Aareal Bank Group is a leading provider of smart financing, software products and digital solutions for the property sector and related industries. It is active in more than 20 countries across three continents – in Europe, North America and Asia/Pacific.

Group Management Report

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Fundamental Information about the Group

Business model

Aareal Bank AG, headquartered in Wiesbaden, Germany, is the parent company of the Group. Its shares are admitted to trading on the regulated market (geregelter Markt) of the Frankfurt Stock Exchange, and are included in the mid-cap MDAX® index.

Aareal Bank Group's strategic business segments comprise commercial property finance as well as services, software products and digital solutions for the property sector and related industries.

Structured Property Financing

In the Structured Property Financing segment, Aareal Bank facilitates property investments for its domestic and international clients, and is active in this respect in Europe, North America and the Asia/Pacific region. It stands out here especially for the direct and long-standing relationships it has established with its clients. Aareal Bank finances commercial property investments, especially for office buildings, hotels, retail, logistics and residential properties, with a focus on existing buildings. Its particular strength lies in its success in combining local market expertise and sector-specific know-how. This allows Aareal Bank to offer tailor-made financing concepts that meet the special requirements of its national and international clients. In particular, the Bank excels with its structuring expertise, as well as in portfolio and cross-border financings.

Aareal Bank manages its sales activities in the individual regions worldwide via a network of sales centres (hubs). In addition to the locally-based experts, the distribution centres for sector specialists covering hotels, retail and logistics properties, as well as those catering to the specific needs of investment fund clients, are located in Wiesbaden.

There are two regional hubs in Europe: one hub combines sales activities for the euro zone, with a focus on the Benelux countries, France, Germany, Italy and Spain. An additional hub focuses on sales activities outside the euro zone, with a focus on Central and Eastern Europe, Northern Europe, and the UK. As before, the hubs have a network – comprising branches in London, Paris, Rome, Stockholm and Warsaw – at their disposal. Furthermore, the Dublin branch holds securities. The branch office in Brussels was closed at the end of 2018. Representative offices are located in Istanbul, Madrid, and Moscow.

Aareal Bank Group's activities on the North American market are carried out through the subsidiary Aareal Capital Corporation, operating from New York City. The Singapore subsidiary Aareal Bank Asia Limited conducts the sales activities in the Asia / Pacific region.

Funding

Aareal Bank has a broad and solid refinancing base. It has established itself as an active issuer of Pfandbriefe, which account for a major share of its long-term funding. The AAA rating of the Pfandbriefe additionally confirms the quality of the cover assets pool. To cater to a broad investor base, Aareal Bank covers a wide range of other refinancing tools, including promissory notes and debt securities. Depending on market conditions, the Bank places large-sized public issues or private placements. In the Consulting / Services segment the Bank also generates deposits from the housing industry, which represent a strategically important additional source of funding. Furthermore, it has recourse to institutional money market investor deposits. The success of our capital and money market activities, and the business with housing industry clients, are the results of a combination of a sustainable business model with a sound understanding of the capital markets, and the quality of the cover assets pool.

Consulting / Services

In the Consulting / Services segment, Aareal Bank Group offers its clients from the property sector and related industries – such as the energy sector – a combination of specialised banking services, software products and digital solutions. With its subsidiary Aareon, Aareal Bank can boast the leading international consultancy and IT systems house for the property sector in Europe.

Aareon Group offers its customers consulting, software and services to optimise IT-supported business processes in the digital age. With its Enterprise Resource Planning (ERP) systems distributed from 37 locations in Austria, Finland, France, Germany, the Netherlands, Norway, Sweden and the UK, Aareon generates stable, long-term business volume. In addition, Aareon develops a portfolio of digital solutions with its international research and development teams and in cooperation with PropTech enterprises, offering these solutions internationally. "Aareon Smart World", the digital ecosystem, connects these solutions, networking property companies with customers, staff and business partners, as well as connecting technical devices in apartments and buildings. Aareon Group benefits from a transfer of cross-border know-how, leveraging the respective country-specific focal areas of digitalisation to expand its range of products and services. Aareon offers software solutions both in Germany and abroad that may be used in various types of operating environments: in-house services, hosting and Software as a Service (SaaS) from the exclusive Aareon Cloud.

In its Housing Industry division, Aareal Bank offers its customers process optimisation, electronic banking and asset management and markets its BK 01 software which is the leading procedure in the German housing property industry for the automated settlement of mass payments. The procedure is integrated in licensed bookkeeping systems. Therefore, customers in Germany may process their payment transactions and account management from the administration software employed. In addition to the German property industry, the German energy sector forms a second major client group of the Bank's Housing Industry division for the services mentioned above. This enables the offer of further products, facilitating the cross-sector cooperation of client groups and realising synergies via end-to-end digital processes. In conjunction with payment transactions processed via Aareal Bank's systems, deposits are generated that contribute significantly to Aareal Bank Group's refinancing base.

Within the Consulting/Services segment, Aareon AG and the Bank's Housing Industry division work closely together. A large number of clients in the Bank's Housing Industry division are also clients of Aareon.

Management system

Aareal Bank Group is managed using key financial performance indicators, taking the Group's risk-bearing capacity into account. Management takes place primarily at Group level, and is additionally differentiated by business segment. Group management is based on medium-term Group planning, prepared annually, which is geared towards the Group's long-term business strategy. An extensive (management) reporting system regularly provides the information required for management and monitoring purposes.

The indicators set out below are key financial performance indicators for Aareal Bank Group; they are used for the purposes of managing the business and the Group's profitability.

- **Group/consolidated:**
  - » Net interest income (in accordance with IFRSs)
  - » Loss allowance (in accordance with IFRSs)
  - » Net commission income (in accordance with IFRSs)
  - » Administrative expenses (in accordance with IFRSs)
  - » Operating profit (in accordance with IFRSs)
  - » Return on equity (RoE; before taxes)[1)]
  - » Earnings per ordinary share (EpS)[2)]
  - » Common Equity Tier I ratio (CET I ratio) – Basel IV (estimate) –
  - » Liquidity Coverage Ratio (LCR)

- **Structured Property Financing segment**
  - » New business
  - » Credit portfolio of Aareal Bank Group

- **Consulting/Services segment**
  - » Aareon's contribution to consolidated operating profit (in accordance with IFRSs)

The Group's existing risk management system is used to manage and monitor the various risk exposures of Aareal Bank Group entities, in a centralised manner. All management-relevant information is systematically collected and analysed, to develop suitable strategies for risk management and monitoring. We also employ forecasting models for balance sheet structure, liquidity and portfolio development for strategic business and revenue planning.

In addition to business-related management tools, we also use various other instruments to optimise our organisation and workflows. These include comprehensive cost management, centralised management of project activities and Human Resources controlling, for example.

Structured Property Financing also deploys supplementary management tools and indicators. For example, we manage our new business in this segment using lending policies which are specific to the relevant property type and country, and which are monitored within the scope of the lending process.

The property financing portfolio is actively managed throughout Aareal Bank Group, with the aim of optimising its risk diversification and profitability. To develop risk- and return-oriented strategies for our portfolio, we evaluate market and business data, using this as a basis to simulate potential lending strategies, and to identify a target portfolio, which is part of Group planning. This helps us to identify – and to respond to – market changes at an early stage. Active portfolio management makes it possible for us to optimally allocate equity to the most attractive products and regions from

[1)] $$\text{RoE before taxes} = \frac{\text{Operating profit ./. consolidated net income attributable to non-controlling interests ./. AT1 coupon}}{\text{Average equity (IFRS) excluding non-controlling interests, other reserves, AT1 bond, and dividends}}$$

[2)] $$\text{Earnings per share} = \frac{\text{Operating profit ./. income taxes ./. consolidated net income attributable to non-controlling interests ./. AT1 coupon (net)}}{\text{Number of ordinary shares}}$$

[3)] New business = newly-originated loans plus renewals a risk/return perspective, within the scope of our strategy. By taking into consideration maximum allocations to individual countries, products and property types in the portfolio, we ensure a high level of diversification and avoid risk concentrations.

In the Consulting/Services segment, management of the Group entities allocated to the segment is oriented on specific indicators, depending on each entity's business focus – primarily Aareon's contribution to consolidated operating profit. We also use specific performance indicators that are typical for consulting and services in the IT business, the focus of this segment. These include indicators relating to regular client satisfaction surveys, as well as capacity utilisation indicators in the consultancy business. The volume of deposits is a key indicator for the Bank's Housing Industry division.

Report on the Economic Position

Macro-economic environment

In the financial year 2018 the environment was defined by geopolitical uncertainties. Besides the protectionist measures taken in the US, economic imbalances in some emerging markets fuelled uncertainty. The economy remained intact and economic expansion was robust, albeit at a slightly less dynamic pace than the year before. The economic cycle is likely to have peaked overall.

Economy

While economic growth in the euro zone was robust in 2018, it was significantly lower than the year before. This was largely attributable to a fall in external demand and to one-off effects in the respective countries. Spain and the Netherlands recorded the strongest growth within the euro zone, while growth in Germany, France and Italy was markedly below the average. New emissions tests in Germany led to a marked slump in car sales, while growth in France was lower as a result of industrial action. Italy fell into a technical recession in the second half-year as growth eased due to weaker domestic demand in response to political uncertainties.

Economic growth in other countries within the European Union (EU) was higher than in the euro zone. As was the case in the previous year, growth in Poland and Sweden was considerably stronger than in the euro zone.

Growth in the UK on the other hand was weaker, although the economy proved more robust than originally assumed. In addition, considerable uncertainty was created by the exit agreement that was negotiated with the EU towards the end of the year and then rejected by a large majority in the UK Parliament on 15 January 2019. This took enterprises planning certainty.

Solid fundamental data and fiscal stimulus led to strong growth in the US in the year under review while the budget deficit rose significantly. Higher import duties imposed on important trading partners, counter-reactions by the countries in question, and the unilateral termination of international projects heightened political uncertainty and the risk of an open trade war. Growth in Canada was markedly lower year-on-year, on account of less pronounced investment and lower oil production.

Economic growth in Australia was significantly stronger year-on-year. The Chinese economy lost momentum during the course of the year, with slightly weaker exports and the negative effects of high levels of private debt cited as some of the reasons for this. China responded to the import tariffs imposed by the US by also levying import taxes on a raft of US products.

Global labour markets benefited from the fundamentally good economy and the sustained economic cycle. In the euro zone, unemployment rates continued to fall slightly during the year under review, whilst they remained stable, at a low level, in the UK and the US.

Annual rate of change in real gross domestic product

%	2018[1]	2017[2]
Europe		
Euro zone	1.8	2.5
Austria	2.6	2.7
Belgium	1.4	1.7
Finland	2.4	2.8
France	1.5	2.3
Germany	1.4	2.5
Italy	0.9	1.6
Luxembourg	3.0	1.5
Netherlands	2.6	3.0
Spain	2.5	3.0
Other European countries		
Denmark	1.1	2.3
Poland	5.3	4.9
Russia	1.6	1.5
Sweden	2.3	2.4
Switzerland	2.6	1.6
Turkey	2.9	7.4
United Kingdom	1.4	1.8
North America		
Canada	2.1	3.0
USA	2.9	2.2
Asia/Pacific		
Australia	3.0	2.4
China	6.6	6.8
Japan	0.8	1.9

[1] Preliminary figures [2] Adjusted to final results

Financial and capital markets, monetary policy and inflation

The year 2018 on the financial markets was defined by slightly higher volatility compared with the previous year, triggered by geopolitical events and changes in monetary policy. This resulted in negative effects for some emerging markets in particular. Particular noteworthy in this context was the political situation in Italy, which drove up Italian government bond yields. The fear of a trade war and political turmoil surrounding Brexit also weighed on the markets.

The ECB set the course in the first half of 2018 for a turnaround in its monetary policy. In June, it announced that the net asset purchase programme would finish at the end of 2018. This was confirmed again in December. Monthly purchase volumes of € 30 billion were reduced to € 15 billion in the fourth quarter. No additional assets have been purchased since January 2019 – with only maturing securities being reinvested. Furthermore, the ECB plans to keep key interest rates low through summer 2019. The Bank of England raised the base rate in August by 25 basis points to its present level of 0.75 %. The US Federal Reserve (Fed) increased its Fed Funds corridor four times during the year, by 25 basis points each time – most recently in December, to 2.25 %-2.50 %. The Bank of Canada raised its base rate during the year in three stages, to reach 1.75%. Sweden's Riksbank lifted its main interest rate from -0.50 % to -0.25 % in December.

The US dollar appreciated significantly against the euro, following an initial marked depreciation. The pound sterling on the other hand remained virtually constant vis-a-vis the euro, before losing slightly in value towards the end of the year, due to the political uncertainty surrounding the Brexit agreement. The Canadian dollar weakened considerably against the euro in the first half of the year but managed to appreciate again slightly in the second half, before losing significant ground again at the end of the year. The Swedish krona weakened slightly against the euro over the course of the year.

Short-term interest rates[3] exhibited significant differences between different currencies throughout the year under review, not least due to differences in monetary policy. They increased considerably during the year in pound sterling, the Canadian dollar and the US dollar. They were constant initially in Swedish krona before rising slightly at year-end

[3] Calculated on the basis of 3-month Euribor or the corresponding LIBOR or other comparable rates for other currencies

in the wake of the key interest rate hike. On the other hand, they remained relatively constant at a negative level in the euro zone.

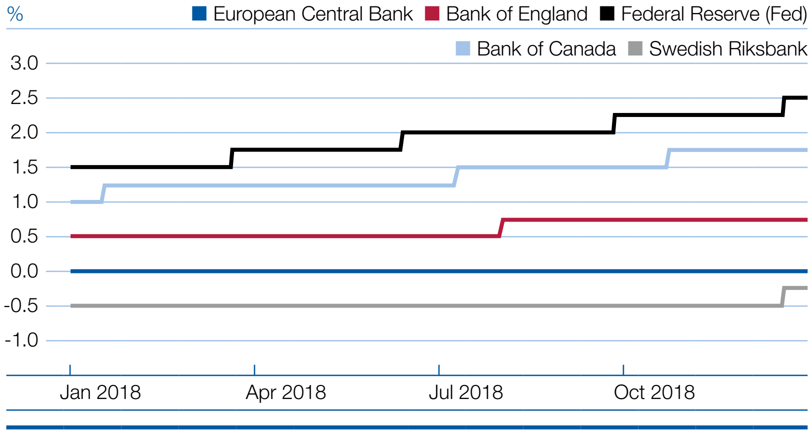
Long-term interest rates[2] in the currency areas that are relevant to Aareal Bank initially rose consistently compared with the end of the previous year, whereas US dollar, Canadian dollar and pound sterling rates were markedly higher at the end of the year, compared to the 2017 year-end. Towards the year-end, euro zone and Swedish krona rates fell back again to (or slightly below) the levels seen at the end of 2017.

The performance of ten-year government bond yields diverged during the year, owing to geopolitical uncertainty and adjustments in monetary policy. They fell in Germany, particularly at the end of the year, to a lower level than at year-end 2017, owing to safe-haven demand. On the other hand, yields in Italy increased strongly. In the first half-year, the Italian government announced a far-reaching, expansive fiscal policy to replace the reform policy of the previous years – which meanwhile triggered a budget debate with the Euro Group. Although yields fell again slightly at the end of the year, they remained high by European standards. The continuous – albeit moderate – upward trend continued in the US, with ten-year government bond yields climbing above the 3.0 % threshold in some instances.

Euro zone inflation rose by just under 2.0 % compared with the previous year. Inflation in the US also rose during the year to average 2.5 %. In the UK, it fell again slightly from the highs of the previous year and remained at 2.5 % for 2018 on average. The driver here was higher energy prices.

Also in 2018 the Pfandbrief market continued to be significantly influenced by the ECB's asset purchase programme. However, the impact declined due to the programme's termination at the year-end and the reduction in purchasing volumes, from an initial level of 50 % of new issues to merely 10 % in October 2018. Credit spreads of new issues increased, especially during the fourth quarter. The volume of private placements continued to

Key rate developments in 2018 [1]



[1] The upper level of the corridor for the Fed Funds is shown in the chart.

decline, whereas the volume of benchmark issues increased.

Regulatory environment

The environment in which banks are operating continues to be defined by highly dynamic regulatory requirements, as well as by changes in banking supervision. This includes, in particular, the implementation of the final draft of the Basel III framework into EU law (known as "Basel IV"), which was endorsed by the Basel Committee's Group of Governors and Heads of Supervision (GHOS). Furthermore, the EU Commission's proposals to revise supervisory regimes (CRR, CRD IV, BRRD and SRMR) as well as the EBA documents (Guidelines on PD and LGD estimation, treatment of defaulted exposures, and determination of downturn LGD), will all bring about further regulatory changes. In addition, the amendments proposed by the ECB, EBA and the EU Commission on the treatment of non-performing loans must also be taken into account. New requirements related to resolution, such as BaFin's "MaBail" (Minimum Requirements for the Implementation of a Bail-in), which is currently being consulted on, present new challenges. Moreover, both national and inter-

[2] Based on the 10-year swap rate

national regulators are imposing various new requirements – including in connection with IT/information security risks, or regarding the prevention of money laundering, tax evasion, and terrorist financing.

The ECB's Supervisory Review and Evaluation Process (SREP) ensures a common approach on the supervisory review of banks, within the framework of Pillar 2. The SREP is built around a business model analysis, an assessment of governance, as well as of the capital and liquidity risks. The results of the individual areas are aggregated in a score value, from which the ECB derives supervisory measures on holding additional capital and/or additional liquidity buffers.

Sector-specific and business developments

Structured Property Financing segment

Unlike previous years, no uniform trend in traded volumes of commercial property could be observed in the course of the year. Whilst volumes in North America rose considerably, they fell sharply in Europe compared with the previous year, remaining stable in the Asia/Pacific region. However, traded volumes remained high overall.

The commercial property markets have been subject to significant changes for quite some time. As a market participant itself, Aareal Bank continuously analyses the environment so that trends can be identified early on. The development in retail trade must be emphasised here initially. Digitalisation has led to a marked change in consumers' buyer and leisure behaviour. Likewise, the demands of a retail property – and of retail traders – have changed. At the same time, we find ourselves in a phase in the economic cycle, in which investor and financing circumstances are changing, the effects of which stand out most in the retail sector. Accordingly, new concepts are being established that support and define the change. Retail property will have a future as new concepts also need to have a physical presence, as is becoming increasingly apparent.

New office property concepts are also being established, such as co-working or the serviced office, where the general trends of the sharing economy and pay-per-use are being applied. One provider offers fully-equipped office space, which users can rent on a variable basis. This will make office rental more flexible, as users are not tied to specific premises and some providers worldwide offer modern office space that can also be used for short periods of time only, if required. These providers already represent the largest tenant group in terms of floor space at some locations.

Very low prime yields were observed on numerous commercial property markets around the world. This compares with the increases seen in secondary market yields on many markets. Rents for prime properties partly were in different phases of their business cycles. In the US, average rental growth in the office market flattened out. In Europe, on the other hand, average rental growth in the office market continued to rise slightly, supported in particular by the high rental volume. In contrast, rental growth for European retail property stagnated, but was still slightly positive in the US.

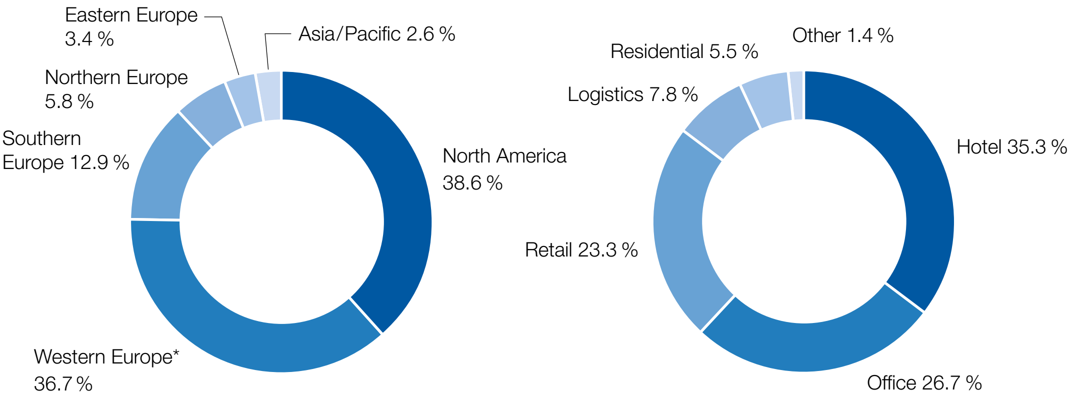
Fierce competition for the financing of commercial properties persisted in many markets. Margins in the European and US markets were under pressure during the year, although they remained considerably higher in the US than in Europe.

In a highly competitive business environment that is defined by a wealth of uncertainty factors, Aareal Bank succeeded in generating new business of € 9.5 billion in 2018, which exceeded the previous year's figure of € 8.8 billion. The target that was originally announced – and then raised in the third quarter – was clearly exceeded due to the high volume of early renewals and larger portfolio financings. Newly-originated loans amounted to € 7.2 billion (2017: € 6.5 billion).

At 58.8 % (2017: 64.4 %), the highest share of our new business was originated in Europe, followed by North America with 38.6 % (2017: 34.8 %). 2.6 % of new business was originated in the Asia/Pacific region (2017: 0.8 %). The increase in the

New business[1] 2018

by region | by type of property



[1] New business, excluding former WestImmo's private client business and local authority lending business
* Including Germany

North American share is in line with the targets of our "Aareal 2020" programme for the future.

Europe

Commercial property transaction volumes generated in Europe were noticeably lower, compared with the previous year, yet remained at very high levels for the fourth year in a row. Growth shifted towards smaller markets. Whilst France, Germany, the Netherlands, Spain and the UK saw noticeable declines, slightly higher volumes were observed in Poland. Cross-border and institutional investors were on the buy side for the most part, whereas private investors tended to be sellers. REIT structures had balanced positions.

Rents for prime commercial properties in the European economic centres showed a largely stable to slightly rising trend in 2018 compared with the end of the previous year. In the office property segment, slight increases were visible in some markets such as Berlin and Madrid. Average rents were stable in numerous markets, as were prime rents for logistics and retail property.

Prime yields for commercial property showed a mixed picture in the European economic centres.[2] For office properties, yields – which were already at very low levels in some cases – continued to decline in only a few markets, such as the Netherlands and in Warsaw, compared to the end of the previous year. Yields for retail properties continued to decline in Germany and the Netherlands, whilst they increased slightly in France and in the UK. Yields for prime commercial logistics properties fell noticeably in 2018, compared with the end of 2017. Political uncertainty in Italy had no direct impact on property market yields there – in fact, they even declined slightly. For office properties outside the top-class range, yields tended to be stable to slightly lower. Yields on retail property beyond the prime locations were stable. However, they increased noticeably in some cases – particularly in France, Italy, the Netherlands, and the UK.

The hotel markets in the European economic centres painted a diverging picture in 2018. Occupancy rates rose compared with 2017 in some markets such as Brussels, London, Madrid and Paris. They

[2] Falling yields are associated with rising property market values, whilst rising yields correspondingly produce falling values, all other things remaining equal.

fell slightly in Hamburg and Munich, for example, and to a slightly greater extent in Barcelona and Warsaw. The indicator of average revenue per available room (which is important for hotel markets) recorded a slight increase in most markets, such as Amsterdam and London; strong increases were seen in Brussels and Paris. Average revenues per available hotel room in Hamburg and Munich were down slightly on the previous year. Barcelona and Warsaw, however, reported marginally greater declines.

Aareal Bank originated new business of € 5.6 billion (2017: € 5.6 billion) in Europe during the year under review. As in the previous years, Western Europe accounted for the largest share of € 3.5 billion (2017: € 4.2 billion), followed by Southern Europe with € 1.2 billion (2017: € 0.9 billion) and Northern Europe with € 0.6 billion (2017: marginal new business). New business of € 0.3 billion was generated in Eastern Europe (2017: € 0.5 billion).

North America

Transaction volumes in commercial property rose markedly in comparison with the previous year. The volume was in a higher range by historical standards. Investor interest thus remained high, despite rising interest rates.

REIT structures were clearly on the sell side, while private investors reported balanced investment positions. Cross-border and institutional investors were active market participants, and clearly on the buy side.

Rents for office and retail properties were virtually stable on a national average in the US, compared to the final quarter of 2017. There were marginal differences in the regional centres. Rents for office properties rose slightly in, for example, Atlanta, Chicago and Los Angeles. By contrast, they stagnated in Boston, New York and Washington, DC. Retail property rents rose for example in Atlanta and Denver, but showed a slightly declining trend in New York and San Francisco.

The year under review was characterised by largely constant yield developments. On a national average, investment yields in the US hardly moved – compared to the year-end 2017 – for office and retail properties. A slight increase was observed for office properties in Washington DC, both in and outside prime locations.

In the US, average occupancy rates for hotel properties remained stable compared with the previous year. Average revenue per available hotel room climbed slightly, when measured against the comparable value from 2017. In Canada, occupancy rates rose slightly, whilst average revenue per available hotel room increased significantly.

Aareal Bank originated new business of € 3.7 billion in North America during the year under review (2017: € 3.1 billion). This business was originated in the US and in Canada.

Asia / Pacific

Transaction volumes in the Asia / Pacific region were stable compared to the previous year in 2018. The volume was very high, historically.

Cross-border and institutional investors were on the buy side for the most part, while REIT structures and private investors were clearly on the sell side.

Rents for prime office properties hardly changed compared to the 2017 year-end, whilst they declined slightly in Shanghai. Rents for retail properties in Beijing declined significantly; they remained stable in Shanghai. Yields were stable to slightly rising for office properties, whereas they declined marginally for retail properties. By contrast, prime rents for office properties in Australia rose slightly in Melbourne and Sydney. Prime retail rents remained stable, while rising slightly for logistics property in (for example) Adelaide and Melbourne.

Investment yields for newly-acquired, high-quality office property remained stable in Beijing and Shanghai. Yields for retail property were stable in Beijing, whilst a slight decline was observed in Shanghai. In Australia, yields for office, retail and logistics properties fell in most markets.

Developments on the hotel markets in Beijing and Shanghai varied during the year under review, compared with the corresponding prior-year period. Whilst the average revenue per available hotel room rose markedly and occupancy rates increased slightly in Beijing, occupancy figures in Shanghai fell slightly on stable average revenues per available hotel room.

Aareal Bank originated new business of € 0.2 billion in the Asia / Pacific region during the year under review (2017: € 0.1 billion).

Acquisition of Düsseldorfer Hypotheken-bank AG (Düsselhyp)

Aareal Bank Group successfully closed the acquisition of Düsseldorfer Hypothekenbank AG (Düsselhyp), announced on 10 September 2018. The purchase was completed with effect from 31 December 2018 (the closing date). Düsselhyp is therefore now a legally independent subsidiary under the umbrella of Aareal Bank Group. The purchase price paid amounted to € 149 million. Aareal Bank will not pursue any further strategic objectives with this acquisition, and will consistently pursue the orderly run-down.

Items acquired within the scope of the acquisition included € 0.3 billion in loan receivables, and money and capital market receivables of € 2.0 billion. The acquisition resulted in a negative goodwill of € 55 million, which was recognised in income. Further information is included in the section "Consolidation".

Consulting / Services segment

Bank division Housing Industry

Business development in the German housing industry proved solid in 2018 as well. Largely constant rental income and long-term funding structures secure a solid foundation and facilitate entrepreneurial investments in conjunction with the very low interest rates. The German Federation of German Housing and Real Estate Enterprises (Bundesverband deutscher Wohnungs- und Immobilienunternehmen – "GdW") expected a record number of new builds (31,000 apartments) in 2018 from the housing enterprises that are organised in its regional associations. Nationwide rent levels in Germany were up by around 2.9 % year-on-year in 2018 – a slight slowdown compared to the third quarter when the increase over the previous year's figure still amounted to 3.5 %.

However, market development varied from region to region. The contrast observed – up to 2017 – between rising demand for housing in the major cities and university cities, and the constant population loss in rural areas, eased in the year under review. Although population figures continued to rise in the big cities due to ongoing migration into Germany and a record number of students, many of those searching for accommodation turned to the outskirts of the urban centres.Despite the falling trend in Germany, the vacancy ratio in the classic shrinking regions continues to rise. The vacancy ratio based on the housing stock managed by GdW enterprises is stable, forecast for 2018 at 1.6 % (2017: 1.7 %) in the former West German Federal states and at 8.1 % (2017: 8.2 %) in the former East German states.

The Bank's Housing Industry division further strengthened its market position in the 2018 financial year, bringing in more business partners from the institutional housing industry and the commercial property sector – managing around 160,000 residential units between them – for the payments and deposit-taking businesses. Moreover, it intensified existing business relationships. We also continuously expanded our client base in the energy and waste disposal industries, especially through interface products (such as BK 01 eConnect and BK 01 immoconnect) facilitating cross-sector collaboration amongst our client groups. Examples include accounting documentation and invoicing of energy supplies. Projects were started – together with clients – which are aimed at further improving and automating cross-sector cooperation.

In addition, the Housing Industry division is analysing the development of alternative online payment systems very intensively. Projects were also launched here to integrate these into existing programmes and processes.

At present, just under 4,000 business partners throughout Germany are using our process-optimising products and banking services. The high volume of deposits, averaging € 10.4 billion (2017: € 10.0 billion) in the year under review, is in line with the "Aareal 2020" programme for the future. The share of rent deposits and reserves in accordance with the German Residential Property Act was increased once again. Deposits averaged € 10.4 billion in the fourth quarter of 2018 (2017: € 10.4 billion). All in all, this reflects the strong trust that clients place in Aareal Bank.

Aareon

Aareon is the leading international consultancy and IT systems house for the property industry in Europe. It is pursuing a profitable growth strategy, and continued to grow during the 2018 financial year. Key factors to its success are customer orientation, the growth in digital solutions, further strengthening of the ERP systems and exploration of new markets and related sectors associated with the property industry. The process of internal optimisation to enhance the organisational performance and profitability also continued.

With € 36 million (2017: € 34 million), Aareon exceeded its contribution to earnings figure for the previous year. This was achieved especially by the increased licence and maintenance business. Non-recurring effects incurred with three large-scale projects, in terms of higher costs and delays, prevented a better performance in the advisory business, on which the original forecast was based. Moreover, Aareon increased research and development investments in order to boost future growth.

As expected, numerous additional customers opted for Wodis Sigma in Germany during the course of 2018, bringing the total number to around 1,000. As expected, the favoured version is the one that uses Wodis Sigma as a service from the exclusive Aareon Cloud. The volume of business conducted with SAP® solutions and Blue Eagle is down slightly on the previous year, due to the aforementioned higher costs incurred on a major project. Additional commercial property customers were acquired for the RELion ERP solution. In the Netherlands, several key accounts opted for the Tobias AX ERP solution within the scope of a tender – some products were rolled out, too. Demand for the ERP service range increased in France, as legal requirements had to be implemented in the software. Further customers also opted for a Platinum contract with higher service levels. Despite intense competition in the UK, Aareon UK succeeded in winning several tenders for Aareon QL. Likewise, Aareon Sverige won key tenders with its Incit Xpand ERP solution. Aareon Sverige has also proved successful in the Finnish market. The business in Norway was burdened by delays and higher costs incurred on two major projects.

Digitalisation is becoming increasingly important for the property industry. With its Aareon Smart World digital ecosystem, Aareon offers integrated solutions for automating the business process and networking business partners and market participants. The digital transformation process for customers is therefore focused on creating added value. Aareon continues to steadily expand this offer, and benefits from the transfer of international know-how in research and development. With the digital solutions, the cross-border development of Aareon CRM to simplify customer relationship management between the tenants/owners in particular was driven forward. In addition, Aareon Smart World is being expanded to include digital solutions from PropTech cooperation partners. In order to participate to a greater extent in interesting and innovative enterprises, Aareon Group founded AV Management GmbH. It operates under the brand name Ampolon Ventures and is strongly linked to the start-up scene.

The business volume of the digital solutions has continued to grow strongly year-on-year, driven in particular by migration business related to the ERP solutions, since customers usually acquire one or several new digital solutions when switching.

Within the area of add-on products, Aareon was able to extend its outsourcing business in Germany. BauSecura's insurance business has been running at the previous year's level. On the international market, the outsourcing business in the Netherlands made a significant contribution to the increase in revenue. Following the full acquisition of the Dutch company SG2ALL B.V. in 2016, it was merged into Aareon Nederland on 1 January 2018, together with its outsourcing business.

Aareon is now targeting new markets, such as utilities. The marketing process for the Aareon Occupant Change Management solution has started: several customers have already decided in favour of it.

Financial Position and Financial Performance

Financial performance

Group

Consolidated operating profit in the 2018 financial year amounted to € 316 million (2017: € 328 million), thus corresponding to our raised profit forecast. The figure includes the € 55 million negative goodwill from the initial consolidation of Düsselhyp. The comparative figure for the previous year's period also included material non-recurring income of € 50 million in net reversals of provisions in connection with the acquisition of Corealcredit in 2014, recognised in net other operating income/expenses, as well as a corresponding income tax expense of € 26 million. The expected decrease in net interest income was more than offset by increased commission income, lower loss allowance and reduced administrative expenses. However, the volatile market-driven net derecognition gain was significantly below our expectations and the previous year's figure. After taking taxes into consideration, the segment result rose slightly in comparison with the previous year.

Net interest income totalled € 535 million, an expected reduction from the previous year (2017: € 584 million), which was largely due to the portfolio decline seen in 2017, reflecting – amongst other factors – the scheduled reduction of the former WestImmo and Corealcredit portfolios.

Consolidated net income of Aareal Bank Group

€ mn	1 Jan-31 Dec 2018	1 Jan-31 Dec 2017 [1]
Net interest income	535	584
Loss allowance	72	82
Net commission income	215	206
Net derecognition gain or loss	24	50
Net gain or loss from financial instruments (fvpl)	-2	14
Net gain or loss from hedge accounting	-2	-7
Net gain or loss from investments accounted for using the equity method	0	–
Administrative expenses	462	511
Net other operating income/expenses	25	74
Negative goodwill from acquisitions	55	–
Operating profit	**316**	**328**
Income taxes	90	115
Consolidated net income	**226**	**213**
Consolidated net income attributable to non-controlling interests	2	6
Consolidated net income attributable to shareholders of Aareal Bank AG	224	207

[1] Comparative amounts reclassified according to the new classification format

Loss allowance amounted to € 72 million (2017: € 82 million) and was thus in line with our expectations as well.

Net commission income increased to € 215 million (2017: € 206 million), which was mainly due to higher sales revenue at Aareon.

The volatile, market-driven net derecognition gain of € 24 million (2017: € 50 million) declined due to lower effects from early loan repayments and was thus significantly below our expectations.

The net loss from financial instruments (fvpl) and on hedge accounting in the aggregate amount of € -4 million (2017: € 7 million) mainly resulted from exchange rate fluctuations and changes in the measurement of hedging derivatives (fvpl).

At € 462 million (2017: € 511 million), administrative expenses were reduced slightly more than expected, thanks to lower transformation costs and lower running costs.

All in all, consolidated operating profit for the 2018 financial year totalled € 316 million, after € 328 million in 2017. Taking into consideration tax expenses of € 90 million and non-controlling interest income of € 2 million, consolidated net income attributable to shareholders of Aareal Bank AG amounted to € 224 million (2017: € 207 million). Assuming the pro rata temporis accrual of net interest payments on the AT1 bond, consolidated net income allocated to ordinary shareholders stood at € 208 million (2017: € 191 million). Earnings per ordinary share amounted to € 3.48 (2017: € 3.20) and return on equity (RoE) before taxes stood at 11.6 % (2016: 11.9 %).

Structured Property Financing segment

Operating profit in the Structured Property Financing segment was € 338 million, below the previous year's figure of € 351 million. The figure includes the € 55 million negative goodwill from the initial consolidation of Düsselhyp. The comparative figure for the previous year's period also included material non-recurring income of € 50 million in net reversals of provisions in connection with the acquisition of Corealcredit in 2014, recognised in net other operating income/expenses, as well as a corresponding income tax expense of € 26 million. The expected decrease in net interest income

Structured Property Financing segment result

€ mn	1 Jan-31 Dec 2018	1 Jan-31 Dec 2017 [1)]
Net interest income	547	596
Loss allowance	73	82
Net commission income	9	7
Net derecognition gain or loss	24	50
Net gain or loss from financial instruments (fvpl)	-2	14
Net gain or loss from hedge accounting	-2	-7
Net gain or loss from investments accounted for using the equity method	0	–
Administrative expenses	241	296
Net other operating income/expenses	21	69
Negative goodwill from acquisitions	55	–
Operating profit	**338**	**351**
Income taxes	99	123
Segment result	**239**	**228**

[1)] Comparative amounts reclassified according to the new classification format was more than offset by lower loss allowance and reduced administrative expenses. However, the volatile market-driven net derecognition gain was significantly below our expectations and the previous year's figure. After taking taxes into consideration, segment result rose slightly in comparison with the previous year.

Segment net interest income of € 547 million showed an expected decline from the previous year (€ 596 million), which was largely due to the portfolio decline seen in 2017, reflecting – amongst other factors – the scheduled reduction of the former WestImmo and Corealcredit portfolios.

Loss allowance amounted to € 73 million (2017: € 82 million) and was thus in line with our expectations as well.

The volatile net derecognition gain of € 24 million (2017: € 50 million) declined due to lower effects from early loan repayments and was thus significantly below our expectations.

The net loss from financial instruments (fvpl) and on hedge accounting in the aggregate amount of € -4 million (2017: € 7 million) mainly resulted from exchange rate fluctuations and changes in the measurement of hedging derivatives (fvpl).

At € 241 million (2017: € 296 million), administrative expenses were reduced slightly more than expected, thanks to lower transformation costs and lower running costs.

Overall, operating profit for the Structured Property Financing segment was € 338 million (2017: € 351 million). Taking income tax expenses of € 99 million into consideration (2017: € 123 million), the segment result was € 239 million (2017: € 228 million).

Consulting/Services segment

As expected, sales revenue generated in the Consulting/Services segment developed positively, driven particularly by Aareon's higher sales revenues in the amount of € 242 million (2017: € 226 million). The persistent low interest rate environment continued to burden margins from the deposit-taking business that are reported in sales revenues.

Consulting/Services segment result

€ mn	1 Jan-31 Dec 2018	1 Jan-31 Dec 2017[1]
Sales revenue	242	226
Own work capitalised	8	4
Other operating income	7	7
Cost of materials purchased	42	35
Staff expenses	159	151
Depreciation, amortisation and impairment losses	15	12
Other operating expenses	63	62
Interest and similar income/expenses	0	0
Operating profit	**-22**	**-23**
Income taxes	-9	-8
Segment result	**-13**	**-15**

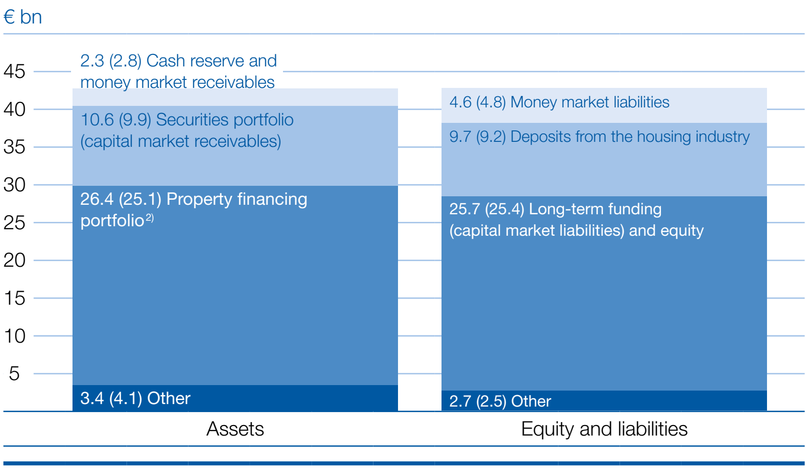
[1] Comparative amounts reclassified according to the new classification format

Both cost of materials purchased and staff expenses increased as expected to € 42 million (2017: € 35 million) and € 159 million (2017: € 151 million), respectively.

Overall, segment operating profit for 2018 was € -22 million (2017: € -23 million). Aareon's contribution was € 36 million (2017: € 34 million).

Taking income taxes into consideration, the segment result amounted to € -13 million (2017: € -15 million).

Statement of financial position – structure as at 31 Dec 2018 (31 Dec 2017[1])



[1] Comparative amounts reclassified according to the new classification format
[2] Excluding € 0.6 billion in private client business (31 December 2017: € 0.8 billion) and € 0.5 billion in local authority lending business by the former Westdeutsche ImmobilienBank AG (WestImmo) (31 December 2017: € 0.5 billion), and excluding loss allowance

Financial position

Consolidated total assets as at 31 December 2018 amounted to € 42.7 billion, after € 41.9 billion as at 31 December 2017.

Cash reserve and money market receivables

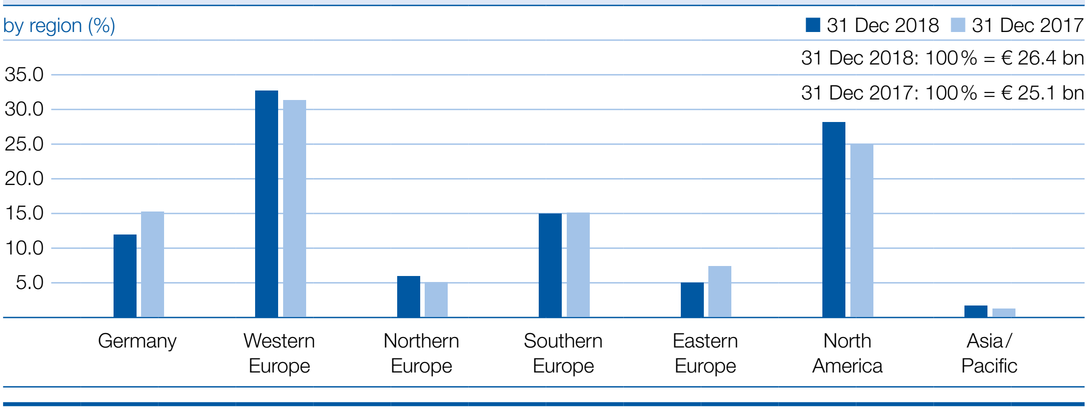
The cash reserve and money market receivables position contains excess liquidity invested at short maturities. As at 31 December 2018, this comprised predominantly cash funds and deposits with central banks and money-market receivables from banks.

Property financing portfolio

The volume of Aareal Bank Group's property financing portfolio stood at € 26.4 billion as at 31 December 2018, up by approx. 5 percentage points from the year-end level 2017 (€ 25.1 billion). This was especially due to both the scheduled expansion of the strategic business as well as the acquisition of Düsselhyp (€ 0.3 billion). The international share of the portfolio increased to 88.0 % (31 December 2017: 84.8 %).

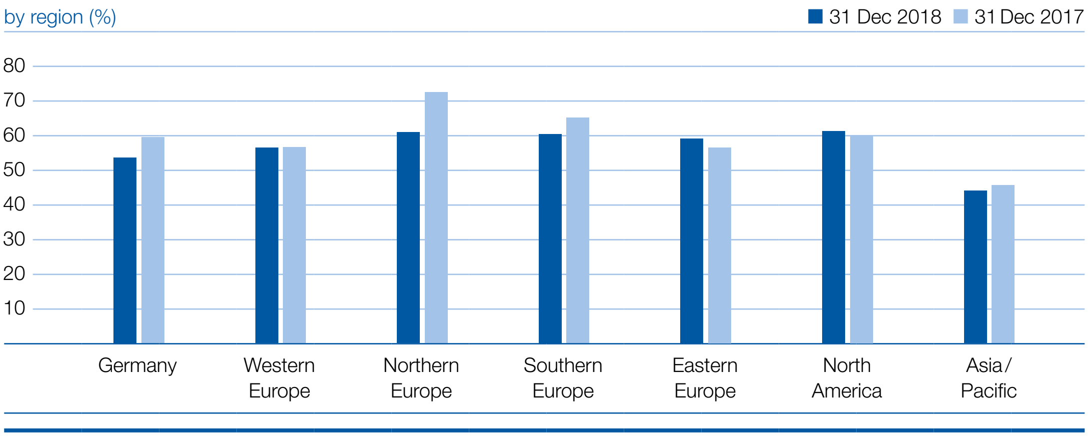
At the reporting date (31 December 2018), Aareal Bank Group's property financing portfolio was composed as shown in following graphs, compared with year-end 2017.

Property financing volume[1] (amounts drawn)



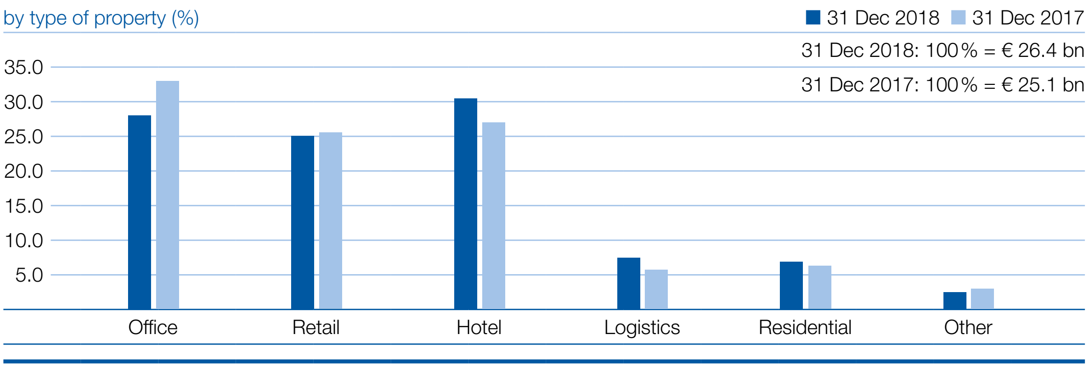
[1] Excluding former WestImmo's private client business and local authority lending business

Average LTV of property financing[1]

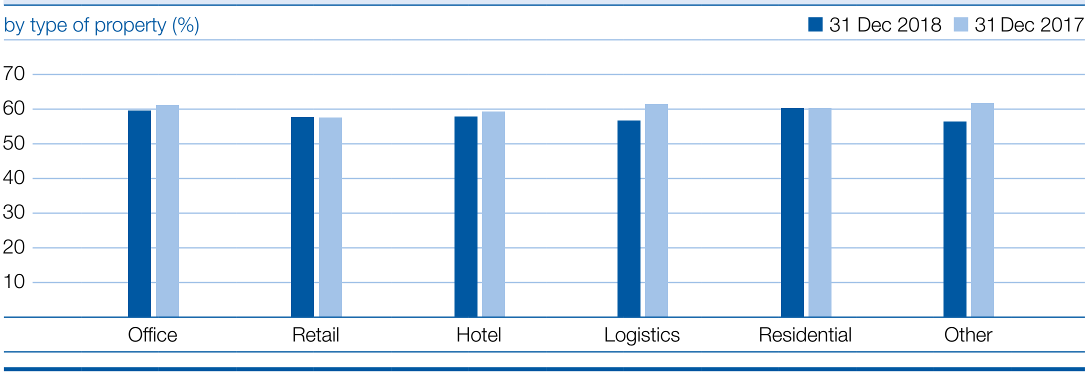


Note that the loan-to-value ratios are calculated on the basis of drawdowns and market values, including supplementary collateral with sustainable value, excluding defaulted property financings.

Property financing volume[1] (amounts drawn)



Average LTV of property financing[1]



Note that the loan-to-value ratios are calculated on the basis of drawdowns and market values, including supplementary collateral with sustainable value, excluding defaulted property financings.

[1] Excluding former WestImmo's private client business and local authority lending business

Portfolio allocation by region and continent changed only selectively compared with the end of the previous year. Whilst the portfolio share of exposures in North America rose by about 3.1 percentage points, it was down by around 3.2 percentage points for Germany, and approx. 2.5 percentage points down for Eastern Europe, remaining relatively stable for all other regions.

The breakdown of the portfolio by property type did not change significantly during the reporting period. The share of hotel property increased by 3.5 percentage points compared to year-end 2017, whilst the share of office property was reduced by 4.9 percentage points. The share of financings for residential, logistics, and retail property as well as other financings in the overall portfolio remained almost unchanged compared to the year-end 2017.

All in all, the high degree of diversification by region and property type within the property financing portfolio was maintained during the period under review.

Securities portfolio

Aareal Bank holds a portfolio of high-quality securities, used as economic and regulatory liquidity reserve as well as for the cover management of Pfandbriefe.

As at 31 December 2018, the nominal volume of the consolidated securities portfolio[1] was € 8.7 billion (31 December 2017: € 8.3 billion), of which € 1.4 billion was contributed by the portfolio of Düsselhyp.

Key aspects taken into account for portfolio management are good credit quality and the related value stability, as well as a high degree of liquidity. The securities portfolio comprises three asset classes: public-sector borrowers, covered bonds and Pfandbriefe, as well as bank bonds.

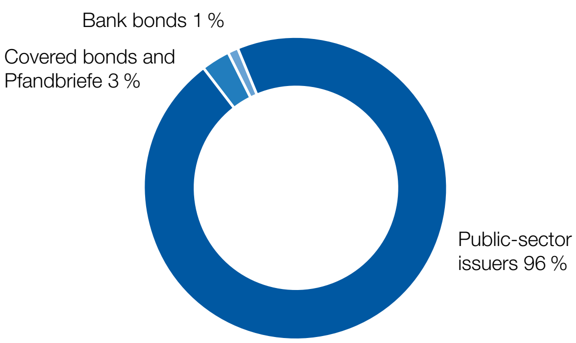
99 % of the overall portfolio is denominated in euro. 99 % of the portfolio has an investment grade rating.[2] More than 75 % of the portfolio fulfils the requirements for "High Quality Liquid Assets" (as defined in the Liquidity Coverage Ratio (LCR)).

Public-sector borrowers are the largest asset class held, accounting for a share of approx. 96 %. These include securities and promissory note loans that qualify as ordinary cover for Public-Sector Pfandbriefe. 99 % of these issuers are headquartered in the EU. Around 72 % are rated AAA or AA, and a further 7 % are rated single-A.

The share of Pfandbriefe and covered bonds at year-end was 3 %, exclusively including European covered bonds and Pfandbriefe, of which more than 85 % were rated AAA.

Securities portfolio as at 31 December 2018

% Total volume (nominal): € 8.7 bn



Financial position

Money-market liabilities and deposits from the housing industry

Generally, in addition to customer deposits, Aareal Bank also uses interbank and repo transactions for short-term refinancing, the latter being used primarily to manage liquidity and cash positions.

As at 31 December 2018, Aareal Bank had € 9.7 billion at its disposal in deposits generated from the business with the housing industry (31 December 2017: € 9.2 billion). Money-market

[1] As at 31 December 2018, the securities portfolio was carried at € 10.6 billion (31 December 2017: € 9.9 billion).

[2] The rating details are based on the composite ratings.

liabilities amounted to € 4.6 billion (31 December 2017: € 4.8 billion). Beyond that, there were no repos and no liabilities vis-à-vis Deutsche Bundesbank or the ECB.

Long-term funding and equity

Funding structure

Aareal Bank Group's funding remains very solid indeed, as evidenced by the high proportion of long-term refinancing. This encompasses registered and bearer Pfandbriefe, promissory note loans, medium-term notes, other bonds and subordinated issues. The latter include subordinated liabilities and Additional Tier 1 (AT1) issues.

As at 31 December 2018, the long-term refinancing portfolio amounted to € 23.1 billion. Of this amount, Mortgage Pfandbriefe accounted for € 10.9 billion, public-sector Pfandbriefe for € 3.0 billion, uncovered long-term refinancing for € 7.9 billion and subordinated long-term refinancing for € 1.3 billion.

The Liquidity Coverage Ratio (LCR) at Group level exceeded 150 % on the reporting days during the period under review.

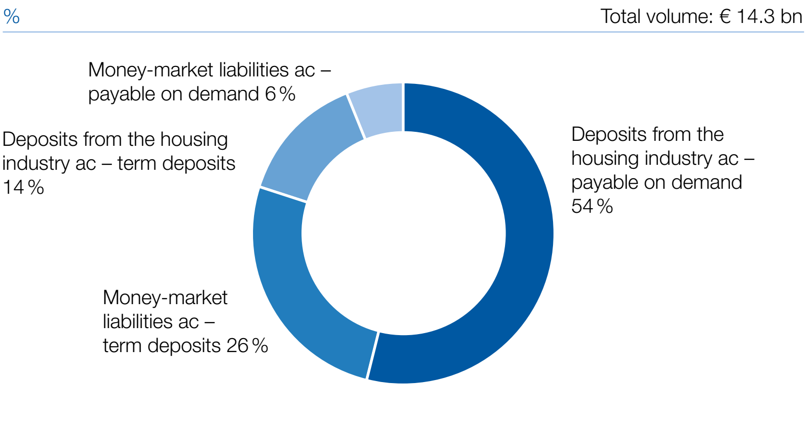
Refinancing activities

Throughout the financial year 2018 Aareal Bank Group was able to very successfully raise liquidity in the amount of € 3.4 billion on the capital market. Of this volume, € 2.5 billion are attributable to Pfandbriefe, € 0.7 billion to Senior Preferred Bonds and € 0.2 billion to Senior Non-Preferred Bonds.

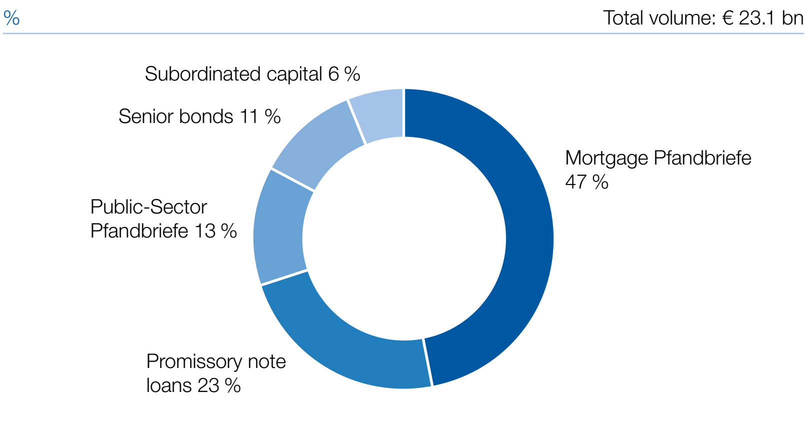
It contains, among other things, four Mortgage Pfandbriefe of € 0.5 billion each, as well as a Pfandbrief transaction amounting to £ 0.3 billion. The remaining volume was raised via private placements.

Since we conduct our business activities in a range of foreign currencies, we have secured our foreign currency liquidity over the longer term by means of appropriate measures.

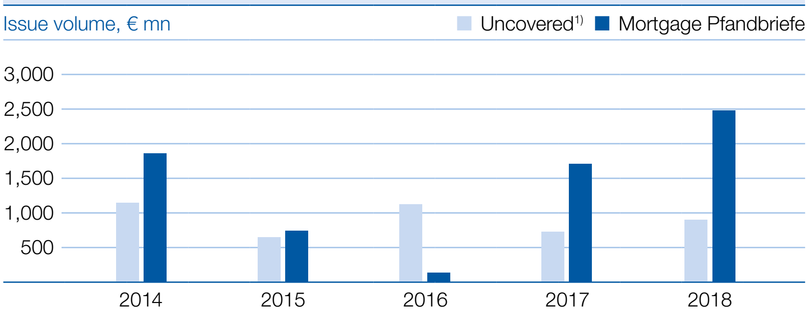
Money market funding mix as at 31 December 2018



Capital market funding mix as at 31 December 2018



Issuing activities – 2014 to 2018



[1] Excluding SoFFin-guaranteed issues and subordinated capital

Equity

Aareal Bank Group's total equity as disclosed in the statement of financial position amounted to € 2,928 million as at 31 December 2018 (31 December 2017: € 2,924 million), comprising € 300 million for the Additional Tier 1 (AT 1) bond. Please also refer to the statement of changes in shareholders' equity, and to our explanations in Note 55.

For further information on the transitional effects resulting from the introduction of IFRS 9, please refer to the section "First-time application of IFRS 9 Financial Instruments" in Note 2 "Changes in accounting policies".

Regulatory indicators [1)]

	31 Dec 2018 [2)]	31 Dec 2017
€ mn		
Common Equity Tier 1 (CET 1)	2,241	2,305
Tier 1 (T1)	2,541	2,600
Total capital (TC)	3,419	3,536
%		
Common Equity Tier 1 ratio (CET 1 ratio)	17.2	19.6
Tier 1 ratio (T1 ratio)	19.5	22.1
Total capital ratio (TC ratio)	26.2	30.0
Common Equity Tier 1 ratio (CET 1 ratio) (%) – Basel IV (estimate) – [3)]	13.2	13.4

1) Aareal Bank AG utilises the rules set out in section 2a of the KWG in conjunction with Article 7 of the CRR, pursuant to which regulatory indicators of own funds may only be determined at Group level. In this respect, the following disclosures relate to Aareal Bank Group.

2) When calculating own funds, annual profits including negative goodwill were taken into account, based on the Management Board's proposal for appropriation of profits for the 2018 financial year. The appropriation of profits is subject to approval by the Annual General Meeting. The expected relevant impact of the TRIM exercise on commercial property financings, and of the SREP recommendations concerning ECB's NPL guidelines (NPL stock), were taken into account for determining regulatory indicators for 2018. Due to the fact that the ECB has not yet approved the application for inclusion of profits (including negative goodwill) as at 31 December 2018, the corresponding regulatory report did not incorporate attributable annual profits (including negative goodwill), nor the effects of the TRIM exercise. CET1 amounted to € 1,994 million, with T1 at € 2,294 million and TC at € 3,172 million. The CET1 ratio thus stood at 18.5 %, the T1 ratio at 21.3 %, and the TC ratio at 29.4 %. Assuming the ECB's approval, the regulatory report as at 31 December 2018 would incorporate annual profits including negative goodwill, but excluding the TRIM effects. CET1 would amount to € 2,263 million, with T1 at € 2,563 million and TC at € 3,442 million. The CET1 ratio would amount to 21.0 %, the T1 ratio 23.8 %, and the TC ratio 31.9 %.

3) Underlying estimate, given a 72.5 % output floor based on the final Basel Committee framework dated 7 December 2017. The calculation of the material impact upon Aareal Bank is subject to the outstanding EU implementation as well as the implementation of additional regulatory requirements (CRR II, EBA requirements etc.).

Our Employees

Employee data as at 31 December 2018

	31 Dec 2018	31 Dec 2017	Change
Number of employees at Aareal Bank Group	2,748	2,800	-1.9 %
Years of service	12.7 years	12.9 years	- 0.2 years
Staff turnover rate	5.8 %	4.0 %	

The overview of employee key indicators in the "Responsibility" section of the Company's website (www.aareal-bank.com/en/responsibility/reporting-on-our-progress/) provides more information, including the breakdown by gender, age and region.

Qualification and training programmes

Qualified and motivated employees make a decisive contribution to our Company's economic performance and are thus a key factor in its success – as well as a competitive advantage. For this purpose, Aareal Bank Group operates a human resources approach aimed at the further qualification of its managers, experts and employees. In line with the corporate strategy, the human resources policy is continuously developed in a targeted way. Aareal Bank Group supports employees in change processes, and promotes lifelong professional learning.

The Group consistently pursued this strategy throughout the year under review. The Bank focused on specific and generic training measures – for example, in the form of qualification programmes for (agile as well as traditional) project management, as well as supporting measures related to organisational and team development, which were tailored to the Group-wide reorganisation efforts. At Aareon, the training focus was on targeted development measures for managers, comprising training, diagnostics and consulting offers, as well as SAP HANA® training. Expanding professional knowledge of the Aareon Smart World, within the scope of a weekly WodisSigma University WebEx session, was another focal area. Both Aareal Bank and Aareon also attached great importance to further building language and communications skills: to this end, a digital language learning portal was introduced, which provides instructions for learning English as well as five other European languages. This learning portal allows all employees throughout the Group to improve their language skills, anywhere (even at home) and at any time.

Promoting the next generation

Promoting the next generation through training is a central element of Human Resources work at Aareal Bank Group. The specialist knowledge required in our business segments requires us to invest continuously – and in a targeted manner – in training the next generation.

The Bank's "Junior Training Programmes" provided support for young people in terms of training, including trainees for office management (within training courses at the Chamber of Commerce and Industry (IHK)), work-study students in the fields of business administration, banking, and business information systems from the Baden-Württemberg Cooperative State University (Duale Hochschule Baden-Württemberg/DHBW), Mannheim, as well as business administration students from the University of Applied Sciences Mainz (Hochschule Mainz).

Besides training programmes, Aareon offers the dual course of study "Business information systems" and "Media, IT and management" as well as various vocational training opportunities for office managers, IT applications developers or IT systems integrators.

As in previous years, the Bank and Aareon held the Girls' Day as part of its measures for promoting the next generation. Furthermore, Aareon supported the initiative JOBLINGE aimed at socially deprived young citizens. First participants of this programme have meanwhile embarked on their training. To promote trainees and science, Aareon is cooperating with several universities, as well as with students, as part of the German scholarship of the Johannes Gutenberg University in Mainz.

Remuneration system

In addition to a fixed remuneration component, all permanent employees receive performance-based variable remuneration. Salaries are reviewed annually, to ensure that individual remuneration packages are appropriate. The objective is to offer a remuneration level that is both appropriate and attractive to all Group employees.

Work-life balance

Aareal Bank Group places great importance on supporting its employees to achieve compatibility between career and family. This is emphasised by a broad range of dedicated support services such as partnerships with childcare institutions or service providers for the provision of private childcare, holiday programmes for employees' children, the availability of parent-child workrooms, flexible working policies, part-time positions and the option of working remotely or alternating teleworking for all employees. Another component of improving the work-life balance of the employees consists of services that make it easier to combine working life with the care of those who require it. This includes, among other things, the offer of counselling and support in the event of illness as well as nursing care for close relatives (available throughout Germany), and the option of participating in various training courses for better compatibility between family, care and work. As an innovative company that promotes the digital transformation process holistically and manages the related process of change for its employees, Aareon had already launched the "work4future" project in 2017. Based on the existing principles of a human resources policy aligned to different phases in life, it focuses on enhancing work models, effective and smart employee collaboration, and the digital workplace.

Health

In order to verify the effectiveness and continuous improvement of occupational safety management, occupational safety committees meet quarterly. These include the respective company doctor and occupational safety specialists, in addition to various company officers.

In order to protect and promote the health of its employees in a targeted manner, Aareal Bank Group offers a comprehensive range of health-promoting measures in the areas of information, prophylaxis, exercise and ergonomics, nutrition, mental health and relaxation that are always based on employees' current needs. In the year under review, these included preventative, individual health consultations held in the Bank on various topics, workshops on topics such as relaxation, nutrition and fasciae, management and employee workshops on the topics of healthy leadership and remaining healthy in times of change, stress prevention and management measures, health checks, colon cancer screening, skin screenings and flu vaccinations. The motto for Aareon's occupational health management in 2018 was "#fit4work4future" and numerous measures for supporting employees in a digital working world were implemented to this end.

Risk Report

Aareal Bank Group Risk Management

The ability to correctly assess risks, and to manage them in a targeted manner, is a core skill in banking. Accordingly, being able to control risks in all their relevant variations is a key factor for a bank's sustainable, commercial success. This economic motivation for a highly-developed risk management system is continuously increased by extensive regulatory requirements for risk management. We therefore continued to drive the development of our processes for identifying, measuring, limiting and managing risks in the financial year under review, too – with a focus on implementing the ECB's new guidelines for the Internal Capital Adequacy Assessment Process (ICAAP) and the Internal Liquidity Adequacy Assessment Process (ILAAP). During the course of the year, this resulted – inter alia – in a changed risk taxonomy, as already outlined in the half-yearly report.

Risk management – scope of application and areas of responsibility

Aareal Bank Group's business activities comprise the Structured Property Financing and Consulting/Services segments. Aareal Bank AG, as the parent entity of the Group, has implemented extensive systems and procedures to monitor and manage the Group's risk exposure.

Uniform methods and procedures are deployed to monitor material risks generally associated with banking business across all entities of Aareal Bank Group. Specific risk monitoring methods have been developed and deployed to suit the relevant risk exposure at the subsidiaries. In addition, risk monitoring for these subsidiaries at Group level is carried out via the relevant control bodies of the respective entity, and equity investment controlling.

Overall responsibility for risk management and risk monitoring remains with the Management Board and the Supervisory Board of Aareal Bank AG. The adjacent diagram provides an overview of the responsibilities assigned to the respective organisational units.

Overall responsibility: Management Board and Supervisory Board of Aareal Bank AG

Type of risk		Risk management	Risk monitoring
Credit risks	Property Financing	Loan Markets & Syndication Credit Risk Project & Credit Portfolio Management Credit Transaction Management	Risk Contolling
	Treasury business	Treasury	Risk Controlling
	Country risks	Treasury Credit Risk Credit Transaction Management	Risk Controlling
Interest rate risk in the banking book (IRRBB)		Treasury; Transaction Committee	Risk Controlling Finance & Controlling
Credit spread and migration risks in the banking book (CSRBB)		Treasury; Transaction Committee	Risk Controlling
Other market risks		Treasury; Transaction Committee	Risk Controlling
Operational risk		Process owners	Risk Controlling
Investment risks		Group Strategy	Risk Controlling Finance & Controlling Controlling bodies
Property risks		Aareal Estate AG	Risk Controlling
Business and strategic risks		Group Strategy	Risk Controlling
Liquidity risks		Treasury	Risk Controlling

Process-independent monitoring: Revision

The Management Board formulates the business and risk strategies, as well as the so-called Risk Appetite Framework. For this purpose, "risk appetite" means the maximum risk exposure where the Bank's continued existence is not threatened, even in the event of risks materialising (the "going-concern" approach). For individual business units (the "First Line of Defence"), the Risk Appetite Framework defines guidelines for the independent and responsible handling of risks.

The risk monitoring function (the "Second Line of Defence") regularly measures utilisation of risk limits, and reports on the risk situation. In this context, the Management Board is supported by the Risk Executive Committee (RiskExCo). The RiskExCo develops proposals for resolutions in line with delegated tasks, and promotes risk communications and a risk culture within the Bank. The risk management system was supplemented by a recovery plan, in line with regulatory requirements, which comprises the definition of threshold values for key performance indicators – both from an economic and a normative perspective. These are designed to ensure that any negative market developments having an impact upon our business model are identified at an early stage and corresponding action is taken in order to safeguard the sustained continuation of business operations.

On top of this, Group Internal Audit (as the "Third Line of Defence") reviews the organisational structure and procedures, as well as risk processes – including the Risk Appetite Framework – and assesses their appropriateness. Moreover, internal processes provide for the involvement of the Compliance function whenever there are facts which are compliance-relevant.

In order to efficiently perform its control duties, amongst other measures, the Supervisory Board has established a Risk Committee, whose responsibility includes the risk strategies as well as the management and monitoring of all material types of risk.

Strategies

The business policy set by the Management Board, and duly acknowledged by the Supervisory Board, provides the conceptual framework for Aareal Bank Group's risk management. Taking this as a basis, and strictly considering the Bank's risk-bearing capacity, we have formulated detailed strategies for managing the material types of risk. Taken together, these represent the Group's risk strategy. These strategies are designed to ensure a professional and conscious management of risks. Accordingly, these strategies include general policies, to ensure a uniform understanding of risks across all parts of the Group. They also provide a cross-sectional, binding framework applicable to all divisions. The Bank has implemented adequate risk management and risk control processes to implement these strategies, and to safeguard the Bank's risk-bearing capacity.

The business strategy and the risk strategies are subject to review on an ongoing basis, and are updated if necessary. Besides the regular review (and, if appropriate, adjustment) of the business strategy (and consequently, the Group risk strategy), the Bank's risk-bearing capacity is validated at least once a year. For this purpose, the appropriateness of risk measurement methods, processes, and risk limits is examined in particular. During the financial year under review, the strategies were adopted by the Management Board, duly noted, and approved by the Supervisory Board.

The Bank has defined escalation and decision-making processes to deal with limit breaches. Risk Controlling ensures the timely and independent risk monitoring to the Management Board.

Aareal Bank Group maintains a decentralised Internal Control System (ICS), with control activities and results being outlined in the Written Set of Procedural Rules. These describe individual processes of divisions, subsidiaries, or other units. Internal controls may run upstream, downstream, or in parallel to workflows; this applies both to automatic control and monitoring functions as well as to the respective manual steps. Accordingly, the ICS comprises the entire universe of control activities; its objective is to ensure that qualitative and quantitative standards are adhered to (compliance with legal or regulatory requirements, with limits etc.).

The appropriateness and effectiveness of controls is reviewed on an event-driven basis; in any case, at least once a year. The results are discussed with the corresponding units within the Second and Third Lines of Defence (Risk Controlling, Compliance and Internal Audit), and reported to the Management Board and the Supervisory Board. In the event of any irregularities or violations, depending on the severity of the event, the Management Board must be notified without delay, so that adequate measures or audit activities can be initiated at an early stage.

Risk-bearing capacity and risk limits

The Bank's ability to carry and sustain risk is a core determining factor governing the structure of its risk management system. To ascertain its uninterrupted risk-bearing capacity, Aareal Bank Group has adopted a dual management approach whereby its risk management is primarily based on the assumption of a going concern. This approach ensures that risk positions are only established to an extent that the institution's continued existence will not be threatened should the risks materialise. A secondary management process ensures that risk positions are only established to an extent that even in the event of liquidation there will still be sufficient potential risk cover in order to service all liabilities (the "gone concern" approach). The statements below relate to the going-concern approach which the Bank has implemented as a primary management process.

In accordance with this approach, potential risk cover is determined using data derived from the income statement and from the statement of financial position; this derivation also forms the basis for determining regulatory capital. The risk-bearing capacity concept is based on the conservative planning of Tier I capital until the next year-end date, and the subsequent year-end, respectively. This involves setting aside the maximum amount of own funds required as potential risk cover to offset risks without causing a breach of minimum requirements pursuant to the Capital Requirements Regulation (CRR). Aareal Bank has set Tier I (T1) capital (as defined by the CRR) at a level of 7.75 % of forecast risk-weighted assets (RWA) as a deductible, in accordance with regulatory requirements. Only free own funds exceeding this level are applied as potential risk cover.

The reduction of regulatory capital, in the course of the changeover to IFRS 9, had an identical impact on aggregate risk cover. Given the use of planned Tier 1 capital, this effect was already accounted for as at 31 December 2017. The regular rolling forward of aggregate risk cover to the planning date of 31 December 2019 took place during the second quarter [of 2018].

We are also currently working intensively on the implementation of the ECB's ICAAP guideline, published for consultation. In this context, and within the scope of regular adjustments to the cover assets pools, we adjusted the risk taxonomy in line with regulatory expectations. Specifically, the previous category of market price risk has been broken up with the introduction of risk categories IRRBB (interest rate risk in the banking book) and CSRBB (credit spread risk in the banking book), in line with regulatory requirements; individual limits have been set for these new categories. Foreign exchange risk remains assigned to other market risk. The risk-reducing inclusion of inter-risk correlations is no longer permitted for the purposes of determining risk-bearing capacity utilisation – a key cause for the increase of this indicator. Property risk has been excluded from credit risk, now forming a separate risk type with specific limits. Likewise, "Other risks" has been split, with specific counterparty credit risk (CVA exposure) having been reclassified to CSRBB; business and strategic risks remain within "Other risks".

As a result, we have distinguished eight risk categories since April 2018 (instead of five previously), each with separate limits.

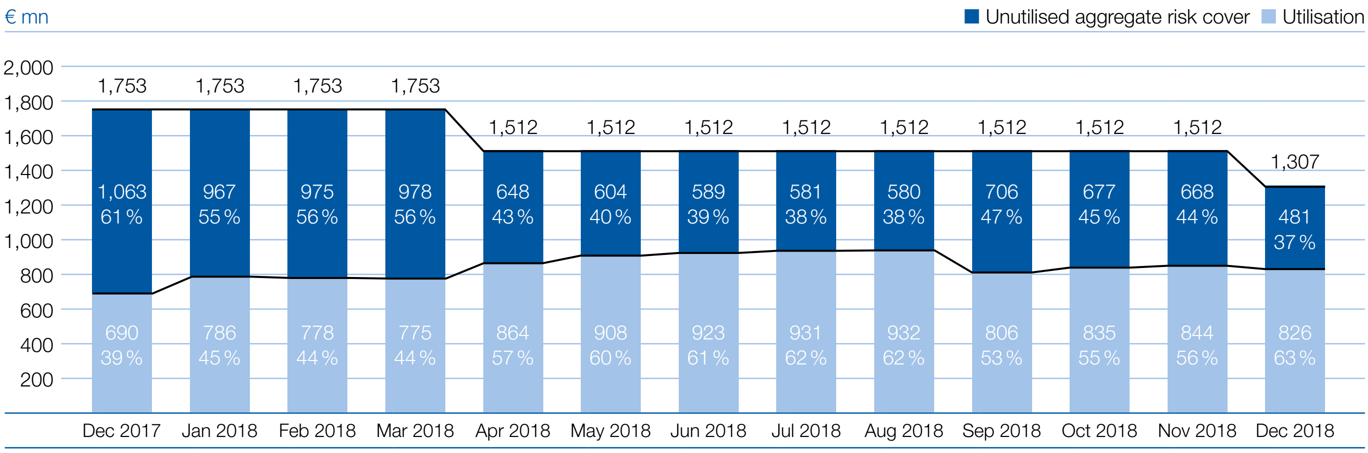
We adopt a conservative stance with respect to setting risk limits. The aggregation of individual limits is based on the assumption that no risk-mitigating correlation effects exist amongst different types of risk. Taking into account the prior deduction of a minimum Tier 1 ratio of 7.75 % of RWA (including the expected impact of the TRIM exercise on commercial property financings, and the SREP recommendations concerning ECB's NPL guidelines (NPL stock)), the value-at-risk (VaR) models used to quantify risks are based on a confidence interval of 95 % and a one-year holding period (250 trading days). Limits are defined at Group level, as well as for the individual Group entities. A detailed monthly report provides information regarding the utilisation of individual limits for the material types of risk, as well as on the overall limit utilisation. These are being monitored as part of daily reporting. No limit breaches were detected during the period under review.

€ mn	31 Dec 2018
Own funds for risk cover potential	2,521
less 7.75 % of RWA1) (Tier 1 capital)	1,214
Freely available funds	**1,307**
Utilisation of freely available funds	
Loan loss risks	195
Interest rate risk in the banking book (IRRBB)	54
Credit spread and migration risks in the banking book (CSRBB)	327
Other market risks	95
Operational risks	85
Investment risks	21
Property risks	27
Business and strategic risks	21
Total utilisation	**826**
Utilisation as a percentage of freely available funds	**63 %**

[1] Including the expected impact of the TRIM exercise on commercial property financings, and of the SREP recommendations concerning ECB's NPL guidelines (NPL stock).

€ mn	31 Dec 2017
Own funds for risk cover potential	2,623
less 7.75 % of RWAs (Tier 1 capital (T1))	870
Freely available funds	**1,753**
Utilisation of freely available funds	
Credit risks	265
Market risks	145
Operational risks	86
Investment risks	21
Other risks	173
Total utilisation	**690**
Utilisation as a percentage of freely available funds	**39 %**

Development of risk limit utilisation during the course of 2018



Given the change in the risk taxonomy in April 2018, comparison with the values as at the previous year-end is not possible.

Utilisation of risk limits developed during the course of the year as shown above.

The expected increase in utilisation in April 2018 was the result of the changeover effect (as outlined above), whereby utilisation levels for new types of risk are now being aggregated. In addition, aggregate risk cover as well as RWAs used to calculate prior deductions are regularly extrapolated to expected year-end values for 2019 in April. The higher utilisation in December 2018 resulted from the acquisition of Düsselhyp as at 31 December 2018, and from the expected impact of the TRIM exercise on commercial property financings, and of the SREP recommendations concerning ECB's NPL guidelines (NPL stock).

Since aggregate risk cover is an inadequate measure to assess the risk-bearing capacity for liquidity risk, we have defined special tools for managing this type of risk. These tools are described in detail in the section "Liquidity risks".

Stress testing

Stress testing, and the analysis of stress test results, form an additional focal aspect of our risk management system. This involves conducting stress tests for all material risks, using both historical parameters as well as hypothetical stress testing scenarios. To also be able to assess cross-relationships between the various types of risk, we have defined multi-factor stress scenarios, so-called "global" stress tests. For instance, the impact of the crisis affecting financial markets and the economy, which broke out in 2007, on individual types of risk and aggregate risk is analysed within the scope of a historical scenario. In the hypothetical scenario, current potential developments are derived from factors such as political developments, and are combined with significant macroeconomic deterioration. The stress testing methodology implemented also takes into account the impact of any risk concentrations. Stress scenarios are analysed both from an economic and a normative perspective, with the respective cross-relationships being taken into consideration – meaning that any economic risks which may materialise (from a normative view) over the analysis period being incorporated in the normative perspective, unless they are sufficiently covered already.

Aareal Bank Group started analysing the impact of Brexit at an early stage: besides the usual (risk) management tools, this has included monitoring the impact on Aareal Bank's risk exposures and business activities by reference to a Brexit Plan. In this plan, the Bank has drawn up various options for action designed to minimise the impact upon the Bank.

The Management Board and the Supervisory Board are informed of the results of stress analyses and the Brexit Plan on a quarterly basis.

Lending business

Division of functions and voting

Aareal Bank Group's structural organisation and business processes are consistently geared towards Group-wide effective and professional risk management. This includes the extensive implementation of regulatory requirements regarding the organisational structure and procedures in the credit business.

Processes in the credit business are designed to consistently respect the clear functional division of Sales units ("Markt") and Credit Management ("Marktfolge"), up to and including senior management level. In addition, the Risk Controlling division, which is not involved in making lending decisions, is responsible for monitoring all material risks whilst ensuring an adequate and targeted risk reporting system at a portfolio level.

Lending decisions regarding credit business classified as relevant for the Bank's risk exposure require two approving votes submitted by a Sales unit and a Credit Management unit. The Bank's Schedule of Powers defines the relevant lending authorities within Sales units and Credit Management. Where authorised persons are unable to come to a unanimous lending decision, the loan involved cannot be approved, or must be presented to the next-highest decision-making level for a decision.

The RiskExCo, which has delegated authority to the heads of Risk Controlling, Operations, and Project & Credit Portfolio Management (which are independent of Sales units), is responsible for the approval of counterparty, issuer, or country limits.

We have implemented and documented the clear separation of Sales and Credit Management processes across all relevant divisions.

Process requirements

The credit process comprises the credit approval and further processing phases, each governed by a control process. Credit exposures subject to increased risks involve supplementary processes for intensified handling, the handling of problem loans, and – if necessary – for recognising allowance for credit losses. The corresponding processing principles are laid down in the Bank's standardised rules and regulations. Important factors determining the counterparty credit risk of a credit exposure are identified and assessed on a regular basis, adequately taking into account sector and (where appropriate) country risks. Critical issues regarding an exposure are highlighted, and analysed assuming different scenarios where appropriate.

Suitable risk classification procedures are applied to evaluate risks for lending decisions, as well as for regular or event-driven monitoring of exposures. This classification scheme is reviewed at least once a year; depending on the risk situations, the review cycle may be shortened significantly. Furthermore, the risk assessment results influence pricing.

The organisational guidelines contain provisions governing escalation procedures and further handling in the event of limit breaches, or of a deterioration in individual risk parameters. Measures involved may include the provision of extra collateral, or an impairment test.

Early risk detection procedures

The early identification of credit risk exposure, using individual or combined (early warning) criteria is a core element of our risk management approach.

In particular, the procedures applied for the early detection of risks serve the purpose of identifying borrowers or exposures where higher risks start emerging, at an early stage. For this purpose, we generally monitor individual exposures and the parties involved (such as borrowers or guarantors) regularly throughout the credit term, assessing quantitative and qualitative factors, using instruments such as periodic monitoring and internal ratings. The intensity of the ongoing assessments is based on the risk level and size of the exposure. The Group's risk management processes ensure that counterparty credit risk is assessed at least once a year.

An "On-watch Committee" has been established in order to enhance the Bank's procedures for the early detection of risks. Whenever there are indications of specific risks, this Committee has global authority – regardless of exposure size – to classify exposures as "normal" or "subject to intensified handling", and to decide on the measures to be taken as well as the composition of the Deal Team handling the exposure. The transfer of know-how is enhanced through the cross-divisional representation on the Committee.

Extensive IT resources are deployed to identify risk positions, and to monitor and measure risks. Overall, the existing set of tools and methods enables the Bank to adopt suitable risk management measures, where required, at an early stage.

Actively managing client relationships is crucially important in this context: approaching clients in time to jointly develop a solution to any problems which may arise. Where necessary, we muster the support of experts from the independent restructuring and recovery functions.

Risk classification procedures

Aareal Bank employs risk classification procedures tailored to the requirements of the respective asset class for the initial, regular, or event-driven assessment of counterparty credit risk. The rating scales and exposure definitions have been customised to match the respective methods. Responsibility for development, quality assurance, and monitoring implementation of risk classification procedures, and for annual validation, lies with two separate divisions outside the Sales units.

The ratings determined using internal risk classification procedures are an integral element of the Bank's approval, monitoring, and management processes.

Property financing business

The Bank employs a two-level risk classification procedure for large-sized commercial property finance exposures, specifically designed to match the requirements of this type of business.

In a first step, the client's probability of default (PD) is determined using a rating procedure. The method used in this context comprises two main components, a property rating and a corporate rating.

The relative impact of the two components on the rating result is determined by the structure of the exposure concerned. The client's current and future default probability is determined based on specific financial indicators, together with qualitative aspects and expert knowledge.

The second step involves calculating the loss given default (LGD). The LGD estimates the extent of the economic loss in the event of a borrower defaulting. In simple terms, this is the amount of the claim not covered by the proceeds from the realisation of collateral.

When evaluating collateral, haircuts are applied or recovery rates used, depending on the type of collateral involved and specific realisation factors. For financings of domestic properties, recovery rates are taken from a pool of data used across the Bank, whilst recovery rates for international properties are derived using statistical methods, given the low number of realisations.

The expected loss (EL) in the event of default of an exposure is determined as the product of PD and LGD. As a risk parameter related to the financing, EL is used as an input factor for the tools used to manage the property financing business.

Financial institutions
Aareal Bank employs an internal rating procedure for financial institutions, which incorporates qualitative and quantitative factors as well as our client's group affiliation, to classify the risk exposure to banks, financial services providers, securities firms, public-sector development banks, and insurance companies. Financial institutions are assigned to a specific rating grade by way of assessing relevant financial indicators and taking into account expert knowledge.

Sovereign states and local authorities
In addition, Aareal Bank Group employs internal rating methods for sovereign borrowers and regional governments, local and other public-sector entities. In this context, rating grades are assigned using clearly-defined risk factors, such as fiscal flexibility or the level of debt. The expert knowledge of our rating analysts is also taken into account for the rating.

In general, the risk classification procedures employed by the Bank are dynamic methods which are permanently adapted to changing risk structures and market conditions.

Trading activities

Functional separation

We have implemented a consistent functional separation between Sales units and Credit Management for the conclusion, settlement and monitoring of trading transactions, covering the entire processing chain.

On the Sales side, the processing chain comprises the Treasury division, whilst Credit Management tasks are carried out by the independent Operations and Risk Controlling divisions. Beyond this, Finance & Controlling and Audit are responsible for tasks not directly related to processes.

We have laid down organisational guidelines providing for binding definitions of roles and responsibilities along the processing chain; with clearly defined change processes.

The detailed assignment of responsibilities is outlined below.

Treasury is responsible for risk management and trading activities as defined by the Minimum Requirements for Risk Management ("MaRisk"). Treasury is also responsible for asset / liability management, and for managing the Bank's market and liquidity risk exposures. In addition, we have established a Transaction Committee, to develop strategies for the Bank's asset / liability management and proposals for their implementation. The Committee, which comprises the Management Board member responsible for Treasury, the Head of Treasury, and other members appointed by the Management Board, meets on a weekly basis.

Operations is responsible for controlling trading activities, confirming trades to counterparties, and for trade settlement. The division is also responsible for verifying that trades entered into are in line with prevailing market conditions, as well as for the legal assessment of non-standard agreements, and of new standard / master agreements.

To assess counterparty credit risk in the trading business, Operations prepares a rating for all counterparties and issuers on a regular or event-driven basis. The rating is a key indicator used to determine the limit for the relevant counterparty or issuer.

The RiskExCo is responsible for voting on all limit applications. The Committee has delegated corresponding authority to the Heads of Risk Controlling, Operations, and Project & Portfolio Management, who are responsible for conducting annual limit reviews, as well as for reducing (or revoking) counterparty or issuer limits whenever required.

The tasks of the Risk Controlling division comprise identifying, quantifying and monitoring market price, liquidity and counterparty credit risk exposure from trading activities, and the timely and independent risk reporting to senior management.

Process requirements

Processes are geared towards ensuring end-to-end risk management, from conclusion of the trade right through to monitoring portfolio risk. The monitoring and reporting function comprises deploying adequate risk measurement systems, deriving limit systems, and ensuring the transparency of Aareal Bank Group's overall risk exposure from trading activities, in terms of scope and structure.

Change processes (as defined in section AT 8 of the MaRisk) are consistently measured via Group-wide framework guidelines, with the RiskExCo involved in all cases. Moreover, processes and systems are designed in a way that allows to incorporate new products into the risk monitoring system swiftly and adequately, in order to ensure the flexibility of the Sales units in their business activities.

A standardised process exists for the intensified handling of counterparties and issuers, and for dealing with problems. This process comprises identifying early warning indicators, applying them for the purposes of risk analysis, and determining further action to be taken. In the event of counterparty or issuer default, the RiskExCo will be involved in devising an action plan, in cooperation with the Bank's divisions involved.

Escalation and decision-making processes have been set out to deal with limit breaches.

Loan loss risks

Definition

Aareal Bank defines credit risk – or counterparty credit risk – as the risk of losses being incurred due to (i) a business partner defaulting on contractual obligations; (ii) collateral being impaired; or (iii) a risk arising upon realisation of collateral. Both credit business and trading activities may be subject to counterparty credit risk. Counterparty credit risk exposure from trading activities may refer to risk exposure vis-à-vis counterparties or issuers. Country risk is also defined as a form of counterparty credit risk.

Credit risk strategy

Based on the Bank's overall business strategy, Aareal Bank's credit risk strategy sets out all material aspects of the Group's credit risk management and policies. The credit risk strategy serves as a strategic guideline for dealing with each respective category of risk within Aareal Bank Group; it also provides a binding, overarching framework applicable to all divisions.

The credit risk strategy will be reviewed, at least once a year, as to its suitability regarding the Bank's risk-bearing capacity and its business environment; amendments will be made as necessary. The associated process is instigated by senior management, and implemented by Risk Controlling, which submits a proposal, which has been agreed upon with all divisions, to senior management. The Supervisory Board then duly acknowledges and approves the credit risk strategy adopted.

Designed in principle for a medium-term horizon, the credit risk strategy is adapted when necessary to reflect material changes in the Group's credit risk and business policies, or in the Group's business environment (as in the case of the financial markets crisis).

Risk measurement and monitoring

Aareal Bank's structural organisation and business processes are consistently geared towards effective and efficient risk management. Regulatory requirements are fully taken into account for the organisation of operations and workflows in the credit and trading businesses.

Processes in the credit and trading businesses are designed to consistently respect the clear functional division of Sales units ("Markt") and Credit Management ("Marktfolge"), up to and including senior management level. The independent Risk

Controlling division is responsible for identifying, quantifying and monitoring all material risks at portfolio level, and for maintaining a targeted risk reporting system.

Aareal Bank employs different risk classification procedures tailored to the requirements of the respective type of business for the initial, regular, or event-driven assessment of counterparty credit risk. Forward-looking as well as macro-economic information is taken into consideration for risk classification procedures, and in the valuation of collateral. The respective procedures and parameters are subject to permanent review and adjustment. Responsibility for development, quality assurance, and monitoring implementation of procedures, is outside the Sales units.

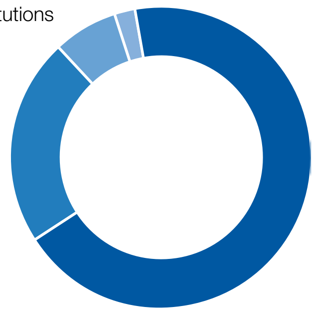
Methods used to measure, control and monitor concentration and diversification effects on a portfolio level include two different credit risk models. Based on these models, the Bank's decision-makers are regularly informed of the performance and risk content of property financing exposures, and of business with financial institutions. The models in question allow the Bank to include in particular, rating changes and correlation effects in the assessment of the risk concentrations.

Within the process-oriented monitoring of individual exposures, the Bank uses various tools to monitor exposures on an ongoing basis: besides the tools already described, this includes rating reviews, the monitoring of payment arrears, and the regular, individual analysis of the largest exposures. The intensity of loan coverage is oriented upon the credit risk exposure. Intensified handling triggers recognition of loss allowance, in the amount of lifetime expected credit loss for the financial instrument concerned (Stage 2).

The tables on the following pages provide a breakdown of gross carrying amounts of on-balance sheet as well as off-balance sheet credit business, money-market business, and capital markets business, by rating class and loss allowance stages, in line with credit risk management at

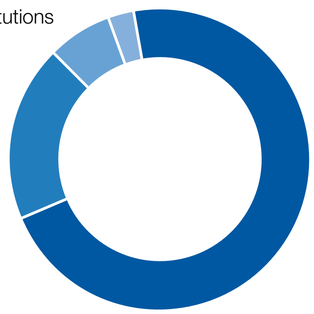
Breakdown of on-balance sheet and off-balance sheet business

by rating procedure, € bn 31 Dec 2018



Breakdown of on-balance sheet and off-balance sheet business [1)]

by rating procedure, € bn 1 Jan 2018



1) Excluding hedge adjustment
* Including the private client business of former WestImmo

Group level. Figures are based on Aareal Bank Group's internal default risk rating classes. The default definition follows the definition pursuant to Article 178 of the CRR, which is decisive for management purposes. To facilitate comparison, figures as at 1 January 2018 including adjustments pursuant to IFRS 9 (excluding hedge adjustments) were shown as previous year's values.

On-balance sheet commercial property finance business with mandatory rating

31 December 2018

€ mn	Stage 1	Stage 2	Stage 3	fvpl[1]	Total	1 Jan 2018
Class 1						
Class 2	117				**117**	88
Class 3	255				**255**	399
Class 4	1,486				**1,486**	1,345
Class 5	3,566			94	**3,660**	3,025
Class 6	3,966	21		256	**4,243**	3,717
Class 7	3,420				**3,420**	3,242
Class 8	5,166	112		181	**5,459**	5,620
Class 9	3,463	42		116	**3,621**	3,335
Class 10	1,510	28			**1,538**	1,368
Class 11	285	91		39	**415**	480
Class 12	531	62			**593**	518
Class 13		66			**66**	261
Class 14						3
Class 15				3	**3**	
Defaulted			1,564	22	**1,586**	1,614
Total	**23,765**	**422**	**1,564**	**711**	**26,462**	**25,015**

[1] fvpl = at fair value through profit and loss (in accordance with IFRSs)

Off-balance sheet commercial property finance business with mandatory rating

31 December 2018

€ mn	Stage 1	Stage 2	Stage 3	fvpl[1]	Total	1 Jan 2018
Classes 1-2						
Class 3						57
Class 4	39				**39**	25
Class 5	32			6	**38**	33
Class 6	190			25	**215**	365
Class 7	175				**175**	242
Class 8	312	5			**317**	254
Class 9	120				**120**	223
Class 10	75				**75**	106
Class 11	5				**5**	17
Class 12	29				**29**	12
Classes 13-15						
Defaulted			78		**78**	108
Total	**977**	**5**	**78**	**31**	**1,091**	**1,442**

[1] fvpl = at fair value through profit and loss (in accordance with IFRSs)

On-balance sheet loans and advances to financial institutions

31 December 2018

€ mn	Stage 1	Stage 2	Stage 3	fvpl[1]	Total	1 Jan 2018
Class 1	1,242				**1,242**	
Class 2	32				**32**	1,398
Class 3	15				**15**	25
Class 4	85				**85**	55
Class 5	514				**514**	5
Class 6	100				**100**	43
Class 7	387			35	**422**	466
Class 8	284				**284**	516
Class 9	16			43	**59**	30
Class 10	25			26	**51**	51
Classes 11-18						
Defaulted						
Total	**2,700**			**104**	**2,804**	**2,589**

[1] fvpl = at fair value through profit and loss (in accordance with IFRSs)

On-balance sheet loans and advances to sovereign states and local authorities

31 December 2018

€ mn	Stage 1	Stage 2	Stage 3	fvpl[1]	Total	1 Jan 2018
Class 1	2,621				**2,621**	1,601
Class 2	2,666			76	**2,742**	1,579
Class 3	797			70	**867**	1,784
Class 4	145			32	**177**	348
Class 5	239			62	**301**	57
Class 6	436				**436**	207
Class 7	163			105	**268**	119
Class 8						104
Class 9	711	805		89	**1,605**	1,186
Classes 10-20						
Defaulted						
Total	**7,778**	**805**		**434**	**9,017**	**6,985**

[1] fvpl = at fair value through profit and loss (in accordance with IFRSs)

Monthly reporting covers the material aspects of credit risk; it is supplemented by detailed information – which also fully covers specific credit portfolio developments (broken down by country, property and product type, risk classes, and collateral categories, for example), in line with regulatory requirements – at least on a quarterly basis. Risk concentrations are being taken into account in particular.

Trading activities are restricted to counterparties for whom the requisite limits are in place. All trades are immediately taken into account for the purposes of borrower-related limits. Compliance with limits is monitored in real time by Risk Controlling. Persons holding position responsibility are informed about relevant limits and their current usage, regularly and without delay.

In principle, Aareal Bank pursues a "buy and manage" strategy in managing its credit portfolio – with the primary objective of holding the majority of loans extended on its balance sheet until maturity; at the same time, targeted exit measures are deployed for actively managing the portfolio and the risks involved.

In summary, during the period under review, the existing set of tools and methods continued to enable the Bank to adopt suitable risk management or risk mitigation measures, where required, at an early stage.

Credit risk mitigation

The Bank accepts various types of collateral to reduce default risk exposure. This includes impersonal collateral, such as liens on immobile (property) and mobile assets; liens on receivables, such as rents; and third-party undertakings, such as guarantees.

As an international property finance house, Aareal Bank focuses on property when collateralising loans and advances. As a rule, loans are granted and the security interest perfected in accordance with the jurisdiction in which the respective property is located.

Mortgage lending values or fair values are set or determined in accordance with the responsibilities for decision-making on lending, and form an integral part of the lending decision. The values to be determined by the Bank are generally pegged on the valuation prepared by a valuer; any discrepancies must be substantiated in writing. In any case, the market and mortgage lending values determined by the Bank must not exceed the values assessed by independent internal or external valuers.

To mitigate credit risk, the Bank also accepts collateralisation through a pledge of shareholdings in property companies or special purpose entities not listed on a stock exchange. The Bank has set out detailed provisions governing the valuation of such collateral.

The Bank also accepts guarantees or indemnities as well as financial collateral (such as securities or payment claims) as standard forms of collateral. The collateral value of the indemnity or guarantee is determined by the guarantor's credit quality. For this purpose, the Bank differentiates between banks, public-sector banks, and other guarantors. The value of financial collateral is determined according to the type of collateral. Haircuts are generally applied when determining the value of guarantees/indemnities and financial collateral.

The credit processes provide for the regular review of collateral value. The risk classification is adjusted in the event of material changes in collateral value, and other measures taken as deemed appropriate. An extraordinary review of collateral is carried out where the Bank becomes aware of information indicating a negative change in collateral value. Moreover, the Bank ensures that disbursement is only made after the agreed conditions for payment have been met.

Collateral is recorded in the Bank's central credit system, including all material details.

Credit risk mitigation for trading activities

To reduce counterparty risk in Aareal Bank's trading business, the master agreements for financial derivatives and master agreements for securities repurchase transactions (repos) used by the Bank[1] provide for various credit risk mitigation techniques, via mutual netting framework agreements.

The master agreements for financial derivatives used by the Bank contain netting framework agreements at a single transaction level (so-called "payment netting"), and arrangements for the termination of individual transactions under a master agreement (so-called "close-out netting").

In general, all master agreements are based on the principle of a common agreement. This means that, in the case of a termination, the individual claims are netted, and that only such net amount can and may be claimed with regard to the defaulted counterparty. This claim must not be affected by any insolvency, i. e. it must be legally valid and enforceable. This, in turn, means that the jurisdictions concerned must recognise the concept of a common agreement which protects the net amount of the claim from imminent access by the insolvency administrator.

Above all, the close-out netting is subject to (international) legal risks. The Bank reviews these legal risks by reference to legal opinions regarding the validity and enforceability of mutual netting framework agreements in the case of a counterparty's insolvency. These legal opinions are evaluated based on various criteria such as product type, jurisdiction of the registered office and branch office of the counterparty, individual contract supplements and other criteria, and using a database developed for this purpose. In doing so, the Bank decides for each individual transaction whether or not netting is possible. The Bank uses eligible bilateral netting framework agreements within the meaning of the CRR for all transactions with financial institutions; in many cases there are additional collateral agreements which further reduce the relevant credit risk.

The Bank enters into repo transactions both on a bilateral basis and via Eurex Clearing AG as a central counterparty. For repo transactions, depending on the counterparty, payment or delivery netting is agreed upon. Master agreements for repo transactions generally contain provisions on close-out netting. The Bank does not use the option permitted by regulatory authorities to reduce capital requirements for repo transactions.

Furthermore, counterparty risk is reduced through derivatives settlement via central counterparties (CCPs): Aareal Bank uses Eurex Clearing AG and LCH.Clearnet Limited.

The Bank uses an internal rating system to assess the credit quality of counterparties. Operations is responsible for the daily valuation of the Bank's trades, including collateral accepted or pledged, and using validated valuation procedures.

Cash collateral only is accepted for derivatives transactions; such collateral is pledged in regular intervals, as set out in the individual agreements. Repo transactions are usually collateralised through securities, pledged on a daily basis.

Some collateral agreements provide for higher collateral levels in the event of material downgrade to a contracting party's rating.

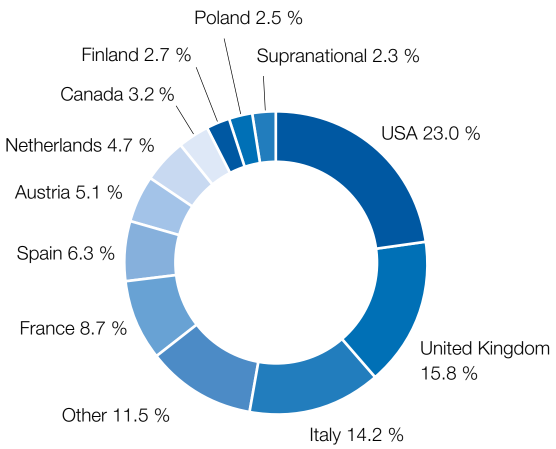
Country risks

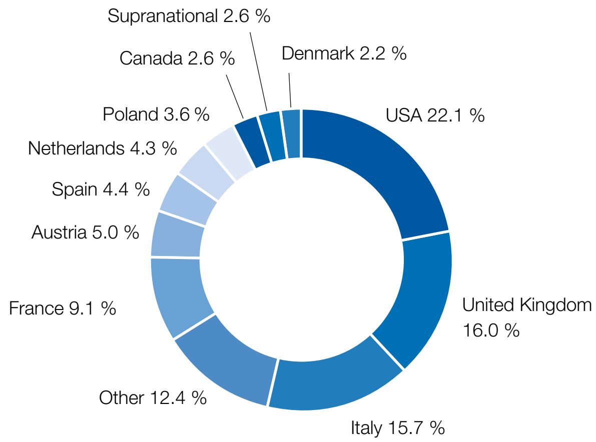
Our comprehensive approach to risk management also includes measuring and monitoring country risk exposure. When defining country risk, in addition to the risk of sovereign default or default of state entities, Aareal Bank also considers the risk that a counterparty could become unable to meet its payment obligations as a result of government action, despite being willing and able to pay, due to restrictions being imposed on making payments to creditors (transfer risk). Country risk exposure is managed using a cross-divisional process. The

[1] Any comments below referring to the German Master Agreement on Financial Derivatives (Deutscher Rahmenvertrag für Finanztermingeschäfte – "DRV") also pertain to the master agreement issued by the International Swaps and Derivatives Association Inc. (ISDA) (the "ISDA Master Agreement"). Both agreements are standardised agreements recommended by leading associations – among others, by the Association of German Banks (Bundesverband deutscher Banken – "BdB").

Breakdown of country exposure in the international business

% 31 Dec 2018 | 31 Dec 2017





respective country limits are determined on the basis of a country risk assessment by the Bank's senior management. The Risk Controlling division is responsible for the continuous monitoring of country limits and limit utilisation, and for periodical reporting.

The diagram below illustrates the risk exposure by country (comprising receivables and off-balance sheet obligations) in the Bank's international business, at year-end. In the property financing business, country exposures are allocated by location of the property used as collateral. For exposures not collateralised by property, the allocation is based on the borrower's country of domicile. This reflects the exposure of the property finance business, as well as the activities of Treasury.

Interest rate risk in the banking book

Definition

Interest rate risk in the banking book (IRRBB) is defined as the risk exposure of instruments held in the banking book which are sensitive to changes in interest rates, caused by yield curve shifts.

Specifically, for Aareal Bank this includes:

- risks arising from maturity transformation in the event of yield curve shifts (so-called gap risk), which, in turn, are broken down into:
  - risks from cash flows which are sensitive to interest rates, relative to the general yield curve (interest rate risk or repricing risk);
  - risks arising from the valuation of future cash flows, relative to the general yield curve (yield curve risk);
- risks from cash flows which are sensitive to interest rates, in terms of spreads to the general yield curve (basis risk);
- risks from explicit and implied options (option risk);
- risks arising from changing valuation of pension liabilities (pension risk);
- risks from fluctuations in the value of fund assets (fund risk); and
- risks from changes in Aareal Bank's specific funding spreads (funding risk).

Risk measurement and monitoring

Risk Controlling informs the members of the Management Board responsible for Treasury and risk monitoring about the risk position and the exposure to interest rate risk in the banking book on a daily basis.

The VaR concept has been broadly accepted as the predominant method for measuring economic interest rate risk in the banking book. VaR quantifies risk as the maximum loss that will occur within a certain period of time, and given a defined probability.

A variance-covariance approach (delta-normal method) is used throughout the Group to determine the VaR indicator. Determined on a daily basis for the Group and all its operating units, the VaR figure takes into account the correlation between individual risk types. Statistical parameters used in the VaR model are calculated directly from a 250-day historical data pool maintained within the Bank. The loss potential is determined applying a 95 % confidence interval. As part of the implementation of the new ICAAP requirements imposed by the ECB, this will increase to 99.9 % from 2019 onwards.

By their very nature, VaR calculations are based on numerous assumptions regarding the future development of the business, and the related cash flows. Key assumptions used include current account balances and overnight deposits which are factored into calculations for a period of up to five years, using the average residual amount of deposits observed in the past. Loans are taken into account using their fixed-interest period (for fixed-rate exposures), or using their expected maturity (variable-rate exposures). Aareal Bank Group's consolidated equity is not taken into account as a risk-mitigating item. This tends to overstate VaR, demonstrating the conservative approach adopted in our risk measurement processes.

Interest rate sensitivity

An additional instrument used to quantify interest rate risk exposure is the calculation of interest rate sensitivity, expressed by the so-called "delta" parameter. The first step to determine this parameter requires calculating the present values of all asset and equity/liability items on the statement of financial position. In a second step, the interest rates of yield curves used for this calculation are subjected to a one basis point parallel shift up (a method known as the "key rate method"). Delta is the present value of the profit or loss resulting from this yield curve change.

Present-value impact of an interest rate shock in accordance with section 25a of the KWG

The following table provides a breakdown of present value changes by currency as at the reporting date, based on interest rate shock scenarios prescribed by banking regulators for external reporting purposes. For this purpose, the yield curve is subjected to a parallel 200 basis point downshift, down to the zero per cent line at the maximum, unless the relevant interest rate was already negative to start with. As in the previous years, the ratio

31 December 2018

	Present value change	
	-200 bp	+200 bp
€ mn		
EUR	-140	204
GBP	-12	-12
USD	-10	-10
Other	-12	-12
Total	**-174**	**170**
Percentage ratio to regulatory capital	**5.3**	**5.2**

of the aggregate of all foreign-currency amounts to Aareal Bank Group's regulatory capital is clearly below the prescribed threshold of 20 %.

Interest rate gap analysis

Further, the gap analysis per currency provides information on all of the Bank's positions in respect of which the interest rate has been fixed. In addition to disclosing the net gap positions in the respective maturity bucket, this data allows for specific analyses concerning the risks and returns from the current portfolio.

Credit spread and migration risks in the banking book

Definition

We define credit spread and migration risks in the banking book (CSRBB) as any type of spread risk exposure of instruments held in the banking book which are sensitive to changes in interest rates, where the risk cannot be assigned to IRRBB nor to counterparty credit risk.

Specifically, for Aareal Bank this includes:

- valuation risks that are dependent upon spreads (credit spread risk);
- specific price risks from the bond portfolio, wherein the bonds are mainly sovereign bonds (sovereign risk);
- exposure of loans to rating migration (migration risk); and
- replacement risk (CVA buffer).

Risk measurement and monitoring

Risk Controlling informs the members of the Management Board responsible for Treasury and risk monitoring about the risk position and the exposure to credit spread risk in the banking book on a daily basis.

Risk measurement differentiates between underlying exposures and sub-risks. Accordingly, credit spread risks from securities and sovereign risk are calculated using VaR concepts, in line with the methods described in connection with interest rate risk in the banking book. In this context, VaR quantifies risk as the loss that will not be exceeded within a certain period of time, and given a defined probability.

A variance-covariance approach (delta-normal method) is used throughout the Group to determine the VaR indicator. Determined on a daily basis for the Group and all its operating units, the VaR figure takes into account the correlation between individual risk types for this risk category. Statistical parameters used in the VaR model are calculated directly from a 250-day historical data pool maintained within the Bank. The loss potential is determined applying a 95 % confidence interval. As part of the implementation of the new ICAAP requirements imposed by the ECB, this will increase to 99.9 % from 2019 onwards.

Loan migration risks are determined by reference to stressed migration matrices: risk is defined as the change in expected loss over the lifetime of the loan, based on a 95 % confidence interval. The CVA buffer amount is taken from the amount determined in accordance with CRR requirements.

Other market risks

Definition

Other market risks are broadly defined as the threat of losses due to changes in market parameters.

Residual market risks which are not assigned to IRRBB or CSRBB are summarised under "market risk". Specifically, for Aareal Bank this includes:

- risks resulting from fluctuations of spot foreign exchange (FX) rates;
- risks resulting from fluctuations of forward foreign exchange rates (FX risk); and

- risks from the regulatory review of the trading book (Financial Risk in the Trading Book – FRTB).

Being authorised to maintain a trading book, Aareal Bank AG is the Group entity that is in a position to assign transactions to the trading portfolio as defined by the CRR. Given that no such trades have been concluded during the year under review, trading book risks were not relevant during the period under review.

Commodities are irrelevant for the Bank's business. Hence, the market risk exposures are currently related to the relevant risk parameters of spot and forward foreign exchange rates only. These exchange rate risks are largely eliminated through hedges.

Risk measurement and monitoring

Risk Controlling informs the members of the Management Board responsible for Treasury and risk monitoring about the risk position and exposure to other market risks on a daily basis.

The VaR concept has been broadly accepted as the predominant method for measuring economic market risk. VaR quantifies risk as the maximum loss that will occur within a certain period of time, and given a defined probability.

A variance-covariance approach (delta-normal method) is used throughout the Group to determine the VaR indicator. Determined on a daily basis for the Group and all its operating units, the VaR figure takes into account the correlation between individual risk types. Statistical parameters used in the VaR model are calculated directly from a 250-day historical data pool maintained within the Bank. The loss potential is determined applying a 95 % confidence interval. As part of the implementation of the new ICAAP requirements imposed by the ECB, this will increase to 99.9 % from 2019 onwards.

Furthermore, in addition to the risk category limit, a separate trading limit has been determined for Aareal Bank AG, as an institution authorised to maintain a trading book.

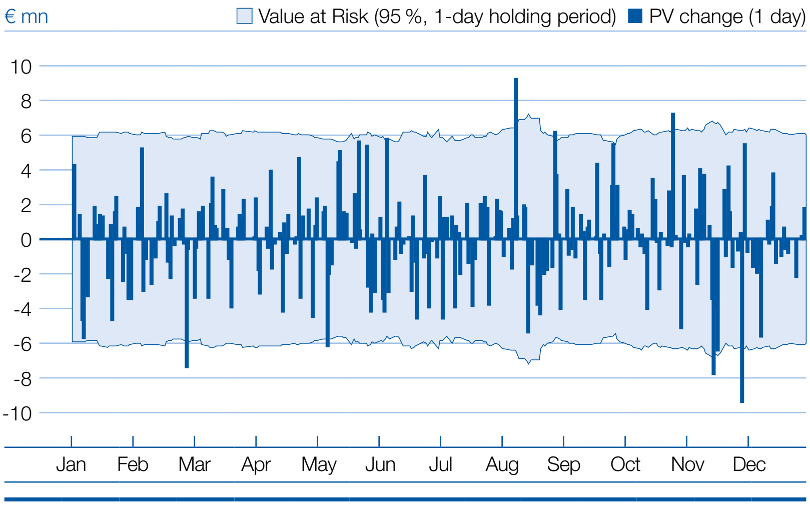
Backtesting

The quality of forecasts made using statistical models is checked through a monthly backtesting process. The quality of the statistical procedure used to measure risk is checked using a binomial test, whereby daily profits and losses from market fluctuations are compared with the upper projected loss limit (VaR) forecast on the previous day (known as "clean backtesting"). In line with the selected confidence level of 95 %, only a small number of events are expected to break out of the VaR projection (≤ 17 for a 250-day period).

The backtesting exercise shown below comprises all risk positions subject to daily changes from the "Other market risks" category.

Four negative outliers at Group level occurred during the last 250 trading days, affirming the high forecasting quality of the VaR model we use.

Present values and 1-day VaR during the course of 2018



Operational risks

Definition

The Bank defines operational risk as the threat of losses caused by inappropriate internal procedures, human resources and systems (or their failure), or through external events. This definition also includes legal risks. To the extent that they are caused by operational risks, model and reputational risks are also taken into consideration within this type of risk. Systemic risks (or their impact on operational risks) are not affected by this.

Risk measurement and monitoring

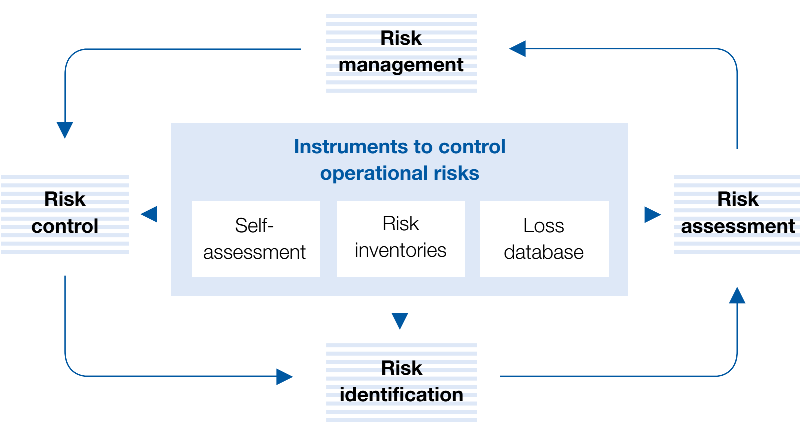
It is the objective of the policy pursued by Aareal Bank to achieve a risk-minimising or loss-limiting effect at an early stage by employing a pro-active approach.

The Bank currently uses the following risk control tools to manage operational risks:

- Self-assessments: analysis thereof can provide management with indicators of any potential risks within the organisational structure.
- Risk inventories that include a periodic systematic identification and compilation of all relevant risks.
- A loss database, in which relevant damages incurred are reported, and in which they can be monitored until they are officially closed.

By means of this control toolkit, decentralised data capture as well as centralised and timely compilation of all material operational risks across the Group are ensured.

Management of operational risks



The three tools described above are used to prepare the regular risk reporting to the Bank's senior management. The responsibility for implementing operative risk-reducing measures rests with those responsible for the Bank's risk management. The utilisation of freely available funds for operational risks – as part of the Bank's risk-bearing capacity – are determined using the regulatory standardised approach.

In addition to the reports prepared from the tools stated above, suitable and plausible stress tests are conducted every quarter. These are hypothetical as well as historical scenarios and sensitivity analyses on the risk inventories. The results of the stress tests are reported regularly to the Management Board and serve as an indicator for potential developments within the operational risks that could jeopardise the continued existence of the Group.

Aareal Bank's legal department deals with any litigation the Bank is involved in, as well as with any legal issues of fundamental importance – where necessary, using the support of external lawyers.

Legal also compiles all information concerning any legal disputes involving Aareal Bank Group, whether in or out of court. To this extent, the involvement of the legal department is based on corresponding Group-wide guidelines. The Bank's decentralised operating legal entities, as well as the legal departments of subsidiaries submit quarterly reports on legal risks identified to Aareal Bank's legal department; where particular risks have occurred, such reports are submitted on an event-driven basis. When required, Aareal Bank's legal department discusses and coordinates any concrete measures with the reporting unit.

The legal department reports to the Management Board, (at least) on a quarterly basis, as well as on an event-driven basis. Moreover, information about legal risks is included in operational risk reporting.

Analyses conducted using the instruments employed have shown that the Bank is not exposed to disproportionate operational risks; nor did they indicate any material risk concentration. Even though loss cases were recorded in the loss database during the financial year under review, the aggregate impact of such losses amounted to less than 10 % of the regulatory capital to be maintained for operational risks.

Further to these tools, the Bank reviews relevant individual scenarios, and implements any measures required, on the basis of external data. Taken together, these tools for managing operational risks result in an integrated control circuit which leads to risk identification, evaluation, and management – through to risk control.

Tools to control operational risk are supplemented by a system to manage and monitor outsourced activities and processes (outsourcing), whereby the relevant organisational units regularly assess the performance of outsourcing providers, using defined criteria. The results of this process, and actions taken, are communicated to the Bank's senior management within the scope of operational risk reporting, thus allowing for risk-mitigating steps to be taken where needed.

Investment risks

Definition

Aareal Bank defines investment risk as the threat of unexpected losses incurred due to an impairment of the investment's carrying amount, or a default of loans extended to investees. The concept of investment risk also encompasses additional risks arising from contingencies vis-à-vis the relevant Group entities.

Risk measurement and monitoring

All relevant Group entities are subject to regular audits, including a review and assessment of their risk situation within the framework of risk measurement and monitoring. Due to the special character of some exposures (e.g. marketing risks), special methods and procedures are employed to deal with investment risk. The Bank uses an internal valuation method to quantify investment risk, and to include it in the calculations of the Bank's ability to carry and sustain risk, and for the purpose of limitation. The limit defined for investment risk was always complied with during the financial year under review.

The existing procedures used to measure and monitor risk exposure are supplemented by subjecting the equity portfolio to regular stress testing.

Strategy Development, as well as Finance & Controlling and Risk Controlling, are responsible for measuring and monitoring investment risk exposure.

Risk Controlling is responsible for submitting a quarterly equity investment risk report to the Bank's Management Board.

Property risks

Definition

We define property risk as the threat of unexpected losses arising from changes in the value of property held by the Bank, or by fully-consolidated subsidiaries.

Due to the special character of property risk (involving marketing risks, for example), special methods and procedures are employed to deal with investment risk. All relevant property holdings are subject to regular audits, including a review and assessment of their risk situation. There were no significant changes in property risk during the period under review.

Risk measurement and monitoring

In order to measure and monitor risks, property yields are analysed for different regions, and over the time horizons available: on this basis, potential yield increases over a one-year horizon are determined applying a 95 % confidence interval. As part of the implementation of the new ICAAP requirements imposed by the ECB, this confidence interval will increase to 99.9 % from 2019 onwards. The loss in a property's value results from the difference between the current market value and the property value adjusted for the yield increase.

Business and strategic risks

Definition

Business and strategic risk is defined as the risk of unexpected losses, usually brought about by a decline in profits due to income falling short of expectations, whereby the shortfall cannot be compensated for by cost reductions. Strategic risk may emerge from changes in the competitive or regulatory environment, or due to unsuitable positioning in the macroeconomic environment.

Risk measurement and monitoring

In this context, we distinguish between investment risk and allocation risk, whereby allocation risk is already covered by various planning scenarios, and is thus incorporated in aggregate risk cover.

Investment risk is measured across segments: it is quantified assuming that additional upfront investment is required to establish an investment opportunity which was previously unavailable. Such upfront investment is assumed to represent potential risk.

Liquidity risks

Definition

Liquidity risk in the narrower sense is defined as the risk that current or future payment obligations cannot be met in full or on time. Aareal Bank Group's liquidity risk management system is designed to ensure that the Bank has sufficient cash and cash equivalents to honour its payment obligations at any future point in time. The risk management and monitoring processes have been designed to cover refinancing and market liquidity risks in addition to liquidity risk in the narrower sense.

Risk measurement and monitoring

Treasury is responsible for managing liquidity risks, whilst Risk Controlling ensures the continuous monitoring, including a daily liquidity report submitted to Treasury, and a contribution to the monthly risk report to the entire Management Board. The following tools are used for this purpose:

Cash flow forecast

We have developed a cash flow forecast, tracking cash flows from all balance sheet items and derivatives, on a daily basis, over a ten-year period. This liquidity risk information helps to assess the Bank's short-term liquidity position, broken down by currency or product. Strategic liquidity is taken into account using this ten-year cash flow profile. We use statistical modelling to incorporate the expected cash flow profile of products without a fixed contractual lifetime.

Liquidity run-off profile

The appropriateness of the Bank's liquidity is assessed using a liquidity run-off profile: the aggregate of all potential cash inflows and outflows over a three-month period is compared to the liquidity stock. This liquidity stock comprises all assets that can be liquidated at very short notice. The difference of both figures (in absolute terms) indicates excess liquidity, once all claims assumed in the run-off profile have been fulfilled through the liquidity stock. There were no liquidity shortages throughout the period under review.

Stress testing

Moreover, we employ stress tests and scenario analyses to assess the impact of sudden stress events onto the Bank's liquidity situation. The various standardised scenarios used are evaluated on the basis of the liquidity run-off profile.

From our point of view, the most significant scenario is the institution-specific "idiosyncratic stress" scenario, which simulates a withdrawal of funds deposited by public-sector entities and banks, as well as a 30 % reduction in current account balances. Even in this stress scenario, liquidity is sufficient to cover the expected liquidity needs under stress conditions.

Time to illiquidity

To safeguard adequate liquidity beyond the three-month horizon covered by the liquidity run-off profile, we use the concept of time to illiquidity as a parameter. For this purpose, a liquidity run-off profile was developed which compares liquidity requirements occurring with the liquidity stock, for a one-year period. Time to illiquidity (”TtI”) denotes the remaining period (expressed in days) during which Aareal Bank Group can be regarded as sufficiently liquid, even under adverse conditions. In other words, liquidity requirements (including security add-on for adverse future events) do not exceed the liquidity stock.

The calculations are based on contractual cash flows and the short-term risk assessment methodology (liquidity run-off profile), as well as the portfolio development within the current plan scenario.

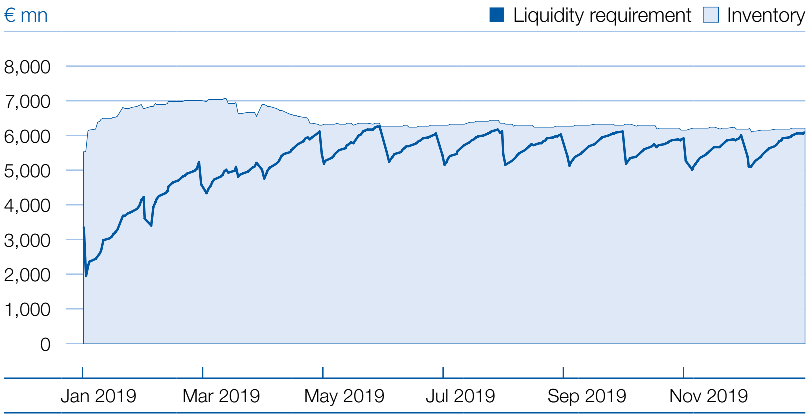
The chart above shows the projected development of the liquidity stock, together with aggregate liquidity requirements (incorporating planned portfolio developments, and including security add-ons for adverse future events) until the end of 2019. The chart demonstrates that the liquidity stock will always exceed liquidity requirements, even under adverse conditions.

Further details are provided in the comments on the Bank's liquidity in the section on the ”Financial position”.

Funding profile

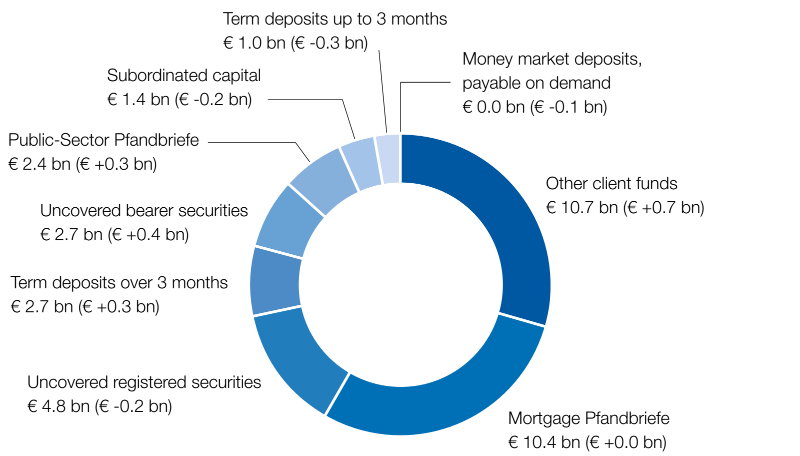
Diversifying the Bank's refinancing profile by type of investor, and by product, represents a further key aspect of our approach to liquidity risk management. Core sources of funding such as customer deposits and funds invested by institutional clients – alongside covered and uncovered bond issues – constitute the foundation of our liability profile.

Liquidity development



Refinancing portfolio diversification by product

as at 31 Dec 2018 versus 31 Dec 2017 Total volume (nominal): € 36.1 bn



Besides the pure measurement of risk indicators, we also monitor concentrations of liquid assets and of funding sources, determining the percentage share of the ten largest counterparties and/or positions, relative to the total portfolio. A limit is set for each indicator in order to restrict the dependency upon individual positions or counterparties.

Concentration limits

Besides the pure measurement of risk indicators, we also monitor concentrations of liquid assets and of funding sources, determining the percentage share of the ten largest counterparties and/or positions, relative to the total portfolio. A limit is set for each indicator in order to restrict the dependency upon individual positions or counterparties.

LCR forecast

We have developed the LCR forecast as a measurement tool designed to ensure that we maintain compliance with the regulatory Liquidity Coverage Ratio. A preview of the Liquidity Coverage Ratio is calculated over a horizon of up to three years, determining the ratio of highly liquid assets to cumulative net cash outflows for various end-of-month dates – thus identifying any potential liquidity shortfalls or reserves.

Taking the prevailing regulatory reporting as a basis for the LCR forecast, LCR is projected for future dates, incorporating short-term business activities as well as portfolio developments in the planned scenario.

NSFR forecast

The NSFR forecast, which is a projection of the Net Stable Funding Ratio over a period of up to three years, represents another important component of our liquidity management. This measurement tool allows us to forecast the regulatory Net Stable Funding Ratio for future dates, thus identifying any potential liquidity shortfalls or reserves in terms of the NSFR at an early stage.

Taking the prevailing regulatory reporting as a basis for the NSFR forecast, NSFR is projected for future dates, incorporating portfolio developments in the planned scenario.

Accounting-related Internal Control and Risk Management System

Tasks of the accounting-related Internal Control System (ICS) and the Risk Management System (RMS)

The accounting-related Internal Control and Risk Management System includes principles, procedures and measures to ensure the effectiveness and the efficiency of internal and external accounting, in accordance with applicable legal provisions. The tasks of the accounting-related Internal Control System mainly include ensuring proper conduct of business activities, guaranteeing proper internal and external accounting, as well as ensuring compliance with relevant statutory and legal requirements applicable to the Company.

The objective of the accounting-related Risk Management System is to identify, assess and limit risks which may impede the compliance of the financial statements with applicable rules and regulations. As with any other Internal Control System, the accounting-related ICS and RMS may only provide reasonable – but not absolute – assurance with regard to achieving this objective, regardless of how much care is used to design and operate this system.

Organisation of the accounting-related ICS and RMS

The Internal Control System of Aareal Bank takes into account the principles established by the Minimum Requirements for Risk Management (MaRisk) related to company-specific design of the ICS. The design of this Internal Control System comprises organisational and technical measures to control and monitor the Company's activities, covering all entities of Aareal Bank Group. The Management Board of Aareal Bank AG is responsible for designing, implementing, applying, developing and reviewing an appropriate accounting-related Internal Control System. The Management Board makes decisions as regards the scope and the design of specific requirements; it has defined the responsibilities for the individual process steps in connection with accounting by means of organisational guidelines, and has delegated these responsibilities to individual organisational units.

Aareal Bank prepares its consolidated financial statements in accordance with International Financial Reporting Standards (IFRSs). The Finance & Controlling division controls Group accounting processes and is responsible for ensuring compliance of Group accounting with legal requirements, as well as with any further internal and external provisions. Based on the IFRSs, the Finance & Controlling division establishes accounting-related requirements that have to be applied consistently throughout the Group. These requirements are set out in the IFRS Group Accounting Manual.

Aareal Bank Group entities prepare an IFRS package as at the relevant balance sheet date. This includes financial statements prepared under IFRSs and in accordance with the IFRS Group Accounting Manual, as well as the Notes and consolidation information (intercompany balances). All packages are recorded by the Finance & Controlling division in consolidation software and aggregated for the purpose of preparing the consolidated financial statements. The number of employees within Aareal Bank's Finance & Controlling division is adequate, as are their qualifications. Furthermore, they possess the necessary knowledge and experience relevant for their functions.

The Supervisory Board is responsible for monitoring the Management Board. It approves the single-entity financial statements of Aareal Bank AG as well as the consolidated financial statements and group management report. Measures taken by the Supervisory Board to ensure an efficient performance of its control functions include the establishment of an Audit Committee, which is primarily responsible for financial reporting issues and monitors the effectiveness of Aareal Bank's Internal Control System. The committee analyses and assesses the financial statements submitted to it, the internal risk reports, and the annual Internal Audit report. In addition, the Audit Committee is responsible for determining the focal points of the audit, as well as for evaluating the auditors' findings. The Audit Committee includes an expert in the fields of accounting or auditing, pursuant to section 100 (5) of the German Public Limited Companies Act (Aktiengesetz – "AktG").

Internal Audit also has a process-independent monitoring function. It reports directly to the Management Board, and provides auditing and consulting services which are designed to optimise Aareal Bank's business processes with regard to accuracy, safety and efficiency. The Internal Audit division supports the Management Board by evaluating the effectiveness and appropriateness of the process-dependent Internal Control System and of the Risk Management System in general. Any detected weaknesses regarding the identification, evaluation and reduction of risks are reported and addressed within the context of specific action plans.

Internal Audit also performs Group audit functions for Aareal Bank's subsidiaries, within the context of the Group's risk management. The review of the risk management's effectiveness and appropriateness covers the risk management and risk control systems, reporting, information systems, and the accounting process. To perform its tasks, Internal Audit has full and unrestricted information rights with respect to activities, processes and IT systems of Aareal Bank AG and its subsidiaries. Internal Audit is informed on a regular basis about material changes related to the Internal Control and Risk Management System.

The review of process-integrated controls conducted by Internal Audit is based on a set of internal regulations, procedural instructions and guidelines of Aareal Bank Group. The audit activities of Internal Audit comprise all of the Group's operational and business processes, and are carried out using a risk-based approach.

Components of the accounting-related ICS and RMS

Within Aareal Bank, various measures related to the Bank's organisational structures and procedures help to fulfil the monitoring duties within the framework of its Internal Control System.

A prerequisite for the monitoring system to work efficiently is a written set of procedural rules governing the distribution of tasks between the individual divisions and the scope of the respective activities. The organisational structure of the

Finance & Controlling division is set out in the Bank's organisational guidelines. Aareal Bank's accounting system is structured observing the principle of separation of functions. The functional separation makes for a split between operative and administrative roles, and is designed to ensure a sufficient level of control.

Various guidelines exist for activities and processes. These guidelines are set out in the Written Set of Procedural Rules of Aareal Bank and available for inspection to all employees. There are requirements as regards data entry and control – as well as data storage – which have to be observed in general by all of the Bank's posting units. If necessary, results are reconciled across divisions or companies. Uniform accounting methods and measurement techniques are guaranteed through guidelines applicable throughout the Group. The requirements of these Group-wide guidelines substantiate legal provisions, and are adjusted on an ongoing basis to take current standards into account. The valuation techniques used, as well as the underlying parameters, are controlled regularly, and adjusted if necessary. For further information on measurement, please refer to the relevant Notes to the consolidated financial statements.

In addition, the Bank's Risk Manual summarises the material elements of Aareal Bank Group's Risk Management System. Specifically, the Manual describes the organisational workflows as well as methods and instruments used in the context of risk management. In this context, reference is made to our explanations in the Risk Report.

Clearly-defined rules as regards delegation of authorities facilitating the allocation of professional responsibilities also contribute to reliable financial reporting. Any decisions taken are always based on relevant authorities. Internal controls defined on the basis of risk considerations are embedded in the accounting process. Compliance with the principle of dual control in all material processes is one of the principles for ensuring accurate accounting. Where no integrated approval system/dual control feature has been implemented in the Group accounting IT systems for material transactions, this has been integrated and documented in the manual process workflows.

Adherence of Group accounting to generally accepted accounting principles is ensured by both preventive and detective controls within the accounting process itself, as well as through a comprehensive review of processed data. The preparation of the consolidated financial statements is characterised by multiple analyses and plausibility checks. Besides the evaluation of individual accounting issues, these include comparisons of periods, and between plan and actual data. Adequate control processes have been implemented for both manual and automated accounting transactions.

In order to increase the level of control quality, all relevant divisions are involved in the reconciliation process. An example of cross-divisional reconciliation is the process for the preparation of annual and interim reports. All divisions involved must ensure and (prior to preparation by the Management Board) confirm the quality of the sections of the reports they are responsible for. This represents an additional control level for the data to be disclosed.

In terms of organisational workflows, the accounting-related Internal Control and Risk Management System is based on a comprehensive standardisation of processes and software. Aareal Bank Group uses both standard and customised software. The consolidation software provides technical support to the reconciliation of Group-internal relationships, in a clearly-defined process. The data of the units included is reported using a uniform standardised chart of accounts. The Group's accounting-related IT systems were designed in such a way that both manual controls and automatic plausibility checks are performed for material technical and procedural system steps of the applications used. The controls in relation to processing within the IT systems are also integrated in the processes, as well as being independently performed. Process-integrated controls comprise, for example, the review of error and exception reports or the regular analysis of internal service quality. In contrast, IT reviews are conducted independently from processes, by Internal Audit.

Data and IT systems must be protected from unauthorised access. A differentiated access authorisation concept is in place for the systems used for finance and accounting, preventing manipulation of data. Authorisations are allocated to responsible employees, reviewed regularly, and adjusted if necessary in accordance with internal criteria.

Aareal Bank reviews its accounting-related Internal Control and Risk Management System on an ongoing basis. Necessary adjustments are made with respect to the accounting process based on the Bank's reviews. Adjustments may have to be made, for example, in connection with changes in the Group structure, to the business model, or new legal requirements.

Aareal Bank has to comply with legal requirements. If these requirements change, for example in the form of new laws or changes in accounting standards, the processes or IT systems will be adjusted as required in separate projects across divisions – based on a clearly-defined allocation of functions, and the accounting-related Risk Management System will be adjusted to take the amended rules into account. Current developments of statutory and legal provisions applicable for Aareal Bank are constantly monitored and reported, not only by the responsible division, but also by a steering committee established by the Bank. This committee also initiates any required adjustments to be made to systems and processes, and reports the results to the Management Board.

Report on Expected Developments and Opportunities

Macro-economic environment

Developments for the economy, as well as for financial and capital markets, are exposed to diverse major risks and threats - which also have an impact on the commercial property markets. The economic forecast is defined by significant uncertainty. The key factors in this regard relate to geopolitical risks, protectionist economic policy, changing monetary policy and the impact of a weakening economy.

Changing monetary policies, with rising interest rates or the expectation of rising interest rates in an environment of abating quantitative measures, represent a risk. Sudden or excessive changes in interest rates may trigger a revaluation and changes in investor behaviour, potentially leading to a collapse in asset prices arising from a change in asset allocation. Emerging economies in particular will have to face capital outflows, and may have to raise their own interest rates. The economies were rendered vulnerable due to the protracted period of low interest rates caused by a lack of effort to reform and consolidate and increased levels of private debt. On the other hand, a longer-lasting period of low interest rates complicates an exit from such an environment, heightening the risks for the financial and capital markets. In this context, traditional central bank policy may lose its impact.

Protectionist measures adopted by the US pose a threat to both macro-economic performance and the financial markets. An open trade war cannot currently be ruled out, which, in addition to the reduction in trade in goods and services, could also cause turbulence on the financial markets.

However, the political shift away from European cohesion not only represents the greatest threat for the EU but for Europe too. This is substantiated by Brexit, regional pro-secession efforts for example in Catalonia, and in particular by nationally focused governments in Central and Eastern Europe, and in Italy. Besides the loss of political clout, this can also have negative implications for the economy.

Higher and continuing high levels of indebtedness in some instances pose another risk in many countries and regions. In this context, changes in monetary policy may have a negative impact upon market confidence, triggering crises. Furthermore, private debt has risen considerably, especially in the emerging markets, and could lead to market corrections and systemic crises.

Economy

A multitude of risks, easing fiscal measures and muted global trading are expected to slow down the pace of global economic growth in 2019. This could generate more pronounced regional differences than the year before. Moreover, risks and uncertainty factors, were they to materialise to a substantial extent, could mute the economic development, or even cause recessive tendencies in certain regions.

Although the euro zone is expected to continue showing slightly weaker growth in 2019, the threat of a recession is rated as low. The weaker growth is explained above all by a lower trade balance. We expect growth rates to be slightly lower for the most part in the euro zone markets that are relevant for Aareal Bank, while the Italian economy is likely to stagnate. Possible positive impetus from an expansionary fiscal policy in Italy should counter negative effects resulting from higher interest rates. Despite robust domestic demand, growth in the Netherlands is expected to be noticeably lower.

Economic growth in the EU this year is expected to exceed the euro area slightly. Expectations for the UK will be influenced significantly by the planned exit from the EU; the high degree of uncertainty surrounding the planned Brexit at the moment makes any forecast difficult. At present, it is fair to expect economic development to be stable at first – unless a hard Brexit (without an agreement with the EU) were to occur, in which case growth would likely be significantly weaker, possibly even tilting into recession.

Various indicators in the US suggest that the economic cycle has peaked there. Although considerably weaker growth is expected in 2019, it should nonetheless be much higher than in Europe. Slightly weaker growth is forecast in Canada, reaching a sustainable level following the previously very high growth rates.

Owing to easing investment in the energy sector, we see slightly weaker growth in Australia in 2019, which should however be better supported by investment in other areas.

In China, we expect the trend of slowing real GDP growth rates to continue. Factors influencing economic development in China are the targeted reduction of over-capacity in heavy industry and the transition to an overall lower investment ratio. We are still witnessing uncertainty with regard to the increase of macro-economic debt. Moreover, protectionist measures could also have a negative impact on trade, which is why federal support measures can be expected this year too.

Against a backdrop of positive economic growth, we expect most labour markets across the euro zone as well as in other European countries to register slowly decreasing to virtually stagnating unemployment rates for 2019. The US unemployment rate is also likely to continue to fall moderately.

Financial and capital markets, monetary policy and inflation

These risks and uncertainties listed above are also impacting on financial markets in the current year. Were they to materialise to a significant extent, they might cause turbulence on capital markets as well. Under these conditions, volatility is expected to be higher overall than the year before. We continue to believe that the financial markets will remain receptive towards refinancing and new securities issues.

With a possible moderate increase in, for example, deposit interest rates in the second half of the year and no renewed expansion of the quantitative measures, the ECB will slowly distance itself this year from the expansionary measures resulting from the financial crisis. In the US, the Fed has signalled a cautious stance regarding further interest rate hikes; therefore, only a slight increase in key interest rates is anticipated during the current year. In the UK, the Bank of England has tied its monetary policy orientation to the effects of Brexit. It will likely raise the base rate further in the event of an orderly Brexit.

Besides changes in monetary policy, the robust economy supports a further interest rate hike this year in the US, which is expected to be followed by another moderate rise in short and long-term interest rates. However, the yield curve will flatten increasingly and short-term interest rates will rise more sharply than at the long end of the curve. Developments in the US could exert a certain upside pressure on euro zone interest rates, especially for long-term rates. This must also be seen in the face of the expired asset purchase programme. Nevertheless, levels in the euro zone should remain low, with the exception of Italy.

Noticeably lower energy prices lead us to expect lower inflation in the euro zone, the UK and the US in 2019. This could have a positive effect on economic growth and limit interest rate hikes by the central banks.

Regulatory environment

The trend towards a tighter regulatory framework in the banking business is set to persist during the coming years. For instance, the finalisation of the Basel III framework, adopted by the Basel Committee's Group of Governors and Heads of Supervision (GHOS), will bring about extensive changes to the approaches used for determining risk-weighted capital requirements (a concept known as "Basel IV").

Furthermore, the EBA has finalised its Guidelines related to the Internal Capital Adequacy Assessment Process (ICAAP) and the Internal Liquidity Adequacy Assessment Process (ILAAP). In addition, the expectations of the Single European Supervisory Mechanism (SSM) regarding the structure of ICAAP and ILAAP must be implemented, based on a multi-year plan.

Moreover, the Target Review of Internal Models (TRIM) of ECB-supervised institutions within Pillar I has not yet been completed. Finalisation of new requirements under CRR II, CRD V and BRRD II is imminent. In addition, EBA has published guidelines on PD and LGD estimates, the treatment of risk exposures, and the determination of downturn LGDs – which will need to be implemented.

To facilitate the timely implementation, we have already continued to pursue the individual issues in numerous projects, devoting considerable resources to this task.

The volatility of requirements presents an additional challenge for institutions: besides the new requirements mentioned by way of example, this volatility is particularly a function of the concrete specifications for instruments implemented by the ECB and/or the national supervisory authorities. For instance, the capital buffers to be set on a national level (the anticyclical buffer and the buffer for systemic risks), or the annual results of the Supervisory Review and Evaluation Process (SREP) for individual banks, can only be planned to a certain extent. Moreover, these instruments may lead to changes in a bank's individual capital requirements, at short notice.

Following an amendment to the German Regulation Determining Critical Infrastructure (Verordnung zur Bestimmung Kritischer Infrastrukturen – "BSI-KritisV") in 2017, Aareal Bank AG is now additionally subject to reporting requirements vis-à-vis the German Federal IT Security Authority (BSI). The BSI requires that areas and systems classified as "critical infrastructure" must be certified by mid-2019. The Bank has launched a corresponding project and commissioned this certification.

Sector-specific and business developments

Structured Property Financing segment

Demand for commercial properties will vary in 2019, depending on the region and property type. A shortage of sought-after top-class properties, along with reticence among different investors to invest in specific markets (such as Italy and the UK) or in specific property types (such as retail), will make itself felt in global transaction volumes. These are likely to be lower this year than in 2018.

Commercial property markets, as well as the economy, are exposed to major risks and threats. An excessively sharp interest rate hike could have a negative effect on performance. Moreover, other uncertainty factors and risks in the macroeconomic environment are also relevant for commercial property markets.

Several factors will influence the market value of commercial property over the course of the year. Whilst the still-robust economy and historically low interest rates will support property values, political uncertainty, a potential strong rise in interest rates, or investor reticence might have an adverse effect on values. Despite the sustained economic cycle, the market cycle is still intact, therefore also potentially leading to cyclical downturns in the commercial property market.

Based on the conditions described above, we therefore anticipate a largely stable development in the market values of commercial property in many markets this year.

We expect a stable development of market values in 2019 in most European countries, such as Finland, France, Germany, the Netherlands, Poland, Russia and Sweden. For Spain, on the other hand, we consider slightly positive growth to be possible. Brexit is creating uncertainty in the UK, whereby a hard Brexit may lead to declining values. Political uncertainty in Italy could have a negative impact on property values. Despite the stable development overall, we could see declining values in some European markets or for some property types.

We assume property values in the US will remain stable on the whole. Increasing interest rates pose certain risks for this development. A stable performance also looks likely for Canada.

In Australia and China, stable market values for commercial property are expected.

The trends described above are expected to apply to office, retail and logistics properties.

As was the case last year already, the European hotel markets are for the most part expected to report growth in average revenues per available room. Occupancy rates remain very high in most markets. Relocations on the back of Brexit could lead to higher occupancies in individual continental European markets. Stable indicators are expected in the UK hotel market. Although the weak pound is boosting tourism, Brexit is likely to have a negative effect.

A less dynamic economy in the US is expected to lead to stagnating growth in occupancy rates in the hotel market there in 2019. However, higher average disposable income among consumers is likely to lead to a further increase in average room rates, so that average revenue per available room is expected to increase slightly in 2019. In Canada, the positive development of occupancy and average revenue per available room is likely to continue. However, the slowdown in the pace of economic growth should lead to a marginally smaller increase than in previous years.

For the Asia/Pacific region, we anticipate occupancy ratios and average revenues per available room to remain stable throughout 2019 in the hotel markets of many metropolitan areas.

The intense competition in commercial property financing is also likely to persist in many markets during the current year and we believe lenders are willing to lower margins, even if this might slowly lead to the formation of a plateau. We anticipate a virtually stable development in loan-to-value ratios across the various regions. Banks are expected to continue adhering to their preference for financing first-class properties in top locations.

We have incorporated various market aspects and our "Aareal 2020" programme for the future, amongst other factors, in our assessment of anticipated new business volumes for the current year. For the Structured Property Financing segment, we are targeting new business of between € 7 billion and € 8 billion for the 2019 financial year, whereby the focus is set to remain on the high-margin US market. Aareal Bank Group's property financing portfolio should amount to between € 26 billion and € 28 billion at the end of 2019, subject to currency fluctuations. To manage our portfolio and risk exposure, we also use syndications which facilitate larger-sized financing solutions.

The forecasts are based on the assumption that the macro-economic risks and uncertainty factors described above will not materialise to a significant extent, or only in a manageable manner: otherwise, they might influence business development, for example, in terms of new business.

Consulting/Services segment

Bank division Housing Industry

The German housing and commercial property industries are expected to continue showing solid development in 2019, on the back of stable rental income and a high degree of stability in property values.

Companies in this sector will continue to pursue sustainable portfolio optimisation. Energy-efficient renovation, deployment of technical assistance systems, expanding the digital infrastructure and serial construction activity are developments currently shaping investment trends.

Political developments and their impact on the profitability of individual measures may be affecting future corporate investment activities. Stricter regulations regarding energy efficiency measures to be incorporated during renovations, and rising requirements for new construction, might restrict the volume of investments.

The stable development on the residential property market is expected to prevail in 2019. Regional differences are expected to further increase, as a consequence of migration driven by education and labour market factors. Due to the ongoing urbanisation trend, we expect demand for apartments to rise further, especially in economically strong conurbations. Property investors and potential sellers within the housing and commercial property industries should continue to be able to benefit from these market developments.

We see good opportunities during 2019 to acquire new clients and to intensify the business relationships with our existing client base. This also applies to utilities and the waste disposal industry. In addition, in line with our "Aareal 2020" programme for the future, we continue to invest in the expansion of the "Housing Industry Ecosystem", the cross-sector development of interface products, and the expansion to adjacent ecosystems. The focus here is on, for example, the functional expansion of the Aareal Portal corporate client platform as regards the digitalisation of client communication and account processing.

In our view, the range of services that connect alternative online payment solutions to existing systems, thus helping to overcome process breaks (even across industry sectors), are particularly interesting. We will continue to intensify our activities in the projects for connecting alternative payment systems. We also see potential in techniques that facilitate direct communication between a large number of paying agencies in the so-called Internet of Things (IoT), thus facilitating standardised settlement for a growing number of micro payments. We will also examine cooperations with Fintech and Proptech companies in order to realise corresponding approaches to development.

Besides these future technologies, we are also confident about the economic viability of established processes and procedures, which is why we will continue, for example, to expand the range of services we offer in the area of deposit management.

We expect the volume of deposits taken to remain on a high level. The persistent low interest rate environment, which is relevant for the results from our deposit-taking business, will continue to burden segment results. However, the importance of this business goes way beyond the interest margin generated from the deposits, which is under pressure in the current market environment. This is because the deposits from the housing industry represent a strategically important additional source of funding for Aareal Bank.

Aareon

Aareon will continue in 2019 to pursue the growth strategy based on its strategy programme integrated in the "Aareal 2020" programme for the future. Sales revenue is expected to rise significantly, especially driven by higher market penetration with digital solutions, a strengthening of the ERP business, and by an expansion of activities in the energy utility and commercial property markets. Furthermore, Aareon plans to make significant investments in expanding its range of digital products, solutions related to new technologies, and to participate in the start-up scene, to accelerate organic growth. These investments serve to further develop the entire Aareal Bank Group in the long term.

We anticipate a slight increase in sales revenue in the ERP business. The focus in this context will be on the migration of GES clients to Wodis Sigma in Germany, which in 2019 will continue to account for a significant part of the consultancy business. There is potential for several complex major projects to be concluded in Germany and on international markets, which will lead to a higher volume of business in 2019. Projects are also expected to be completed in the energy utility and commercial property markets, which will lead to a higher volume of advisory business. Licence revenue from the ERP products will fall, as the migration business is expiring in Germany and no significant licence revenues are expected with key accounts in 2019. We will see a decline in ERP products business with international clients, as only a few regular licence extensions are scheduled for Dutch clients in the 2019 financial year.

The digital solutions will help realise growth potential, as they are poised to become more important in the property industry and to attract greater customer interest. Further product roll-outs are expected to lead to a marked increase in sales revenue, particularly for the digital solution Aareon CRM and mobile services. New CRM product generations will be introduced in the UK and the Netherlands, which will drive up demand. Further revenue growth will be realised in Sweden, as digital products will be marketed there in the future independent of the ERP products.

The volume of business generated with add-on products, such as insurance management with BauSecura and outsourcing services will remain on par with last year.

Based on the explanations outlined above, Aareon envisages a marked overall increase in sales revenue for the following year. Excluding strategic investments into accelerated growth, Aareon plans for a contribution to consolidated operating profit of around € 41 million; including these investments, the contribution to consolidated operating profit is expected to amount to around € 35 million.

Business strategy

Aareal Bank Group's strategy focuses on sustainable business success. With its Group-wide "Aareal 2020" programme for the future, the Bank is addressing the challenges of the future. In an environment characterised by technological change, further growing regulatory requirements, altered client needs and fiercer competition, this programme allows us to secure our strong foundation while also leveraging new revenue potential. Aareal Bank developed an extensive strategic roadmap for the implementation of "Aareal 2020", including various initiatives and projects for the further development of the Group. The measures introduced within the scope of the programme to increase efficiency and optimise structures and processes were implemented successfully, and most of the organisational and personnel changes they entail are applied.

We are also on the right track with our strategic initiatives to further develop the business models in both segments. This included expanding the business of the Structured Property Financing segment in attractive markets such as the United States, exploring additional options along the value creation chain through the partnership with Mount Street or the investment in BrickVest, and winning new syndication partners. In the Consulting/Services segment, Aareal Bank Group has grown its business beyond the core housing industry business, moving into related industries such as energy utilities or the commercial property sector. Having established digital platforms, the Bank has built a good foundation and sees opportunities for further growth with digital solutions. Moreover, to boost the segment's innovative strength and to supplement the product portfolio, partnerships with start-ups were agreed upon.

Group targets

We anticipate the challenging business environment to prevail during the current financial year – with continued low interest rates in Europe, strong competitive and margin pressure on key target markets, combined with an increasingly uncertain market environment and persistently strict regulatory requirements. Against this background, we will continue to adhere to our business policy with a strict focus on risks and returns. We will further accelerate our strategic development, within the framework of the "Aareal 2020" programme for the future – especially through our enhanced digital offensive in the Consulting/Services segment.

We expect net interest income (excluding net derecognition gain or loss) for the full year 2019 in a range between € 530 million and € 560 million. We estimate the volatile, market-driven net derecognition gain to be between € 20 million and € 40 million. Loss allowance is expected to remain in a range between € 50 million and € 80 million. Net commission income, whose importance for the Group is continuously rising due to the expansion of business activities in the Consulting/Services segment, in line with the strategy, is anticipated to rise further, to between € 225 million and € 245 million. Administrative expenses, including Aareon's additional investments to accelerate growth as well as integration costs for Düsselhyp, are expected between € 470 million and € 510 million.

Against this background, we expect consolidated operating profit for the current year to be in a range between € 240 million and € 280 million; this is in line with the previous year's figure, adjusted for the positive non-recurring effect related to Düsselhyp. We envisage RoE before taxes of between 8.5 % and 10 % for the current financial year, with earnings per share at around € 2.40 to € 2.80. We affirm our medium-term target RoE of at least 12 % before taxes.

We will continue the reduction of non-strategic portfolios in the Structured Property Financing segment during 2019. At the same time, our core credit portfolio is planned to grow in line with respective market conditions. Overall, subject to exchange rate fluctuations, Aareal Bank Group's aggregate property financing portfolio is expected to range between € 26 billion and € 28 billion. We are targeting new business of between € 7 billion and € 8 billion for the current year, with a continued focus on the high-margin US market. Our IT subsidiary Aareon is expected to contribute approximately € 35 million to consolidated operating profit, taking strategic investments into accelerated growth into account (excluding strategic investments: approximately € 41 million).

Subject to further regulatory changes, Aareal Bank considers a target CET1 ratio (post-finalisation of Basel III – so-called "Basel IV") of around 12.5 % to be appropriate. The Liquidity Coverage Ratio (LCR) is expected to be at least 150 %.

Remuneration Report

Remuneration is a key element of managing the business, and of managing risk. The remuneration strategy at Aareal Bank Group forms part of the Company's efforts to ensure that employees' remuneration is in line with market conditions and the performance achieved. At the same time, it helps to align the Group's remuneration intentions with current regulatory requirements. When setting remuneration, Aareal Bank Group therefore pays attention to ensuring that the proposed remuneration motivates employees to achieve the Group's strategic business and earnings targets whilst remaining within the boundaries set by the Group's risk appetite and corporate values. Whilst good performance is remunerated accordingly (through a bonus), any breaches of internal or external rules are penalised through sanctions (penalties).

Remuneration system for the Management Board

Overview

The Supervisory Board of Aareal Bank AG designs a remuneration system which provides incentives to Management Board members for achieving entrepreneurial goals and targets, within the framework of the defined risk appetite and risk strategies. As a "significant institution" which is subject to direct supervision by the European Central Bank, Aareal Bank's scope in setting remuneration is subject to tight restrictions, pursuant to the specific regulatory requirements for banks, pursuant to the EU Capital Requirements Regulation (2013/575/EU), the German Banking Act (Kreditwesengesetz – KWG), and the German Regulation on Remuneration in Financial Institutions (Institutsvergütungsverordnung – InstVergV).

Remuneration comprises a fixed component (including ancillary benefits and contributions to retirement provisions) and a variable component, the structure of which is governed by law. Variable remuneration must not exceed fixed remuneration.

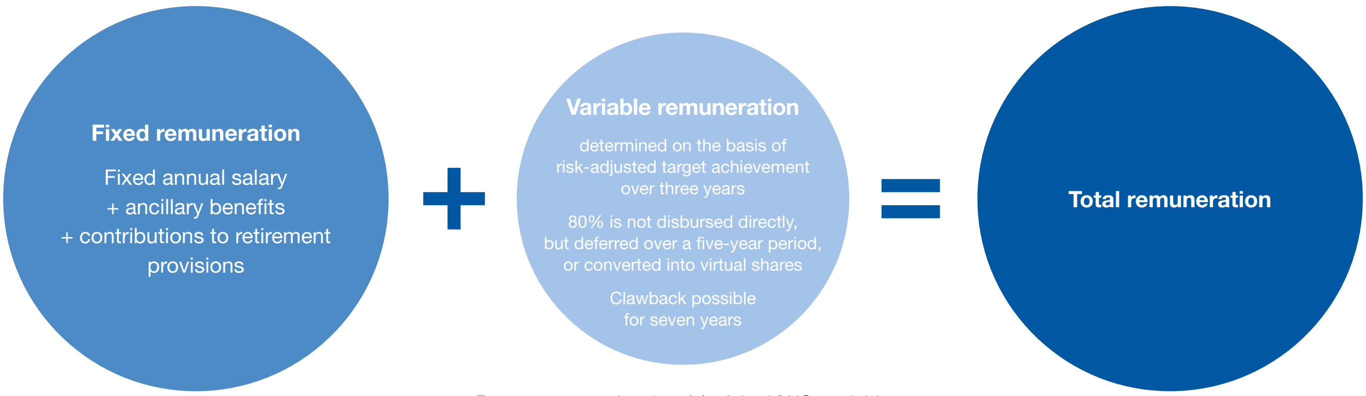
In a first step, pursuant to the InstVergV, the amount of variable remuneration must be determined in line with the degree of achievement of specific targets, which are based on a three-year period. Such targets must be derived from the business strategy, and must relate to three levels: targets related to Aareal Bank Group, to the respective Management Board member's area of responsibility, as well as that member's individual targets. Targets have both quantitative and qualitative, as well as financial and non-financial components. The Supervisory Board has not provided any discretionary components; it has capped the overall level of target achievement at 150 %.

Disbursement of 80 % of variable remuneration is deferred, in accordance with the InstVergV; 60 % of variable remuneration must be retained for up to five years. 50 % each of deferred and non-deferred variable remuneration components are converted into virtual shares, which allow Management Board members to participate in Aareal Bank's performance for up to six years. Performance of virtual shares is capped at 300 %.

Taking the target determination period together with the deferral and holding periods, the actual amount of variable remuneration for a given financial year is determined over an aggregate period of nine years. Given this very long period, which is prescribed by regulations, the Supervisory Board has refrained from imposing any further conditions or disbursement modalities. There is no need for an agreement requiring Management Board members to enter into any proprietary investments in Aareal Bank shares, since the Supervisory Board believes that the existing system meets the purpose of such an investment. By granting 50 % of variable remuneration in the form of virtual shares, together with the fact that variable remuneration – assuming a target achievement level of 100 % – is roughly equivalent to the fixed annual salary, Management Board members will have regularly earned virtual shares equivalent to their fixed annual salary level after two years. Given the long deferral periods and the holding periods, this is a value which they usually retain until the end of their term on the Management Board (cf. section "(Virtual) shareholdings of Management Board members and share-based remuneration"). At present, active Management Board members hold – on average – around 150,000 virtual Aareal Bank AG shares, equivalent to a single-digit million euro amount – which not least creates a parallel interest with shareholders.

Achievement of initial targets is regularly reviewed during the deferral period, and the amount of variable remuneration originally agreed upon (and hence, variable remuneration) adjusted ex-post if necessary **(back-testing).** Variable remuneration for a given financial year may be reduced in the event of inappropriate behaviour, or behaviour in breach of duties. In the case of negative performance contributions, as defined in detail by the Supervisory Board, in the form of significant losses or material regulatory sanctions, variable remuneration must be reduced to zero **(penalty review).** Where a portion of variable remuneration for such financial

General breakdown of Management Board remuneration



Pursuant to section 25a (5) of the KWG, variable remuneration must not exceed fixed remuneration

year has already been disbursed, this portion may be reclaimed on the basis of corresponding provisions in Management Board contracts **(clawback).** Variable remuneration will no longer be paid in the event of any threats to the Bank's risk-bearing capacity, sufficient capitalisation or liquidity, or if certain minimum profitability indicators are not achieved.

Service contracts with Management Board members do not provide for any severance pay in the event of a contract being terminated prematurely by way of mutual consent, without good cause. In such cases, severance pay may be made on the basis of an individual agreement, which however is capped at a maximum of two annual remuneration amounts, or the value of the remaining contract term (severance cap).

Fixed remuneration component

The fixed remuneration component of a Management Board member consists of three components – the fixed annual salary, ancillary benefits, and contributions to retirement provisions.

Fixed annual salary

Within Aareal Bank AG's corporate governance system, the members of the Bank's Management Board discharge operative functions in addition to their managerial duties. They prepare and implement strategic objectives in cooperation with their employees. Management Board members are remunerated in line with this comprehensive set of duties.

In order to prevent any motivation for Management Board members to enter into inappropriate risks, in accordance with Aareal Bank Group's risk culture, fixed remuneration accounts for a significant portion of the total remuneration package. Ordinary members of Aareal Bank AG's Management Board, for whom the so-called "newcomers rule" does not apply, receive a fixed annual salary of € 880,000; the Chairman of the Management Board receives € 1.3 million.

Ancillary benefits

Aareal Bank AG provides a company car to Management Board members, which may also be used for private purposes. Management Board members are covered by the group accident insurance in case of death or invalidity. In addition, Aareal Bank AG bears the costs incurred for certain security expenses.

Pensions and retirement benefits

The benefit regulations as agreed in the service contract apply to the members of the Management Board. Management Board members who were appointed prior to 1 January 2013 are entitled to claim pension benefits as of the time at which they turn 60. For members of the Management Board who were appointed on or after 1 January 2013, claims arise as of the time at which they turn 62. In the event of permanent disability, a Management Board member may be entitled to claim benefits prior to turning 60 or 62, respectively.

The pension claims are adjusted to take account of the development of standard wages within the private banking sector as from the beginning of actual payments of pensions, to the extent that these are based on defined benefit plans. If the payments refer to defined contribution plans, the guaranteed amount is adjusted by 1 % p.a. The pension paid to widows amounts to 60 % of the pension of the member of the Management Board, while pensions to half-orphans and orphans amount to 10 % and not more than 25 %, respectively.

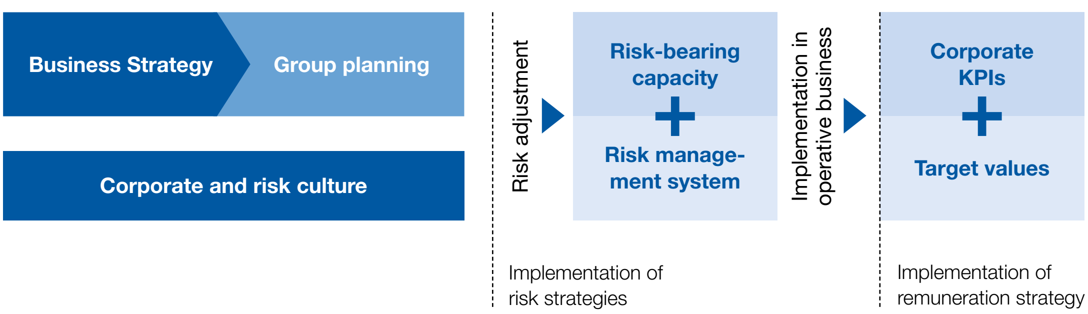
Performance-related variable remuneration

Management Board members receive variable remuneration, the amount of which depends upon achievement of pre-determined three-year targets derived from the strategy. In addition, the amount of variable remuneration also depends upon the performance of virtual shares, which allow Management Board members to participate in the Company's ongoing performance for a six-year period (for details, please refer to the following chapter). This means that the variable remuneration effectively reflects a period spanning nine years in total (three-year assessment basis plus five-year deferral period and one-year holding period for the virtual shares) and is largely of a forward-looking nature. There are no discretionary components besides this. The reference value for 100 % target achievement amounts to € 1.4 million for the Chairman of the Management Board, and to € 800,000 for ordinary Management Board members for whom the so-called "newcomers rule" does not apply.

Remuneration and target derivation system

As a matter of principle, Aareal Bank derives remuneration targets from its strategic planning for the following years, which was already verified as to its compatibility with the corporate and risk culture, and risk-adjusted in line with the Bank's risk strategies. Hence, the target parameters (KPIs) derived from the strategy are geared towards the sustainable development of Aareal Bank Group – as opposed to short-term successes – and are thus aligned with the interests of shareholders, employees and other stakeholders.

Derivation of remuneration strategy, indicators, and target values



Remuneration parameters (ex-ante risk adjustment)

A significant part of Aareal Bank's variable remuneration is governed by law: besides the general requirement – pursuant to the German Public Limited Companies Act (Aktiengesetz – "AktG") – that the remuneration system be focused on a sustainable company development, sections 19 and 20 of the German Regulation on Remuneration in Financial Institutions (Institutsvergütungsverordnung – "InstVergV") require that target achievement be determined on the basis of at least three target levels, and over a minimum assessment period of three years. Accordingly, Aareal Bank AG's remuneration system for the Management Board provides for the target levels of:

- Group performance;
- sectional performance; and
- individual performance.

Target achievement for each target level is determined on the basis of a three-year assessment period.

All targets for Management Board members are geared towards achieving the objectives set out in the Bank's business and risk strategies **(pay-for-performance principle).** When setting targets, the Supervisory Board pays attention to defining ambitious but realistic targets which are in line with Aareal Bank's risk appetite as well as the corporate and risk culture. The targets comprise quantitative and qualitative components, which are also related to non-financial parameters.

Amongst other things, the Company's interests are duly taken into account by the fact that **Group targets** are geared towards the KPIs used for corporate management purposes. Consolidated operating profit before taxes is generally chosen as an income target, whereas risk-weighted assets (RWAs) are used as a risk-adjusted target. Specific values are determined annually for both target components, which correspond to a 100% target achievement level. These targets at least complied with the corporate objectives communicated to the capital markets in the past, and will continue to do so in the future. The maximum achievement

Methodology for the calculation of annual target achievement

Example shown: financial year 2018

level for target consolidated operating profit is 150 %; for the RWA target, it is 125 %. The overall target achievement level is calculated by multiplying both target values; it is capped at a target achievement level of 150 %.

Sectional targets are related to the respective Management Board member's area of responsibility pursuant to the schedule of responsibilities. Accordingly, the Supervisory Board sets targets which the organisational units assigned to the respective Management Board members need to fulfil in order to achieve the strategic objectives of the Company as a whole. These targets may comprise income and budget targets, target values for specific risk indicators, or for implementation of key strategic projects. In line with Aareal Bank Group's management system, sectional targets for Management Board members responsible for Sales units comprise, among other things, specific target values for new business, or regarding credit portfolios, or the contribution of material subsidiaries such as Aareon AG. In accordance with Aareal Bank Group's risk management system, these income targets must not exceed the risk appetite as determined by reference to certain limits; hence, there is no incentive to enter into inappropriate risks. Sectional targets for Management Board members responsible for central staff functions or control units are based on other indicators, such as the amount of the administrative expenses. Moreover, within the framework of sectional targets, all members of the Management Board are required to fulfil specific projects in order to implement the Company's strategy. such as projects for the digitalisation of processes and products.

Individual targets are related to each Management Board member's individual performance, and also comprise specific sustainability (environmental, social, governance – "ESG") targets: in this respect, Management Board members are required in particular to exercise their function as role models vis-à-vis staff and the general public. They also need to achieve material sustainability aspects, such as the implementation of Aareal Bank Group's cultural objectives; targets include assessments as to whether communication with employees is effective, if the Management Board member complies with his or her own governance requirements, and whether he or she acts as a role model.

The members of the Management Board are responsible – and epitomise – the Company's success. This is also reflected in the **weighting of the target levels.** Accordingly, achieving Group performance targets accounts for the clear majority (70 %) of target achievement, with the other two target levels weighted at 15 % each.

As the strategy refers to a period of several years, targets are also set to refer to multiple years. To measure and monitor target achievement, annual targets are derived from the overall strategy; the level of achievement is, however, viewed over a three-year period **(three-year assessment basis).**

To date, only Group performance targets covered a period of several years. Due to new regulatory requirements set out by the InstitutsVergV, this multiple-year assessment must be extended to cover all target levels for remuneration determined for the 2019 financial year for the first time. In order to continue setting ambitious targets and a strong incentive for successful Management Board work, target achievement levels are set to be incorporated at different levels over time: following a transition period, the most recent reporting year will be weighted at 60 %, the preceding one at 30 %, and the oldest year in the assessment period at 10 %. The transition period will end with the 2021 financial year.

Deferred disbursement, through retention of variable remuneration components and virtual shares

To ensure that the remuneration system provides long-term incentives, the initial value for variable remuneration – as determined according to the principles set out above – is awarded at the end of the financial year, according to the following principles:

- 20 % of the variable remuneration is disbursed as a cash bonus after the Supervisory Board has determined the overall target achievement level.

- A further 20 % of the variable remuneration is awarded as a share bonus subject to a holding period (and forms part of the share-based bonus plan), in the form of virtual shares, also after the Supervisory Board has determined the overall target achievement level.

- 30 % of the variable remuneration is retained (cash deferral), and disbursed in cash – pro rata temporis – over a five-year deferral period.

- The remaining 30 % of the variable remuneration is credited, as a cash amount, to a virtual account maintained on behalf of each Management Board member, and forms part of the share deferral plan (share deferral with holding period).

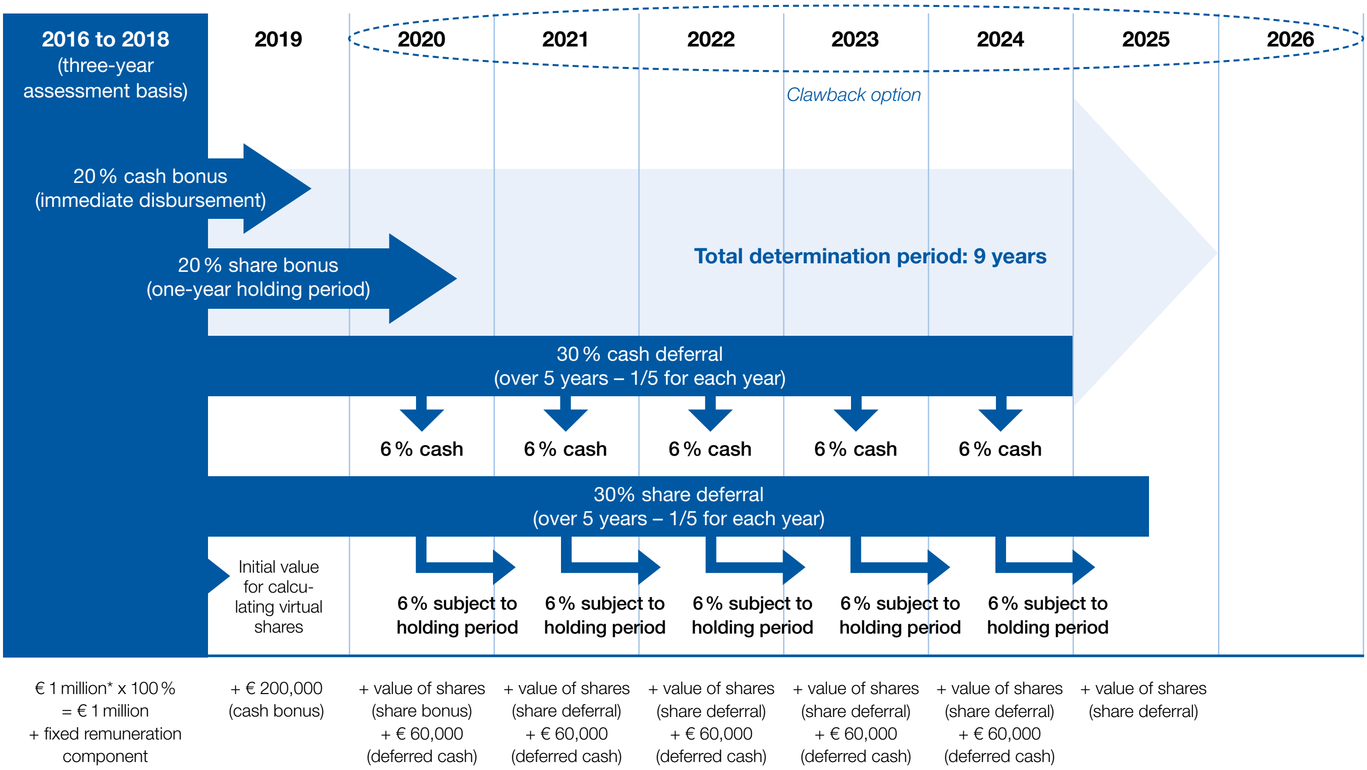
This means that deferred disbursement over a period of up to six years applies to 80 % of variable remuneration determined.

Five-year deferral period

With regard to the portion of performance-related remuneration that is deferred initially as a cash deferral or a share deferral, the Supervisory Board makes a decision regarding the granting of one third of the amount, as well as the associated interest, in the five years following the determination of the performance-related remuneration (retention period – cf. "Ex-post review of target achievement and behaviour of the Management Board").

Sample disbursement methodology, based on 100 % target achievement for the 2018 financial year

The Supervisory Board regularly examines, at the beginning of each year and prior to disbursement or conversion into virtual shares, whether the original target achievement still applies, and whether a penalty-triggering event has occurred which requires reduction or clawback of variable remuneration.



* For the sake of simplicity of this sample presentation, variable remuneration for a 100 % target achievement level was set to a notional value of € 1 million.

Until the end of each respective deferral period, there is no right to the relevant remuneration components. No interest or dividends will accrue. Once the deferred remuneration components for Management Board members are vested, the cash deferral is paid out in cash and the share deferral is converted into virtual shares, subject to a one-year holding period.

Share bonus with holding period

The portion of the performance-related remuneration which is subject to the share bonus plan will be converted into an equivalent number of virtual shares. The calculation of the number of virtual shares is based on the weighted average price on the basis of five (Xetra®) exchange trading days after publication of the preliminary results for the financial year for which the share bonus is granted (subscription price). The date of publication of the preliminary results is used as the reference date.

The virtual shares so determined are posted to a virtual account, and are held for one year. They will be converted, automatically and without delay, into a cash amount and disbursed immediately after the Supervisory Board meeting which passes the resolution on the adoption of the annual financial statements for the first financial year following the financial year for which the virtual shares were granted ("holding period"). The conversion will be effected using the weighted average price calculated on the basis of the five (Xetra®) exchange trading days following the publication of the preliminary results for the year preceding the payout.

The payout amount of the share bonus of a given financial year may vary depending on the share price development and has been limited to a maximum of 300 % of the agreed initial value (ceiling).

Share Deferral Plan

In the five years following determination of performance-related remuneration (deferral period), the Supervisory Board decides whether in each case a fifth of the share deferral should be converted into virtual shares.

The rules of the share bonus plan are applicable to the calculation of the number of virtual shares, subject to the proviso that the weighted average price calculated on the basis of the five (Xetra®) exchange trading days following the publication of the preliminary results for the financial year in respect of which variable remuneration was determined. This is designed to preserve the reference to the original assessment period.

The ceiling value is applicable for the conversion of the virtual shares, with the proviso that the payout amount following the conversion of the virtual shares of a tranche into a cash payment must not exceed 300 % of the share deferral (30 % of the initial value of performance-related remuneration) set for the financial year in question (which may have been reduced following the application of a penalty rule or as a result of an instruction by BaFin).

Remuneration system prior to the 2018 financial year

The remuneration system for Management Board members was adjusted in various places, reflecting amendments to the InstVergV. Specifically, the deferral period for variable remuneration determined from 2018 onwards was extended from three to five years. Accordingly, decisions concerning remuneration for financial years prior to 2018 refer to one-third of deferred remuneration in each case; for variable remuneration determined for financial years from 2018 onwards, decisions refer to one-fifth for each deferral period. For variable remuneration determined prior to the 2018 financial year, the applicable holding period is three years for the share bonus, and two years for the share deferral. A uniform one-year holding period applies from the 2018 financial year onwards.

Given that these changes were mandatory under banking regulations, they were not submitted to the Annual General Meeting for approval. In principle, Aareal Bank endeavours to obtain the Annual General Meeting's approval for the Management Board remuneration system in regular intervals of at least four to five years. However, considering the Bill to Implement the Second EU Shareholder Rights Directive ("ARUG II"), which is yet to be forthcoming, and possible new recommendations on remuneration provided by the German Corporate Governance Code (which is currently being revised), the Supervisory Board will have to deal with potential further adjustments to the remuneration system for the Management Board (and related reporting). The Supervisory Board intends to submit this system to the Annual General Meeting for approval once this process has been concluded.

Ex-post review of target achievement and behaviour of the Management Board

Backtesting regarding retained remuneration components

Before the Supervisory Board decides on conversion or disbursement of retained remuneration components, it reviews whether the target achievement level originally agreed upon is still held to be correctly determined, based on current knowledge. For example, where an indicator used to determine remuneration needs to be adjusted ex-post, this can also reduce the variable remuneration determined – and hence, result in a reduction in the amount retained. If it turns out, at a later date, that a project did not achieve the objectives on which the original remuneration calculation was based, then the variable remuneration can also be reduced ex-post.

Penalty review

When determining variable remuneration, as well as prior to every disbursement of cash components or conversion into virtual shares, the Supervisory Board verifies whether there are any reasons, besides the achievement of targets, for reducing variable remuneration, possibly to zero.

Such penalty-triggering events include inappropriate behaviour, behaviour in breach of duties, or negative performance contributions of Management Board members, which cannot be offset through positive performance contributions at other levels. For example, breaches of the Code of Conduct and/or Compliance guidelines, conduct that damages the Bank's reputation, or other misconduct may give rise to a penalty. If any retained performance-related remuneration components are not awarded, or only in part, the remaining sum is forfeited, i. e. it is not carried forward into subsequent years.

Clawbacks

Starting with variable remuneration for the 2018 financial year, agreements concluded with members of the Management Board ensure that variable remuneration already disbursed may be reclaimed ("clawed back") in the event of certain cases of negative performance contribution – for instance, if supervisory authorities of Aareal Bank AG demand that a Management Board member be removed due to lack of aptitude.

Restrictions and additional provisions

Impact of special external conditions (modifiers)

The Supervisory Board is entitled to increase or decrease the level of target achievement for the Group component by up to 20 percentage points (a so-called modifier) in the event of unforeseeable changes to the economic environment which are beyond the Management Board's influence or control (i. e. only on the basis of external conditions). This will not affect the restrictions set out below, especially the 150 % cap, which cannot be circumvented by the modifier.

1:1 cap, plus 150 % cap for variable remuneration

Pursuant to section 25a (5) of the German Banking Act (KWG), the variable remuneration must not exceed the fixed remuneration component for Management Board members, even in the event of maximum target achievement. The option of allowing the Annual General Meeting to approve higher variable remuneration corresponding to up to 200 % of the fixed remuneration component, as set out in section 25a (5) sentence 5 KWG, has not been used for the Management Board members.

The maximum overall target achievement level for determining performance-related remuneration is additionally capped at 150 %. Hence, variable remuneration determined cannot exceed 150 % of the reference level.

Hedging ban
The contracts of Management Board members prohibit them from undertaking to limit or override the risk orientation of their remuneration by initiating personal protection or countermeasures (hedging ban).

Additional constraints regarding target achievement

For the purpose of additional risk adjustment, for each financial year, the Supervisory Board sets a target level for the Common Equity Tier I ratio (CET I ratio) as the measurement threshold in order to secure adherence of the regulatory capital adequacy and a suitable liquidity measure (Liquidity Coverage Ratio – LCR). No variable remuneration will be determined for any financial year where any of these two targets has not been achieved.

Risk-bearing capacity, and parallel interest with shareholders

To preserve the Company's continued survival (and hence, shareholders' investment), variable remuneration is generally subject to a review performed by the Supervisory Board pursuant to section 7 of the InstitutsVergV. This review is based on the Recovery Plan (which is mandatory for Aareal Bank as a significant institution) and the thresholds defined therein. These thresholds include achieving minimum profitability indicators such as the return on equity. In the event of these so-called "early warning thresholds" being reached, the Supervisory Board will decide, in its reasonable discretion, whether variable remuneration for the Management Board needs to be reduced. The total amount of variable remuneration is set to zero if Aareal Bank's risk-bearing capacity is no longer sufficiently ensured. In addition, pursuant to section 45 (2) sentence 1 no. 5a KWG, the German Federal Financial Supervisory Authority (BaFin) may impose further conditions or restrictions, or may instruct that the total amount of variable remuneration be cancelled.

Rules governing severance pay

The agreements concluded with members of the Management Board do not include any obligation to make severance payments in cases involving the early termination of employment relationships **(rescission of the agreement without good cause).** However, severance payments may be included in individual termination agreements, provided that these are specified in accordance with regulatory requirements, in particular with the InstitutsVergV. The agreements concluded with members of the Management Board state that, in the event of the premature termination of their term on the Management Board without good cause within the meaning of section 4.2.3 of the German Corporate Governance Code (hereinafter referred to as the "Code"), payments, including ancillary benefits, made to the Management Board member in question must not exceed twice the annual remuneration (severance cap) and must not constitute remuneration for more than the remaining term of the employment contract.

In the case of a compulsory loss of a Management Board position **(change of control),** the Management Board members are to be paid the fixed remuneration component, the performance-based remuneration, as well as the contractually agreed benefits for the remainder of the term of the contract. The performance-related remuneration is subject to the above-mentioned conditions; that is, in particular the deferral periods, the holding periods and the penalty rules are applicable. In addition, the extent to which sectional and individual targets were achieved on average during the last three years prior to the termination of the Management Board position will be used as a basis to determine the target achievement level for the remaining term of the contract. In the case of a voluntary termination of the Management Board position following a change of control, the members of the Management Board merely receive the fixed remuneration and the contractually agreed ancillary benefits for the remainder of the contractual term. In this case, there is no entitlement to the variable remuneration component.

The total amount of payments in the case of termination due to a change of control is limited to 150 % of the severance cap of an employment contract, in accordance with section 4.2.3. of the Code.

Newcomer rule

The Supervisory Board intends to remunerate newly-appointed members who have not previously held a position on the Management Board of a comparable institution in line with an entry level of 80 % of fixed and variable remuneration for ordinary members of the Management Board, reflecting lack of experience. If the Management Board member is re-appointed, the Supervisory Board will also decide upon the potential increase of remuneration to the normal level. However, since the Supervisory Board decided upon the specific selection as well as remuneration of individual Management Board members, within its reasonable discretion, and taking the Company's specific needs into account, it is possible to diverge from this rule.

When implementing the InstitutsVergV, as amended on 3 July 2017, the Supervisory Board decided to only gradually build up the three-year assessment period; in the Supervisory Board's view, newly-appointed members of the Management Board should not be held accountable for past developments. In accordance with the regulatory requirements pursuant to the InstitutsVergV, the deferral period is extended for periods with a shortened assessment period. Hence, for the first year, the assessment period is only one year, with the deferral period extended from five to seven years. For the second year, the assessment period is extended to two years and the deferral period shortened to six years. The remuneration system for the Management Board will be applied, as provided, from the third year onwards.

Remuneration of the Management Board

Total remuneration

In accordance with German commercial law in conjunction with GAS 17, the following table shows fixed and other remuneration for members of the Management Board, variable remuneration determined for the respective financial year (total amount, plus a breakdown into its components), as well as the total target achievement levels, as determined by the Supervisory Board.

€	Year	Fixed remuneration	Variable remuneration: Cash component		Share-based component				Ancillary benefits	Total remuneration
			Cash bonus	Cash deferral[1]	Share bonus	Share deferral[1]	Target achievement level[2]	Total		
Hermann J. Merkens	2018	1,300,000	304,248	456,372	304,248	456,372	108.7 %	1,521,240	34,024	2,855,264
	2017	1,300,000	343,994	515,991	343,994	515,991	122.9 %	1,719,970	39,557	3,059,527
Marc Hess[3]	2018	220,000	40,329	60,493	40,329	60,493	100.0 %	201,644	3,244	424,888
	2017	–	–	–	–	–	–	–	–	–
Dagmar Knopek	2018	880,000	164,256	246,384	164,256	246,384	102.7 %	821,280	19,598	1,720,878
	2017	880,000	196,568	294,852	196,568	294,852	122.9 %	982,840	32,605	1,895,445
Christiane Kunisch-Wolff	2018	704,000	139,085	208,627	139,085	208,627	108.7 %	695,424	25,466	1,424,890
	2017	704,000	157,254	235,882	157,254	235,882	122.9 %	786,272	27,922	1,518,194
Thomas Ortmanns	2018	880,000	173,856	260,784	173,856	260,784	108.7 %	869,280	18,504	1,767,784
	2017	880,000	194,168	291,252	194,168	291,252	121.4 %	970,840	55,260	1,906,100
Christof Winkelmann	2018	704,000	139,085	208,627	139,085	208,627	108.7 %	695,424	70,329	1,469,753
	2017	704,000	159,174	238,762	159,174	238,762	124.4 %	795,872	24,062	1,523,934
Total	**2018**	**4,688,000**	**960,859**	**1,441,287**	**960,859**	**1,441,287**	**107.2 %**	**4,804,292**	**171,165**	**9,663,457**
	2017	**4,468,000**	**1,051,158**	**1,576,739**	**1,051,158**	**1,576,739**	**122.9 %**	**5,255,794**	**179,406**	**9,903,200**

[1] The deferrals shown are subject to the criteria on retention of variable remuneration components and penalty criteria, as set out above.
[2] 2018: excluding the positive non-recurring effect (negative goodwill) from the acquisition of Düsselhyp
[3] Marc Hess was appointed to the Management Board on 1 October 2018.

No benefits were granted to any member of the Management Board by third parties with respect to his/her Management Board activities during the year under review. Payments to former Management Board members of Aareal Bank AG and their surviving dependants totalled € 3.0 million (2017: € 2.9 million).

(Virtual) shareholdings of Management Board members and share-based remuneration

Within Aareal Bank's remuneration system for Management Board members, the reference value for 100% target achievement is slightly higher than the fixed annual salary that makes up the fixed remuneration component. Given that 50% of variable remuneration is disbursed in the form of virtual shares, Management Board members typically earn virtual shares amounting to more than 100% of the fixed component after two years of service. Provided that they also earn variable remuneration in subsequent years, the equivalent value of the virtual shares will not fall below this 100% threshold until the end of their term on the Management Board.

The following table shows the portion of the variable component attributable to share-based payment arrangements as well as the corresponding number of virtual shares granted in 2018 and 2017, respectively – as well as the number of virtual shares already held as at the reporting date:

		Share-based remuneration		Total quantity of virtual shares held (31 Dec)
	Year	Value (€)	Quantity (number)[1]	Quantity (number)
Hermann J. Merkens	2018	760,620	28,182	55,340
	2017	859,985	21,995	50,638
Mark Hess[2]	2018	100,822	3,736	–
	2017	–	–	–
Dagmar Knopek	2018	410,640	15,215	36,772
	2017	491,420	12,568	31,924
Christiane Kunisch-Wolff	2018	347,712	12,883	9,726
	2017	393,136	10,055	3,798
Thomas Ortmanns	2018	434,640	16,104	38,112
	2017	485,420	12,415	41,136
Christof Winkelmann	2018	347,712	12,883	7,659
	2017	397,936	10,177	2,389
Total	**2018**			**147,609**
	2017			**129,885**

[1] The stated number of virtual shares granted for 2018 is a preliminary figure, based on the price of Aareal Bank AG's share on 31 December 2018 (€ 26.99). The final conversion rate may only be determined after publication of preliminary results for 2018. The stated number of virtual shares granted for 2017 differs slightly from the previous year's figure since the former was calculated using a final conversion rate of € 39.10.

[2] Marc Hess was appointed to the Management Board on 1 October 2018.

Target remuneration granted

The following table shows the target remuneration (fixed annual salary and variable remuneration based on a 100 % target achievement) for the year under review, in accordance with sections 4.2.4 and 4.2.5 of the German Corporate Governance Code:

Remuneration granted	Hermann J. Merkens – Chairman of the Management Board			
	2017	2018	2018 (min)[1]	2018 (max)[2]
€				
Fixed remuneration	1,300,000	1,300,000	1,300,000	1,300,000
Ancillary benefits	39,557	34,024	34,024	34,024
Total	**1,339,557**	**1,334,024**	**1,334,024**	**1,334,024**
Variable remuneration based on a single-year assessment	280,000	280,000	–	420,000
Variable remuneration based on a multiple-year assessment				
Cash deferral 2018 (March 2024)	–	420,000	–	630,000
Share bonus 2018 (March 2019)	–	280,000	–	420,000
Share deferral 2018 (March 2024)	–	420,000	–	630,000
Cash deferral 2017 (March 2021)	420,000	–	–	–
Share bonus 2017 (March 2018)	280,000	–	–	–
Share deferral 2017 (March 2021)	420,000	–	–	–
Total	**1,400,000**	**1,400,000**	**–**	**2,100,000**
Benefit expense	726,347	847,178	847,178	847,178
Total remuneration	**3,465,904**	**3,581,202**	**2,181,202**	**4,281,202**

Remuneration granted	Marc Hess[3]			
	2017	2018	2018 (min)[1]	2018 (max)[2]
€				
Fixed remuneration	–	220,000	220,000	220,000
Ancillary benefits	–	3,244	3,244	3,244
Total	**–**	**223,244**	**223,244**	**223,244**
Variable remuneration based on a single-year assessment	–	40,329	–	60,493
Variable remuneration based on a multiple-year assessment				
Cash deferral 2018 (March 2024)	–	60,493	–	90,740
Share bonus 2018 (March 2019)	–	40,329	–	60,493
Share deferral 2018 (March 2024)	–	60,493	–	90,740
Cash deferral 2017 (March 2021)	–	–	–	–
Share bonus 2017 (March 2018)	–	–	–	–
Share deferral 2017 (March 2021)	–	–	–	–
Total	**–**	**201,644**	**–**	**302,466**
Benefit expense	–	148,056	148,056	148,056
Total remuneration	**–**	**572,944**	**371,300**	**673,766**

[1] Minimum amount of the remuneration component granted in the year under review
[2] Maximum amount of the remuneration component granted in the year under review
[3] Marc Hess was appointed to the Management Board on 1 October 2018.

Remuneration granted	**Dagmar Knopek**			
€	**2017**	**2018**	**2018 (min)**[1]	**2018 (max)**[2]
Fixed remuneration	880,000	880,000	880,000	880,000
Ancillary benefits	32,605	19,598	19,598	19,598
Total	**912,605**	**899,598**	**899,598**	**899,598**
Variable remuneration based on a single-year assessment	160,000	160,000	–	240,000
Variable remuneration based on a multiple-year assessment				
Cash deferral 2018 (March 2024)	–	240,000	–	360,000
Share bonus 2018 (March 2019)	–	160,000	–	240,000
Share deferral 2018 (March 2024)	–	240,000	–	360,000
Cash deferral 2017 (March 2021)	240,000	–	–	–
Share bonus 2017 (March 2018)	160,000	–	–	–
Share deferral 2017 (March 2021)	240,000	–	–	–
Total	**800,000**	**800,000**	**–**	**1,200,000**
Benefit expense	399,791	488,691	488,691	488,691
Total remuneration	**2,112,396**	**2,188,289**	**1,388,289**	**2,588,289**

Remuneration granted	**Christiane Kunisch-Wolff**			
€	**2017**	**2018**	**2018 (min)**[1]	**2018 (max)**[2]
Fixed remuneration	704,000	704,000	704,000	704,000
Ancillary benefits	27,922	25,466	25,466	25,466
Total	**731,922**	**729,466**	**729,466**	**729,466**
Variable remuneration based on a single-year assessment	128,000	128,000	–	192,000
Variable remuneration based on a multiple-year assessment				
Cash deferral 2018 (March 2024)	–	192,000	–	288,000
Share bonus 2018 (March 2019)	–	128,000	–	192,000
Share deferral 2018 (March 2024)	–	192,000	–	288,000
Cash deferral 2017 (March 2021)	192,000	–	–	–
Share bonus 2017 (March 2018)	128,000	–	–	–
Share deferral 2017 (March 2021)	192,000	–	–	–
Total	**640,000**	**640,000**	**–**	**960,000**
Benefit expense	697,851	422,142	422,142	422,142
Total remuneration	**2,069,773**	**1,791,608**	**1,151,608**	**2,111,608**

[1] Minimum amount of the remuneration component granted in the year under review
[2] Maximum amount of the remuneration component granted in the year under review

Remuneration granted	Thomas Ortmanns			
€	2017	2018	2018 (min)[1]	2018 (max)[2]
Fixed remuneration	880,000	880,000	880,000	880,000
Ancillary benefits	55,260	18,504	18,504	18,504
Total	**935,260**	**898,504**	**898,504**	**898,504**
Variable remuneration based on a single-year assessment	160,000	160,000	–	240,000
Variable remuneration based on a multiple-year assessment				
Cash deferral 2018 (March 2024)	–	240,000	–	360,000
Share bonus 2018 (March 2019)	–	160,000	–	240,000
Share deferral 2018 (March 2024)	–	240,000	–	360,000
Cash deferral 2017 (March 2021)	240,000	–	–	–
Share bonus 2017 (March 2018)	160,000	–	–	–
Share deferral 2017 (March 2021)	240,000	–	–	–
Total	**800,000**	**800,000**	**–**	**1,200,000**
Benefit expense	544,137	621,605	621,605	621,605
Total remuneration	**2,279,397**	**2,320,109**	**1,520,109**	**2,720,109**

Remuneration granted	Christof Winkelmann			
€	2017	2018	2018 (min)[1]	2018 (max)[2]
Fixed remuneration	704,000	704,000	704,000	704,000
Ancillary benefits	24,062	70,329	70,329	70,329
Total	**728,062**	**774,329**	**774,329**	**774,329**
Variable remuneration based on a single-year assessment	128,000	128,000	–	192,000
Variable remuneration based on a multiple-year assessment				
Cash deferral 2018 (March 2024)	–	192,000	–	288,000
Share bonus 2018 (March 2019)	–	128,000	–	192,000
Share deferral 2018 (March 2024)	–	192,000	–	288,000
Cash deferral 2017 (March 2021)	192,000	–	–	–
Share bonus 2017 (March 2018)	128,000	–	–	–
Share deferral 2017 (March 2021)	192,000	–	–	–
Total	**640,000**	**640,000**	**–**	**960,000**
Benefit expense	663,349	498,191	498,191	498,191
Total remuneration	**2,031,411**	**1,912,520**	**1,272,520**	**2,232,520**

[1] Minimum amount of the remuneration component granted in the year under review
[2] Maximum amount of the remuneration component granted in the year under review

Remuneration paid

The following table shows the remuneration disbursed in the year under review, as defined in sections 4.2.4 and 4.2.5 of the German Corporate Governance Code. It also outlines disbursements under variable remuneration components related to multiple years which expired during the year under review:

Remuneration paid	Hermann J. Merkens Chairman of the Management Board		Marc Hess[1]		Dagmar Knopek		Christiane Kunisch-Wolff	
	2018	2017	2018	2017	2018	2017	2018	2017
€								
Fixed remuneration	1,300,000	1,300,000	220,000	–	880,000	880,000	704,000	704,000
Ancillary benefits	34,024	39,557	3,244	–	19,598	32,605	25,466	27,922
Total	**1,334,024**	**1,339,557**	**223,244**	**–**	**899,598**	**912,605**	**729,466**	**731,922**
Variable remuneration based on a single-year assessment	343,994	377,720	–	–	196,568	212,320	157,254	135,309
Variable remuneration based on a multiple-year assessment								
Cash deferral 2014 (April 2018)	103,957	–	–	–	103,711	–	–	–
Cash deferral 2015 (April 2018)	151,605	–	–	–	107,621	–	–	–
Cash deferral 2016 (April 2018)	189,653	–	–	–	106,606	–	67,939	–
Share bonus 2014 (April 2018)	199,945	–	–	–	199,471	–	–	–
Share deferral 2012 (April 2018)	249,699	–	–	–	–	–	–	–
Share deferral 2013 (April 2018)	135,779	–	–	–	79,204	–	–	–
Share deferral 2014 (April 2018)	100,872	–	–	–	100,633	–	–	–
Cash deferral 2013 (April 2017)	–	112,727	–	–	–	65,757	–	–
Cash deferral 2014 (April 2017)	–	103,030	–	–	–	102,785	–	–
Cash deferral 2015 (April 2017)	–	150,686	–	–	–	106,969	–	–
Share bonus 2013 (April 2017)	–	239,867	–	–	–	139,922	–	–
Share deferral 2012 (April 2017)	–	222,358	–	–	–	–	–	–
Share deferral 2013 (April 2017)	–	121,816	–	–	–	71,060	–	–
Dividends	138,349	101,276	–	–	91,929	63,848	24,316	7,595
Total	**1,613,853**	**1,429,480**	**–**	**–**	**985,743**	**762,661**	**249,509**	**142,904**
Benefit expense	847,178	726,347	148,056	–	488,691	399,791	422,142	697,851
Total remuneration	**3,795,055**	**3,495,384**	**371,300**	**–**	**2,374,032**	**2,075,057**	**1,401,117**	**1,572,677**

[1] Marc Hess was appointed to the Management Board on 1 October 2018.

Remuneration paid	Thomas Ortmanns		Christof Winkelmann		Dr Wolf Schumacher[2]		Dirk Große Wördemann[3]	
	2018	2017	2018	2017	2018	2017	2018	2017
€								
Fixed remuneration	880,000	880,000	704,000	704,000	–	–	–	–
Ancillary benefits	18,504	55,260	70,329	24,062	–	–	–	–
Total	**898,504**	**935,260**	**774,329**	**728,062**	**–**	**–**	**–**	**–**
Variable remuneration based on a single-year assessment	194,168	213,600	159,174	85,120	–	–	–	–
Variable remuneration based on a multiple-year assessment								
Cash deferral 2014 (April 2018)	103,135	–	–	–	181,493	–	–	–
Cash deferral 2015 (April 2018)	106,973	–	–	–	139,658	–	–	–
Cash deferral 2016 (April 2018)	107,249	–	42,739	–	–	–	–	–
Share bonus 2014 (April 2018)	198,365	–	–	–	349,075	–	–	–
Share deferral 2012 (April 2018)	249,699	–	–	–	421,271	–	202,720	–
Share deferral 2013 (April 2018)	135,779	–	–	–	229,075	–	–	–
Share deferral 2014 (April 2018)	100,075	–	–	–	176,108	–	–	–
Cash deferral 2013 (April 2017)	–	112,727	–	–	–	190,184	–	–
Cash deferral 2014 (April 2017)	–	102,215	–	–	–	179,875	–	–
Cash deferral 2015 (April 2017)	–	106,325	–	–	–	138,812	–	–
Share bonus 2013 (April 2017)	–	239,867	–	–	–	404,684	–	–
Share deferral 2011 (April 2017)	–	–	–	–	–	–	–	238,390
Share deferral 2012 (April 2017)	–	222,358	–	–	–	375,143	–	180,523
Share deferral 2013 (April 2017)	–	121,816	–	–	–	205,519	–	–
Dividends	95,279	82,271	19,149	4,778	88,048	111,251	–	10,369
Total	**1,290,722**	**1,201,179**	**221,062**	**89,898**	**1,584,728**	**1,605,468**	**202,720**	**429,282**
Benefit expense	621,605	544,137	498,191	663,349	–	–	–	–
Total remuneration	**2,810,831**	**2,680,576**	**1,493,582**	**1,481,309**	**1,584,728**	**1,605,468**	**202,720**	**429,282**

[1] Dr Wolf Schumacher resigned with effect from 30 September 2015. [2] Dirk Große Wördemann resigned with effect from 31 May 2013.

Pensions

	2018			2017		
	Pension claims p.a.[1]	Balance of pension obligations (IFRS) as at 31 Dec 2018	Increase of pension obligations (IFRS) in 2018	Pension claims p.a.[1]	Balance of pension obligations (IFRS) as at 31 Dec 2017	Increase of pension obligations (IFRS) in 2017
€ 000's						
Hermann J. Merkens	307	7,270	847	285	6,422	726
Marc Hess[2]	37	148	148	–	–	–
Dagmar Knopek	134	2,510	489	113	2,021	400
Christiane Kunisch-Wolff	118	1,172	422	116	750	698
Thomas Ortmanns	280	6,357	622	267	5,735	544
Christof Winkelmann	115	1,228	498	113	730	663
Total	**991**	**18,685**	**3,026**	**894**	**15,658**	**3,031**

[1] Pension claims are calculated based on the earliest possible pension payment.
[2] Marc Hess was appointed to the Management Board on 1 October 2018.

Service cost (in accordance with IFRSs) incurred in the 2018 financial year in connection with the pension claims of members of the Management Board totalled € 2.7 million (2017: € 2.8 million). The pension obligations for current members of the Management Board as well as for former members of the Management Board and their surviving dependants increased by € 2.8 million in the year under review (2017: € 2.4 million). The total amount of pension obligations was € 51.5 million (2017: € 48.7 million). Of that amount, € 32.8 million related to former members of the Management Board and their surviving dependants (2017: € 33.1 million).

Remuneration system for members of the Supervisory Board

Remuneration for the services of the Supervisory Board members is specified in Article 9 of the Memorandum and Articles of Association of Aareal Bank AG. The remuneration system for the Supervisory Board only comprises a fixed remuneration, supplemented by a compensation for attending meetings. Where membership in the Supervisory Board falls short of an entire financial year, said remuneration shall be paid on a pro rata temporis basis. Furthermore, the Supervisory Board members will be reimbursed for their expenses. Any value-added tax invoiced will also be deemed to be a refundable expense.

The fixed remuneration is € 50,000 p.a. for each Supervisory Board member. The Chairman of the Supervisory Board shall receive three times this amount, while the deputies shall receive one and a half times as much as a normal member. The fixed remuneration is increased for each membership in a committee (with the exception of the Committee for Urgent Decisions, which is part of the Risk Committee).

This additional fixed remuneration amounts to € 20,000 p.a. for membership of the Risk Committee and the Audit Committee; fixed remuneration is increased by € 40,000 p.a. for the chairmanship of one of these committees.

The additional fixed remuneration amounts to € 15,000 p.a. for membership of the other Supervisory Board committees; fixed remuneration is increased by € 30,000 p.a. for the chairmanship of one of these committees.

The meeting attendance compensation amounts to € 1,000 for each meeting attended (except for the Committee for Urgent Decisions).

The remuneration for any financial year shall be due and payable one month after the end of the respective financial year.

Supervisory Board remuneration

€	Year	Fixed remuneration	Attendance fees	Total remuneration
Marija Korsch Chairman	2018	265,000	36,000	301,000
	2017	265,000	33,000	298,000
Prof. Dr Stephan Schüller Deputy Chairman	2018	125,000	27,000	152,000
	2017	125,000	25,000	150,000
Dieter Kirsch, Deputy Chairman (31 March to 31 December 2018)	2018	100,000	20,000	120,000
	2017	85,000	17,000	102,000
York-Detlef Bülow Deputy Chairman (until 31 March 2018)	2018	31,250	9,000	40,250
	2017	125,000	24,000	149,000

>

€	Year	Fixed remuneration	Attendance fees	Total remuneration
Thomas Hawel	2018	65,000	12,000	77,000
	2017	65,000	10,000	75,000
Petra Heinemann-Specht (from 1 April 2018)	2018	52,500	10,000	62,500
	2017	–	–	–
Richard Peters	2018	100,000	23,000	123,000
	2017	100,000	21,000	121,000
Dr Hans-Werner Rhein	2018	85,000	16,000	101,000
	2017	85,000	15,000	100,000
Sylvia Seignette	2018	90,000	13,000	103,000
	2017	90,000	10,000	100,000
Elisabeth Stheeman[1]	2018	85,000	17,000	102,000
	2017	85,000	14,000	99,000
Hans-Dietrich Voigtländer	2018	115,000	26,000	141,000
	2017	115,000	24,000	139,000
Prof. Dr Hermann Wagner	2018	110,000	19,000	129,000
	2017	110,000	16,000	126,000
Beate Wollmann	2018	65,000	12,000	77,000
	2017	50,000	6,000	56,000
Total	**2018**	**1,288,750**	**240,000**	**1,528,750**
	2017	**1,300,000**	**215,000**	**1,515,000**

[1] Income tax plus solidarity surcharge for the Supervisory Board member subject to limited tax liability was declared pursuant to section 50a (1) no. 4 of the German Income Tax Act (Einkommensteuergesetz – "EStG"), and paid to the German Central Tax Offfice (Bundeszentralamt für Steuern, BZSt).

Remuneration system for employees

When it comes to the structure of the remuneration system for employees, a general distinction is made between three groups of employees. First of all, Aareal Bank has employees whose remuneration is governed by collective agreements. Then, there are employees whose remuneration is not governed by collective agreements. These employees who are not covered by collective agreements are then split into two further groups. First, there are those employees whose duties have a material impact on the overall risk profile of Aareal Bank (risk takers) or of Aareal Bank Group (Group risk takers). The variable remuneration paid to these "risk takers" is subject to very stringent regulatory requirements. The other employees who are not covered by collective agreements and are not risk takers either are not subject to these provisions and make up the third group.

The report below starts by explaining the remuneration system for risk takers and then addresses the differences compared with the other groups.

Remuneration system for risk takers

In order to identify those employees who are classed as "risk takers", Aareal Bank carries out an annual independent risk analysis, identifying the employees in question based on a uniform set of criteria.

The remuneration system for risk takers is subject to the same basic conditions as the remuneration system for Management Board members, and is also aligned with the business and risk strategy of Aareal Bank AG and Aareal Bank Group respectively. As is the case with the Management Board remuneration, risk takers receive both fixed and variable remuneration. The fixed component comprises a fixed annual salary and ancillary benefits.

Performance-related variable remuneration

Remuneration parameters and target level weighting

As with the Management Board members, the variable remuneration is measured based on targets derived from the corporate strategy. One difference compared with the Management Board system is that the assessment period for the target achievement is one year. The targets set for risk takers are split into three components that are added together, as is the case for the remuneration paid to the Management Board: a Group component, an organisational unit component (referring to the organisational unit that the risk taker works for) and an individual component (individual target achievement). The performance of the organisational unit for divisions allocated to Sales is measured using the Structured Property Financing segment operating profit, as well as in terms of risk weighted assets. The performance of the Housing Industry division is measured by reference to the segment operating profit of the Consulting/Services segment. The other organisational units, i.e. in particular central staff functions and control units, as well as the Treasury division, are measured based on their cost target. The remuneration system also takes account of the risk taker's position in the organisation's hierarchy, reflecting the influence that he/she can exert over the Group's/Bank's success. This results in differences in the weightings attached to the three additive components depending on an individual's responsibility within the Company. The weighting assigned to the Group and organisational unit components, for example, gradually increases from 15 % and 25 % to 25 % and 35 % respectively, while the weighting assigned to the individual component can be reduced from 60 % to 40 % at the same time. For further information on the individual targets and possible resulting KPIs, please refer to the information on Management Board remuneration.

Deferred disbursement, through retention of variable remuneration components and virtual shares

To ensure that the remuneration system provides long-term incentives, the initial value for variable remuneration – as determined according to the principles set out above – is generally paid out on a deferred basis after the end of the financial year. The payout terms are based on those that apply to the Management Board remuneration system but once again vary depending on the risk taker's position within the organisational structure.

60 % of the variable remuneration paid to risk takers assigned to the management level below the Management Board is subject to a five-year deferral period. As with the variable Management Board remuneration, 50 % each of deferred and non-deferred components are converted into virtual shares that are held for a minimum period of one year. Unlike with the Management Board remuneration system, risk takers can, however, opt to select when they want their virtual shares to be converted into cash after the end of the one-year holding period, selecting a conversion date that falls within a period of up to three years.

By contrast, 40 % of the variable remuneration paid to the other risk takers is subject to deferral over a period of three years.

All other aspects relating to the calculation of virtual shares are explained in the section on the Management Board remuneration system.

Ex-post review of target achievement and behaviour of the risk takers

As in the Management Board remuneration system, the original target achievement level is back-tested and, where appropriate, reduced before virtual shares are paid out/granted. Penalty-triggering events can also result in reductions, in the forfeiture of the variable remuneration entitlement in full and, as a result, also in variable remuneration that has already been paid out being clawed back. Details can be found in the information on the Management Board remuneration system.

Remuneration system for employees covered by, and exempt from, collective agreements who are not classed as risk takers

Employees who are not risk takers also receive variable remuneration. The variable remuneration paid to those employees whose remuneration is governed by a collective agreement is based on an annual appraisal. The initial value for measuring the variable remuneration corresponds to 0.75 gross monthly salaries for employees covered by a collective agreement. The variable remuneration paid to those employees who are not covered by a collective agreement is based on contractually agreed target-variable remuneration and is measured based on an annual overall appraisal that also takes the target achievement level for the individual targets that have been set for the employee in question into account.

Restrictions and link to risk-bearing capacity for all employee remuneration systems

All employee remuneration systems feature provisions corresponding to those found in the Management Board remuneration system regarding the impact of special external conditions (modifiers). In cases involving risk takers, the ban on hedging also applies. There are, however, differences with regard to the caps and the safeguarding of the risk-bearing capacity. The contracts of employment with those employees below Management Board level do not include contractual provisions on severance pay.

Caps and proportion of variable remuneration

For risk takers, the target achievement level for the Group component and the organisational component is capped at 150 %. The individual targets are capped at a target achievement level of 200 %. If the individual target achievement level is 0 %, no variable remuneration is paid at all. Performance of virtual shares is capped at 300 %. For non-risk takers whose variable remuneration is determined based on an appraisal and, where appropriate, individual targets, the variable compensation is also limited to 200 % in relation to the target achievement level.

In order to comply with the requirements set out in section 25a (5) KWG, the reference value for the variable remuneration in cases involving a target achievement level of 100 % generally corresponds to a maximum of 50 % of the fixed remuneration. This means that, even if an employee achieves the maximum target achievement level, the variable remuneration does not exceed the fixed remuneration. Consequently, if an employee receives fixed annual remuneration of € 100,000, for example, the reference value for the variable remuneration paid out if that employee achieves 100 % target achievement is limited to a maximum of € 50,000. It is very common, however, for variable remuneration to account for a smaller proportion of an employee's total remuneration.

In 2014, the Annual General Meeting of Aareal Bank AG approved exemptions from this 1:1 rule for certain groups of employees. In order to ensure that the remuneration paid by Aareal Bank AG and its international subsidiaries is competitive in an international comparison, employees working in international sales at Aareal Bank AG, as well as executives and employees working for the subsidiaries Aareal Capital Corporation, New York, and Aareal Bank Asia Ltd., Singapore, have to be paid remuneration in line with local market standards. This applies to fewer than 25 positions.

Consideration of corporate performance and risk-bearing capacity

Both the variable remuneration paid to risk-takers and the variable remuneration paid to non-risk takers take account of the Company's performance.

The variable remuneration paid to non-risk takers is initially calculated, for the assessment year in question, as the total of all variable remuneration paid to non-risk takers in the event of a target achievement level of 105 % (hereinafter referred to as the "bonus pool") as part of a two-step procedure, with the first step (30 %) also taking the operating profit and RWA into account. The variable remuneration to be paid out to non-risk takers cannot exceed the bonus pool, which is to be calculated on an annual basis. If the relevant lower thresholds for RWA and operating profit set out in the recovery plan for the corresponding assessment year are reached or undercut, then the first step is dispensed with entirely and the bonus pool volume corresponds to a maximum of 70 % from the second step. In such cases, due to the struc-

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ture of the model, the variable remuneration paid to risk-takers results in a reduction in the Group component, or in the Group component ceasing to apply, anyway.

The bonus pool volume referred to above for non-risk takers can be restricted further or reduced to zero if the corresponding thresholds set out in the recovery plan are undercut further, or if the corresponding lower thresholds are met. If a threshold is only undercut for a brief period, the Management Board can opt not to reduce the bonus pool. The Management Board can make the same decision for the variable remuneration paid to risk-takers or can also opt to reduce the variable remuneration to be distributed.

If the total amount of variable remuneration available for distribution is to be reduced, the variable remuneration to be paid out to the employees is reduced by the same proportion.

In all other respects, the provisions on risk-bearing capacity explained in the section on the Management Board system (see risk-bearing capacity, and parallel interest with shareholders) apply accordingly.

Amendments to the remuneration systems last year

In order to implement the new requirements set out in the German Regulation on Remuneration in Financial Institutions, the deferral period for the variable remuneration payable to risk takers assigned to the management level below the Management Board was increased from three to five years and a clawback rule was agreed. Provisions were also developed stating that no interest or dividends can be paid on deferred remuneration components.

Reporting on quantitative disclosure requirements

This report only covers the qualitative disclosure requirements regarding employee remuneration set out in Article 450 of the EU's Capital Requirements Regulation 2013/575 (CRR) and section 16 InstitutsVergV. The quantitative disclosure requirements relating to the provisions set out above are published in a separate report entitled "Disclosure of Remuneration Indicators", which can be found on the website of Aareal Bank AG. This report is made available within six months of the end of the financial year. www.aareal-bank.com/en/investors-portal/finance-information/regulatory-disclosures/archive/2018/

Remuneration governance

Governance of Supervisory Board remuneration

The role of the Annual General Meeting

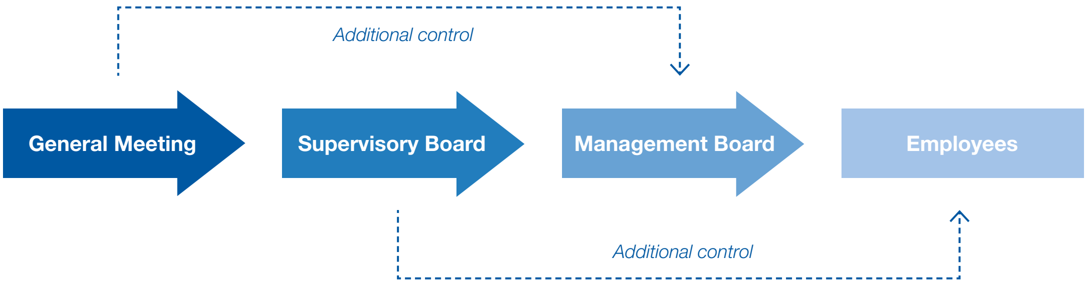
Given the Supervisory Board's role as a supervisory body, remuneration for its members must not provide any incentives which would counter this surveillance function. The Annual General Meeting (AGM) determines the remuneration of the Supervisory Board, in Aareal Bank AG's Memorandum and Articles of Association; the AGM therefore also resolves on any adjustments to Supervisory Board remuneration (cf. Article 9 (4) and (5) of the Memorandum and Articles of Association).

Implementing the Second Shareholder Rights Directive, from the financial year 2020 onwards, the AGM will need to discuss Supervisory Board remuneration at least every four years, even without any concrete proposals for amendments, and will need to resolve whether it still approves it.

The role of the Supervisory Board

The Supervisory Board shall review the appropriateness of remuneration for its members at least once a year. Every four years, it shall retain an external remuneration advisor to obtain an opinion as to the appropriateness of its remuneration – and especially, on whether remuneration is in line with common practice and comparable. The Supervisory Board shall present the results of this review as part of its report to the AGM. Where appropriate, the Supervisory Board will prepare recommendations for adjustments to its remuneration, and will submit them to shareholders at the next AGM.

Determination and control of remuneration systems



Governance of Management Board remuneration

The role of the Supervisory Board

The Supervisory Board shall act in the Company's interests; accordingly, it shall ensure that Management Board remuneration is geared towards the Company's sustainable development (cf. section 87 of the AktG). The Supervisory Board decides on Management Board remuneration, monitors appropriateness, defines targets for determining variable remuneration, and decides on target achievement. During the seven years following determination of variable remuneration, the Supervisory Board shall review, within the framework of backtesting/penalty reviews, whether variable remuneration determined originally must be adjusted or reclaimed (clawback).

As part of examining appropriateness of Management Board remuneration, the Supervisory Board shall review whether the remuneration system for the Management Board (as well as the corresponding targets for Management Board members derived therefrom) is consistent with the Company's business and risk strategies, the objectives derived from these strategies, the corresponding risk management, as well as with the defined risk appetite and the corporate values. As further elements of this examination of appropriateness, a vertical comparison with the average remuneration of relevant employees and the top management level below the Management Board is to be carried out, as well as a horizontal comparison with the remuneration of management board members of comparable enterprises. These components reflect the orientation of Management Board remuneration towards sustainable Company development, meaning that remuneration is aligned with the long-term interests of Aareal Bank's stakeholders.

When taking decisions concerning the structure of the remuneration system for the Management Board, the Supervisory Board shall take the views of Aareal Bank AG's relevant shareholders and of proxy advisors into account.

The role of the Remuneration Control Committee

The Remuneration Control Committee supports the Supervisory Board in its monitoring duties and prepares the plenary meeting's resolutions concerning remuneration. The Committee monitors the appropriateness of the structure of Management Board remuneration, proposes targets for variable remuneration and for target achievement at the end of the year, and also monitors the levels of target achievement during the course of each year. Moreover, the Committee assesses the effects of the remuneration systems on the Group's risk, capital and liquidity management. In the run-up to determining remuneration, in cooperation with the Audit Committee, it reviews whether there are any backtesting or penalty-triggering events which may result in a reduction of variable remuneration.

The role of the Risk Committee

The duties of the Risk Committee with regard to remuneration are unaffected by the assessment by the Remuneration Control Committee, as set out above. The Risk Committee verifies whether the incentives created by the remuneration system take the Company's risk, capital and liquidity structure into account, as well as the probability and timing of income.

The role of the Audit Committee

Circumstances where variable remuneration may be reduced may occur where Management Board members fail to fulfil any of their duties, or where they breach external or internal requirements. To the extent that any such events have occurred, these are identified in the reports prepared by Compliance, addressed to the Audit Committee as well as to the plenary meeting of the Supervisory Board. Internal conduct rules are also defined in a Code of Conduct which must be presented to the Audit Committee at least once a year.

The role of the Annual General Meeting

Under current legislation, Management Board remuneration may be submitted to the AGM for approval. In line with its own understanding of good corporate governance, Aareal Bank makes such submission in the event of any material changes to the remuneration system for the Management Board. Implementation of the Second EU Shareholder Rights Directive (2017/828 (EU)) will require a mandatory submission at least every four years, from 2020 onwards. The Supervisory Board of Aareal Bank will give due consideration to the vote of the AGM.

Governance of staff remuneration

The role of the Management Board

The Management Board is responsible for structuring the remuneration system for employees. As an element of appropriate and effective risk management, staff remuneration is monitored as to whether it is consistent with the corporate and risk culture, and with Aareal Bank's risk appetite. Especially with respect to the remuneration of material risk takers, the Management Board will take care to adjust remuneration parameters to such employees' influence on the Bank's risk exposure.

The role of the Supervisory Board/ the Remuneration Control Committee/ the Risk Committee

The Supervisory Board and its Remuneration Control Committee monitor the structure of staff remuneration. In this context, the Remuneration Control Committee also assesses the criteria for, and the actual selection of, Aareal Bank Group's material risk takers. Together with the Risk Committee, and in line with the rules for Management Board remuneration, the Remuneration Control Committee monitors whether the remuneration system for employees is consistent with the Company's business and risk strategies, the objectives derived from these strategies, its risk appetite and the risk management.

Further information on the Supervisory Board and its committees

The composition and responsibilities of the Supervisory Board committees, and of the plenary meeting, are described in the Corporate Governance Statement/the Corporate Governance Report and in the Notes to the consolidated financial statements.

The Supervisory Board presents the remuneration-related activities of its plenary meetings and of its committees as part of its report to the AGM. This report also provides details regarding the number of meetings, and on attendance of the members of the Supervisory Board and its committees.

The role of the Remuneration Officer

Following consultation of the Supervisory Board, the Management Board of Aareal Bank AG shall appoint a Remuneration Officer in order to ensure appropriate, sustained and effective monitoring of staff remuneration. Aareal Bank has appointed a

Remuneration Officer, to carry out duties in accordance with section 24 of the InstitutsVergV. These duties include supporting the Supervisory Board and the Remuneration Control Committee in structuring and monitoring the remuneration system. The Remuneration Officer is obliged to respond to queries of the Remuneration Control Committee's Chairman.

The Remuneration Officer reports on the appropriate structure of the remuneration systems for employees in the form of a Remuneration Report at least once a year. Due to the responsibility of monitoring the appropriateness of the remuneration systems on a continuing basis, the Remuneration Officer is being included in the conceptional new drafting (and future development), as well as in the application of the remuneration systems. In particular, the Remuneration Officer plays an active part in the process for the determination of the total amount available for variable remuneration, the annual review of penalty rules, the regular (at least spot checks) review of appropriate compliance structures, the monitoring of the hedging ban (and potential violations), the drafting of the annual remuneration report (pursuant to section 16 of the InstitutsVergV in connection with Article 450 of the CRR) as well as the review of the risk taker analysis.

Involvement of external remuneration advisors

As a matter of principle, the executive bodies of Aareal Bank decide upon remuneration themselves; they also come to an independent assessment of appropriateness. Especially for the purpose of examining whether remuneration is in line with common practice, compared with other companies, Aareal Bank retains external remuneration advisors such as hkp Deutschland GmbH.

Explanatory Report of the Management Board on Takeover Disclosures in Accordance with Section 315a (1) of the German Commercial Code (Handelsgesetzbuch – "HGB")

Composition of subscribed capital, and rights and obligations attached to shares

The composition of Aareal Bank AG's subscribed capital is shown in Note 60 ("Equity") to the consolidated financial statements. Each share casts one vote at a General Meeting. There are no shares with special rights granting supervisory powers to any shareholder or shareholder group. The Company currently does not hold any treasury shares, which would not be entitled to vote.

Restrictions affecting voting rights or the transfer of shares

The transfer and exercise of voting rights is governed exclusively by legal restrictions. Voting rights are not limited to a certain number of shares, or of votes. All shareholders who have registered to attend a General Meeting in good time, and who have provided the Company with evidence of their shareholding and their right to vote, are entitled to attend the General Meeting, and to exercise their voting rights from all shares held and so registered. The exercise of voting rights from the shares concerned is precluded by law in the cases where section 136 of the German Public Limited Companies Act (Aktiengesetz – "AktG") applies. Where the Company holds treasury shares, section 71b of the AktG prohibits the exercise of rights vested in such shares. We are not aware of any other restrictions affecting voting rights or the transfer of shares.

Shareholdings exceeding 10 % of voting rights

Details regarding any shareholdings exceeding 10 % of voting rights are provided in Note 82 to the consolidated financial statements.

Shares with special rights granting the holder supervisory powers

Aareal Bank AG's Memorandum and Articles of Association do not grant any shareholder the right to nominate members to the Supervisory Board, nor are there any other shares with special rights granting the holder supervisory powers.

Type of control of voting rights regarding shares held by employees with their rights of control not being directly exercised

There are no Aareal Bank AG shares held by employees where the rights of control cannot be directly exercised.

Statutory provisions, and provisions in the Memorandum and Articles of Association regarding the appointment and removal of members of the Management Board, and regarding amendments to the Memorandum and Articles of Association

The appointment and removal of members of the Management Board of Aareal Bank AG is carried out in accordance with sections 84 and 85 of the AktG and Article 7 of the Memorandum and Articles of Association, according to which the Management Board must have a minimum of two members. The Supervisory Board shall appoint the Members of the Management Board and determine their number. The Supervisory Board may appoint deputy members, and may appoint one member of the Management Board to be the Chairman of the Management Board. The members of the Management Board are appointed for a maximum term of five years. This term of office may be renewed or extended for a maximum of five years in each case.

Pursuant to section 179 of the AktG, the Memorandum and Articles of Association may be amended by way of resolution passed by the General Meeting. Resolutions of the General Meeting regarding amendments to the Memorandum and Articles of Association are passed by a simple majority of the votes cast, or – to the extent permitted by law – by the majority of the issued share capital present at the Meeting. In accordance with section 181 (3) of the AktG, such amendments become effective upon their entry in the Commercial Register. In the event of a capital change, the Supervisory Board is authorised to modify the wording of the Articles of Association in line with the amount of the capital change (Article 5 (7) of the Memorandum and Articles of Association).

Authorisation of the Management Board to issue or repurchase shares

Authorised capital

The Annual General Meeting held on 31 May 2017 resolved to authorise the Management Board to increase, on one or more occasions, the Company's share capital, subject to the approval of the Supervisory Board, by up to a maximum total amount of € 89,785,830 by issuance of new shares for contribution in cash or in kind; the Management Board is also authorised, within defined limits, to disapply pre-emptive rights, given the fulfilment of certain conditions. This authorisation will expire on 30 May 2022. When exercising this authorisation, the Management Board will restrict the exclusion of shareholders' pre-emptive rights to a total of 20 % of the Company's share capital – including treasury shares and any shares issued during the term of this authorisation, under the authorisation under agenda item no. 6 of the Annual General Meeting held on 21 May 2014. The authorised capital has not been utilised to date.

Conditional capital

Based on a resolution passed by the General Meeting on 21 May 2014, the Management Board was authorised to issue, on one or more occasions until 20 May 2019, profit-participation rights with a limited or unlimited term for contribution in cash or in kind in a total nominal amount of € 1,000,000,000. Holder or creditor conversion rights may be attached to such profit-participation rights, provided they are not issued against contribution in kind. Conversion rights may be attached exclusively to no-par value bearer shares and are limited to a maximum amount of € 89,785,830 of the Company's share capital. Issuance of profit-participation rights may also be effected by domestic or foreign enterprises in which the Company either directly or indirectly holds a majority interest. In such cases, the Company may itself assume guarantees and offer shares of Aareal Bank AG, subject to the approval of the Supervisory Board, in order to meet the resulting conversion rights. Subject to the approval of the Supervisory Board, the Management Board may exclude shareholders' pre-emptive rights in relation to the profit-participation rights in certain cases.

The issued share capital is subject to a conditional capital increase not exceeding € 89,785,830 by issuance of up to 29,928,610 new no-par value bearer shares ("Conditional Capital 2014"). The conditional capital increase shall be implemented only insofar as (i) the holders or creditors of conversion rights from convertible profit-participation rights issued by the Company (or by an enterprise in which the Company either directly or indirectly holds a majority interest) until 20 May 2019 on the basis of the Annual General Meeting's authorisation resolution of 21 May 2014 exercise their conversion rights or (ii) the holders or creditors of convertible profit-participation rights issued by the Company (or by an enterprise in which the Company either directly or indirectly holds a majority interest) until 20 May 2019 on the basis of the Annual General Meeting's authorisation resolution of 21 May 2014 and who are obliged to exercise those rights fulfil their obligation or (iii) the Company makes use of alternative performance; insofar as treasury shares are not used to service the rights or, in the aforementioned cases (i) and (ii), no cash compensation is granted. The new shares shall be entitled to a share in the profits from the beginning of the financial year in which they come into existence through the exercise of conversion rights or the fulfilment of conversion obligations. The Management Board is authorised to determine the details of the conditional capital increase.

Authorisation to purchase treasury shares

The General Meeting held on 20 May 2015 authorised the Management Board, pursuant to section 71 (1) no. 7 of the AktG, to purchase and sell treasury shares for the purposes of securities trading, at a price not falling below or exceeding the average closing price of the Company's share in Xetra trading (or a comparable successor system) during the three trading days on the Frankfurt Stock Exchange prior to the relevant transaction by more than 10 %. This authorisation expires on 19 May 2020. The volume of shares acquired for this purpose must not exceed 5 % of the issued share capital of Aareal Bank AG at the end of any given day.

Furthermore, the General Meeting held on 20 May 2015 authorised the Management Board, pursuant to section 71 (1) no. 8 of the AktG, to purchase treasury shares with a volume of up to 10 % of the issued share capital for purposes other than securities trading. This authorisation expires on 19 May 2020. Such purchases may be effected via stock exchanges or public purchase offers made to all shareholders, taking into account the prices as specified in the respective Annual General Meeting's resolution, which are in turn based on the Company's stock exchange share price. The authorisation may be exercised on one or more occasions, covering partial amounts or the total amount.

Subject to the approval of the Supervisory Board, the shares acquired under this or an earlier authorisation may be sold outside stock exchanges and without an offer to all shareholders, thereby excluding shareholders' pre-emptive rights, provided that the shares sold do not exceed the threshold value of 10 % of the Company's share capital and that the issue price is not significantly lower than the stock exchange price, or if the sale of such shares is made against contribution in kind, or if the shares are given to the holders of conversion or option rights, even if they had been issued by subsidiaries. The treasury shares may also be given to the holders of conversion or option rights in lieu of new shares from a contingent capital increase. The shares can also be withdrawn, without such a withdrawal or its implementation requiring a further resolution by the General Meeting.

The Management Board was also authorised to effect the acquisition of treasury shares by using put or call options. However, any and all share purchases involving the use of derivatives shall be limited to a maximum threshold value of 5 % of the Company's share capital. In addition, any acquisition of shares shall count towards the 10 % threshold for the authorisation for the acquisition of treasury shares. Where treasury shares are acquired using equity derivatives, the shareholders' right to enter into any option transactions with the Company is excluded in analogous application of section 186 (3) sentence 4 of the AktG.

Material agreements which are subject to change of control clauses triggered in the event of a takeover offer

There are no material agreements which are subject to change of control clauses triggered in the event of a takeover offer. Any public offers to acquire the Company's shares are governed exclusively by the law (including the provisions of the German Securities Acquisition and Takeover Act), and the Memorandum and Articles of Association.

Compensation agreements entered into with members of the Management Board or employees in the event of a takeover offer

For details regarding compensation agreements entered into with members of the Management Board or employees in the event of a takeover bid, please refer to the Remuneration Report, which forms part of the Group Management Report.

Consolidated Non-financial Statement

The Combined Separate Non-financial Report pursuant to sections 289b (3) and 315b (3) of the HGB has been published on the Company's website, on www.aareal-bank.com/en/responsibility/reporting-on-our-progress/.

Corporate Governance Statement

Since Aareal Bank AG is the only listed Group entity, and also the Group's parent undertaking, only one Corporate Governance Statement will be issued.

The full Corporate Governance Statement pursuant to sections 289f and 315d of the HGB is publicly available on the Company's website (www.aareal-bank.com/en/about-us/corporate-governance/), and in the "Transparency" section of the Group Annual Report.