ANNUAL REPORT AAREAL BANK AG 2007

2007

Aareal Bank

KEY FIGURES

	2007	2006	Change	Change
Income Statement	**€ mn**	**€ mn**	**€ mn**	
Operating profit	80	107	-27	
Profit before taxes	273	179	94	
Net income	285	117	168	
Portfolio data (31 December)	**€ mn**	**€ mn**	**€ mn**	**%**
Property financing	22,265	20,573	1,692	8
of which: international	16,481	13,932	2,549	18
Shareholders' equity	1,553	1,289	264	20
Total assets	41,335	39,513	1,822	5

	31 Dec 2007	31 Dec 2006
Rating		
Fitch Ratings, London		
Long-term	A-	A-
Short-term	F2	F2

MANAGEMENT REPORT

Dear shareholders, business associates and Aareal Bank employees,

The 2007 financial year marks a milestone in the history of Aareal Bank AG, the parent company of the Aareal Bank Group. Thanks to the early completion of our six-point programme, we concluded our strategic realignment ahead of schedule. This allowed us to successfully embark upon our growth programme "FUTURE 2009" in April 2007. Our clearly-defined focus on two core business segments – Structured Property Financing and Consulting / Services – is bearing fruit: at € 285 million, including non-recurring effects, Aareal Bank AG posted the best annual result in its corporate history. Aareal Bank Group coped well with the impact of the US sub-prime crisis on global credit markets. This clearly shows that we are holding our course, even in a challenging market environment.

Business and environment

Corporate structure and business activities

Aareal Bank Group is one of the leading international specialist property banks and a provider of finance. It also provides advisory and other services to the commercial property and institutional housing sectors, and supports German and international clients as a financing partner and related service provider.

Aareal Bank's business model is made up of two segments:

1. Structured Property Financing

Structured Property Financing, which brings together all the property finance and treasury activities of Aareal Bank, is at the core of Aareal Bank Group.

Aareal Bank has more than 15 years experience in domestic and international commercial property finance, and services clients in more than 25 countries. It is active in Europe, North America and Asia within the scope of its "three-continent strategy". Leveraging our successful European business model, we are establishing similar distribution structures in North America and in the Asia / Pacific region. We provide our clients with an established network of regional market experts and industry specialists in our target markets to offer financing solutions tailored to meet their requirements.

Aareal Bank is an established issuer on the capital market, where it covers a wide range of refinancing tools including asset-covered bonds to cater for a broad investor base.

2. Consulting / Services

The Consulting / Services segment offers the institutional housing sector services and products for managing residential property portfolios and processing payment flows. Within this segment, the Institutional Housing Business cooperates closely with the two Group subsidiaries Aareon AG and Aareal First Financial Solutions AG.

Aareon AG provides IT systems consultancy and other services to the institutional housing sector. Established more than 50 years ago as a computing centre, Aareon AG today offers its customers advisory and training services, as well as software products plus support and IT services.

Aareal First Financial Solutions AG is responsible for developing the highly-automated IT system for mass payments and deposit-taking.

The settlement of payment transactions via Aareal Bank generates client deposits that also contribute to the refinancing mix of the entire Group.

Company management

Aareal Bank Group is managed on the basis of various economic indicators, in particular, return on equity (RoE) after taxes and risk-weighted assets.

Key indicators used to manage the Structured Property Financing segment are predominantly RoE, new business originated, and the cost / income ratio.

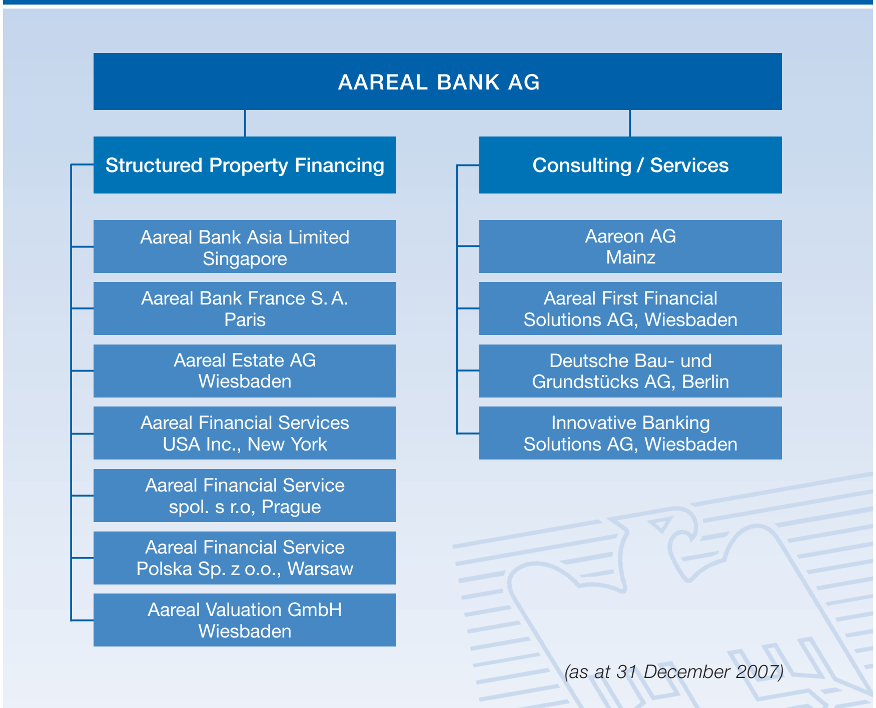
The indicators used in the management of the Consulting / Services segment depend on the characteristics of the individual subsidiaries, including EBIT and EBIT margin.

Macroeconomic and industry-specific environment

Global business environment

Although global economic development eased slightly in 2007 after the surge in 2006, the global economy was robust overall. The sharp rise in commodity prices and the crisis on financial markets, owing to the sub-prime crisis in the US, had not yet impacted severely on economic growth in 2007.

Group Structure of Aareal Bank



Gross domestic product in 2007 rose by a total of 3.6 % on a global scale, supported by sustained positive economic development in the US and the European Union. Economic growth in the emerging markets remained at the high level of recent years – this is particularly true for China, but also for India and Russia. Southeast Asia, Latin America and the Eastern European countries continued on the path of further growth.

Towards the end of the year, the positive economic environment was overshadowed by accelerating inflation. This development is particularly worrying since, in conjunction with the crisis on financial markets, it places the central banks in a difficult situation in terms of deciding whether to combat inflation or support the economy through monetary policy.

The good economic environment led to positive development on international financial markets, albeit not without volatility. Contributory factors were the predominantly positive company figures, relatively stable outlook and reliable monetary policy together with a fiscal policy that was focused mainly on stability. Equity prices climbed and bond yields fell.

However, the situation changed with the onset of the sub-prime crisis in the US and the ripple effects on individual American and European banks. The "sub-primes" are loans extended for owner-occupied houses in the US with a high loan-to-value ratio, offered to private borrowers with poor credit rating. The number of payment defaults on these frequently variable-rate loans mounted in the course of interest rate hikes in the US and several mortgage lenders were forced to apply for creditor protection. Given that the sub-prime loans were refinanced, amongst other things, by securitised investments on the capital market, the crisis extended to other economic areas. A number of banks in Germany that had undertaken obligations for special purpose investment vehicles (SIVs) that had been launched specifically for this investment purpose found themselves in difficulty. Given that some banks managed these obligations off-balance sheet and the securities were frequently tied into complex structures, the uncertainty in relation to the transparency of the ensuing risks led to a scarcity of liquidity amongst banks. The European Central Bank (ECB), the US Federal Reserve and other central banks provided the markets with considerable amounts of short-term liquidity through quick tenders, in order to bridge the credit crunch.

The European Central Bank determined in its monthly report for December 2007 that corporate loans in the US, UK and the eurozone were subject to considerably stricter lending criteria in the third quarter of 2007. In the euro zone, the guidelines for retail lending were adjusted to a much lesser extent than for corporate lending. This differs significantly from the US, where the guidelines for retail housing construction loans were tightened substantially. The banks gave the more difficult conditions for accessing market finance and lower risk tolerance as material reasons for these measures. Conditions on the market for securitisations, where off-balance sheet loans were placed, were considerably more difficult in the second half of the year.

The confidence and liquidity crisis gradually led to a sharp rise in term deposit interest rates on the interbank market compared with secured borrowing in the repo market. The difference between 3-month Euribor and the 3-month Eurepo rate, which was only around seven basis points at the start of the year, rose to a peak of 93 basis points during the course of the year.

Global commercial property markets

Following a record number of transactions in the property sector in 2006, the first half of 2007 was also defined by good demand for commercial property. At first, strong demand from investors drove down the yields on commercial property worldwide.

These yields fell to a particularly low level on the long-established markets. As interest rates rose and the more restrictive lending environment took effect, demand for property eased in the course of the year. The volume transacted in commercial property in the second half of 2007 was therefore down considerably on the same period of the previous year.

The more difficult situation on the market for securitised transactions in the second half of the year impacted primarily on the Anglo-Saxon and Western European markets, consequently reducing the loan offers for commercial property finance. CMBS (commercial mortgage-backed securities) were particularly affected by the collapse of the securitisation market. The volume of new issues launched in the first half of the year was € 45.2 billion (compared with € 23.1 billion in the first half of 2006). Issuance in the second half of 2007 amounted to only € 2.6 billion.

Large-sized property transactions in particular, and those with a high borrowing ratio, were blocked; in some cases, individual transactions were even called off. Research studies calculated that the volume of commercial property transactions concluded in Europe in the second half of 2007 was down 25 % year-on-year. On a one-year comparison, the decline was 13 % compared with 2006.

A fall in property prices was evident in some cases, so that yields that had fallen in the first half of the year stabilised in many places or rose towards the end of the year. Many markets for commercial property were characterised by stable to rising rents with falling vacancy ratios.

Positive global economic development also had an affirmative effect on the retail market in many countries. Retail premises in good locations were able to command mainly stable to slightly rising rents. Rent increases were seen in the dynamic markets of Asia in particular. The fall in yields on retail property investments in the first half of the year was halted or turned around in the second half.

The hotel industry was another beneficiary in 2007 of the positive trend in the global economy. Hence, demand for hotel property investments was generally good, particularly in Asia, where investors favoured upmarket and luxury hotels.

The logistics industry, and hence the associated financing of logistics properties, also gained from the positive economic development and related increase in international trading. However, the yields for logistics property investments varied greatly, with established markets such as the UK yielding around 6 % and growing markets such as Russia generating approx. 13 %.

Performance of mainly regional markets

Europe

In the European Monetary Union (EMU) the positive growth trend of the previous year lasted into autumn of 2007. However, a few of the trend indicators collapsed in the final months of the year. This was due to the continued rise in the price of oil, the financial and liquidity crisis as well as the appreciation of the euro.

The enduring good economic environment and continuation of the budget consolidation substantially improved the negative balance of public-sector authorities. All in all, growth of 2.9 % in the European Union was only slightly lower than the previous year. The engines of growth in the EMU included Ireland, Slovenia, Finland, Spain, Austria and for the first time in many years, Germany. Further there was another strong reduction in unemployment across the European Monetary Union, to close to 7 %.

By mid-2007, the European Central Bank had increased the main refinancing rate to 4 %, adhering to its commitment of pursuing a policy of stability. The crisis on financial markets emanating from the US led to a sharp increase in money market rates. This factor, coupled with the significant appreciation of the euro, prompted the European Central Bank to leave key rates unchanged, despite the looming threat of inflation in the second half of the year.

Germany

The German economy continued to recover in 2007: gross domestic product rose by 2.5 % and unemployment fell to 8.1 % for the year as a whole, which is the lowest rate recorded since 1995.

Residential construction investment fell in 2007 as it continued to be affected by the abolition of the ”Eigenheimzulage“ home-ownership subsidies that came into effect on 1 January 2006. Domestic demand by private consumers dropped considerably after the 1 January 2007 VAT increase, but rose again in the course of successive quarters to reach the previous year's levels. Private consumption fell by 0.3 % on an annual basis. Inflation, particularly energy and food inflation, gathered pace towards the end of the year.

Rising employment generally raises the demand for office property, which is reflected in higher turnover of office space. At the same time, vacancies decline – with the exception, on this occasion, of the Munich market. Top rents increased for office space in Munich, Frankfurt, Hamburg and Dusseldorf, which are the key locations for office properties. The only market in which rents remained unchanged from last year was Berlin, which is the fifth largest market for office properties.

The trend for retail property rents in good inner-city locations was stable or rising.

The increasing importance of Germany as a logistics location enhances demand for good logistics property, in line with prevailing market conditions and with close proximity to transport routes. Rents were stable to rising.

The transaction volume for hotels in Germany in 2007 was unchanged from the previous year. The first half of the year was defined by buoyant investment activity on the hotel markets, and also accounted for roughly two-thirds of the transactions conducted. Owing to the sub-prime crisis, the volume of transactions concluded was lower in the second half of the year.

In 2007, occupancy rates and the recovery ratio per hotel room in Berlin increased over the previous year, while in Frankfurt vacancies were unchanged and the recovery rate fell only slightly.

Overall, there was a shift in the second half of the year, with investors willing to commit to a higher level of equity investment. Open-ended property funds reduced their stakes in German property during 2007. The decline in yields halted in the third quarter. Some yields have risen again since then. The Act on the Introduction of REITs, which entered into force with retrospective effect from 1 January 2007, created a new, indirect, and tax-effective property investment opportunity – the effects of which remain to be seen. Two REITs were listed on the German stock exchange during the past financial year.

France / Spain / Italy

While Spain's real gross domestic product posted high growth of 3.8 % in 2007, growth in the French and Italian economies of 1.9 % each fell short of the European Union average growth rate of 2.9 %. In all three countries, rents for office properties in the key locations of Madrid, Barcelona, Paris, Milan and Rome were stable or rose slightly. A slight easing of the trend was reported however in Rome, although top rents in the city centre were practically unchanged from the previous year due to a shortage of high-quality office properties. The vacancy ratios remained constant in all three countries. Whilst low in Spain and France, vacancies were higher in Italy, especially in Milan.

Rents for retail properties were unchanged to slightly higher in all three countries. There was evidence of a trend in Spain and Italy towards smaller shopping centres outside of the major conurbations.

In Italy, Milan remains the key location for business hotels. At the same time, there was increased investor interest for tourist hotels in top-class locations. Average hotel bed utilisation in Barcelona, Paris and Milan remained unchanged in 2007. It fell slightly in Madrid but was somewhat higher in Rome. All of the aforementioned locations posted growth in income per room, albeit ranging widely between approx. 14.5 % in Barcelona to just above 1 % in Rome.

Rents for logistics properties were down slightly in Paris compared with a slight rise in Madrid, Barcelona and Milan.

Property investment in France was focused on the greater Paris region.

Switzerland

Overall economic growth in Switzerland was down 2.3 % in 2007 over the previous year.

Office rents varied in the key locations; Zurich posted a rise compared with a decline in Geneva. Demand for hotel beds rose in both the business and the tourist segments. Occupancy and recovery ratios per hotel room were up in Geneva and Zurich.

Logistics properties on the other hand are less important on the Swiss market. They are frequently owner-occupied and are therefore not available to investors. Retail rents in the top location of Zurich increased during the previous financial year. The Swiss market for commercial property is becoming increasingly interesting for international investors.

Scandinavia

The Scandinavian economies continued their above-average progress in 2007, with growth rates of 4.3 % and 1.9 % reported for Finland and Denmark respectively. Nevertheless, the momentum has eased in all countries.

Vacancy ratios for office space remained low in the capital cities of Helsinki, Oslo and Copenhagen. The level of vacancies was higher in Sweden, although it fell in 2007 in the key locations of Stockholm, Goteborg and Malmo. Top rents paid for office space in key locations in Scandinavia were stable, with Oslo even reporting a rise. Retail property rents in key locations were stable. On the other hand, top rents for logistics properties rose in Copenhagen, Oslo and Stockholm whilst remaining stable in Helsinki. The average bed occupancy rate in the four capital cities' hotels was around 70 %. While this figure rose in Oslo, Stockholm and Helsinki during 2007, Copenhagen reported a decline. Average returns per available room rose in all four countries; Oslo posted high growth in average returns, followed by Stockholm.

Benelux

At 2.7 %, economic growth in the Netherlands mirrored that of Belgium. The number of vacant office properties fell slightly in the Netherlands, albeit from a very high level, especially in the Amsterdam region. Supply and demand of office rental space, and hence rents, remained stable in the Netherlands' key locations for office property: Amsterdam, Den Haag, Rotterdam and Eindhoven. In Utrecht, the other key location, rents have recently risen slightly.

The market for office property in Belgium is focused mainly on Brussels. Demand is defined mainly by the public sector and by the European Union in particular. Nevertheless, there was an increase in the demand by private companies for office space in 2007. The vacancy ratio in Brussels fell only slightly, whereby vacancies are low in the city centre and high in the peripheral locations. The logistics sector is very important in the Netherlands and Belgium. Rents here remain stable. On the other hand, retail rents have risen in both countries. The occupancy ratio for hotel beds in Brussels increased by around 2 % compared with a slight fall in Amsterdam, which however still enjoys a high occupancy ratio overall of just over 80 %. The average return per room rose in Brussels and Amsterdam, whereby the level in Amsterdam is considerably higher than in Brussels.

UK

The UK economy progressed well in the first three quarters, before the first effects of price declines on the British residential property market fed through to the fourth quarter and the slowdown in the course of business in the financial sector was noticeable. This had the effect of slowing down the rate of economic expansion, so that the annual growth rate was ultimately 3.1 %.

The rental situation for London office property was stable in 2007: the level of vacancies was low, and top rents climbed. However, the high price level for commercial property and turbulence on financial markets generated uncertainty on the commercial property market, with the result that planned property transactions were increasingly called off. Commercial property in the UK suffered a particular loss in value in the second half of the year, and the previously very low yields rose again. Rents on retail and logistics properties were stable. Tourism is very important for the UK. The occupancy rate remained high in London at more than 81 %. Average returns per hotel room rose by around 10 % in 2007.

Central and Eastern European Countries (CEE)

The high growth rates of the previous year continued unabated in 2007 in most of the CEE countries. Gross domestic product in Poland climbed by 6.5 %, in the Czech Republic by 5.8 %, in Slovakia by 8.7 %, in Bulgaria by 6.3 % and in Romania by 6.0 %. Russia posted a 7.5 % rise in gross domestic product, which was, however, accompanied by high inflation. Hungary is an exception among the CEE states, with below-average growth of only 2.0 % due to the necessary consolidation measures taken by the government.

Investment in the CEE countries has risen continuously in recent years. There are signs of saturation in the markets in the established key locations within Poland, the Czech Republic and Slovakia, which led to a shift to niche markets or to other cities. Rents for office space as well as for retail properties were stable in the important cities of Moscow, Prague and Warsaw.

Rents for logistics properties in the aforementioned locations were also constant, apart from Warsaw, which was still able to post slight growth. Returns per hotel room fell in Moscow, although it still remained at a high level of € 200. There was a slight rise in occupancy rates, as was also the case in Prague, which also posted a slightly improvement in the returns per room.

Although Romania remains underdeveloped with respect to modern floor space across all property market segments, investor interest is growing.

The yields on various types of property in the CEE states have been falling for several years, although the upside trend has meanwhile slowed down. There are considerable differences between the high yields in Moscow and somewhat lower returns in Warsaw and Prague, although by and large they remain above the Western European level. Germany, Austria and the UK accounted for more than 50% of investors in the CEE states.

Turkey

Turkey has enjoyed economic stability for several years now: the high level of economic growth continued in 2007, although at 5.1 %, the gross domestic product increase was down on the previous year. Demand for office property increased, and the number of vacancies declined again. There are practically no empty office properties to be found in the centre of Istanbul, where sites for developing new office properties are scarce, and therefore expensive. Rents for retail properties rose slightly in 2007. High yields, compared with Western Europe, could be attained in the logistics sector. A large proportion, especially of modern properties, is owner-occupied. Additionally, the hotel sector is becoming increasingly important. The occupancy ratio, as well as returns per room, rose in 2007.

Although yields on commercial property in Turkey fell in 2007, they were considerably higher than in Western Europe. Foreign investors have invested heavily in the Turkish market, particularly in retail property and hotels. This trend also continued in Turkey's eastern regions.

North America

Although general economic momentum in the US eased in the first half of the year, it posted a surprisingly strong increase in the third quarter, despite the onset of the mortgage and financial crisis. The fourth quarter followed with a substantial easing. Gross domestic product growth for the year 2007 as a whole was around 2.1 %, down from the previous year's figure of 2.9 %. Inflation, which had eased initially, rose again strongly in the last months of the year to over 4 %. The Federal Reserve ended its restrictive policy in September when it cut the key overnight rate on Federal funds, thereby placing more importance on the credit and liquidity crisis than on combating inflation. By year-end, it had been reduced to 4.25 %.

The property market in the USA throughout 2007 was defined by the sub-prime crisis. Prices for residential property came under pressure. The rental market for office property showed strong form, despite the sub-prime crisis. Office property rents showed a distinct variability according to region. For example, while rents for example in San Francisco or Seattle rose sharply in some cases, they fell in Atlanta. However, rents were unchanged or rising in most major locations. Vacant office space also varied greatly, from just under 5 % in Manhattan to close to 28 % in Detroit. Yields on commercial property rose in the second half of the year.

Vacancies among retail properties varied greatly from region to region in the USA. Rents in the top locations of New York, Los Angeles and Chicago were stable or slightly rising. Vacancies in logistics properties also varied greatly by region, showing no uniform trend. The hotel market in the USA is dominated by the large chains. Average returns per room rose slightly, even in locations such as New York and Washington.

Gross domestic product growth in Canada and Mexico also fell year-on-year to 2.6 % (2006: 2.8 %) and 2.9 % (2006: 4.8 %) respectively.

In Canada, the banks extended relatively few sub-prime loans to their customers. Nonetheless, the high level of dependency on exports to the USA represents a threat to the Canadian economy. However, prices for commercial property were stable, on unchanged to slightly rising rents. Yields on logistics properties showed no uniform trend in Canada, although they remained largely stable for retail property.

Rents in the market for office property in Mexico were unchanged at the two key locations of Mexico City and Monterrey. The vacancy ratios, which were particularly high in Mexico City, were reduced. The logistics property market grew, especially in locations close to the US border and in Mexico City. Demand was seen in the capital city for high-quality properties.

Asia-Pacific region

The sub-prime hardly impacted on Asia during 2007. The economy in the Asian region again posted strong growth, in some parts. China was ranked first, with economic growth of 11.3 %. The Chinese central bank hiked interest rates several times in order to keep economic development in check. Economic growth in India, as well as Southeast Asian countries such as Vietnam and Indonesia was high as well.

In contrast, growth rates in Japan – the second-largest economy worldwide – have been low for many years. Economic growth in 2007 was 1.9 %.

Most of the markets for office property in the East Asian region have progressed steadily in terms of rental activity. Demand from the financial sector drove office space vacancies in Singapore down to a historical low. Office property markets in China and India also enjoyed robust demand, especially for first-class property. Rents in Beijing on the other hand eased slightly. Vacancies in Japan were low.

Retail trade expanded in the Asian region, with the result that the number of vacant retail properties was correspondingly low in 2007. Dynamic economic development in China was accompanied by high demand for rental logistics properties. The upcoming Olympics in 2008, and the World Expo in 2010, have already impacted positively on China. Increased demand was seen in 2007 for storage facilities close to the airport in Beijing, and international hotel companies are focusing increasingly on the cities of Beijing and Shanghai.

The highest rents for logistics properties in the Asia region were in Tokyo, followed by Hong Kong. Rents mainly increased in 2007. On Asia's hotel market, average returns per room in 2007 increased slightly over the previous year.

The share of cross-border investments increased, particularly in Asia. Private equity funds have shown an interest for this region, as have German open-ended property funds – although only in the last few years.

Results of operations

Aareal Bank posted its best result ever in the 2007 financial year. Operating profit of € 285 million (2006: € 117 million) represented a further basis for the bank's successful future.

The aggregate of net interest and net commission income of € 442 million was up 2.0 % on the previous year's figure of € 433 million. Specifically, interest income from lending business and money market transactions grew by € 252 million, whilst interest income from securities increased by € 62 million. Interest expenses rose by € 295 million.

At minus € 13 million, the net result from financial operations reflected the valuation of securities held in the trading portfolio (specifically, bank bonds) in a volatile market environment.

Administrative expenses increased from € 225 million in the 2006 financial year to € 240 million in 2007. € 6 million of this increase was attributable to higher personnel expenses, and € 9 million to increases in other administrative expenses.

The balance of other operating items improved to minus € 4 million after minus € 18 million the year before. This improvement resulted mainly from a compensation payment of € 37 million from DEPFA BANK plc. The net balance also includes € 16 million in expenses incurred in connection with the sale of our stake in Immobilien Scout GmbH.

The balance of provisions for loan losses and the result from securities held as liquidity reserve was minus € 105 million. This figure includes expenditure for specific and general loan loss provisions. Securities held as liquidity reserve were revalued strictly at the lower of cost or market; the item also includes gains and losses realised on this portfolio.

Net other income and expenses include € 45 million in profit transfers and € 153 million in unrealised income from the sale of our stake in Immobilien Scout GmbH.

Taking into account net taxes payable of € 14 million (comprising current taxes payable, and € 10 million in income from the reversal of provisions), net income for the year amounted to € 285 million.

Financial situation

Total assets

Consolidated total assets as at 31 December 2007 amounted to € 41.3 billion, after € 39.5 billion as at 31 December 2006.

Assets

Property financing portfolio

The volume of Aareal Bank's property financing stood at € 22.3 billion as at 31 December 2007. This corresponds to an increase of 8.3 % over the previous year's figure of € 20.6 billion. The rise was largely attributable to the successful expansion of the international financing business, with lower loan prepayments – as a consequence of the sub-prime crisis – also influencing volumes in the second half of the year.

We were able to raise the share of international financings in the overall portfolio in the financial year past by 18.7 %, to € 16.5 billion. The German property financing portfolio was reduced by a total of 13.4 % to € 5.8 billion. We therefore further optimised the diversification of our loan portfolio.

Portfolio management and exit strategies

Our Credit Portfolio Management and Credit Treasury units manage the overall structure of property financing portfolio. We use syndications, and to a lesser extent securitisations, in particular to optimise and manage the portfolio.

The Credit Portfolio Management unit is responsible for designing risk and return-oriented strategies for our financing portfolio. Within this context, it evaluates suitable market and business data, thus facilitating an early reaction to changes in the market. Portfolio management ensures that we allocate our equity in what are the most attractive products and regions from a risk / return perspective within the scope of our three-continent strategy. We apply restrictions set through portfolio limits to guarantee a high degree of diversification within the portfolio.

The Credit Treasury unit is responsible for implementing exit strategies that are consistent with the management of the portfolio. Our activities in this unit are focused in particular on syndication, whose advantages lie in fast, flexible placements of financing solutions related to single exposures. The structuring of securitised transactions on the other hand is complex and cost-intensive. Furthermore, such transactions require the relevant market environment in which to trade.

Syndications and synthetic securitisations

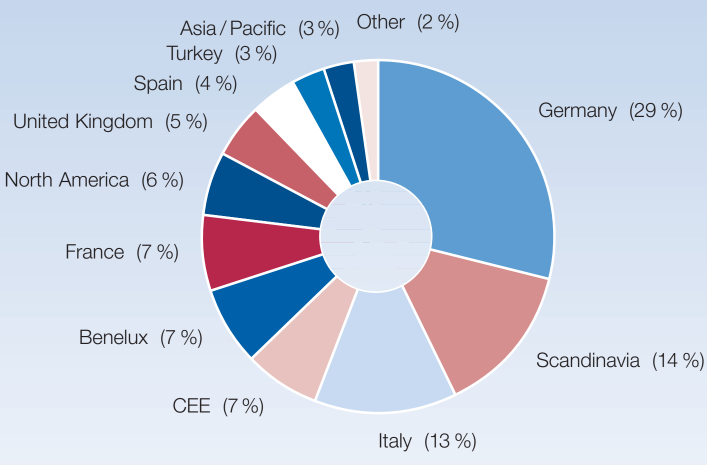
The year 2007 was defined by two distinct halves. The market environment functioned normally until the outbreak of the sub-prime crisis in late summer. Markets for exit instruments largely came to a standstill in the second half of the year.

We syndicated lending volume of just under € 700 million (compared with € 400 million the year before) to our international partner bank network during the period under review. These activites were concentrated mainly in the first half of the year. The change in the market environment brought about by the sub-prime crisis and associated reticence of market participants resulted in a significant decline in these business activities as of autumn 2007.

The unfavourable environment meant that securitisations could not be used as exit instruments. As at 31 December 2007, the volume of Aareal Bank's synthetic securitisations placed in the market amounted to € 2.4 billion, compared with € 3.5 billion as at 31 December 2006.

The considerably more flexible manner of placing financing solutions in the market via securitisations proved itself as a suitable means of portfolio management for Aareal Bank in 2007. Nonetheless, we will continue to take advantage of opportunities presented by the capital market in the medium term, in order to conduct synthetic securitisations.

Property financing portfolio by region



Reducing the NPL portfolio

One feature of early 2007 was the consistent reduction of the volume of non-performing loans (NPL) in our portfolio and the successful exploitation of the market opportunities presented to us. Following the sale of an additional portfolio in the amount of € 132 million, including interest and fees, together with targeted individual sales, the volume of the NPL portfolio was around € 0.4 billion as at year-end 2007. The current portfolio is at a normal and satisfactory level.

Refinancing

Refinancing structure

Aareal Bank refinances its lending activities on the capital market mainly in medium-term and long-term maturities. It refinances its money market activities through institutional housing sector deposits, client deposits and interbank transactions.

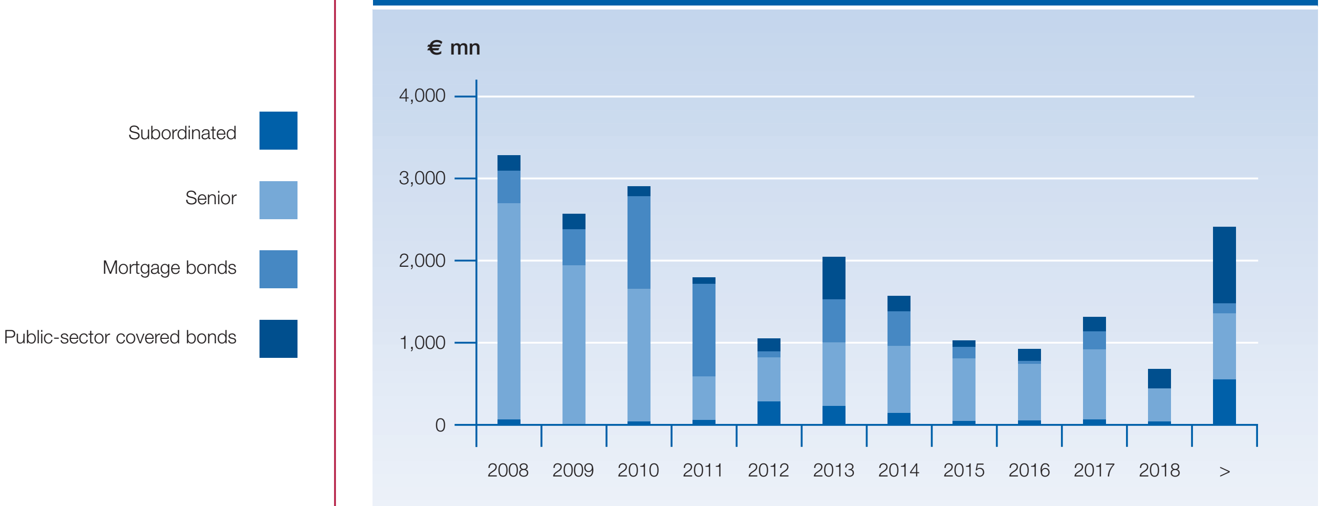
The long-term refinancing portfolio, comprising unsecured issues and asset-covered bonds, amounted to € 23 billion as at 31 December 2007. The deposit volume from the institutional housing sector amounted to € 4.5 billion and from institutional money market clients € 5.2 billion.

These funds are offset by a property loan portfolio to be refinanced in the amount of € 22.3 billion. The excess liquidity is invested in a portfolio of liquid, high-quality securities with a volume of € 7.8 billion, which serves as a liquidity reserve that can be used in the short term, depending on the situation. Further short-term investments are carried out in the money market and via repo transactions.

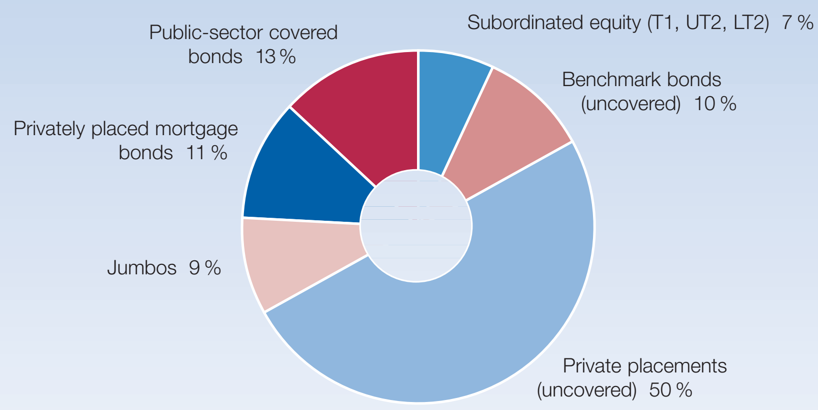
The long-term refinancing funds have an average term of over five years. The volume of funds maturing annually is roughly € 3 billion at present.

As at 31 December 2007, the long-term refinancing funds of € 23 billion comprised

Maturity structure of the long-term refinancing mix as at 31 Dec 2007



Refinancing mix as at 31 Dec 2007



20 % mortgage bonds, 13 % public-sector covered securities, 60 % senior unsecured issues and 7 % subordinated issues.

Refinancing activities in 2007

Aareal Bank successfully expanded its presence on the capital markets during 2007. By 31 December 2007, it had raised a total of € 4.6 billion of long-term refinancing funds.

At € 2.2 billion, mortgage bonds and public-sector covered securities accounted for just short of 48 % of new issuance. The refinancing activities include the successful issue of Aareal's second jumbo mortgage bond, sized at € 1 billion. Public bond issues amounted to an aggregate € 150 million. The majority of private placements (€ 2.5 billion) were issued in the form of registered securities, including promissory note loans and registered mortgage bonds. Additionally, € 940 million in private placements (largely MTN issues) were sold on the capital markets.

In 2007 the share of asset-covered bonds (mortgage bonds and public-sector covered securities) was increased further to roughly one-third of Aareal Bank's long-term funding mix.

In view of the level of quality, legal requirements, and successful capital market history, German Pfandbriefe offer a refinancing option at favourable terms, particularly during turbulent market phases. Aareal Bank benefited particularly from this, through the private placement of mortgage bonds in the last quarter of 2007.

During the financial year under review, we collaborated successfully with more than 40 partners on the capital market, including large and small investment houses as well as more highly-specialised institutions. This provided for a strong level of diversification within our investor base.

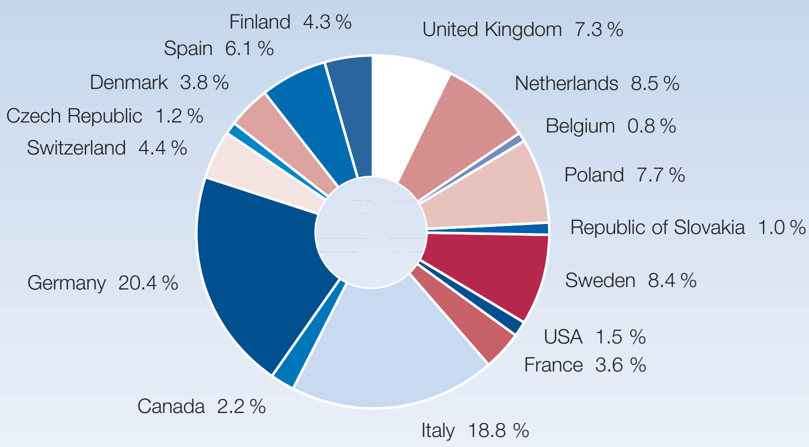
Refinancing strategy

Aareal Bank increasingly uses mortgage bonds to refinance its international loan portfolio. Roughly one quarter (€ 5.3 billion as at 31 December 2007) of the mortgage loans to be refinanced are included in the cover assets pool for mortgage bonds. Aareal Bank's international business model has resulted in a highly-diversified cover portfolio, with financing activities in 16 countries.

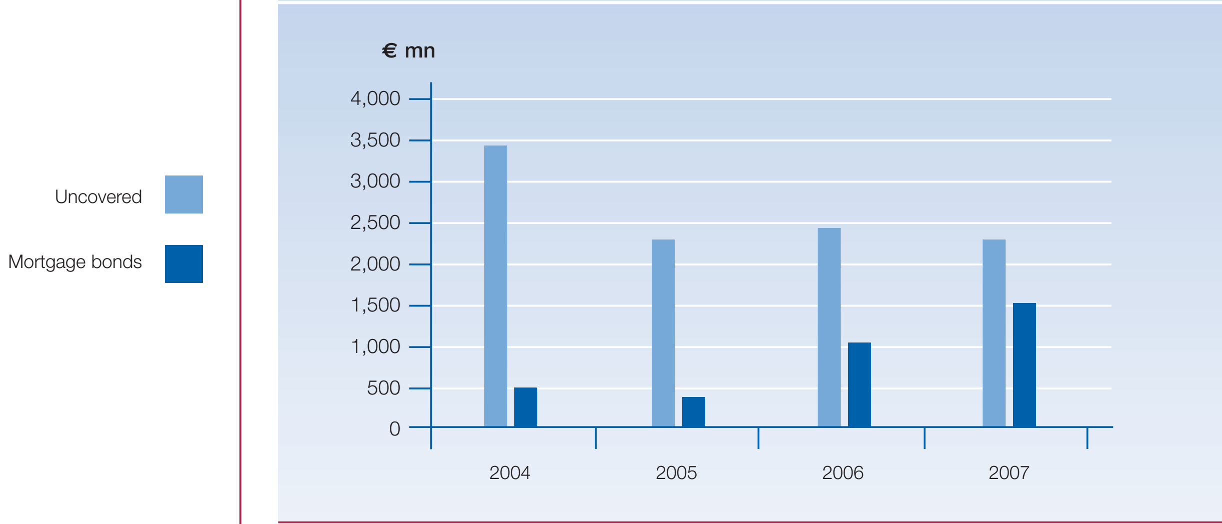
Asset-covered issues are an important instrument for Aareal Bank in its efforts to explore a new range of investors, and to reduce its refinancing costs. New investors, especially in Europe, are attracted to asset-covered bonds, primarily jumbo Pfandbriefe owing to their liquidity and quality.

The strategy pursued by Aareal Bank to issue jumbo Pfandbriefe on a regular basis

Diversification of the cover assets pool for mortgage bonds as at 31 Dec 2007



New issue volume of mortgage bonds vs. senior funding



represents a key step towards the increasing internationalisation of our investor base. The second jumbo Pfandbrief issue attracted many new investors, particularly from Asia, the UK and the Benelux countries. The share of asset-covered bonds relative to refinancing should be increased gradually in 2008, so as to further optimise the liabilities side of the balance sheet.

Aareal Bank offers international property financing solutions in a wide variety of liquid currencies. Our foreign currency-denominated issues are another aspect of the internationalisation of our capital market debut. We issued mortgage bonds denominated in Japanese yen, pound sterling and US dollar during 2007. Since the start of 2006, we have also included derivatives in the cover asset pool for the interest rate and currency management of the entire asset-covered bond business. This has enhanced the efficiency of our refinancing, and improved the quality of the asset-covered issues.

Aareal Bank's medium-term notes programme (MTN) is an internationally renowned documentation framework for securities issues, and is sized at € 10 billion. It allows drawings in subordinate, uncovered debt securities, as well as in mortgage bonds and public-sector covered securities, in all the required currencies and structures. Aareal Bank is a regular issuer of uncovered promissory note loans, registered bonds and bearer instruments.

Settlement of payment transactions for institutional housing sector clients generates residual current account balances and term deposits of over € 4.5 billion on a monthly average. The volume has been stable and rising slightly over recent years. Aareal Bank is also increasingly generating a stable deposit volume from institutional money market clients.

Regulatory indicators

Aareal Bank has opted to determine regulatory indicators at Group level only from 2007 onwards. The relevant Group indicators are provided in the 2007 Group Annual Report.

Report on material events after the reporting date

There have been no material events subsequent to the balance sheet date of 31 December 2007 that need to be disclosed at this point.

Outlook

Development of the environment

The economic framework for the year 2008 deteriorated significantly in the latter months of last year. Although many of the central banks cut interest rates since the outbreak of the sub-prime crisis, the weakening effects of restrictive monetary policy pursued in recent years are now unfolding. The extent of the anticipated rise in commodity prices, and in particular the fallout from the sub-prime crisis, plus the accompanying burden on the banking system, are more decisive for the future economic cycle.

The crisis on financial markets intensified considerably at the start of 2008, and is now increasingly impacting indirect market participants, over and above directly affected market participants. High levels of write-downs (in some instances) on their sub-prime loans and on other structured finance products have impacted on the shareholders' equity of the banks in question and hence restricted their lending opportunities. Consequently, loans have become more expensive, which has eroded the investment activities of companies, thus leading to an economic slowdown.

Global growth is likely to slow down to between 3.0 % and 3.3 %. Momentum in global trading is also expected to ease. The inflationary problems that have concerned many countries since the end of 2007 should be defused during 2008, so that the inflationary trend remains under control. Financial markets will remain volatile for a long time yet, as the sub-prime crisis is by no means over.

Europe

In Western Europe, particularly in Germany, we assume that the slowdown in global economic growth in 2008 will be reflected in weakened export activity. The considerable strength of the euro will also pose an additional burden. Overall, growth in 2008 will be substantially lower than in the previous year, although we do not expect a threat of lasting recession.

The approach of Western European banks to lending should remain restrained in 2008, so that we forecast tighter lending terms and conditions for investors. Despite good profitability, the aforementioned scenario will curb the investment activities of companies and thus diminish the economic expectations of both companies and consumers. The good employment environment on the other hand is positive.

In view of the relatively high currency depreciation in the euro zone over recent months, the burdens from the financial and liquidity crisis, and an anticipated economic slowdown, European monetary policy is currently in a difficult situation. It therefore remains to be seen whether the European Central Bank will continue to change interest rates against this background. We believe that the UK will be affected more by the sub-prime crisis than the euro zone overall, and thus expect the Bank of England to further ease its policy, following the last rate cut on 6 December 2007.

Economic growth in 2008 in the CEE states will be lower than 2007, as a consequence of anticipated developments in the US and Western Europe. Nonetheless, growth in most of the countries will be considerably higher than the level for Western Europe. The growth momentum seen in the CEE countries for the past few years could therefore remain intact.

North America

Given that the United States are particularly affected by the sub-prime crisis, we expect lending to be subdued in the US, which will in turn burden investments. Furthermore, private consumption is expected to fall as a result of the drop in the asset value of residential properties and lower US consumer confidence. This economic structure carries the risk of a recessionary trend. To counter this trend, the US Federal Reserve has already cut its key interest rates several times since September 2007. Moreover, the US administration plans a USD 150 billion spending programme to support the economy.

Given that the economic slowdown in the US should lead to further rate cuts, we are forecasting considerably weaker growth for the year 2008 as a whole, but not a sustained recession. The importance of the trading relationships with the US (NAFTA) will impact indirectly on Canada and Mexico, albeit not to the same extent as the United States.

Asia / Pacific

Asia's emerging markets are not immune to a weakening of the global economy. Nevertheless, growth should remain strong in the region, supported by continued high growth momentum, increasing domestic demand and close economic ties within the region. Relatively strong correlation to developments in the US and Europe will lead to a slight economic slowdown here.

China will remain the top performer in terms of economic growth in 2008. High growth and continuous inflation will require the Chinese central bank to hike key interest rates further. In contrast, growth in Japan will remain very low, as in recent years.

International property markets

The deteriorating economic outlook that is emerging for 2008 will impact by varying degrees on property markets, particularly on commercial property.

Europe

Falling returns on investment in commercial property in Western Europe were halted back in the second half of 2007. Yields have risen again – in part – since then. We expect this trend to continue into 2008, with rising returns on commercial property.

The UK, and London in particular, will be affected most by the increased returns, as yields there have already reached a particularly low level. We also expect rising yields in continental European locations such as for example, the urban areas of Spain, where yields are very low. High-quality property in excellent locations will benefit to a lesser extent by the rise in yields.

We believe that the yield differential between top-class property and properties with locational disadvantages will widen further. We also envisage some Western European regions – such as Scandinavia and the Benelux countries – to benefit from rising yields to a lesser extent.

All in all, the volume of commercial property transactions concluded in Western Europe should be lower in 2008 compared with 2007. Despite low economic growth, we forecast largely stable rents in the good locations of Western Europe against the background of a stable employment situation.

As the negative effects on residential construction investment in Germany from the abolition of the home-ownership subsidies that came into effect on 1 January 2006 is gradually tapering off, we expect residential construction investment and the price trend to be stable.

Compared with 2007, returns on commercial property in the Central and Eastern European countries should be stable to slowly falling. There is still a yield differential between the emerging markets, specifically Russia or Romania, and the Western European markets.

We forecast largely stable rents in Central and Eastern Europe. Rents for office space in Moscow are currently very high. Due to low vacancy ratios for high-quality space, rental levels should remain constant. On the other hand, the levels currently commanded in the established locations of Warsaw and Prague are considerably lower.

North America

Demand for office space by tenants is generally influenced by the economic situation of the companies. We therefore expect lower demand for office space in the US, compared with 2007. Rents for office space should therefore stagnate on average, or even fall in some cases. However, office space in top-class locations will always be in demand, which is why rental prices there will outperform office space in peripheral locations or of lesser quality.

Weaker private consumption feeds through in the form of higher vacancies and pressure on rental prices of retail property. This segment is also affected above all in peripheral locations.

Yields on commercial property investments in the US that had fallen over many years reached their low mid-2007 and started to rise again in the second half of the year. We expect a rise in yields in 2008, as well as a lower volume of commercial property transactions than in 2007.

Residential construction investment should continue to fall initially, as it has done at the end of 2007. We also expect residential property prices to fall on average, although major regional differences are unlikely.

Asia / Pacific

Even though we expect property yields to fall in the Asian emerging markets, they will remain clearly above the levels seen in the North American and West European markets. Despite strong construction activity, such as in Beijing or Shanghai, we assume that demand for new space in particular is so strong that rents in China will remain largely stable. We are also forecasting stable or slightly rising yields in other important Asian centres, such as Tokyo, Seoul or Singapore.

Corporate development

The forecast environment forecast will significantly influence the property financing business. This will present Aareal Bank with opportunities in the 2008 financial year, as well as with risks. In the light of our three-continent strategy in particular, we believe that the opportunities will outweigh the risks.

In particular, we presume that the situation on the capital market in 2008 will make it impossible (except for some individual cases) or very difficult to place loans with third parties. Being able to carry loans on the bank's balance sheet will therefore become a key competitive advantage.

Investor behaviour is changing: international property investors are concentrating increasingly on long-term commitments. Property is being regarded again as a non-current asset class. This will lead to a rise in quality and to an improvement in the risk / return ratio of the financings. We view the return to a more attractive pricing of risks and to higher equity stakes in the financings as positive for the future performance of the property financing business.

Given that the sub-prime crisis has hardly impacted on the Asian markets to date, they should continue to offer good opportunities for Aareal Bank.

The threat of a sustained recession in the US could represent risks for the development of the structured property finance business. This could lead to economic weakness worldwide. The subsequent drop in transaction volumes on the property markets could impair the financing business.

Pfandbrief spreads are expected to remain stable in 2008. Aareal Bank intends to exploit this opportunity by further increasing the share of Pfandbriefe in its refinancing mix. It is difficult at this point in time to estimate the future performance of the margins of unsecured notes. A significant widening of spreads for senior unsecured bonds would increase Aareal Bank's refinancing costs overall. However, we are very confident that rising margins in the lending business can more than compensate for higher refinancing costs.

Our securities portfolios could suffer further temporary negative effects in 2008 as a result of securities being marked to market.

Considering all opportunities and risks, Aareal Bank adjusted its company strategy in line with future business development. Owing to the anticipated market environment, projections assume that there will be only very limited exit opportunities available – or possibly none at all – by way of syndication and securitisation in 2008.

We expect a reduction in the level of prepayments of structured property financings, and hence a drop in net commission income.

We plan to further increase the volume of risk-weighted assets held in 2008. Net interest income will benefit from the rise in risk-weighted assets.

Risk Report

1. Risk management at Aareal Bank AG

The targeted handling of risks – based on a professional risk management – is crucially important to a bank's business performance. Moreover, banks must also meet extensive qualitative and quantitative requirements laid down by supervisory authorities, as defined by their business focus. The importance of risk management quality as an appraisal factor for analysts, rating agencies and investors alike has increased in recent years. Against this background, we consider the continuous development and refinement of our risk management system as a key management task.

1.1 Risk management – scope of application and areas of responsibility

Overall responsibility for risk management and risk monitoring remains with the Management Board and the Supervisory Board of Aareal Bank AG.

The diagram below provides an overview of the responsibilities assigned to the respective organisational units.

Areas of responsibility for risk management and monitoring

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

Type of risk		Risk management	Risk monitoring
Market price risks		Treasury, Dispo Committee	Risk Controlling
Liquidity risks		Treasury	Risk Controlling
Credit risks	Property Finance (single exposures)	Credit Business Market, Credit Management	Risk Controlling, Credit Management
Credit risks	Property Finance (portfolio risks)	Credit Management, Credit Portfolio Management	Risk Controlling
Credit risks	Transactions with financial institutions	Treasury, Counterparty and Country Limit Committee	Risk Controlling
Credit risks	Country risks	Treasury, Credit Management, Counterparty and Country Limit Committee	Risk Controlling
Operational risks		Process owners	Risk Controlling

Process-independent monitoring: Internal Audit

1.2 Strategies

The business strategy of Aareal Bank AG set by the Management Board, and approved by the Supervisory Board, provides the conceptual framework for risk management. Taking this as a basis, and strictly considering the bank's risk-bearing capacity, we have formulated detailed strategies for managing the various types of risk, which are designed to ascertain risks are dealt with consciously and professionally. Accordingly, these strategies include general policies, to ensure a uniform understanding of risks across all parts of the bank, and providing a cross-sectional, binding framework applicable to all departments. The bank has implemented adequate risk management and risk control processes to implement these strategies, and to ensure the bank's risk-bearing capacity. In line with the overall business strategy, risk strategies are revised at least once a year, and are approved by the Management Board.

1.3 Risk-bearing capacity and risk limits

The risk-bearing capacity of Aareal Bank AG – which is defined by the amount of aggregate risk cover – is a core determining factor with regards to the structuring of its risk management system. Aggregate risk cover is defined as the core capital (tier 1 capital) in accordance with the BIS definition, plus the budgeted net income before taxes. The calculation does not include additional funds such as supplementary and subordinated capital, or existing reserves. The aggregate risk cover is updated at least once a year, and additionally in the event of significant changes occurring (such as a capital increase, or a change in earnings projections).

We have thus implemented a system based upon limits defined in a conservative manner, and differentiated according to the type of risk. The aggregation of individual limits is based on the assumption that no risk-mitigating correlation effects exist amongst different types of risk. We also maintain a significant part of our aggregate risk cover as a risk cushion, which is not applied to risk limits, and is thus available for risk types that cannot be quantified (for example, reputational or strategic risks). Overall, limits are set in a way to ensure Aareal Bank AG's ability to bear risk at any time.

2. Organisational structure and workflows

2.1 Credit business

2.1.1 Division of functions and voting

Aareal Bank AG's structural organisation and business processes are consistently geared towards effective and professional risk management. This includes the extensive implementation of regulatory requirements regarding the structural organisation and workflows in the credit business.

Processes in the credit business are designed to consistently respect the clear functional division of market and risk management units, up to and including senior management level. In addition, the Risk Controlling unit, which is not involved in making lending decisions, is responsible for monitoring all material risks whilst ensuring an adequate and targeted risk reporting.

Lending decisions regarding credit business classified as relevant for the bank's risk exposure require two approving votes submitted by a market unit and a risk management unit. The bank's Assignment of Approval Powers defines the relevant lending authorities within market and risk management units. Where discretion holders 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 Counterparty and Country Limit Committee (CCC), which consists of executives from non-market units is responsible for the risk management vote regarding the approval of counterparty, issuer, or country limits.

We have implemented the clear separation of market and risk management processes across all relevant units.

2.1.2 Process requirements

The credit process comprises several phases: specifically, these include credit approval, further processing, and monitoring of loan processing. Credit exposures subject to increased risks involve separate processes for intensified handling, the handling of problem loans, and – if necessary – for risk provisioning. The corresponding processing principles are laid down in the bank's standardised rules and regulations.

Important factors determining the counterparty 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. Furthermore, the risk assessment results are taken into account for pricing purposes.

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.

2.1.3 Early risk detection procedures

The early identification of an increased 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 the exposure and the parties involved (such as borrowers or guarantors) throughout the credit term, assessing quantitative and qualitative factors, using periodic monitoring and internal ratings. The intensity of the ongoing assessments is based on the risk level and size of the exposure. The bank's internal risk management processes ensure that counterparty risk is assessed at least once a year.

Extensive IT resources are deployed to identify risk positions, and to monitor and measure risks. Overall, the existing set of tools and methods enable 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 use the support of experts from the independent risk prevention, restructuring, and recovery units.

2.1.4 Risk classification procedure

Aareal Bank AG employs various risk classification procedures for the initial, regular, or event-driven assessment of counterparty 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 is outside the market units.

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

The bank employs a two-step 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, with the relative impact of the two components on the rating result 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), through an assessment of collateral provided. The bank's maximum risk exposure (plus a cushion for potential fees and charges incurred) is determined for this purpose: expected proceeds from the realisation of collateral, and from uncollateralised residual receivables, are deducted from this exposure at default (EaD). When evaluating collateral, haircuts are applied or estimated recovery rates used, depending on the type of collateral involved and specific realisation factors.

The expected loss (EL) in the event of default of an exposure is determined as the product of PD and LGD. A methodology to classify and map expected loss levels was established during the financial year under review.

Aareal Bank AG 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, investment companies, 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.

Furthermore, Aareal Bank AG introduced a new rating procedure for sovereign states in 2007. 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. A rating method for regional governments, local and other public-sector entities was launched in parallel with the sovereign rating procedure, based on a comparable methodology. This procedure incorporates rating-relevant information regarding the clients concerned.

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

2.2. Trading activities

2.2.1 Functional separation

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

On the market side, the processing chain comprises Treasury and Credit Treasury, whilst risk management tasks are carried out by the independent units of Operations and Risk Controlling. Beyond this Finance 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 entire processing chain; these are adapted to prevailing circumstances without delay. 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“) set out by BaFin. 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.

Within the scope of trading activities, Credit Treasury is responsible for entering into credit derivatives on the bank's behalf, in individual cases requiring specific approval in each case.

Operations is responsible for controlling trading activities, confirming trades to counterparties, and for trade settlement. The unit 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 documentation / master agreements.

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

2.2.2 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 AG's overall risk exposure from trading activities, in terms of scope and structure.

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 market units in their business activities.

As part of the limit monitoring process, the Management Board and Treasury are notified of limits and their current usage on a daily basis.

Clearly-defined escalation and decision-making processes have been set out to deal with limit breaches.

3. Risk exposure by type of risk

3.1 Credit Risks

3.1.1 Definition

Aareal Bank AG defines credit risk or counterparty 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 risk. Counterparty 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 risk.

3.1.2 Credit risk strategy

Based on the bank's overall business strategy, Aareal Bank AG's credit risk strategy sets out all material aspects of credit risk management and policies. Proposals for the credit risk strategy are prepared jointly by market and risk management units, and adopted by the entire Management Board.

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. This process is instigated by management, and implemented by the market and risk management units, who submit a proposal (on which they are both agreed) to management.

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. Aareal Bank AG's credit risk strategy comprises the Group Credit Risk Strategy, containing general guidelines, plus individual sub-strategies (lending policies) defining the type of new business the bank wishes to generate, with respect to various markets and types of business. Given the hierarchical structure of the credit risk strategy, the Group credit risk strategy overrides individual sub-strategies.

3.1.3 Risk measurement and monitoring

The credit business is subject to a variety of risk measurement and monitoring processes. This includes the application of two different credit risk models incorporating concentration and diversification effects at a portfolio level. Both the expected and unexpected loss (credit-value-at-risk) are derived using this model. Credit value-at-risk corresponds to the maximum amount by which the actual loss can exceed the expected loss for a given confidence level.

Based on the results of these models, the bank's decision-makers are regularly informed of the performance and risk content of large-sized property finance exposures, and of business with financial institutions. The models permit to identify, measure, monitor and manage risks at a portfolio level.

In addition, the bank uses specific tools to monitor individual exposures on an ongoing basis where this is required: besides the tools already described, this includes monitoring of construction phase loans or residential property developers, or the monitoring of payment arrears.

A risk report is prepared and submitted to the bank's senior management on a regular basis, at least quarterly. The report provides extensive information regarding the key structural counterparty risk features of the credit portfolio.

Trading activities are generally restricted to counterparties for whom the requisite limits are in place. Replacement and settlement risks are taken into account when determining counterparty limit usage. Persons holding position responsibility are informed about relevant limits and their current usage without delay. Trading activities also require the establishment of issuer limits.

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. Any limit breaches are documented, together with action taken in response. Where limit transgressions exceed an amount defined in line with risk considerations, these are escalated to the responsible members of senior management.

3.1.4 Credit risk mitigation

The bank accepts various types of collateral to reduce default risk exposure from the extension of credit. 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 AG focuses on property when collateralising loans and advances. Loans are granted and the security interest perfected in accordance with the jurisdiction in which the respective property is located.

Market values and mortgage lending values are set 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 an independent appraiser; 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 appraisers.

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 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.

Netting agreements (close-out netting) and / or collateral agreements are concluded with trading counterparties in order to reduce the credit risk exposure associated with derivatives.

Our approach to managing our credit portfolio includes synthetic securitisation and syndication techniques, as well as the sale of sub-portfolios. This active "buy, manage, sell" strategy is designed to optimise our credit portfolio on an ongoing basis, in order to achieve an optimal risk / return ratio.

Any assets acquired upon the realisation of collateral are predominantly properties. The consideration received upon disposal is applied to repay the underlying financing. An immediate sale is generally sought for such properties.

3.1.5 Country risk

Definition

When defining country risk, in addition to the risk of sovereign default or default of state entities, Aareal Bank AG 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). These types of risks arise only if the borrower is located in a different country from the lender, or if the financed property is located in another country.

With the main focus of the portfolio being on the member states of the European Union and North America, exposure is concentrated in countries with very low risk potential.

Country risk measurement and monitoring

Geographical diversification and the avoidance of concentration risks are of greater importance, from the bank's overall perspective, than the observation of transfer risks. The system for managing country risk, utilised within the overall management of the bank, was designed in such a way that it takes both criteria into consideration.

Country risk exposure is managed using a cross-divisional process. The Counterparty and Country Limit Committee carries out a risk assessment of the relevant countries, grades them in country risk groups, and conducts an annual review in terms of country rating. The limits are set by the Management Board. The Risk Controlling unit is responsible for the continuous monitoring of country limits and for monthly reporting on limit utilisation.

In addition to monitoring the bank's international exposure, internal limit monitoring reports utilisations for the bank's domestic business, broken down by German federal states.

3.2 Market Risks

3.2.1 Definition.

Market price risk is broadly defined as the threat of losses due to changes in market parameters. Aareal Bank's market price risk exposure predominantly comprises interest rate risks, whilst currency risks are largely eliminated through hedges. Commodity and other price risks are irrelevant for the bank's business. Hence, the primary market price risk exposures are related to the risk parameters interest rates, equity prices, exchange rates, and implied volatilities. All relevant parameters are covered by our management and monitoring tools.

Derivative financial instruments are entered into predominantly in the trading book, whilst in the banking book they are primarily used as hedging instruments.

Spread risks between the various yield curves (e. g. government / Pfandbrief / swap curve) are also taken into account.

3.2.2 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 market price risk exposure on a daily basis. In addition, the entire Management Board is informed on a monthly basis, within the scope of an extensive risk report. A quarterly report is submitted to the Supervisory Board.

Value-at-risk (VaR) has been broadly accepted as the predominant method for measuring general market price risk. The VaR for market price risk quantifies the exposure as a negative divergence from the current aggregate value of the bank's financial transactions. This absolute amount, expressed in euros, indicates the potential loss incurred before counter-measures take effect. Since this is a statistical approach, the forecast for the potential loss that may be incurred within a specific period of time is for a given confidence interval only.

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, it takes into account the correlation between the individual types of risk. The statistical parameters used in the

VaR model are calculated on the basis of an in-house data pool over a period of 250 days. The loss potential is determined applying a 99 % confidence interval and a ten-day holding period. Besides general market price risk exposure, the daily determination of specific risks for bonds held in the trading book was introduced in 2007.

The limit set for the VaR figure is derived from the analysis of the bank's risk-bearing capacity, which is carried out at least once a year. Being authorised to maintain a trading book, Aareal Bank AG has defined an additional trading book limit, plus a separate value-at-risk limit for fund assets held.

Limits were unchanged during the 2007 financial year. No limit breaches were detected, and overall limit usage was low.

Back testing

The quality of forecasts made using this statistical model is checked through a weekly 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 (< 5 for a 250-day period). The number of negative outliers was always lower than four during 2007 (always lower than two in 2006), affirming the high forecasting quality of the VaR model we use.

Stress testing

Although VaR has become a standard tool, the concept may fail to adequately project the actual risk in extreme situations – for example, the 1997 crisis in Asia. For this reason, the VaR projection is supplemented by simulating stress scenarios on a weekly basis.

Aareal Bank AG calculates present value fluctuations both on the basis of real extreme market movements over recent years (German reunification, Asian crisis, September 11, etc.), and also using simulated market movements (parallel shifts, structural changes, steepening of the yield curve). This analysis requires that all positions are revalued fully on the basis of these market scenarios. The resulting impact on present value is compared against a special stress limit within the scope of weekly and monthly reporting.

The "worst-case" scenario used in the financial year under review was a 100 basis point upwards parallel yield curve shift. This scenario is identical to the interest rate shift scenario for limiting the interest rate risk exposure of mortgage banks, as prescribed by BaFin until the coming into effect of the German Pfandbrief Act in 2006.

Set limits were also adhered to throughout the year on the basis of stress scenarios.

Interest rate sensitivity

An additional instrument used to quantify interest rate risk exposure is the calculation of interest rate sensitivity, expressed by the ”delta“ parameter. The first step to determine this parameter requires calculating the present values of all asset and equity / liability items on the balance sheet. 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.

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.

Trading book

Being authorised to maintain a trading book, Aareal Bank AG is in a position to assign transactions to the trading portfolio as defined for the purposes of the capital ratio according to the German Banking Act (Grundsatz I). Given the small number of transactions and low volumes concluded during 2007, trading book risks played a low role in the overall risk scenario.

During the 2007 financial year, the processes employed proved to be able to quantify the risks arising from market price fluctuations in a timely and accurate manner, also for new products introduced.

3.3 Liquidity Risks

3.3.1 Definition

Liquidity risk in the narrower sense is defined as the risk that current or future payment obligations cannot be met on time. Aareal Bank AG'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.

3.3.2 Risk measurement and monitoring

Treasury is responsible for managing liquidity risks, whilst Risk Controlling ensures the continuous monitoring, including a weekly 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:

a) 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 cash flow profile of products without a fixed contractual lifetime.

b) 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 (i. e. all assets which 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.

c) 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.

Stress tests

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

The scenario regularly having the most significant impact on Aareal Bank's liquidity situation is a 'rollover failure', where rolling funding via the money market is disrupted.

The bank still has sufficient reserve funds even in this most extreme stress scenario.

Liquidity ratio according to the German Banking Act (Grundsatz II)

The requirements of the liquidity ratio in accordance with section 11 of the German Banking Act (Grundsatz II), which is relevant to liquidity management, were always complied with, as were the limits set by reference to the liquidity run-off profile.

3.4 Operational Risks

3.4.1 Definition

Aareal Bank AG 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. In contrast, strategic, reputational and systematic risks are not included.

3.4.2 Risk measurement and monitoring

It is the objective of the policy pursued by Aareal Bank AG 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 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 system of controlling tools, decentralised data capture as well as centralised and timely compilation of relevant information are ensured.

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 on the responsible persons for the bank's risk management.

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. There were cases reported in the loss database during the financial year under review, but there were no losses involving significant monetary damages.

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, assessing, and management – through to risk control.

3.5 Other risks

3.5.1 Definition

Aareal Bank AG uses the category of "other risks" to aggregate those types of risk that cannot be quantified exactly: primarily, this includes reputational and strategic risks.

Reputational risk is defined as the risk of events that negatively affect the bank's reputation with investors, analysts, or clients. Strategic risk is typically associated with the threat of incorrect assumptions regarding market developments, burdening a bank's performance as a result.

3.5.2 Risk measurement and monitoring

Other risks are predominantly managed and monitored through qualitative measures. A Group-wide Code of Conduct sets the framework regarding integrity and professional conduct for all activities. The Code provides a standard that is binding for all employees of Aareal Bank AG – regardless of position, and hence, including members of the Management Board or supervisory bodies. Accordingly, the Code defines the fundamental standards for the conduct of each individual employee. Each employee or member of an executive body is personally responsible for complying with this Code of Conduct. Aareal Bank AG ensures compliance with these standards, employing its internal facilities and organisational units (including, in particular, Internal Audit and Compliance / Anti-Money Laundering / Data Protection). Managers are responsible for raising staff awareness within their area of responsibility.

Aareal Bank AG's Management Board is responsible for managing strategic risk; it coordinates its actions with the Supervisory Board. The Management Board is supported in this task by Corporate Development, for instance, via the continuous monitoring of trends which may be relevant to business policy.

INCOME STATEMENT

OF AAREAL BANK AG FOR THE PERIOD FROM 1 JANUARY TO 31 DECEMBER 2007

EXPENSES			2007	2006
€ mn				
Interest expenditure			1,570.4	1,275.4
Commission expenditure			55.0	47.4
Net expenditure on financial operations			13.2	1.1
General administrative expenses				
a) Staff costs				
aa) Wages and salaries	104.5			
ab) Social security contributions, pensions and other employee benefits	19.2	123.7		
Including: pensions 7.9				
b) Other administrative expenses		109.6	233.3	216.6
Depreciation / amortisation of, and writedowns on intangible and fixed assets			6.8	8.0
Other operating expenses			58.2	45.3
Depreciation / amortisation of, and writedowns on claims and certain securities, additions to loan loss provisions			105.2	82.3
Expenditure for assumption of losses			5.1	17.9
Net income taxes			-14.4	61.9
Other taxes not reported under ”Other operating expenses“			1.6	0.0
Net income			285.4	117.4
Total expenses			**2,319.8**	**1,873.3**

	2007	2006
Net income	285.4	117.4
Profit carried forward	0.0	0.0
Withdrawals from retained earnings		
from the reserve for treasury shares	0.0	0.0
from other retained earnings	0.0	0.0
Transfer to retained earnings		
Amounts transferred to the reserve for treasury shares	0.0	0,0
Amounts transferred to other retained earnings	142.5	58.0
Net retained profit	**142.9**	**59.4**

INCOME		2007	2006
€ mn			
Interest income from			
a) Lending and money market transactions	1,500.2		
b) Fixed-income securities and government ledger bonds	422.2	1,922.4	1,608.6
Current income from			
a) Equities and other non-fixed income securities	38.8		
b) Participating interests	3.4		
c) Interests in affiliated companies	7.3	49.5	40.8
Income from profit pools, profit transfer agreements and partial profit transfer agreements		45.1	86.6
Commission income		95.4	106.5
Income from write-ups to participating interests, shares in affiliated companies and securities held as fixed assets		153.5	3.3
Other operating income		53.9	27.5
Total income		**2,319.8**	**1,873.3**

BALANCE SHEET

OF AAREAL BANK AG AS AT 31 DECEMBER 2007

ASSETS			2007	2006
€ mn				
Cash funds				
a) Cash on hand		0.0		
b) Balances with central banks		1,049.7	1,049.7	1,330.2
Including: with Deutsche Bundesbank 1,027.6				
Loans and advances to banks				
a) Payable on demand		276.4		
b) Other loans and advances		2,751.5	3,027.9	3,416.6
Loans and advances to customers			24,523.3	22,819.9
Including: secured by charges on real property 9,440.5				
Loans to local authorities 2,622.3				
Debt and other fixed-income securities				
a) Money market instruments		–		
b) Bonds and notes				
ba) Public-sector issuers	6,104.0			
Including: securities eligible as collateral with Deutsche Bundesbank 5,132.6				
bb) Other issuers	3,431.9	9,535.9		
Including: securities eligible as collateral with Deutsche Bundesbank 2,894.6				
c) Own bonds		809.8	10,345.7	9,141.9
Nominal amount: 803.7				
Equities and other non-fixed income securities			749.6	589.2
Participating interests			4.8	61.0
Including: interests in banks 0.8				
interests in financial services providers –				
Interests in affiliated companies			381.3	438.8
Including: interests in banks 30.3				
interests in financial services providers –				

SHAREHOLDERS' EQUITY AND LIABILITIES			2007	2006
€ mn				
Liabilities to banks				
a) Payable on demand		206.1		
b) With an agreed maturity or notice period		5,089.6	5,295.7	5,464.0
Liabilities to customers				
a) Savings deposits				
aa) With a notice period of three months	0.0			
ab) With an agreed notice period of more than three months	0.0	0.0		
b) Other liabilities				
ba) Payable on demand	4,119.1			
bb) With agreed maturity or notice period	18,941.2	23,060.3	23,060.3	21,461.7
Certificated liabilities				
a) Bonds issued		8,733.3		
b) Other certificated liabilities		–	8,733.3	8,026.8
Trust liabilities			824.2	1,341.2
Including: trustee loans 822.7				
Other liabilities			105.7	93.7
Deferred items			91.0	97.3
Provisions				
a) Provisions for pensions and similar obligations		59.8		
b) Tax provisions		44.3		
Including: provisions for deferred taxes 33.8				
c) Other provisions		150.5	254.6	270.5
Subordinated liabilities			871.1	922.5
Profit-participation certificates			488.0	487.9
Including: maturing within two years 10.2				

ASSETS	2007	2006
€ mn		
Trust assets	824.2	1,341.2
Including: trustee loans 822.7		
Intangible assets	4.8	8.5
Fixed assets	5.1	5.5
Other assets	312.1	235.2
Deferred items	63.6	77.5
Deferred taxes	43.0	47.3
Total assets	**41,335.1**	**39,512.8**

SHAREHOLDERS' EQUITY AND LIABILITIES			2007	2006
€ mn				
Fund for general banking risks			58.0	58.0
Shareholders' equity				
a) Subscribed capital		128.3		
Contributions by silent partners		220.2		
b) Capital reserve		509.5		
c) Retained earnings				
ca) Legal reserve	4.5			
cb) Reserve for treasury shares	–			
cc) Statutory reserves	–			
cd) Other retained earnings	547.8	552.3		
d) Net retained profit		142.9	1,553.2	1,289.2
Total shareholders' equity and liabilities			**41,335.1**	**39,512.8**

Contingent liabilities (€ mn)			
a) Contingent liabilities from discounted forwarded bills	–		
b) Liabilities from guarantees and indemnity agreements	1,846.4		
c) Liability from the pledging of collateral for third-party liabilities	–	1,846.4	1,451.6

Other commitments (€ mn)			
a) Repurchase obligations from securities repurchase agreements	–		
b) Placement and underwriting obligations	–		
c) Irrevocable loan commitments	4,577.2	4,577.2	3,007.1

ACCOUNTING AND VALUATION PRINCIPLES

The financial statements of Aareal Bank AG for the financial year 2007 were prepared in accordance with the provisions of the German Commercial Code (Handelsgesetzbuch – "HGB") and the supplementary regulations of the German Public Limited Companies Act (Aktiengesetz – "AktG") and the German Accounting Directive for Banks and Financial Services Providers (Verordnung über die Rechnungslegung der Kreditinstitute und Finanzdienstleistungsinstitute – "RechKredV").

Loans and advances

Loans and advances to banks and customers are carried at amortised cost, including deferred interest. Premiums and discounts are shown under deferred items, in accordance with section 340e (2) of the HGB. Credit risks are accounted for by setting aside provisions in the amount of the expected loss, using prudent estimates. At Aareal Bank AG, the calculation of general loan loss provisions is based on a procedure using standard risk costs. These costs are determined on the basis of actual risk provisioning expenditure.

Securities

Bonds and other fixed-income securities, as well as equities and other non-fixed income securities, are measured strictly at the lower of cost or market value, as prescribed for current assets, taking into account hedging instruments. Where the reasons for the write-down no longer apply, such securities must be written up in accordance with section 280 of the HGB. Investment securities are valued at the lower of cost or market. Differences between cost and amounts repayable are amortised in income.

Participating interests, interests in affiliated companies and fixed assets

Participating interests, interests in affiliated companies and fixed assets are stated at the cost of acquisition or manufacture, less scheduled depreciation. Special write-downs are required in the event of impairments in value deemed to be other than temporary.

Where the reasons for the write-down no longer apply, such participating interests or interests in affiliated companies must be written up in accordance with section 280 of the HGB. Where land and buildings were acquired to salvage loans and have been in the possession of the bank for more than five years, these are reported under fixed assets.

Low-value commercial goods ("geringwertige Wirtschaftsgüter") are written down in full in the year of their acquisition, and shown as additions or disposals in the list of investments. The option to disclose a net amount, pursuant to section 340c (2) of the HGB has been exercised.

Treasury shares

Treasury shares are capitalised at cost, and the appropriate amount transferred to the reserve for treasury shares. Treasury shares are measured at the lower of cost or market.

Liabilities

Liabilities are stated at their repayment amount. The difference between the nominal value and the initial carrying amount of liabilities is recognised under deferred items, and amortised over the term of the liability.

Provisions

Provisions for pensions and similar obligations are formed using an interest rate of 6 % applying the cost method (”Teilwertverfahren“) according to section 6 a of the German Income Tax Act (Einkommensteuergesetz – EStG). Provisions for taxes and other provisions have been set aside in the amount of the expected liability, as required by prudent commercial judgement.

Currency translation

Aareal Bank has translated balance sheet items and pending transactions in foreign currency, in accordance with section 340h of the HGB and statement 3/1995 issued by the Banking Committee of the German Institute of Auditors (BFA). The bank has classified all foreign exchange transactions as ”specific cover“ in accordance with section 340h (2) sentence 2. Hence, income and expenses from currency translation were recognised in the income statement, in accordance with section 340h (2) sentences 1 and 2 of the HGB. As all pending foreign currency exposures at the end of 2007 were related to concurrent business operations, no amounts needed to be disclosed separately under section 340h (2) sentence 4 of the HGB.

The bank decomposes foreign exchange forward transactions into an agreed spot base and the swap rate, recognising a deferred asset (reported under other assets) equivalent to the net aggregate difference between the spot base and the exchange rates prevailing on the reporting date. Forward premiums or discounts are amortised in net interest income over the term of the transaction.

Currency translation income and expenses are reported in net profit on financial operations.

Trading portfolio

Aareal Bank AG is authorised to operate a trading book pursuant to section 1 (12) of the KWG. Transactions in the trading book are subject to institutionalised risk management, with a strict limitation of risk exposure and daily risk reporting. Financial transactions accounted for in the trading book are measured strictly at the lower of cost or market in accordance with section 253 of the HGB. This measurement is carried out on a portfolio basis, whereby positive and negative measurement results within the same portfolio are set off; any net unrealised loss on a portfolio basis is reported, while a net unrealised profit is not.

The results of the trading portfolio are reported in net profit on financial operations. Interest from securities and money-market instruments held in the trading portfolio is included in net interest income.

NOTES TO THE INCOME STATEMENT

Income by geographical segment

The aggregate of (i) interest income, (ii) current income on equities and other non-fixed income securities, and on participating interests and interests in affiliated companies, (iii) commission income and (iv) other operating income is broken down by the following regions, in accordance with section 34 of the RechKredV.

	2007 € mn	2006 € mn
Germany	1,830.2	1,550.1
Europe / America / Asia	291.0	233.2
Total	**2,121.2**	**1,783.3**

Administration and intermediation services rendered to third parties

Administration and intermediation services rendered to third parties concerned the administration and intermediation of loans and trust assets.

Other Operating Income / Expense

Net other operating income of € 53.9 million includes a € 37.2 million compensation payment received from DEPFA BANK plc.

Other operating expenses in the amount of € 58.2 million include expenses totalling € 16.1 million incurred in relation to the sale of Immobilien Scout GmbH, and € 10.8 million for the reimbursement of expenses for the sales activities of a Group subsidiary.

Net income tax

The net income tax position amounted to € 14.4 million in income. The net figure comprises € 25.2 million in current tax expense (of which € 13.8 million was payable abroad, and € 11.4 million in Germany); and € 10.4 million in income from the release of provisions for previous periods, plus € 29.2 million in income from the reversal of deferred taxes.

NOTES TO THE BALANCE SHEET

Securities negotiable at a stock exchange

Analysis of securities negotiable at a stock exchange in the balance sheet line items shown below:

	Listed 31 Dec 2007 € mn	Unlisted 31 Dec 2007 € mn
Debt and other fixed-income securities (excluding pro-rata interest)	8,914.1	1,250.1
Equities and other non-fixed income securities	11.2	182.2
Participating interests	–	–
Interests in affiliated companies	–	–

Valuation units with hedging transactions have been created with respect to negotiable securities in an aggregate amount of € 5,722.8 million.

Bonds and notes of € 9,535.9 million (including accrued interest) reported under debt and other fixed-income securities include € 1,508.7 million in securities which are not eligible as collateral with Deutsche Bundesbank. This includes securities used to collateralise synthetic securitisations (which have been funded through the issuance of € 933.2 million in related CLN tranches), plus € 313.5 million in sovereign foreign-currency bonds, which are eligible for securities lending. Other securities account for the remaining € 262.0 million.

Equities and other non-fixed income securities include € 10.3 million of investment fund units which are exclusively reserved to meet the Aareal Bank AG's pension obligations vis-à-vis its active and retired employees in Germany.

Subordinated assets

The following items comprise subordinated assets in the amount shown (excluding pro-rata interest):

	31 Dec 2007 € mn	31 Dec 2006 € mn
Loans and advances to banks	38.1	38.1
Loans and advances to customers	47.0	114.7
Debt and other fixed-income securities	18.8	14.9
Equities and other non-fixed income securities	11.2	1.0
Other assets	–	–

Movements in fixed assets

The changes in fixed assets are presented in the fixed assets development schedule shown below.

	Debt and other fixed-income securities (Assets – item #5)	Participating interests (Assets – item #7)	Interests in affiliated companies (Assets – item #8)	Intangible assets (Assets – item #11)	Fixed assets (Assets – item #12)	
					Office furniture and equipment	Land and buildings
	€ mn	€ mn	€ mn	€ mn	€ mn	€ mn
Purchase or production cost 1 Jan 2007	–	72.6	484.8	40.8	47.9	1.7
Additions	592.7	0.9	720.8	1.0	2.5	0.1
Disposals	12.2	19.7	820.6	0.0	11.6	1.2
Changes in inventory / transfers	–	-36.5	36.5	0.0	0.0	0.0
Amortisation / depreciation (accumulated, as at 31 Dec 2006)	–	11.6	46.0	32.4	43.5	0.6
Depreciation, amortisation and writedowns in the current year	–	0.9	12.3	4.6	2.2	0.0
Disposals	–	0.0	17.5	0.0	11.5	0.5
Transfers	–	0.0	0.0	0.0	0.0	0.0
Write-ups	–	0.0	0.6	0.0	0.0	0.0
Book value as at 31 Dec 2007	**580.5**	**4.8**	**381.3**	**4.8**	**4.6**	**0.5**
Book value as at 31 Dec 2006	–	61.0	438.8	8.5	4.5	1.0

Changes	Carrying amount 31 Dec 2007 € mn	Carrying amount 31 Dec 2006 € mn
Participating interests	4.8	61.0
Interests in affiliated companies	381.3	438.8
Debt and other fixed-income securities		580.5
Equities and other non-fixed income securities	–	–

The values shown for debt and other fixed-income securities includes additions and disposals, as well as changes in inventory due to the amortisation of premiums and discounts (excluding accrued interest). The market for securitised assets of very high credit quality became illiquid during 2007. Given that this market illiquidity is expected to prevail, the intention to realise short-term profits is no longer feasible, requiring a review of the purpose of securities holdings. Taking into account the credit quality of securitised assets and the resulting long-term profit potential, the bank reclassified € 592.7 million in securities from the trading portfolio to investment securities. An examination of cost vs. market values as at 31 December 2007 did not indicate any impairment due to credit quality. Given the liquidity markdown, the market value was € 15.6 million below the book value.

The option to aggregate non-trading assets, pursuant to section 34 (3) of the RechKredV, has been exercised.

The bank has rented the majority of business land and buildings used for its business operations from one of its subsidiaries. As part of the transfer of some of the business activities from DEPFA Deutsche Pfandbriefbank AG to Aareal Bank AG, goodwill has been capitalised and reported under intangible assets.

Given the reverse materiality, this will be amortised over the expected useful life of nine or ten years, respectively.

Other assets

Other assets include, in particular, € 167.7 million in assets recognised from currency translation and € 49.7 million in receivables from assumption of profits.

Deferred taxes

Deferred taxes were reversed during the financial year 2007. At 31 December 2007, € 43.0 million in deferred tax assets and

€ 33.8 million in deferred tax liabilities were reported. Deferrals are made in the amount of the assumed tax burden or relief in coming financial years based on the respective local tax rates for 2008.

Other liabilities

Other liabilities include, in particular, € 10.0 million in liabilities related to the sale of a participation, and € 11.3 million in interest liabilities on silent partnership contributions.

Subordinated liabilities

Subordinated funds raised in accordance with section 10 (5a) of the KWG do not provide for any early repayment obligation for Aareal Bank AG. In the event of liquidation or insolvency, claims on interest and principal from these liabilities are subordinated to the claims of all other creditors of Aareal Bank AG, which are not themselves subordinated. This also applies to those subordinated funds raised that are not specified in detail.

Total interest expenses for subordinated liabilities of € 50.3 million (2006: € 52.3 million) include € 12.8 million (2006: € 13.1 million) in deferred interest not yet due.

Aareal Bank AG has € 250.0 million in subordinated equity from Aareal Capital Funding LLC, Delaware, USA, at its disposal, of which it, in turn, made a partial amount available to Aareal Bank France S.A. (€ 23.0 million). Aareal Bank AG's attributable share of € 227.0 million exceeds 10 % of the aggregate nominal value of all subordinated liabilities; these subordinated funds bear interest at a rate of 7.135 %, and are repayable on 31 December 2026. The bank has had a right to terminate, on a quarterly basis, since 31 December 2006; the creditors do not have any early termination rights.

Profit-participation certificates

The terms and conditions of the profit-participation certificates issued comply with the requirements of section 10 (5) of the KWG. It comprises the following profit-participation certificates issued by Aareal Bank AG (previously: DePfa Bank AG BauBoden):

	Nominal amount € mn	Issue currency	Interest rate (% p.a.)	Maturity
Bearer profit-participation certificates				
	150.0	€	6.750	2002 - 2011
	100.0	€	6.375	2002 - 2011
	60.0	€	6.125	2003 - 2013
	310.0			
Registered profit-participation certificates				
	10.2	DM	6.800	1996 - 2007
	5.0	€	7.010	2002 - 2012
	10.0	€	7.010	2002 - 2012
	5.0	€	7.010	2002 - 2012
	10.0	€	7.010	2002 - 2012
	5.0	€	7.100	2002 - 2012
	10.0	€	7.150	2002 - 2012
	5.0	€	7.030	2002 - 2012
	5.0	€	7.220	2002 - 2016
	5.0	€	7.220	2002 - 2016
	5.0	€	6.080	2003 - 2013
	20.0	€	6.120	2003 - 2013
	5.0	€	6.310	2003 - 2017
	10.0	€	5.750	2004 - 2014
	2.0	€	5.470	2004 - 2014
	5.0	€	5.480	2004 - 2014
	5.0	€	5.380	2004 - 2016
	20.0	€	5.950	2004 - 2016
	6.0	€	5.830	2005 - 2017
	148.2			

Pursuant to the terms and conditions of issue, holders of profit-participation certificates have a claim on interest payments which takes precedence over the profit entitlements of shareholders. Where a distribution during the term of the profit-participation certificates would cause a net loss, said interest claim would be reduced, creating a claim for backpayment during the term of the certificates at the same time. Repayment takes place at the nominal amount (subject to any loss sharing), on the day after the Annual General Meeting passing resolutions regarding the relevant financial year.

€ 29.8 million (2006: € 35.6 million) in interest expenses were incurred in 2007 with respect to profit-participation certificates issued.

The profit-participation certificates evidence creditors' rights; they do not grant any share in the liquidation proceeds.

Profit-participation certificates meet the requirements for liable equity capital pursuant to section 10 (5) of the KWG.

Purchase of treasury shares

The Company has been authorised by the Annual General Meeting held on 30 May 2007 to purchase and sell own shares, pursuant to section 71 (1) no. 7 of the AktG, until 29 November 2008. The volume of shares acquired for this purpose must not exceed 5 % of the bank's share capital at the end of any day. The lowest price at which a share may be acquired is determined by the closing price of the shares in Xetra (or a comparable successor system) on the trading day prior to such purchase less 10 %. The highest price shall not exceed such average closing price plus 10 %.

The Company was authorised at the same Annual General Meeting to purchase own shares not exceeding 10 % of the bank's share capital for other purposes than securities trading until 29 November 2008. Shares may be acquired via the stock exchange or by means of a public offer to buy, directed at all shareholders. Neither the purchase price, excluding ancillary costs, (if the acquisition takes place via the stock market) nor the offering price, excluding ancillary costs, (in case of a public offer to buy) may exceed or fall below the average closing price of the bank's shares in Xetra (or a comparable successor system) during the three trading days prior to the purchase or the public announcement of the purchase offer by more than ten per cent (10 %).

Said authorities were not utilised. No treasury shares were held at the end of the year under review.

Development of shareholders' equity reported on the balance sheet

	€ mn	€ mn
Subscribed capital		
Balance as at 1 Jan 2007 (of which: € 220.2 million contributions by silent partners)	348.5	
Balance as at 31 Dec 2007 (of which: € 220.2 million contributions by silent partners)		348.5
Capital reserve		
Balance at 1 Jan 2007	509.5	
Balance at 31 Dec 2007		509.5
Retained earnings		
Legal reserve		
Balance as at 1 Jan 2007	4.5	
Balance as at 31 Dec 2007		4.5
Other retained earnings		
Balance as at 1 Jan 2007	367.3	
Transfer from net retained profit 2006	38.0	
Transfer from net income	142.5	
Balance at 31 Dec 2007		547.8
Net retained profit		**142.9**
Shareholders' equity as at 31 Dec 2007		**1,553.2**

Subscribed capital is divided into 42,755,159 bearer unit shares (notional no-par value shares).

Aareal Bank has opted to determine regulatory indicators at Group level only from 2007 onwards; as a result of this waiver, regulatory details no longer need to be disclosed at a single-entity level.

Authorised capital

The Annual General Meeting held on 15 June 2005 resolved to approve a new authorised capital. The Management Board is authorised to increase, on one or more occasions, the Company's share capital by up to a maximum total amount of € 58.3 million (Authorised Capital) by issuance of new bearer shares for contribution in cash or in kind (where such contribution may represent the full contribution, or part thereof), subject to the approval of the Supervisory Board; this authority will expire on 14 June 2010. The shareholders shall be granted a subscription right, unless the Management Board exercises its authority to exclude shareholder's pre-emptive subscription rights.

The Management Board may exclude shareholders' subscription rights, subject to approval by the Supervisory Board and the conditions set out below:

- in the event of a capital increase against cash contributions, provided that the issue price is not significantly below the prevailing stock exchange price. However, this authorisation shall be subject to the proviso that the aggregate value of shares issued to the exclusion of shareholders' subscription rights, in accordance with section 186 (3) sentence 4 of the AktG, shall not exceed ten per cent (10 %) of the issued share capital at the time of exercising said authorisation. Any shares that were issued or sold during the term and prior to the exercising of said authorisation, in direct or analogous application of section 186 (3) sentence 4 of the AktG, shall count towards the above threshold of ten per cent (10 %) of the issued capital. Said ten-per-cent threshold shall also include shares which were issued (or the issuance of which is required) under the terms of debt securities with embedded conversion or option rights on shares issued pursuant to section 186 (4) sentence 4 of the AktG, which are outstanding at the time of exercising said authorisation;
- for fractional amounts arising from the determination of the applicable subscription ratio;
- where this is necessary to grant subscription rights to the holders of bonds with warrants or convertible bonds issued (or to be issued) by the Company or its affiliated companies, which subscription rights are required to entitle these holders to the same extent as they would have been entitled upon exercising their conversion or option rights or upon performance of a conversion obligation, if any, thus protecting such holders against dilution;
- up to an amount of € 4.0 million in order to offer employees (of the Company or its affiliated companies) shares for subscription.
- where the new shares will be issued against contributions in kind.

Exercising said authorisations, and with the approval of the Supervisory Board, the Management Board resolved on 6 November 2005 to increase the Company's issued share capital by € 11.7 million (equivalent to 10 % of the issued share capital prior to the increase) to € 128.3, by issuing 3,886,832 no-par value bearer shares against cash contributions, at an issue price of € 25.75. Excluding shareholders' pre-emptive subscription rights, Aareal Holding Verwaltungsgesellschaft mbH, Bayerische Beamtenversicherung and Neue Bayerische Beamten Lebensversicherung AG were admitted to subscribe and acquire the new shares. The capital increase was carried out, and entered in the Commercial Register on 21 November 2005.

Following this increase, the remaining authorised capital amounts to € 46.6 million. This authorisation will expire on 14 June 2010.

Conditional capital

The share capital is subject to a conditional capital increase of up to € 30.0 million by means of issuing 10.0 million new no-par value bearer shares. Such conditional capital increase serves to enable the company to service convertible bonds and / or bonds with warrants on the basis of the authorisation resolution of the Annual General Meeting held on 23 May 2006. Said resolution authorised the Management Board, subject to the consent of the Supervisory Board, to issue, on one or more occasions until 22 May 2011, convertible bonds and / or bonds cum warrants with a limited or an unlimited term in an aggregate nominal amount of € 600.0 million and to grant option and / or conversion rights to bearers or holders of bonds with regard to no-par value bearer shares of the Company, equivalent to a share in the equity capital of up to € 30.0 million. The issuance of bonds may be effected against contributions in kind for the purpose of acquiring companies, interests in companies or divisions of companies.

The bonds may be issued in euro as well as in any other currency – with the corresponding equivalent value – which is the legal tender of, for example, an OECD member state. They may also be issued via an indirect or a direct subsidiary of the Company; in this case, the Management Board is authorised, subject to the consent of the Supervisory Board, to issue a guarantee with regard to the bonds on behalf of the Company or to grant to the bondholders conversion or option rights to new no-par value bearer shares of the Company.

The conditional capital increase will be executed only to the extent that holders of conversion or option rights exercise such rights or any conversion obligation from such convertible bonds and / or bonds with warrants are performed, and to the extent that treasury shares are not utilised to service such convertible bonds and / or bonds with warrants. The new shares will 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 or option rights or the performance of conversion obligations.

No convertible bonds or warrants were in issue as at the balance sheet date.

Contingent liabilities and other commitments

Contingent liabilities as at 31 December 2007 include € 81.9 million in maximum default guarantees extended to DEPFA Deutsche Pfandbriefbank AG (within the scope of splitting the former DePfa Group), for the purpose of providing cover against risks of default with respect to the property loan portfolio held by DEPFA Deutsche Pfandbriefbank AG.

Irrevocable loan commitments are made up of credit and loan commitments. Of the total amount, € 1,009.4 million relates to domestic borrowers and € 3,567.8 million to foreign borrowers.

Remaining terms

	31 Dec 2007 € mn
Loans and advances to banks	**3,027.9**
Payable on demand	276.4
Up to 3 months	1,819.1
Between 3 months and 1 year	45.0
Between 1 year and 5 years	111.0
More than 5 years	167.6
Pro rata interest	608.8
Loans and advances to customers	**24,523.3**
Up to 3 months	1,762.7
Between 3 months and 1 year	1,180.1
Between 1 year and 5 years	11,874.6
More than 5 years	9,513.4
Indefinite maturity	–
Pro rata interest	192.5
Debt securities and other fixed-income securities maturing in the following year (nominal amount)	**1,066.8**
Deposits from other banks	**5,295.7**
Payable on demand	206.0
Up to 3 months	2,477.6

	31 Dec 2007 € mn
Between 3 months and 1 year	378.7
Between 1 year and 5 years	1,154.5
More than 5 years	618.1
Pro rata interest	460.8
Savings deposits with agreed notice period	**0.0**
Up to 3 months	0.0
Between 3 months and 1 year	0.0
Between 1 year and 5 years	0.0
Pro rata interest	0.0
Other deposits from customers	**23,060.3**
Payable on demand	4,119.1
Up to 3 months	5,158.2
Between 3 months and 1 year	946.7
Between 1 year and 5 years	1,765.6
More than 5 years	10,737.9
Pro rata interest	332.8
Bonds issued maturing in the following year (nominal amount)	**1,898.8**
Other certificated liabilities	**–**

Deferred income

Deferred items primarily include upfront payments as well as any premiums and discounts on registered bonds, claims under promissory note loans and other loans, that have been amortised over the relevant terms.

Deferred assets in the amount of € 63.6 million include € 12.9 million in premiums on originated loans, in accordance with section 340 e (2) sentence 3 of the HGB, as well as € 27.3 million in discounts on bonds issued and borrowings pursuant to section 250 (3) of the HGB.

€ 18.9 million of deferred liabilities (total: € 91.0 million) are accounted for by discounts on originated loans, in accordance with section 340 e (2) sentence 2 of the HGB.

Trust business

Trust assets	31 Dec 2007 € mn
Loans and advances to banks	–
Loans and advances to customers	822.7
Equities and other non-fixed-income securities	1.5
Total	**824.2**

Trust liabilities	31 Dec 2007 € mn
Liabilities to banks	497.7
Liabilities to customers	326.5
Total	**824.2**

Notes on affiliated companies and enterprises with a participatory interest

	Affiliated companies		Enterprises with a participatory interest	
	Certificated € mn	Not certificated € mn	Certificated € mn	Not certificated € mn
Loans and advances to banks	–	362.5	–	–
Loans and advances to customers	–	112.9	–	0.1
Debt and other non-fixed-income securities	0.0	0.0	–	–
Deposits from other banks	0.0	0.0	–	–
Deposits to customers	–	145.8	–	0.0
Securitised liabilities	–	–	–	–
Subordinated liabilities	–	250.0	–	–

Interests held in large limited companies

Aareal Bank AG does not hold any participating interest in a large limited company.

Shareholdings

The full list of shareholdings has been published in the electronic Federal Gazette and is available to the public.

Assets pledged as collateral

Total assets pledged as collateral:

	31 Dec 2007 € mn	31 Dec 2006 € mn
Loans and advances to banks	134.6	166.8
Loans and advances to customers	498.6	516.4
Debt and other fixed-income securities	2,535.5	2,026.4
Total	**3,168.7**	**2,709.6**

Repurchase agreements

The book value of bonds pledged under repo agreements totalled € 177.3 million as at 31 December 2007. In addition, outstanding open-market transactions totalled € 1,350.0 million.

Assets and liabilities in foreign currencies

The aggregate equivalent amount of assets denominated in foreign currencies, calculated under the capital ratio according to the German Banking Act (Grundsatz I), was € 9,695.5 million at the balance sheet date, while liabilities totalled € 9,686.5 million.

Forward transactions

The following forward transactions had been entered into as at 31 December 2007:

- **Transactions based on interest rates –** Caps, floors, swaptions, interest rate swaps, forward rate agreements
- **Transactions based on exchange rates –** Spot and forward foreign exchange transactions, cross-currency interest rate swaps
- **Other transactions –** Credit default swaps, credit-linked notes, equity index futures, other forward transactions

Interest-rate based transactions and cross-currency interest rate swaps are primarily used to hedge against interest rate and exchange rate fluctuations. Spot and forward foreign exchange transactions are almost exclusively used for refinancing purposes. Credit derivatives are used both to hedge Aareal Bank AG's existing credit risk exposure and to assume credit risks for the purpose of portfolio diversification.

Derivatives used to hedge interest or exchange rate risks are valued together with the underlying transaction; no individual valuation of underlying transaction and derivative is carried out.

Remaining terms and nominal amounts of derivatives are broken down in the following table:

	Nominal amount by remaining lifetime (31 Dec 2007)				Nominal amount	
	Up to 3 months € mn	3 months to 1 year € mn	1 to 5 years € mn	More than 5 years € mn	31 Dec 2007 € mn	31 Dec 2006 € mn
Interest rate instruments						
OTC products						
Interest rate swaps	2,399.2	3,460.7	18,064.3	18,465.4	42,389.6	40,604.0
Forward rate agreements	–	–	654.0	–	654.0	0.0
Swaptions	41.0	–	154.0	16.0	211.0	452.0
Caps, floors	129.7	309.0	3,692.7	420.8	4,552.2	3,814.0
Exchange-listed contracts						
Interest rate futures	–	–	–	–	0.0	900.0
Options on interest rate futures	–	–	–	–	0.0	10.0
Total interest rate instruments	**2,569.9**	**3,769.7**	**22,565.0**	**18,902.2**	**47,806.8**	**45,780.0**
Currency-related instruments						
OTC products						
Spot and forward foreign exchange transactions	23.4	222.6	4,353.8	–	4,599.8	3,290.0
Cross-currency interest rate swaps	470.7	900.3	1,634.5	356.3	3,361.8	3,382.0
Total currency-related instruments	**494.1**	**1,122.9**	**5,988.3**	**356.3**	**7,961.6**	**6,672.0**
Other forward transactions						
OTC products						
Credit default swaps*	–	–	75.0	2,635.8	2,710.8	3,396.0
Credit-linked notes*	–	–	–	950.5	950.5	1,014.0
Other forward transactions	–	–	–	53.0	53.0	53.0
Exchange-listed contracts						
Equity index futures	27.7	–	–	–	27.7	0.0
Total other forward transactions	**27.7**	**0.0**	**75.0**	**3,639.3**	**3,742.0**	**4,463.0**
Total	**3,091.7**	**4,892.6**	**28,628.3**	**22,897.8**	**59,510.4**	**56,915.0**

** including € 942 million in financial guarantees*

The table below shows positive and negative market values, aggregated by product level (without taking into account collateral or netting agreements): Unless a quoted market price is available, valuation of derivatives is based on recognised methods such as cash flow analyses, or options pricing models.

	Market value (31 Dec 2007)		Market value (31 Dec 2006)	
	positive € mn	negative € mn	positive € mn	negative € mn
Interest rate instruments				
OTC products				
Interest rate swaps	376.0	818.4	396.0	648.0
Forward rate agreements	4.7	4.5		
Swaptions	0,0	0.9	0.0	1.0
Caps, floors	14.2	14.1	9.0	9.0
Exchange-listed contracts				
Interest rate futures	–	–	1.0	0.0
Total interest rate instruments	**394.9**	**837.9**	**406.0**	**658.0**
Currency-related instruments				
OTC products				
Spot and forward foreign exchange transactions	85.3	7.0	32.0	13.0
Cross-currency interest rate swaps	214.6	9.8	88.0	35.0
Total currency-related instruments	**299.9**	**16.8**	**120.0**	**48.0**
Other forward transactions				
OTC products				
Credit default swaps*	14.2	5.1	30.0	–
Credit-linked notes*	–	2.2	–	6.0
Other forward transactions	2.4	2.5	2.0	4.0
Exchange-listed contracts				
Equity index futures	–	0.4	–	–
Total other forward transactions	**16.6**	**10.2**	**32.0**	**10.0**
Total	**711.4**	**864.9**	**558.0**	**716.0**

**excluding financial guarantees*

Derivatives have been entered into with the following counterparties:

	Market value (31 Dec 2007)		Market value (31 Dec 2006)	
	positive € mn	negative € mn	positive € mn	negative € mn
OECD public-sector authorities				
OECD banks	670.9	799.3	548.0	667.0
Non-OECD banks				
Companies and private individuals	40.5	65.6	10.0	49.0
Total	**711.4**	**864.9**	**558.0**	**716.0**

OTHER NOTES

Disclosures in accordance with German Pfandbrief Act (section 28)

Total amount and related cover assets pool of outstanding mortgage bonds and public-sector covered securities

31 Dec 2007	Cover assets pool € mn	Covered bonds outstanding € mn	Excess cover € mn
Mortgage bonds			
Nominal value	5,641.0	4,714.0	927.0
Present value	5,866.5	4,749.0	1,117.5
Public-sector covered bonds			
Nominal value	3,433.9	3,090.3	343.6
Present value	3,423.6	3,057.8	365.8

31 Dec 2006	Cover assets pool € mn	Covered bonds outstanding € mn	Excess cover € mn
Mortgage bonds			
Nominal value	4,271.7	3,119.3	1,152.4
Present value	4,434.2	3,172.8	1,261.4
Public-sector covered bonds			
Nominal value	3,246.8	2,685.2	561.6
Present value	3,445.7	2,799.3	646.4

	2007 Share of derivatives in Cover assets pool %	2006 Share of derivatives in Cover assets pool %	2007 Risk-adjusted net present value € mn	2006 Risk-adjusted net present value € mn
Mortgage bonds	27.5	-0.11	983.3	1,125.8
Public-sector covered bonds	0.1	0.00	287.6	590.2

Maturity structure as well as fixed-interest periods of the corresponding cover assets pool

31 Dec 2007	Cover assets pool € mn	Covered bonds outstanding € mn
Mortgage bonds		
Up to 1 year	535.2	417.6
Between 1 year and 5 years	3,189.2	2,824.1
Between 5 years and 10 years	1,724.8	1,347.3
More than 10 years	191.8	125.0
Total	**5,641.0**	**4,714.0**
Public-sector covered bonds		
Up to 1 year	195.4	190.2
Between 1 year and 5 years	698.3	542.4
Between 5 years and 10 years	940.6	1,110.7
More than 10 years	1,599.6	1,247.0
Total	**3,433.9**	**3,090.3**

31 Dec 2006	Cover assets pool € mn	Covered bonds outstanding € mn
Mortgage bonds		
Up to 1 year	309.9	171.6
Between 1 year and 5 years	2,331.5	1,782.7
Between 5 years and 10 years	1,444.7	1,165.0
More than 10 years	185.6	0.0
Total	**4,271.7**	**3,119.3**
Public-sector covered bonds		
Up to 1 year	276.2	5.0
Between 1 year and 5 years	811.1	445.6
Between 5 years and 10 years	786.5	987.8
More than 10 years	1,373.0	1,246.8
Total	**3,246.8**	**2,685.2**

Loans and advances used to cover mortgage bonds

Distribution of the amounts measured at nominal value by volume:	Cover assets pool 2007 € mn	Cover assets pool 2006 € mn
Up to € 300,000	116.5	167.0
Between € 300,000 to € 5 mn	565.7	516.2
More than € 5 mn	4,958.8	3,588.5
Total	**5,641.0**	**4,271.7**

The loans and advances used for lending against mortgage bonds did not include any items with payment arrears of 90 days or more.

Distribution of the amounts measured at nominal value by countries in which the real property collateral is located:

31 Dec 2007			Commercial property					Residential property				
	Pure building sites	Buildings not yet yielding returns	Office buildings	Whole-sale/retail properties	Industrial	Other	Total	Single-family homes	Multi-family homes	Apart-ments	Total	Total cover assets pool
	€ mn	€ mn	€ mn	€ mn	€ mn	€ mn	€ mn	€ mn	€ mn	€ mn	€ mn	€ mn
Belgium			20.9		7.1		**28.0**				**0.0**	28.0
Canada			48.5			61.0	**109.5**				**0.0**	109.5
Czech Republic			91.9			56.0	**147.9**				**0.0**	147.9
Denmark			104.5	42.4	7.1	31.3	**185.3**				**0.0**	185.3
Finland			27.4	226.1	5.4	20.4	**279.3**				**0.0**	279.3
France			17.9	58.9	106.5	45.3	**228.6**				**0.0**	228.6
Germany	1.4		145.8	37.3	114.2	117.1	**414.4**	51.8	20.6	560.9	**633.3**	1,049.1
Italy			512.1	193.7	10.3	74.0	**790.1**			123.5	**123.5**	913.6
Netherlands			175.4	22.7	111.7	71.6	**381.4**			19.0	**19.0**	400.4
Poland			168.5	295.7	31.5		**495.7**				**0.0**	495.7
Republic of Slovakia						48.6	**48.6**				**0.0**	48.6
Spain				289.6		39.8	**329.4**				**0.0**	329.4
Sweden			149.8	71.9	154.6	57.9	**434.2**				**0.0**	434.2
Switzerland			140.5	50.8	2.8	25.4	**219.5**				**0.0**	219.5
United Kingdom			174.7	56.3	67.5		**298.5**				**0.0**	298.5
USA				13.4			**13.4**			56.6	**56.6**	69.9
Total	**1.4**	**0.0**	**1,777.9**	**1,358.8**	**618.7**	**648.4**	**4,403.8**	**51.8**	**20.6**	**760.0**	**832.4**	**5,237.6**

31 Dec 2006			Commercial property					Residential property				
	Pure building sites	Buildings not yet yielding returns	Office buildings	Whole-sale/retail propertie	Industrial	Other	Total	Single-family homes	Multi-family homes	Apart-ments	Total	Total cover assets pool
	€ mn	€ mn	€ mn	€ mn	€ mn	€ mn	€ mn	€ mn	€ mn	€ mn	€ mn	€ mn
Belgium			4.2				**4.2**					**4.2**
Canada			39.3			41.1	**80.4**					**80.4**
Czech Republic			42.9				**42.9**					**42.9**
Denmark			87.2	46.2	4.0	71.0	**208.4**					**208.4**
Finland				104.3			**104.3**					**104.3**
France		19.5	68.0	34.3	41.8	40.7	**184.8**					**204.3**
Germany			155.2	52.8	44.8	134.2	**387.1**	75.2	30.2	467.5	572.9	**960.0**
Italy			308.5	160.5		21.7	**490.6**					**490.6**
Netherlands			119.3		127.2	37.9	**284.4**			16.4	16.4	**300.8**
Poland			70.9	66.2	22.9		**160.0**					**160.0**
Spain				213.1			**213.1**					**213.1**
Sweden			52.7	66.0	172.3		**290.9**			66.0	66.0	**356.9**
Switzerland			83.9	49.1		26.2	**159.2**					**159.2**
United Kingdom			169.2	61.5	27.5	150.3	**408.4**					**408.4**
USA				4.2		38.8	**43.0**			34.2	34.2	**77.2**
Total	**0.0**	**19.5**	**1,201.2**	**858.3**	**440.4**	**561.9**	**3,061.7**	**75.2**	**30.2**	**584.1**	**689.5**	**3,770.7**

In the financial year 2007, the bank did not acquire any properties for the purpose of loss prevention (2006: none).

As at 31 December 2007, interest payments in the amount of € 2.8 million (2006: € 3.6 million) for commercial property and in the amount of € 0.3 million (2006: € 0.3 million) for residential property were overdue for less than 90 days.

In the year under review, there were no interest payments from mortgagors overdue for at least 90 days.

Redemptions in cover assets pool

	2007 Commercial property € mn	2006 Commercial property € mn	2007 Residential property € mn	2006 Residential property € mn
Scheduled repayments	82.1	41.7	30.1	54.2
Extraordinary repayments	803.8	753.9	127.6	192.0
Total	**885.9**	**795.6**	**157.6**	**246.2**

Distribution of the loans and advances measured at nominal value and used to cover public-sector covered bonds by countries in which the debtor or the guaranteeing body is located:

31 Dec 2007	Sovereigns	Public-sector entities		Other	Total
		regional	municipal		
	€ mn	€ mn	€ mn	€ mn	€ mn
Germany	200.0	1,812.0	0.0	670.1	2,682.1
Italy	114.0	0.0	0.0	0.0	114.0
France	0.0	0.0	0.0	43.2	43.2
United Kingdom	0.0	0.0	0.0	7.5	7.5
Austria	124.2	25.0	0.0	70.0	219.2
Switzerland	0.0	50.0	0.0	0.0	50.0
Spain	0.0	178.5	5.0	4.4	187.9
Hungary	0.0	0.0	0.0	25.0	25.0
Japan	0.0	0.0	0.0	50.0	50.0
Portugal	0.0	0.0	30.0	25.0	55.0
Total	**438.2**	**2,065.5**	**35.0**	**895.2**	**3,433.9**

31 Dec 2006	Sovereigns	Public-sector entities		Other	Total
		regional	municipal		
	€ mn	€ mn	€ mn	€ mn	€ mn
Germany	325.0	1,691.3	0.0	792.6	2,808.9
Italy	210.0	0.0	0.0	0.0	210.0
France	0.0	0.0	0.0	30.2	30.2
Austria	124.2	0.0	0.0	20.0	144.2
Spain	0,0	0.0	35.0	18.5	53.5
Total	**659.2**	**1,691.3**	**35.0**	**861.3**	**3,246.8**

Contingencies

By means of letters of comfort, Aareal Bank AG ensures that Deutsche Structured Finance GmbH, Frankfurt, DSF Beteiligungsgesellschaft mbH, Frankfurt, and Aareal Bank Capital Funding LLC, Wilmington, are able to fulfil their contractual obligations.

Aareal Bank AG has issued a letter of comfort to the Monetary Authority of Singapore, guaranteeing that Aareal Bank Asia Ltd. will honour its obligations at all times.

Due to its participating interest in Liquiditäts-Konsortialbank GmbH, Frankfurt / Main, in the nominal amount of € 1.0 million, Aareal Bank AG has call commitments of up to € 6.0 million. In addition, Aareal Bank AG has a pro-rata principal liability in the event of non-fulfilment of call commitments by other co-shareholders, who hold aggregate interests of € 63.0 million.

Consolidated financial statements

As the parent company of the Aareal Bank Group, Aareal Bank AG, Wiesbaden, prepares Consolidated Financial Statements incorporating the bank. The consolidated financial statements will be deposited with the Register of Companies, published in the electronic German Federal Gazette, and are available on the bank's website, or from Aareal Bank AG in Wiesbaden, Germany.

Loans to executive bodies of Aareal Bank

Loans granted to members of the Supervisory Board amounted to € 3.3 million as at 31 December 2007 (31 December 2006: € 3.5 million). Loans and advances to members of the Management Board totalled € 0.0 million (2006: € 0.0 million). Total loans and advances to other related parties amounted to € 2.6 million (2006: € 2.8 million) as at the balance sheet date. Loans extended generally have a term between ten and 15 years, and bear interest at rates between 3.05 % and 7.64 %.

Remuneration report

Remuneration for members of the Management Board

The Executive Committee of the Supervisory Board determines the structure and amount of remuneration for members of the Management Board. The Committee sets salaries and other remuneration components for members of the Management Board.

Aareal Bank AG has entered into fixed-term service contracts with the members of its Management Board.

In addition to fixed salary components, which are paid in twelve identical monthly instalments, the members of the Management Board receive a bonus in form of a variable remuneration and are granted phantom shares as a long-term remuneration (Long-term Component I), which may be exercised after a waiting period of three years in the three years following such waiting period. The members of the Management Board receive an additional long-term component that entitles them to exercise allocated phantom shares, of which a quarter are allocated in the year of allocation and in the three following years, and provided the member of the Management Board has not terminated his service contract at the time of exercise (long-term component 2).

The basis for this variable remuneration component is a target system, largely based on net income (of the Group) as reported under International Financial Reporting Standards (IFRS), as well as qualitative and quantitative targets, which are re-defined annually.

Cash payments made to members of the Management Board amounted to:

	2007 €	2006 €
Fixed remuneration	1,520,000.00	1,520,000.00
Variable remuneration / bonus	2,145,000.00	2,145,000.00
Other remuneration	376,120.70	99,948.19
Total remuneration	**4,041,120.70**	**3,764,948.19**

The breakdown of the amounts stated amongst the members of the Management Board is shown in the following table.

	Year	Fixed remuneration €	Cash bonus €	Other [1] €	Total €
Dr. Wolf Schumacher	2007	500,000.00	900,000.00	44,493.93	1,444,493.93
	2006	500,000.00	900,000.00	24,144.03	1,424,144.03
Norbert Kickum	2007	300,000.00	435,000.00	238,287.73 [2]	973,287.73
	2006	300,000.00	435,000.00	22,036.35	757,036.35
Hermann J. Merkens	2007	420,000.00	375,000.00	53,163.31	848,163.31
	2006	420,000.00	375,000.00	31,753.05	826,753.05
Thomas Ortmanns	2007	300,000.00	435,000.00	40,175.73	775,175.73
	2006	300,000.00	435,000.00	22,014.76	757,014.76
Total	**2007**				**4,041,120.70**
	2006				**3,764,948.19**

As a long-term remuneration component, the Management Board was allocated a total of 149,928.72 phantom shares; at a price of € 31.30 as at 31 December 2007, their aggregate value was € 4,692,768.84. The breakdown of the phantom shares amongst the members of the Management Board is shown below:

	Year	Long-term component I		Long-term component II		Total		Value as at 31 Dec 2007 (€)
		Value as at award date (€)	Number	Value as at award date (€)	shares [3] [4]	shares	Value as at award date (€)	
Dr. Wolf Schumacher	2007	735,000.00	23,482.43 [3]	500,000.00	14,838.41	38,320.84	1,235,000.00	1,199,442.32
	2006	450,000.00	12,332.15			12,332.15	450,000.00	385,996.30
Norbert Kickum	2007	720,000.00	23,003.19 [3]	500,000.00	14,838.41	37,841.60	1,220,000.00	1,184,442.15
	2006	435,000.00	11,921.07			11,921.07	435,000.00	373,129.49
Hermann J. Merkens	2007	660,000.00	21,086.26 [3]	500,000.00	14,838.41	35,924.67	1,160,000.00	1,124,442.22
	2006	375,000.00	10,276.79			10,276.79	375,000.00	321,663.53
Thomas Ortmanns	2007	720,000.00	23,003.19 [3]	500,000.00	14,838.41	37,841.60	1,220,000.00	1,184,442.15
	2006	435,000.00	11,921.07			11,921.07	435,000.00	373,129.49

[1] *Other remuneration includes payments (in particular for company cars) in the amount of € 53,772.86 in 2007 (2006: € 54,429.13) as well as benefits related to social security contributions totalling € 43,084.32 (2006: € 45,519.06). Figures for 2007 also include payments for theoretical dividends on phantom shares.*

[2] *This amount includes a payment of € 195,532.96 made upon partial exercise of phantom shares.*

[3] *This is equivalent to the value of phantom shares that will be converted at the time of allocation, in line with the rules set out in the plans for share-based remuneration via phantom shares; specifically, following publication of the 2007 financial statements, as confirmed by the Supervisory Board. For the purposes of this report, the number of phantom shares was determined using the share price of € 31.30 as at 31 December 2007.*

[4] *Including 6,851.19 phantom shares each which were already allocated in 2007, at a price of € 36.49 determined in line with regulations.*

This results in the following total amount of phantom shares held by the individual members of the Management Board:

	Phantom shares held at 31 Dec 2006		exercised in 2007	Phantom shares held at 31 Dec 2007	
	Number	Value as at 31 Dec 2006 (€)[1)]	Number	Number	Value as at 31 Dec 2007 (€)[2)]
Dr. Wolf Schumacher	16,828.55	593,542.96	0.00	55,149.39	1,726,175.91
Norbert Kickum	11,921.07	420,456.14	6,851.19	42,911.48	1,343,129.32
Hermann J. Merkens	17,171.27	605,630.69	0.00	53,095.94	1,661,902.92
Thomas Ortmanns	11,921.07	420,456.14	0.00	49,762.67	1,557,571.57

[1)] Price: € 35.27, [2)] Price: € 31.30

Christof M. Schörnig retired from his office on the Management Board on 30 September 2007. In addition to his fixed remuneration of € 225,000 (2006: € 300,000), Mr Schörnig received a payment of € 2,700,000 to compensate his remuneration claims for the remaining term of his contract. Furthermore, he received a payment of € 271,581.17 through the exercise of 6,851.19 phantom shares allocated to him. Mr Schörnig has a right to exercise 20,614.12 phantom shares, which were allocated to him during his period of service and not yet exercised, until 30 September 2008. At a price of € 31.30 as at 31 December 2007, the value of these phantom shares was € 645,221.96.

Additional pension provisions were recognised in an amount of € 643,690.05 (2006: € 242,915.00). The total of pension provisions for active and former members of the Management Board and their surviving dependants amount to € 8,951,446.00 (2006: € 7,910,647.00). Members of the Management Board who joined the Company before 1 January 2005 are entitled to receive contractual pension payments before they reach the age of 65 when they have served for a period of five years, in case the bank rejects to extend their service contracts. Payments from other employment relationships and other pension plans, if any, are taken into account.

Payments to former Management Board members of Aareal Bank AG and their surviving dependants totalled € 571,790.11 (2006: € 490,151.64).

The agreements concluded with members of the Management Board do not include any express obligation to make severance payments in case of an early termination of employment relationships. However, severance payments may be included in individual termination agreements.

In the case of a change of control and a resulting loss of membership in the Management Board, the members affected receive, in settlement of their total remuneration, their fixed remuneration as well as a contractually agreed compensation for the variable remuneration, paid in monthly instalments during the remaining term of the agreements. In addition, the members of the Management Board receive a lump-sum payment of up to 75 % of their annual fixed remuneration.

If, in case of a change of control, members of the Management Board resign from office or are not willing to extend their office in spite of an offer on the part of the Company, the respective member of the Management Board receives, in settlement of the total remuneration, an amount not exceeding 50 % of the relevant fixed remuneration and the contractually agreed compensation for the variable remuneration. In addition, the relevant member of the Management Board receives a lump-sum payment of up to 50 % of the annual fixed remuneration.

Remuneration for members of the Supervisory Board

The remuneration of the Supervisory Board is specified in Section 9 of the Memorandum and Articles of Association of Aareal Bank AG. The resolution passed at the Annual General Meeting of 23 May 2006 determined the current remuneration that was adjusted in line with the remuneration system of the Supervisory Board. For the financial year 2007, the remuneration for the members of the Supervisory Board for the full financial year is based on the new methodology for the first time.

The total remuneration of the Supervisory Board comprises a fixed and a variable remuneration component comparable to the remuneration package of the Management Board. The variable remuneration is performance-related and comprises a short-term and a long-term component.

The fixed remuneration is € 20,000.00 p.a. for each Supervisory Board member. The Chairman of the Supervisory Board shall receive twice the amount, while the deputy shall receive one and a half times as much as a normal member. The fixed remuneration shall be increased by € 10,000.00 p.a. for any Supervisory Board committee member (with the exception of the Committee for Urgent Decisions, which is a part of the Credit and Market Risk Committee). The fixed remuneration shall be increased instead by € 20,000.00 p.a. for Chairmanship of a Supervisory Board committee (also with the exception of the Committee for Urgent Decisions, which is a part of the Credit and Market Risk Committee). The fixed remuneration component of a Supervisory Board member, including the remuneration for the Chairmanship of a Supervisory Board committee, forms a basis for assessing the performance-related remuneration.

The performance-related remuneration only comes into effect if a dividend is paid for the financial year in question that exceeds at least € 0.20 per share.

The short-term performance-related remuneration currently amounts to 12.5 % of the individual assessment basis for each full € 50 million of the consolidated net income attributable to shareholders of Aareal Bank AG as reported in the Group income statement. However, it may not exceed 50 % of the individual assessment basis.

The long-term performance-related remuneration of a Supervisory Board member amounts to 12.5 % of the individual assessment basis for each 10% increase in the consolidated net income attributable to shareholders of Aareal Bank AG (as reported in the consolidated income statement) over the unweighted average of the consolidated net income attributable to shareholders of Aareal Bank AG for the three previous full financial years. The long-term profit-oriented remuneration is not paid if the average value is negative. On this basis, the members of the Supervisory Board are not entitled to a long-term performance-related remuneration for the 2007 financial year.

The maximum long-term performance-related remuneration is capped at 50 % of the individual assessment basis, so that the aggregate variable remuneration may amount to a maximum of 100 % of the fixed remuneration component.

The fixed remuneration is due at the end of each financial year. The variable remuneration component is due after the Annual General Meeting in which a resolution is passed on the appropriation of net income for the relevant financial year. The bank reimburses the VAT amounts to be paid on the remuneration.

In accordance with the presented methodology, the members of the Supervisory Board receive a fixed remuneration for the financial year 2007 in the amount of € 559,300.00 (2006: € 621,971.58) and, provided that the Annual General Meeting approves the proposal of the Management on the appropriation of net income, a variable remuneration of € 202,300.00 (2006: € 63,710.55).

The individual amount of the remuneration for the Supervisory Board is shown in the table on page 79. The variable remuneration was recognised under the assumption that the Annual General Meeting approves the Management's proposal on the distribution of earnings. The figures in the table include the reimbursement for VAT (19 %).

The members of the Supervisory Board did not provide any consulting or agency services, or other personal services in 2007. Therefore, no additional remuneration was paid.

	Fixed remuneration Total €	Variable remuneration Total €	Total remuneration €
Hans W. Reich, Chairman	107,100.00	47,600.00	154,700.00
Erwin Flieger, Deputy Chairman	59,500.00	17,850.00	77,350.00
York-Detlef Bülow, Deputy Chairman	59,500.00	17,850.00	77,350.00
Tamara Birke	35,700.00	11,900.00	47,600.00
Thomas Hawel	23,800.00	11,900.00	35,700.00
Helmut Wagner	23,800.00	11,900.00	35,700.00
Christian Graf von Bassewitz	47,600.00	11,900.00	59,500.00
Manfred Behrens	23,800.00	11,900.00	35,700.00
Joachim Neupel	59,500.00	23,800.00	83,300.00
Dr. Herbert Lohneiß	35,700.00	11,900.00	47,600.00
Prof. Dr. Stephan Schüller	47,600.00	11,900.00	59,500.00
Wolf R. Thiel	35,700.00	11,900.00	47,600.00
Total	**559,300.00**	**202,300.00**	**761,600.00**

Employees

The average staffing level is shown below:

Employees	2007	2006
Full-time employees	945	993
Part-time employees	141	139
Vocational and other trainees	13	13
Total	**1,099**	**1,145**

Auditors' fees

The following auditors' fees were recognised as expenses during the financial year:

Category	€ 000's
Audit	1,644.6
Other audit or valuation services	243.9
Tax advisory services	203.2
Other services	615.9
Total	**2,707.6**

Notice pursuant to section 21 (1) of the WpHG

On 16 January 2008, Fidelity Investment Trust, Boston, Massachusetts, USA, notified us according to section 21 (1) of the German Securities Trading Act (Wertpapierhandelsgesetz, WpHG) that, on the basis of shares held, its share of voting rights in Aareal Bank AG, Wiesbaden, Germany, ISIN: DE0005408116, WKN: 540811, exceeded the threshold of 3 % of total voting rights on 6 August 2007 and now amounts to 3.08 % (corresponding to 1,315,235 voting rights).

On 1 November 2007, Fidelity International, Tadworth, United Kingdom, notified us of the following:

"As a result of an internal merger reorganisation effective from 1st October 2007, FMR LLC. (a Delaware limited liability company with its principal place of business in Boston, USA) became the successor entity to FMR Corp. and has assumed all its rights and obligations. We therefore notify you that on 1st October 2007 FMR LLC. held 3.29 % of the voting rights (voting rights arising of 1,404,640 shares in Aareal Bank AG) and therefore exceeded the threshold of 3%. All of the voting rights of FMR LLC. are attributed to it pursuant to sec. 22 para. 1. sent 1 no. 6 and sent. 2 of the German Securities Trade Act."

Correction of the notification dated 18 September 2007: On 14 September 2007, Julius Bär Holding, Zurich, Switzerland notified us of the following:

"Notification pursuant to section 21 (1) of the WpHG
We herewith notify you in accordance with section 21 (1) of the WpHG that our share of voting rights in Aareal Bank AG, Paulinenstrasse 15, 65189 Wiesbaden, Germany, fell below the threshold of 3 % on 11 September 2007 and amounted to 2.99 % at that time (exact number of voting rights: 1,277,706 shares), both in terms of the total number of voting rights of the issuer and in terms of all shares equipped with voting rights of one and the same class. The voting rights are fully attributable to us via Julius Baer Investment Management LLC, New York, USA, pursuant to section 22 (1) sentence 1 No. 6 of the WpHG in conjunction with section 22 (1) sentence 2 of the WpHG."

Underlying notification of Julius Baer Investment Management LLC, New York, USA:

"We herewith notify you in accordance with section 21 (1) of the WpHG that our share of voting rights in Aareal Bank AG, Paulinenstrasse 15, 65189 Wiesbaden, Germany, fell below the threshold of 3 % on 11 September 2007 and amounted to 2.99 % at that time (exact number of voting rights: 1,277,706 shares), both in terms of the total number of voting rights of the issuer and in terms of all shares equipped with voting rights of one and the same class. The voting rights are fully attributable to us pursuant to section 22 (1) sentence 1 No. 6 of the WpHG."

In September 2007, Aareal Bank AG published the notification of Julius Baer Investment Management LLC:

"We herewith notify you in accordance with section 21 (1) of the WpHG that our share of voting rights in Aareal Bank AG, Paulinenstrasse 15, 65189 Wiesbaden, Germany, fell below the threshold of 3 % on 11 September 2007 and amounted to 2.99 % at that time (exact number of voting rights: 1,277,706 shares), both in terms of the total number of voting rights of the issuer and in terms of all shares equipped with voting rights of one and the same class. The voting rights are fully attributable to us via Julius Baer Investment Management LLC, 330 Madison Avenue, NY 10017 New York, USA, pursuant to section 22 (1) sentence 1 No. 6 of the WpHG in conjunction with section 22 (1) sentence 2 of the WpHG."

Underlying notification of Julius Baer Investment Management LLC, New York, USA:

"We herewith notify you in accordance with section 21 (1) of the WpHG that our share of voting rights in Aareal Bank AG, Paulinenstrasse 15, 65189 Wiesbaden, Germany, fell below the threshold of 3 % on 11 September 2007 and amounted to 2.99 % at that time (exact number of voting rights: 1,277,706 shares), both in terms of the total number of voting rights of the issuer and in terms of all shares equipped with voting rights of one and the same class. The voting rights are fully attributable to us pursuant to section 22 (1) sentence 1 No. 6 of the WpHG."

On 14 September 2007, Julius Baer Americas Inc., USA, notified us of the following:

"Notification pursuant to section 21 (1) of the WpHG
We herewith notify you in accordance with section 21 (1) of the WpHG that our share of voting rights in Aareal Bank AG, Paulinenstrasse 15, 65189 Wiesbaden, Germany, fell below the threshold of 3 % on 11 September 2007 and amounted to 2.99 % at that time (exact number of voting rights: 1,277,706 shares), both in terms of the total number of voting rights of the issuer and in terms of all shares equipped with voting rights of one and the same class. The voting rights are fully attributable to us via Julius Baer Investment Management LLC, 330 Madison Avenue, NY 10017 New York, USA, pursuant to section 22 (1) sentence 1 No. 6 of the WpHG in conjunction with section 22 (1) sentence 2 of the WpHG."

On 3 August 2007, BT Pension Scheme, London, United Kingdom, notified us as follows:

"Notification pursuant to § 21, 22 WpHG: Aareal Bank AG (Sedol No. 7380062)
We hereby give notice, pursuant to § 21 para. 1 of the WpHG, that on 2nd August 2007 the voting interest held by Hermes Focus Asset Management Europe Limited., Lloyds Chambers, 1 Portsoken Street, London E1 8HZ U. K. in Aareal Bank AG, Paulinenstrasse 15, 65189 Wiesbaden, Germany, increased above the threshold of 3 % and amounted to 10,225 %, i.e. 4,371,792 voting rights at this day.

9.596 % of the voting shares are held by Hermes Focus Asset Management Europe Limited. These are attributable to the BT Pension Scheme in accordance with § 22 para. 1 sent. 1 No. 7 of the WpHG.

As the majority of shares in Hermes Focus Asset Management Europe Limited is owned by BT Pension Scheme, the following notification is also necessary:

We hereby give notice, pursuant to § 21 para. 1 of the WpHG, that on 2nd August 2007 the voting interest held by BT Pension Scheme, Lloyds Chambers, 1 Portsoken Street, London E1 8HZ U. K. in Aareal Bank AG, Paulinenstrasse 15, 65189 Wiesbaden, Germany, increased above the threshold of 3 % and amounted to 10.225 %, i.e. 4,371,792 voting rights at this day. All voting rights are attributable to BT Pension Scheme in accordance with § 22 para. 1 sent. 1 no. 6 and sent. 2 of the WpHG. BT Pension Scheme is the majority shareholder of Hermes Focus Asset Management Europe Limited."

On 19 June 2007, Union Investment Privatfonds GmbH, 60329 Frankfurt, Germany, notified us according to section 21 (1) of the WpHG that, on the basis of shares held, its share of voting rights in Aareal Bank AG, Wiesbaden, Germany, ISIN: DE0005408116, WKN: 540811, fell below the threshold of 3 % of all voting rights on 19 June 2007 and now amounts to 2.91 % (corresponding to 1,244,500 voting rights).

On 23 May 2007, Union Investment Luxembourg S. A. 308, route d'Esch, L-1471 Luxembourg, Luxembourg, notified us according to section 21 (1) of the WpHG that, on the basis of shares held, its share of voting rights in Aareal Bank AG, Wiesbaden, Germany, ISIN: DE0005408116, WKN: 540811, fell below the threshold of 3 % of total voting rights on 22 May 2007 and now amounts to 1.38 % (corresponding to 588,147 voting rights).

Corporate Governance Code

The declaration regarding the German Corporate Governance Code, pursuant to section 161 of the AktG, has been published on our website: http://www.aareal-bank.com/servlet/PB/menu/1002243_l1/index.html.

Proposal on the appropriation of profits

The Management Board proposes to the Annual General Meeting to pay a dividend of € 0.50 per no-par value share, totalling € 21,377,579.50, from net retained profit of € 142,877,579.50 reported in the financial year 2007.

They also propose to the Annual General Meeting to transfer the remaining distributable profit of € 121,500,000.00 million to other retained earnings.

EXECUTIVE BODIES OF AAREAL BANK AG

OFFICES HELD IN ACCORDANCE WITH SECTION 285 No. 10 OF THE GERMAN COMMERCIAL CODE (HGB) IN CONJUNCTION WITH SECTION 125 (1) SENTENCE 3 OF THE GERMAN STOCK CORPORATION ACT (AktG)

Membership in other statutory Supervisory Boards and similar offices held in other governing bodies

SUPERVISORY BOARD

Hans W. Reich, Chairman of the Supervisory Board

Chairman Public Sector Group, Citigroup (since 1 July 2007), Chairman Public Sector Group Europe, Middle East, Africa of Citigroup Global Markets Deutschland AG & Co. KGaA (until 30 June 2007)

Aareal Bank AG	Chairman of the Supervisory Board	
DEPFA BANK plc	Non-executive member of the Board of Directors	until 5 Oct 2007
HUK-COBURG Haftpflicht Unterstützungskasse kraftfahrender Beamter Deutschlands a. G. in Coburg	Member of the Supervisory Board	
HUK-COBURG-Holding AG	Member of the Supervisory Board	
ThyssenKrupp Steel AG	Member of the Supervisory Board	

Erwin Flieger, Deputy Chairman of the Supervisory Board

Chairman of the Management Boards of Bayerische Beamten Lebensversicherung a.G., of BBV Holding AG and Bayerische Beamten Versicherung AG (until 13 July 2007), Chairman of the Supervisory Boards of Bayerische Beamten Lebensversicherung Gruppe (since 13 July 2007)

Aareal Bank AG	Deputy Chairman of the Supervisory Board	
Bayerische Beamten Lebensversicherung a.G.	Chairman of the Management Board	until 13 July 2007
Bayerische Beamten Lebensversicherung a.G.	Chairman of the Supervisory Board	since 13 July 2007
Bayerische Beamten Versicherung AG	Chairman of the Management Board	until 13 July 2007
Bayerische Beamten Versicherung AG	Chairman of the Supervisory Board	since 13 July 2007
BBV Holding AG	Chairman of the Management Board	until 13 July 2007
BBV Holding AG	Chairman of the Supervisory Board	since 13 July 2007
BBV Krankenversicherung AG	Chairman of the Supervisory Board	
DePfa Holding Verwaltungsgesellschaft mbH	Chairman of the Supervisory Board	
Neue Bayerische Beamten Lebensversicherung AG	Chairman of the Supervisory Board	

York-Detlef Bülow, Deputy Chairman of the Supervisory Board*

Aareal Bank AG

Aareal Bank AG	Deputy Chairman of the Supervisory Board

** Employee representative member of the Supervisory Board of Aareal Bank AG*

Christian Graf von Bassewitz

Banker (ret'd.)

Aareal Bank AG	Member of the Supervisory Board	
Bank für Sozialwirtschaft Aktiengesellschaft	Member of the Supervisory Board	
Deutscher Ring Krankenversicherungsverein a.G.	Member of the Supervisory Board	
OVB Holding AG	Member of the Supervisory Board	
Societaet CHORUS AG	Member of the Supervisory Board	

Manfred Behrens

Managing Director of Schweizerische Lebensversicherungs- und Rentenanstalt (Swiss Life), German branch office

Aareal Bank AG	Member of the Supervisory Board	
DePfa Holding Verwaltungsgesellschaft mbH	Member of the Supervisory Board	
Swiss Life Insurance Solutions AG	Chairman of the Supervisory Board	
Swiss Life Partner AG	Chairman of the Supervisory Board	until 30 Dec 2007

Tamara Birke *

Aareal Bank AG

Aareal Bank AG	Member of the Supervisory Board	
SIRWIN AG	Member of the Supervisory Board	

Thomas Hawel*

Aareon Deutschland GmbH

Aareal Bank AG	Member of the Supervisory Board	
Aareon Deutschland GmbH	Deputy Chairman of the Supervisory Board	

Dr. Herbert Lohneiß

Chief Executive Officer of Siemens Financial Services GmbH (until 30 September 2007)
(until 31 March 2008 Employee of Siemens Financial Services GmbH)

Aareal Bank AG	Member of the Supervisory Board	
INNOVEST Finanzdienstleistungs AG	Member of the Supervisory Board	until 30 Sep 2007
Siemens Financial Services Inc. USA	Chairman of the Supervisory Board	until 30 Sep 2007
Siemens Kapitalanlagegesellschaft	Chairman of the Supervisory Board	
Siemens Project Venture GmbH	Member of the Shareholder Representatives Group	until 30 Sep 2007
UBS Real Estate Kapitalanlagegesellschaft mbH	Deputy Chairman of the Supervisory Board	

** Employee representative member of the Supervisory Board of Aareal Bank AG*

Joachim Neupel, Chairman of the Accounts and Audit Committee

Certified Accountant and Tax Advisor		
Aareal Bank AG	Member of the Supervisory Board	
IKB Immobilien Management GmbH	Chairman of the Supervisory Board	until 31 Aug 2007

Prof. Dr. Stephan Schüller

Spokesman of the General Partners of Bankhaus Lampe KG		
Aareal Bank AG	Member of the Supervisory Board	
BVT-Equity-Holding	Chairman of the Board of Directors	
BVT-Holding GmbH	Chairman of the Supervisory Board	
Choren Fuel Freiberg GmbH & Co KG,	Chairman of the Supervisory Board	
Choren Industries GmbH	Chairman of the Supervisory Board	
Condor/Optima Versicherungen AG	Deputy Chairman of the Supervisory Board	
DePfa Holding Verwaltungsgesellschaft mbH	Member of the Supervisory Board	
NANORESINS AG	Chairman of the Supervisory Board	
PONAXIS AG	Chairman of the Supervisory Board	
Universal-Investment-Gesellschaft mbH	Member of the Supervisory Board	
hanse chemie AG	Chairman of the Supervisory Board	since 5 Mar 2007

Wolf R. Thiel

President and Chairman of the Management Board of Versorgungsanstalt des Bundes und der Länder	
Aareal Bank AG	Member of the Supervisory Board
DePfa Holding Verwaltungsgesellschaft mbH	Member of the Supervisory Board

Helmut Wagner*

Aareon Deutschland GmbH	
Aareal Bank AG	Member of the Supervisory Board
Aareon Deutschland GmbH	Member of the Supervisory Board

** Employee representative member of the Supervisory Board of Aareal Bank AG*

MANAGEMENT BOARD

Dr. Wolf Schumacher, Chairman of the Management Board

Aareal Asset Management GmbH	Member of the Supervisory Board	until 28 Feb 2007
Aareal Estate AG	Deputy Chairman of the Supervisory Board	
Aareal Valuation GmbH	Chairman of the Supervisory Board	
Aareon AG	Member of the Supervisory Board	

Norbert Kickum, Member of the Management Board

Aareal Bank France S.A.	Member of the Board of Directors	
Aareal Financial Service Polska Sp.z o.o.	Member of the Supervisory Board	
Aareal Bank Asia Limited (formerly Aareal Financial Services (Singapore) Pte. Ltd.)	Member of the Board of Directors	
Aareal Bank Asia Limited (formerly Aareal Financial Services (Singapore) Pte. Ltd.)	CEO (Chairman)	
Aareal Financial Services USA, Inc.	Chairman of the Board of Directors	
Aareal Financial Service spol. s r.o.	Member of the Supervisory Board	
Aareon AG	Member of the Supervisory Board	since 3 Sep 2007
Deutsche Structured Finance GmbH	Member of the Advisory Board	

Hermann Josef Merkens, Member of the Management Board

Aareal Asset Management GmbH	Chairman of the Supervisory Board	until 28 Feb 2007
Aareal Estate AG	Chairman of the Supervisory Board	
Aareal Bank Asia Limited (formerly Aareal Financial Services (Singapore) Pte. Ltd.)	Member of the Board of Directors	
Aareal First Financial Solutions AG	Member of the Supervisory Board	
Aareal Immobilien Kapitalanlagegesellschaft mbH	Chairman of the Supervisory Board	until 28 Feb 2007
Aareal Property Services B.V.	Chairman of the Supervisory Board	
Aareal Valuation GmbH	Member of the Supervisory Board	
Aareon AG	Member of the Supervisory Board	
Deutsche Bau- und Grundstücks-Aktiengesellschaft	Chairman of the Supervisory Board	

Deutsche Interhotel Holding GmbH & Co. KG	Member of the Council of Shareholders	
Deutsche Structured Finance GmbH	Member of the Advisory Board	
Immobilien Scout GmbH	Member of the Supervisory Board	19 Apr 2007 until 19 Nov 2007
RMS Risk Management Solutions GmbH	Member of the Supervisory Board	since 12 Dec 2007

Thomas Ortmanns, Member of the Management Board

Aareal First Financial Solutions AG	Chairman of the Supervisory Board	
Aareal Financial Services USA, Inc.	Member of the Board of Directors	since 30 Aug 2007
Aareal Bank France S.A.	Member of the Board of Directors	since 25 Jan 2008
Aareon AG	Chairman of the Supervisory Board	
Innovative Banking Solutions AG	Member of the Supervisory Board	

Christof M. Schörnig, Member of the Management Board (until 8 August 2007)

Aareal Asset Management GmbH	Member of the Supervisory Board	until 28 Feb 2007
Aareal Bank France S.A.	Member of the Board of Directors	until 8 Aug 2007
Aareal Bank Asia Limited (formerly Aareal Financial Services (Singapore) Pte. Ltd.)	Member of the Board of Directors	until 8 Aug 2007
Aareal Financial Services USA, Inc.	Member of the Board of Directors	until 8 Aug 2007
Aareal First Financial Solutions AG	Member of the Supervisory Board	until 8 Aug 2007
Aareon AG	Member of the Supervisory Board	until 8 Aug 2007
FPM Frankfurt Performance Management AG	Member of the Supervisory Board	
Mansart Conseil S.A.S.	Member of the Supervisory Board	until 8 Aug 2007

OFFICES HELD BY EMPLOYEES

OF AAREAL BANK AG PURSUANT TO SECTION 340 a (4) No. 1 OF THE HGB

Dr. Bernd Bach, Bank Director

ICAS Consulting und Anwendungssysteme AG	Member of the Supervisory Board	

Dr. Michael Beckers, Bank Director

Aareal Financial Service Polska Sp.z o.o.	Member of the Supervisory Board	
Aareal Financial Service spol. s.r.o.	Member of the Supervisory Board	

Sven Eisenblätter

Immobilien Scout GmbH	Member of the Supervisory Board	until 19 Nov 2007
Aareal Valuation GmbH	Member of the Supervisory Board	

Hartmut Eisermann, Bank Director

Terrain-Aktiengesellschaft Herzogpark	Member of the Supervisory Board	until 31 Jul 2007

Dr. Christian Fahrner, Bank Director

Innovative Banking Solutions AG	Deputy Chairman of the Supervisory Board	

Ralf Gandenberger, Bank Director

Terrain-Aktiengesellschaft Herzogpark	Deputy Chairman of the Supervisory Board	
Deutsche Interhotel Holding GmbH & Co. KG	Member of the Council of Shareholders	

Uli Gilbert

Terrain-Aktiengesellschaft Herzogpark	Member of the Supervisory Board	since 23 Aug 2007

Dagmar Knopek, Bank Director

Aareal Financial Services USA, Inc.	Member of the Board of Directors	
Aareal Bank Asia Limited (formerly Aareal Financial Services (Singapore) Pte. Ltd.)	Member of the Management Board	

Dr. Stefan Lange, Bank Director

Aareal Estate AG	Member of the Supervisory Board	
Aareal First Financial Solutions AG	Member of the Supervisory Board	since 27 Aug 2007
Deutsche Bau- und Grundstücks-Aktiengesellschaft	Deputy Chairman of the Supervisory Board	
Immobilien Scout GmbH	Member of the Supervisory Board	until 19 Nov 2007
Terrain-Aktiengesellschaft Herzogpark	Chairman of the Supervisory Board	
Via Capital Ltd.	Non-executive Director	until 10 Feb 2007

Peter Mehta, Bank Director

Innovative Banking Solutions AG	Member of the Supervisory Board	

Dr. Peter Schaffner, Bank Director

Aareal Partecipazioni S.p.A.	Member of the Supervisory Board	until 30 Apr 2007

Markus Schmidt

Deutsche Bau- und Grundstücks-Aktiengesellschaft	Member of the Supervisory Board	
Immobilien Scout GmbH	Member of the Supervisory Board	19 Apr 2007 until 19 Nov 2007

Peter Schott, Bank Director

Via Capital Ltd. i.L.	Non-executive Director	until 10 Feb 2007

Christine Schulze Forsthövel, Bank Director

Aareal Bank France S.A.	President of the Board of Directors	
Aareal Financial Service Polska Sp.z o.o.	Member of the Supervisory Board	
Aareal Financial Service spol. s r.o.	Member of the Supervisory Board	
Aareal Partecipazioni S.p.A.	Member of the Board of Directors	until 30 Apr 2007
Mansart Conseil S.A.S.	Chairman of the Supervisory Board	

Martin Vest, Bank Director

Aareal Bank France S.A.	Member of the Board of Directors	

CAST OF COMMITTEES OF THE SUPERVISORY BOARD

Executive Committee

Mr. Reich	Chairman
Mr. Flieger	Deputy Chairman
Mr. Bülow	Deputy Chairman
Prof. Dr. Schüller	
Mr. Thiel	

Accounts and Audit Committee

Mr. Neupel	Chairman
Prof. Dr. Schüller	Deputy Chairman
Mr. Reich	
Graf von Bassewitz	
Mr. Bülow	

Credit and Market Risk Committee

Mr. Reich	Chairman
Dr. Lohneiß	Deputy Chairman
Graf von Bassewitz	
Mr. Flieger	
Mr. Neupel	
Mrs. Birke	

Committee for Urgent Decisions

Mr. Reich	Chairman
Dr. Lohneiß	
Graf von Bassewitz	
Mr. Flieger	
Mr. Neupel	

Wiesbaden, 8 February 2008

The Management Board

Dr. Wolf Schumacher   Norbert Kickum   Hermann J. Merkens   Thomas Ortmanns

RESPONSIBILITY STATEMENT

DECLARATION PURSUANT TO SECTION 37V OF THE WPHG

To the best of our knowledge, and in accordance with the applicable reporting principles for financial reporting, the financial statements give a true and fair view of the assets, liabilities, financial position and profit or loss of the company, and the management report includes a fair review of the development and performance of the business and the position of the company, together with a description of the principal opportunities and risks associated with the expected development of the company.

Wiesbaden, 8 February 2008

The Management Board

Dr. Wolf Schumacher   Norbert Kickum   Hermann J. Merkens   Thomas Ortmanns

AUDITORS' REPORT

After the final results of our audit, we issued the following unqualified audit opinion dated 8 February 2008:

Auditors' Report

We have audited the Financial Statements of Aareal Bank AG, Wiesbaden, comprising the Balance Sheet, Income Statement, and Notes to the Financial Statements for the financial year from 1 January to 31 December 2007. The company's Management Board is responsible for the accounting and the preparation of the Financial Statements and the Management Report in accordance with the German Commercial Code and supplementary provisions of the company's Memorandum and Articles of Association. Our responsibility is to express an opinion, having conducted an audit which included the accounting records, on the Financial Statements and the Management Report.

We conducted our audit in accordance with section 317 of the German Commercial Code, observing the generally accepted German auditing principles laid down by the Institute of Public Auditors in Germany (IDW). These standards require that we plan and perform the audit to obtain reasonable assurance on whether the Financial Statements (based on generally accepted accounting principles) and the Management Report are free of material misrepresentations and present a true and fair view of the net worth, financial position and results of the company. In determining specific actions within the scope of our audit, we considered the Company's business activities as well as its economic environment and legal structure. Expectations regarding potential sources of error were also taken into account. The conduct of an audit includes examining the efficiency of the company's internal controlling mechanisms for its accounting system, as well as, on a sample basis, evidence supporting the disclosures in the accounting records, the Financial Statements and the Management Report.

The scope of an audit also includes assessing the accounting principles used and significant estimates of the Management Board, as well as evaluating the overall presentation of the Financial Statements and the Management Report. We believe that our audit provides a reasonable basis for our opinion.

Our audit has not led to any objections.

In our opinion, the financial statements present, in compliance with legal requirements, generally accepted accounting principles and the supplementary provisions of the Company's Memorandum and Articles of Association, a true and fair view of the Company's net worth, financial position and results.

The management report is in accordance with the annual financial statements. On the whole, the management report provides a suitable understanding of the Company's position, and suitably presents the opportunities and risks of future developments.

Frankfurt / Main, 8 February 2008

PricewaterhouseCoopers
Aktiengesellschaft
Wirtschaftsprüfungsgesellschaft
(auditing firm)

Christian Rabeling
Wirtschaftsprüfer
(German Public
Auditor)

ppa. Alexander Schack
Wirtschaftsprüfer
(German Public
Auditor)

CORPORATE GOVERNANCE
OF AAREAL BANK AG, WIESBADEN

Responsible corporate governance is of great importance to Aareal Bank AG, and considered the essence of prudent commercial conduct by both the Management Board and the Supervisory Board. Accordingly, Aareal Bank welcomes and supports the objectives and purposes of the German Corporate Governance Code, and regularly observes the amendments and extensions of the guidelines adopted by the German Government Commission on Corporate Governance.

Each year we review the bank's Corporate Governance Code and Memorandum and Articles of Association, as well as the internal rules of procedure for the Management Board and the Supervisory Board, regarding their compliance with the Commission's new suggestions. Our annual Declaration of Compliance gives information on the extent to which the bank complies with recommendations, and which suggestions are not being followed.

Code of Conduct

The principles of integrity and responsible conduct must be observed by all our employees across the enterprise, regardless of their functions and duties. Therefore, our internal Code of Conduct is an integral part of responsible corporate governance. We revised and extended the Code of Conduct for our staff during the 2007 financial year. The Code contains binding rules governing the legal and ethical conduct of employees vis-à-vis colleagues, clients, and business partners.

Aareal Bank's efforts in this context are also motivated by the desire to affirm and further strengthen confidence in the company.

Recommendations of the German Corporate Governance Code

The German Corporate Governance Code (the "Code"), as last amended on 14 June 2007, comprises new suggestions for responsible corporate governance, in addition to the applicable legal framework. Having reviewed the most recent amendments to the Code in detail, the bank's Management Board and Supervisory Board issued and signed their Declaration of Compliance pursuant to section 161 of the German Public Limited Companies Act (AktG) on 17 December 2007. The Declaration was published on the bank's website, and is shown after this Corporate Governance Report. In accordance with the recommendation of the Code, the Declarations of Compliance regarding the past five years are available on our website.

Aareal Bank AG complies with the German Corporate Governance Code, as last amended, to a large extent, and only diverges in a few aspects, as outlined below.

In the section on the cooperation between the Management Board and the Supervisory Board, section 3.8 of the Code recommends that a deductible be agreed where a company takes out D&O insurance cover. Aareal Bank has taken out a D&O liability insurance policy for members of the Management Board and the Supervisory Board that does not provide for a deductible. Responsible action is an integral obligation for all members of the company's executive bodies. For this reason, the members of the company's executive bodies believe that it does not require a deductible.

Item 4.2.2 in the section on the composition and remuneration of the Management Board also recommends that upon proposal by the Board, the plenary meeting of the Supervisory Board deals with the contracts for the members of the Management Board, advises on the structure of the remuneration system for the Management Board as well as reviewing it on a regular basis. In its meeting on 23 May 2006, the Supervisory Board of Aareal Bank AG passed on all issues related to the remuneration of the Management Board to the Executive Committee for independent assessment and handling. This was due to the abolishment of the separate Human Resources Committee as of this date. The procedure of delegating this duty to a committee has stood the test of time. The Executive Committee advises on a regular basis on the determination and structure of the emoluments paid to the members of the Management Board and reports to the plenary meeting of the Supervisory Board on its deliberations in this respect, and on results.

The newly-added section 5.3.3 of the Code contains a recommendation that the Supervisory Board shall form a nomination committee, composed exclusively of shareholder representatives, which proposes suitable candidates to the Supervisory Board for recommendation to the General Meeting. There is no need for Aareal Bank AG to immediately implement this recommendation, as the Supervisory Board of Aareal Bank AG in its current composition has been in office for approximately one year; therefore, there is no current need for nominating new candidates. The bank plans to conduct a review regarding market acceptance of said recommendation in 2008.

Aareal Bank AG was unable to adhere to the recommendation of the Code to elect Supervisory Board members at varied dates. The reason for this was that historically, all terms of office end on a single termination date. The recommendation could not be adhered to without breaching the principle of equal treatment of all candidates. Furthermore, grading the terms of office would represent an unnecessary increase in the bank's administrative expenditure.

The regulations laid down in item 7.1.3 in the section on accounting practises in the Code refer to the breakdown of the remuneration as of page 74.

The Management Board

The Management Board is responsible for managing the company. In doing so, it is obliged to act in the best interest of the company and undertakes to increase its sustainable enterprise value. The Management Board ensures that all provisions of law are complied with, and endeavours to achieve their compliance throughout Group companies. The Management Board develops company strategy, coordinates it with the Supervisory Board, and ensures its implementation. It ensures appropriate risk management and risk controlling throughout the company. The Management Board cooperates on the basis of trust with Aareal Bank AG's other executive bodies, and with employee representatives.

There were no conflicts of interest affecting members of the Management Board within the meaning of the Corporate Governance Code in the 2007 financial year.

Following the retirement of Christof M. Schörnig from his office as a member of the Management Board of Aareal Bank AG, Mr Schörnig's duties have been distributed amongst the remaining members of the Management Board. The Management Board believes that its remaining four members are capable of exercising the management duties previously held by Mr Schörnig in full, and with the required due care and diligence, despite the additional burden placed upon them. This Management Board resolution was passed after discussions with, and approval by the Supervisory Board.

Main components of the compensation system for members of the Management Board

The Executive Committee of the Supervisory Board determines the structure and amount of remuneration for members of the Management Board. The Committee sets fixed and variable, and any other, remuneration components for members of the Management Board. Details regarding the remuneration for members of the Management Board are provided in the Remuneration Report, which complies with all of the bank's obligations pursuant to the German Act on the Disclosure of Executive Board Remuneration (VorstOG).

The Supervisory Board

The task of the Supervisory Board is to advise regularly, and to supervise the Management Board in the management of the company. It is involved in decision-making that is of fundamental importance to the company, and cooperates closely and on the basis of trust with the Management Board.

The Supervisory Board has created committees for its work. Responsibility for individual duties has been delegated to these committees. The members of the Supervisory Board and their functions in the Supervisory Board's committees are identified in this Annual Report, after the List of Offices Held.

The Supervisory Board reports on its duties and the events of the 2007 financial year in its report on page 104 of this Annual Report. The Executive Committee prepares the plenary meetings of the Supervisory Board. The option of preparing meetings separately was neither exercised by the shareholder representatives nor by the employee representatives and is used by the Supervisory Board in exceptional cases only. No such separate preparations took place during 2007, nor were there any Supervisory Board meetings without the members of the Management Board in attendance.

In line with the recommendation of section 5.2 of the Code, the Chairman of the Supervisory Board does not chair the Accounts and Audit Committee: this position is held by Joachim Neupel, an experienced public auditor and tax advisor.

Section 5.4.2 of the Code, which forms part of the section on the composition and remuneration of the Supervisory Board, recommends that the members of the Supervisory Board do not exercise directorships or advisory tasks for important competitors of the company. The merger of DEPFA BANK plc, Dublin, with the Hypo Real Estate Group could have resulted in conflicts of interest for the Chairman of the Supervisory Board, Hans W. Reich. For this reason, Mr Reich retired from his office as a non-executive director of DEPFA BANK plc, with effect from 5 October 2007.

The members of the Supervisory Board have stated that there were no conflicts of interest (as defined in section 5.5.2 of the Corporate Governance Code) during the financial year under review.

The Supervisory Board reviews the efficiency of its own activities on a regular basis. The following considerations in particular are examined:

- Meetings (contents, duration, results)
- Information provided to the Supervisory Board by the Management Board
- Composition of the Supervisory Board
- Specific topics relevant to the committees

The results serve to further improve the work carried out by the Supervisory Board as well as enhancing the cooperation between the Supervisory Board and Management Board. The analysis showed that the Supervisory Board largely works efficiently. The Chairman of the Supervisory Board presented the results in the meeting on 17 December 2007, and discussed these with the Supervisory Board members in detail. No organisational changes to enhance efficiency were required.

The Report of the Supervisory Board on page 104 of this Annual Report provides a detailed review of the activities of the Supervisory Board and its Committees.

Remuneration system for the Supervisory Board

The remuneration structure for members of the Supervisory Board is governed by the resolution passed by the Annual General Meeting 2006. Details regarding the remuneration structure and amounts paid in 2007 are provided in the separate Remuneration Report on page 74 of this Annual Report.

Purchase or sale of the company's shares

No transactions involving the company's shares were carried out in 2007 by members of the company's executive bodies. At the end of the financial year, aggregate shareholdings of members of executive bodies in the company's shares were less than 1 % of the issued share capital of Aareal Bank AG.

Transactions with related parties

Related party transactions are detailed in the notes to the financial statements, on page 73 of this Annual Report.

Accounting policies

Aareal Bank AG prepares the Group's accounts in accordance with the International Financial Reporting Standards (IFRS). The single-entity financial statements of Aareal Bank AG are prepared in accordance with the provisions of the German Commercial Code (Handelsgesetzbuch – HGB). The Management Board prepares the financial statements of Aareal Bank AG and the consolidated financial statements. The external auditors submit their report on the audit of the financial statements and consolidated financial statements to the Supervisory Board. The Annual General Meeting on 30 May 2007 elected Pricewaterhouse-Coopers Aktiengesellschaft Wirtschafts-prüfungsgesellschaft, Frankfurt / Main, as the auditors for the 2007 financial year. The Supervisory Board appointed Pricewaterhouse-Coopers Aktiengesellschaft Wirtschafts-prüfungsgesellschaft, and defined the focal points of the audit. The external auditors conducted the audit in line with instructions given. The fees paid to the auditors are set out on page 79 of the notes to the financial statements.

The Supervisory Board approves the financial statements and the consolidated financial statements, and thus confirms them, provided that no objections are raised against the financial statements or the results of the audit. Details regarding the examinations carried out by the Supervisory Board, and the results of such examinations, are provided in the Report of the Supervisory Board.

Relationship to shareholders

Aareal Bank holds a General Meeting of shareholders once a year. Shareholders are thus given the opportunity to actively participate in the development of the company.

At the Annual General Meeting, the shareholders decide, in particular, on the formal approval for the members of the Supervisory Board and Management Board for the financial year under review, on the appropriation of any net retained profit, amendments to the Memorandum and Articles of Association, and authorisations on capital adjustments. The Annual General Meeting also elects the auditor for the company.

The company's shareholders may submit statements or proposals in writing, by fax or e-mail, to the company or may request to speak at the Annual General Meeting. The shareholders may also submit counter or supplemental motions to the agenda items at the Annual General Meeting so that they participate in structuring and influencing the meeting. At the Annual General Meeting, the Management Board or Supervisory Board shall comment on or answer the contributions made by shareholders.

Communication

Aareal Bank assigns great importance to extensive communications with all of the bank's stakeholders. This is also reflected in our FUTURE 2009 growth programme, where we have set ourselves the targets of actively and openly communicating with all stakeholders, taking into account the interests of all stakeholders. In this context, we make extensive use of our website to inform about current developments affecting the Group, and to provide information to all target groups at the same time.

All press releases, ad-hoc disclosures, corporate presentations, as well as annual and quarterly reports published by Aareal Bank are available on the bank's website, and may be downloaded from there. In addition, the financial calendar is regularly updated, providing information about relevant corporate events.

Aareal Bank publishes details on the financial position and performance four times annually. On these occasions, the Management Board gives a personal account of results, during press conferences and analysts' events.

We are currently not broadcasting parts of the Annual General Meeting on the internet, nor is it currently possible to give instructions or cast votes online. This is because the low level of acceptance of such a service amongst our shareholders would render the related technical efforts and costs excessive. Nevertheless, Aareal Bank will continue to review demand for such a service on a regular basis.

As a further step towards modern and transparent communications, the Annual General Meeting adopted an amendment to the Memorandum and Articles of Association, according to which it will be possible in future to disseminate information to holders of securities issued by Aareal Bank AG by way of electronic media.

Declaration of Compliance within the meaning of section 161 of the German Stock Corporation Act (AktG)

The Management Board and Supervisory Board of Aareal Bank AG declare, in accordance with section 161 of the AktG, that:

Aareal Bank AG has complied with the recommendations of the Government Commission "German Corporate Governance Code" (as amended on 12 June 2006 and, with effect from 14 June 2007, as amended on that date) since the last Declaration of Compliance was issued in December 2006; in each case, except for the recommendations stated below.

Item 3.8 of the Code recommends that a suitable deductible be agreed where the company takes out a D&O (directors and officers' liability insurance) policy for members of the Management Board and Supervisory Board.

Aareal Bank AG has taken out a D&O liability insurance policy for members of the Management Board and the Supervisory Board that does not provide for a deductible. Responsible action is an integral obligation for all members of Aareal Bank AG's executive bodies; for this reason it does not require a deductible.

Item 4.2.2 of the Code recommends that upon proposal by the Board, the plenary meeting of the Supervisory Board deals with the contracts for the members of the Management Board, advises on this structure of the remuneration system for the Management Board and reviews it on a regular basis.

The Supervisory Board of Aareal Bank AG has passed on all issues related to the remuneration of the Management Board to the Executive Committee for independent assessment and handling. This procedure has stood the test of time. The Executive Committee advises on a regular basis on the determination and structure of the emoluments paid to the members of the Management Board and reports to the plenary meeting of the Supervisory Board on its deliberations in this respect.

The newly-added section 5.3.3 of the Code contains a recommendation that the Supervisory Board shall form a nomination committee, composed exclusively of shareholder representatives, which proposes suitable candidates to the Supervisory Board for recommendation to the General Meeting.

There is no need for Aareal Bank AG to immediately implement this recommendation, as the Supervisory Board of Aareal Bank AG in its current composition has been in office approximately one year; therefore, there is no current need for nominating new candidates. The bank plans to conduct a review regarding market acceptance of said recommendation in 2008.

Aareal Bank will also comply with the recommendations of the German Corporate Governance Code (as amended on 14 June 2007) throughout the financial year 2008, with the aforementioned exceptions of sections 3.8, 4.2.2, and 5.3.3.

Aareal Bank AG has also adopted its own Corporate Governance Code as early as 1999. The bank's Code has been adapted to incorporate amendments to the German Corporate Governance Code; it goes beyond the recommendation of the Government Commission.

For further details on the Corporate Governance Principles of Aareal Bank AG, please refer to our website: http://www.aareal-bank.com/en/profile/corpgov/index.en.html.

Wiesbaden, 8 February 2008

The Management Board

Dr. Wolf Schumacher | Norbert Kickum | Hermann J. Merkens | Thomas Ortmanns

For the Supervisory Board

Hans W. Reich (Chairman)

REPORT OF THE SUP

REPORT OF THE SUPERVISORY BOARD
OF AAREAL BANK AG, WIESBADEN

Ladies and gentlemen, dear shareholders,

During the financial year under review, the Supervisory Board continually advised, monitored, and supervised the management of the company. The Management Board informed the Supervisory Board regularly, without delay and comprehensively, both orally and in writing, of all issues important to the Group with regard to its situation, business development, and key financial indicators. In addition, detailed reports and explanations were given to the Supervisory Board regarding the prevailing risk situation, and on risk control and risk management measures taken. The Supervisory Board also received comprehensive reports on the development of business segments, and on operative and strategic planning. The Supervisory Board was informed about, and involved in, all important decisions. All material events were discussed and examined in detail; where required, Supervisory Board approval was given.

Between the meetings of the Supervisory Board, the Chairman of the Management Board kept me informed, on a continuous and regular basis, both orally and in writing, on all material developments of the company. The Chairman of the Management Board maintained close contact with myself in order to discuss key issues and important decisions personally.

Activities of the plenary meeting of the Supervisory Board

The Supervisory Board met on four scheduled occasions during the financial year under review, plus two meetings dedicated to the discussion of strategic options. Moreover, a conference call was held to discuss the enhancement of the bank's strategic options regarding its stake in Immobilien Scout GmbH.

During the scheduled meetings, the members of the Supervisory Board received reports and explanations by the members of the Management Board, and discussed these in detail. A focal point was the FUTURE 2009 growth programme: reports and extensive discussions covered the programme as well as various individual aspects and consequences. Reports on the disposal of the stake in Immobilien Scout GmbH represented a further point of attention.

As described in the Annual Report 2006, the Management Board had provided comprehensive reports on the sale of the Asset Management sub-group and other changes to the Group structure. The Management Board provided a concluding report on the preceding disposals during the first Supervisory Board meeting in 2007.

In its March meeting, the Supervisory Board concerned itself in detail with the financial statements presented for the 2006 financial year, and with the auditors' report. The relevant facts were presented in the report for the previous year.

The Management Board kept the Supervisory Board informed without delay, comprehensively and transparently, regarding the distortions on international securities markets as soon as these occurred. The Management Board provided a full account on the additional audit measures undertaken (in addition to existing comprehensive reporting) in order to gain a full image on the potential impact of the US sub-prime crisis and the resulting market distortions on Aareal Bank AG.

The comprehensive information submitted regarding the crisis affecting the US sub-prime residential mortgage market (the 'sub-prime crisis') was discussed in detail during the September meeting, together with detailed explanations provided by the Management Board. This included statements by the Management Board in which it confirmed to the Supervisory Board that Aareal Bank AG has no exposure to US sub-prime loans, as it is (i) exclusively engaged in commercial property finance; and (ii) does not hold any exposures to US RMBS, CDOs, or conduit programmes. More than 90 per cent of the bank's € 625 million ABS portfolio consist of AAA-rated issues; less than € 50 million are invested in US Commercial Mortgage Backed Securities (CMBS). This investment policy is based on a conservative business policy complementing the extensive internal reporting and control mechanisms implemented.

During the same meeting, the Supervisory Board also concerned itself in detail with Mr Schörnig's retirement, and the resulting need to re-define the distribution of responsibilities amongst Management Board members. The proposed new distribution of responsibilities amongst the remaining four Management Board members was approved. The Supervisory Board believes that the distribution of responsibilities adopted will enable the Management Board to perform its duties appropriately and successfully.

Deliberations during the fourth Supervisory Board meeting, in December, focused on the company's performance, developments related to the sub-prime crisis, and on Group planning for the years 2008 to 2010. The Management Board submitted the planning and explained it in detail. Corporate governance issues were discussed as well: the Supervisory Board adopted the Declaration of Compliance, pursuant to section 161 of the AktG, for the year 2007, which was subsequently published on the bank's website. The Supervisory Board also regularly examines the efficiency of its activities in order to identify any areas requiring improvement. The examination of efficiency conducted in the 2007 financial year confirmed the previous year's good results. The results were acknowledged by the members of the Supervisory Board, and were discussed in detail. No organisational changes to enhance efficiency were required.

The Management Board regularly informed the Supervisory Board regarding the implementation of regulatory rules and regulations (including those within the Basel II framework), outlined the impact of such regulations on the bank, and discussed any changes to the regulatory framework with the Supervisory Board. The regular strategic analysis in accordance with the Minimum Requirements for Risk Management in Banks (MaRisk) was submitted and discussed.

The Chairmen of Supervisory Board committees regularly gave account of the work in the committees to the plenary meeting, answering all related questions by the plenary meeting in detail.

In addition to the four scheduled plenary meetings of the Supervisory Board, as described above, two meetings were convened exclusively to discuss the bank's strategic options. During the first of the two meetings, in January 2007, the Management Board presented the strategic options within the scope of the FUTURE 2009 growth programme to the Supervisory Board, who approved them. During the second meeting, in December, the Management Board gave an overview of market developments, and of the impact on the growth programme. This was accompanied by a presentation of the level of target achievement under the FUTURE 2009 growth programme, and a detailed discussion on its specifications for the year 2008.

No conflicts of interest of members of the Supervisory Board, as defined in No. 5.5.3 of Aareal Bank AG's Corporate Governance Code, arose during the financial year 2007. Due to the acquisition of DEPFA BANK plc by a competitor of Aareal Bank AG, my office as a member of the Board of Directors of DEPFA BANK plc might have resulted in a conflict of interest for myself. To avoid any such conflict, I did not participate in discussions, plannings, or votes related to this takeover. Furthermore, it was for this reason that I retired from office as a non-executive director of DEPFA BANK plc, with effect from 5 October 2007.

Activities of Supervisory Board committees

The Supervisory Board has established four committees in order to perform its supervisory duties in an efficient manner: the Executive Committee, the Credit and Market Risk Committee, the Committee for Urgent Decisions, and the Accounts and Audit Committee.

The Executive Committee, which advises the Management Board and prepares the resolutions of the Supervisory Board, met on four occasions. The Executive Committee's area of responsibility also includes assessing the internal condition of the Group with regard to its operative strength, efficiency and its potential for achieving set objectives. Further tasks include personnel planning and negotiating contracts with the Management Board, plus the assessment and – where necessary – approval of all issues involving loans to closely-associated persons or entities, or any other transactions to be entered into between members of the Management Board or the Supervisory Board with the company or any of its subsidiaries.

During its meetings, the Executive Committee prepared the plenary meetings of the Supervisory Board, together with proposed resolutions. In its meeting in March 2007, the Executive Committee also discussed the degree to which the Management Board had achieved set targets in the 2006 financial year, and determined the variable remuneration for the members of the Management Board on that basis. The implications of Mr Schörnig's retirement from the Management Board were discussed in detail during the meeting in September.

The Credit and Market Risk Committee convened three times. The Management Board submitted detailed reports to the committee, covering all markets in which the bank is active in the property finance business; the committee members discussed these reports and market views. The committee also dealt with the granting of loans requiring approval. The committee also noted any transactions subject to reporting requirements, and any other issues requiring the Supervisory Board's approval pursuant to the company's Memorandum and Articles of Association, or the Managing Board's internal rules of procedure. This also included the decision regarding the update of the bank's credit risk strategy, in accordance with Minimum Requirements for Risk Management in Banks (MaRisk). The committee discussed reports on the bank's risk situation, which were submitted and explained by the Management Board. Having discussed the contents with the Management Board in detail, these were duly noted and approved by the members of the committee.

The Committee for Urgent Decisions is a sub-committee of the Credit and Market Risk Committee. As the Committee for Urgent Decisions approves loans subject to approval requirements by way of circulation, it did not convene any meeting.

In accordance with the duties incumbent upon it pursuant to the Memorandum and Articles of Association, the Accounts and Audit Committee discussed the appointment of the external auditors, and the focal points of the audit, in the course of two meetings held during the year under review. In March 2007, the Accounts and Audit Committee received the external auditors' report on the 2006 financial year and discussed the results with the auditors. Having examined the audit reports presented and discussed these with the external auditors, the members of the committee formed their own judgement of audit results. During the autumn meeting, information was given on the progress with the audit for the 2007 financial year, and issues discussed which arose in the course of preparing the financial statements. The committee also received reports submitted by Internal Audit, and the Compliance Report, requesting and receiving detailed explanations. The updated three-year planning was also submitted and explained during the committee's autumn meeting.

In its meeting on 14 March 2008, the Accounts and Audit Committee received the external auditors' detailed report on the audit and audit results for the 2007 financial year, and extensively discussed these results with the auditors and the Management Board.

Where members of the Supervisory Board were unable to attend a meeting, they had announced their absence in advance, giving reasons. The average attendance rate at meetings of the Supervisory Board and its committees was 94 %.

Transactions of particular importance during 2007

On 21 August 2007, Aareal Bank AG signed an agreement to sell its shareholding in Immobilien Scout GmbH to a syndicate of investors led by Macquarie Bank Ltd and Publishing and Broadcasting Ltd, both based in Sydney, Australia. This transaction had been preceded by an extensive review of all investments within the framework of the realignment of Aareal Bank AG, focusing the bank on its core areas of expertise. The review had indicated that Immobilien Scout GmbH did not represent a core business of Aareal Bank AG. The Supervisory Board had been involved in this review process, with information provided by the Management Board regarding the alternative courses of action available. The Management Board had presented the planned course of action, together with the underlying rationale, in detail. The Supervisory Board had supported the plans, approving all steps necessary for implementation.

Given the complex contractual arrangements involved, the favoured alternative was to extend the bank's flexibility by acquiring the stakes held by other shareholders in Immobilien Scout GmbH. Through the acquisition of further shareholdings, Aareal Bank AG managed to significantly improve its position, thus evolving from one amongst several minority shareholders into a majority owner. The corresponding acquisitions were made upon approval by the Supervisory Board. The subsequent examination of options resulted in the decision to sell Aareal Bank AG's shareholding to the syndicate, as outlined above. Deutsche Telekom Group subsequently exercised its pre-emptive right, and an agreement was signed on this basis on 28 September 2007. The transaction was settled in full in the year 2007. Aareal Bank AG has used the proceeds from this sale to strengthen its capital base, in order to further enhance its core business.

Effective 30 July 2007, Aareal First Financial Solutions AG sold its Paco unlimited product line – an access control and automated micropayment billing system for companies managing large residential portfolios – to employees of Aareal First Financial Solutions AG, within the scope of a management buy-out. As Paco unlimited did not represent a strategic element of Aareal First Financial Solutions AG's product range, the Management Board and Supervisory Board of Aareal Bank AG were open-minded towards the concept of a management buy-out. We welcome the entrepreneurial spirit demonstrated by this venture, and wish our former staff members every success in their independent business.

Financial statements and consolidated financial statements

The Supervisory Board instructed PricewaterhouseCoopers Aktiengesellschaft Wirtschaftsprüfungsgesellschaft, Frankfurt / Main, who were elected as auditors by the Annual General Meeting 2007, with the audit of the financial statements. The external auditors appointed submitted a statement regarding their independence to the Supervisory Board, who duly noted it. The Supervisory Board has no reason to doubt the accuracy of this statement of independence. Fulfilling their duties as commissioned by the Supervisory Board, PricewaterhouseCoopers Aktiengesellschaft Wirtschaftsprüfungsgesellschaft audited the financial statements prepared in accordance with the German Commercial Code (HGB) and the consolidated financial statements prepared in accordance with IFRS, the Management Report, the Group Management Report and the Report of the Supervisory Board, and certified the financial statements without qualification.

All members of the Supervisory Board received the audit reports regarding the financial statements and the consolidated financial statements, including all annexes thereto, in good time before the meeting during which the audit results were discussed, and informed themselves about the audit results on the basis of these documents. The representatives of the external auditors attended this meeting, giving a detailed account of the results of their audit and were available to answer further questions, and to provide additional information. All questions were answered to the full satisfaction of the Supervisory Board.

No objections were raised following the detailed examination of the financial statements and Management Report of Aareal Bank AG, prepared in accordance with the HGB; the consolidated financial statements prepared in accordance with IFRS; the Group Management Report; the proposal of the Management Board regarding the appropriation of profit; and of the audit report. In its meeting on 14 March 2008, the Supervisory Board approved the results of the audit. The Supervisory Board approved the financial statements and Management Report of Aareal Bank AG, prepared in accordance with the HGB, which are thus confirmed. The Supervisory Board also approved the consolidated financial statements prepared in accordance with IFRS and the Group Management Report. Having examined and discussed it with the Management Board, the Supervisory Board has endorsed the proposal for the appropriation of profit submitted by the Management Board.

Personnel matters

The appointment of Dr Herbert Lohneiß as a member of the Supervisory Board was approved by shareholders at the Annual General Meeting held on 30 May 2007. Dr Lohneiß, who had been appointed to succeed Dr Nolting by order of the court, had agreed to also stand for election by the shareholders. The Annual General Meeting confirmed his appointment with a significant majority. To preserve the equal treatment of all members of the Supervisory Board, and to avoid additional administrative efforts, the end of Dr Lohneiß's term of office will coincide with the end of office for all other shareholder representatives who had been elected by the previous year's Annual General Meeting. The members of the Supervisory Board are delighted that Dr Lohneiß, a skilled and renowned expert in international financial markets, could be retained to join the Supervisory Board of Aareal Bank AG.

Christof M. Schörnig retired from the Management Board with effect from 8 August 2007, upon his own request. We would like to thank Mr Schörnig for his strong commitment and successful performance, and wish him every success for the future.

In conclusion, the Supervisory Board would like to thank all of the company's employees for their successful work during the 2007 financial year. In consultation with the Supervisory Board, the Management Board expressed its appreciation for the strong commitment shown by all employees in realigning the company through a special bonus paid. Without the impressive commitment and contribution of all members of staff, in a challenging situation for Aareal Bank AG, it would not have been possible to successfully conclude the realignment within a much shorter period than anticipated – which, in turn, allowed to start the FUTURE 2009 growth programme ahead of time.

Kronberg, March 2008

For the Supervisory Board

Hans W. Reich, Chairman

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FINANCIAL CALENDAR

14 May 2008	Presentation of interim report as at 31 March 2008
21 May 2008	Annual General Meeting – Kurhaus, Wiesbaden
12 August 2008	Presentation of interim report as at 30 June 2008
November 2008	Presentation of interim report as at 30 September 2008

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Locations Real Estate Structured Finance

Locations Institutional Housing Unit

Treasury activities

Countries with lending operations

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