

# Dear Shareholders,

1998 was a turbulent year in the world's financial markets, but Morgan Stanley Dean Witter performed exceptionally well. We were there for our clients, and our shareholders were rewarded with strong financial results:

- \* *Morgan Stanley Dean Witter earned a record \$3.3 billion in 1998, an increase of \$690 million, or 27 percent over 1997. Diluted earnings per share were \$5.33 — up 28 percent from \$4.16 in 1997.*
- \* *Return on equity was 24.5 percent, which compares favorably with our goal of an average of 18 percent to 20 percent over the course of the business cycle.*
- \* *In January 1999, our Board of Directors increased the quarterly cash dividend per common share by 20 percent to \$0.24.*

1998 was a year in which we set ourselves apart from our competitors. Many firms in our industry suffered large trading losses, announced layoffs and began to scale back on their global commitments. Our disciplined approach to trading and risk management kept us on an even keel; we continued to expand the number of financial advisors serving individual investors; and we achieved record results in our individual securities, individual asset management and credit services businesses. We *increased* our commitment to global markets with a 20 percent staff increase in Europe and 10 percent in Asia.

There are countless examples of how we have served our clients and customers during difficult times this past year. Perhaps the most dramatic example was our role as lead-manager in raising \$4.4 billion in the first step of DuPont's spin-off of Conoco, which was the largest U.S. initial public offering in history. The timing of the deal was particularly significant since it was launched in late September when market turmoil had virtually frozen the new issues business. We believe it is an example of our firm's leadership and our ability to execute superbly in even the most difficult market conditions.

A deal such as Conoco brings together the skills and talent of literally thousands of Morgan Stanley Dean Witter professionals. We believe our firm's combined origi-

# THE WISDOM OF OUR LONG-TERM STRATEGY IS INCREASINGLY APPARENT



**PHILIP J. PURCELL**  
Chairman & Chief Executive Officer

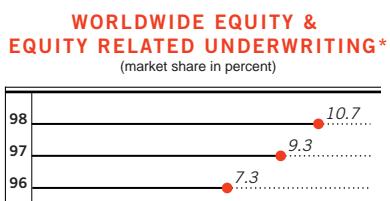
**JOHN J. MACK**  
President & Chief Operating Officer

nation and distribution strengths — forged in our merger two years ago — are particularly noteworthy. Conoco was not only the largest U.S. IPO in history, it also provided an extraordinary opportunity for individual investors. Through their Morgan Stanley Dean Witter financial advisors, our clients purchased an unprecedented 20 million shares, or \$460 million, in more than 40,000 client accounts.

In last year's Annual Report, we said we had put the merger behind us. That is true. But it also is true that the success of the merger continues to have enormous benefits, as evidenced by market share gains in our securities business. This past year, we solidified our leadership position in global equity underwriting — since the merger, our market share has increased from 7.3 percent to 10.7 percent. We were No.1 in IPOs for U.S. issuers in 1998. In underwriting asset-backed securities, our ranking has improved from No. 8 to No.1 since the merger. In our individual securities business, market share measured by both financial advisors and branch revenues has also increased. As a result of a 10 percent annual growth rate in financial advisors since the merger, we now rank as the second largest securities sales organization in the U.S.

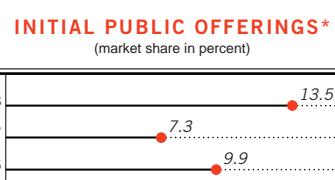
Our two other major businesses — asset management and credit services — also performed well. Despite the fear and uncertainty in many markets during much of the year, we had a net inflow of more than \$24 billion in investor funds in our individual and institutional asset management businesses. Two of our newest funds — Competitive Edge and Senior Income Trust — together attracted more than \$4 billion in 1998. Our credit services business had a record year as we refocused on our highly successful Discover® Card brand. By year-end, we had begun several new initiatives, including the launch of the new Discover Platinum Card, which we believe will be a major source of future growth. In addition, our international expansion plans now are well underway, and we plan to launch a card outside of North America in 1999.

figure 1



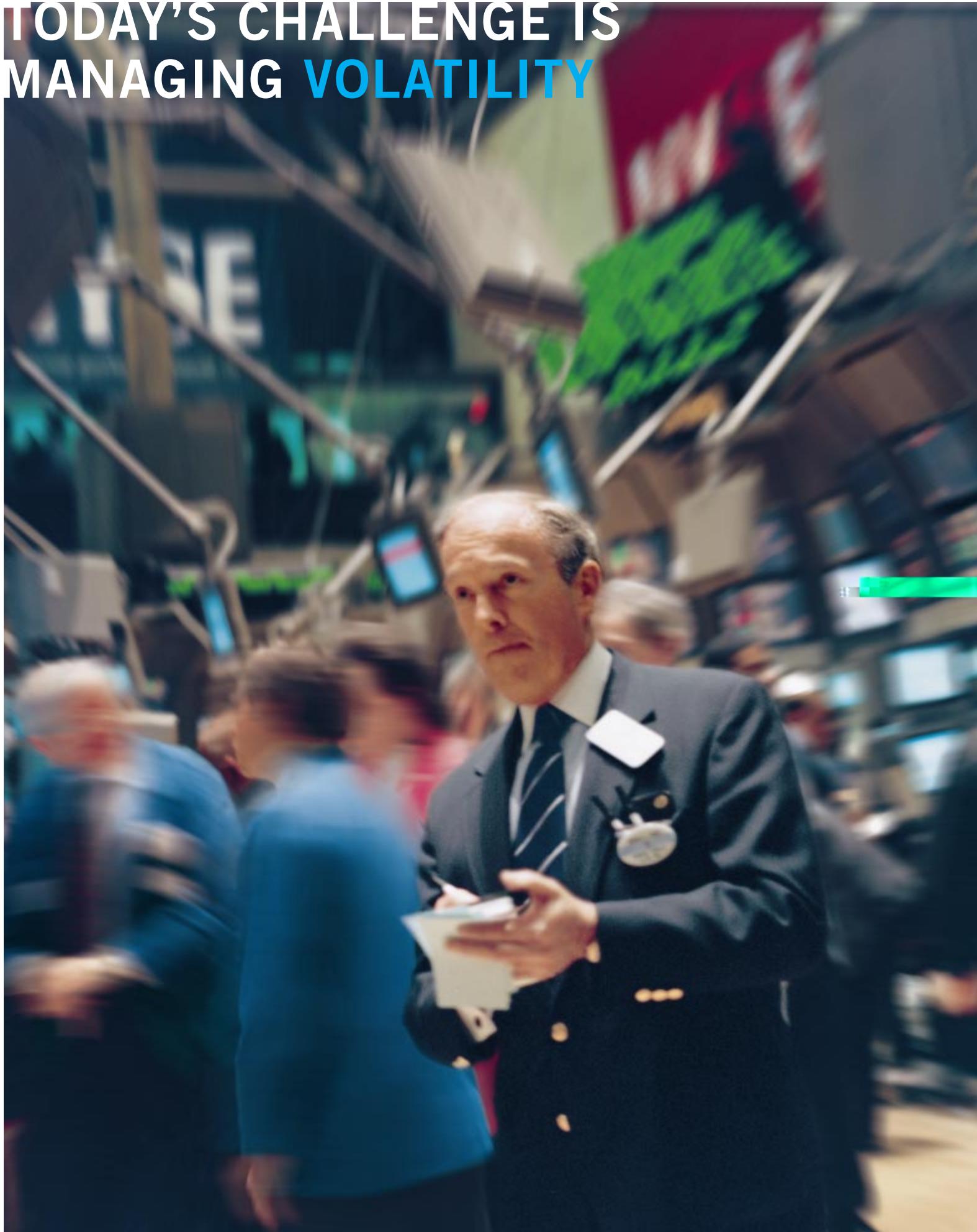
\*Securities Data Company

figure 2



\*Securities Data Company

TODAY'S CHALLENGE IS  
MANAGING VOLATILITY



We clearly had an excellent year in 1998, but we are not going to pretend that it was easy. Like many in our industry, our firm was severely tested, and we are proud to look back and say that we passed the test. But what of the future? It is clear that certain long-term trends in the financial services marketplace, very evident this past year, will continue to create challenges and opportunities. These trends are increasing volatility, globalization, complexity and consolidation. Our strategy has been built to take full advantage of these forces of change. And we believe our performance this past year demonstrates the success of our strategy.

#### **OUR DIVERSE REVENUE STREAMS AND EFFECTIVE RISK MANAGEMENT PROVIDE STABILITY**

If there is one word to characterize financial markets in 1998, it is volatility. The Dow swung from a high of 9,340 in July to 7,539 in August and back to a near record by year-end. The Russian bond default in August contributed to a flight to quality, unprecedented bond spreads and several weeks of paralysis in fixed income markets. Continuing instability in Asia caused capital flight and currency fluctuations that led to a virtual standstill in capital market activity.

Our own stock price was not immune from the wild swings in financial markets: \$96 $\frac{1}{2}$  in July, down to \$38 $\frac{1}{2}$  in October only to rebound by year-end. When you look at our steady revenue streams, it is difficult to understand this volatility. But it is symptomatic of the view that all financial services firms are equally impacted by volatile markets. The question is: How do you counter this perception? We believe there are two ways: diversity of revenues and effective risk management.

We have diversified revenue streams from three major businesses — securities, asset management and credit services. This diversity was important in the difficult third quarter when record earnings in credit services helped us to report stronger earnings than all of our major competitors. Asset management also tends to produce steady revenue streams. We offer a wide range of asset management products and

figure 3

#### **FINANCIAL ADVISORS**

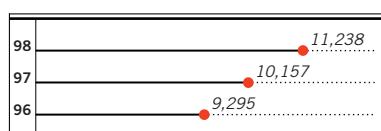


figure 4

#### **TOTAL ASSETS UNDER MANAGEMENT**

(in billions of U.S. dollars)



services, including 45 mutual funds ranked 4- or 5-Star by Morningstar. This past year, we brought our diverse asset management activities under a single organizational roof to create an even stronger presence in the marketplace.

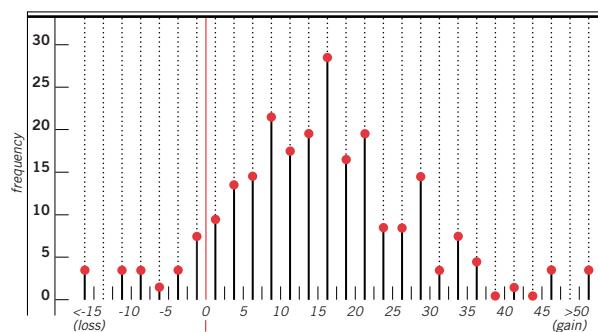
There also is great diversity in our securities business. In individual securities, we achieved stable growth in client assets despite volatile markets largely because our 11,238 financial advisors provided a steady influence and kept clients focused on long-term objectives. In institutional equities, foreign exchange and commodities, we had strong revenues in part because we do not take major proprietary market positions, but focus on assisting customers with a wide array of products, hedging solutions and transaction execution.

Our record earnings were a tribute to our strong culture of managing risk. Like most firms, we review market risk exposure in our institutional securities business using both quantitative and qualitative approaches. But we believe our success in managing risk comes down to the experience and discipline of our people.

**OUR COMMITMENT TO GLOBAL MARKETS IS UNDIMINISHED** The events of 1998 forced people to rethink the concept of globalization. The information technology that makes it possible for capital to flow freely and for investors to seek the best returns, regardless of national borders, also makes it possible for capital to exit a country just as readily. This is what happened in Asia, and, with the links between economies worldwide, it created uncertainty in other parts of the world. The operative word became “contagion,” and suddenly talk turned from the benefits of globalization to fears of worldwide recession.

figure 5

**HISTOGRAM OF DAILY INSTITUTIONAL TRADING REVENUE**  
(in millions of U.S. dollars)





**GLOBALIZATION CREATES  
OPPORTUNITIES AND RISKS**

# CLIENTS MUST DEAL WITH INCREASED COMPLEXITY



In the midst of these uncertainties, Morgan Stanley Dean Witter remained focused, and both our customers and shareholders have benefited. We were able to structure large financings for oil ventures in Mexico and Venezuela and an innovative high-yield financing for the Republic of Argentina during a period when the markets were not receptive to emerging market securities. We continued to expand our activities in Europe, providing financing for a high-growth telecommunications company in the Netherlands, entering and achieving substantial share in the Italian lira markets, and even leading the first asset-backed offering for a group of British pubs. Our company ranked No.1 in M&A in Europe for the fourth straight year, acting as advisor on groundbreaking mergers such as British Petroleum-Amoco and Deutsche Bank-Bankers Trust. At year-end, the influential European publication, *International Financing Review*, named us Bank of the Year, Bond House of the Year and Equity House of the Year. It was the first time ever that one firm has won these three top awards in a single year.

There is no better example of our global commitment than our 1998 performance in Asia. Despite the continuing turmoil, we expanded our presence in equity markets throughout the region, attaining market leadership on both the Tokyo and Hong Kong Stock Exchanges. We grew our equity business in Australia and Taiwan, provided advisory services in restructuring two national banks in Korea and coordinated the \$1.1 billion secondary offering of Bangkok Bank — the largest ever equity offering by a Thai company. Despite Japan's continuing economic troubles, we significantly expanded our investment banking and brokerage businesses as Japan embarks on a comprehensive reform of its financial markets.

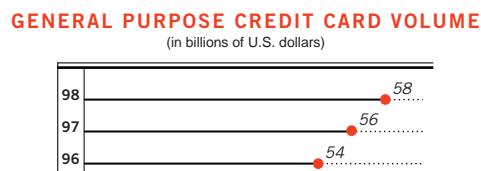
**WE SUPPORT OUR CLIENTS WITH INNOVATIVE SOLUTIONS** The increased complexity of today's financial marketplace reflects the forces of globalization, which have made the world a smaller place but also have created wider opportunities. Investors can

figure 6



\*Securities Data Company

figure 7



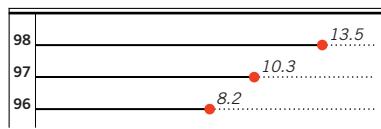
seek higher returns across national borders and diverse products, while issuers have a much greater variety of financing sources. The great proliferation of products and financial strategies has added a further layer of complexity. A third element of complexity in financial services is the challenge posed by technology, which has greatly accelerated the speed of transactions and created a much wider bandwidth in the flow of information.

Since the world is unlikely to become a simpler place in the foreseeable future, we believe the best response to ever-increasing complexity is continuous, relentless innovation. For our firm, innovation and the application of new technology to financial challenges have been hallmarks of our success. Whether in mergers and acquisitions, the use of derivatives to hedge risk, new high-yield or asset-backed securities, or making research and securities available to individual investors on the Internet, we will continue to use the flexibility and intellectual capital of our people to serve customers and create opportunities. Examples of continuing innovation this past year include our underwritings for Amazon.com in the first-ever high yield financing for an Internet retailer, the expansion of online services for our 2 million individual investor clients and the successful launch of Discover Card's high-speed transaction report system for its merchant network.

**PRODUCT RANGE AND SCOPE OF DISTRIBUTION ARE PRIZED ATTRIBUTES** Last year we noted that in bringing together Morgan Stanley and Dean Witter in mid-1997, we had anticipated a trend. Our merger was the first of the blockbuster combinations in financial services. The wave of consolidation has continued. In 1998, M&A activity in financial services reached \$700 billion compared with \$117 billion two years ago. We believe that consolidation in our industry will continue, driven by customer needs. Customers now want advice, products and liquidity across all geographic markets, and they are turning to the global firms that can meet their needs.

figure 8

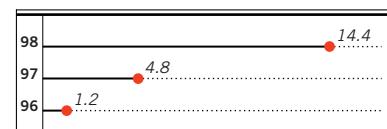
**U.S. HIGH-YIELD  
DEBT OFFERINGS\***  
(market share in percent)



\*Securities Data Company

figure 9

**U.S. PUBLIC RETAIL  
PREFERRED STOCK OFFERINGS\***  
(market share in percent)



\*Securities Data Company

MORGAN STANLEY  
DEAN WITTER  
INVESTMENT CENTER

MARKET FORCES ARE  
DRIVING CONSOLIDATION



**IN UNCERTAIN TIMES, CLIENTS LOOK  
FOR FINANCIAL STRENGTH**

Few firms can match Morgan Stanley Dean Witter in range of products and scale of distribution. In fact, this was the reason for our merger. By bringing top-ranked research and underwritten products to retail clients, we achieved significant gains in our individual client business. By the same token, investment banking has gained market share because of the distribution power of our 11,238 financial advisors.

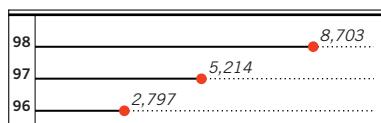
The newest and most rapidly growing distribution channel is the Internet. Our firm has positioned itself on the Internet through Discover Brokerage Direct, our online provider of financial services to individuals. In 1998, Discover Brokerage Direct expanded its product line to include proprietary equity research, 24-hour trading of U.S. government securities and a mutual funds marketplace. We also have introduced several Internet initiatives for Discover Card customers, including online payment capabilities and Discover ShopCenter,<sup>SM</sup> a new Internet shopping link. In 1999, we will focus on the growing number of consumers interested in using the Internet to purchase a variety of products and services.

The next frontier is the global distribution of securities and asset management products to individuals, particularly to capitalize on the huge pool of savings in Japan and the trend toward privatization of pension funds in Europe. There is no firm yet with a global retail capability, but we believe that firms that have the most extensive products and distribution today will have the advantage in developing such a capability tomorrow. In late 1998, we founded a new business unit to pursue global opportunities in retail securities and asset management, and we expect significant strides in 1999.

**FEW FIRMS CAN MATCH OUR STAYING POWER** We believe that Morgan Stanley Dean Witter clearly has demonstrated its ability to adapt, prosper and grow in a rapidly changing and often turbulent marketplace. We believe the diversity of our revenue

figure 10

**DISCOVER BROKERAGE DIRECT  
INTERNET TRADES PER DAY\***



\*Average for last month of fiscal year

figure 11

**NUMBER OF TOP-RATED  
ANALYSTS WORLDWIDE\***



\*Institutional Investor 1998 Ranked Analysts

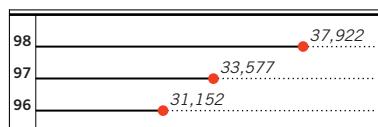
streams and our ability to manage risk make us less subject to market volatility. Our global commitment and expertise position us to take full advantage of the continuing trend of globalization. Our capacity for innovation enables us to serve our clients in an increasingly complex financial marketplace. And as the consolidation of the financial services industry continues, we believe we have the range of products and broad distribution channels that will enable us to continue to gain market share.

These capabilities and strategies are the source of considerable financial strength. Underlying them is a capital base that is one of the largest in our industry. At fiscal year-end, our shareholders' equity stood at \$14.1 billion, significantly higher than any of our U.S. securities industry competitors. Our total capital (including long-term debt) was \$38 billion. The diversity and growth potential of our revenue stream mean we should continue to generate substantial capital internally. This was particularly evident in 1998 as we were able to repurchase approximately \$3 billion of our stock. Because we have three profitable businesses (securities, asset management and credit services), a broad institutional and individual customer base, a global presence and a strong stream of continuing revenues, we believe our earnings will be less subject to volatility than many of our competitors.

In November, Moody's upgraded our credit rating to Aa3, which brought independent confirmation of our financial strength and the continued success of our strategy. We believe the timing of this affirmation was particularly significant. It came when many of our competitors had suffered setbacks in the difficult environment and had their ratings downgraded or placed on negative credit watch. In its analysis of our upgrade, Moody's echoed most of the same themes that we have emphasized in this letter: namely, that our performance, capabilities and strategy have set us apart from most of our competitors.

figure 12

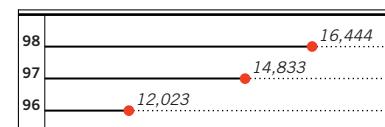
**TOTAL CAPITAL\***  
(in millions of U.S. dollars)



\*Excludes the current portion of long-term debt  
and includes Capital Units and Preferred Securities  
Issued by Subsidiaries.

figure 13

**NET REVENUES**  
(in millions of U.S. dollars)



1998 was a great year for Morgan Stanley Dean Witter. But it was by no means an easy year. So we would like to thank each of our 45,000 employees for their strong spirit and hard work, in often tough circumstances, on behalf of our clients, our shareholders and our firm. We are pleased that our employees own approximately 25 percent of the stock in our company, which helps ensure that their interests are closely aligned with our shareholders.

In April, Richard B. Fisher and Thomas C. Schneider, who played key roles in the merger and helped create our new company, will be leaving our Board of Directors. As Chairman of Morgan Stanley, Dick led the company's successful global expansion. Tom was Chief Financial Officer of Dean Witter Discover and had a central part in taking the company public in 1993. They have served our company exceptionally well and will continue to play active roles. We are pleased that Charles F. Knight, the Chairman and CEO of Emerson Electric Co., has joined our Board of Directors. The company will benefit from his counsel and experience.

At the time of the merger, we said our goal was to be the world's preeminent financial services company. Since then, we have had two straight years of record earnings and strong business growth in varying market conditions, and the goal we set for ourselves two years ago now is well within our reach. Some enormous opportunities, as well as challenges, lie just ahead. We also know there will be surprises. But we believe our firm is well-prepared for whatever lies in store and we are excited about the future. We want to thank our fellow shareholders for your support. We will continue to do everything we can to reward your commitment.



**PHILIP J. PURCELL**  
Chairman & Chief Executive Officer

**JOHN J. MACK**  
President & Chief Operating Officer

February 5, 1999