Letter to Shareholders
Half Year 2014 Results

LifeWatch®
Watching Life™

Dear shareholders of LifeWatch,

LifeWatch First Half Highlights

- **Volume growth of above 13% year-on-year**
- **Restructuring process on-going leading to improved second half figures**
- **Vital Signs Patch (VSP) on track for launch in 2015**

LifeWatch is pleased to report continued topline growth for the first half of 2014, with total revenues reaching USD 48.12 million, an increase of 10.2% over the first half of 2013. This increase was achieved in spite of an 8% price reduction imposed by Medicare for 2014, which would theoretically have led to a 2.9% decrease in revenues, based on the company's payor mix. In pure volume terms, the company therefore achieved growth of over 13%. Our U.S.-based subsidiary, LifeWatch Services Inc., contributed over 99% of total revenues. By working closely with hospital executives, physicians and clinical support staff, our well-trained sales force again successfully delivered significant and concrete results that align with our collective goals and objectives. The Medicare price decrease together with our restructuring measures (see below) however also had a negative effect on the gross margin which reduced to 52.1% from 59.3% in the first half of 2013. As reported at the Annual General Meeting in May this year, 2014 will be a year of transition and the restructuring measures implemented during the first half of 2014 have had a one-time impact on profitability (see below). However, the various streamlining activities initiated thus far are expected to bear fruit as of the second half of this year and beyond.

The new management team of LifeWatch presented an in-depth analysis and "Roadmap to Success" to the public in late May 2014 and to shareholders at the Annual General Meeting. The objectives being addressed include the broadening of the product and service offering, the expansion of the current technology globally, the assessment of developing a mHealth accessory device as well as the move towards becoming a fully-integrated biomedical informatics provider. To date, the Company has already implemented the following measures and strategies of the roadmap:

- Restructuring and redefinition of our Israeli R&D operation to better reflect and support future activities; this led to a reduction in staff numbers of 36% and will significantly reduce costs and improve efficiency going forward. Furthermore, a constant review of "make or buy" opportunities should allow a further streamlining of costs going forward.
- Realignment of our US sales territories and regions to improve the efficiency of the US sales force and refocusing the sales commission plan to more aggressively incentivize achievements above plan. This involved reducing our sales regions from 8 to 6 and the number of sales representatives by 20%. This measure is expected to bring sales and marketing costs as a percentage of sales back in line with previous years following a significant increase in the first half of 2014.
- Implementation of a global Governance, Risk and Compliance (GRC) program; the work in this area has already led to the resolution of several older legal cases and should lead to a reduction in such cases going forward.
- Updating and standardization of our financial and reporting systems to enable quicker and better analysis as well as improving efficiency; this process is on-going and will be completed during 2015.
- Several structural changes including realigning the business along global lines, appointing an executive management team to manage these global operations and focusing on retaining exceptional talent. Dr. Stephan Rietiker, hitherto Delegate of the Board of Directors, was appointed Chief Executive Officer (CEO) as of June 1, 2014.

Key Figures (Unaudited)

USD millions	Adjusted H1 2014	H1 2014	H1 2013
Revenues	48.12	48.12	43.68
Gross Profit	26.93	25.09	25.92
As % of revenues	*56.0%*	*52.1%*	*59.3%*
EBITDA (LBITDA)	1.45	(1.52)	*4.32*
As % of revenues	*3.0%*	*NA*	*9.9%*
EBIT (LBIT)	(1.16)	(4.13)	*2.71*
As % of revenues	*NA*	*NA*	*6.2%*
Net income (loss)	(1.75)	(4.72)	*8.88*
Earnings per share (basic)		(0.36)	*0.68*
Total fixed assets, net		13.02	*7.76*
Total Assets		68.54	*69.28*
Total equity		34.82	*44.12*
As % of assets		51%	*64%*
Net Cash Flow		(3.92)	*4.97*
Employees		561	*535*

Adjustments to H1 2014 figures	USD millions
LifeWatch V Healthphone inventory write-off	1.19
One-off costs for improved phone contract	0.40
Memory cards purchase	0.25
Adjustment to Gross Profit	**1.84**
Disputed billings	0.38
Israel restructuring	0.25
Legal reserve	0.50
Total adjustment *	**2.97**
* to EBITDA (LBITDA), EBIT (LBIT) and Net Income (Loss)	

Results Overview

Revenues continued to expand and reached USD 48.12 million in H1 2014 as compared to USD 43.68 million in H1 2013. This is a 10.2% increase versus H1 2013. Additionally Q2 2014 revenues grew by nearly 4% in comparison to Q1 2014.

The gross margin for the half-year decreased to 52.1% from 59.3% in H1 2013. The reduction in Medicare prices by 8%, implemented at the beginning of 2014, would however be expected to negatively impact the gross margin by around 1.2%, based on the company's payor mix. In this scenario, the gross margin would be expected to reduce to around 57.7% in 2014 from 58.9% during 2013, all things being equal. The drop in H1 gross margin is attributable in particular to one-off costs charged to cost of goods sold, such as an inventory write-off of USD 1.19 million for the LifeWatch V, a change of a contract for telephone lines of USD 0.4 million and the purchase of additional memory cards of USD 0.25 million. Adjusting for these one-off costs would result in a gross margin of 56.0%, which would be an improvement over Q1 2014 but still a little below 2013 after taking into account the Medicare price reduction. We however expect the gross margin to improve in the second half of the year and head back towards the 2013 level despite the Medicare price reductions.

Research and Development (R&D) expenses for the half-year were USD 3.28 million, or 6.8% of revenues, compared with USD 3.4 million, or 7.8% of revenues, in H1 2013. The reduction from 2013 to 2014 is the result of the capitalization of USD 0.56m of development costs for our VSP project. Without this capitalization R&D expenses would have been slightly higher as a percentage of revenues at 8.0%. The level of expenditure reduced to USD 1.41 million in Q2 compared to USD 1.87 million in Q1 2014 as a result of the restructuring measures undertaken.

Sales and Marketing (S&M) expenses for the half-year amounted to USD 12.50 million, or 25.9% of revenues, compared with USD 9.48 million or 21.7% in H1 2013. The significant increase in costs as a percentage of revenue versus 2013 was caused by the recruitment of several new sales representatives, who require time to become fully productive, and above plan commission payouts. As mentioned above, management has taken steps to address the increase in S&M expenses and expects the percentage of revenue ratio to return to the level of 2013 going forward.

General and Administration (G&A) expenses for the first half year stood at USD 12.69 million, or 26.4% of revenues, compared with USD 10.32 million, or 23.6% of revenues, during H1 2013. The significant increase in the revenue percentage was mainly a result of higher labor costs in the US, a higher bad debt provision and higher legal and advisor costs, some of which are non-recurring. As a result of our restructuring efforts as well as the non-recurring nature of some of the costs we expect G&A expenses as a percentage of revenue for the year as a whole to be significantly lower than in 2013.

Legal expenses and other relate to one-off expenses of USD 0.25 million for restructuring costs attributed to the LifeWatch V project as well as a provision of USD 0.50 million for legal reserves.

As a result of several one-off costs as well as higher expenses, the causes of which have subsequently been addressed, the Operating Loss (LBIT) for the first half-year of 2014 amounted to USD 4.13 million compared with an EBIT of USD 2.71 million in H1 2013.

The restructuring and streamlining measures mentioned above should lead to considerable cost savings going forward. Furthermore, a recently instigated "Operational Efficiency Program" should also help to reduce costs in the second half of the year. We therefore expect that the second half of 2014 will produce improved and positive results. For the year as a whole, we expect revenue to exceed USD 100 million with the second half showing a positive EBITDA, EBIT and Net Income. This should lead to positive EBITDA and EBIT numbers for the year as a whole, although Net Income is likely to remain negative. We also expect the operating cash flow to improve in the second half of the year leading to an increase in the cash position by year-end.

Monitoring Services Update

In H1 2014, as mentioned above, LifeWatch continued to realize growth in our core cardiac monitoring services business, including appreciable market share gains thanks to its strong franchise. The increased sales results support our 2014 strategic initiatives and focus across all markets served by LifeWatch. The Company signed 19 new or amended agreements for NiteWatch Home Sleep Test services and Ambulatory Cardiac Telemetry (ACT) services during the first half of 2014.

In May, LifeWatch exhibited at the Heart Rhythm Society annual meeting in San Francisco, where our messaging and product/service mix resonated well with physician attendees. With increasing awareness and prevalence globally around the impact of Atrial Fibrillation and Stroke, we introduced and expanded our monitoring service offerings to this ever-increasing market with largely unmet needs.

Interoperability of disparate systems and Electronic Medical Records ("EMR") integration continue to play an important role as physician practices and hospitals seek streamlined workflow to improve clinical management and patient outcomes. As previously outlined, we invested in resources, tools, and training to support a highly effective sales team, as well as our core messaging that outlines the inherent benefits of LifeWatch products and services to improve outcomes and diagnostic yield.

Research and Development Update

Vital Signs Patch (VSP) Technology: "Proof of Concept" studies, currently underway with leading healthcare institutions in the United States, are in progress and look promising. We expect to launch the VSP in H1 of 2015, following 510 (k) marketing clearance from the FDA. The adoption of the VSP can support hospitals and other healthcare providers in meeting the legislative mandates in the American Affordable Care Act associated with outcome measures of improving patient care at reduced costs.

The VSP is an easy to use sensor worn on a patient's upper chest. Once activated, the system provides automation and alerts of key vital signs via continuous wireless monitoring. The clinical data is interoperable with virtually any EMR system.

The VSP sensor measures the following vital signs:

- ECG, Heart Rate
- Body Surface Temperature
- Blood Oxygen Saturation
- Respiration Rate
- Body Position
- Blood pressure

Another product in development, as disclosed in May 2014, is a transmitting ECG Patch that was designed to address a subsection of our U.S. market. The Company is also reviewing the market needs for its mHealth initiatives and the competencies required in becoming a fully integrated Biomedical Informatics provider.

Outlook

As already mentioned above, LifeWatch expects to exceed its goal of USD 100 million in revenues, with an improvement in EBIT and EBITDA for the second half of 2014. We are confident of growing revenues by strengthening our market share in existing markets as well as globalizing our service offerings. With the various "Roadmap to Success" measures already initiated and the implementation thereof underway, LifeWatch is poised to improve its global positioning and return to profitable growth going forward.

Further investments are being made to both our existing product line and a broadening of product offerings that should increase market share in the reimbursed sector of our business. One of these investments, the Vital Signs Patch (VSP), is progressing well and according to plan and is due for market introduction in 2015. A pilot trial at Mount Sinai hospital is on-going where roughly half of the targeted number of patients have been enrolled so far. Two other pilot trials with different goals are also planned for 2014 with the first scheduled to begin at the Montefiore hospital in September. These trials are providing us with valuable patient and physician feedback, which will enable us to successfully launch this exciting new product in the first half of next year.

We would like to thank all our employees, patients, physicians and shareholders for their continued trust and support during this year of transition.

Sincerely,

Patrick Schildknecht, Chairman of the Board	Dr. Stephan Rietiker Chief Executive Officer

Information for shareholders, analysts and media

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LIFEWATCH AG

CONDENSED CONSOLIDATED FINANCIAL STATEMENTS FOR JUNE 30, 2014

UNAUDITED

CONTENTS

CONDENSED CONSOLIDATED BALANCE SHEET

USD thousands	June 30 2014	June 30 2013	December 31 2013
	Unaudited	Unaudited	Audited
Assets			
Cash and cash equivalents	6,220	10,824	10,136
Restricted bank deposit	815	800	812
Marketable securities and structures	-	43	-
Accounts receivable (trade & other), net	13,962	15,318	14,233
Deferred income taxes	9,438	6,582	9,426
Inventories	1,758	1,724	2,010
Total current assets	32,193	**35,291**	**36,617**
Marketable securities and structures	52	52	52
Deferred income taxes	6,807	10,448	6,826
Other investments and non-current receivables (trade and others)	903	718	912
Total non-current investments	7,762	**11,218**	**7,790**
Fixed assets, net	13,025	7,764	12,053
Goodwill, intangible and other assets, net	15,557	15,003	14,999
Total assets	68,537	**69,276**	**71,459**
Liabilities and stockholders' equity			
Current maturities of long-term loans and other liabilities	1,961	103	1,157
Accounts payable and accruals (trade and other)	18,735	12,805	18,520
Provision for settlement	2,565	2,524	2,545
Total current liabilities	23,261	**15,432**	**22,222**
Loans and other liabilities, net of current maturities	3,537	62	2,491
Liability for employee rights upon retirement, net	108	102	107
Provision for settlement	6,061	8,626	7,349
Accrued expenses	755	930	844
Total non-current liabilities	10,461	**9,720**	**10,791**
Total liabilities	33,722	**25,152**	**33,013**
Share capital, warrants, treasury shares, capital surplus and accumulated other comprehensive income (loss)	148,710	147,336	147,616
Accumulated deficit	(109,170)	(112,092)	(112,092)
Net (loss) income for the period	(4,725)	**8,880**	**2,922**
Total shareholders' equity	34,815	**44,124**	**38,446**
Total liabilities & shareholders' equity	68,537	**69,276**	**71,459**

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

	3 months ending June 30,		6 months ending June 30,	
USD thousands (except share and per share data)	2014 Unaudited	2013 Unaudited	2014 Unaudited	2013 Unaudited
Revenues	24,538	22,658	48,120	43,682
Cost of revenues	12,505	9,162	23,027	17,764
Gross profit	12,033	13,496	25,093	25,918
Research and development expenses	1,409	1,847	3,282	3,398
Selling and marketing expenses	6,110	5,042	12,501	9,485
General and administrative expenses	6,938	5,063	12,690	10,323
Legal expenses and other	751	-	751	-
Total operating expenses	15,208	11,952	29,224	23,206
(Loss) Income from operation	(3,175)	1,544	(4,131)	2,712
Financial and other expenses, net	124	78	204	128
(Loss) Income before taxes	(3,299)	1,466	(4,335)	2,584
Tax (expense) income	(97)	7,278	(390)	6,296
(Loss) Income for the period	(3,396)	8,744	(4,725)	8,880

WEIGHTED AVERAGE NUMBER OF SHARES IN THOUSANDS USED IN COMPUTATION OF (LOSS) EARNINGS PER SHARE				
Basic	13,194	13,116	13,255	13,101
Diluted	13,234	13,237	13,289	13,225
(LOSS) EARNINGS PER SHARE (USD)				
Basic	(0.26)	0.67	(0.36)	0.68
Diluted	(0.26)	0.66	(0.36)	0.67

Condensed Consolidated Statements of Comprehensive (Loss) Income

Net (Loss) income	(3,396)	8,744	(4,725)	8,880
Other comprehensive loss:				
Foreign currency translation adjustment	(1)	(1)	(2)	-
Total other comprehensive loss	(1)	(1)	(2)	-
Comprehensive (loss) income	(3,397)	8,743	(4,727)	8,880

CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY

USD thousands	Paid in share capital including premium	Warrants	Accumulated deficit	Capital reserve	Treasury Shares	Accumulated other comprehensive loss	Total
BALANCE AT JANUARY 1, 2014 (AUDITED)	147,024	1,063	(109,170)	70	(370)	(171)	38,446
Changes During The Six Months Ended June 30, 2014 (Unaudited):							
Net loss for the period	-	-	(4,725)	-	-	-	(4,725)
Other comprehensive loss	-	-	-	-	-	(2)	(2)
Issuance of shares in respect of exercise of options granted to employees and service provision	1,067	-	-	-	-	-	1,067
Stock-based compensation expense	17	12	-	-	-	-	29
BALANCE AT JUNE 30, 2014 (UNAUDITED)	148,108	1,075	(113,895)	70	(370)	(173)	34,815

USD thousands	Paid in share capital including premium	Warrants	Accumulated deficit	Capital reserve	Treasury Shares	Accumulated other comprehensive loss	Total
BALANCE AT JANUARY 1, 2013 (AUDITED)	146,559	1,006	(112,092)	-	(370)	(168)	34,935
Changes During The Six Months Ended June 30, 2013 (Unaudited):							
Net Income for the period	-	-	8,880	-	-	-	8,880
Issuance of shares in respect of exercise of options granted to employees	257	-	-	-	-	-	257
Stock-based compensation expense	24	28	-	-	-	-	52
BALANCE AT JUNE 30, 2013 (UNAUDITED)	146,840	1,034	(103,212)	-	(370)	(168)	44,124

CONDENSED CONSOLIDATED STATEMENT OF CASH FLOW

	3 months ending June 30,		6 months ending June 30,	
USD thousands	2014 Unaudited	2013 Unaudited	2014 Unaudited	2013 Unaudited
CASH FLOWS FROM OPERATING ACTIVITIES:				
Net (loss) income for the period	(3,396)	8,744	(4,725)	8,880
Adjustments required to reconcile (loss) income for the period to net cash (used in) provided by operating activities:				
Income and expenses not involving cash flows:				
Depreciation and amortization	1,357	831	2,611	1,613
Compensation expenses charged in respect of options and warrants granted to employees and service providers	8	21	29	52
Change in deferred income tax, net	47	(7,312)	7	(6,525)
Changes in operating assets and liabilities:				
Decrease in accounts receivable, including non-current portion	2,395	24	280	2,533
Decrease (increase) in inventories	706	(267)	252	(699)
(Decrease) Increase in accounts payable and accruals:				
Provision for settlement	(635)	(750)	(1,267)	(750)
Trade and others	(1,029)	140	34	1,367
Net cash (used in) provided by operating activities	(547)	1,431	(2,779)	6,471
CASH FLOWS FROM INVESTING ACTIVITIES:				
Purchase of fixed assets	(949)	(698)	(2,339)	(1,535)
Purchase of other assets	(281)	-	(561)	-
Restricted bank deposit	(4)	(15)	(3)	(21)
Net cash used in investing activities	(1,234)	(713)	(2,903)	(1,556)
CASH FLOWS FROM FINANCING ACTIVITIES:				
Issuance of shares in respect of exercise of employee stock options	671	175	1,067	257
Obligation under capital lease undertaken, net	911	(13)	624	(25)
Discharge of long term loan – received from a bank and others	(8)	(7)	(16)	(14)
Net cash provided by financing activities	1,574	155	1,675	218
Translation differences on cash balances of subsidiaries	75	(23)	91	(168)
(Decrease) increase in cash and cash equivalents	(132)	850	(3,916)	4,965
Balance of cash and cash equivalents at beginning of period	6,352	9,974	10,136	5,859
Balance of cash and cash equivalents at end of period	6,220	10,824	6,220	10,824

SUPPLEMENTARY DISCLOSURE OF NON-CASH ACTIVITIES				
Capital leases of fixed assets	146	-	1,242	-

NOTE 1

Basis of presentation

The unaudited condensed consolidated interim financial statements for LifeWatch AG and its subsidiaries (the "Company") have been prepared on the basis of accounting principles generally accepted in the Unites States of America ("US GAAP") for interim financial information. Accordingly, such financial statements do not include all the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. These interim financial statements should be read in conjunction with the audited consolidated financial statements of the Company for the year ended December 31, 2013.

NOTE 2

Fixed Assets

a. Composition of assets, grouped by major classifications, is as follows:

USD thousands	June 30, 2014	June 30, 2013	December 31, 2013
	Unaudited	Unaudited	Audited
Cost			
Manufacturing and peripheral equipment	11,670	10,679	11,352
Office furniture and equipment	2,737	2,772	2,781
Monitoring units	20,167	13,989	17,891
Motor vehicles	161	186	161
Leasehold improvements	1,521	1,480	1,517
Total costs	**36,256**	**29,106**	**33,702**
Less – accumulated depreciation and amortization	**23,231**	**21,342**	**21,649**
Total	**13,025**	**7,764**	**12,053**

b. Depreciation expenses in respect of fixed assets totaled USD 2,608 thousand, USD 1,610 thousand and USD 3,642 thousand for the six months ended June 30, 2014, June 30, 2013, and for the twelve months ended December 31, 2013, respectively.

NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS

NOTE 3

Segment and geographic information

The Company operates in four reportable operating segments:

- Sales of Systems - Development, manufacture and marketing of trans-telephonic and wireless diagnostic equipment for the medical industry.
- Mobile Health - Mobile medical device platform designed for self-testing of vital signs for the consumer market.
- Services - Cardiac event monitoring, ambulatory heart monitoring and sleep disorder services.
- Other - Company activities and expenses that are not assigned directly to either of the above segments.

The table below presents information about reported segments:

USD thousands	Sales of Systems	Mobile Health	Services	Other	Reconciling items	Consolidated total
For the 6 months ended June 30, 2014 (Unaudited):						
Revenues from external customers	1,400	20	46,700	-	-	48,120
Inter-segments revenues	5,951	2	-	-	(5,953)	-
Total	7,351	22	46,700	-	(5,953)	48,120
Operating income (loss)	2,755	(4,576)	926	(3,295)	59	(4,131)
Depreciation and amortization	176	-	7,957	-	(5,522)	2,611
Goodwill	-	-	14,976	-	-	14,976
Capital investments	385	-	8,381	16	(5,202)	3,580
Total assets	102,072	-	84,884	2,717	(121,136)	68,537
For the 6 months ended June 30, 2013 (Unaudited):						
Revenues from external customers	935	-	42,747	-	-	43,682
Inter-segments revenues	3,793	-	-	-	(3,793)	-
Total	4,728	-	42,747	-	(3,793)	43,682
Operating income (loss)	522	(3,156)	5,520	(2,344)	2,170	2,712
Depreciation and amortization	98	-	7,302	-	(5,787)	1,613
Goodwill	-	-	14,976	-	-	14,976
Capital investments	110	-	4,740	-	(3,315)	1,535
Total assets	100,607	789	87,476	1,620	(121,216)	69,276

NOTE 3

Segment and geographic information (*continued)*

Following are data regarding revenues and long-lived assets classified by geographical location of the customers:

USD thousands	USA and Canada	Europe	Asia	Other	Total
For the 6 months ended June 30, 2014 (Unaudited)					
Revenues	46,700	31	1,107	282	48,120
Long-lived assets	11,923	118	-	984	13,025
For the 6 months ended June 30, 2013 (Unaudited)					
Revenues	42,752	68	862	-	43,682
Long-lived assets	7,154	90	-	520	7,764