would be made to borrowers with similar credit ratings and for similar remaining maturities and, where available, discount rates were based on current market rates.

Notes to Consolidated Financial Statements

December 31, 1996, 1997, and 1998

The fair value of performing loans tied to the Company's reference rate with normal credit risk is assumed to approximate their book value. The fair value for these floating rate loans with increasing credit risk was estimated by calculating their present value using a yield the Company would currently require for loans with similar terms to borrowers with similar credit quality.

Loans that are on nonaccrual status were not included in the loan valuation methods discussed previously. The fair value of these assets was estimated assuming these loans were sold on a liquidation basis.

The fair value of performing mortgage loans was based on quoted market prices for loans with similar credit and interest rate risk characteristics.

The fair value of performing credit card loans and credit lines is assumed to approximate their book value. For credit lines and credit card loans that were past due at December 31, 1997 and 1998, the fair value was estimated by segregating them according to their past due status and then discounting them based on the Company's historical probability of loss.

Noninterest bearing deposits: The fair value of noninterest bearing deposits is the amount payable on demand at the reporting date. The fair value of the demand deposit intangible has not been estimated.

Interest bearing deposits: The fair value of savings accounts and certain money market accounts is the amount payable on demand at the reporting date. The fair value of fixed maturity certificates of deposit was estimated using rates currently being offered on certificates with similar maturities.

Borrowed funds: The book values of federal funds purchased and securities sold under repurchase agreements and other short-term borrowings are assumed to approximate their fair value due to their limited duration characteristics. The fair value for commercial paper and term federal funds purchased was estimated using market quotes.

Subordinated capital notes: The fair value of fixed-rate subordinated capital notes was estimated using discounted cash flows based on market rates for A-rated bank borrowings. The book values for variable-rate subordinated capital notes are assumed to approximate fair market value.

Note 14.

Derivative Instruments and Other Financial Instruments With Off-Balance Sheet Risk

The Company is a party to certain derivative and other financial instruments that are not reflected on the balance sheet but represent obligations or assets of the Company in the normal course of business. These financial instruments are used for trading activities of the Company, to meet the needs of customers, and to reduce the impact on the Company's operating results due to market fluctuations in currency or interest rates.

These financial instruments involve, to varying degrees, elements of credit and market risk which are not recognized on the balance sheet. Credit risk is defined as the possibility that a loss may occur from the failure of another party to perform in accordance with the terms of the contract which exceeds the value of the existing collateral, if any. Market risk is the possibility that future changes in market conditions may make the financial instrument less valuable.

Derivative Instruments

The fair value of the derivative financial instruments was calculated based on quoted market prices where available. If quoted market prices were not available, the Company used the estimated amount it would receive or pay to offset or terminate the agreements at December 31, 1998 based upon the terms of such contracts relative to prevailing interest rates.

Trading Activities in Derivative Instruments

The following table reflects the Company's positions relating to trading activities in derivative instruments. Trading activities include both activities for the Company's own account and for customers. At December 31, 1997 and 1998, the majority of the Company's derivative transactions for customers are hedged with essentially offsetting contracts with other counterparties. The average fair value of derivatives held or written for trading purposes during the year is not significant. The notional amount of derivative instruments reflects the extent of the Company's involvement in these instruments. For interest rate swap, cap and floor agreements, notional amounts do not represent exposure to credit or market risk. Notional amounts are not exchanged, but serve as a point of reference for calculating payments.

Notes to Consolidated Financial Statements

December 31, 1996, 1997, and 1998

The following is a summary of derivative instruments held or written for trading purposes.

December 31,	Notional Amounts 1997	Credit Risk[1] 1997	Estimated Fair Value 1997	**Notional Amounts 1998**	**Credit Risk[1] 1998**	**Estimated Fair Value 1998**
(Dollars in thousands)						
Held or Written for Trading Purposes and Customer Accommodations						
Foreign exchange forward contracts:						
Commitments to purchase	$ 531,330	$ 366	$(34,304)	**$ 451,123**	**$22,297**	**$ 20,675**
Commitments to sell	709,512	40,671	40,274	**553,351**	**1,878**	**(21,599)**
Foreign exchange OTC options:						
Options purchased	46,533	—	(634)	**3,000**	**1**	**1**
Options written	46,533	637	637	**3,000**	**—**	**(1)**
Currency swap agreements:						
Commitments to pay	55,725	—	(5,971)	**36,725**	**1,546**	**1,546**
Commitments to receive	55,725	5,971	5,971	**36,725**	**—**	**(1,436)**
Interest rate contracts:						
Caps purchased	1,189,791	796	796	**1,031,599**	**1,453**	**1,453**
Floors purchased	119,000	612	612	**186,564**	**926**	**926**
Caps written	1,189,791	—	(796)	**1,031,599**	**—**	**(1,453)**
Floors written	119,000	—	(612)	**186,564**	**—**	**(926)**
Swap contracts:						
Pay variable/receive variable	58,000	301	—	**58,000**	**306**	**—**
Pay fixed/receive variable	976,180	364	(29,579)	**1,040,042**	**1,049**	**(41,593)**
Pay variable/receive fixed	976,180	30,240	29,926	**1,040,042**	**44,360**	**43,430**

[1] Credit risk amounts reflect the replacement cost for those contracts in a gain position in the event of nonperformance by counterparties.

Asset and Liability Management Derivative Instruments

Derivative positions are integral components of the Company's designated asset and liability management activities. Therefore, the Company does not believe it is meaningful to separately analyze the derivative components of its risk management activities in isolation from related positions. The Company uses interest rate derivative instruments as part of its management of asset and liability positions. Derivatives are used to manage interest rate risk relating to specified groups of assets and liabilities, including LIBOR-based commercial loans, deposit liabilities, and certain subordinated capital notes. The Company uses foreign currency forward contracts as a means of managing foreign exchange rate risk associated with assets or liabilities denominated in foreign currencies.

The following table reflects summary information on derivative contracts used to hedge or modify the Company's risk as of December 31, 1997 and 1998. Amounts included in the fair value column do not include gains or losses from changes in the value of the underlying asset or liability being hedged. Notional amounts are not exchanged, but serve as a point of reference for calculating payments. For interest rate swap, cap and floor agreements, notional amounts do not represent exposure to credit or market risk.

Notes to Consolidated Financial Statements

December 31, 1996, 1997, and 1998

December 31,	Notional Amounts 1997	Unamortized Premium Paid (Received) 1997	Credit Risk[1] 1997	Estimated Fair Value 1997	**Notional Amounts 1998**	**Unamortized Premium Paid (Received) 1998**	**Credit Risk[1] 1998**	**Estimated Fair Value 1998**
(Dollars in thousands)								
Held for Asset and Liability Management Purposes								
Foreign exchange forward contracts:								
Commitments to purchase	$ 341,298	$ —	$ 862	$(5,055)	**$ 233,380**	**$ —**	**$ 2,185**	**$ 989**
Commitments to sell	51,754	—	35	(822)	**53,607**	**—**	**235**	**145**
Currency swap agreements:								
Commitments to pay	26,400	—	2,590	2,590	**25,432**	**—**	**—**	**(1,104)**
Interest rate contracts:								
Caps purchased	15,420	—	—	—	**—**	**—**	**—**	**—**
Floors purchased	3,550,000	11,730	4,040	4,040	**2,350,000**	**5,737**	**24,303**	**24,303**
Caps written	250,000	(335)	273	273	**—**	**—**	**—**	**—**
Floors written	1,850,000	(534)	—	(1,309)	**1,350,000**	**—**	**—**	**(3,740)**
Swap contracts:								
Pay variable/receive fixed	575,000	—	2,302	2,302	**525,000**	**—**	**9,755**	**9,755**

[1] Credit risk amounts reflect the replacement cost for those contracts in a gain position in the event of nonperformance by counterparties.

Other Financial Instruments with Off-Balance Sheet Risk

Commitments to extend credit are legally binding agreements to lend to a customer provided there are no violations of any condition established in the contract. Commitments have fixed expiration dates or other termination clauses and may require payment of a fee or maintenance of compensatory balances. Such fees are deferred and, upon partial or full exercise of the commitment, amortized over the life of the loan or, if exercise is deemed remote, amortized over the commitment period. Since many of the commitments are expected to expire without being drawn upon, the contractual amounts do not necessarily represent future cash requirements. With respect to commitments to extend credit and letters of credit, the Company's exposure to credit risk in the event of nonperformance by customers is represented by the contractual amount of those instruments.

Standby letters of credit are provided to customers to assure their performance to a third party, generally in the production of goods and services or under contractual commitments in the financial markets. Commercial letters of credit are issued to customers to facilitate foreign or domestic trade transactions. The Company charges fees for the issuance of standby and commercial letters of credit. The majority of these types of commitments have terms of one year or less and any fees charged are recognized as noninterest income upon extension of the commitment. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers and is represented by the contractual amount of those instruments. When deemed necessary, the Company holds appropriate collateral supporting those commitments. Management does not anticipate any material losses as a result of these transactions.

The Company uses the same credit underwriting policies in granting or accepting such commitments or contingent obligations as it does for on-balance sheet instruments, by evaluating customers' credit worthiness. The amount of collateral obtained, if deemed necessary by the Company upon extension of credit, is based on management's evaluation of the customer. The nature of the collateral varies but may include deposits held in financial institutions, marketable securities, accounts receivable, inventory, property and equipment, and real estate. The Company also provides for potential losses from either commitments to extend credit or standby letters of credit as a component of its evaluation in determining the adequacy of its allowance for credit losses and resulting level of provision charged against current period earnings.

The Company's pricing of these financial instruments is based on the credit quality and other covenants or

Notes to Consolidated Financial Statements
December 31, 1996, 1997, and 1998

requirements. Management believes that the current fees assessed on these off-balance sheet items represent market rates that would be charged for similar agreements. Based on this belief, the Company feels that the carrying amounts are reasonable estimates of the fair value of these financial instruments. At December 31, 1997 and 1998, fair value represents management's estimate of the unamortized fee income associated with these instruments. The following is a summary of other financial instruments with off-balance sheet risk.

December 31,	Contractual Amounts 1997	Fair Value 1997	**Contractual Amounts 1998**	**Fair Value 1998**
(Dollars in thousands)				
Commitments to extend credit	$15,111,062	$27,571	**$14,850,571**	**$36,592**
Standby letters of credit	2,289,878	5,776	**2,215,476**	**8,523**
Other letters of credit	314,594	—	**305,842**	**—**

The Company conducts securities lending transactions for institutional customers as a fully disclosed agent, and, at times, indemnifies its customers against counterparty default. All lending transactions are collateralized, primarily by cash. The amount of securities lent with indemnification was $1,268 million and $1,259 million at December 31, 1997 and 1998, respectively. The market value of the associated collateral was $1,294 million and $1,284 million at December 31, 1997 and 1998, respectively.

Note 15.

Restrictions on Cash and Due From Banks, Securities, Loans and Dividends

Federal Reserve Board regulations require the Bank to maintain reserve balances based on the types and amounts of deposits received. Average reserve balances were approximately $339 million and $229 million for the years ended December 31, 1997 and 1998, respectively.

As of December 31, 1997 and 1998, securities carried at $1.7 billion for each of the years, and loans of $2.6 billion and $2.5 billion, respectively, were pledged as collateral for borrowings, to secure public and trust department deposits, and for repurchase agreements as required by contract or law.

The Federal Reserve Act restricts the extension of credit by the Bank to BTM and affiliates and to the Company and its non-bank subsidiaries and requires that such loans be secured by certain types of collateral. At December 31, 1998, $67 million remained outstanding on three Bankers Commercial Corporation notes payable to the Bank, and $7 million remained outstanding on a UnionBanCal Leasing Corporation note payable to the Bank. The respective notes were fully collateralized with equipment leases pledged by both Bankers Commercial Corporation and UnionBanCal Leasing Corporation.

The payment of dividends by the Bank to the Company is subject to the approval of the Office of the Comptroller of the Currency (OCC) if the total of all dividends declared in any calendar year exceeds certain calculated amounts. The payment of dividends is also limited by minimum capital requirements imposed on national banks by the OCC. At December 31, 1998, the Bank could have declared dividends aggregating $354 million without prior regulatory approval.

Note 16.

Regulatory Capital Requirements

The Company and the Bank are subject to various regulatory capital requirements administered by the federal banking agencies, including minimum capital requirements. Failure to meet minimum capital requirements can initiate certain mandatory, and possibly additional discretionary, actions by regulators that, if undertaken, could have a direct material effect on the Company's Consolidated Financial Statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Company and the Bank must meet specific capital guidelines that involve quantitative measures of the Company's and Bank's assets, liabilities, and certain off-balance sheet items as calculated under regulatory accounting practices. The Company's and the Bank's capital amounts and the Bank's prompt corrective action classification are also subject to qualitative judgments by the regulators about components, risk weightings and other factors.

Quantitative measures established by regulation to ensure capital adequacy require the Company and the Bank to maintain minimum amounts and ratios (set forth in the table below) of total and Tier 1 capital (as defined in the regulations) to risk-weighted assets (as defined) and of Tier 1

Notes to Consolidated Financial Statements

December 31, 1996, 1997, and 1998

capital (as defined) to quarterly average assets (as defined). Management believes, as of December 31, 1998, that the Company and the Bank met all capital adequacy requirements to which they are subject.

As of December 31, 1997 and 1998, the most recent notification from the OCC categorized the Bank as "well capitalized" under the regulatory framework for prompt corrective action. To be categorized as "well capitalized", the Bank must maintain minimum total risk-based, Tier 1 risk-based, and Tier 1 leverage ratios as set forth in the following table. There are no conditions or events since that notification that management believes have changed the Bank's category.

The Company's and the Bank's capital amounts and ratios are presented in the following tables.

	Actual		For Capital Adequacy Purposes	
	Amount	Ratio	Amount	Ratio
(Dollars in thousands)				
Capital Ratios for the Company:				
As of December 31, 1997:				
Total capital (to risk-weighted assets)	$3,188,173	11.05%	≥ $2,308,988	≥ 8.0%
Tier 1 capital (to risk-weighted assets)	2,587,071	8.96	≥ 1,154,494	≥ 4.0
Tier 1 capital (to quarterly average assets)[1]	2,587,071	8.53	≥ 1,213,381	≥ 4.0
As of December 31, 1998				
Total capital (to risk-weighted assets)	$3,570,803	11.61%	≥ $2,460,243	≥ 8.0%
Tier 1 capital (to risk-weighted assets)	2,965,865	9.64	≥ 1,230,122	≥ 4.0
Tier 1 capital (to quarterly average assets)[1]	2,965,865	9.38	≥ 1,265,081	≥ 4.0

[1] Excludes certain intangible assets.

	Actual		For Capital Adequacy Purposes		To Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
(Dollars in thousands)						
Capital Ratios for the Bank:						
As of December 31, 1997:						
Total capital (to risk-weighted assets)	$3,025,030	10.58%	≥ $2,286,296	≥ 8.0%	≥ $2,857,870	≥ 10.0%
Tier 1 capital (to risk-weighted assets)	2,527,468	8.84	≥ 1,143,148	≥ 4.0	≥ 1,714,722	≥ 6.0
Tier 1 capital (to quarterly average assets)[1]	2,527,468	8.35	≥ 1,210,898	≥ 4.0	≥ 1,513,622	≥ 5.0
As of December 31, 1998						
Total capital (to risk-weighted assets)	$3,396,596	11.16%	≥ $2,433,917	≥ 8.0%	≥ $3,042,396	≥ 10.0%
Tier 1 capital (to risk-weighted assets)	2,895,757	9.52	≥ 1,216,959	≥ 4.0	≥ 1,825,438	≥ 6.0
Tier 1 capital (to quarterly average assets)[1]	2,895,757	9.21	≥ 1,257,875	≥ 4.0	≥ 1,572,343	≥ 5.0

[1] Excludes certain intangible assets.

Notes to Consolidated Financial Statements

December 31, 1996, 1997, and 1998

Note 17.

Earnings Per Share

Basic EPS is computed by dividing net income after preferred dividends by the weighted average number of common shares outstanding during the period. Diluted EPS is computed based on the weighted average number of common shares outstanding adjusted for common stock equivalents, which include stock options. The following table presents a reconciliation of basic and diluted EPS for the years ended December 31, 1996, 1997 and 1998, in accordance with SFAS No. 128:

	Basic	Diluted	Basic	Diluted	**Basic**	**Diluted**
December 31,	1996		1997		**1998**	
(Amounts in thousands, except per share data)						
Net income	$249,458	$249,458	$411,296	$411,296	**$466,461**	**$466,461**
Less: Dividends on preferred stock	(11,306)	(11,306)	(7,600)	(7,600)	**—**	**—**
Income available to common shareholders	$238,152	$238,152	$403,696	$403,696	**$466,461**	**$466,461**
Weighted average common shares outstanding	174,391	174,391	174,683	174,683	**175,127**	**175,127**
Additional shares due to:						
Assumed conversion of dilutive stock options	—	393	—	506	**—**	**610**
Adjusted weighted average common shares outstanding	174,391	174,784	174,683	175,189	**175,127**	**175,737**
Net income per share	$ 1.37	$ 1.36	$ 2.31	$ 2.30	**$ 2.66**	**$ 2.65**

Options to purchase 277,200 shares of common stock at $18 per share and options to purchase 519,600 shares of common stock at $35 per share were outstanding but not included in the computation of diluted EPS in 1996 and 1998, respectively. There were no anti-dilutive options in 1997.

Note 18.

Accumulated Other Comprehensive Income

The following is a summary of the components of accumulated other comprehensive income:

	Foreign Currency Translation			Net Unrealized Gains (Losses) on Securities Available for Sale		
Years Ended December 31,	1996	1997	**1998**	1996	1997	**1998**
(Dollars in thousands)						
Beginning balance	$(1,240)	$ (3,183)	**$(12,458)**	$ 24,900	$14,064	**$19,886**
Change during the year	(1,943)	(9,275)	**2,807**	(10,836)	5,822	**9,223**
Ending balance	$(3,183)	$(12,458)	**$ (9,651)**	$ 14,064	$19,886	**$29,109**

	Minimum Pension Liability Adjustment			Accumulated Other Comprehensive Income (Loss)		
Years Ended December 31,	1996	1997	**1998**	1996	1997	**1998**
(Dollars in thousands)						
Beginning balance	$—	$—	**$ —**	$ 23,660	$10,881	**$ 7,428**
Change during the year	—	—	**(1,748)**	(12,779)	(3,453)	**10,282**
Ending balance	$—	$—	**$(1,748)**	$ 10,881	$ 7,428	**$17,710**

Notes to Consolidated Financial Statements

December 31, 1996, 1997, and 1998

Note 19.

Contingencies

The Company is subject to various pending and threatened legal actions that arise in the normal course of business. The Company maintains reserves for losses from legal actions that are both probable and estimable. In the opinion of management, the disposition of claims currently pending will not have a material adverse effect on the Company's financial position or results of operations.

Note 20.

Transactions With Affiliates

The Company had, and expects to have in the future, banking transactions and other transactions in the ordinary course of business with BTM and with its affiliates and associates. During 1996, 1997 and 1998, such transactions included, but were not limited to, origination, participation, servicing and remarketing of loans and leases, purchase and sale of acceptances, interest rate derivatives and foreign exchange transactions, funds transfers, custodianships, electronic data processing, investment advice and management, deposits and credit examination, and trust services. In the opinion of management, such transactions were made at prevailing rates, terms, and conditions and do not involve more than the normal risk of collectibility or present other unfavorable features. In addition, some compensation for services rendered to the Company is paid to the expatriate officers from BTM, and reimbursed by the Company to BTM under a services agreement.

Note 21.

Business Segments

The Company is organized based on the products and services that it offers and operates in five principal areas:

- The Community Banking Group provides loan products and deposit services primarily to consumers and small businesses.
- The Commercial Financial Services Group provides a wide variety of banking services, principally loans, to commercial customers.
- The International Banking Group provides trade-finance products to banks, and extends primarily short-term credit to corporations engaged in international business. The group's revenue predominately relates to foreign customers.
- The Trust and Private Financial Services Group principally provides fiduciary, private banking, investment and asset management services for individuals and institutions.
- The Global Markets Group manages the Company's securities portfolio, trading operations, wholesale funding needs, and interest rate and liquidity risk.

The information, set forth in the table on page 81, reflects the condensed income statements and a selected balance sheet item by business unit. The information presented does not necessarily represent the business units' financial condition and results of operations as if they were independent entities. Unlike financial accounting, there is no authoritative body of guidance for management accounting equivalent to generally accepted accounting principles. Consequently, reported results are not necessarily comparable with those presented by other companies.

The information in this table is derived from the internal management reporting system used by management to measure the performance of the segments and the Company overall. The management reporting system assigns balance sheet and income statement items to each segment based on internal management accounting policies. Net interest income is determined by the Company's internal funds transfer pricing system, which assigns a cost of funds or a credit for funds to assets or liabilities based on their type, maturity or repricing characteristics. Noninterest income and expense directly attributable to a segment are assigned to that business. Indirect costs, such as overhead, operations, and technology expense, are allocated to the segments based on studies of billable unit costs for product or data processing. The provision for credit losses is allocated based on the formula and specific reserves and the net chargeoffs for each respective segment. Equity is allocated based on a combination of regulatory requirements and management's assessment of economic risk factors, primarily credit, operating, foreign exchange, and interest rate risk. Depreciation and capital expenditures are not used by management when measuring the performance of the segments.

"Other" is comprised of goodwill, merger and integration expense, certain parent company non-bank subsidiaries, the elimination of the fully taxable-equivalent amounts, the unallocated allowance and related provision for credit losses, the net impact of transfer pricing, the earnings associated with the unallocated equity capital, and the residual costs of support groups. In addition, it includes two units, the Credit and Compliance Group, which manages nonperforming assets, and the Pacific Rim Group, which offers financial products to Asian-owned subsidiaries located in the U.S. On an individual basis, none of the items in "Other" are significant to our business.

Notes to Consolidated Financial Statements

December 31, 1996, 1997, and 1998

	Community Banking Group			Commercial Financial Services Group			International Banking Group			Trust and Private Financial Services Group		
Years Ended December 31,	1996	1997	**1998**	1996	1997	**1998**	1996	1997	**1998**	1996	1997	**1998**
Results of operations (dollars in thousands):												
Net interest income	$658,144	$682,782	**$673,463**	$401,912	$440,804	**$494,713**	$ 48,175	$ 49,405	**$ 55,741**	$ 11,539	$ 20,995	**$ 22,979**
Noninterest income	133,559	142,944	**178,208**	78,238	100,316	**109,520**	62,373	62,238	**65,834**	110,182	128,100	**145,593**
Total revenue	791,703	825,726	**851,671**	480,150	541,120	**604,233**	110,548	111,643	**121,575**	121,721	149,095	**168,572**
Noninterest expense	577,655	568,031	**596,714**	201,870	231,906	**257,124**	72,719	64,874	**66,967**	108,495	123,102	**134,977**
Credit expense (income)	35,644	57,870	**4,300**	14,362	18,872	**21,316**	(4,361)	234	**11,304**	927	155	**345**
Income (loss) before income tax expense (benefit) and performance center earnings (expense)[1]	178,404	199,825	**250,657**	263,918	290,342	**325,793**	42,190	46,535	**43,304**	12,299	25,838	**33,250**
Performance center earnings (expense)[1]	7,688	10,040	**7,769**	4,141	3,926	**2,270**	(6,917)	(3,759)	**(4,087)**	(674)	(1,472)	**122**
Income (loss) before income tax expense (benefit)	186,092	209,865	**258,426**	268,059	294,268	**328,063**	35,273	42,776	**39,217**	11,625	24,366	**33,372**
Income tax expense (benefit)	75,319	86,063	**102,138**	108,494	120,676	**127,854**	14,276	17,542	**14,773**	4,705	9,992	**13,133**
Net income (loss)	$110,773	$123,802	**$156,288**	$159,565	$173,592	**$200,209**	$ 20,997	$ 25,234	**$ 24,444**	$ 6,920	$ 14,374	**$ 20,239**
Total assets (dollars in millions)	$ 10,511	$ 10,783	**$ 10,230**	$ 9,940	$ 11,172	**$ 13,543**	$ 2,558	$ 2,657	**$ 1,717**	$ 241	$ 283	**$ 374**

	Global Markets Group			Other			UnionBanCal Corporation		
Years Ended December 31,	1996	1997	**1998**	1996	1997	**1998**	1996	1997	**1998**
Results of operations (dollars in thousands):									
Net interest income	$ 13,342	$ 25,348	**$ 35,472**	$ 35,466	$ 12,348	**$ 35,855**	$1,168,578	$1,231,682	**$1,318,223**
Noninterest income	22,101	21,189	**29,854**	12,223	8,214	**4,522**	418,676	463,001	**533,531**
Total revenue	35,443	46,537	**65,326**	47,689	20,562	**40,377**	1,587,254	1,694,683	**1,851,754**
Noninterest expense	20,535	22,574	**26,718**	153,630	34,178	**52,718**	1,134,904	1,044,665	**1,135,218**
Credit expense (income)	—	—	**—**	(6,572)	(77,131)	**7,735**	40,000	—	**45,000**
Income (loss) before income tax expense (benefit) and performance center earnings (expense)[1]	14,908	23,963	**38,608**	(99,369)	63,515	**(20,076)**	412,350	650,018	**671,536**
Performance center earnings (expense)[1]	(10,236)	(10,194)	**(9,231)**	5,998	1,459	**3,157**	—	—	**—**
Income (loss) before income tax expense (benefit)	4,672	13,769	**29,377**	(93,371)	64,974	**(16,919)**	412,350	650,018	**671,536**
Income tax expense (benefit)	1,891	5,647	**11,608**	(41,793)	(1,198)	**(64,431)**	162,892	238,722	**205,075**
Net income (loss)	$ 2,781	$ 8,122	**$ 17,769**	$(51,578)	$ 66,172	**$ 47,512**	$ 249,458	$ 411,296	**$ 466,461**
Total assets (dollars in millions)	$ 4,565	$ 3,961	**$ 4,479**	$ 1,419	$ 1,729	**$ 1,933**	$ 29,234	$ 30,585	**$ 32,276**

[1] Performance center earnings (expense) represent the allocation of net interest income, noninterest income and noninterest expense between the business segments for products and services originated in one segment but managed by another.

Notes to Consolidated Financial Statements

December 31, 1996, 1997, and 1998

Note 22.

Condensed UnionBanCal Corporation Unconsolidated Financial Statements

Condensed Balance Sheets

December 31,	1997	**1998**
(Dollars in thousands)		
Assets		
Cash and due from banks	$ 66,872	**$ 123,976**
Investment in and advances to subsidiaries	2,879,898	**3,264,207**
Other assets	7,971	**5,252**
Total assets	$2,954,741	**$3,393,435**
Liabilities and Shareholders' Equity		
Commercial paper	$ —	**$ 99,958**
Subordinated capital notes	250,000	**200,000**
Other liabilities	25,442	**35,233**
Total liabilities	275,442	**335,191**
Shareholders' equity	2,679,299	**3,058,244**
Total liabilities and shareholders' equity	$2,954,741	**$3,393,435**

Condensed Statements of Income

Years Ended December 31,	1996	1997	**1998**
(Dollars in thousands)			
Income:			
Dividends from bank subsidiary	$270,662	$ 85,660	**$ 98,159**
Dividends from nonbank subsidiaries	421	—	**23,000**
Interest income on advances to subsidiaries and deposits in bank	24,366	12,217	**11,744**
Other income	959	1,040	**404**
Total income	296,408	98,917	**133,307**
Expense:			
Interest expense	22,220	11,174	**15,573**
Other expense, net	1,072	1,583	**2,706**
Total expense	23,292	12,757	**18,279**
Income before income taxes and equity in undistributed net income of subsidiaries	273,116	86,160	**115,028**
Income tax expense (benefit)	889	204	**(2,346)**
Income before equity in undistributed net income of subsidiaries	272,227	85,956	**117,374**
Equity in undistributed net income (loss) of subsidiaries:			
Bank subsidiary[1]	(32,894)	314,739	**360,738**
Nonbank subsidiaries[2]	10,125	10,601	**(11,651)**
Net Income	$249,458	$411,296	**$466,461**

[1] In 1996, the amount represents dividends distributed by the Bank in excess of its 1996 net income.

[2] In 1998, the amount represents dividends distributed by nonbank subsidiaries in excess of their 1998 net income.

Notes to Consolidated Financial Statements

December 31, 1996, 1997, and 1998

Condensed Statements of Cash Flows

Years Ended December 31,	1996	1997	**1998**
(Dollars in thousands)			
Cash Flows from Operating Activities:			
Net income	$ 249,458	$ 411,296	**$ 466,461**
Adjustments to reconcile net income to net cash provided by operating activities:			
Equity in undistributed (earnings) losses of subsidiaries	22,769	(325,340)	**(349,087)**
Other, net	(3,772)	1,059	**(6,007)**
Net cash provided by operating activities	268,455	87,015	**111,367**
Cash Flows from Investing Activities:			
Advances to subsidiaries	(12,779)	(130,805)	**(34,747)**
Repayment of advances to subsidiaries	70,000	76,104	**18,088**
Sales and maturities of securities	322	—	**—**
Net cash provided (used) by investing activities	57,543	(54,701)	**(16,659)**
Cash Flows from Financing Activities:			
Net increase (decrease) in short-term borrowings	(632,296)	—	**99,958**
Proceeds from reduction of investment in subsidiary equity	3,966	—	**—**
Maturity and redemption of subordinated capital notes and long term debt	(70,000)	(50,000)	**(50,000)**
Proceeds from issuance of subordinated capital notes	—	200,000	**—**
Payments of cash dividends	(182,652)	(93,303)	**(98,160)**
Redemption of preferred stock	—	(135,000)	**—**
Other, net	17,813	9,119	**10,598**
Net cash used by financing activities	(863,169)	(69,184)	**(37,604)**
Net increase (decrease) in cash and due from banks	(537,171)	(36,870)	**57,104**
Cash and due from banks at beginning of year	640,913	103,742	**66,872**
Cash and due from banks at end of year	$ 103,742	$ 66,872	**$ 123,976**
Cash Paid (Received) During the Year for:			
Interest	$ 25,785	$ 9,814	**$ 16,056**
Income taxes	(198)	1,148	**(4,836)**
Supplemental Schedule of Noncash Investing and Financing Activities:			
Dividends declared but unpaid	$ 20,383	$ 24,528	**$ 33,300**

Notes to Consolidated Financial Statements

December 31, 1996, 1997, and 1998

Note 23.

Summary of Quarterly Financial Information (Unaudited)

Certain amounts in the following unaudited quarterly financial information have been reclassified to conform with current presentation. In the opinion of management, all adjustments necessary to fairly present the results of operations have been made.

1997 Quarters Ended	March 31	June 30	September 30	December 31
(Dollars in thousands, except per share data)				
Interest income	$485,031	$504,663	$520,237	$523,530
Interest expense	191,000	197,647	207,983	205,149
Net interest income	294,031	307,016	312,254	318,381
Provision for credit losses	—	—	—	—
Noninterest income	114,786	111,021	116,820	120,374
Noninterest expense	253,138	255,753	253,317	282,457
Income before income taxes	155,679	162,284	175,757	156,298
Income tax expense	63,177	65,739	45,953	63,853
Net income	$ 92,502	$ 96,545	$129,804	$ 92,445
Net income applicable to common stock	$ 89,676	$ 93,718	$127,857	$ 92,445
Net income per common share—basic	$ 0.51	$ 0.54	$ 0.73	$ 0.53
Net income per common share—diluted	$ 0.51	$ 0.54	$ 0.73	$ 0.53
Dividends per share[(1)]	$ 0.12	$ 0.12	$ 0.14	$ 0.14

1998 Quarters Ended	**March 31**	**June 30**	**September 30**	**December 31**
(Dollars in thousands, except per share data)				
Interest income	**$508,653**	**$511,996**	**$535,973**	**$528,557**
Interest expense	**191,203**	**186,440**	**199,340**	**189,973**
Net interest income	**317,450**	**325,556**	**336,633**	**338,584**
Provision for credit losses	**20,000**	**15,000**	**10,000**	**—**
Noninterest income	**128,030**	**147,994**	**123,925**	**133,582**
Noninterest expense	**268,475**	**277,325**	**290,378**	**299,040**
Income before income taxes	**157,005**	**181,225**	**160,180**	**173,126**
Income tax expense	**61,428**	**72,704**	**11,913**	**59,030**
Net income	**$ 95,577**	**$108,521**	**$148,267**	**$114,096**
Net income applicable to common stock	**$ 95,577**	**$108,521**	**$148,267**	**$114,096**
Net income per common share—basic	**$ 0.55**	**$ 0.62**	**$ 0.85**	**$ 0.65**
Net income per common share—diluted	**$ 0.54**	**$ 0.62**	**$ 0.84**	**$ 0.65**
Dividends per share[(1)]	**$ 0.14**	**$ 0.14**	**$ 0.14**	**$ 0.19**

(1) Dividends per share are based on the Company's common stock outstanding as of the declaration date.

Note 24.

Subsequent Event

On March 3, 1999, the Company completed a secondary offering of 28.75 million shares of its Common Stock owned by BTM. The Company received no proceeds from this transaction. Concurrent with the secondary offering, the Company repurchased 8.6 million shares of its outstanding Common Stock from BTM and 2.1 million shares owned by Meiji Life Insurance Company with $311 million of the net proceeds from the issuance of $350 million of 7⅜ percent capital securities that occurred on February 19, 1999. After the secondary offering and the repurchase, BTM owns 64 percent of the Company, or 105.6 million shares, compared with 82 percent prior to the transactions.

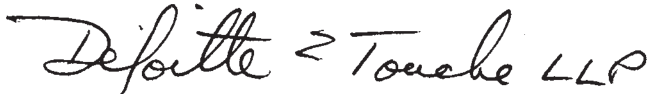
Independent Auditors' Report

To the Shareholders and Directors of UnionBanCal Corporation:

We have audited the accompanying consolidated balance sheets of UnionBanCal Corporation and subsidiaries (the "Company") as of December 31, 1997 and 1998, and the related consolidated statements of income, changes in shareholders' equity, and cash flows for each of the three years in the period ended December 31, 1998. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of UnionBanCal Corporation and subsidiaries as of December 31, 1997 and 1998, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 1998, in conformity with generally accepted accounting principles.



San Francisco, California
March 3, 1999

Deloitte & Touche

Boards of Directors and Executive Officers

As of January 1999

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Chairman of the Board

Takahiro Moriguchi (6, 7)
President and Chief Executive Officer

Yoshihiko Someya (5, 6, 7)
Deputy Chairman of the Board

Richard D. Farman (2, 3, 7)
Chairman and Chief Executive Officer
Sempra Energy

Stanley F. Farrar (2, 6)
Partner, Sullivan & Cromwell
Attorneys at Law

Herman E. Gallegos (4, 5)
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Jack L. Hancock (3, 5, 7)
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Judicial Arbitration &
Mediation Services, Inc.

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Senior advisor
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Chief Executive Officer
Headquarters for the Americas
The Bank of Tokyo-Mitsubishi, Ltd.

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California State University, Northridge

Kenji Yoshizawa*
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The Bank of Tokyo-Mitsubishi

Executive Management Committee

Takahiro Moriguchi
President and Chief Executive Officer

Yoshihiko Someya
Deputy Chairman of the Board,
Credit and Administration and
Trust and Private Financial Services

Richard C. Hartnack
Vice Chairman of the Board
Community Banking

Robert M. Walker
Vice Chairman of the Board
Commercial Financial Services

Peter R. Butcher
Executive Vice President
Chief Credit Officer

Katsuyoshi Hamahashi
Executive Vice President and Treasurer
Global Markets

David Matson
Executive Vice President
Chief Financial Officer

Magan C. Patel
Executive Vice President
International Banking

Charles L. Pedersen
Executive Vice President
Systems Technology and
Item Processing

Michael A.C. Spilsbury
Executive Vice President
Operations and Services

Ikuzo Sugiyama
Executive Vice President
Pacific Rim Corporate

Philip M. Wexler
Executive Vice President
Specialized Lending

* UnionBanCal Corporation Board Only

Summary of Principal Board Committee Responsibilities:

1. The Audit and Examining Committee oversees the company's financial reporting and control environment. It meets regularly with the company's general auditor and its independent auditors to review the scope and results of their work. The Committee reviews the company's quarterly and annual financial statements and regulatory disclosures with the officers in charge of the company's financial reporting, control and disclosure functions. The committee also makes an annual recommendation to the Board of Directors of the company's independent auditors. In addition, the committee reviews reports of examination conducted by bank and bank holding company regulatory agencies and follows up with appropriate management, so that recommendations and corrective actions are implemented.

2. The Credit Policy and Review Committee oversees the credit functions of the company, including the overall credit portfolio, composite credit policies, credit review and examination policies, and the methodology and adequacy of the allowance for credit losses. It also reviews a compliance program for credit functions and the establishment and delegation of credit authority. In addition, the committee reviews reports of examination conducted by bank and bank holding company regulatory agencies and follows up with appropriate management, so that recommendations and corrective actions may be implemented.

3. The Executive Compensation and Benefits Committee reviews and approves executive officer compensation criteria and levels and oversees the company's and the bank's employee benefit plans. The committee approves the compensation of the chief executive officer and other executive officers. In addition, it approves restricted stock awards and stock option grants under the company's Management Stock Plan.

4. The Public Policy Committee is responsible for identifying relevant political, social and environmental trends. The committee monitors the bank's programs that carry out the purposes of the Community Reinvestment Act, equal employment opportunity laws and other related federal, state and local programs.

5. The Trust Committee supervises the administration of the fiduciary powers of the holding company, the bank and their non-fiduciary investment management activities. The committee reviews reports of examination conducted by bank and bank holding company regulatory agencies, the company's general auditor and its independent auditors and follows up with appropriate management, so that recommendations and corrective actions may be implemented.

6. A new Finance and Capital Committee was created to oversee all aspects of the company's financial matters (except those that are the specific responsibility of the Audit & Examining Committee, Executive Compensation & Benefits Committee, or the Credit Policy and Review Committee) focusing on financial planning, financial performance compared to plan, financial processes, capital management, dividend and investment policies, management of net interest margin and other Asset and Liability management processes. The Committee also approves new issuances and redemptions, retirements or repurchases of common and preferred stock and debt.

7. The Nominating and Corporate Governance Committee is responsible for screening, interviewing and proposing qualified candidates to fill vacancies on the board of the company and the bank as they occur and recommending to the respective board the director nominees to be elected by shareholders at the annual meeting. In carrying out its responsibilities, the committee also considers candidates recommended by shareholders. The committee is also responsible for corporate governance matters.

Bank Directory

As of December 31, 1998

Head Office

350 California Street
San Francisco, CA
94104-1476
415 705 7000

Regional Headquarters

Los Angeles
San Diego*

Full-Service Community Branch Offices

California

Anaheim (2)
Anaheim Hills
Apple Valley
Artesia
Atascadero
Auburn
Bakersfield (3)
Barstow
Bellflower
Berkeley
Beverly Hills
Big Bear Lake
Bishop
Blythe
Borrego Springs
Brawley
Burbank
Burlingame
Calexico
Carlsbad (3)
Chino Hills
Chula Vista (4)
Citrus Heights
City of Industry
Clovis
Coalinga
Concord
Corona (2)
Coronado
Cypress
Dana Point
Danville
Davis
Del Mar
Delano
El Cajon (3)
El Centro
Encinitas (2)
Encino
Escondido
Fallbrook
Fountain Valley
Fremont
Fresno (10)
Fullerton (2)
Galt
Garden Grove
Gardena (2)
Hanford
Hawthorne
Hermosa Beach
Hesperia
Hollister
Huntington Beach (2)
Imperial Beach
Irvine (4)
Kentfield
La Habra
La Jolla (2)
La Mesa
Laguna Hills
Laguna Niguel (2)
Lakewood
Lemon Grove
Lemoore
Lodi
Lompoc
Long Beach (2)
Los Angeles (9)
Madera (2)
Mammoth Lakes
Manhattan Beach (2)
Manteca
Martinez
Menifee
Menlo Park
Merced
Mill Valley
Milpitas
Mission Viejo (2)
Modesto (2)
Montebello
Moreno Valley
National City
Newport Beach (4)
North Hollywood
Norwalk
Oakland
Oceanside (3)
Orange
Orange Cove
Palm Desert (2)
Palm Springs
Palo Alto (2)
Panorama City
Pasadena
Placerville
Porterville (2)
Poway
Rancho Bernardo
Rancho Cucamonga
Rancho Mirage
Rancho Santa Fe
Redding
Redondo Beach
Redwood City
Reedley
Ridgecrest
Riverside (4)
Rolling Hills Estates
Roseville
Sacramento (2)
Salinas
San Carlos
San Clemente (2)
San Diego (24)
San Francisco (4)
San Gabriel
San Jose (6)
San Juan Capistrano
San Leandro
San Luis Obispo
San Marcos
San Mateo
San Ramon
Santa Ana
Santa Maria
Santa Monica (2)
Santee
Selma
Solvang
Sonora
Spring Valley
Stockton (2)
Sunnyvale (2)
Tehachapi
Temecula
Torrance (2)
Tracy
Tulare
Turlock
Tustin (2)
Vallejo
Visalia (2)
Vista
Walnut Creek
Wasco
Westminster
Whittier
Woodland Hills
Yuba City
Yucca Valley

Oregon

Eugene
Portland*

Washington

Bellevue
Seattle*
Tacoma
Wenatchee

Limited Service California Branches

Bakersfield
Berkeley
Beverly Hills*
City of Commerce
City of Industry
Fresno (3)
Fullerton
Huntington Park
Indian Wells*
Irvine*
La Jolla
Los Angeles (2)
Lynwood
Monterey Park
Oakland (3)
Oxnard
Panorama City
Porterville
Portola Valley
Riverside
Sacramento
San Diego (5)
San Francisco* (6)
San Jose
Santa Ana
Torrance
Walnut Creek

Other Locations

New York
Texas

Overseas Offices

Brazil
Cayman Islands*
Guam (2)
Hong Kong
India
Indonesia
Japan
Korea
Malaysia
Philippines (2)
Saipan
Singapore
Taiwan (2)
Thailand

* Includes an office of The Private Bank

Shareholder Information

Common Stock

Stock Exchange Listing: Nasdaq: NNM/UNBC
Transfer Agent: Harris Trust Company of California
601 S. Figueroa Street, Suite 4900
Los Angeles, California 90017
(800) 554-3406

Capital Securities

Stock Exchange Listing: NYSE/UBT
Trustee & Transfer Agent: First National Bank of Chicago
One First National Plaza, Suite 0126
Chicago, Illinois 60670
(800) 346-5153

Dividend Reinvestment and Stock Purchase Plan

The UnionBanCal Corporation Dividend Reinvestment and Stock Purchase Plan provides holders of common stock a convenient method of investing cash dividends and cash payments to acquire shares of the company. A participant may reinvest cash dividends to purchase shares of common stock at 95 percent of the market price, and may also make optional cash payments of not less than $25 nor more than $3,000 per quarter to purchase common stock at the full market price. The company obtains shares required for reinvestment through open-market purchases or by the issuance of new shares from its authorized but unissued common stock. For more information, contact:

Harris Trust Company of California
601 S. Figueroa Street, Suite 4900
Los Angeles, California 90017
(800) 554-3406

Dividend Policy

The UnionBanCal Corporation Board of Directors considers dividends quarterly. The current annualized dividend rate is $0.76 per share.

This annual report of UnionBanCal Corporation is intended primarily to provide financial information and analysis to shareholders and investors while satisfying various regulatory requirements.

Additional information and financial data can be found in the corporation's annual report to the Securities and Exchange Commission (Form 10-K). The report for 1998 became available in March 1999. Supplemental financial information is published quarterly in the corporation's quarterly report (SEC Form 10-Q).

Also, financial information and a link to the company's disclosure documents filed with the Securities and Exchange Commission are available on the Investor Relations section of Union Bank of California's home page, at <http://www.uboc.com>.

Additional copies of the 1998 UnionBanCal Corporation annual report, the Form 10-K and Form 10-Q are available without charge and will be mailed upon request. Direct requests to:

John A. Rice, Jr., Vice President and Manager
Investor Relations Department
UnionBanCal Corporation
400 California Street — 13th Floor
San Francisco, California 94104
(415) 765-2969

UnionBanCal Corporation also files corporate disclosure documents with the Securities and Exchange Commission electronically, so interested parties may also acquire financial information about the company from the SEC home page at <http://www.sec.gov>.

Annual Meeting

The annual meeting of shareholders will be held in San Francisco in the Embassy Room of the Mandarin Oriental Hotel, 222 Sansome Street, on Wednesday, May 26, 1999, at 10:30 a.m.

This paper contains 10% post-consumer fiber.

UnionBanCal Corporation
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