LOCAL EXPERTISE
MEETS GLOBAL EXCELLENCE

2008

Aareal Bank AG – Annual Report 2008

Aareal Bank

Key Figures

	2008	2007	Change	
	Euro mn	Euro mn	Euro mn	
Income Statement				
Operating profit	42	80	-38	
Profit before taxes	-18	273	-291	
Net income	4	285	-281	

	2008	2007	Change	
	Euro mn	Euro mn	Euro mn	%
Portfolio data (31 December)				
Property finance	20,878	22,265	-1,387	-6
of which: international	16,613	16,481	+132	+1
Shareholder's equity	1,536	1,553	-17	-1
Total assets	42,545	41,335	+1,210	+3

	31 Dec 2008	31 Dec 2007		
Rating				
Fitch Ratings, London				
Long-term	A–	A–		
Short-term [1]	F2	F2		

[1] since 25 February 2009 "F1"

Contents

Management Report

Business and environment

Group structure and business activities

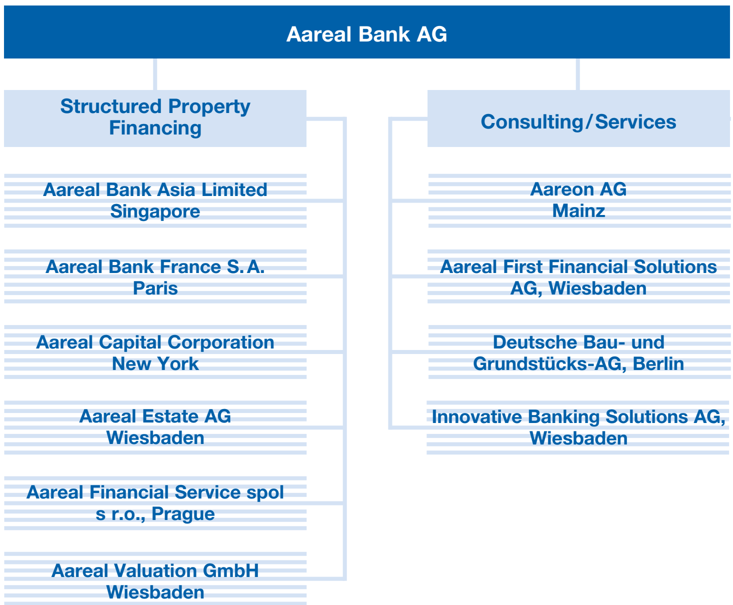
Aareal Bank AG, with its registered office in Wiesbaden, Germany, is the parent company of the Aareal Bank Group and one of the leading international specialist property banks. It provides finance, as well as advisory and other services to the commercial property and institutional housing sectors, supporting national and international clients as a financing partner and related service provider.

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

1. Structured Property Financing

The Structured Property Financing segment brings together all the property finance and refinancing activities of Aareal Bank.

Group structure of Aareal Bank



(as at 31 December 2008)

In this segment, Aareal Bank services domestic and international clients on their property projects in more than 25 countries. Its particular strength lies in the combination of local market expertise and sector-specific know-how. In addition to local experts, the bank also has industry specialists at its disposal, to create financing packages for logistics properties, shopping centres and hotels. We can offer financing solutions that are tailored to meet our clients' requirements in our target markets.

Aareal Bank has many years of experience in national and international commercial property finance. It is active in Europe, North America and Asia within the scope of its "three-continents strategy".

Aareal Bank is a regular and reliable issuer on the capital market, where it covers a wide range of refinancing tools including German asset-covered bonds ("Pfandbriefe") to cater for a broad investor base. Despite the turbulence on financial markets, Aareal Bank continued to issue its targeted volume of Pfandbriefe, albeit incurring higher costs than in the past.

Aareal Bank is a member of the Association of German Mortgage Banks (vdp).

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 subsidiary Aareon AG.

Aareal Bank provides IT systems consultancy and other services to the institutional housing sector through Aareon AG: established over 50 years ago, Aareon now offers its customers software products as well as advisory and training services plus support and IT services.

Aareal Bank operates automated mass payments systems for its institutional housing clients, which are integrated in their administrative processes. The settlement of payment transactions via Aareal Bank generates client deposits that also contribute to the refinancing mix of the entire Group.

Company management

Sustained company development is at the core of Aareal Bank Group's management concept, where the standard is to create continued added value for our shareholders, our clients and for our employees.

Aareal Bank Group is managed on the basis of various economic indicators. Besides key overall business indicators and the management of operational risks, we manage our business through a conservative risk policy and liquidity management process.

Specific key indicators are also used for each segment. In the Structured Property Financing segment, these include among others return on equity (RoE), the risk indicators (as defined in the risk report), lending policies, and the cost income ratio for the Structured Property Financing segment.

The management of the Consulting/Services segment is oriented on specific ratios of individual subsidiaries; these include EBIT and EBIT margin, as well as specific indicators for IT advisory and consultancy services, such as the first-call resolution rate for support services or utilisation ratios for consultants.

Macroeconomic and industry-specific environment

Global business environment

The environment of the 2008 financial year was defined by a significant economic downturn that was heightened by the crisis affecting financial markets and which saw the recession deepening in many economic regions.

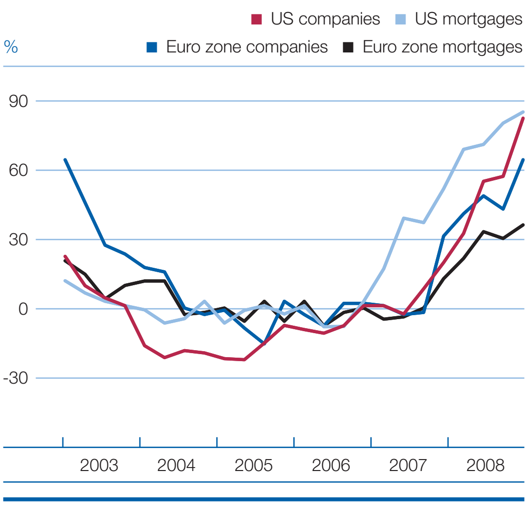
Financial markets crisis

What started as a crisis associated with the so-called sub-prime loans on the American housing market gave rise to a global financial crisis in 2007, which gathered pace even further in 2008.

The crisis was triggered by distortions on the housing market in the USA. The fall in house prices that started in the second half of 2006 in the USA led to an increase in sub-prime loan defaults in the months that followed. These defaults spread already to Europe in mid-2007 via the securitised products that had been sold worldwide.

As a consequence of this, activity on all other markets for securitised transactions – used by many banks for refinancing purposes and to provide relief for balance sheet ratios – came to a virtual standstill. A loss of confidence prevailed among the banks and investors, and the rise in write-downs among many banks led to a shortage of liquidity on the interbank market. The risk premiums increased.

Change



Source: Bank for International Settlements

This situation intensified during 2008: the economic downturn, the credit crunch and uncertainty in relation to the risk situation led to much stricter lending criteria for corporate loans being imposed in the US and the euro zone. Companies found it increasingly difficult to gain access to loans.

The crisis heightened in September 2008 when US investment bank Lehman Brothers was forced to file for creditor protection owing to threatening insolvency. This had the effect of drying up the interbank market. Various central banks once again provided banks within their respective jurisdictions with considerable amounts of liquidity, in order to bridge the credit crunch.

There was a general rise in the risk premiums on financial markets, and lending conditions as well as access to credit were hampered anew.

Having taken action in relation to individual financial institutions, the US administration and many European governments (including the German government) agreed to launch rescue packages across the industry. The bailouts – in Germany, in the form of the Financial Markets Stabilisation Act (”FMStG“) – include recapitalisation, where the respective governments take a shareholding in the affected financial institutions; the provision of indemnities or guarantees covering the liabilities of the banks in question, to facilitate refinancing; as well as the purchase of troubled assets. Many European countries also reinforced their deposit protection schemes.

Individual countries, such as Iceland, the Ukraine, Hungary or Latvia, experienced financial problems and received financial assistance from the IMF.

The crisis affecting financial markets and economic concerns impacted on equity markets, leading to a significant fall in equity prices across the globe. The DAX fell by 40.2% at year-end compared with the start of the year, while the Dow Jones EURO STOXX 50 was down 44.2% and the Dow Jones Industrial Average Index down by 33.8% year-on-year. This situation, together with the declining prices on housing markets of the US and many other countries such as the UK and Spain, contributed to the slide in asset values. Bank indices were hit particularly hard, with the Dow Jones EURO STOXX Banks index losing 63.7% and the CXPB Prime Performance Banks index down 70.9% over the course of the year.

Economic trends

The global economic boom, which began to weaken already in 2007, finally came to an end in 2008. Having enjoyed growth rates of 4.0% in 2006 and 3.7% in 2007, global economic growth contracted to around 2.5% in 2008.

The economic downturn in Europe and North America was considerable, especially in the second half of the year. Many countries are technically in a recession, which is defined by negative growth in at least two consecutive quarters. The downturn has recently spread to Asia as well.

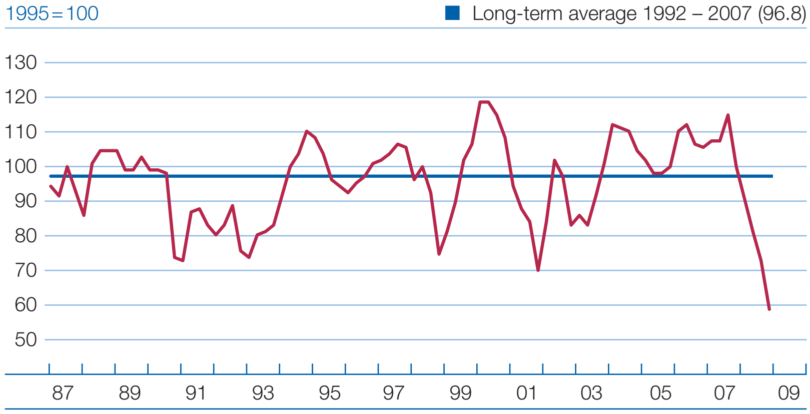
Besides the end of the growth phase of an economic cycle, the crisis affecting financial markets also contributed to the global economic downturn. Real economic development is also burdened by hesitant consumption among private households and the poor sentiment in many sectors of the economy.

In the fourth quarter of 2008, many countries announced – or had already launched – economic stimulus programmes designed to support the economy, and to slow down (or at best halt) the momentum of the downturn.

Consumer confidence in the EU

Source: European Commissions
Taken from the ECB Monthly Report, January 2009

ifo Global Economic Climate*



Source: ifo World Economic Survey (WES) IV/2008.
* Arithmetic mean of assessment of current situation and expected developments

Inflation, monetary policy and exchange rates

Inflation rose considerably worldwide in the first half of 2008, driven by the sharp price increases on commodity markets, especially in crude oil and foodstuffs. Inflation eased initially from August/September onwards and declined more sharply towards year-end. Highly volatile crude oil prices were also a key factor behind this scenario.

As inflation accelerated in the first half of the year, many central banks faced the dilemma of combating inflation on the one hand and countering the economic downturn on the other. The ECB initially gave precedence to its inflation target and on 3 July 2008, hiked the key interest rate for the first time in over a year by 0.25 %. However, easing inflation and the deterioration of the economic situation and the financial markets crisis forced the ECB to change tack from October onwards, where it cut its key interest rate in three steps, to 2.5 %.

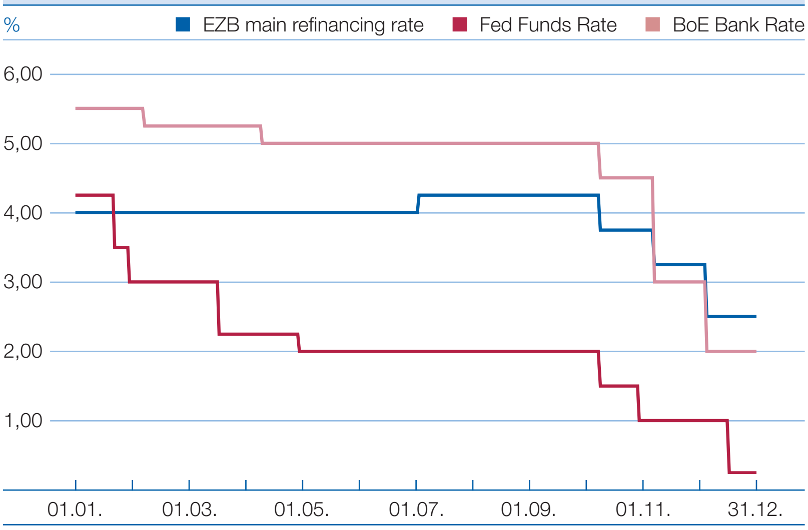
In contrast, the American Federal Reserve Bank (Fed) and the Bank of England reacted to the threat of recession by cutting key rates several times throughout the year. The Fed cut its key interest rate from 4.25 % to a corridor of 0.00 % to 0.25 % at year-end, and the Bank of England from 5.50 % to 2.00 %.

As the crisis affecting financial markets heightened, other central banks followed suit – sometimes in concerted actions – with key rate cuts. During the last two months of the year, the Russian central bank was the only one among the economically significant central banks to still hike key interest rates.

Apart from interest rate policy, the key role of the central banks in 2008 was to provide commercial banks with liquidity. When the interbank market came to a virtual standstill, the ECB announced its intention to conduct its main refinancing operations as a fixed-price auction procedure as of October 2008. It also agreed to increase the frequency of the refinancing operations and extend the range of collateral accepted for these transactions. Other important central banks also opened up the provision of liquidity to the commercial banks.

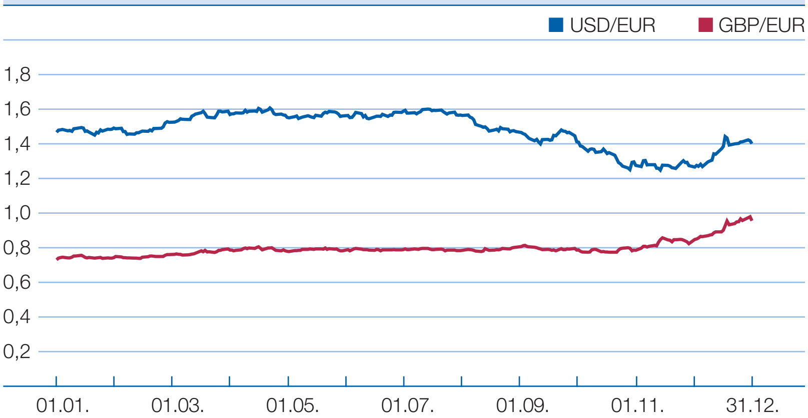
The euro / US dollar exchange rate was highly volatile during 2008. The euro appreciated continuously against the US dollar up until mid-April, and remained at a relatively high level until well into the month of July. The euro then entered a phase of significant depreciation until November, which reverted again into a quick recovery. The euro appreciated slightly against pound sterling initially, remaining stable for a long period of time

Key interest rates 2008



Sources: ECB, Federal Reserve, Bank of England

Exchange rates 2008



Source: Bloomberg

after which it appreciated considerably in the last month of the year. Towards year-end the euro reached its highest level against sterling since it was launched.

Global commercial property markets

The financial markets crisis and the economic slowdown worldwide continued to weigh on property market development in 2008. Restricted lending as a consequence of the withdrawal of liquidity from the interbank market impacted heavily on the markets for commercial property.

Negative performance aside, restrictive lending also contributed considerably to lower volume of commercial property transactions in 2008, after the record levels of the previous two years.

Insecurity among investors, uncertainty regarding economic development, and the divergence in the price perceptions of property buyers and sellers constituted further key reasons behind the fall in the volume of transactions. Large-volume transactions are becoming increasingly less important since the securitisation and syndication markets have ground to a halt.

Price declines in 2008 drove up yields on commercial property investments almost universally in all regions and for the different types of commercial property (office, hotel, retail and logistics property), having been at a very low level in 2007.

Rents for commercial property came under pressure in 2008. However, top rents for top-quality property in the best locations remained stable in many markets during the year, owing to the very positive development in the first six months. Nonetheless, top rents fell in important markets, such as the market for office and logistics property in London.

Performance of mainly regional markets

Europe

Europe was affected by the sharp economic downturn and the recession, albeit to varying degrees in the individual countries. Inflation gathered pace initially before declining again. The rate of inflation in the euro zone – calculated on an annual basis – climbed from 3.2 % in January to a high of 4.0 % in July, after which it retreated to 1.6 % at year-end.

The volume of commercial property transactions was considerably lower in 2008 compared with the year before. Top rents remained stable on many commercial property markets. Investment returns on most European markets increased on the back of price declines in the course of the year.

Western Europe

The downturn impacted heavily on West European economies in 2008. In Germany, economic output declined as of the second quarter compared with the relevant previous quarters. Economic growth, which still measured at 1.3% for 2008 as a whole, was supported by the sharp increase at the start of the year. The labour market, which generally lags behind economic trends, developed favourably and the number of registered unemployed in Germany fell below 3 million for the first time since 1992. However, the figure rose again to 3.1 million at year-end.

The French and Swiss economies came under pressure too, with economic growth in France coming in at only around 0.9% and at around 1.9% in Switzerland. The Benelux countries faced a similar scenario with lower economic growth in Belgium (approx. 1.5%), Holland (approx. 2.2%) and Luxembourg (approx. 2.4%).

In addition to the crisis affecting financial markets, Great Britain was particularly affected by the fall in residential property prices. Year-on-year growth was very low at roughly 0.8%.

Despite the economic slowdown, top rents in Germany for office premises in the five main locations of Berlin, Dusseldorf, Frankfurt, Hamburg and Munich remained stable or climbed marginally year-on-year. The vacancy ratio for office space even fell slightly in the course of the year. The positive labour market undoubtedly had a stabilising effect here.

Office rentals in France and the Netherlands were also quite constant. In fact, top rents for office properties climbed slightly in Paris and Lyon. The vacancy ratio for office space in Lyon fell slightly compared with Paris, which posted a moderate rise. Top rents for office properties in Switzerland were down in the key locations of Zurich, Basle and Geneva. The vacancy ratio for office space declined in Zurich, but rose in Basle and Geneva.

Vacancy ratios also fell during 2008 in the Netherlands' key locations for office properties: Amsterdam, Den Haag, Rotterdam and Utrecht. Top rents in the four cities remained unchanged or rose marginally during the year. At around 2% in 2008, the vacancy ratio for office space was very low in the city of Luxembourg, where top rents for office properties remained constant for the year. On the other hand, development on the markets for office properties was more negative in Great Britain and Belgium. Top office rents in Brussels fell in 2008, while the vacancy ratio fell slightly. London also experienced a sharp decline in the top rents paid for office properties: the vacancy ratio also rose from 4.2% to 5.1%, in line with rental development. Top office rents posted a moderate fall in Manchester, compared with slight year-on-year increases recorded by other secondary UK cities such as Birmingham, Edinburgh, Leeds or Glasgow.

Unlike office properties, retail properties in London saw a rise in top rents for first-class properties on an annual basis. Logistics properties in London on the other hand posted a slight decline. Top rents for retail properties in most of the UK's secondary cities such as Manchester, Birmingham, Glasgow and Leeds, were down. The only exception was Edinburgh, where performance was constant. Top rents for logistics properties were still constant in most of the British secondary cities, apart from Manchester where top rents in fact increased on an annual basis. Top retail property rents in the key locations of France and Germany rose for the year as a whole. The top rents for logistics properties in the key locations of France and Germany were largely unchanged. Hamburg alone posted a rise in top rents, with a decline seen in Lyon.

The logistics sector is very important in the Netherlands and Belgium. Top rents here remained stable or rose on an annual basis. Top rents in the retail sector were also seen to be stable or rising in the key locations of the Netherlands and Belgium. In Switzerland, top rents for retail properties were down in Zurich, Basle and Geneva, whilst rising in Bern. Logistics properties on the other hand carry less weight on the Swiss market. They are frequently owner-occupied and are therefore not available to investors.

The deteriorating macro-economic environment also impacted on the market for hotel property. Average occupancy on the German hotel market fell in both Berlin and Munich, compared with Hamburg, where rates were virtually constant or rose slightly. Average return per hotel room were well down year-on-year in Berlin and Munich, but up in Hamburg. Falling returns were also recorded in Paris and Amsterdam. Average occupancy ratios were also down in these two hotel locations, especially in Amsterdam. Whilst average occupancy ratios also declined in London, at more than 80%, they remain the highest in Europe. Owing to higher room rates, average return per hotel room remained quite constant in London.

Investment returns on the Western European markets increased in 2008 due to price declines across all types of commercial property. The rise in yield was particularly pronounced in Great Britain's secondary cities such as Manchester, Birmingham or Edinburgh. Relatively minor increases in return were seen in Germany.

Southern Europe

Economic development in Southern Europe was also defined by serious problems in 2008. The Italian economy, which had grown only marginally in previous years, came under pressure in 2008 and contracted by around 0.4%. Strong construction activity in Spain led to high growth in recent years. However, owing to the decline in residential property prices and collapse of the construction industry, growth was considerably lower in Spain in 2008.

Rents for office properties in Southern Europe developed differently. Office rents in Spain came under remarkable pressure with a decline in rent levels in Barcelona. At the same time, the vacancy ratios for office space rose in Barcelona and Madrid. In contrast, top office rents in Milan posted a year-on-year increase on falling vacancy ratios (from 7.2% to 6.0%).

The year-on-year trend for top rents for retail and logistics properties in Milan was still rising. Top rents for retail properties in Barcelona and Madrid fell slightly, but remained robust for logistics properties with a slight increase.

Investment returns on commercial property increased in Italy and Spain. As a result of price declines, the returns on office property, in particular in Barcelona and Madrid, increased from previously low levels.

Northern Europe

The decline in residential property prices posed another burden to the Danish economy, which virtually stagnated in 2008. On the other hand, positive economic growth rates (albeit easing) were recorded by Finland (approx. +2.1%), Norway (approx. +2.7%) and Sweden (approx. +0.8%).

Development of top rents for office properties varied. Top rents rose in Helsinki compared with Stockholm and Oslo, where they were already in decline. The vacancy ratios for office properties fell in Oslo and Stockholm, but rose in Helsinki. The top rents for retail properties in the Northern European capital cities were still stable or rising slightly. Rental levels for logistics properties on the other hand were constant in Stockholm and Oslo, but declined in Helsinki. Investment returns rose in all Northern European countries.

Central and Eastern European Countries (CEE)

The markets in the Central and Eastern European countries developed very differently: Although growth rates in Poland (economic growth of approx. +5.4%), the Czech Republic (approx. +4.4%) and Slovakia (approx. +7.3%) were considerably lower than in 2007, other countries such as Hungary are facing serious problems and have encountered significant financial difficulties. The IMF and the EU have committed financial assistance to Hungary to tackle its financial problems.

Russia benefited from the rise in commodity prices at the start of the year, posting economic growth rates of around 6%. However, the sharp drop in commodity prices and the financial markets crisis, which also led to liquidity shortages and distortions in the banking system, weighed heavily on the Russian economy in the second half of the year. Industrial production collapsed at the end of the year. At 13.5%, the annual rate of inflation was very high.

The Baltic States are particularly affected by the crisis of the financial markets and the economy. Economic output in Estonia and Latvia even shrunk, following the very high growth rates of previous years. Latvia received financial assistance from the EU, the International Monetary Fund (IMF), the World Bank and various European countries, to tackle the crisis affecting financial markets.

In Turkey, economic growth slowed to around 3.3%, after the good results of recent years.

Moscow and London command the highest office rents in Europe. However, top rents for office property in Moscow fell on an annual basis and particularly towards year-end. The fall in rental prices was accompanied by a significant rise in the vacancy ratio (5.2% to 14.3%). Top office rents increased in Prague but were lower in Warsaw. The vacancy ratio for office space in Prague rose (5.8% to 9%) whilst the – already low – ratio in Warsaw fell again slightly year-on-year (3.1% to 2.9%).

Top rents for logistics properties in Prague and Moscow were stable. Warsaw posted a rise. Whilst retail rents for first-class properties in Prague and Warsaw rose, Moscow suffered a sharp decline at year-end. As in many other European cities, average vacancy ratios for hotels in Prague and Warsaw were down, as were average returns per room.

Poland, the Czech Republic and Russia each posted rising returns on the various property types. Returns in Moscow remained considerably higher than Western European levels.

Retail property in Turkey is particularly interesting for international investors. The rise in rents for Turkish retail properties in recent years has been followed by a saturation trend, especially in Istanbul. Nonetheless, rents in top-class locations rose. The lack of first-class modern office properties in the main business centre of Istanbul has driven up rents there. Rents for logistics properties in Istanbul were also up due to the continued short supply of modern sites in Turkey. Rent levels for commercial property in Turkey remained considerably higher than the levels commanded in established European locations.

North America (NAFTA states)

Although the US still enjoyed notable growth rates in the second quarter, due to the government's economic programme, economic output contracted as of the third quarter, mainly because of falling consumption and exports. Economic growth for the full year was only around 1.4%. Unemployment in the US rose sharply in the second half of the year. Inflation also climbed during the course of the year, only to decline again later.

Canada and Mexico also saw lower growth rates of around 0.5% and 1.9% respectively, due to shrinking exports.

The volume of commercial property transactions concluded was down significantly on the previous year in North America, especially in the United States.

The economic downturn and sharp rise in unemployment burdened demand for office space in the US, especially in the second half of the year. This resulted in a rise in the average vacancy ratio nationwide. Higher vacancy ratios led to a year-on-year drop in the average top rents for office properties nationwide.

Financial market hubs such as Manhattan, and suburban regions, were particularly affected by the rise in vacancies. The effects of concerns about economic development and falling consumer confidence on retail properties in the US became apparent, and were reflected in pressure on, and declines in rents. The market for logistics properties in the US is also affected by diminishing consumer confidence and falling transport volumes. Rental demand was sluggish, leading to higher average vacancy ratios and downside pressure on rents. The hotel market in the US was also adversely affected by economic developments. The average occupancy ratio and returns per hotel room fell in the US.

The volume of new construction projects for commercial property fell recently and even halted in some instances, due to lack of rental interest or insufficient financing available. Commercial property prices contracted in the course of 2008, enhancing investment returns.

The commercial property market in Canada was relatively robust compared with the US, with top rents for office property rising slightly in the course of the year. There was a moderate increase in the average vacancy ratio nationwide. Despite the recent rise in the vacancy ratio on the logistics market, rents remained constant. The average occupancy ratio on the Canadian hotel market declined, while the average return per room rose slightly.

The Mexican market for commercial property was also relatively stable in 2008, defined by stable rents and moderate, albeit rising, vacancy ratios for office properties.

The volume of property investments fell in Canada as well as in Mexico. Consequently, investment returns rose in both countries.

Asia/Pacific

The Japanese economy is severely affected by the downturn. Economic output has fallen since the second quarter of 2008, and has posted a slight decline for the year as a whole.

Singapore's economy shrunk significantly in the last two quarters and economic growth for the year as a whole was only achieved due to the very strong economic performance in the first quarter: full-year economic growth was roughly 1.5% after 7.7% in 2007.

The emerging markets in Asia were robust in the first half of the year. However, falling import demand from North America and Europe also burdened these countries, leading to lower growth rates over the previous year, even though they are higher by worldwide standards (China roughly +9.4%; India roughly +6.3%). Inflation in Asia also eased at year-end.

While the volume of transactions concluded at the start of the year on the Asian market for commercial property was very robust compared with North America and Europe, the year-on-year decline in the second half of the year was significant.

The effects of the crisis affecting financial markets and the global economic downturn also affected the Asian office property market in the second half of the year. Demand for renting office premises in the Chinese centres of Beijing and Shanghai dropped. Pressure on rents on China's office property markets was evident in the second half of the year, leading to a fall in the top rents for office space in most of Beijing's and Shanghai's individual markets at year-end. On a year-on-year comparison, however, office rents rose there – apart from a few exceptions in individual markets.

Rental growth for office premises in Singapore declined substantially at the start of the year, although it still remained robust. Meanwhile, rents came under pressure in the second half of the year, and were down overall on an annual basis. The vacancy ratios for office premises rose in

Beijing, Shanghai and Singapore. However, the level in Singapore remains considerably lower compared to Beijing or Shanghai.

Top rents for office premises in Tokyo were already declining during the year as a whole, accompanied by a rise in the vacancy ratio. The development of top rents for first-class retail properties in Beijing and Shanghai was inconsistent; rents rose in Shanghai on an annual basis, Beijing also saw increases in some individual markets while others posted a decline. Retail rents in Singapore came under pressure at year-end.

Rents for logistics properties in Beijing and Shanghai rose slightly during the course of the year. A substantial increase in supply in Japan resulted in a higher vacancy ratio. In Singapore, rents for logistics properties rose only at the start of the year but declined at year-end. On an annual basis however, rent increases outweighed in 2008.

Tourism in Asia eased, so that the average occupancy ratio on the Asian hotel market declined.

In the second half of the year, there were signs of investors demanding higher returns across all Asian markets.

Summary

Aareal Bank AG's Structured Property Financing segment comprises the bank's property finance business and its funding activities (cf. page 4). The bank anticipated the sector developments outlined in the section describing the "Performance of key regional markets" at an early stage during the 2008 financial year, taking appropriate action. Monitoring of the bank's lending portfolios was clearly intensified regarding countries showing property market volatility, such as the UK, Spain, and the US. The success of these measures is evident in our risk provisioning: despite a portfolio allowance for credit risks, overall risk provisions were in line with the original budget. (Please refer to the report on expected developments for more details on risk provisioning.)

Results of operations

Aareal Bank AG concluded the 2008 financial year, during which the crisis affecting financial markets intensified, with operating profit before loan loss provisions of € 244 million.

Including allowances and provisions, and net taxes payable, the bank achieved net income of € 4 million. In addition to the loan loss provisions plus the valuation of the liquidity reserves, an amount of € 72 million was transferred to the fund for general banking risks pursuant to section 340g of the HGB. The aggregate of net interest and net commission income rose by a substantial 13.3% or € 59 million, and now stands at € 501 million. Interest income from lending business and money market transactions grew by € 79 million (2007: € 252 million), interest income from securities increased by € 76 million (2007: € 62 million). Interest expenses were up by € 69 million (2007: € 295 million).

The net expense on financial operations of € -48 million (2007: € -13 million) reflects the valuation of the bank's trading portfolio in a volatile market environment that is defined by the crisis affecting financial markets. The net figure includes € 7.9 million write-down on a bond issued by Lehman Brothers with a nominal amount of € 8.5 million.

Administrative expenses of € 230 million (2007: € 240 million) were significantly lower, reflecting the strict cost discipline pursued by the bank. Expenses were lower in human resources (€ 6 million) and regarding depreciation, amortisation and write-downs on intangible and tangible fixed assets (€ 3 million).

Net other operating income and expenses improved by € 24 million over the previous year, to a positive figure of € 20 million. The improvement is largely attributable to payments received from Deutsche Interhotel GmbH & Co. KG and for use-of-money interest on overpaid taxes in previous years, pursuant to section 233 a of the German

General Tax Code (Abgabenordnung – ”AO“). The previous year’s results included expenditure in the amount of € 16 million incurred in relation to the sale of the Immobilien Scout GmbH subsidiary.

The balance of loan loss provisions and the result from securities held as liquidity reserve amounted to € -202 million (2007: € -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.

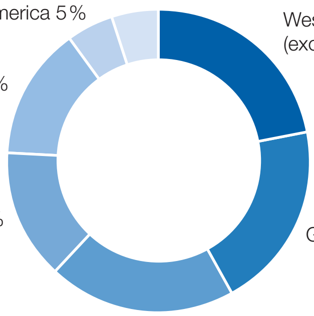
Net other income and expenses, at € -60 million, includes mainly the appropriation of € 72 million to reserves under section 340g of the HGB. Additionally, the net figure includes results and valuations of subsidiaries with which the bank has entered into profit transfer agreements (€ +12 million). Last year’s figure of € 193 million included unrealised profits of € 153 million on the disposal of the investment in Immobilien Scout GmbH.

Taking into account a net tax refund claim of € 22 million (comprising current taxes payable and taxes refunded by the authorities), net income for the year amounted to € 4 million (2007: € 285 million).

Property financing portfolio as at 31 Dec 2008

by region

Total volume: € 20.9 billion



Assets and financial position

Assets

The assets are defined by the property finance business, and investments in securities. As at 31 December 2008, the securities portfolio amounted to € 13.0 billion, comprising high-quality investments of securities and promissory note loans of public-sector issuers (approx. 70%), covered bonds (approx. 8%), and bank bonds (approx. 17%). A minor part of the portfolio, with a nominal value of less than € 600 million (approx. 5% of the portfolio), is invested in an ABS portfolio predominantly based on European assets. These assets are refinanced by deposits generated from the commercial housing sector and institutional money market investors, unsecured issues, promissory note loans, and Pfandbriefe.

Consolidated total assets as at 31 December 2008 amounted to € 42.5 billion, after € 41.3 billion as at 31 December 2007. This was partly due to an increase in the securities portfolio.

Property financing portfolio

The property financing portfolio totalled € 20.9 billion as at 31 December 2008, a slight decline from the previous year’s figure of € 22.3 billion. The reduction was largely attributable to the sale of a € 1 billion portfolio of performing retail loans, which was no longer in line with the bank’s strategy. A major portion of the US loan portfolio originated and managed by Aareal Bank AG was sold to the newly-established subsidiary Aareal Capital Corporation in 2008.

Within the scope of originating new business, we have applied a policy of conservative lending that is aimed at mortgage lending value ratio and a sustained ability to cover interest and principal payments.

We were able to raise the share of international financings in the overall portfolio to a total of 80%, whilst the share of the German portfolio was reduced to 20%.

Portfolio management and exit strategies

In order to develop risk and return-oriented strategies for our financing portfolio, we evaluate suitable market and business data, simulating appropriate strategies for our lending business. This makes it easier for us to react in good time to changes in the market that could potentially impact on our portfolio. 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 maximum portfolio limits for individual countries, products and property types to guarantee a high degree of diversity within the portfolio.

Our exit strategies are consistent with our portfolio management. We use techniques such as syndication to optimise and manage 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.

Syndications and synthetic securitisations

The developments that emerged in the second half of 2007 continued into 2008. The markets for exit instruments became less receptive as the crisis affecting financial markets and the related reticence among market participants continued.

Nonetheless, we were able to syndicate lending volume of € 0.5 billion (2007: € 0.7 billion) to our network of international partner banks during 2008. The continued unfavourable environment meant that securitisations could still not be used as exit instruments. Due to terminations, the total volume of synthetic securitisations – all of which were entered into during previous years – fell from € 2.4 billion as at 31 December 2007 to a residual volume of € 23.9 million.

Disposal of a portfolio of residential property loans portfolio of residential property loans

In the second quarter of 2008, Aareal Bank AG disposed of a portfolio of domestic residential property loans totalling € 1.47 billion to Deutsche Postbank AG. The portfolio comprised exclusively performing loans. The portfolio consisted of Aareal Bank exposures in the amount of around € 1.04 billion, plus roughly € 0.43 billion from DEPFA Deutsche Pfandbriefbank AG's residual property finance portfolio, which Aareal Bank has managed since 1999. The disposal of the portfolio of residential property loans complies fully with Aareal Bank's policy of focusing consistently on its core business of commercial property financing. We have no longer been active in the private client business since 2002. The transaction reduced roughly 84% of Aareal Bank's residential property loan portfolio. The transaction was closed on 11 July 2008.

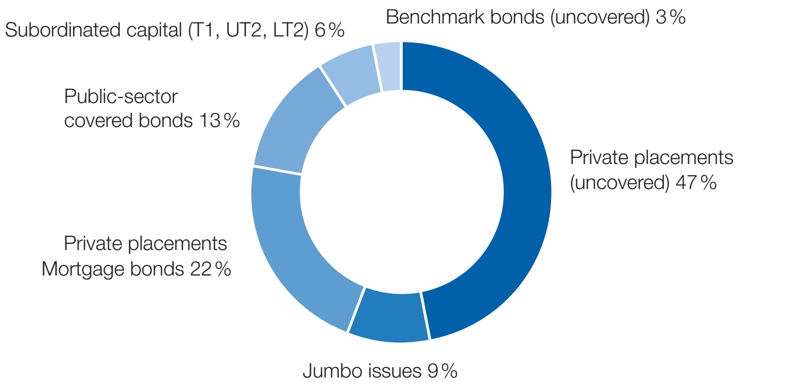
Refinancing

Refinancing structure

Aareal Bank Group successfully conducted the refinancing activities planned for 2008, even in the extremely challenging macro-economic environment that was defined by immense turbulence on financial markets. However, Aareal Bank was unable to escape fully the changed circumstances on the capital markets. The numerous negative reports from the financial world heightened investors' preference for secure investments. Government bonds and Pfandbriefe were the main beneficiaries here, in contrast to unsecured issues. This is also clearly reflected in Aareal Bank's capital market activities: the share of mortgage bonds in the funding mix has risen significantly compared with previous years.

Aareal Bank refinances its lending activities on the capital market mainly in medium-term and long-

Refinancing mix as at 31 Dec 2008



term maturities. The long-term refinancing portfolio, comprising unsecured issues and asset-covered bonds, amounted to just under € 23 billion as at 31 December 2008. The long-term refinancing funds comprised 31% mortgage bonds, 13% public-sector covered bonds, 50% unsecured issues and 6% subordinated issues.

Our capital market activities are enhanced by our exposures on the money market, where we generate deposits from our institutional housing clients and other institutional investors.

The average volume of deposits generated from the institutional housing sector amounted to € 4.3 billion in 2008. Reflecting the structure of the commercial housing sector business, these deposits fluctuate each month, with a residual balance that is generally equivalent to the month-end size of deposits. These deposits were largely stable.

As the crisis affecting financial markets deepened in September 2008, many institutional investors withdrew their short-term deposits from the banks. Our bank was also affected by this, and we reported a decline in short-term client deposits in this segment. In the meantime, these deposits increased again. The unsecured interbank market dried up increasingly in 2008 as a consequence of the crisis. Aareal Bank therefore only invested excess liquidity in secured transactions in the repo market.

Mortgage bonds, unsecured and subordinated issues in the amount of € 20.1 billion, as well as deposits of € 3.6 billion from the institutional housing sector (as at 31 December 2008) plus institutional investor deposits of € 3.6 billion are used to refinance the € 20.9 billion property finance portfolio. The excess liquidity is invested in a portfolio of liquid, high-quality securities eligible for ECB or repo refinancing, which is additionally refinanced through public-sector covered bonds in the amount of € 2.9 billion. The part of the securities portfolio that is used as a liquidity reserve can be used for the purposes of open-market transactions with the ECB, at short notice and where required. Further short-term investments are made in the money market and via repo transactions.

The long-term refinancing has an average term of 5.0 years, whilst the average contractual lifetime of the loan portfolio is 3.7 years. The analysis of Aareal Bank's maturity profile confirms our comfortable liquidity position. The contractual repayments from the property loan portfolio will exceed the maturities of the long-term funds in the years ahead.

Refinancing activities in 2008

During the period under review, Aareal Bank raised a total of € 3.5 billion in long-term funds, including just under € 2.7 billion in mortgage bonds and € 83 million in public-sector covered bonds. Pfandbriefe therefore account for around 80% of new issuance, thus highlighting how quickly Pfandbriefe are becoming increasingly important to Aareal Bank's funding mix. At € 710 million, issuance of long-term unsecured funding fell significantly as a result of the market environment and accompanying high costs. The figure includes the successful public placement of a € 400 million bearer bond. Aareal Bank successfully used a window of opportunity in June of 2008 to place this issue, which was well-received in the market.

The Pfandbrief has established itself as a guarantee for security, especially in these turbulent financial markets. The Pfandbrief business will continue to play a central role in Aareal Bank's refinancing mix. In view of the level of quality, strict legal requirements and successful capital market history, Pfandbriefe offer a reliable refinancing source and allow Pfandbrief-issuing banks to acquire long-term funding, especially in times when investors are demanding high security requirements. This gives us a clear refinancing advantage. In 2008, the share of asset-covered bonds (mortgage bonds and public-sector covered bonds) was increased further, to around 44% of Aareal Bank's long-term funding mix.

Impact of the financial markets crisis

Aareal Bank has emerged from the current crisis affecting financing markets as a fundamentally sound company, with profitable operations and a coherent business model, together with committed and experienced employees and a strong management team. In the midst of severe distortions on the financial markets over the past year, alongside the more recent drastic economic downturn, we achieved results that – given the circumstances – are very satisfying. We see this as confirmation of our focus on two business segments. Similarly, our large international network of small, flexible teams of experts within the framework of our three-continent strategy contributed to this success.

Nonetheless, Aareal Bank was unable to escape fully the changed circumstances brought about by the financial market crisis that deteriorated further in 2008. We therefore deliberately scaled back new business originated by Aareal Bank AG in the 2008 financial year, from € 11.5 billion in 2007 to € 4.7 billion. We view this volume to be appropriate in light of the prevailing market situation in 2008. It is a sign of the difficult market environment that was defined by the financial market crisis and is also a reflection of the considerably lower transaction volumes on the markets for commercial property compared with previous years.

The effects of the crisis affecting financial markets on our credit exposures were at the core of our business strategy. We thus adopted a very restrictive lending policy in the 2008 financial year and stepped up the monitoring and active management of the credit risk exposure considerably. In this context, we carried out a comprehensive additional risk analysis for all material individual exposures in our property finance portfolio.

One result of the measures taken was an increase in the volume of exposures included in cover for Pfandbrief issues. Our new business activities concentrated above all on supporting our existing clients, whose property expertise we are familiar with.

The changed circumstances on the capital markets also impacted on Aareal Bank. The deposit volume from institutional money market clients, which amounted to roughly € 6.3 billion at mid-year, declined after the insolvency of Lehman Brothers. Aareal Bank experienced a peak draw-down on institutional client deposits to the tune of € 3 billion, compared with the level seen in June 2008. However, we have seen a slight trend turnaround since mid-November, with institutional deposit volumes stabilising at around € 4 billion. We were able to offset this loss in client deposits without any problems and at any time, for example through repo transactions on the basis of our liquid securities portfolio. We met the heightened need for information amongst our institutional investors in this environment by actively targeting investors.

Deposits of our institutional housing investors were largely stable over the year.

Suitable measures secured our foreign currency liquidity on a longer-term basis. In some cases, this also involved incurring additional costs.

Owing to the increased inclusion in the cover assets pool, especially of property financings, Aareal Bank successfully issued just under € 2.7 billion in Pfandbriefe, albeit at higher costs than in the past.

Despite the high quality of our securities portfolio, the financial markets crisis also resulted in price losses, especially owing to spread widening among sovereigns and financial institutions.

We had already embarked on a programme of risk reduction and portfolio restructuring at the start of 2008, within the scope of our investment strategy. We scaled back our equity investments almost entirely during the course of the year. Fund investments were also reduced.

The effects on our securities portfolio and the risk-reducing measures are reflected in the income statement in the net expense on financial operations, and the result from securities held as liquidity reserve items, within the scope of the risk provisioning balance. Moreover, securities in the amount of € 2.9 billion were reclassified as tangible fixed assets.

On the basis of more intensive risk monitoring, we proactively adjusted our counterparty and issuer limits during the year.

Regulatory indicators

Aareal Bank has opted to determine regulatory indicators at Group level only since 2007. As at 31 December 2008, Aareal Bank Group had a Tier 1 ratio of 8% in accordance with the German Banking Act (Credit Risk Standard Approach).

Report on material events after the reporting date

To ensure the long-term future of its highly profitable business and to help get through the very difficult market environment, Aareal Bank Group has entered into an agreement with the German Financial Markets Stabilisation Fund ("SoFFin") on a comprehensive set of measures on 15 February 2009. In accordance with this agreement, SoFFin will make € 525 million in capital available to Aareal Bank, in the form of a silent participation. In addition, SoFFin will extend a guarantee facility with a total volume of up to € 4 billion and a maximum term of 36 months to Aareal Bank for new, unsecured issues. This agreement is subject to the conclusion of the final agreements and approval by the European Commission. Taking into account the silent participation from SoFFin, which is eligible for inclusion in Tier 1 capital at a rate of 100%, Aareal Bank's Tier 1 ratio increased significantly.

This recapitalisation in the form of a silent participation considers the interests of shareholders as it avoids a dilution of existing shareholdings. Aareal Holding Verwaltungsgesellschaft mbH will not change its existing 37.23% stake held in Aareal Bank during the term of the silent participation. Aareal Holding and SoFFin will enter into a voting agreement, obliging Aareal Holding to maintain a blocking minority stake. This will ensure the stability of the shareholder structure and the independence of Aareal Bank Group, with Aareal Holding as an anchor shareholder.

SoFFin has not imposed any conditions on Aareal Bank Group that go beyond the statutory provisions. In particular, there will be no state influence on the company's corporate governance, nor will any changes be required to its proven business model. In the interest of a swift redemption of the silent participation, Aareal Bank will not distribute any dividends for the 2008 and 2009 financial years.

Risk Report

1. Risk management at Aareal Bank AG

The assumption of risk is an integral part of banking business. In order to control risk in a responsible manner, and to ensure the sustained development of the company, our operational decision-making process centres around professional risk management. Against this background, we have established a comprehensive system for the measurement, limitation and control of risk, which we continuously update and expand, using considerable human and technical resources.

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

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

Type of risk		Risk management	Risk monitoring
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 Contolling, Credit Management
Credit risks	Property Finance Portfolio risks	Credit Management, Credit Portfolio Management	Risk Controlling
Credit risks	Treasury business	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 policy 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 safeguard the bank's risk-bearing capacity. During the financial year under review, risk strategies as well as the bank's business strategy were adapted to the changed environment, and the new strategies adopted by the Management Board and the Supervisory Board.

1.3 Risk-bearing capacity and risk limits

The bank's ability to carry and sustain risk – which is defined by the amount of aggregate risk cover – is a core determining factor governing the structure of its risk management system. Aggregate risk cover is defined as Tier I capital plus the budgeted net income before taxes. The calculation does not include additional funds such as supplementary and subordinated capital. 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 so as to ensure Aareal Bank AG's ability to bear risk at any time, even against the background of market distortions as a result of the financial markets crisis during the financial year under review.

Concerning liquidity risk, aggregate risk cover is not an appropriate measure to assess risk-bearing capacity. Therefore, we have defined special tools for managing this type of risk. These tools are described in detail in the section "Liquidity risk".

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 system at a portfolio level.

Lending decisions regarding credit business classified as relevant for the bank's risk exposure require two approving votes submitted by a market unit and a credit management unit. The bank's Assignment of Approval Powers defines the relevant lending authorities within market and credit 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 credit management vote regarding the approval of counterparty, issuer, or country limits.

We have implemented and documented the clear separation of market and credit management process 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 supplementary processes for intensified handling, the handling of problem loans, and – if necessary – for provisioning/impairment. 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; depending on the risk situations, the review cycle may be significantly shortened. 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 credit risk exposure, using individual or combined (early warning) criteria is a core element of our risk management approach.

In particular, the procedures applied for the early detection of risks serve the purpose of identifying borrowers or exposures where higher risks start emerging, at an early stage. For this purpose, we generally monitor individual exposures and the parties involved (such as borrowers or guarantors) 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 muster 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, and on its pricing.

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

In a first step, the client's probability of default (PD) is determined using a rating procedure. The method used in this context comprises two main components, a property rating and a corporate rating, 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 for the relevant financing. 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 recovery rates used, depending on the type of collateral involved and specific realisation factors. For financings of domestic properties, recovery rates are taken from a pool of data used across the bank, whilst recovery rates for international properties are derived using statistical methods, given the low number of realisations.

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

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

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

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

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 (verification of market conformity), as well as for the legal assessment of non-standard agreements, and of new standard documentation / master agreements.

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

The bank has also established a Counterparty and Country Limit Committee that votes on all limit applications, and is responsible for conducting the annual review of limits. Where required by current developments, the Committee may reduce or revoke counterparty or issuer limits.

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 Group'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.

During the financial year under review, a new process was established for intensified handling, and handling of problematic exposures of counterparties and issuers. This standardised process comprises identifying early warning indicators, applying them for the purposes of risk analysis, and determining further action to be taken. In the event of counterparty or issuer default, the Counterparty and Country Limit Committee will coordinate an action plan in cooperation with the bank's departments involved.

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's credit risk strategy sets out all material aspects of the Group's 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 sections, 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, from which both the expected and unexpected loss (credit-value-at-risk) are derived. Credit value-at-risk corresponds to the maximum amount by which the actual loss can exceed the anticipated loss, at portfolio level, for a given confidence interval.

Based on the results of these models, the bank's decision-makers are regularly informed of the performance and risk content of property finance exposures, and of business with financial institutions. The models permit to identify, measure, monitor and manage risks at a portfolio level. We deployed a new technical environment for the special model used to analyse the property finance business during the financial year under review. As a result, portfolio information required to take risk management decisions are now available within an even shorter timeframe than before.

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 rating reviews, monitoring of construction phase loans or residential property developers, the monitoring of payment arrears, and the regular, individual analysis of the largest exposures.

A risk report that complies with the Minimum Requirements for Risk Management (MaRisk) 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 properties 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, using a standardised escalation process.

3.1.4 Credit risk mitigation

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

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

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

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

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

The derivatives master agreements used by the bank contain netting agreements to reduce prepayment risk at a single transaction level (payment netting), and arrangements for the termination of individual or all transactions under a master agreement (close-out netting). For repo transactions, depending on the counterparty, payment or delivery netting is agreed upon; contract documentation also generally provides for close-out netting.

To further reduce default risks, the provision of collateral is agreed upon.

Derivatives entered into with financial institutions provide equity relief in accordance with the Solvability Ordinance ("SolvV"); repo transactions are generally not eligible.

Prior to entering into agreements, the responsible legal services unit within the Operations department assesses the legal risks, and the legal effectiveness and enforceability. The bank uses an internal rating system to assess the credit quality of counterparties. For derivatives transactions entered into with financial institutions, where the bank is looking for capital adequacy relief in accordance with the SolvV, a clause providing for a review of eligibility is added to the netting agreements. This review is carried out in accordance with sections 206 et seq. of the SolvV, particularly through obtaining regular legal opinions, using a database developed for this purpose.

Operations is responsible for the daily valuation of the bank's trades, including collateral accepted or pledged, and using validated valuation procedures. Collateral for derivatives transactions is transferred on a regular basis, as provided for in the respective agreements. Margin calls for repo transactions are determined on a daily basis. Haircuts are applied to account for potential fluctuations in collateral value.

Only cash collateral is accepted for derivatives, whereas collateral for repos can be provided in cash or in securities. Some of the collateral agreements the bank has entered into provide for a reduction in the allowance and the minimum transfer amount under the collateral agreement in the event of a downgrade of the bank's external rating; as a result, the bank might have to provide additional collateral.

Aareal Bank enters into credit derivatives exclusively with financial institutions having an investment-grade rating.

In principle, Aareal Bank pursues a "buy, manage and hold" strategy in managing its credit portfolio: this means that loans are generally held until maturity; sales of loans to third parties during their term are only used on a selective basis, and by selling parts of exposures. Loan syndication is used as an active element of portfolio management.

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 risks, 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. Country limits defined for the purposes of risk management were always observed during the financial year under review.

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. The methods and procedures used to manage the bank's country risk exposure were refined further during the period under review, implementing a new technical infrastructure.

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. The risk exposure from bonds that is not related to market price or interest rate risks – in particular, credit and liquidity risk exposure of the bond portfolio – is managed as part of "specific" risk.

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.

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

Since 2008, the Group has extended the calculation of "specific" risks (those which are not correlated with general market movements) to include all bonds held (as opposed to only those in the trading book). Accordingly, overall Group VaR increased as of 1 January 2008.

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. Limits are defined at Group level, as well as for the individual Group entities. 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. The average utilisation of the VaR limit, which we have defined for the aggregate of general market price risk and specific risk exposure, was 43% during the course of the year.

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). Due to increased volatility in interest rate markets, a detailed review of the parameters used to calculate interest rate risk was carried out, and the relative parameters recalibrated in view of continued market turbulence. The number of negative outliers – after recalibration – did not exceed five during 2008 (always lower than three in 2007), 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 implied a present value loss of 31% of the limit as at 31 December 2008. No breach of set limits occurred during 2007.

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 the Group entity that is in a position to assign transactions to the trading portfolio as defined by the German Banking Act. Given the small number of transactions and low volumes concluded during 2008, trading book risks played a low role in the overall risk scenario. During the 2008 financial year, the processes employed proved to be able to quantify the risks arising from market price fluctuations in a timely and accurate manner.

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. Despite the decline in the liquidity reserve, on account of the financial markets crisis, no liquidity shortages occurred during 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 evaluated on the basis of the liquidity run-off profile. We generally consider the withdrawal of customers' current account balances as the most significant scenario. Even in this stress scenario, liquidity is sufficient to cover the expected liquidity needs under stress conditions.

Liquidity Ordinance (Liquiditätsverordnung)

The requirements of the liquidity ratio in accordance with the Liquidity Ordinance, 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 control toolkit, decentralised data capture as well as centralised and timely compilation of all material operational risks across the Group 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 with those responsible 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, evaluation, and management – through to risk control.

We continued to develop the system deployed for monitoring and managing risks from outsourced activities and processes during the financial year under review. Under this system, the relevant organisational units assess the performance of the service provider in regular intervals, using defined criteria. The results of this process, and actions taken, are communicated to the bank's senior management within the scope of operational risk reporting, thus allowing for risk-mitigating steps to be taken where needed.

3.5 Other risks

3.5.1 Definition

Aareal Bank 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. The Aareal Bank Group 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.

Future opportunities and outlook

Development of the environment

The deterioration in the economic environment, which became apparent as early as in 2006, was further significantly exacerbated by the crisis affecting financial markets.

The global economy collapsed on a massive scale towards the end of 2008, with many countries already in recession or approaching it.

The weak economy is burdened further by the financial markets crisis, where banks are facing large-scale write-downs in conjunction with higher capital adequacy requirements. On top of this, liquidity is essentially invested with central banks, restricting banks' ability to lend as one of the consequences. In addition, private households saw their wealth diminish, burdening consumption. Sentiment indicators, which already had been in negative territory, fell dramatically during the final months of 2008. The dire mood and negative outlook prevailing in numerous sectors of the economy represent an additional major burden for economic developments over the next 12 to 24 months.

Against this background, it is fair to expect the various sources of demand – corporate investment, consumption, and exports – to remain under significant pressure in 2009. Through feedback effects and cross-relationships, factors burdening individual sources of demand (for example, the impact of lost wealth on consumption) negatively influence other demand components. The economic decline is expected to continue throughout 2009, with any recovery in 2010 likely to be slow and gradual.

Essentially, global economic output is expected to stagnate in 2009. Developed economies are likely to face shrinking output and recession, with very few exceptions. Although the Asian emerging economies will also see a marked slowdown, they can still expect positive growth rates. As a consequence of the economic decline, a global increase in unemployment is anticipated, which may last until 2010.

The numerous action plans adopted by governments to support the financial markets help stabilise markets, which is positive – even though differences in their objectives might lead to critical distortions of the competitive environment.

Economic stimulation packages currently being implemented in many countries may also have a positive effect. To what extent they will in fact be effective will not only depend on the specific actions taken, but also to the extent to which these measures will have a lasting effect improving the dire mood. Despite such positive effects, it cannot be excluded that downside risks exceed opportunities.

Thanks to lower commodity prices, particularly for crude oil, global inflation declined significantly towards the end of 2008. Given the weak state of the economy, inflation is likely to remain low in 2009 as well. Against the background of lower inflation and economic weakness, ECB cut its interest rate for the Eurosystem's main refinancing facility on 15 January 2009 by 50 basis points to 2.00 %, effective 21 January 2009.

Deflationary risks cannot be excluded for some countries in 2009. Since commodity prices depend upon industrial and consumer demand – with speculative factors also playing a role – a precise forecast is difficult. The slight recovery expected for 2010 is likely to push up inflation again.

We are unable to asses how extensive and lasting the negative effects on the economy will be, given the numerous imponderabilities involved. Specifically, these include the length and intensity of the financial markets crisis, which still impedes the supply of credit to the economy.

Europe

All West European countries are expected to suffer from a shrinking economy. The situation in Central and Eastern Europe is more diverse: even though we expect the economies of Poland, the Czech Republic and Slovakia to slow down in the current macro-economic environment, in contrast to Western Europe, their output is likely to remain largely unchanged, and might even show a minor increase. The situation is markedly different in countries that faced significant financial difficulties at the end of 2008, such as Hungary or the Baltic states. These economies are expected to decline in 2009. The Russian economy came under pressure not only as a result of the crisis affecting financial markets and the economy, but also on account of falling commodity prices. Given the weak global economy, commodity prices are expected to remain rather low, adding further pressure for Russia.

North America (NAFTA states)

The outlook for the US is similar to Western Europe, with the economy in recession during 2009 and some hope for a slight recovery in the following year. The US administration has also launched extensive economic stimulation programmes; whether this will be effective remains to be seen.

Due to the importance of the trading relationships with the US, the economic decline also strongly impacts on Canada and Mexico; our assessment for the US thus applies to the entire NAFTA area.

Asia/Pacific

Japan and Singapore already saw declining economic output during the second half of 2008. In view of the deteriorating world economy and the troubles in the financial sector, these economies will remain under significant pressure during 2009, with lower BIP expected.

Following strong performance over recent years, the Asian emerging economies have also been affected by the global economic slowdown. Lower opportunities for exports to North America and Europe pose the risk of excess industrial production capacity, which could in turn feed back into domestic demand. Even though countries like China are still expected to grow, the rates of growth will be significantly lower compared to previous years, due to the factors discussed.

International property markets

The financial markets crisis has caused uncertainty amongst commercial property investors as well as tenants, leading to great reluctance. As a result, any forecast remains difficult. The following trends are currently foreseeable.

Transaction volumes are expected to remain at very low levels during 2009, and probably also into 2010, particularly compared to the record levels seen in 2006 and 2007. We anticipate higher expected investment yields – and hence, lower prices – for commercial property. We expect rental levels for commercial property to be under pressure around the globe. Even top locations may well see rents fall, albeit at a lower scale of the problem compared to peripheral locations. Rent reductions will become visible in the form of rent-free periods, fixtures and improvements paid for by the landlord, lower rent indexing, and shorter contractual terms, rather than an outright lowering of nominal rent. We believe that office, retail, logistics and hotel properties will suffer from lower returns, given the impact of economic decline across all sectors. Since commercial property markets tend to follow the economic cycle with a certain time lag, we expect this impact to be felt well into 2010.

Europe

Against the background of economic decline and an expected increase in unemployment, we expect vacancies at European locations to increase, with the risk of falling rents (albeit to a varying extent). In our view, this will not be limited to Western Europe, but will also affect the Central and Eastern European economies. We expect yields to rise further as prices fall: this will also affect countries – such as Russia – where yields are already high by European standards.

North America (NAFTA states)

We forecast very low transaction volumes and rising returns (due to falling prices) for commercial property in North America, and particularly in the US. Rents will come under pressure, with declines expected in 2009 on the back of recession and unemployment which rose strongly during the second half of 2008. Whether this trend will continue into 2010 will depend on whether there are any signs of economic recovery by then. The Canadian and Mexican markets, which were still relatively resilient in 2008, will not be immune to the development outlined over the longer term.

Asia/Pacific

Transaction volumes in Asia will also decline in the context of global economic trends. There is a high probability for yields to rise due to falling prices in the region. In view of strong construction activity in China over recent years, and the slowing economies in Japan and Singapore, the commercial property markets will come under pressure.

Going forward, economic activity and developments of commercial property markets will be strongly influenced by market sentiment. Although market participants currently anticipate a negative trend, there is a chance for currently unanticipated positive factors – such as the programmes launched by governments to stimulate the economy – to emerge, improving the mood in the market.

Positive signs in the property markets could materialise if well-capitalised investors start buying again, or if pressure on rents turns out to be less than expected, due to the decline in construction activity.

Corporate development

With the agreement entered into with SoFFin at the beginning of 2009, Aareal Bank has addressed the key risks resulting from the crisis. The bank is well positioned to weather the challenges it faces in the years to come. In particular, the bank has retained full flexibility in its operative business, improving its starting position for the post-crisis period. At the same time, this maintains a level playing field for Aareal Bank for competing with various domestic and international banks who have already received government support. The bank will continue to be a reliable partner for its clients and investors. Moreover, by seeking support the bank complied with its social responsibility, and secured jobs.

In our property finance business, we continue to feel the negative influence of the financial markets crisis and economic decline. Given the high volatility prevailing on capital markets, it is currently impossible to responsibly communicate a concrete projection for the next 24 months. The fees payable for the provision of the silent participation, and for any utilisation of the guarantee facility, will burden Aareal Bank's net interest income and net commission income.

We anticipate the returns on properties serving as collateral for our exposures to decline on account of the economic decline. In conjunction with the difficult situation many property investors find themselves in anyway, this may lead to higher loan loss provisions in the years 2009 and 2010, compared to 2007 and 2008. The silent participation has increased our risk-bearing capacity. Moreover, we focus on first-ranking property loans, concentrating on financing existing properties which ensure a stable cash flow thanks to their good rental situation. At around 70 %, the average loan to value ratio of our exposures is significantly lower than during other crises in the past. Accordingly, given the high quality and broad regional and sector diversification of our property financing portfolio (and our clients), there is the chance of being able to compensate for potential spikes in individual markets.

We also expect that property investors in particular will face increasing problems to procure follow-up financing to refinance their existing loans. Accordingly, we envisage that many property investors – irrespective of the outstanding quality of their properties – will be forced to rely on their existing banking relationships for extending the terms of existing loans. Repayments are thus expected to be low during the current year. Having gained access to government-backed funding, we are in a position to continue financing our clients' projects. In doing so over the next twelve months, our main focus will be on our existing client base, and on existing financings. Over and above such extensions of existing facilities, we will continue to adopt a selective stance in originating new business in 2009, consistently exploiting opportunities as they arise.

We have a sound refinancing structure: we have access to sufficient liquidity, and the average term of loans extended is shorter than the maturities of refinancing in place. However, in a scenario where our credit clients are unable to repay their loans when due, over a longer period of time and in a significant amount, forcing us to extend the maturity of such exposures, combined with our possible inability to roll over our own liabilities, we will take necessary steps such as utilising SoFFin guarantees.

We observe a re-entry of well-capitalised property investors with a long-term investment horizon: this is a good sign for the medium to long-term development. Those investors focus on generating long-term returns from property investments, rather than on short-term profits from market fluctuations. In the long run, this will lead to a rise in market 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.

So far, the various rescue and development programmes launched in 2008 to support banks have not yet sustainably boosted confidence amongst market participants, which is a precondition for reducing market volatility. The resulting scope for volatility to remain high during the current financial year holds major challenges for banks.

On a medium to long-term view, we expect competitive pressures to abate, as some competitors will abandon or cut back their activities, thus reducing the overall number of banks competing for property finance business.

Taking into account the silent participation by SoFFin, which is fully eligible for inclusion in Tier I capital, Aareal Bank Group's Tier I ratio (based on the Credit Risk Standard Approach) would have increased to 10.3% as at the end of 2008.

Main features of the remuneration system

The Supervisory Board determines the structure and amount of remuneration for members of the Management Board. It determines 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 variable remuneration, which is made up of a bonus and a long-term component in the form of phantom shares (long-term component 1) that must be held for three years, after which they can be exercised in the three following years. 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.

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.

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.

Please refer to the Notes to the Financial Statements (Remuneration Report) on page 70 for further details about the remuneration system for members of the Management Board and the Supervisory Board of Aareal Bank AG as well as on the existing change of control regulations.

Disclosure pursuant to section 289 (4) of the HGB and explanatory report pursuant to section 120 of the AktG

Composition of subscribed capital

The issued share capital of Aareal Bank AG amounts to € 128,265,477.00, divided into 42,755,159 notional no-par value bearer shares ("unit shares"), with a proportionate share in the share capital of € 3.00 per share. Each share casts one vote at a General Meeting. There are no shares with special rights granting supervisory powers to any shareholder or shareholder group. The company currently does not hold any treasury shares, which would not be entitled to vote.

Restrictions affecting voting rights or the transfer of shares

The exercise of voting rights and the transferability of shares by shareholders are governed exclusively by applicable law. The exercise of voting rights from the shares concerned is precluded by law in the cases where section 136 of the AktG applies. Where the company holds treasury shares, section 71b of the AktG prohibits the exercise of rights vested in such shares. We are not aware of any other restrictions affecting voting rights or the transfer of shares.

Shareholdings exceeding 10% of voting rights

Pursuant to the German Securities Trading Act (WpHG), any investor whose shareholding in a listed company reaches, exceeds or falls short of certain threshold values in terms of voting rights (whether by purchase, sale or by any other means) must notify the company and the German Federal Financial Supervisory Authority. The lowest threshold for this notification duty is 3%. 62.77% of Aareal Bank AG shares are held in free float. Aareal Holding Verwaltungsgesellschaft mbH is the company's largest shareholderl, with a stake of 37.23%. During the course of the financial year under review, BT Pension Scheme Trustees Limited, London, reduced its shareholding to less than 10% of voting rights. Aside from these shareholdings, we are not aware of any direct or indirect shareholding which would exceed 10% of voting rights.

Shares with special rights granting the holder supervisory powers

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

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

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

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

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

Pursuant to section 179 of the AktG, the Memorandum and Articles of Association may be amended by way of resolution passed by the General Meeting. In the event of a capital change, the Supervisory Board is authorised to modify the wording of the Articles of Association in line with the amount of the capital change (Article 5 (8) of the Memorandum and Articles of Association). Resolutions of the General Meeting regarding amendments to the Memorandum and Articles of Association are passed by a simple majority of the votes cast, or – to the extent permitted by law – by the majority of the issued share capital present at the Meeting. In accordance with section 181 (3) of the AktG, amendments to the Memorandum and Articles of Association become effective upon their entry in the company's Commercial Register.

Authorisation of the Management Board to issue or repurchase shares

Authorised capital

The Annual General Meeting held on 15 June 2005 resolved to authorise the Management Board to increase, on one or more occasions, the Company's share capital by up to a maximum total amount of € 58,300,000 (Authorised Capital) by issuance of new shares for contribution in cash or in kind. This authorisation will expire on 14 June 2010. The shareholders must be granted subscription rights in the event of a capital increase against cash contributions. The Management Board is authorised to exclude shareholders' pre-emptive subscription rights in the event of a capital increase not exceeding 10% of the issued share capital at the time of exercising the authorisation, subject to approval by the Supervisory Board and provided that the issue price is not significantly lower than the prevailing market price. Article 5 (4) lit. b) to d) of the Memorandum and Articles of Association sets out further conditions for excluding shareholders' pre-emptive subscription rights. The Management Board may exclude shareholders' pre-emptive subscription rights in the event of a capital increase against contributions in kind. Following the capital increase resolved on 6 November 2005 and implemented on 21 November 2005, the residual amount of this authorised capital currently amounts to € 46,639,504.00,

In addition, the Annual General Meeting held on 21 May 2008 resolved to authorise the Management Board to increase, on one or more occasions, the company's share capital by up to a maximum nominal amount of € 12,826,545.00 by issuance of new shares for contribution in cash or in kind. This authorisation will expire on 20 May 2013. In the event of a capital increase against cash contributions, shareholders must be granted a subscription right unless this is exceeded by virtue of one of the reasons set out in Article 5 (6) lit. a)-d) of the Memorandum and Articles of Association. The Management Board may exclude shareholders' pre-emptive subscription rights in the event of a capital increase against contributions in kind.

Conditional capital

Pursuant to Article 5 (5) of the Memorandum and Articles of Association, the share capital is subject to a conditional capital increase of up to € 30 million by means of issuing up to € 10 million new notional no-par value bearer shares. The purpose of the conditional capital increase is the granting of shares to holders or creditors of convertible bonds and/or bonds cum warrants issued in accordance with the authorisation by the General Meeting held on 21 May 2008, which authorises the issue of convertible bonds and/or bonds cum warrants in an aggregate nominal amount of € 600 million until 20 May 2013. Under the authorisation, subsidiaries of Aareal Bank AG may also issue convertible bonds and/or bonds cum warrants, and subject to approval by the Supervisory Board allows the company to guarantee such issues as well as to issue shares to fulfil the resulting conversion or option rights. Subject to the approval of the Supervisory Board, the Management Board may exclude shareholders' pre-emptive rights in the certain cases. Notwithstanding the provisions of section 9 (1) of the AktG, in certain circumstances holders of conversion or option rights are entitled to be protected against dilution. The new shares will be issued at the conversion or option price to be set as defined in the resolution passed by the General Meeting on 21 May 2008. 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 is performed, and to the extent that treasury shares are not utilised to service such convertible bonds and/or bonds cum 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, by way of exercise or conversion. The Management Board is authorised to determine any further details of the conditional capital increase, subject to approval by the Supervisory Board. The purpose of this authorisation to issue convertible bonds and/or bonds cum warrants (where the issue of shares to honour the obligations under such convertible bonds and/or bonds cum warrants is covered by the conditional capital) is to provide the Management Board with the flexibility to act swiftly when raising finance, in the interests of the company. The Management Board has not yet exercised this authorisation.

Authorisation to purchase treasury shares

The General Meeting held on 21 May 2008 authorised the Management Board, pursuant to Section 71 (1) No. 8 of the AktG, up to 20 November 2009, to acquire and sell treasury shares for purposes other than securities trading, up to a maximum volume of ten per cent (10%) of the issued share capital at the time of passing the resolution or – if this value is lower – of the share capital existing at the time of exercising this authorisation for purposes other than securities trading. Shares may be acquired via the stock exchange or by means of a public offer to buy, directed at all shareholders. The Management is authorised to effect the sale of any treasury shares acquired in accordance with this authorisation, subject to approval by the Supervisory Board, via channels other than the stock exchange or an offer to all shareholders, provided that the sale is carried out at a price that is not significantly lower than the stock exchange price of the company's shares at the time of sale. This authorisation is subject to the proviso that the aggregate value of shares sold under this authorisation and 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. Subject to approval by the Supervisory Board, pre-emptive subscription rights on the sold shares may also be excluded in the event of a sale against contributions in kind, or if the sold shares are given to the holders of conversion or option rights in lieu of new shares from a contingent capital increase. The Management Board is also authorised to exclude the pre-emptive subscription rights to the extent required to grant subscription rights to new shares to owners of convertible bonds or bonds cum warrants which were issued in the meantime in such an amount as would be due to them once they exercised their option rights. The Management Board is authorised to call in any of the shares acquired under this authorisation, without any further resolutions by the General Meeting being necessary. The company did not exercise this authorisation to purchase or dispose of treasury shares during the year under review.

Renewing the authorisation to purchase treasury shares on an annual basis is in line with widely accepted practice of German listed companies. In line with authorised capital and conditional capital, this serves the company's interest of having access to flexible financing options.

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

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

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

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 approx. 45% 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 approx. 30% of the annual fixed remuneration.

Financial Statements
Income statement

of Aareal Bank AG for the period from 1 January to 31 December 2008

Euro mn			2008	2007
Expenses				
Interest expenses			**1,639.8**	1,570.4
Commission expenses			**37.4**	55.0
Net expense on financial operations			**47.6**	13.2
General administrative expenses				
a) Staff costs				
aa) Wages and salaries	98.2			
ab) Social security contributions, pensions				
and other employee benefits	19.3	117.5		
Including: pensions 8.2				
b) Other administrative expenses		108.7	**226.2**	233.3
Amortisation and write-downs on intangible assets and tangible fixed assets			**3.5**	6.8
Other operating expenses			**12.8**	58.2
Amortisation and write-downs on loans and advances and certain securities, as well as additions to loan loss provisions			**201.5**	105.2
Amortisation and write-downs on participating interests, interests in affiliated companies and securities held as fixed assets			**6.5**	0.0
Expenses for assumption of losses			**4.6**	5.1
Additions to the fund for general banking risks			**72.0**	0.0
Net income taxes			**-22.3**	-14.4
Other taxes not reported under Other operating expenses			**0.0**	1.6
Net income			**4.0**	285.4
Total expenses			**2,233.6**	**2,319.8**
Net income			**4.0**	285.4
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
Transfers to retained earnings				
Amounts transferred to the reserve for treasury shares			**0.0**	0.0
Amounts transferred to other retained earnings			**0.0**	142.5
Net retained profit			**4.0**	**142.9**

Euro mn		2008	2007
Income			
Interest income from			
a) Lending and money market transactions	1,579.3		
b) Fixed-income securities and debt register claims	498.2	**2,077.5**	1,922.4
Current income from			
a) Equities and other non-fixed-income securities	13.5		
b) Participating interests	0.8		
c) Interests in affiliated companies	6.1	**20.4**	49.5
Income from profit pools, profit transfer agreements and partial profit transfer agreements		**22.8**	45.1
Commission income		**80.1**	95.4
Income from write-ups to participating interests, shares in affiliated companies and securities held as fixed assets		**0.0**	153.5
Other operating income		**32.8**	53.9
Total income		**2,233.6**	**2,319.8**

Balance sheet

of Aareal Bank AG as at 31 December 2008

Euro mn			2008	2007
Assets				
Cash funds				
a) Cash on hand		0.0		
b) Balances with central banks		692.7	**692.7**	1,049.7
Including: with Deutsche Bundesbank 650.4				
Loans and advances to banks				
a) Payable on demand		658.8		
b) Other loans and advances		2.077.7	**2,736.5**	3,027.9
Loans and advances to customers			**24,122.3**	24,523.3
Including: secured by charges on real property 8,596.0				
Loans to local authorities 1,779.8				
Debt and other fixed-income securities				
a) Money market instruments		–		
b) Bonds and notes				
ba) Public-sector issuers	6.171.0			
Including: securities eligible as collateral with Deutsche Bundesbank 5,751.5				
bb) Other issuers	4.290.2	10.461.2		
Including: securities eligible as collateral with Deutsche Bundesbank 3,855.3				
c) Own bonds		2.167.2	**12,628.4**	10,345.7
Nominal amount: 2,157.4				
Equities and other non-fixed income Securities			**619.9**	749.6
Participating interests			**4.8**	4.8
Including: Interests in banks 0.8				
interests in financial services providers –				
Interests in affiliated companies			**492.3**	381.3
Including: Interests in banks 30.4				
interests in financial services providers –				

Euro mn			2008	2007
Shareholders' equity and liabilities				
Liabilities to banks				
a) Payable on demand		648.4		
b) With an agreed maturity or notice period		8,637.1	**9,285.5**	5,295.7
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	2,894.3			
bb) With an agreed maturity or notice period	17,832.4	20,726.7	**20,726.7**	23,060.3
Certificated liabilities				
a) Bonds issued		8,526.3		
b) Other certificated liabilities		–	**8,526.3**	8,733.3
Trust liabilities			**694.0**	824.2
Including: trustee loans 692.4				
Other liabilities			**95.0**	105.7
Deferred items			**78.2**	91.0
Provisions				
a) Provisions for pensions and similar obligations		65.7		
b) Tax provisions		27.0		
Including: provisions for deferred taxes 20.5				
c) Other provisions		128.2	**220.9**	254.6
Subordinated liabilities			**802.1**	871.1
Profit-participation certificates			**450.4**	488.0
Including: maturing within two years 0.0				

Euro mn	2008	2007
Assets		
Trust assets	**694.0**	824.2
Including: trustee loans 692.4		
Intangible assets	**4.7**	4.8
Tangible fixed assets	**7.1**	5.1
Other assets	**414.2**	312.1
Deferred items	**72.0**	63.6
Deferred taxes	**56.0**	43.0
Total assets	**42,544.9**	**41,335.1**

Euro mn			2008	2007
Shareholders' equity and liabilities				
Fund for general banking risks			**130.0**	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	669.3	673.8		
d) Net retained profit		4.0	**1,535.8**	1,553.2
Total shareholders' equity and liabilities			**42,544.9**	**41,335.1**

Contingent liabilities			
a) Contingent liabilities from discounted forwarded bills	–		
b) Liabilities from guarantees and indemnity agreements	1,292.7		
c) Liabilities from the pledging of collateral for third-party liabilities	–	**1,292.7**	1,846.4
Other commitments			
a) Repurchase obligations from securities repurchase agreements	–		
b) Placement and underwriting obligations	–		
c) Irrevocable loan commitments	2,989.2	**2,989.2**	4,577.2

Notes

Accounting and valuation principles

The financial statements of Aareal Bank AG for the financial year 2008 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. Taking into account the further deterioration in the economic outlook, the bank has recognised an additional increase in general loan loss provisions.

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 tangible 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 of the HGB. 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 2008 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.

Euro mn	2008	2007
Germany	1,927.2	1,830.2
Europe/America/Asia	283.7	291.0
Total	**2,210.9**	**2,121.2**

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/expenses

Other operating income totals € 32.8 million (2007: € 53.9 million) and includes, among other items, a payment received from Deutsche Intermodal GmbH & Co. KG as well as supplementary interest payments pursuant to section 233 a of the German Tax Code (Abgabenordnung – "AO") for overpaid interest.

Other operating expenses total € 12.8 million (2007: € 58.2 million) and include, among other items, expenses for various subsidiaries in the amount of € 5.0 million (2007: € 16.1 million).

Net income taxes

The net income tax position amounted to € 22.3 million in income. This amount results from current tax expenses as well as from income from deferred taxes. Current tax expenses in the amount of € 4.0 million (of which € 12.4 million was payable abroad and € -8.4 million were received in Germany) were mainly characterised by tax refunds arising from the completed tax audit in Germany. Current tax expenses are offset with income from the reversal of deferred tax liabilities and the recognition of deferred tax assets in the amount of € 26.3 million.

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:

Euro mn	Listed 31 Dec 2008	Unlisted 31 Dec 2007
Debt securities and other fixed-income securities (excluding pro-rata interest)	12,156.3	227.9
Equities and other non-fixed income securities	0.7	149.1
Participating interests	–	–
Interests in affiliated companies	–	–

Valuation units with hedging transactions have been created with respect to negotiable securities in an aggregate amount of € 5,856.3 million.

Bonds and notes of € 10,461.2 million (including accrued interest) reported under debt and other fixed-income securities include € 854.5 million in securities which are not eligible as collateral with Deutsche Bundesbank. Of that amount, € 399 million relate to sovereign foreign-currency bonds, which are eligible for securities lending.

Equities and other non-fixed income securities include € 10.7 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):

Euro mn	31 Dec 2008	31 Dec 2007
Loans and advances to banks	38.0	38.1
Loans and advances to customers	24.5	47.0
Debt and other fixed-income securities	14.9	18.8
Equities and other non-fixed-income securities	0.7	11.2
Other assets	–	–

Movements in fixed assets:

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

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). Since 2008, the markets have been characterised by a severe confidence crisis among banks. This applies particularly to transactions with securities issued by public-sector entities from Eastern and Southern Europe, as well as by North American financial institutions. As a result of this confidence crisis, these securities – even if issued by entities with good credit quality – have been exposed to significant market price declines. Aareal Bank is convinced that these market anomalies will disappear in the long term, at the latest upon maturity of the securities (2011-2037). Due to the quality of the securities and the resulting long-term profit potential until the end of their term, the bank decided to reclassify these securities (having a book value of € 2,879.1 million as at 31 December 2008) from the liquidity reserve and the trading portfolio to fixed assets, on the basis of the book values as at 1 January 2008 (historical cost), with changes in book value recognised directly in equity.

As at 31 December 2008, the securities held as fixed assets include an ABS portfolio of high credit quality, bonds of North American financial institutions as well as securities issued by public-sector entities from Eastern and Southern Europe. Securities with an aggregate nominal amount of € 3,362.0 million were not valued at the lower of cost or market. An examination of cost vs. market value as at 31 December 2008 did not indicate any permanent impairment. The difference between market value and book value of these securities amounted to € -431.0 million.

	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)	Tangible fixed assets (Assets – item #12)	
					Office furniture and equipment	Land and buildings
Euro mn						
Purchase or production costs (1 Jan 2008)	580.5	17.3	421.6	41.8	38.8	0.6
Additions	3,033.0	0.1	202.2	1.4	4.2	0.0
Disposals	50.2	1.1	87.6	5.0	10.9	0.0
Changes in inventory / transfers	–	-11.3	11.3	0.0	0.0	0.0
Depreciation/amortisation (accumulated, as at 31 Dec 2007)	–	12.5	40.2	37.0	34.2	0.1
Depreciation, amortisation and write-downs in the current year	–	0.0	6.4	1.5	2,0	0.0
Disposals	–	1.0	2.3	5.0	10.7	0.0
Transfers	–	-11.3	11.3	0.0	0.0	0.0
Write-ups	–	0.0	0.4	0.0	0.0	0.0
Book value as at 31 Dec 2008	**3,563.2**	**4.8**	**492.3**	**4.7**	**6.6**	**0.5**
Book value as at 31 Dec 2007	580.5	4.8	381.3	4.8	4.6	0.5

Euro mn	Book value 31 Dec 2008	Book value 31 Dec 2007
Change		
Participating interests	4.8	4.8
Interests in affiliated companies	492.3	381.3
Debt and other fixed-income securities	3,563.2	580.5
Equities and other non-fixed-income securities	–	–

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 five or ten years, respectively.

Other assets

Other assets include, in particular, € 328.3 million in assets recognised from currency translation and € 22.6 million in receivables from assumption of profits.

Deferred taxes

In the financial year 2008, deferred tax liabilities of € 13.3 million were reversed and deferred tax assets of € 13.0 million were recognised. Accordingly, as at 31 December 2008, € 56.0 million in deferred tax assets and € 20.5 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 2009.

Other liabilities

Other liabilities include € 12.1million in interest liabilities on silent participations.

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 € 48.1 million (2007: € 50.3 million) include € 11.5 million (2007: € 12.8 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 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 Dec 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:

Euro mn	Nominal amount	Issue currency	Interest rate (% p.a.)	Maturity
Bearer profit-participation certificates:	125.0	EUR	6.750	2002 – 2011
	100.0	EUR	6.375	2002 – 2011
	60.0	EUR	6.125	2003 – 2013
	285.0			
Registered profit participation certificates:	5.0	EUR	7.010	2002 – 2012
	10.0	EUR	7.010	2002 – 2012
	5.0	EUR	7.010	2002 – 2012
	10.0	EUR	7.010	2002 – 2012
	5.0	EUR	7.100	2002 – 2012
	10.0	EUR	7.150	2002 – 2012
	5.0	EUR	7.030	2002 – 2012
	5.0	EUR	7.220	2002 – 2016
	5.0	EUR	7.220	2002 – 2016
	5.0	EUR	6.080	2003 – 2013
	20.0	EUR	6.120	2003 – 2013
	5.0	EUR	6.310	2003 – 2017
	10.0	EUR	5.750	2004 – 2014
	2.0	EUR	5.470	2004 – 2014
	5.0	EUR	5.480	2004 – 2014
	5.0	EUR	5.380	2004 – 2016
	20.0	EUR	5.950	2004 – 2016
	6.0	EUR	5.830	2005 – 2017
	138.0			

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.

€ 28.4 million (2007: € 29.8 million) in interest expenses were incurred in 2008 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 21 May 2008 to purchase and sell treasury shares, pursuant to section 71 (1) no. 7 of the AktG, until 20 November 2009. 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 20 November 2009. 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

Euro mn		
Subscribed capital		
Balance as at 1 Jan 2008	348.5	
(of which: € 220.2 million contributions by silent partners)		
Balance as at 31 Dec 2008		348.5
(of which: € 220.2 million contributions by silent partners)		
Capital reserve		
Balance as at 1 Jan 2008	509.5	
Balance as at 31 Dec 2008		509.5
Retained earnings		
Legal reserve		
Balance as at 1 Jan 2008	4.5	
Balance as at 31 Dec 2008		4.5
Other retained earnings		
Balance as at 1 Jan 2008	547.8	
Transfer from net retained profit 2007	121.5	
Transfer from net income 2008	0.0	
Balance as at 31 Dec 2008		669.3
Net retained profit		**4.0**
Shareholders' equity as at 31 Dec 2008		**1,535.8**

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 Jun 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 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 (3) sentence 4 of the AktG, which are issued during the validity of this 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 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 million, by issuing 3,886,832 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 Nov 2005.

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

The Annual General Meeting held on 21 May 2008 resolved to approve additional 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 € 12,826,545.00 (Authorised Capital 2008) via the issuance of up to 4,275,515 new notional no-par value bearer shares, representing a share of € 3.00 each in the share capital, 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 20 May 2013. The shareholders shall be granted a subscription right in the event of a capital increase against cash contributions. However, subject to the approval of the Supervisory Board, the Management Board may exclude shareholders' subscription rights in the following cases:

- in the event of a capital increase against cash contributions, provided that the issue price does not fall significantly below the prevailing stock exchange price of the exchange-listed shares of the same description and features, and the total pro-rata share of the new shares, for which the subscription right has been excluded, in the share capital does not exceed ten per cent (10%) at the time of this authorisation entering into effect or – if this amount is lower – does not exceed the share capital existing at the time this authorisation is exercised. 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 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 (3) sentence 4 of the AktG, which are issued during the validity of this authorisation;

- for fractional amounts arising from 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 million in order to offer employees (of the Company or its affiliated companies) shares for subscription;

Subject to the approval of the Supervisory Board, the Management Board may exclude shareholders' subscription rights in the event of a capital increase against contributions in kind.

Conditional capital

The share capital is subject to a conditional capital increase of up to € 30 million by means of issuing up to 10 million new no-par value bearer shares equivalent to a share in the share capital of € 3.00 each. 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 21 May 2008. Said resolution authorised the Management Board, subject to the consent of the Supervisory Board, to issue, on one or more occasions until 20 May 2013, convertible bonds and/or bonds with warrants with a limited or an unlimited term in an aggregate nominal amount of € 600 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 million.

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 2008 include € 81.2 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, € 494.3 million relates to domestic borrowers and € 2,494.9 million to foreign borrowers.

Remaining terms

Euro mn	31 Dec 2008
Loans and advances to banks	**2,736.5**
Payable on demand	658.8
Up to 3 months	1,085.1
Between 3 months and 1 year	29.8
Between 1 year and 5 years	149.0
More than 5 years	185.9
Pro rata interest	627.9
Loans and advances to customers	**24,122.3**
Up to 3 months	1,176.4
Between 3 months and 1 year	1,438.3
Between 1 year and 5 years	13,306.0
More than 5 years	7,999.2
Indefinite maturity	–
Pro rata interest	202.4
Debt and other fixed-income securities maturing in the following year (nominal amount)	**891.2**
Liabilities to banks	**9,285.5**
Payable on demand	648.4
Up to 3 months	3,769.6
Between 3 months and 1 year	3,539.5
Between 1 year and 5 years	499.2
More than 5 years	346.8
Pro rata interest	482.0
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

Euro mn	31 Dec 2008
Other liabilities to customers	**20,726.8**
Payable on demand	2,894.3
Up to 3 months	3,328.5
Between 3 months and 1 year	1,175.7
Between 1 year and 5 years	2,880.3
More than 5 years	10,102.1
Pro rata interest	345.9
Bonds issued maturing in the following year (nominal amount)	**2,280.8**
Other certificated liabilities	**–**

Deferred items

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 € 72.0 million (2007: € 63.6 million) include € 9.7 million (2007: € 12.9 million) in premiums on originated loans, in accordance with section 340e (2) sentence 3 of the HGB, as well as € 24.5 million (2007: € 27.3 million) in discounts on bonds issued and borrowings pursuant to section 250 (3) of the HGB.

€ 13.0 million (2007: € 18.9 million) of deferred liabilities (total 2008: € 78.2 million; total 2007: € 91.0 million) are accounted for by discounts on originated loans, in accordance with section 340e (2) sentence 2 of the HGB.

Trust business

Euro mn	Trust assets 31 Dec 2008
Loans and advances to banks	–
Loans and advances to customers	692.5
Equities and other non-fixed-income securities	1.5
Total	**694.0**

Euro mn	Trust liabilities 31 Dec 2008
Liabilities to banks	452.2
Liabilities to customers	241.8
Total	**694.0**

Notes on affiliated companies and enterprises with a participatory interest

	Affiliated companies 2008		Enterprises with a participatory interest 2008		Affiliated companies 2007		Enterprises with a participatory interest 2007	
	Certificated	Not certificated	Certificated	Not certificated	Certificated	Not certificated	Certificated	Not certificated
Euro mn								
Loans and advances to banks	–	344.0	–	–	–	362.5	–	–
Loans and advances to customers	–	1,933.6	–	0.0	–	112.9	–	0.1
Debt and other-fixed-income securities	0.0	0.0	–	–	0.,0	0,0	–	–
Liabilities to banks	0.0	0.0	–	–	0.0	0.0	–	–
Liabilities to customers	–	278.1	–	1.2	–	145.8	–	0.0
Certificated liabilities	–	–	–	–	–	–	–	–
Subordinated liabilities	–	250.0	–	–	–	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 2008	31 Dec 2007
Euro mn		
Loans and advances to banks	437.3	134.6
Loans and advances to customers	0.0	498.6
Debt and other fixed-income securities	6,239.7	2,535.5
Total	**6,677.0**	**3,168.7**

Repurchase agreements

The book value of bonds pledged under repo agreements totalled € 3,253.3 million as at 31 December 2008. In addition, outstanding open-market transactions totalled € 2,750.0 million.

Assets and liabilities in foreign currencies

The aggregate equivalent amount of assets denominated in foreign currencies, calculated pursuant to the German Solvability Ordinance (Solvabilitätsverordnung), was € 11,445.8 million at the balance sheet date, while liabilities totalled € 11,430.9 million.

Forward transactions

The following forward transactions had been entered into as at 31 December 2008:

- Transactions based on interest rates
  Caps, floors, swaptions, interest rate swaps
- Transactions based on exchange rates
  Spot and forward foreign exchange transactions, cross-currency interest rate swaps
- Other transactions
  Credit default swaps, credit-linked notes, 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 primarily used 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 2008)				Nominal amount	
	Up to 3 months	3 months to 1 year	1 to 5 years	More than 5 years	31 Dec 2008	31 Dec 2007
Euro mn						
Interest rate instruments						
OTC products						
Interest-rate swaps	1,985.1	3,321.1	20,937.7	16,862.8	43,106.6	42,389.6
Forward rate agreements	–	–	–	–	0,0	654.0
Swaptions	26.0	30.0	134.0	10.0	200.0	211.0
Caps, floors	97.8	630.2	2,944.8	454.0	4,126.8	4,552.2
Exchange-listed contracts						
Interest rate futures	–	–	–	–	0,0	0.0
Options on interest rate futures	–	–	–	–	0,0	0.0
Total interest rate instruments	**2,108.9**	**3,981.3**	**24,016.5**	**17,326.8**	**47,433.4**	**47,806.8**
Currency-related instruments						
OTC products						
Spot and forward foreign exchange transactions	3,227.3	1,101.0	19.1	–	4,347.4	4,599.8
Cross-currency interest rate swaps	307.3	1,177.3	3,293.3	578.1	5,356.0	3,361.8
Total currency-related instruments	**3,534.6**	**2,278.3**	**3,312.4**	**578.1**	**9,703.4**	**7,961.6**
Other forward transactions						
OTC products						
Credit default swaps	–	–	50.0	748.9	798.9	2,710.8
Credit-linked notes	–	–	–	21.4	21.4	950.5
Other forward transactions	–	–	53.0	–	53.0	53.0
Exchange-listed contracts						
Equity index futures	0.0	–	–	–	0.0	27.7
Total other forward transactions	**0.0**	**0.0**	**103.0**	**770.3**	**873.3**	**3,742.0**
Total	**5,643.5**	**6,259.6**	**27,431.9**	**18,675.2**	**58,010.1**	**59,510.4**

The following table 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, derivatives are measured using generally accepted methods on the basis of current market parameters (yield curves, volatility factors, etc.). Methods used include standard methods and models such as discounted cash flow analyses and option pricing models. Structured products are measured after they have been split into their individual components.

	Market value (31 Dec 2008)		Market value (31 Dec 2007)	
	positive	negative	positive	negative
Euro mn				
Interest rate instruments				
OTC products				
Interest rate swaps	987.0	1,115.9	376.0	818.4
Forward rate agreements	–	–	4.7	4.5
Swaptions	0.0	1.2	0.0	0.9
Caps, floors	16.5	16.4	14.2	14.1
Exchange-listed contracts				
Interest rate futures	–	–	–	–
Total interest rate instruments	**1,003.5**	**1,133.5**	**394.9**	**837.9**
Currency-related instruments				
OTC products				
Spot and forward foreign exchange transactions	217.8	45.7	85.3	7.0
Cross-currency interest rate swaps	453.1	144.1	214.6	9.8
Total currency-related instruments	**670.9**	**189.8**	**299.9**	**16.8**
Other forward transactions				
OTC products				
Credit default swaps	–	60.0	14.2	5.1
Credit-linked notes	–	–	–	2.2
Other forward transactions	2.0	5.9	2.4	2.5
Exchange-listed contracts				
Equity index futures	–	–	–	0.4
Total other forward transactions	**2.0**	**65.9**	**16.6**	**10.2**
Total	**1,676.4**	**1,389.2**	**711.4**	**864.9**

Derivatives have been entered into with the following counterparties:

Euro mn	Market value (31 Dec 2008) positive	negative	Market value (31 Dec 2007) positive	negative
OECD public-sector authorities				
OECD banks	1,375,6	1,378.2	670.9	799.3
Non-OECD banks				
Companies and private individuals	300,8	11.0	40.5	65.6
Total	**1,676,4**	**1,389.2**	**711.4**	**864.9**

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

Euro mn	Cover assets pool	Covered bonds outstanding	Excess cover
31 Dec 2008			
Mortgage bonds			
Nominal value	7,731.3	7,016.1	715.2
Present value	8,288.1	7,219.1	1,069.0
Public-sector covered bonds			
Nominal value	3,263.8	2,984.5	279.3
Present value	3,488.5	3,228.6	259.9

Euro mn	Cover assets pool	Covered bonds outstanding	Excess cover
31 Dec 2007			
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

Euro mn	Share of derivatives in the cover assets pool 2008	Share of derivatives in the cover assets pool 2007	risk-adjusted net present value 2008	Risk-adjusted net present value 2007
Mortgage bonds	195.7	27.5	800.0	983.3
Public-sector covered bonds	51.9	0.1	203.7	287.6

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

Euro mn	Cover assets pool	Covered bonds outstanding
31 Dec 2008		
Mortgage bonds		
Up to 1 year	1,101.7	1,052.2
Between 1 year and 5 years	4,281.4	4,207.7
Between 5 years and 10 years	2,178.5	1,539.3
More than 10 years	169.7	216.9
Total	**7,731.3**	**7,016.1**
Public-sector covered bonds		
Up to 1 year	220.9	223.2
Between 1 year and 5 years	687.6	883.4
Between 5 years and 10 years	721.4	828.6
More than 10 years	1,633.9	1,049.3
Total	**3,263.8**	**2,984.5**

Euro mn	Cover assets pool	Covered bonds outstanding
31 Dec 2007		
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**

Loans and advances used to cover mortgage bonds

Euro mn	Cover assets pool 2008	Cover assets pool 2007
Distribution of the amounts measured at nominal value by volume		
Up to € 300,000	10.5	116.5
between € 300,000 and € 5 million	755.4	565.7
More than € 5 million	6,965.4	4,958.8
Total	**7,731.3**	**5,641.0**

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:

			Commercial property					Residential property				
Euro mn	Pure building sites	Buildings not yet yielding returns	Office buildings	Whole-sale/ Retail	Industrial	Other	Total	Single-family homes	Multi-family homes	Apart-ments	Total	Total cover assets pool
31 Dec 2008												
Belgium		3.4	70.8		9.0	36.3	116.1					119.5
Denmark		19.4	85.5	32.6	7.0	25.1	150.1					169.5
Germany	1.5	26.5	210.8	79.0	223.1	198.0	710.9	3.3	3.8	659.5	666.6	1,405.5
Finland			38.6	216.4	5.4	20.5	280.9					280.9
France		150.1	262.0	53.8	182.9	83.0	581.7					731.8
UK	40.9		135.1	147.0	65.2	77.8	425.1					466.0
Italy			613.9	321.0	12.8	93.7	1041.3			85.6	85.6	1,126.9
Canada			59.6			118.5	178.1					178.1
Luxembourg			4.5				4.5					4.5
Netherlands			159.0		168.2	91.7	418.9			16.4	16.4	435.3
Norway					4.0		4.0					4.0
Poland		29.0	178.6	218.1	45.4		442.1					471.1
Sweden		10.9	218.1	62.2	219.7	35.1	535.1			81.5	81.5	627.5
Switzerland		20.5	156.7	56.6	3.1	65.5	281.9					302.4
Spain		131.8		229.7		46.4	276.1					407.9
Republic of Slovakia					7.7		7.7					7.7
Czech Republic			157.9	9.6	16.2	99.0	282.6					282.6
USA			179.3	192.1		48.4	419.9			59.8	59.8	479.7
Total	**42.4**	**391.6**	**2,530.4**	**1,618.1**	**969.7**	**1,039.0**	**6,157.0**	**3.3**	**3.8**	**902.8**	**909.9**	**7,500.9**

Euro mn	Pure building sites	Buildings not yet yielding returns	Commercial property: Office buildings	Commercial property: Whole-sale/ Retail	Commercial property: Industrial	Commercial property: Other	Commercial property: Total	Residential property: Single-family homes	Residential property: Multi-family homes	Residential property: Apart-ments	Residential property: Total	Total cover assets pool
31 Dec 2007												
Belgium			20.9		7.1		28.0					28.0
Denmark			104.5	42.4	7.1	31.3	185.3					185.3
Germany	1.4		145.8	37.3	114.2	117.1	414.4	51.8	20.6	560.9	633.3	1,049.1
Finland			27.4	226.1	5.4	20.4	279.3					279.3
France			17.9	58.9	106.5	45.3	228.6					228.6
UK			174.7	56.3	67.5		298.5					298.5
Italy			512.1	193.7	10.3	74.0	790.1			123.5	123.5	913.6
Canada			48.5			61.0	109,5					109.5
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					495.7
Sweden			149.8	71.9	154.6	57.9	434.2					434.2
Switzerland			140.5	50.8	2.8	25.4	219.5					219.5
Republic of Slovenia						48.6	48.6					48.6
Spain				289.6		39.8	329.4					329.4
Czech Republic			91.9			56.0	147.9					147.9
USA				13.4			13.4			56.6	56.6	70.0
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**

In the financial year 2008, the bank did not acquire any properties for the purpose of loss prevention (2007: none).

As at 31 December 2008, interest payments in the amount of € 7.2 million (2007: € 2.8 million) for commercial property and in the amount of € 0.3 million (2007: € 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.

As at 31 December 2008, there were no foreclosures or forced administration procedures pending.

Redemptions in cover assets pool

Euro mn	Commercial property 2008	Commercial property 2007	Residential property 2008	Residential property 2007
Scheduled repayments	159.6	82.1	50.1	30.1
Extraordinary repayments	482.8	803.8	130.3	127.6
Total	**642.4**	**885.9**	**180.4**	**157.7**

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:

		Public-sector entities			
Euro mn	Sovereigns	regional	municipal	Other	Total
31 Dec 2008					
Germany	164.6	2,224.9	36.8	33.3	2,459.6
Italy	89.0				89.0
France	25.0			49.4	74.4
Great Britain				7.5	7.5
Ireland	25.0				25.0
Austria	195.2	25.0			220.2
Switzerland		50.0			50.0
Spain		148.5	35.0	4.6	188.1
Hungary	25.0				25.0
Japan	50.0		20.0		70.0
Portugal	25.0	30.0			55.0
Total	**598.8**	**2,478.4**	**91.8**	**94.8**	**3,263.8**

		Public-sector entities			
Euro mn	Sovereigns	regional	municipal	Other	Total
31 Dec 2007					
Germany	200.0	1,812.0		670.1	2.682,1
Italy	114.0				114,0
France				43.2	43,2
United Kingdom				7.5	7,5
Austria	124.2	25.0		70.0	219,2
Switzerland		50.0			50,0
Spain		178.5	5.0	4.4	187,9
Hungary				25.0	25.0
Japan				50.0	50.0
Portugal			30.0	25.0	55.0
Total	**438.2**	**2.065.5**	**35.0**	**895.2**	**3.433,9**

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

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.

By means of a letter of comfort in favour of the Monetary Authority of Singapore, Aareal Bank AG has undertaken to ensure that Aareal Bank Asia Ltd. is able to fulfil its obligations at any time.

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 at the Wiesbaden local court (Amtsgericht Wiesbaden, company reg. no. HRB 13 184), and will also be available from Aareal Bank AG in Wiesbaden, Germany.

Loans to executive bodies of Aareal Bank

Loans granted to members of the Supervisory Board amounted to € 1.5 million as at 31 December 2008 (31 December 2007: € 3.3 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 € 2.1 million (2007: € 2.6 million) as at the balance sheet date. Loans extended generally have a term between 10 and 16 years, and bear interest at rates between 3.06 % and 7.29 %.

Remuneration report

Remuneration for members of the Management Board

The Supervisory Board determines the structure of the compensation package for the members of the Management Board; the amount of remuneration is set by the Supervisory Board's Executive Committee.

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

All details disclosed in the remuneration report were regrouped, and the previous year's comparative figures adjusted where necessary, to bring the report into line with the German Accounting Standard 17 (GAS 17), which was adopted in 2008.

In addition to fixed salary components, which are paid in twelve identical monthly instalments, the members of the Management Board receive other awards and benefits, as well as variable remuneration comprising a cash bonus plus a long-term remuneration component.

The long-term component includes a cash-settled, share-based compensation scheme (so-called ”phantom shares“), which are granted in the form of a long-term component I and a long-term component II. Phantom shares awarded under long-term component I must be held for three years, after which they can be exercised in the three following years. The allocation of phantom shares awarded under long-term component II is split in four equal parts over the year of allocation and the three following years, provided the member of the Management Board has not terminated his service contract at the time of exercise. The payments resulting from allocated phantom shares are taxable. For information related to the additional terms of this cash-settled, share-based compensation scheme, please refer to the explanations included in the corresponding section of the remuneration report.

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.

Fixed remuneration, cash bonus, and other awards and benefits received by each Management Board member are analysed below:

	Year	Fixed remuneration	Cash bonus	Other remuneration	Total
Dr Wolf Schumacher	2008	725,000.04	712,500.00	22,864,84	1,460,364.88
	2007	500,000.00	900,000.00	22,377,26	1,422,377.26
Norbert Kickum	2008	562,500.03	243,750.00	25,018,20	831,268.23
	2007	300,000.00	435,000.00	23,091,84	758,091.84
Hermann J. Merkens	2008	592,500.03	243,750.00	33,288,31	869,538.34
	2007	420,000.00	375,000.00	30,875,28	825,875.28
Thomas Ortmanns	2008	562,500.03	243,750.00	20,595,74	826,845.77
	2007	300,000.00	435,000.00	20,512,80	755,512.80
Total	**2008**	2,442,500.13	1,443,750.00	101,767,09	**3,988,017.22**
	2007	1,520,000.00	2,145,000.00	96,857,18	**3,761,857.18**

[1)] Other remuneration includes payments (in particular for company cars) in the amount of € 58,233.74 in 2008 (2007: € 53,772.86) as well as benefits related to social security contributions totalling € 42,794.40 (2007: € 43,084.32).

As a consequence of the bank’s agreement with the German Financial Markets Stabilisation Fund (”SoFFin“), fixed remuneration of the members of the Management Board for the financial years 2009 and 2010 have been capped at € 500,000 per annum. No cash bonus will be payable for these financial years.

The members of the Management Board received phantom shares as set out below, as a long-term remuneration component in line with the terms of the cash-settled, share-based compensation scheme.

		Long-term component I		Long-term component II		Total	
	Year	Value as at award date	Number	Value as at award date	Number	Number	Value as at award date
Dr Wolf Schumacher	2008	375,000.00	65,217.39 [1]	0,00	0.00	65,217.39	375,000.00
	2007	735,000.00	32,666.67 [2]	1,000,000.00 [3]	44,444.44	77,111.11	1,735,000.00
Norbert Kickum	2008	375,000.00	65,217.39 [1]	0.00	0.00	65,217.39	375,000.00
	2007	720,000.00	32,000.00 [2]	1,000,000.00 [3]	44,444.44	76,444.44	1,720,000.00
Hermann J. Merkens	2008	375,000.00	65,217.39 [1]	0.00	0.00	65,217.39	375,000.00
	2007	660,000.00	29,333.33 [2]	1,000,000.00 [3]	44,444.44	73,777.77	1,660,000.00
Thomas Ortmanns	2008	375,000.00	65,217.39 [1]	0.00	0.00	65,217.39	375,000.00
	2007	720,000.00	32,000.00 [2]	1,000,000.00 [3]	44,444.44	76,444.44	1,720,000.00

[1] The conversion was made on the basis of the share price as at 31 December 2008 (€ 5.75) as the final allocation price can be determined only after publication of the 2008 financial statements.

[2] In the remuneration report for 2007, the conversion of awarded euro amounts into a certain number of phantom shares was based on the share price as at 31 December 2007 (€ 31.30). However, the actual share price upon the allocation of phantom shares after publication of the 2007 financial statements was € 22.50. Accordingly, the number of phantom shares shown in the 2007 remuneration report was adjusted to reflect the actual allocation.

[3] In 2007 and 2008, each member of the Management Board was awarded of long-term component II in the amount of € 1 million, to honour their performance in the respective previous years. This component is allocated to the year it is financially attributable to.

As a consequence of the bank's agreement with the German Financial Markets Stabilisation Fund ("SoFFin"), no phantom shares will be awarded for the financial years 2009 and 2010.

Additional pension provisions were recognised in an amount of € 1,688,796.00 (2007: € 643,690.05). The total of pension provisions for active and former members of the Management Board and their surviving dependants amount to € 10,640,242.00 (2007: € 8,951,446.00). 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 to former Management Board members of Aareal Bank AG and their surviving dependants totalled € 510,059.46 (2007: € 571,790.11).

The agreements concluded with members of the Management Board do not include any 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 approx. 45% (2007: 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 30% (2007: 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 adopted by the Annual General Meeting on 23 May 2006, which resulted in a change of the remuneration system of the Supervisory Board, currently applies.

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 is increased by € 10,000.00 p.a. for any Supervisory Board committee membership (with the exception of the Committee for Urgent Decisions, which is a part of the Credit and Market Risk Committee). The fixed remuneration is increased instead by € 20,000.00 p.a. for the chairmanship of a Supervisory Board committee (again 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 the 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 2008 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 the 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 an unchanged fixed remuneration for the financial year 2008 in the amount of € 559,300.00. Provided that the Annual General Meeting approves the proposal of the Management Board not to distribute any dividends for the 2008 financial year, no variable remuneration (2007: € 202,300.00) will be paid to the members of the Supervisory Board.

The individual amount of the remuneration for the Supervisory Board is shown in the following table. The figures in the table include the reimbursement for VAT at the legally applicable rate (19%).

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

The members of the Supervisory Board did not provide any consulting or agency services, or other personal services in 2008. Therefore, no additional remuneration was paid.

Employees

The average staffing level is shown below:

	2008	2007
Employees		
of which:		
Full-time employees	902	945
Part-time employees	159	141
Vocational and other trainees	13	13
Total	**1,074**	**1,099**

Auditors' fees

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

€ 000's	
Category	
Audit	2,299.9
Other audit or valuation services	433.5
Tax advisory services	176.1
Other services	1,148.6
Total	**4,058.1**

Notice pursuant to section 21 (1) of the WpHG:

26 November 2008

Below, we Hermes Administration Services Limited as the authorised administration agent on behalf of BT Pension Scheme Trustees Limited, London, England ("BTPSTL") would like to make the following notifications regarding the holding of voting rights held in the Company according to §§ 21, 22 WpHG in the name of BTPSTL and its subsidiaries:

- BriTel Fund Nominees Limited, London, England ("BFNL");
- BriTel Fund Trustees Limited, London, England ("BFTL");
- Hermes Fund Managers Limited, London, England ("HFML");
- Hermes Focus Asset Management Europe Limited, London, England ("HFAMEL");
- Hermes Focus Asset Management Limited, London, England ("HFAML"); and
- Hermes European Focus Fund I, London, England ("HEFF").

1 Notification of voting rights for BTPSTL
On 25th November 2008 the voting interest held by BTPSTL in the Company fell below the 3% threshold of § 21 para. 1 WpHG and amounted to 2.948% of the voting rights (i.e. 1,260,521 shares with voting rights) on that day.
All of these 2.948% of the voting rights were attributed to BTPSTL pursuant to § 22 para. 1 sent. 1 no. 6 in connection with § 22 para. 1 sent. 2 WpHG.
2.813% of the voting rights (i.e. 1,202,623 shares with voting rights) were also attributed to BTPSTL pursuant to § 22 para. 1 sent. 1 no. 2 in connection with § 22 para. 1 sent. 2 WpHG. 2.813% of the voting rights (i.e. 1,202,623 shares with voting rights) were held directly by Chase Nominees Limited, London.

2 Notification of voting rights in the name and on behalf of BFNL
On 25th November 2008 the voting interest held by BFNL in the Company fell below the 3% threshold of § 21 para. 1 WpHG and amounted to 2.948% of the voting rights (i.e. 1,260,521 shares with voting rights) on that day.
All of these 2.948% of the voting rights were attributed to BFNL pursuant to § 22 para. 1 sent. 1 no. 6 in connection with § 22 para. 1 sent. 2 WpHG.

2.813 % of the voting rights (i.e. 1,202,623 shares with voting rights) were also attributed to BFNL pursuant to § 22 para. 1 sent. 1 no. 2 in connection with § 22 para. 1 sent. 2 WpHG. 2.813% of the voting rights (i.e. 1,202,623 shares with voting rights) were held directly by Chase Nominees Limited, London.

3 Notification of voting rights in the name and on behalf BFTL
On 25th November 2008 the voting interest held by BFTL in the Company fell below the 3 % threshold of § 21 para. 1 WpHG and amounted to 2.948 % of the voting rights (i.e. 1,260,521 shares with voting rights) on that day.
All of these 2.948 % of the voting rights were attributed to BFTL pursuant to § 22 para. 1 sent. 1 no. 6 in connection with § 22 para. 1 sent. 2 WpHG.
2.813 % of the voting rights (i.e. 1,202,623 shares with voting rights) were also attributed to BFTL pursuant to § 22 para. 1 sent. 1 no. 2 in connection with § 22 para. 1 sent. 2 WpHG. 2.813 % of the voting rights (i.e. 1,202,623 shares with voting rights) were held directly by Chase Nominees Limited, London.

4 Notification of voting rights in the name and on behalf of HFML
On 25th November 2008 the voting interest held by HFML in the Company fell below the 3 % threshold of § 21 para. 1 WpHG and amounted to 2.948 % of the voting rights (i.e. 1,260,521 shares with voting rights) on that day.
All of these 2.948 % of the voting rights were attributed to HFML pursuant to § 22 para. 1 sent. 1 no. 6 in connection with § 22 para. 1 sent. 2 WpHG.
2.813 % of the voting rights (i.e. 1,202,623 shares with voting rights) were also attributed to HFML pursuant to § 22 para. 1 sent. 1 no. 2 in connection with § 22 para. 1 sent. 2 WpHG. 2.813% of the voting rights (i.e. 1,202,623 shares with voting rights) were held directly by Chase Nominees Limited, London.

5 Notification of voting rights in the name and on behalf of HFAMEL
On 25th November 2008 the voting interest held by HFAMEL in the Company fell below the 3% threshold of § 21 para. 1 WpHG and amounted to 2.813% of the voting rights (i.e. 1,202,623 shares with voting rights) on that day.
All of these 2.813% of the voting rights were attributed to HFAMEL pursuant to § 22 para. 1 sent. 1 no. 6 and § 22 para. 1 sent. 1 no. 2 in connection with § 22 para. 1 sent. 2 WpHG. All of these 2.813% of the voting rights were held directly by Chase Nominees Limited, London.

6 Notification of voting rights in the name and on behalf of HFAML
On 25th November 2008 the voting interest held by HFAML in the Company fell below the 3 % threshold of § 21 para. 1 WpHG and amounted to 2.813 % of the voting rights (i.e. 1,202,623 shares with voting rights) on that day.
All of these 2.813 % of the voting rights were attributed to HFAML pursuant to § 22 para. 1 sent. 1 no. 2 in connection with § 22 para. 1 sent. 2 WpHG.
All of these 2.813 % of the voting rights were held directly by Chase Nominees Limited, London.

7 Notification of voting rights in the name and on behalf of HEFF
On 21st November 2008 the voting interest held by HEFF in the Company fell below the 3 % threshold of § 21 para. 1 WpHG and amounted to 2.717 % of the voting rights (i.e. 1,161,652 shares with voting rights) on that day.

All of these 2.717 % of the voting rights in the Company were attributed to HEFF pursuant to § 22 para. 1 sent. 1 no. 2 WpHG. All of these 2.717 % of the voting rights were held directly by Chase Nominees Limited, London.'

28 October 2008

On 24 October 2008, Franklin Mutual Advisers, LLC, New Jersey, USA, notified us in accordance with 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, German Securities ID: 540811, fell below the threshold of 3% of total voting rights on 23 October 2008 and amounted to 2.91% (corresponding to 1,245,152 voting rights) since that date. 2.91% of the voting rights (corresponding to 1,245,152 voting rights) are attributable to the company pursuant to section 22 (1) sentence 1 No. 6 of the WpHG.

15 October 2008

On 14 October 2008, Franklin Templeton Investment Funds, Luxembourg, Luxembourg notified us in accordance with section 21(1) of the German Securities Trading Act (Wertpapierhandelsgesetz, WpHG) that its share of voting rights in Aareal Bank AG, Wiesbaden, Germany, ISIN: DE0005408116, German Securities ID: 540811, fell below the threshold of 3% of total voting rights on 13 October 2008 and amounted to 2.98% (corresponding to 1,273,666 voting rights) on that day.

Furthermore, on 14 October 2008, Franklin Mutual Advisers, Short Hills, USA, notified us in accordance with section 21 (1) of the WpHG that its share of voting rights in Aareal Bank AG, Wiesbaden, Germany, ISIN: DE0005408116, German Securities ID: 540811, fell below the threshold of 5% of total voting rights on 10 October 2008 and amounted to 4.78% (corresponding to 2,043,434 voting rights) on that day. These 4.78% of the voting rights (corresponding to 2,043,434 voting rights) are attributable to Franklin Mutual Advisers, LLC pursuant to section 22 (1) sentence 1 No. 6 of the WpHG.

09 April 2008

Union Investment Privatfonds GmbH, Frankfurt, Germany, notified us in accordance with section 21 (1) of the WpHG, in a letter dated 11 March 2008 (which we received on 9 April 2008), that its voting rights arising from shares held in Aareal Bank AG, Wiesbaden, Germany (ISIN: DE00005408116; German Securities ID: 540811) fell below the threshold of 3%, amounting to 2.98% (or 1,272,900 voting rights) as at 11 March 2008.

31 January 2008

"29 January 2008

Notification of Voting Rights (Stimmrechtsmitteilung)

in the name and on behalf of FMR LLC, Boston, Massachusetts 02109, USA, we hereby notify you in accordance with section 21 (1) WpHG of the following:

On 25th January 2008 the voting rights held by FMR LLC fell below the threshold of 3% of the voting rights in Aareal Bank AG, Paulinenstrasse 15, 65189 Wiesbaden, Germany. On that date, FMR LLC held 2,56% of the voting rights in Aareal Bank AG, arising from 1.096.609 voting rights.

All voting rights in Aareal Bank AG were attributed to FMR LLC pursuant to section 22 (1) sent. 1 no. 6 in connection with sent. 2 WpHG.

29 January 2008
Notification of Voting Rights (Stimmrechtsmitteilung)

in the name and on behalf of Fidelity Management & Research Company, Boston, Massachusetts 02109, USA, we hereby notify you in accordance with section 21 (1) WpHG of the following:

On 25th January 2008 the voting rights held by Fidelity Management & Research Company fell below the threshold of 3% of the voting rights in Aareal Bank AG, Paulinenstrasse 15, 65189 Wiesbaden, Germany. On that date, Fidelity Management & Research Company held 2,56% of the voting rights in Aareal Bank AG, arising from 1.094.534 voting rights.

All voting rights in Aareal Bank AG were attributed to Fidelity Management & Research Company pursuant to section 22 (1) sent. 1 no. 6 WpHG.

29 January 2008

Notification of Voting Rights (Stimmrechtsmitteilung)

in the name and on behalf of Fidelity Investment Trust, Boston, Massachusetts 02109, USA, we hereby notify you in accordance with section 21 (1) WpHG of the following:

On 25th January 2008 Fidelity Investment Trust crossed below the threshold of 3% of the voting rights in Aareal Bank AG, Paulinenstrasse 15, 65189 Wiesbaden, Germany. On that date, Fidelity Investment Trust held 2,56% of the voting rights in Aareal Bank AG, arising from 1.094.534 voting rights."

Corporate Governance Code

The Declaration of Compliance regarding the German Corporate Governance Code, pursuant to section 161 of the AktG, has been published on our website: http://www.aareal-bank.com/investor-relations/corporate-governance/entsprechenserklaerung-gemaess-161-aktg/.

Proposal on the appropriation of profits

The Management Board proposes to the Annual General Meeting that the net retained profit of € 4,000,000.00 for the financial year 2008 be transferred 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 Public Limited Companies Act (AktG)

Supervisory Board

Hans W. Reich
Chairman Public Sector Group, Citigroup

Aareal Bank AG	Chairman of the Supervisory Board	
Citigroup Global Markets Deutschland AG & Co.KGaA	Chairman of the Supervisory Board	since 01 Sep 2008
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 Supervisory Boards of Bayerische Beamten Lebensversicherung Gruppe

Aareal Bank AG	Deputy Chairman of the Supervisory Board	
Bayerische Beamten Lebensversicherung a.G.	Chairman of the Supervisory Board	
Bayerische Beamten Versicherung AG	Chairman of the Supervisory Board	
BBV Holding AG	Chairman of the Supervisory Board	
BBV Krankenversicherung AG	Chairman of the Supervisory Board	until 31 Aug 2008
DePfa Holding Verwaltungsgesellschaft mbH	Chairman of the Supervisory Board	
Neue Bayerische Beamten Lebensversicherung AG	Chairman of the Supervisory Board	
MEAG MUNICH ERGO Kapitalanlagegesellschaft mbH	Member of the Supervisory Board	since 01 Jul 2008

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

Aareal Bank AG	Deputy Chairman of the Supervisory Board	

Christian Graf von Bassewitz,
Banker (ret'd.); former Spokesman of the General Partners of Bankhaus Lampe KG

Aareal Bank AG	Member of the Supervisory Board	
Balance Vermittlungs- und Beteiligungs-AG	Deputy Chairman of the Supervisory Board	since 27 Nov 2008
Bank für Sozialwirtschaft Aktiengesellschaft	Member of the Supervisory Board	
Deutscher Ring Krankenversicherungsverein a.G.	Member of the Supervisory Board	
Deutscher Ring Krankenversicherungsverein a.G.	Deputy Chairman of the Supervisory Board	since 06 Jun 2008
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	until 31 Oct 2008
Swiss Life Insurance Solutions AG	Chairman of the Supervisory Board	until 30 Jun 2008

Tamara Birke*
Aareal Bank AG

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

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

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		
Former Chief Executive Officer of Siemens Financial Services GmbH (ret'd.)		
Aareal Bank AG	Member of the Supervisory Board	
Siemens Kapitalanlagegesellschaft	Chairman of the Supervisory Board	until 19 Dec 2007
UBS Real Estate Kapitalanlagegesellschaft mbH	Deputy Chairman of the Supervisory Board	until 18 Mar 2008
UBS Global Asset Management (Deutschland) GmbH	Member of the Supervisory Board	since 01 Jul 2008

Joachim Neupel, Chairman of the Accounts and Audit Committee		
Certified Accountant and Tax Advisor		
Aareal Bank AG	Member of the Supervisory Board	

Prof Dr Stephan Schüller		
Spokesman of the General Partners of Bankhaus Lampe KG		
Aareal Bank AG	Member of the Supervisory Board	
Condor / Optima Versicherungen AG	Deputy Chairman of the Supervisory Board	until 30 Sep 2008
DePfa Holding Verwaltungsgesellschaft mbH	Member of the Supervisory Board	
NANORESINS AG	Chairman of the Supervisory Board	
PONAXIS AG	Chairman of the Supervisory Board	until 22 Sep 2008
Universal-Investment-Gesellschaft mbH	Member of the Supervisory Board	
hanse chemie AG	Chairman of the Supervisory Board	

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 Estate AG	Deputy Chairman of the Supervisory Board	
Aareal Valuation GmbH	Chairman of the Supervisory Board	
Aareon AG	Member of the Supervisory Board	
Leica AG	Member of the Supervisory Board	since 11 Apr 2008
Leica AG	Chairman of the Supervisory Board	since 18 Jun 2008

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 Capital Corporation	Member of the Board of Directors	since 21 Feb 2008
Aareal Capital Corporation	Chairman of the Board of Directors	since 21 Feb 2008
Aareal Financial Services USA, Inc.	Chairman of the Board of Directors	until 31 Mar 2008
Aareal-Financial Service spol. s r.o.	Member of the Supervisory Board	
Aareon AG	Member of the Supervisory Board	
Deutsche Structured Finance GmbH	Member of the Advisory Board	

Hermann J. Merkens, Member of the Management Board		
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 Capital Corporation	Member of the Board of Directors	since 21 Feb 2008
Aareal First Financial Solutions AG	Member of the Supervisory Board	
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	
RMS Risk Management Solutions GmbH	Member of the Supervisory Board	

Thomas Ortmanns, Member of the Management Board		
Aareal Bank France S.A.	Member of the Board of Directors	since 25 Jan 2008
Aareal First Financial Solutions AG	Chairman of the Supervisory Board	
Aareal Financial Services USA, Inc.	Member of the Board of Directors	until 31 Mar 2008
Aareon AG	Chairman of the Supervisory Board	
Innovative Banking Solutions AG	Member of the Supervisory Board	

Offices held

by employees of Aareal Bank AG pursuant to section 340a (4) no. 1 of the HGB

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		
Aareal Valuation GmbH	Member of the Supervisory Board	
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	
Dr Stefan Lange, Bank Director		
Aareal Estate AG	Member of the Supervisory Board	
Aareal First Financial Solutions AG	Member of the Supervisory Board	
Deutsche Bau- und Grundstücks-Aktiengesellschaft	Deputy Chairman of the Supervisory Board	until 25 Jul 2008
Deutsche Bau- und Grundstücks-Aktiengesellschaft	Member of the Supervisory Board	since 23 Feb 2009
Terrain-Aktiengesellschaft Herzogpark	Chairman of the Supervisory Board	
Peter Mehta, Bank Director		
Innovative Banking Solutions AG	Member of the Supervisory Board	
Markus Schmidt		
Deutsche Bau- und Grundstücks-Aktiengesellschaft	Member of the Supervisory Board	until 25 Jul 2008
Deutsche Bau- und Grundstücks-Aktiengesellschaft	Deputy Chairman of the Supervisory Board	25 Jul 2008 until 23 Feb 2009
Christine Schulze Forsthövel, Bank Director		
Aareal Bank France S.A.	President of the Board of Directors	until 22 Dec 2008
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	
Mansart Conseil S.A.S.	Chairman of the Supervisory Board	until 22 Dec 2008
Martin Vest, Bank Director		
Aareal Bank France S.A.	Member of the Board of Directors	

Composition of Supervisory Board committees

Executive Committee	
Hans W. Reich	Chairman
Erwin Flieger	Deputy Chairman
York-Detlef Bülow	Deputy Chairman
Prof Dr Stephan Schüller	
Wolf R. Thiel	

Committee for Urgent Decisions	
Hans W. Reich	Chairman
Christian Graf von Bassewitz	
Erwin Flieger	
Dr Herbert Lohneiß	
Joachim Neupel	

Accounts and Audit Committee	
Joachim Neupel	Chairman
Prof Dr Stephan Schüller	Deputy Chairman
Christian Graf von Bassewitz	
York-Detlef Bülow	
Hans W. Reich	

Nomination Committee
Hans W. Reich
Erwin Flieger

Credit and Market Risk Committee	
Hans W. Reich	Chairman
Dr Herbert Lohneiß	Deputy Chairman
Christian Graf von Bassewitz	
Tamara Birke	
Erwin Flieger	
Joachim Neupel	

Wiesbaden, 18 February 2009

The Management Board

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

Responsibility Statement

Statement pursuant to section 37y of the WpHG in conjunction with section 37w (2) no. 3 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, 18 February 2009

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 19 February 2009:

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 2008. 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, 19 February 2008

PricewaterhouseCoopers
Aktiengesellschaft
Wirtschaftsprüfungsgesellschaft (auditing firm)

Christian Rabeling	ppa. Thorsten Mohr
Wirtschaftsprüfer	Wirtschaftsprüfer
(German Public Auditor)	(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.

Aareal Bank AG implemented its own Corporate Governance Code in 1999. At the time, this code was established to ensure internal corporate governance standards exceeding the suggestions stipulated by the German Government Commission on Corporate Governance. Over recent years, Aareal Bank AG's code has been regularly reviewed and harmonised with the German Corporate Governance Code.

As a result of the ongoing developments and enhancements which have improved the German Corporate Governance Code, a separate, company-specific code has become largely redundant. To emphasise the importance of the German Corporate Governance Code, the Management Board and Supervisory Board of Aareal Bank AG have therefore decided to no longer maintain a company-specific Corporate Governance Code for Aareal Bank AG, to the extent that this Code is identical with the German Corporate Governance Code. The Corporate Governance principles Aareal Bank has implemented over and above the German Corporate Governance Code have been published on the bank's website.

Aareal Bank AG regularly monitors and analyses the annual amendments to the German Corporate Governance Code. The bank's Memorandum and Articles of Association, as well as the internal rules of procedure for the Management Board and the Supervisory Board, are reviewed regarding their compliance with the Government Commission's suggestions and recommendations, and amendments made as appropriate. Our annual Declaration of Compliance gives information on the extent to which the bank complies with recommendations. Once it has been adopted by the Management Board and the Supervisory Board, the Declaration of Compliance is published on the bank's website, which also includes archived Declarations of Compliance issued for previous years.

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. Our internal Code of Conduct is an integral part of responsible corporate governance. We revised the Code of Conduct for our staff during the 2008 financial year. The Code contains binding rules governing the legal and ethical conduct of employees vis-à-vis clients, business partners and colleagues. In this way, Aareal Bank also aims to affirm and further strengthen stakeholders' confidence in the company.

Recommendations of the German Corporate Governance Code

The German Corporate Governance Code (the "Code"), as last amended on 6 June 2008, comprises new recommendations and 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 18 December 2008. The Declaration was published on the bank's website, and is shown after this Corporate Governance Report.

Aareal Bank 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 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 a company's executive bodies. For this reason, the members of the company's executive bodies believe that it does not require a deductible.

Section 4.2.3 nos. 4 and 5 recommend that severance payments for members of the Management Board be capped. The Supervisory Board of Aareal Bank AG already discussed severance payment caps in detail in the past: for instance, the contracts entered into with members of the Management already provide for capped severance payments in the event of a change of control. The newly-added recommendation regarding caps on severance payments in the event of premature termination of the term of office on the Management Board refers to new contracts to be entered into with Management Board members. The recommendation is thus currently irrelevant for Aareal Bank AG. In the event of a new contract being considered, Aareal Bank AG's Supervisory Board will review implementing the recommendation.

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. In the previous year, there was no immediate need to implement this, as at the time, the Supervisory Board of Aareal Bank AG in its current composition had been in office for only a short term. As indicated last year, Aareal Bank AG assessed and reviewed this provision and its implementation in the marketplace during the 2008 financial year. Based on the results of its review, the Supervisory Board resolved to implement the recommendation even though there is no immediate need to do so, given the ongoing term of office of the current Supervisory Board. The Chairman of the Supervisory Board coordinated the identification of candidates for the Nomination Committee, from amongst shareholder representatives, reporting to the plenary meeting of the Supervisory Board on 18 December 2008. Shareholder representatives elected the members of the Nomination Committee at this plenary meeting.

Please refer to the remuneration report on page 68 for details on incentive systems in accordance with section 7.1.3 of the Code.

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 2008 financial year.

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

The Supervisory Board determines the structure and amount of remuneration for members of the Management Board. It determines the overall structure of the compensation package; specifically, setting fixed and variable (and any other) remuneration components for members of the Management Board. Details regarding remuneration for members of the Management Board are provided in the remuneration report on page 68 of this 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 2008 financial year in its report on page 89 of this Annual Report. The Executive Committee prepares the plenary meetings of the Supervisory Board.

The option of preparing meetings separately with shareholder representatives and employee representatives is used by the Supervisory Board in exceptional cases only. No such separate preparations took place during 2008, nor were there any Supervisory Board meetings without the members of the Management Board in attendance.

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

The members of the Supervisory Board have declared in writing that no conflicts of interest pursuant to section 5.5.2 of the Corporate Governance Code arose during the financial year under review.

The Supervisory Board reviews the efficiency of its own activities on a regular basis, where considerations are examined regarding the content, frequency and results of Supervisory Board meetings, as well as specific topics pertaining to the Supervisory Board and its 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 2008 review has not indicated any material need for improvement to the work of the Supervisory Board. The Chairman of the Supervisory Board presented the results of the examination of efficiency in the meeting on 18 December 2008, and discussed these with the members in detail. No organisational changes to enhance efficiency were required.

The Report of the Supervisory Board on page 89 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 2008 are provided in the separate Remuneration Report on page 68 of this Annual Report.

Purchase or sale of the company's shares

One transaction involving the company's shares was carried out in 2008 by members of the company's executive bodies. This was published on our website (amongst other places) in accordance with the legal provisions. 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 on page 68 of this Annual Report.

Accounting policies

Aareal Bank AG prepares the Group's accounts in accordance with 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 21 May 2008 appointed PricewaterhouseCoopers Aktiengesellschaft Wirtschaftsprüfungsgesellschaft, Frankfurt/Main, as the auditors for the 2008 financial year. The Supervisory Board appointed PricewaterhouseCoopers Aktiengesellschaft Wirtschaftsprüfungsgesellschaft, 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 73.

The Supervisory Board approves the financial statements and the consolidated financial statements, and thus confirms the financial statements. 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 internal growth programme, where we have set ourselves among other things 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 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 its financial position and results of operations four times annually. On these occasions, the Management Board gives a personal account of results, within the scope of press conferences and analysts' events.

We are not currently using 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 degree of acceptance 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.

Declaration of Compliance within the meaning of section 161 of the German Public Limited Companies 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 14 June 2007 and, with effect from 6 June 2008, as amended on that date) since the last Declaration of Compliance was issued in December 2007; in each case, except for the recommendations stated below.

Section 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 4.2.3 sections 4 and 5 of the Code recommend that severance payments be capped within the scope of the remuneration of members of the Management Board. The Supervisory Board of Aareal Bank AG already discussed severance payment caps in detail in the past: The present contracts for members of the Management Board already include for example, capped severance payments in the event of a change of control.

The newly-added recommendation regarding caps on severance payments in the event of premature termination of the term of office on the Management Board refers to new contracts to be entered into with Management Board members. The recommendation is thus currently irrelevant for Aareal Bank AG. In the event of a new contract being considered, Aareal Bank AG's Supervisory Board will review implementing the recommendation.

Aareal Bank AG will also comply with the recommendations of the German Corporate Governance Code (as amended on 6 June 2008) throughout the financial year 2009, with the aforementioned exceptions of section 3.8 and section 4.2.3 nos. 4 and 5.

For further details on the Corporate Governance Principles of Aareal Bank AG, please refer to our website: http://www.aareal-bank.com/investor-relations/corporate-governance/entsprechens-erklaerung-gemaess-161-aktg/.

Wiesbaden, December 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 Supervisory Board of Aareal Bank AG, Wiesbaden

Ladies and gentlemen, dear shareholders,

During the financial year under review, the crisis affecting international financial markets subjected the financial sector to turbulences on an unprecedented scale. To date, Aareal Bank AG successfully weathered the resulting challenges. The Supervisory Board takes this as a confirmation of the viability of Aareal Bank Group's business model. During the difficult 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, key financial indicators, and market developments. In addition, detailed reports and explanations were given to the Supervisory Board regarding the prevailing risk situation, and on the Group's 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 a Supervisory Board resolution was required, the proposals and documentation were submitted to the Supervisory Board, and a decision taken.

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 five scheduled occasions during the financial year under review. 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. Dealing with the challenges brought about by the financial markets crisis was a focal aspect of deliberations and reporting during all meetings. Specifically, this included monitoring the prevailing developments in Aareal Bank's business and regulatory environment, and the bank's necessary response. A further key aspect of the Supervisory Board's work was the reporting on the internal growth programme, together with related discussions and the implementation of measures. Reports and extensive discussions covered the programme as well as various individual aspects and consequences. The Supervisory Board supports the Management Board in implementing the programme, which is essential for the Company's future.

The main aspects discussed during individual meetings are outlined below.

The Management Board kept the Supervisory Board informed on the developments and consequences of the crisis affecting financial markets throughout the financial year, during all meetings as well as outside meetings, in a timely, detailed and transparent manner. The Management Board gave a comprehensive and complete account of the measures taken to respond adequately to the prevailing challenges for Aareal Bank AG posed by the financial markets crisis, and its consequences for the bank.

Aareal Bank Group was not invested in US sub-prime or US RMBS securities, nor in Collateralised Debt Obligations (CDOs), Asset Backed Commercial Paper (ABCP), Structured Investment Vehicles (SIVs); it also did not hold any exposures secured by monoline insurers. Aareal Bank has not held any Icelandic exposures (including any investments with banks in Iceland). The bank's exposure to products issued by Lehman Brothers was less than € 10 million. More than 90 per cent of the bank's approximately € 590 million ABS portfolio consist of AAA-rated issues; this includes approximately € 50 million invested in US Commercial Mortgage Backed Securities (CMBS). The loans underlying these instruments have been serviced without any defaults so far, which is why the amount invested is continuously falling. The bank's conservative investment policy, supported by its comprehensive internal reporting and control mechanisms continued to pay off.

Presentations regarding the progress made in implementing the internal growth programme were given at all Supervisory Board meetings, with detailed discussions held on the achievements in 2008.

In its March meeting, the Supervisory Board concerned itself in detail with the financial statements presented for the 2007 financial year, and with the auditors' report. The relevant facts were presented in the Supervisory Board report for the previous year. The meeting discussed the proposal for election of the external auditors to be submitted to the Annual General Meeting, as well as the subsequent instruction of the auditors. This included the scope and focal points of the Supervisory Board of the audit for the 2008 financial year.

Other topics of the March meeting were preparations for the Annual General Meeting in May 2008, the annual reviews prepared by Internal Audit and by the Compliance Officer. Adequate time was also dedicated to discussing the early extension of the terms of office of the members of the Management Board, Dr Schumacher and Messrs Kickum and Ortmanns, as well as the extension of Mr Merkens' term which was up for renewal.

The Supervisory Board held two meetings during the month of May. The first of these meetings involved the detailed discussion of the bank's strategic options given the current situation on the financial markets. The second meeting, held immediately after the Annual General Meeting, focused largely on the follow-up of the Meeting, and on the current state of planning regarding the organisational realignment of sales and risk management units in the Structured Property Financing segment.

The September meeting was dedicated to discussing the basics of corporate planning for the years ahead, as well as Corporate Governance issues.

The meeting in December focused on Group planning for the years 2009 to 2011. The Management Board submitted the planning and explained it in detail. Corporate governance issues were discussed as well. The Supervisory Board approved giving up the bank's own Corporate Governance Code, in favour of the German Corporate Governance Code, and adopted the Declaration of Compliance, pursuant to section 161 of the AktG, 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 2008 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. As in the previous year, no organisational changes to enhance efficiency were required.

In its plenary meeting in September, the Supervisory Board resolved to establish a Nomination Committee, in line with the recommendation of the German Corporate Governance Code, and on the basis of preceding discussions. Shareholder representatives discussed the composition of the Committee during the plenary meeting in December, under my direction. The members of the Committee were elected, and the Committee constituted, during the same plenary meeting. Please refer to the list of Supervisory Board Committees on page 81 of this Annual Report for details on the composition of the Committees.

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 strategic guideline 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.

Several Supervisory Board decisions were taken in writing, by way of circulation; a report on the implementation of said decisions was given in the subsequent meeting.

No conflicts of interest of members of the Supervisory Board, as defined in No. 5.5.3 of the German Corporate Governance Code, have been reported during the financial year 2008.

Activities of Supervisory Board committees

The Supervisory Board has established five 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, as well as the Nomination Committee, which was established during the year under review.

The Executive Committee, which advises the Management Board and prepares the resolutions of the Supervisory Board, met on three occasions. The Executive Committee's area of responsibility also includes assessing the internal condition of the Group. Further tasks include personnel planning and negotiating service contracts with regard to each member of 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.

The Executive Committee prepared the plenary meetings of the Supervisory Board, together with proposed resolutions. In its meeting in March 2008, the Executive Committee also discussed the degree to which the Management Board had achieved set targets in the 2007 financial year, and determined the variable remuneration of the members of the Management Board on that basis. In the same meeting, the Executive Committee renewed the appointment of incumbent members of the Management Board, Dr Wolf Schumacher (Chairman of the Management Board), Norbert Kickum, and Thomas Ortmanns, prior to the regular expiration of their service contracts. Their appointment to the Management Board was thus extended for another five years, from 1 April 2008 to 31 March 2013. The appointment of Hermann J. Merkens was also extended; his contract was up for renewal. By extending the terms of office of said Management Board members ahead of their renewal, the Supervisory Board wanted to demonstrate that Aareal Bank's executive team is strong and well-recognised in the market. With their successful execution of a fundamental realignment of the company, they have guided the bank towards sustainable growth, on the basis of a viable strategy. In doing so, it was the Supervisory Board's objective to retain this successful management team for the long term. During the same meeting, the Executive Committee discussed the membership of the Chairman of the Management Board in an executive body outside the Group, and approved it.

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, as well as supplementary reports on property markets that have been affected by the current financial markets crisis in particular. The committee members discussed these reports and market views in detail. The committee also dealt with the granting of loans requiring approval. The committee also noted any transactions subject to reporting requirements. The Management Board presented individual exposures of material importance for the bank to the committee members, who discussed these exposures with the Management Board. Furthermore, the committee discussed 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. The committee discussed reports submitted on the bank's risk situation, which were 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. Besides credit and country risks, the committee concerned itself with market and operational risks.

The Committee for Urgent Decisions is a subcommittee 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. Any decisions taken outside scheduled meetings of the Credit and Market Risk Committee were dealt with in the subsequent meeting of the parent committee.

The Accounts and Audit Committee, which is responsible for all Group accounting and audit issues, held five meetings during the year under review. The committee is responsible for preparing and supervising the conduct of the audit of the bank's financial statements and consolidated financial statements; it prepares the Supervisory Board decisions on the basis of its analysis of the audit reports submitted by the external auditors. For this purpose, it reports on the results of its analysis, and the resulting assessments, to the Supervisory Board. Preparing the audit of the financial statements also includes the preparations for instructing the external auditors, in accordance with the resolution adopted by the Annual General Meeting, verifying the independence of the external auditors, negotiating the audit fee, and determining focal points for the audit. Additional responsibilities of the Accounts and Audit Committee include verifying the budget planning submitted by the Management Board, and receiving the report of the Group Compliance Officer.

In its meetings, in line with its duties under the bank's 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 March 2008, the Accounts and Audit Committee received the external auditors' report on the 2007 financial year and discussed the results with the auditors. Having examined the audit reports presented and discussed these with the external auditors (who gave a personal account of the audit), the members of the committee formed their own judgement of the audit results. During the autumn meeting, preliminary information was given on the progress of the audit for the 2008 financial year, and issues discussed, which arose in the course of preparing the financial statements. This also included current developments in accounting practices and their implications for Aareal Bank Group. 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 December meeting, together with an update on the audit progress.

Following the publication of amendments to the German Corporate Governance Code, the committee convened additional meetings during which the quarterly results to be published were presented to the committee members, and discussed with the Management Board.

In its meeting on 19 March 2009, the Accounts and Audit Committee received the external auditors' detailed report on the audit and audit results for the 2008 financial year, and extensively discussed these results with the auditors and the Management Board.

In its September meeting, the Supervisory Board resolved to establish a Nomination Committee, in accordance with the recommendations of the German Corporate Governance Code. As outlined above, the committee was elected during the December plenary meeting, but held no meetings in 2008. The task of the committee is to coordinate and conduct the search for new Supervisory Board members in the event of shareholder representatives retiring. Given that the incumbent Supervisory Board's current term of office is still ongoing, no activities of the committee were required.

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 above 90%.

Transactions of particular importance during 2008

On 20 May 2008, Aareal Bank AG announced an agreement on the successful disposal of a portfolio of residential property loans totalling € 1.47 billion to Deutsche Postbank AG. The retail business no longer forms part of Aareal Bank's core business, and is thus no longer actively pursued. Shareholders gave their required approval of this transactions with a resolution passed by the Annual General Meeting on 21 May 2008. With this transaction, which was also approved by the antitrust authorities, Aareal Bank reduced its retail home loan portfolio by approx. 84%. For Aareal Bank AG, securing a sustained and comprehensive service for customers was a priority: this has been safeguarded with the sale to one of Germany's largest retail banks. Both parties to the transaction took great care to ensure that the legal details preserve customers' rights without restriction.

In September 2008, Aareon AG took over Sylogis.com AG, a French software house, acquiring 100% of its capital effective 1 October 2008. This has allowed the bank's subsidiary to significantly strengthen its business in France, where it has been present with its Aareon France unit since 2000. Besides Aareon France, Sylogis.com is one of the leading providers of property management software: the new subsidiary is well established in the social housing, commercial housing, and corporate property market segments. The Supervisory Boards of Aareal Bank and Aareon approved this acquisition, which has turned Aareon into a leading French provider.

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 2008, 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 and the Group Management Report, and certified them 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, PriceWaterhouseCoopers Aktiengesellschaft Wirtschaftsprüfungsgesellschaft, 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 26 March 2009, 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, together with the consolidated financial statements prepared in accordance with IFRS and the Group Management Report, and thus confirmed the financial statements. 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.

In conclusion, the Supervisory Board would like to thank all of the company's employees for their successful work during the 2008 financial year. Throughout the recent months, which were characterised by fundamental upheaval on the international financial markets and indeed the entire banking sector, their commitment and motivation contributed to the successful manner in which Aareal Bank Group mastered the challenges of these exceptional times.

Kronberg, March 2009

For the Supervisory Board

Hans W. Reich, Chairman

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Financial Calendar

7 May 2009	Annual General Meeting – Kurhaus, Wiesbaden
12 May 2009	Presentation of interim report as at 31 March 2009
August 2009	Presentation of interim report as at 30 June 2009
November 2009	Presentation of interim report as at 30 September 2009

North America

Europe

Asia/Pacific

- Structured Property Financing
- Consulting/Services

Aareal Bank, Real Estate Structured Finance: Amsterdam, Berlin, Brussels, Copenhagen, Dublin, Hamburg, Helsinki, Istanbul, London, Madrid, Milan, Moscow, Munich, New York, Paris, Prague, Rome, Shanghai, Singapore, Stockholm, Warsaw, Wiesbaden, Zurich | **Aareal Valuation GmbH:** Wiesbaden | **Aareal Estate AG:** Wiesbaden

Aareal Bank, Institutional Housing Unit: Berlin, Essen, Hamburg, Leipzig, Munich, Stuttgart, Wiesbaden | **Aareon AG:** Berlin, Coventry, Dortmund, Dresden, Erfurt, Hamburg, Hannover, Hückelhoven, Leipzig, Mainz, Meudon La Foret, Munich, Oberhausen, Orléans, Rostock, Rome, Stuttgart | **Deutsche Bau- und Grundstücks-AG:** Berlin, Bonn, Moscow, Munich | **Aareal First Financial Solutions:** Wiesbaden | **Innovative Banking Solutions AG:** Wiesbaden

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Aareal Bank