

We're delivering on our promises.



William C. Foote
Chairman, CEO and President

The power of our strategies – and our brand – is producing record results. In 1999, we sold record quantities of most of our major products. Our net sales climbed 15 percent over 1998, to \$3.6 billion. Operating profit increased 25 percent, net earnings rose 27 percent and diluted earnings per share were \$8.39 compared with \$6.61 in 1998. We received higher ratings on our debt from both Moody's (B_{aa2})

and Standard and Poor's (BBB+). We increased our quarterly dividend to \$.15 per share and made great progress on our five million-share repurchase plan, with purchases totaling almost 1.7 million so far.

Our success in 1999 extends a remarkable six-year performance. Since completing our restructuring in 1993, we have repaid nearly \$1 billion in debt while investing close to \$1.3 billion in our business. We have increased sales by 88 percent and more than quadrupled our net earnings. And while we think that it should be higher, by the end of 1999 the value of our stock had increased from less than \$10 to nearly \$50 per share, substantially more than the increases in either the S&P Midcap or the Russell Midcap Value indices during the same period. Our share price has moderated since the end of 1999, providing us with an even greater opportunity to repurchase our stock.



Our experience has taught us that the only way to keep moving ahead is to do even more – and to do it “the better way.”

We have kept our promises by holding to our mission. We are committed to providing the better way. Our goal is to deliver the solutions that our customers need and want. Our success is based on strong relationships that we build through integrity, dependability and innovation.

We demonstrated our mission all across our organization during 1999. Our new Home Center Service Organization strengthens our ties to leading retailers and has already helped them increase same store sales. We formed our Architectural Sales Team, uniting the strengths of our gypsum and ceilings businesses to provide integrated design solutions and help streamline project management. Our new USG Drywall Suspension System for ceilings offers architects and designers new creative

“We’re the number one wallboard manufacturer, and our new plants and manufacturing lines will extend our lead. From the ground up, they’re designed for safety, and they house the world’s fastest wallboard machines. A special team of our best manufacturing experts, drawn from our operations across the country, is getting them up and running

freedom, while our new RADAR ceiling panels, which can be installed in any direction, are built for speed. When used with DONN DX Suspension Systems, USG offers the fastest-to-install ceiling system in the industry. Throughout USG’s product lines, we are introducing new products designed to deliver contractors improved quality in less time.

Our ability to go above and beyond—to provide the better way—rests upon five central strategies. Because they are critical to our success, I’d like to examine them in more detail.



and helping train employees. Every start-up we complete will help make the next one go even faster and more smoothly.”

Pedro Menendez

Plant Manager, Aliquippa, Pennsylvania

Build for Profitable Growth

The demand for wallboard has grown at an average rate of more than five percent a year during the past five years, and we expect it to

keep growing. During 1999, we ran our wallboard lines 24 hours a day, 7 days a week and shipped record amounts of SHEETROCK Brand Gypsum Panels. Yet we, along with others in the industry, had to allocate shipments of our products. We recognize that allocation caused difficulties for our customers, and we worked hard to alleviate their concerns.

To meet growing demand, we are investing in state-of-the-art manufacturing facilities. In May 1999, the first of our new wallboard lines, in Bridgeport, Alabama, went into operation—at full design speed—ahead of schedule. We were equally successful in starting up our new line in East Chicago, Indiana, in November. A third line will start in a few months in Aliquippa, Pennsylvania. We also broke ground on two facilities to serve the West Coast market.

New production capacity will help us meet the increasing demands of all of our valued customers — independent specialty dealers, retailers and our own L&W Supply. New capacity also will improve our profitability. We are the leading, low-cost producer throughout North America and we intend to do even better. When all five of the new wallboard manufacturing lines come on stream by early 2001, they will replace older, high-cost operations. For example, once our new Bridgeport plant was opened, we moved forward with plans to close our Plasterco, Virginia plant. We also have closed our old line at East Chicago.

“\$500 million of cash earnings in 1999 on \$2.3 billion of market capitalization—when it comes to generating cash, we’re a powerhouse. What’s more, we’re using it to create more value. Our return on capital employed was an outstanding 21 percent. And while we are building our long-term value, we haven’t overlooked investors. In 1999, we allocated 19 percent of



our cash earnings—\$94 million in all—to repurchasing our stock and paying dividends. And, in November, we increased the dividend by 50 percent and doubled the rate of stock repurchase activity.”

Rick Fleming

Executive Vice President and Chief Financial Officer

In total, we'll replace more than one billion square feet of old capacity while adding more than two billion square feet of net new capacity with operating costs roughly one-half of our older facilities.

But we aren't just expanding our wallboard business. Sales of our joint compounds, DUROCK Brand Cement Board and HYDROCAL industrial gypsum products now exceed \$500 million and are showing strong growth. We're adding to

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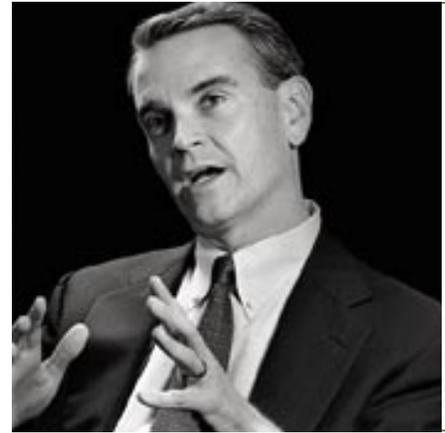
our capacity in these and other businesses. New joint compound lines were added in Bridgeport, Alabama and Torrance, California. A new line at our Gypsum, Ohio plant began making FIBEROCK Brand Panels. We purchased Beadex Manufacturing, Inc. and the Synkoloid Company of Canada, leading producers of interior finishing products that complement our existing line of contractor-preferred gypsum products.

Lead in Innovation Our new production facilities will be devoted to making products that will extend our competitive lead. In January 2000, we reinvented our largest product line with the launch of the “Next Generation” of SHEETROCK Brand Gypsum Panels. Our gypsum plants are now using a revolutionary, patent-pending technology to manufacture our flagship SHEETROCK Brand Gypsum Panels. These panels feature three high-performance benefits – cleaner scoring and snapping, durability and flatness. Independent field studies show that “Next Generation” board

reduces installation time, a tremendous benefit for contractors and builders, especially at a time of labor shortages.

We're making some equally large advances in offering other high-performance building panel solutions. In 1999, we introduced FIBEROCK Brand AQUA-TOUGH Sheathing. Our new sheathing products provide strength, durability and most importantly, comprehensive water resistance that is much better than any existing gypsum or wood-based exterior sheathing. We'll introduce more FIBEROCK Brand products in 2000. In an industry where innovation traditionally has come gradually, we're changing the game.

Expand Distribution We're applying the same creativity in bringing our products to market. Expanding our distribution business, our third strategic initiative, is an important factor in our growth. L&W Supply Corporation, our specialty building materials distribution business, now represents approximately one-third of our sales. The business has grown by acquiring leading specialty distributors, opening new locations and increasing sales of such products as acoustical ceilings, drywall metal, insulation and roofing. L&W Supply is not the company store, but a leading building products distributor with 193 locations in 37 states and sales of more than \$1.3 billion.



"Today, we're the largest wallboard distributor in the U.S. and much more. Ceilings, drywall metal, insulation, roofing, tools and other products now account for about half our sales. We can answer more of our customers' needs, offer them more integrated solutions and serve them across the country. High-value support services like assisting contractors calculate the amount of materials needed to complete a job, delivering products in the building of the job site and assistance in handling credit create long-term relationships with contractors. We want to be their first—and only—stop on the way to the job site."

Jim Metcalf

President and CEO, L&W Supply Corporation

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but a leading building products distributor
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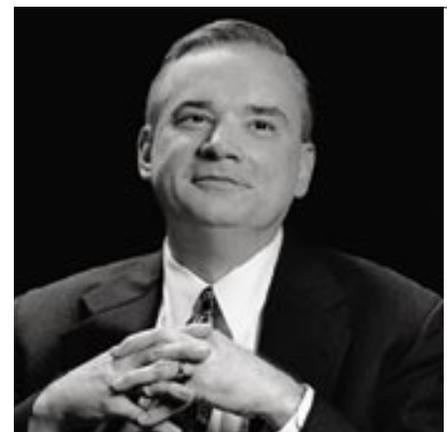
Serve the Best We are delivering more value to our customers. No other wallboard manufacturer can match our ability to serve customers, including specialty dealers, co-ops and the “big box” retailers that are growing about twice as fast as our industry as a whole. In 1999, we reorganized our gypsum sales operation to make our relationships with our customers even stronger. Backed by a \$10 million customer information system, everyone from our sales representatives to senior management is spending more time with customers. From helping retailers and specialty dealers train their sales people to helping contractors stay on top of new trends, we’re doing more for our customers than ever before.

Build Our Brands Our dealers are committed to providing contractors the top brands. Our SHEETROCK and DUROCK brands rank number one in our industry in both brand recognition and brand preference and we are working harder to extend our lead. In 1999, we became an official marketing partner of the NASCAR Truck Series. It’s been a great association for us, because research indicates that many drywall installers and construction workers attend NASCAR races or watch them on TV. In 2000, we have increased our exposure even more by becoming the Official Building Products Supplier of NASCAR.

“You can summarize our value proposition in one word: flow. For our large customers, flow means faster delivery, responsive information and consistently high-quality products that generate sales. For contractors, flow means improved, faster installation, fewer callbacks and the materials and services that are needed to keep crews flowing smoothly from one job to the next. For USG, flow means creating and delivering tangible value, exactly when and where our customers want it. That’s what drives customer satisfaction and strengthens our high-value relationships with all of our customers.”

Ed Bosowski

President and CEO, U.S. Gypsum



“We’re using technology to meet our customers’ demands and improve our efficiency. Our Customer Service Center handles over 700,000 orders a year, and is growing as we continue to realize increases in our demand and capacity. New training and quality monitoring



programs help us provide ‘one and done’ service — answering more questions and completing more transactions with a single customer contact. This enables us to be more responsive to our customers, reduce costs and handle our business growth efficiently.”

Jean Holley

Vice President and Chief
Information Officer

To be the company we want to be, we can’t take anything — or anyone — for granted. We want to do what’s best for our employees and neighbors as well as for our customers, suppliers and shareholders. That’s why working safely is the only way we do business. I am pleased to report that 25 plants have exceeded one million safe hours and 39 plants have exceeded one thousand safe days without a lost workday due to injury. Our overall safety rating is nine times better than the average for all U.S. durable goods manufacturers. At L&W Supply, 173 of our 193 specialty dealer centers did not have a lost workday. An outstanding example is L&W’s San Diego, California Heartland Building Materials, which has gone more than 10,000 days without a lost workday.

Our SHEETROCK and DUROCK brands rank number one in our industry in both recognition and brand preference, and we are working hard to extend our lead.

“In wallboard manufacturing, like real estate, the three most important words are ‘location, location, location.’ Our new facilities are located near growing customers across the U.S.



Accessible rail and water links will enable us to speed deliveries while we lower our manufacturing and shipping costs. We have the opportunity to turn our supply chain into a competitive advantage and forge stronger links with customers. Our combination of low-cost manufacturing and efficient distribution is hard to beat.”

Jack O'Bryan

Vice Chairman

pace through 2000 and beyond. The repair and remodel market is growing at double-digit rates due to the record number of existing home sales in 1999, since many buyers remodel their homes within two years of purchase. Repair and remodel sales should also continue to grow as major home improvement retailers continue to add locations. Longer term, the United States has a growing number of aging buildings that will need to be rehabbed or modernized. Half of the country's 120 million homes were built before 1970, and three-quarters of its office space was constructed before 1980.

We also work to be a good neighbor. When an explosion rocked the town of Bridgeport, Alabama in January 1999, our plant employees, construction crews and equipment assisted in the clean-up effort. Last spring and summer we donated truckloads of products to help towns in Oklahoma and Iowa rebuild after they were struck by tornadoes.

The Year Ahead 1998 and 1999 were record years, and we are aiming for another record year in 2000. We will continue to execute our strategy through profitable growth and driving costs down.

We expect to enjoy favorable conditions for growth. Americans are likely to continue to build and renovate homes, offices, schools and hospitals at a healthy

Business Overview

	Gypsum	Distribution	Ceilings
Businesses	United States Gypsum Company CGC Inc. Yeso Panamericano S.A. de C.V.	L&W Supply Corporation	USG Interiors, Inc. USG International CGC Inc.
Products and Services	Manufactures and markets gypsum wallboard, joint treatments and textures, cement board, gypsum fiber panels, plaster, water-managed exterior systems, shaft wall systems and industrial gypsum products	Specializes in delivering construction materials to job sites	Manufactures and markets acoustical ceiling tile, ceiling suspension grid, specialty ceilings, relocatable wall systems and other building products for U.S. and international markets
Best-Known Brand Names	SHEETROCK gypsum panels, SHEETROCK joint compound, DUROCK cement board, FIBEROCK gypsum fiber panels, HYDROCAL gypsum cement, IMPERIAL and DIAMOND building plasters		AURATONE and ACOUSTONE ceiling tile; DONN DX, FINELINE and CENTRICITEE ceiling grid; COMPASSO suspension trim; CURVATURA 3-D ceiling system; ULTRAWALL relocatable wall systems
Leadership Position	World's largest producer of gypsum wallboard, ready-mixed joint compounds, fiberglass-reinforced cement board	United States' largest specialty distributor of gypsum wallboard	World's largest producer of ceiling suspension grid; world's second-largest producer of ceiling tile
Geographical Areas Served	United States, Canada, Mexico	United States	More than 125 countries in all parts of the world: North, Central and South America, the Caribbean, Europe, the Middle East, Asia, the Pacific Rim, Africa
Customers	<p>purchasers: specialty drywall centers, distributors, hardware cooperatives, buying groups, home centers, mass merchandisers</p> <p>influencers: architects, specifiers, building owners</p> <p>end users: contractors, builders, do-it-yourselfers</p>	<p>purchasers and end users: contractors, builders</p>	<p>purchasers: specialty acoustical centers, distributors, hardware cooperatives, home centers, contractors</p> <p>influencers: architects, specifiers, interior designers, building owners, tenants, facility managers</p> <p>end users: contractors, builders, do-it-yourselfers</p>

Our new products, enhanced service, expanded distribution, new low-cost capacity and increasingly powerful brands will create even greater value.

“Our new Architectural Sales Team gives us one-on-one relationships with the firms responsible for half of



all of the projects built in the United States. And we are giving them better materials to work with. The standard, pre-engineered components in our drywall suspension system allow architects to shape curved and arcing drywall ceilings. Now we are developing additional specialty products as well as products for applications in specific market segments, such as transportation and health care. We’re challenging our partners to ‘Imagine the Upside’ in 2000 because when we execute properly, there’s no ceiling to our performance.”

John Meister

President and CEO, USG Interiors

We are also optimistic about the new residential construction market. Housing starts and new home sales are expected to moderate from 1999’s frenetic pace but remain at healthy levels. The less interest-rate sensitive, higher-end segments with larger homes, higher ceilings and more amenities remain strong. And, both our gypsum and ceilings businesses will benefit from the new commercial construction that usually follows new residential construction, as stores, schools and hospitals are built to serve new and growing communities.

These healthy construction markets should absorb the new wallboard capacity that USG plans to add during 2000. This new domestic capacity will supplant the high-cost imported board that was arriving from as far away as Europe and the Far East. Another large producer has announced that, like USG, it will also remove older, high-cost capacity from the market.

We are looking at every aspect of our cost structure in order to continue to grow profitably. New process technologies, best practice productivity programs and improved logistics will produce millions of dollars in savings and help keep us ahead of our competitors. For example, we’ve reduced our wallboard weights to record lows, while exceeding the most stringent quality standards. To reduce waste paper costs, we’re installing new systems at our paper mills which allow us to use

lesser-quality waste paper while still producing a superior final product. And, a logistics project begun in 1999 will take more than \$10 million a year out of shipping costs.

Through these programs and a variety of other efforts throughout USG, we expect to widen our cost advantage. Low costs enable us to manage our future risks and enable us to compete effectively in a free supply environment.

In closing, on behalf of the management and employees, I would like to express our gratitude to our shareholders, customers and suppliers for their tremendous support of USG. And, as a fellow shareholder, I want to thank our employees for their record-producing accomplishments and continuing dedication to the better way. Looking to the future, we are confident our new products, enhanced service, expanded distribution, new low-cost capacity and increasingly powerful brands will create even greater value. We'll continue to go above and beyond. That is where we want to be.

A handwritten signature in black ink, appearing to read "William C. Foote". The signature is written in a cursive style with a large, stylized "F" at the end.

William C. Foote

Chairman, CEO and President

February 11, 2000