QUALITY made by AAREAL

# In motion.
# By conviction.

Aareal Bank Group – Interim Report
1 January to 30 June 2016

Aareal

# Key Indicators

| | 1 Jan-30 Jun 2016 | 1 Jan-30 Jun 2015 |
|---|---|---|
| **Results**[1] | | |
| Operating profit (€ mn) | 207 | 296 |
| Consolidated net income (€ mn) | 142 | 250 |
| Consolidated net income allocated to ordinary shareholders (€ mn)[2] | 124 | 232 |
| Cost/income ratio (%)[3] | 42.4 | 45.3 |
| Earnings per ordinary share (€)[2] | 2.08 | 3.87 |
| RoE before taxes (%)[2] [4] | 15.1 | 24.2 |
| RoE after taxes (%)[2] [4] | 10.1 | 20.4 |

| | 30 Jun 2016 | 31 Dec 2015 |
|---|---|---|
| **Statement of financial position** | | |
| Property finance (€ mn)[5] | 30,271 | 30,894 |
| of which: international (€ mn) | 25,393 | 25,243 |
| Equity (€ mn) | 3,025 | 3,044 |
| Total assets (€ mn) | 50,925 | 51,948 |
| | | |
| **Regulatory indicators** | | |
| Risk-weighted assets (€ mn) | 16,308 | 16,709 |
| Common Equity Tier 1 ratio (CET1 ratio) (%) | 13.7 | 13.8 |
| Tier 1 ratio (T1 ratio) (%) | 16.9 | 17.2 |
| Total capital ratio (TC ratio) (%) | 23.8 | 23.8 |
| | | |
| Common Equity Tier 1 ratio (CET1 ratio) (%) – fully phased – | 13.2 | 13.1 |
| | | |
| **Employees** | 2,813 | 2,861 |
| | | |
| **Rating** | | |
| Fitch Ratings, London | | |
| long-term | BBB+ (outlook: stable) | BBB+ (outlook: stable) |
| short-term | F2 | F2 |
| Fitch Pfandbrief ratings | AAA | AAA |
| **Sustainability**[6] | | |
| oekom | prime (C) | prime (C) |
| Sustainalytics | 68 | 68 |

[1] Adjustment of previous year's figures due to completion of purchase price allocation for Westdeutsche ImmobilienBank AG (WestImmo), in accordance with IFRS 3

[2] The allocation of earnings is based on the assumption that net interest payable on the AT1 bond is recognised on an accrual basis.

[3] Structured Property Financing segment only

[4] On an annualised basis

[5] Excluding € 1.3 billion in private client business (31 December 2015: € 1.5 billion) and € 0.6 billion in local authority lending business by WestImmo (31 December 2015: € 0.6 billion)

[6] Please refer to our Sustainability Report for more details.

This report contains rounded numbers, which may result in slight differences when aggregating figures and calculating percentages.

# Contents

# Letter from the Management Board

Dear shareholders,
business associates and staff members,

The market environment in which Aareal Bank Group does business was exposed to strong pressure and significant uncertainty during the second quarter. The situation remained challenging, both in terms of economic development and industry-specific issues as well as the geopolitical environment. Essentially, the past months were shaped by events which further increased uncertainty – in society and on the capital markets. Market volatility received yet another boost from the surprising vote by the UK population to leave the EU, whilst the awful terrorist attacks in Brussels exacerbated fears of a terrorist threat to Western society. The terrorist attacks in France and Germany, and the dramatic situation in Turkey following the failed military coup – which each occurred after the period under review – have shown that the situation will remain tense, with the corresponding impact on the global economy.

Global economic growth remained muted: even though the US economy continued to develop favourably, it failed to match the growth rates seen in the previous year. The same applies to Asia, where economic momentum remained subdued, especially due to a more restrained development in China. The European economy is likely to see a moderate development this year – whereby the economic impact of Brexit cannot even be assessed yet. Whilst the suspension of various open-ended UK property funds are seen as initial signals of a burden placed by the referendum on the UK commercial property market, we do not perceive these developments as being representative of the overall market, nor do we see any immediate impact on our UK portfolio. The response on financial and capital markets was accordingly nervous during the course of the quarter. For instance, the German blue-chip DAX® index temporarily dropped by as much as ten per cent on the day following the referendum – the biggest fall since the collapse of US investment bank Lehman Brothers in 2008. Nonetheless, thanks to the continued high levels of liquidity, markets were prepared to absorb new issues from banks, corporates, and sovereign issuers. Equity markets have recovered in the meantime, however: the DAX® reached its pre-Brexit level.

The monetary policy stance of the major central banks continued to diverge during the second quarter: whilst the US Federal Reserve (Fed) refrained from any further hikes in its key interest rate since turning around in December 2015, the European Central Bank (ECB) and the Bank of Japan further loosened their respective monetary policies. The ECB once again expanded its corporate bond purchasing programme, raising it to a volume of € 80 billion per month and including investment-grade bonds from non-bank issuers in the range of eligible issues. Negative interest rates continue to apply to central bank deposits of commercial banks. Still, the monetary policy measures continue to hardly trigger any discernible positive effects.

Hence, the banking sector will continue to face the known challenges from the low interest rate environment for the time being. Additionally, public attention shifted towards the situation of various Italian banks with significant holdings of potentially impaired loans. Competitive pressure in the attractive commercial property business segment remained high, with a trend continuing to emerge whereby finance providers are prepared to accept higher risks and lower margins. In line with the "Aareal 2020" programme presented in February, the focus in the Bank's new business origination is on the US market, which accounted for a share in newly-originated loans of approximately 40 per cent during the first half of 2016. In this way, Aareal Bank continued to be successful in largely offsetting margin pressures in the Structured Property Financing segment in the quarter under review. The trend towards declining transaction volumes, which became evident at the start of the year, has prevailed, with pressure on investment yields subsiding slightly. The regulatory environment will remain demanding for the foreseeable future, whereby the specific impact of various impending initiatives is still rather hard to assess.

However, in this environment characterised by numerous uncertainty factors and intense competition, Aareal Bank Group has continued its successful business development. Consolidated operating profit rose to € 120 million in the second quarter, a marked increase over the same period of the previous year (€ 79 million, adjusted for the negative goodwill from the acquisition of Westdeutsche Immobilien-Bank AG – "WestImmo"). Results were influenced by two non-recurring effects: on the one hand, by non-recurring income of € 61 million from the announced sale of a commercial property in Sweden, closed in April – and on the other hand, by non-recurring effects in the amount of € 30 million affecting administrative expenses, predominantly related to the integration of WestImmo – which is proceeding on schedule – as well as for strategic projects and investments. We see the fact that we once again posted a very good set of results as proof that Aareal Bank Group, with its two segments of Structured Property Financing and Consulting/Services, is in an excellent position to benefit from opportunities available – even in a challenging environment.

As expected, net interest income in the Structured Property Financing segment failed to match the very good figure posted in the previous year. This was predominantly due to the reduction of non-strategic portfolios in the meantime, as well as to lower year-on-year effects from early loan repayments. Margin levels remained robust during the first half of the year. Following the low level seen in the first quarter of 2016, due to seasonal factors, allowance for credit losses was slightly lower year-on-year, within our expected range. Overall, we continue to forecast allowance for credit losses to fall to a range between € 80 million and € 120 million. Once again, this is proof of the high quality of Aareal Bank Group's credit portfolio, and its outstanding risk management skills.

New business originated in the segment showed a very dynamic development during the second quarter. Thanks to several larger-sized portfolio financings, new business originated during the second quarter totalled € 3.5 billion, bringing the total figure for the first six months to € 4.4 billion. Newly-originated loans accounted for approximately 68 per cent of new business. The target for new business in this segment for the full year 2016 remains unchanged, at between € 7 billion and € 8 billion.

In the Consulting/Services segment, which – pursuant to the new Group strategy communicated at the beginning of the year – constitutes the Group's growth driver, IT subsidiary Aareon AG once again developed positively. The market leader in IT services to the housing industry increased sales revenues by more than ten per cent, boosting operating results by roughly one-third year-on-year. In this context, Aareon especially pursued international cross-selling of its products, together with the development and/or market launch of new digital services within the framework of the Aareon Smart World.

In the segment's banking business, the volume of client deposits from the housing industry remained at a high level, averaging € 9.5 billion during the quarter under review (Q1 2016: € 9.3 billion). Aareal Bank Group continues to enjoy significant levels of trust as the long-standing lead bank to the housing industry. Nonetheless, results in the banking business with the housing industry continue to be burdened by historically low interest rates. On aggregate, this led to a segment operating loss of € 8 million.
Yet the importance of deposit-taking goes way beyond the interest margin generated from the deposits, which is under pressure in the current market environment. For Aareal Bank, deposits from the housing industry remain a strategically important additional source of funding for the property financing business, and one that is largely independent of developments on the capital markets. In addition to the German

Pfandbrief and unsecured bank bonds, they represent an important pillar in the Bank's long-term funding mix. We must assume that the ECB is unlikely to turn around its interest rate policy in the near future.

We continued to be able to implement our funding activities during the second quarter of 2016, as planned – further strengthening our solid funding situation by raising € 0.4 billion in unsecured issues. In any case, thanks to its broadly-diversified long-term funding mix, which includes a significant share of private placements as well as the deposits from the housing industry, Aareal Bank Group is less dependent – compared to its competitors – upon the ability of capital markets to absorb new issues. As at 30 June 2016, the Bank's Tier 1 ratio was 16.9 per cent, which is comfortable on an international level. Assuming full implementation of Basel III, the fully phased-in Common Equity Tier 1 (CET1) ratio would be 13.2 per cent. This means that Aareal Bank continues to have a very solid capital base.

Overall, we can once again be very satisfied with business developments during the quarter under review. Aareal Bank Group has proven itself once again, in a persistently challenging environment.

In spite of the prevailing uncertainty factors and challenges, we remain generally optimistic for the remainder of the financial year. We must continue to assume a subdued performance of the global economy, which will remain susceptible to disruption, given a variety of uncertainty factors and burdens. Likewise, uncertainty remains regarding the final specifications of various regulatory initiatives, which may also have significant implications for the property finance business. Yet we affirm the full-year forecasts we communicated in February. We continue to anticipate being able to generate consolidated operating profit of € 300 million to € 330 million in the current financial year.

There are good reasons for our confidence. Thanks to our operative strength, the risk-averse nature of our business model, and our deep market knowledge, we are able to deliver outstanding results even during challenging times. What is more: with our forward-looking "Aareal 2020" programme, we have set the course for Aareal Bank Group to remain successful in the future. In this context, the Structured Property Financing segment will remain the Group's solid foundation, whilst the Consulting/Services segment has already started taking the role of a growth driver. We are making good progress implementing the programme. We are promoting cooperation and mutual learning across the Group, not least thanks to the changes in our internal organisational structure. In this way, we will enhance the Bank's overall agility, its power to innovate and readiness for change – for you, Aareal Bank Group's shareholders, for our clients and for the Group's staff.

**For the Management Board**

Yours sincerely,

**Hermann J. Merkens**
**Chairman**

# Group Management Report

## Report on the Economic Position

### Macro-economic environment

#### Economy

Global economic development remained subdued during the first half of 2016, posting only a very modest year-on-year increase. Whilst the first quarter was characterised by a variety of uncertainty factors and volatility in emerging markets, the referendum on the UK's exit from the EU was the dominant event during the second quarter. In contrast, the ifo World Economic Survey index rose slightly during the second quarter, compared to the first quarter of 2016, bringing the index decline seen during previous quarters to a halt in virtually all regions. The index even showed marked improvement in North America, whereas it remained at a low level in Asia. Uncertainty and burdening factors for the global economy remained high nonetheless, facing geopolitical risks and upheavals (such as in China). Uncertainty surrounding interest rate moves in the US had an additional dampening effect. Crude oil prices rose during the first half-year, remaining stable at the mid-year point.

Unemployment in the European Union (EU) further declined slightly until the middle of the year, a trend observed in almost all member states. Job creation in the US was low in May, but clearly stronger in June. The unemployment rate rose slightly at the mid-year point, remaining however at a low level overall.

#### Financial and capital markets, monetary policy and inflation

Having experienced stronger volatility at the beginning of the year, the financial markets stabilised during the course of the first half-year, with an improving economic outlook. On 23 June, the United Kingdom's population voted in favour of the UK leaving the EU. The outcome of the referendum triggered strong volatility on the financial markets, creating political uncertainty in the United Kingdom as well as in the EU member states.

One day following the referendum, Moody's cut the rating outlook for the UK from "stable" to "negative", citing the threat of falling consumer spending and lower investments as some of the factors behind the downgrade. Fitch lowered the UK's sovereign rating from "AA+" to "AA"; S&P also lowered its rating. The rating agencies saw no need to adjust ratings or the outlook for other EU countries after the first half of the year. Moreover, the focus shifted towards the situation of Italian banks: the Italian government planned to support domestic banks with € 40 billion in capital or guarantees. The country had already launched a € 4 billion rescue fund in April, designed to salvage distressed banks. Markets generally remained liquid and receptive.

The most important central banks maintained their diverging monetary policies during the first half of the year. This meant that central banks' generally expansive monetary policy stance remained unchanged. Accordingly, the European Central Bank (ECB) left its key interest rates (last decided upon in March) unchanged at its meeting on 2 June 2016. As of 8 June 2016, the ECB increased its bond-buying programme by € 20 billion to a monthly volume of € 80 billion. For the first time, the ECB also bought investment-grade bonds of non-bank corporate issuers. The ECB commenced its targeted longer-term refinancing operations (TLTROs) on 24 June 2016. The Bank of Japan retained its negative interest rate (-0.1 %) on excess reserves held with the central bank. Whilst the key Swedish interest rate remained unchanged, at -0.50 %, the expansive monetary policy was increased further by the announcement of an additional SEK 45 billion of government bond purchases during the second half of 2016.

In contrast, the US Federal Reserve (Fed), which had slightly raised its key interest rate – for the first time in almost ten years – in December 2015, made no further adjustments to monetary policy during the first six months of 2016. Instead, the Fed remained on the sidelines, faced with diverging fundamental data as well as uncertainty with regard to the referendum in the UK.

The first half of the year was characterised by diverging interest rate developments in the various currency areas, and for different maturities. Whilst short-term interest rates[1] in the US and Canada remained virtually unchanged from the levels seen in December 2015, they decreased markedly in the euro area, Sweden, Denmark, Japan and Switzerland. In the UK, medium- to long-term interest rates fell strongly during the first days following the referendum, whereas short-term rates only declined marginally, having already stabilised during the week following the referendum. In contrast, long-term interest rates[2] were in decline – in some cases even strongly – in all currency areas mentioned. The yield on ten-year German government bonds fell below zero in mid-June. Yields on ten-year Spanish and Italian government bonds continued to fall during the course of the year. Even though yields in Italy and Spain rose by a few basis points following the referendum in the UK, they remained at a very low level. In Japan, ten-year government bond yields continued to decline, also following the referendum.

Exchange rates of important currencies for Aareal Bank AG versus the euro showed strong fluctuations at the end of June. The euro, which had shown marked gains against the US dollar at the outset, surrendered its gains towards the end of the first half-year – a trend that was also influenced by the referendum in the UK. Hence, at the mid-year point, the euro/US dollar exchange rate traded at similar levels to the end of 2015.

During the first six months of the year, the Harmonised Consumer Price Index (HCPI) in the euro zone continued to reflect low energy prices, with an inflation rate close to zero. Core inflation was unchanged, remaining just below one per cent. However, towards the end of the first half-year, the impact of low energy prices weakened. In contrast, medium-term inflation expectations[3] continued to decline. The US inflation rate (not seasonally adjusted) was one per cent at the end of June.

## Regulatory environment

The environment in which banks are operating continues to be defined by highly dynamic regulatory requirements, as well as by changes in banking supervision. Especially when considering the extensive work the Basel Committee is undertaking to complete the already-implemented Basel III regime, it is currently not possible to fully assess the impact. However, according to a statement by the Group of Central Bank Governors and Heads of Supervision (GHOS), the changes are not expected to lead to significant burdens overall. Moreover, amendments to the Minimum Requirements for Risk Management in Banks (MaRisk) will bring about further regulatory changes, especially concerning the aggregation of risk data and risk reporting.

Following the introduction of the Single Supervisory Mechanism (SSM), Aareal Bank Group has been directly supervised by the ECB since 4 November 2014.

The Supervisory Review and Evaluation Process (SREP) ensures a common approach is taken by the ECB on the supervisory review of banks, within the framework of Pillar II. The SREP is built around a business model analysis, an assessment of governance and controls, as well as of the capital and liquidity risks. The results of the individual areas are aggregated in a score value, from which the ECB derives supervisory measures on holding additional capital (via an SREP assessment notice) and/or additional liquidity requirements. Aareal Bank Group's current SREP requirement is a Common Equity Tier 1 capital ratio (CET1 ratio), including capital conservation buffer, of 8.75 %. No additional liquidity requirements were set.

[1] Calculated on the basis of 3-month Euribor or the corresponding LIBOR or other comparable rates for other currencies
[2] Based on the 10-year swap rate
[3] Based on the 5y/5y forward swap for the euro zone

## Sector-specific and business developments

### Structured Property Financing segment

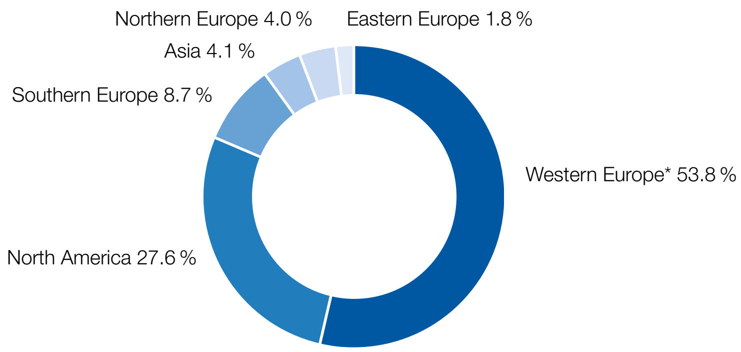
In the persistent low interest rate environment, commercial property continued to be a sought-after asset class in the first half of 2016. However, global transaction volumes (the aggregate capital invested in newly-acquired commercial properties) showed a marked decline from the extraordinarily high levels seen in the same period of the previous year. During the second quarter of 2016, volumes remained virtually unchanged, compared to the first quarter, in Europe and the US, whereas they declined in the Asia/Pacific region. Investment yields for newly-acquired commercial property remained low, with signs of the downtrend seen in previous periods flattening. This meant that investment yields for first-class properties remained almost constant in many markets, compared to the fourth quarter of 2015 and the first quarter of 2016, with slight declines seen only in some places.[1] Rents for first-class commercial properties were virtually stable on most markets; although rents were rising in some markets, and declined in others when let to new tenants.

Commercial property financing has remained a highly competitive business on most markets. Margins solidified in Europe, as well as in the US – where they remained at higher levels than in many European countries, particularly when compared to Western and Northern Europe. Pricing levels on the US market are also influenced by the market for commercial mortgage-backed securities (CMBS). Transactions in this segment fell short of expectations, thus supporting margins.

Aareal Bank originated higher new business[2] during the first half of 2016 than in the same period of the previous year – in a highly competitive business environment and a general framework characterised

**New business 1 January-30 June 2016**

by region (%) Total volume: € 4.4 bn




* Including Germany

by uncertainty. Aareal Bank Group's new business during the second quarter rose considerably over the first quarter, reflecting the closing of several larger-sized portfolio financings. It amounted to € 3.5 billion (Q2 2015: € 1.8 billion), bringing the total for the first half of 2016 to € 4.4 billion (H1 2015: € 3.6 billion). Newly-originated loans accounted for 68.4 % or € 3.0 billion during the first six months (H1 2015: 57.1 % / € 2.1 billion). During the quarter under review, newly-originated loans totalled € 2.4 billion (Q2 2015: € 1.2 billion) of new business, or 68.9 % (Q2 2015: 66.1 %).

At 68.3 % (Q2 2015: 73.3 %), Europe accounted for the largest share of new business, followed by North America (27.6 % vs. 25.3 %) and Asia (4.1 % vs. 1.4 %). Overall, new business developed in line with projections for the year as a whole.

#### Europe

Interest in commercial property remained high, not least given a lack of investment alternatives. Still, despite remaining above their long-term average,

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

[2] Excluding new business for private clients and local authority lending by WestImmo

transaction volumes showed a marked decline compared to the same period of the previous year. The decline was particularly evident in the markets of the UK, Germany and France. Besides uncertainty weighing on the markets, a lack of suitable properties on the market was a factor contributing to the decline – as well as the fact that the previous year's figure was particularly high. Private investors were seen as sellers, whereas the majority of buyers were institutional investors. Poland bucked the general market trend in Europe, showing higher transaction volumes, whilst they remained constant in Italy. Transaction volumes in Europe increased slightly, compared to the first quarter of the year; in some countries (including France, Italy, Spain and Poland) they even increased during the period under review. Yields for newly-acquired first-class commercial property in the European economic centres were virtually unchanged compared to the 2015 year-end. Yield spreads between prime and second-tier cities, as well as between the property types of offices, retail and logistics generally continued to decline.

Stable rents were observed in most European economic centres during the second quarter, with slight rent increases in some markets: this applied to office, retail and logistics properties. Rent increases for first-class office properties were observed in Barcelona, Berlin, Madrid, and Stockholm, for example. Examples for retail rent increases included Berlin and London. Rents for logistics properties remained stable overall, with slight declines in Brussels, for example.

Hotel markets in the big European economic centres showed a mixed picture during the first half of 2016, not least due to the terrorist attacks in Paris and Brussels. Average revenue per available room, a key performance indicator for the hotel markets, improved over the corresponding period of the previous year in some markets, such as Amsterdam, Barcelona, Berlin, Madrid and Prague, whereas it declined in other markets including London and Cologne. In Paris, average revenue per available hotel room decreased noticeably, as occupancy ratios clearly fell short of last year's levels – quite obviously a consequence of the terrorist attacks in November of last year. The Brussels terrorist attacks in March caused similar effects, with repercussions also felt until the mid-year point.

Aareal Bank Group succeeded in generating € 2.7 billion of new business in Europe during the second quarter (Q2 2015: € 1.6 billion), and therefore € 3.0 billion overall during the first half of the year (H1 2015: € 2.7 billion). Western Europe accounted for the highest share, followed by Southern, Northern, and Eastern Europe.

### North America (NAFTA states)

Commercial property transaction volumes in North America (NAFTA states) declined markedly year-on-year during the first half of 2016. Besides the fact that the previous year's figures were particularly high, declining volumes during the first six months of this year reflected a lower engagement by Asian investors in particular. Whilst listed companies were net sellers, cross-border buyers and institutional investors were seen on the buyers' side. Transaction volumes in the US remained virtually stable during the second quarter, compared to the first quarter of 2016.

In the office property segment, a slight yield increase was observed in some markets (such as Boston and San Francisco) during the first half-year. Property yields in the retail and logistics segments also increased to a very modest extent.

Rents slightly increased on a national average in the US, compared to the end of 2015, for the various types of property, with virtually constant vacancy ratios. This development also applied for many of the leading regional markets in the US.

The moderate improvement in some indicators for the US hotel markets, which had already been evident in the previous year, continued into the first six months of 2016. Average revenues rose compared to the same period of the previous year, especially due to slightly higher room rates, whilst the occupancy ratio was slightly lower year-on-year.

Aareal Bank Group originated new business of € 0.7 billion in North America during the second quarter (Q2 2015: € 0.2 billion), bringing aggregate new business in North America to € 1.2 billion for the first half-year (H1 2015: € 0.9 billion). All of this was originated in the US.

### Asia

Transaction volumes in the Asia/Pacific region during the first half of the year were markedly lower compared to the same period of the previous year; they also declined compared to the previous quarter. Whilst the share of cross-border investments rose, investments by private and institutional investors declined. Both Japan and China saw significant volume declines, whereby large-sized transactions were lacking in Japan in particular.

Yields for first-class properties in Japan continued to decline during the first half of the year. In China, they remained stable in Beijing, whereas yields for office property in Shanghai continued to decline slightly. In Singapore, yields for office property declined during the first six months, whilst remaining constant for the retail segment. Rents for first-class office, retail and logistics properties in the three metropolitan areas of Beijing, Shanghai and Tokyo hardly changed, remaining stable during the period under review. In contrast, rents for these three property types were under pressure in Singapore.

The hotel markets in Beijing, Shanghai, Singapore and Tokyo developed favourably, compared to the first half of 2015, with rising average revenues per available hotel room. The picture was only clouded, to a minor extent, by a slight decline in occupancy ratios in Tokyo – albeit still generally on a high level.

Aareal Bank Group originated new business of € 0.1 billion in Asia during the second quarter, bringing the total figure for the first half to € 0.2 billion – compared to only minor new business in the same period of the previous year.

## Consulting/Services segment

### Bank division Housing Industry

Business development in the German housing and commercial property industries continued to be stable during the first half of 2016. This was evidenced in particular by largely constant rental income and long-term financing structures.

The industry is considered to be the engine for the development of towns and city quarters in Germany. Accordingly, companies continued to pursue a sustainable development of their portfolios during the course of the year to date, as well as improving energy efficiency.

Given growing demand for social housing – especially in conurbations and university cities – commercial housing enterprises continue to focus their investments on creating affordable housing space. The German Federal government has provided additional funds in the amount of € 800 million to promote the construction of social housing.

The stable development on the residential property market in Germany remained intact during the year to date, even though the development of rents lost some of its momentum. Rents offered in April across Germany were around 1.9 % higher than in the second quarter of 2015. Due to high price levels and the lack of supply in economically strong metropolitan areas, second-tier locations benefited from rising demand in particular. Rents for new-built properties in rural districts (Landkreise) were up by approximately 2.7% year-on-year.

Our clients from the housing and property sectors – and from the utilities and waste disposal industries – continue to make strong use of the combination of our specialist services in conjunction with automated mass electronic payments processing. They also use the related advice we offer, as well as the Bank's cash investment schemes. This enables us to maintain a strong position in the market, despite strong competitive pressure – which is also reflected in the acquisition of new clients: during the second quarter of 2016, we were able to win new business partners from the housing industry, managing more than 50,000 residential units between them.

The volume of deposits taken remained high, averaging € 9.5 billion during the quarter under review (Q1 2016: € 9.3 billion). Deposits averaged

€ 9.4 billion during the period under review (H1 2015: € 9.2 billion).

At the same time, the persistently low interest rate environment in the quarter under review burdened income generated from the deposit-taking business, and therefore the segment result. Yet the importance of the deposit-taking business in the Consulting/Services segment goes far beyond the interest margin generated from the deposits – which is under pressure in the current market environment. For Aareal Bank, deposits from the housing industry are a strategically important additional source of funding for the lending business, and one that is largely independent of capital markets developments. In addition to the German Pfandbrief and unsecured bank bonds, they represent an important pillar in the Bank's long-term funding mix.

### Aareon

Aareon's contribution to consolidated operating profit amounted to € 15 million during the first half of the year (H1 2015: € 11 million).

#### Germany

Aareon held the 26th Aareon Congress in Garmisch-Partenkirchen in June, under the motto: "Time for change – change as a success factor". The event is a meeting point for the German property industry. Change brought about by digitalisation, globalisation, demographic trends, and migration has an impact on business and society – yet it also offers numerous opportunities. Housing enterprises may seize upon the opportunities of digitalisation as a success factor for the future. In this context, digital solutions respond to changing tenant needs, the future of housing, as well as energy issues. Following the inaugural presentation of Aareon Smart World in the previous year, this year's edition of the Aareon Congress focused on the latest trends and developments, as well as on practical case studies. The Aareon DesignLab was another new development showcased at the Congress. "Design thinking", a structured process for the development of new, digital and – above all – user-oriented solutions deeply involves customers in a creative development approach.

In Germany, Aareon distributes the Wodis Sigma ERP solutions, SAP® solutions and Blue Eagle. Additional Aareon customers opted for Wodis Sigma during the second quarter, including many GES customers who decided to change within the scope of our migration campaign. As expected, the favoured version is the one that uses Wodis Sigma as a service from the exclusive Aareon Cloud. Aareon is implementing a large number of migration projects, which are developing on schedule.

The licensing business for SAP® solutions and Blue Eagle has been developing very positively indeed, especially due to additional licenses sold to a large account, as well as through the acquisition of new customers.

Customer interest was particularly pronounced regarding Mobile Services: Aareon has been successful in winning more than 100 companies for this offer. The new digital solution Aareon Smart World Cockpit (previously Aareon 360°) was presented in Germany at the Aareon Congress for the first time. Aareon's customers in the UK have been using this mobile full-service solution for the field staff of housing enterprises for some time.

Business involving Aareon Smart World digital solutions – including the Mareon service portal, Aareon Archiv kompakt, Aareon CRM, and Aareon Immoblue Plus – performed as planned. These solutions also benefit from migrations of ERP solutions.

BauSecura's insurance business developed favourably during the first six months of the year.

Integration of phi-Consulting GmbH, which Aareon acquired effective 1 October 2015 in order to expand its business activities onto the energy sector, is progressing on schedule and is expected to be completed in 2016.

#### International Business

Demand for Aareon Smart World digital solutions was evident in the Netherlands, involving the Mareon service portal, Aareon Archiv kompakt, Aareon CRM, as well as the Treasury solution:

for example, de Alliante, Huizen (Netherlands), managing 64,000 units, was a large customer opting for Mareon. Moreover, the Tobias AX ERP system was rolled out for several customers. Integration of Square DMS B.V. (formerly Square DMS Groep B.V.), which was acquired with effect from 1 October 2015, has been progressing on schedule, strengthening our market position.

Aareon France is supporting several customers with the realisation of Aareon Smart World digital solutions. Demand is focused particularly on the tenant portals, as well as on billing services and mobile property inspection. A development worth noting was the roll-out of Aareon France's billing service to Marseille-based Erilia, a major account managing 89,000 residential units. Aareon France's annual customer congress took place in May; the event also focused on digitalisation and the associated opportunities.

In the UK, Aareon UK took part in several calls for tender, winning most of them and thus boosting new customer business. Looking at digitalisation, the UK market has already reached a high degree of maturity, especially regarding mobile solutions. Aareon's 1st Touch subsidiary is providing new impulses in this respect, through the Aareon Smart World Cockpit and the tenant portal. These solutions attract significant customer interest, which led to additional contracts being closed. The UK housing market is undergoing fundamental change: housing assocations will have to reduce social housing rents by one per cent each year until 2020. As a consequence, housing enterprises are forced to enhance their efficiency, for example, by optimising business processes. This offers sales potential for ERP and digital solutions. Business development in the UK has been stable in the wake of Brexit: since Aareon's UK subsidiaries service customers in the UK, Brexit is not expected to have a direct impact upon business volumes.

Swedish Incit AB Group has won further new customers for its Incit Xpand ERP solution, including a major hotel group in Scandinavia. A campaign designed to win new customers for Incit Xpand Smart Start – a pre-configured template which simplifies our customers' data migration to Incit Xpand – has been running successfully.

## Financial Position and Financial Performance

### Financial performance

#### Group

In the first six months of the financial year, consolidated operating profit amounted to € 207 million and was thus considerably higher than in the corresponding period of the previous year (€ 146 million, adjusted for negative goodwill of € 150 million resulting from the acquisition of WestImmo).

Net interest income totalled € 357 million, which represents a slight reduction over the previous year (€ 369 million), due particularly to lower early loan repayments. The increase in lending volume – due to the acquisition of WestImmo – was largely offset by the planned reduction of non-strategic portfolios.

Allowance for credit losses amounted to € 31 million (H1 2015: € 49 million) and was thus in line with our expectations. Net additions to specific allowance for credit losses contributed € 21 million, while net additions to portfolio-based allowance for credit losses amounted to € 11 million.

Net commission income increased to € 93 million (H1 2015: € 83 million), which was mainly due to higher sales revenue at Aareon.

The aggregate of net trading income/expenses and the net result on hedge accounting of € 18 million (H1 2015: € 3 million) resulted largely from the measurement and close-out of derivatives used to hedge interest rate and currency risk. The net result from non-trading assets amounted to € 61 million (H1 2015: € -2 million) and was due to the disposal of all shares in Aareal Bank's wholly-owned subsidiary, Aqvatrium, as announced on 8 December 2015. Aqvatrium is the owner of a commercial property located in Stockholm.

**Consolidated net income of Aareal Bank Group[1)]**

| € mn | 1 Jan-30 Jun 2016 | 1 Jan-30 Jun 2015 |
|---|---|---|
| Net interest income | 357 | 369 |
| Allowance for credit losses | 31 | 49 |
| **Net interest income after allowance for credit losses** | **326** | **320** |
| Net commission income | 93 | 83 |
| Net result on hedge accounting | 1 | 8 |
| Net trading income/expenses | 17 | -5 |
| Results from non-trading assets | 61 | -2 |
| Results from investments accounted for using the equity method | 0 | 0 |
| Administrative expenses | 290 | 268 |
| Net other operating income/expenses | -1 | 10 |
| Negative goodwill from acquisitions | – | 150 |
| **Operating profit** | **207** | **296** |
| Income taxes | 65 | 46 |
| **Consolidated net income** | **142** | **250** |
| Consolidated net income attributable to non-controlling interests | 10 | 10 |
| Consolidated net income attributable to shareholders of Aareal Bank AG | 132 | 240 |

At € 290 million (H1 2015: € 268 million), administrative expenses exceeded the level of the corresponding previous year's period, as expected. The increase was due particularly to running costs for WestImmo as well as integration costs.

Net other operating income/expenses amounted to € -1 million (H1 2015: € 10 million).

Second-quarter consolidated operating profit thus stood at € 207 million (H1 2015: € 296 million). Taking into consideration tax expenses of € 65 million and non-controlling interest income of € 10 million, consolidated net income attributable to shareholders of Aareal Bank AG amounted to € 132 million (H1 2015: € 240 million). Assuming the pro rata temporis accrual of net interest payments on the AT1 bond, consolidated net income attributable to ordinary shareholders stood at € 124 million (H1 2015: € 232 million).

### Structured Property Financing segment

At € 128 million, operating profit generated in the Structured Property Financing segment during the second quarter of 2016 was clearly higher than in the corresponding period of the previous year (Q2 2015: € 86 million, adjusted for negative goodwill of € 150 million resulting from the acquisition of WestImmo).

Segment net interest income amounted to € 181 million in the second quarter of 2016, slightly down year-on-year (Q2 2015: € 192 million), which was particularly due to lower early loan repayments. The increase in lending volume – due to the acquisition of WestImmo – was largely offset by the planned reduction of non-strategic portfolios.

Allowance for credit losses amounted to € 29 million (Q2 2015: € 31 million) and was thus in line with our expectations. Net additions to specific allowance for credit losses contributed € 21 million, while net additions to portfolio-based allowance for credit losses amounted to € 6 million.

1) Adjustment of previous year's figures due to completion of purchase price allocation for WestImmo, in accordance with IFRS 3

### Structured Property Financing segment result[1)]

| € mn | Quarter 2 2016 | Quarter 2 2015 |
|---|---|---|
| Net interest income | 181 | 192 |
| Allowance for credit losses | 29 | 31 |
| **Net interest income after allowance for credit losses** | **152** | **161** |
| Net commission income | 1 | 2 |
| Net result on hedge accounting | 0 | -3 |
| Net trading income/expenses | 8 | 2 |
| Results from non-trading assets | 61 | 1 |
| Results from investments accounted for using the equity method | – | – |
| Administrative expenses | 94 | 89 |
| Net other operating income/expenses | 0 | 12 |
| Negative goodwill from acquisitions | – | 150 |
| **Operating profit** | **128** | **236** |
| Income taxes | 41 | 26 |
| **Segment result** | **87** | **210** |

The net result from non-trading assets amounted to € 61 million (Q2 2015: € 1 million) and was due to the disposal of all shares in Aareal Bank's wholly-owned subsidiary, Aqvatrium, as announced on 8 December 2015. Aqvatrium is the owner of a commercial property located in Stockholm.

At € 94 million (Q2 2015: € 89 million), the segment's administrative expenses exceeded the level of the corresponding previous year's period, as expected. The increase was due particularly to running costs for WestImmo as well as integration costs.

Overall, operating profit for the Structured Property Financing segment was € 128 million in the second quarter (Q2 2015: € 236 million). Taking tax expenses of € 41 million into consideration (Q2 2015: € 26 million), the segment result for the quarter under review was € 87 million (Q2 2015: € 210 million).

### Consulting/Services segment

Sales revenue generated in the Consulting/Services segment developed positively during the second quarter of 2016, totalling € 52 million (Q2 2015: € 47 million), driven particularly by higher sales revenue of Aareon. The persistent low interest rate environment continued to burden margins from the deposit-taking business that are reported in sales revenues.

Staff expenses of € 35 million for the quarter under review were slightly higher than in the same period of the previous year (Q2 2015: € 33 million).

Other items were unchanged from the previous year's levels.

Overall, segment operating profit in the second quarter of 2016 was € -8 million (Q2 2015: € -7 million). Aareon's contribution was € 8 million (Q2 2015: € 6 million).

After taking taxes into consideration, the segment result in the second quarter amounted to € -5 million (Q2 2015: € -5 million).

[1)] Adjustment of previous year's figures due to completion of purchase price allocation for WestImmo, in accordance with IFRS 3

### Consulting/Services segment result

| € mn | Quarter 2 2016 | Quarter 2 2015 |
|---|---|---|
| Sales revenue | 52 | 47 |
| Own work capitalised | 2 | 1 |
| Changes in inventory | 0 | 0 |
| Other operating income | 0 | 2 |
| Cost of materials purchased | 9 | 7 |
| Staff expenses | 35 | 33 |
| Depreciation, amortisation and impairment losses | 3 | 3 |
| Results from investments accounted for using the equity method | 0 | 0 |
| Other operating expenses | 15 | 14 |
| Interest and similar income/expenses | 0 | 0 |
| **Operating profit** | **-8** | **-7** |
| Income taxes | -3 | -2 |
| **Segment result** | **-5** | **-5** |

## Financial position

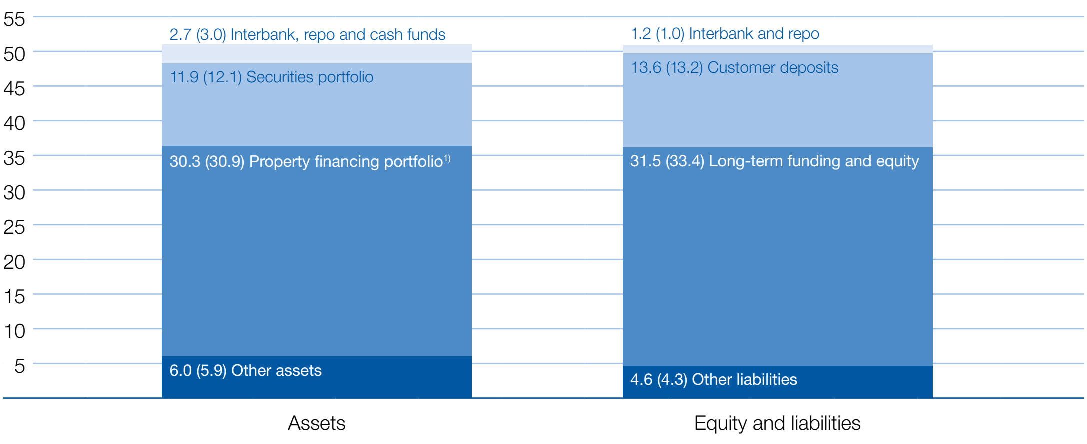
Aareal Bank Group's consolidated total assets amounted to € 50.9 billion as at 30 June 2016, after € 51.9 billion as at 31 December 2015.

### Property financing portfolio

The volume of Aareal Bank Group's property financing portfolio[1)] stood at € 30.3 billion as at 30 June 2016, a decline of approximately 2 % compared to the 2015 year-end figure of € 30.9 billion.

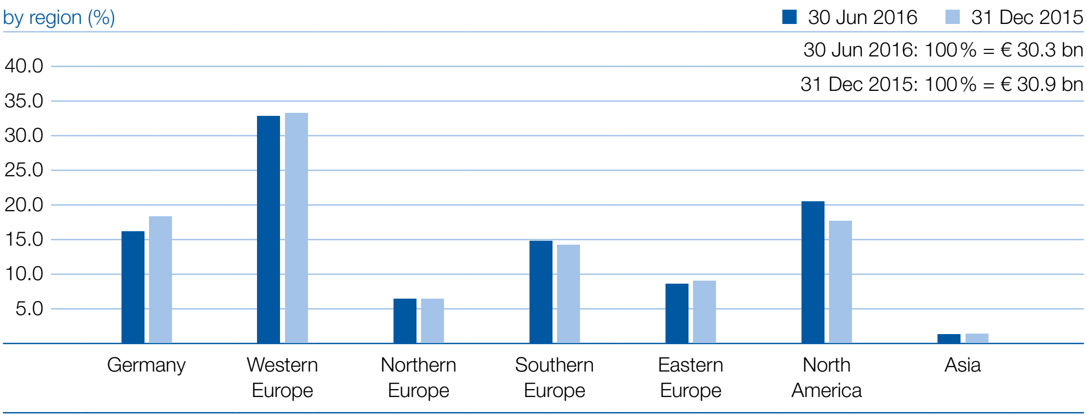
### Statement of financial position – structure as at 30 Jun 2016 (31 Dec 2015)

€ bn

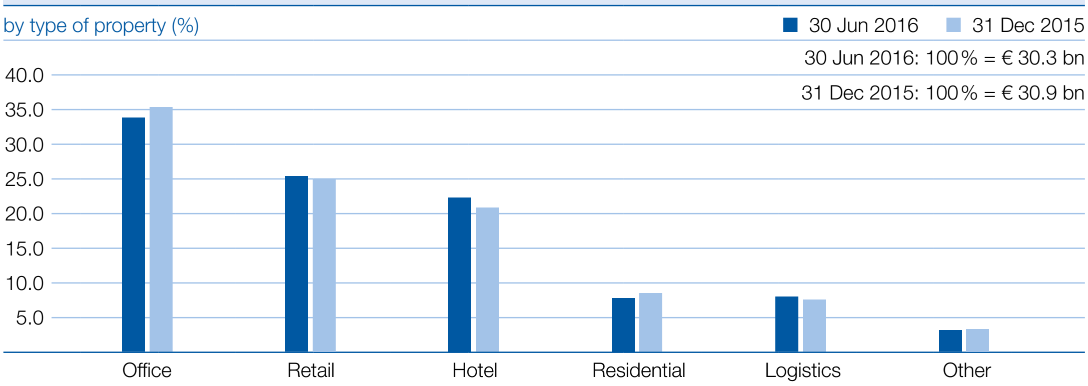



[1)] Excluding € 1.3 billion in private client business (31 December 2015: € 1.5 billion) and € 0.6 billion in local authority lending business by WestImmo (31 December 2015: € 0.6 billion)

**Property financing volume[1] (amounts drawn)**




**Property financing volume[1] (amounts drawn)**




[1] Excluding € 1.3 billion in private client business (31 December 2015: € 1.5 billion) and € 0.6 billion in local authority lending business by WestImmo (31 December 2015: € 0.6 billion)

This development was largely attributable to the planned reduction of non-strategic portfolios and exchange rate fluctuations. The international share of the portfolio increased slightly to 83.9 % (31 December 2015: 81.7 %).

At the reporting date (30 June 2016), Aareal Bank Group's property financing portfolio was composed as shown in the charts on the following page, compared with year-end 2015.

The allocation of the portfolio by region and continent changed only marginally compared with the end of the previous year. Whilst the portfolio share of exposures in North America rose slightly (+2.8 %) in line with our strategy, it declined in Germany (-2.2 %). However, it remained almost stable for all other regions.

The breakdown of the portfolio by property type did not change significantly during the reporting period. The share of financings for office properties declined slowly (-1.5 %), while the share of hotel properties increased by 1.5 %. The share of financings for residential, logistics, and retail property as well as other financings remained almost unchanged compared to the year-end 2015.

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

### Securities portfolio

As at 30 June 2016, the nominal volume of the securities portfolio[1] was € 9.6 billion (31 December 2015: € 10.2 billion). It comprises four asset classes: public-sector borrowers, covered bonds and Pfandbriefe, bank bonds and asset-backed securities (ABS). 98 %[2] of the overall portfolio is denominated in euro. 98 %[2] of the portfolio has an investment grade rating.[3] More than 70 % of the portfolio fulfils the requirements of "High Quality Liquid Assets" (as defined by the CRR) in the Liquidity Coverage Ratio (LCR).

## Financial position

### Funding and equity

#### Funding

Aareal Bank Group has remained very solidly funded throughout the first half of 2016. Total long-term funding as at 30 June 2016 amounted to € 29.0 billion (31 December 2015: € 30.9 billion), comprising Pfandbrief issues as well as senior unsecured and subordinated issues. As at the reporting date, Aareal Bank also had € 8.8 billion at its disposal from deposits generated from the business with the housing industry (31 December 2015: € 8.4 billion). Institutional money market investors' deposits amounted to € 4.8 billion (31 December 2015: € 4.8 billion).

Aareal Bank Group raised € 0.9 billion on the capital market during the first half of 2016, comprising € 0.8 billion in senior unsecured, and € 0.1 billion in secured issues. One of the highlights was the increase of an existing senior unsecured bond by € 150 million in March 2016, to reach a benchmark volume of € 500 million.

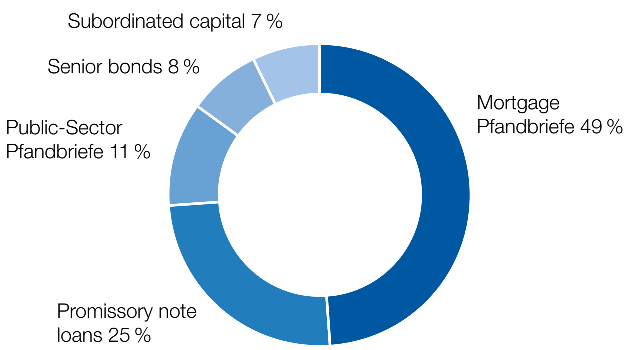
Since we conduct our business activities in a range of foreign currencies, we have secured our foreign currency liquidity over the longer term by means of appropriate measures.

#### Equity

Aareal Bank Group's total equity as disclosed in the statement of financial position amounted to € 3,025 million as at 30 June 2016 (31 December 2015: € 3,044 million), comprising € 300 million in the Additional Tier 1 (AT1) bond and € 242 million in non-controlling interests.

**Capital market funding mix as at 30 June 2016**

% Total volume: € 29.0 bn




### Regulatory capital

| | 30 Jun 2016 | 31 Dec 2015 |
|---|---|---|
| € mn | | |
| Common Equity Tier 1 (CET1) | 2,236 | 2,298 |
| Tier 1 capital (T1) | 2,762 | 2,882 |
| Total capital (TC) | 3,879 | 3,977 |
| % | | |
| Common Equity Tier 1 ratio (CET1 ratio) | 13.7 | 13.8 |
| Tier 1 ratio (T1 ratio) | 16.9 | 17.2 |
| Total capital ratio (TC ratio) | 23.8 | 23.8 |

The regulatory measurement of risk-weighted assets (RWAs) in the area of credit risks is based on both the Advanced Internal Ratings Based Approach (AIRBA) and on the standardised approach (CRSA).

[1] As at 30 June 2016, the securities portfolio was carried at € 11.9 billion (31 December 2015: € 12.1 billion).
[2] Details based on the nominal volume
[3] The rating details are based on the composite ratings.

### Analysis of risk-weighted assets (RWA)

**30 June 2016**

| € mn | EAD | Risk-weighted assets (RWA) | | | Regulatory capital requirements |
|---|---|---|---|---|---|
| | | AIRBA | CRSA | Total | |
| **Credit risks** | **52,002** | **10,733** | **3,427** | **14,160** | **1,133** |
| Companies | 32,724 | 8,699 | 2,136 | 10,835 | 867 |
| Institutions | 4,598 | 547 | 99 | 646 | 52 |
| Public-sector entities | 12,458 | 0 | 21 | 21 | 2 |
| Other | 2,222 | 1,487 | 1,171 | 2,658 | 212 |
| **Market price risks** | | | | **156** | **12** |
| **Credit Valuation Adjustment** | | | | **311** | **25** |
| **Operational risks** | | | | **1,681** | **135** |
| **Total** | **52,002** | **10,733** | **3,427** | **16,308** | **1,305** |

**31 December 2015**

| € mn | EAD | Risk-weighted assets (RWA) | | | Regulatory capital requirements |
|---|---|---|---|---|---|
| | | AIRBA | CRSA | Total | |
| **Credit risks** | **53,053** | **10,629** | **4,029** | **14,658** | **1,173** |
| Companies | 33,463 | 8,481 | 2,647 | 11,128 | 890 |
| Institutions | 4,455 | 462 | 101 | 563 | 45 |
| Public-sector entities | 12,507 | 0 | 20 | 20 | 2 |
| Other | 2,628 | 1,686 | 1,261 | 2,947 | 236 |
| **Market price risks** | | | | **124** | **10** |
| **Credit Valuation Adjustment** | | | | **264** | **21** |
| **Operational risks** | | | | **1,663** | **133** |
| **Total** | **53,053** | **10,629** | **4,029** | **16,709** | **1,337** |

## Events after the Reporting Date

There have been no material events subsequent to the end of the interim reporting period under review that need to be disclosed at this point.

## Risk Report

### Aareal Bank Group Risk Management

The Annual Report 2015 contains a comprehensive description of Aareal Bank Group's risk management approach, including the corresponding organisational structure and workflows in the lending and trading businesses, as well as the methods and procedures used for measuring and monitoring risk exposure. Within the scope of this interim report, we will once again briefly outline the key components of our risk management structure, together with the key developments during the period under review. The business policy set by the Management Board, and duly acknowledged by the Supervisory Board, provides the conceptual framework for Aareal Bank Group's risk management. Taking this as a basis, and strictly considering the Bank's risk-bearing capacity, we have formulated detailed strategies for managing the various types of risk. These risk strategies, as well as the Bank's business strategy, are adapted to the changed environment at least once a year, adopted by the Management Board, and duly acknowledged by the Supervisory Board. Suitable risk management and risk control processes are deployed to implement the risk strategies, and to ascertain the Bank's ability to bear risk.

### Risk-bearing capacity and risk limits

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

In accordance with this approach, potential risk cover is determined using data derived from the income statement and from the statement of financial position; this derivation also forms the basis for determining regulatory capital. This involves setting aside the maximum amount of own funds required as potential risk cover to offset risks without causing a breach of minimum requirements pursuant to the Capital Requirements Regulation (CRR). Aareal Bank has decided to considerably exceed this minimum requirement, and to prudently apply a Tier I ratio (calculated in accordance with the CRR) equivalent to 8 % of forecast risk-weighted assets (RWA), plus buffer. Only free own funds exceeding this level are applied as potential risk cover, of which a further minimum of 10 % (currently 11 %) is retained as a risk cushion. This cushion is not applied to risk limits, and is thus available for risk types that cannot be quantified (for example, reputational or strategic risks).

We adopt an equally conservative stance with respect to setting risk limits. The aggregation of individual limits is based on the assumption that no risk-mitigating correlation effects exist amongst different types of risk. Taking into account the prior deduction of a minimum Tier I ratio of 8 % of RWA, the value-at-risk models used to quantify

**Risk-bearing capacity of Aareal Bank Group as at 30 June 2016**
**– Going-concern approach –**

| € mn | 30 Jun 2016 | 31 Dec 2015 |
|---|---|---|
| Own funds for risk cover potential | 2,598 | 2,937 |
| less 8 % of RWA (Tier 1 capital (T1)) | 1,477 | 1,606 |
| **Freely available funds** | **1,121** | **1,331** |
| **Utilisation of freely available funds** | | |
| Credit risks | 295 | 313 |
| Market risks | 239 | 244 |
| Operational risks | 101 | 100 |
| Investment risks | 60 | 65 |
| **Total utilisation** | **694** | **721** |
| **Utilisation as a percentage of freely available funds** | **62 %** | **54 %** |

risks are based on a confidence interval of 95 % and a one-year holding period (250 trading days). A monthly report submitted to the Management Board provides information regarding the utilisation of individual limits for the material types of risk, as well as on the overall limit utilisation. The table on page 20 summarises the Group's overall risk-bearing capacity as at 30 June 2016.

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

## Credit risks

### Definition

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

### Risk measurement and monitoring

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

Processes in the credit and trading businesses are designed to consistently respect the clear functional division of Sales units ("Markt") and Credit Management ("Marktfolge"), up to and including senior management level. The independent Risk Controlling division is responsible for identifying, quantifying and monitoring all material risks at portfolio level, and for maintaining a targeted risk reporting system.

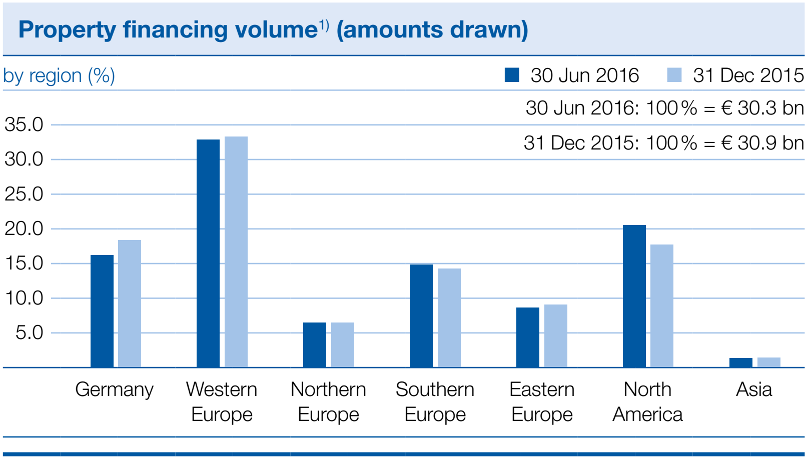
Aareal Bank employs various risk classification procedures for the initial, regular, or event-driven assessment of counterparty credit risk; these procedures are adapted specifically to meet the requirements of the relevant business activity and are subject to permanent review and improvement. Responsibility for development, quality assurance, and monitoring implementation of risk classification procedures, is outside the Sales units.

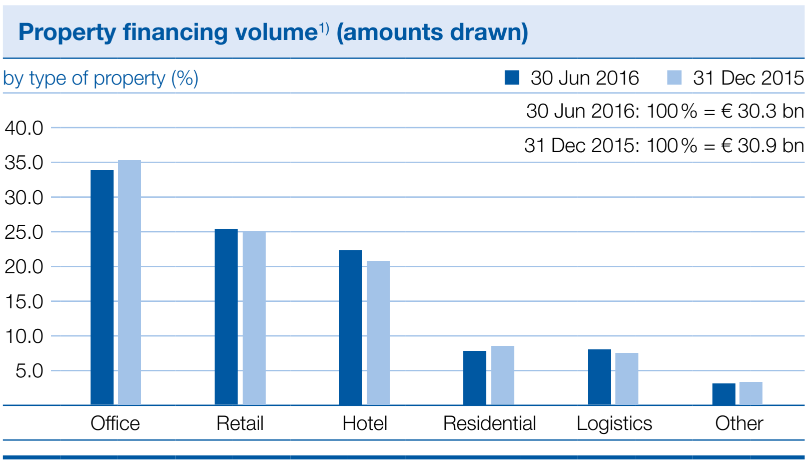
Methods used to measure, control and monitor concentration and diversification effects on a portfolio level include two different credit risk models. Based on these models, the Bank's decision-makers are regularly informed of the performance and risk content of property financing exposures, and of business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

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 credit risk report that complies with the Minimum Requirements for Risk Management (MaRisk) is prepared and submitted to the Bank's Management Board and Supervisory Board on a regular basis, at least quarterly. This report contains extensive information on the development of the credit portfolio (covering countries, types of property and product types, risk classes and categories of collateral), with a particular focus on risk concentrations.

Trading activities are generally restricted to counterparties for whom the requisite limits are in place. All trades are immediately taken into account for the purposes of borrower-related limits. Compliance with limits is monitored in real time by Risk Controlling. Persons holding position responsibility are




[1)] Excluding € 1.3 billion in private client business (31 December 2015: € 1.5 billion) and € 0.6 billion in local authority lending business by WestImmo (31 December 2015: € 0.6 billion)

informed about relevant limits and their current usage, regularly and without delay.

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.

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

### Country risks

Our comprehensive approach to risk management also includes measuring and monitoring country risk exposure. When defining country risk, in addition to the risk of sovereign default or default of state entities, Aareal Bank also considers the risk that a counterparty could become unable to meet its payment obligations as a result of government action, despite being willing and able to pay, due to restrictions being imposed on making payments to creditors (transfer risk). Country risk exposure is managed using a cross-divisional process. The respective country limits are determined on the basis of a country risk assessment by the Bank's senior management. The Risk Controlling division is responsible for the continuous monitoring of country limits and limit utilisation, and for periodical reporting.

### Market price risks

#### Definition

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

Derivative financial instruments are primarily used as hedging instruments. Spread risks between the various yield curves (e.g. government, Pfandbrief and swap curves) are taken into account. The risk exposure from bonds that is not related to market price or interest rate risks is managed as part of "specific risk", in particular, credit and liquidity risk exposure of the bond portfolio.

## 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 indicates the potential loss incurred before countermeasures 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, the VaR figure takes into account the correlation between individual risk types. Statistical parameters used in the VaR model are calculated directly from a 250-day historical data pool maintained within the Bank. The loss potential is determined applying a 95% confidence interval and a 250-day holding period.

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

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.

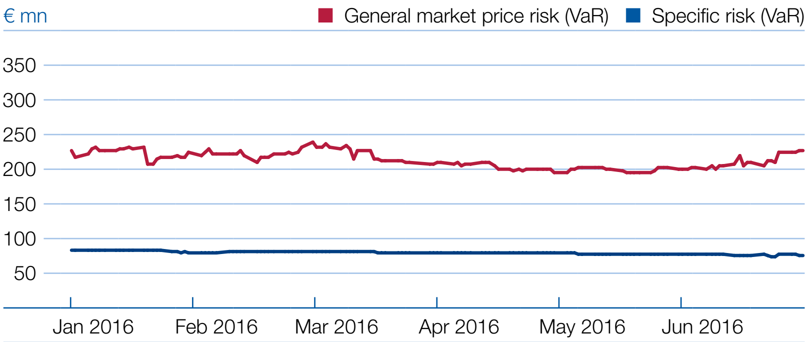
When interpreting the VaR figures stated below, it should be taken into account that these refer to the overall portfolio (thus including all non-trading positions as defined in IFRSs). Hence, the analysis provided represents a very extensive disclosure of market price risks by industry standards.

| € mn | MAX | MIN | Mean | Limit |
|---|---|---|---|---|
| **Year-to-date (full previous year) 95%, 250-day holding period** | | | | |
| Aareal Bank Group – general market price risk | 242.6 (422.3) | 193.2 (187.5) | 213.4 (263.3) | – (–) |
| Group VaR (interest rates) | 184.3 (404.4) | 128.9 (119.5) | 146.9 (216.5) | – (–) |
| Group VaR (FX) | 146.6 (170.5) | 103.5 (61.0) | 120.9 (114.7) | – (–) |
| VaR (funds) | 5.2 (4.7) | 3.5 (2.8) | 4.6 (3.7) | 20.0 (20.0) |
| Aggregate VaR in the trading book (incl. specific VaR) | 0.0 (0.0) | 0.0 (0.0) | 0.0 (0.0) | 5.0 (5.0) |
| Trading book VaR (interest rates) | 0.0 (0.0) | 0.0 (0.0) | 0.0 (0.0) | – (–) |
| Trading book VaR (FX) | 0.0 (0.0) | 0.0 (0.0) | 0.0 (0.0) | – (–) |
| VaR (equities) | 0.0 (0.0) | 0.0 (0.0) | 0.0 (0.0) | – (–) |
| Group VaR (specific risks) | 85.9 (92.0) | 72.8 (72.3) | 80.6 (83.8) | – (–) |
| Aggregate VaR – Aareal Bank Group | 256.2 (428.7) | 208.4 (207.5) | 228.1 (277.4) | 390.0 (435.0) |

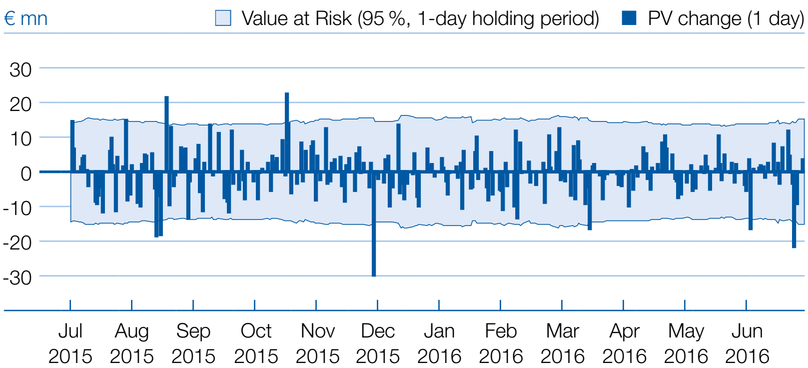
To ensure that Aareal Bank's figures are comparable to those published by other institutions, the risk parameters shown below were determined for a one-day holding period:

| € mn | MAX | MIN | Mean | Limit |
|---|---|---|---|---|
| **Year-to-date (full previous year) 95 %, 1-day holding period** | | | | |
| Aareal Bank Group – general market price risk | 15.3 (26.7) | 12.2 (11.9) | 13.5 (16.7) | – (–) |
| Group VaR (interest rates) | 11.7 (25.6) | 8.2 (7.6) | 9.3 (13.7) | – (–) |
| Group VaR (FX) | 9.3 (10.8) | 6.5 (3.9) | 7.6 (7.3) | – (–) |
| VaR (funds) | 0.3 (0.3) | 0.2 (0.2) | 0.3 (0.2) | 1.3 (1.3) |
| Aggregate VaR in the trading book (incl. specific VaR) | 0.0 (0.0) | 0.0 (0.0) | 0.0 (0.0) | 0.3 (0.3) |
| Trading book VaR (interest rates) | 0.0 (0.0) | 0.0 (0.0) | 0.0 (0.0) | – (–) |
| Trading book VaR (FX) | 0.0 (0.0) | 0.0 (0.0) | 0.0 (0.0) | – (–) |
| VaR (equities) | 0.0 (0.0) | 0.0 (0.0) | 0.0 (0.0) | – (–) |
| Group VaR (specific risks) | 5.4 (5.8) | 4.6 (4.6) | 5.1 (5.3) | – (–) |
| Aggregate VaR – Aareal Bank Group | 16.2 (27.1) | 13.2 (13.1) | 14.4 (17.5) | 24.7 (27.5) |

**General market price risk and specific risk during 2016**




**Present values and 1-day VaR during the course of 2015/2016**




### Aggregate VaR – Aareal Bank Group

Group-wide limits are being continuously monitored as part of the analysis of the Bank's risk-bearing capacity. These limits were adjusted in line withe the updated risk-bearing capacity during the quarter under review; no limit breaches were detected.

### Backtesting

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 (≤ 17 for a 250-day period). Six negative outliers at Group level occurred during the last 250 trading days, affirming the high forecasting quality of the VaR model we use.

### 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 that no such trades were concluded during the period under review, trading book risks played a negligible role in the overall risk scenario during the quarter under review.

### Liquidity risks

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

Treasury is responsible for managing liquidity risks, whilst Risk Controlling ensures the continuous monitoring, including a daily liquidity report submitted to Treasury, and a contribution to the monthly risk report to the entire Management Board.

The appropriateness of the Bank's liquidity is assessed in a liquidity report prepared using an internal liquidity risk model: the aggregate of all potential cash inflows and outflows over a three-month period is compared to the liquidity stock. There were no liquidity shortages throughout the period under review. Further details are provided in the comments on the Bank's liquidity in the section on "Funding and equity".

### Operational risks

The Bank defines operational risk as the threat of losses caused by inappropriate internal procedures, human resources and systems (or their failure), or through external events. This definition also includes legal risks and model risks. Aareal Bank's legal department (Corporate Development – Legal) compiles all information concerning any legal disputes involving Aareal Bank Group, whether in or out of court. The involvement of the legal department is based on corresponding Group-wide guidelines. The Bank's decentralised operating legal entities, as well as the legal departments of subsidiaries submit quarterly as well as event-driven reports on legal risks identified to Aareal Bank's legal department, which reports to the Management Board, also (at least) on a quarterly basis. Moreover, information about legal risks is included in operational risk reporting. Strategic, reputational and systematic risks are not covered by operational risk management. These risks are managed largely through qualitative measures.

Aareal Bank's policy for managing and monitoring operational risks is geared to achieving a risk-minimising or loss-limiting effect at an early stage, by employing a pro-active approach. The Risk Report in the 2015 Annual Report contains a detailed description of controlling tools employed by the Bank to manage operational risk, plus the relevant responsibilities.

The current analysis conducted using these control instruments has shown that the Bank is not exposed to disproportionate operational risks; nor did it indicate any material risk concentration.

Operational risk management also includes the reporting to the Bank's Management Board about outsourced activities and processes.

### Investment risks

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

Due to the special character of some exposures (e.g. marketing risks), special methods and procedures are employed to deal with investment risk. All relevant Group entities are subject to regular audits, including a review and assessment of their risk situation. A quarterly investment risk report is submitted to the Bank's Management Board. There were no significant changes in investment risk during the period under review.

## Report on Expected Developments

### Macro-economic environment

Further developments for the economy, as well as for financial and capital markets are exposed to significant risks and threats – which also have an impact on the commercial property markets. At the mid-year point in 2016, the economic forecast is characterised by significant uncertainty.

The current low-interest rate environment and an expansive monetary policy pose particular risks as market participants might be induced to seek higher risk exposure, thereby increasing the risk of capital misallocation and exaggerated asset prices. This may result in prices and values sharply declining, should the need for asset revaluations arise or if interest rates rise swiftly. Low interest rates may also encourage a reduction of reform and consolidation efforts.

An interest rate turnaround, however, also carries risks, including investments being postponed, pressure on assets rising, or capital outflows, particularly in emerging economies. For the US, financial markets have been expecting rising interest rates for quite some time. The Federal Reserve's decision to lift its key interest rate in December 2015 was a first step in that direction. However, the scope for 2016 – and corresponding financial markets volatility – remains uncertain. Turmoil in the financial and capital markets may still hurt the global economy.

Further divergence between US and euro zone monetary policies may result in a resurgence of the European sovereign debt crisis – or distortions that could burden the financial and capital markets and the economy. With a potential splitting of the UK, a new uncertainty and risk factor has materialised, following the British people's 23 June vote in favour of leaving the EU. Doubts about European solidarity have also increased, possibly leading to rising volatility in the financial and capital markets. Another important aspect is the refugee crisis and how it is to be overcome. Geopolitical risks, such as the crisis in Ukraine, tensions within Turkey, or the fear of growing terrorism, may also evoke uncertainty and burden economic activity, at least regionally.

Further uncertainty factors and burdens include a reform backlog, and structural economic issues in certain countries across the euro zone. In particular, this includes the high pressure that non-performing loans are placing on Italian banks. Doubts concerning the stability of Italian banks and solutions that fail to materialise may weigh heavily on the European banking sector.

China also poses major risks to the world economy and the financial and capital markets, due to excessive levels of macro-economic debt – which has risen strongly in the recent past – and the marked volatility in the residential property markets seen in the past. Also, the structural change in China will continue to affect the global economy.

### Economy

Against the high number of existing uncertainty factors and burdens, economic momentum is expected to remain low during 2016. Growth rates of real economic performance should be slightly below the levels seen during 2015, and below the long-term average. Risks and uncertainty factors could, were they to materialise to a substantial extent, further mute the economic development, or even cause recessive tendencies in certain regions.

Compared to the previous year, the modest growth rate confirmed the euro zone's solid economic recovery in the first six months. For the full year, we currently expect a stable economic development in Europe. Private consumption should continue to bolster the economy; investments are bound to continue to rise. Better labour market data should offset the negative effects resulting from the increase in oil prices. This positive market sentiment, however, could be dampened by the pending Brexit. For Germany and France, we currently expect economic performance to post a slight rise on the previous year, but the risk of a setback due to uncertainties following the British vote remains high.

In national economies in the EU which are not part of the euro zone, we expect to see a slightly stronger growth rate than in euro member states this year, although the pending Brexit has increased the risk of an economic slump. In Sweden, economic growth is robust, although growth rates should fall slightly from last year's figures. The referendum in the UK about its EU membership marked the start of a multi-year period of uncertainty, especially amongst investors. We expect that economic momentum in the United Kingdom will experience a decline in investments, and possibly also in private consumption. For longer-term development, we need to wait and see what the Brexit negotiations produce in the next two years. The Polish economy should continue its strong growth in the current year, albeit at levels below those registered in the previous year. The Swiss economy remains burdened by the strong Swiss franc. Thus, the real gross domestic product will only increase slowly – as already seen in the previous year. For Turkey, we anticipate a continued economic growth, albeit at a moderate rate below the level achieved in 2015. Moreover, tensions within the country may burden the economy through uncertainty amongst economic actors. Russia will remain in recession for the time being, with another moderate decline in real gross domestic product this year. The slight rise in oil prices, however, should have a positive effect here. Overall, geopolitical risks as well as muted global trade have triggered downside risks.

Growth in the US economy continues to be intact and is expected to receive support especially from private consumption (which benefits from increases in wages) this year. Employment growth, however, will slow down. Corporate investments should also make a major contribution; in our scenario, they would hardly be affected by further interest rate hikes on the part of the Federal Reserve. In light of a weaker first quarter for 2016, more restrained investments caused by low oil prices and decreasing exports due to a strong dollar, we expect a positive growth rate for the full year, albeit markedly below the previous year's level. The Canadian economy is strongly influenced by low oil prices and wildfires. Increases in private consumption are only beginning to offset the cutback in corporate investment. The economy might be supported by fiscal policies, though. Against this background, we expect only a slight increase in real economic growth for Canada, compared to last year's figure.

The Japanese economy should continue to lack momentum this year, with an almost stagnating economic output. Private consumption remains weak, and particularly the strong yen continues to pose risks. In Singapore, we anticipate an economic growth rate at the previous year's level. In China, the trend of decreasing real GDP growth is bound to continue, albeit at a more moderate level than in 2015. Curbing factors are the slowdown in the housing boom, the targeted reduction of over-capacity, especially in heavy industry, and the transition to an overall lower investment ratio. We are also witnessing uncertainties with regard to the increase of macro-economic debt. Low commodity prices have weighed on the economy in many emerging countries year-to-date (and will continue to do so during the remainder of the year), where some of these countries are also burdened by structural economic problems, adding to the factors restraining global economic growth in 2016.

Against a background of moderate, yet positive economic development, we expect labour markets across the euro zone, but also in other European countries to register slowly decreasing or virtually stagnating unemployment rates in 2016. In the US, unemployment should remain at low levels.

### Financial and capital markets, monetary policy and inflation

The risks and uncertainty factors we have listed so far also apply to the financial and capital markets. In this connection, we see the low interest rate environment and the Fed's departure from its zero interest rate policy as particularly noteworthy, but also any of the aforementioned risks could, were they to materialise to a substantial extent, cause turbulences on the financial and capital markets. In the current environment, we assume volatility to remain high. However, we expect the financial and capital markets to remain receptive for securities issues and refinancings.

The ECB's decision to expand its quantitative easing measures underscores our expectations for a continuation of the extremely expansive monetary policy pursued in the euro zone; it cannot be ruled out that the ECB will reinforce that stance during the remainder of the year. Various other European central banks, such as Sweden's Riksbank, are also likely to abide by their expansive fiscal policy during 2016. The US, however, is slowly turning its back on an expansive monetary policy, with December 2015 seeing a first hike in its key interest rate. We see further cautious increases during the course of the year as less likely. The referendum will determine the UK's monetary policy stance going forward. Against this background, there is some likelihood that the Bank of England will take monetary easing measures (such as lowering its key interest rate) during the remainder of the year.

As the referendum on the UK's exit from the EU will most likely defer interest rate hikes in the US into the next year, interest rate levels in the US are expected to remain low as well. The extremely expansive stance on monetary policy currently pursued by the ECB should result in only mild upside pressure to interest rate levels, which is why we expect interest rates to remain low for the remainder of the year.

In spite of slightly higher oil prices, inflationary pressures should remain moderate in the euro zone and other EU member states in the months to come. In fact we may even see temporary deflation in some economies. For the full year 2016, we expect inflation in the euro zone and numerous other EU countries to be minimal to marginal. For the US, we expect the annual average of inflation to be low, and assume a value around zero per cent for Japan. The risk of a deep, permanent deflation in developed economies is rather small, notwithstanding an accelerated development of wages in various countries such as the UK and the US and slightly rising oil prices during the second quarter. China is not expected to differ too much from the picture we have painted for the various regions, with a slight to moderate rate of inflation.

### Regulatory environment

The trend towards a tighter regulatory framework in the banking business is set to persist during the coming years. Numerous initiatives from the Basel Committee on Banking Supervision – such as the revision of the Credit Risk Standard Approach and the basic approaches for operational risk, the capital floor rules or the handling of interest rate risk exposure in the banking book – are currently being discussed, or are in a consultation process. In addition, the European Banking Authority (EBA) published a consultation paper on the future of the Internal Ratings Based Approach (IRBA); the paper discusses various methodological points and aims at harmonising the supervisory assessment methodology across all EU member states. EBA also consulted on its Guidelines on the collection of information related to the Internal Capital Adequacy Assessment Process (ICAAP) and the Internal Liquidity Adequacy Assessment Process (ILAAP). Finalised regulatory requirements such as the "Principles for effective risk data aggregation and risk reporting" (BCBS 239), published by the Basel Committee, are implemented through projects. On ESCB level (European System of Central Banks), the introduction of a standardised granular credit reporting system within the framework of AnaCredit (Analytical Credit Dataset) has taken shape by now. Accordingly, Aareal Bank will continue to focus on the related measures for implementation and how these will affect the Bank's business activities.

Furthermore, additional regulatory requirements of the Single Resolution Mechanism (SRM) need to be fulfilled. These include, for example, the Minimum Requirements for the Design of Recovery Plans (MaSan) on a national level, as well as the EU Bank Recovery and Resolution Directive (BRRD) at a European level. The new metrics – the Minimum Requirement for Eligible Liabilities (MREL), and Total Loss Absorbing Capacity (TLAC, according to the current state of discussion only for global institutions of systemic relevance) – that are currently being developed, also need to be applied.

Regulators have yet to come up with final details for some of these additional regulatory requirements; likewise, various technical standards, guidelines and regulations still have to be finalised, e.g. the final calibration of the Leverage Ratio. Other regulations, e.g. the fifth revision to the Minimum Requirements for Risk Management in Banks (MaRisk), are still being consulted on. To nevertheless facilitate the timely implementation, we have already continued to pursue the individual issues in numerous projects – devoting considerable resources to this task.

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

### Sector-specific and business developments

#### Structured Property Financing segment

Given the current low interest rate environment, combined with a high degree of investor liquidity, commercial property remains a sought-after investment this year, too. Global transaction volumes are therefore expected to remain high. However, quarterly results for the first and second quarter of 2016 support our expectation that the previous year's very high levels constitute a ceiling. Accordingly, transaction volumes this year might see moderate – in some markets noticeable – declines, but still remain above the long-term mean. Continued investor interest for properties outside the top segments seems likely, given the shortage of first-class properties on offer. Strong investor demand is expected to continue to support performance this year. Nonetheless, commercial property markets are also exposed to major risks and threats. One such risk lies in capital misallocation and associated potential bubble-building in commercial property markets; a fundamental revaluation here might result in abrupt declines in values. A turnaround in the US Federal Reserve's interest rate policy also poses a risk for commercial property markets, should interest rate hikes be substantial – in which case they would negatively impact demand for, and the value of commercial property. Moreover, other uncertainty factors and risks in the macro-economic environment are relevant for commercial property markets.

Commercial property – and its performance – will thus be subject to a variety of influencing factors this year. Whilst on the one hand, lively investor demand and the low interest rate environment provide support, on the other hand, commercial property investment yields have already reached very low levels which pose the risk of misallocation. Furthermore, subdued to moderate economic growth is the most likely scenario for various economies. Demand for rental space may therefore decrease.

We are assuming commercial property values to remain stable this year on average for many countries, but also anticipate slight increases for some markets. According to our assessment, most European markets – including Belgium, Finland, France, Italy, the Netherlands, and Turkey, for example – will see virtually stable performance on average. Tensions within Turkey and terrorist attacks in the country pose a risk for the ongoing development of the Turkish property market. We believe that a slight increase in average property values is possible in Germany, Denmark, Poland and Sweden. In the case of the UK, the outlook is influenced by the June vote to leave the EU. Should investors and companies react to political and economic uncertainty by taking a wait-and-see attitude, property values are likely to decrease. With many large property funds halting redemptions in early July, the risk of a negative development of values during 2016 has increased on average. With an average loan-to-value ratio (LTV) of currently 57 %, we see no acute risk in Aareal Bank Group's property financing portfolio, which currently stands at € 4.1 billion. Spain's relatively good economic outlook suggests a slightly positive performance. The forecast continued recession in Russia during 2016 is also likely to burden commercial property markets; we thus anticipate the Russian market to deviate from the overall trend and record a slight drop in property values.

The slightly positive outlook with regard to the US commercial property markets is supported by the high levels of liquidity in these markets and the economic outlook. However, potential interest rate increases, given the Fed's turnaround in monetary policy, represent a risk to performance in the medium term. We assume the average performance of Canadian markets to be stable; the performance outlook for China and Japan this year is similar.

The trends described above are expected, in our view, to apply to office, retail and logistics property markets. The hotel markets of key economic centres in Europe will continue to see a slight upturn – measured in an increase of average revenues per available hotel room – this year. However, hotel markets are being burdened by recent terrorist attacks such as those in Istanbul, Nice, and Brussels. For instance, occupancy ratios in Paris were noticeably lower until the middle of the year (compared with the same period of the previous year). Non-recurring effects may also influence other markets. For example, average revenues in Milan may well be down noticeably this year, after having benefited from the EXPO 2015 held there in the previous year. In contrast, the hotel market in Rome is likely to benefit from the Holy Year. A slight increase in revenues per available hotel room is possible in North America, whilst a largely stable development is assumed for the leading economic centres in Asia. Deviations on individual markets, but also seasonal fluctuations, are likely during the course of 2016.

At present, the market for commercial property financing is characterised by intense competition, and it is fair to expect this situation to prevail during the course of this year. The readiness of finance providers to cut their margins is likely to prevail in some parts of Europe, whilst margins appear to be stabilising in the US and many parts of Europe, despite intense competition. We anticipate a slight increase in loan-to-value ratios across the various regions. Whilst lenders are expected to continue adhering to their preference for financing first-class properties in top locations, just like for investors, the shortage of properties in this segment will drive lenders' readiness to finance properties with development potential, and/or in locations outside the top segment.

We have incorporated various market aspects, amongst other factors, in our assessment of new business volumes for the current year. For the Structured Property Financing segment, we anticipate new business of between € 7 billion and € 8 billion for the 2016 financial year. The credit portfolio of Aareal Bank's core business should amount to between € 25 billion and € 27 billion at the end of 2016, subject to currency fluctuations.

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

## Consulting/Services segment

### Bank division Housing Industry

We expect the development for the German housing and commercial property industries to be characterised by a high degree of stability in the current year.

The industries should continue to pursue a sustainable development of their portfolios, largely aimed at improving energy efficiency in the properties. Especially in conurbations, it is not only construction that matters, but also the demolition of housing in negative growth areas. At the same time, companies have started to show an interest in measures to increase the attractiveness of such "exodus areas".

In view of the demographic and overall economic environment, sentiment on the German residential property market will remain positive this year. It is unlikely that any present signs of relaxation on the housing markets will intensify, as incomes, employment as well as demand for housing all rise. Demand for housing is expected to shift towards lower-quality locations in economically strong large and mid-sized cities.

We continue to see good opportunities during 2016 to acquire new clients and to intensify the business relationships with our existing client base. This also applies to our payments services for utilities and the waste disposal industry. Furthermore, we are currently focusing our investments on payment support services and process optimisation – areas where we anticipate further potential.

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

### Aareon

Aareon's strategy is one of growth, and for the 2016 financial year we plan to considerably increase both consolidated sales revenues and consolidated EBIT, on the back of an ongoing migration to state-of-the-art ERP systems and the Group-wide expansion of digital solutions from the "Aareon Smart World" range. Growth in 2016 will be driven by organic activities and the acquisitions made in 2015.

Both in Germany and in International Business, efficiency enhancements in cost and organisational structures will enhance the contribution to results. For Aareon France, we expect the positive trend in maintenance to continue. Aareon UK plans to launch its next ERP product generation QL.net in 2016, with advisory business QL expected to expand. The Swedish Incit Group is expected to increase sales revenues stemming from its ERP solution Incit Xpand, in particular through a rise in business with new clients and, as a consequence, a more dynamic advisory business. Further potential lies in the intended expansion into the Finnish market.

Aareon anticipates its advisory business to expand both in Germany as the migration of GES clients to the Wodis Sigma ERP solution advances proceeds as planned and in the Netherlands where the volumes of migration to Tobias AX, another ERP solution, rise. As we expect that most new clients in Germany will choose to use the software as a service (SaaS) from the exclusive Aareon Cloud, SaaS sales revenues are likely to rise sustainably. Revenues for ERP solutions GES and Tobias (predecessor product to Tobias AX) are expected to decline, as planned.

Expanding Aareon Smart World is a major factor for success in our endeavour to further penetrate the market with digital solutions. For Germany, France and the Netherlands, we expect market penetration to advance (Aareon CRM, Aareon Archiv kompakt, Mobile Services and Mareon). Demand for digital solutions provided by the British subsidiary 1st Touch should continue to increase on the back of the 1st Touch Mobile and Aareon Smart World Cockpit products (formerly 1st Touch 360°), together with the tenant portal.

In view of the aforesaid, Aareon expects a marked increase in sales revenues and results for 2016 overall, anticipating a contribution to consolidated operating profit of between € 33 million and € 35 million.

## Group targets

Looking at our successful performance during the first six months of the year, and in spite of existing uncertainty factors and challenges, we remain generally confident for the current financial year 2016, and affirm our outlook for the year as a whole, according to which net interest income is expected in a range between € 700 million and € 740 million. We expect allowance for credit losses to be in a range between € 80 million and € 120 million. As in the previous years, the Bank cannot rule out additional allowance for unexpected credit losses that may be incurred during the current year.

Net commission income is projected to be in a range between € 190 million and € 200 million. Administrative expenses are expected in a range between € 520 million and € 550 million.

All in all, we continue to anticipate consolidated operating profit of between € 300 million and € 330 million for the current year. The upper end of this range slightly exceeds the record level of the past year, as adjusted for negative goodwill from the acquisition of WestImmo. We expect RoE before taxes of around 11 % for the current financial year, with earnings per share between € 2.85 and € 3.19, based on an expected tax rate of around 31 %. Our medium-term target RoE of 12 % before taxes remains unchanged.

In the Structured Property Financing segment, the credit portfolio attributable to Aareal Bank's core business should amount to between € 25 billion and € 27 billion, subject to currency fluctuations. New business is targeted between € 7 billion and € 8 billion in 2016. In the Consulting / Services segment, we expect our IT subsidiary Aareon to contribute a significantly higher amount of between € 33 million and € 35 million to consolidated operating profit.

Given prevailing uncertainty with regard to future regulatory requirements, we consider a fully phased Common Equity Tier 1 (CET 1) ratio of at least 10.75 % plus a management buffer of 2.25 % to be appropriate. The Liquidity Coverage Ratio (LCR) is expected to be at least 100 %.

# Consolidated Financial Statements
# Statement of Comprehensive Income[1)]

## Income Statement

| € mn | Note | 1 Jan-30 Jun 2016 | 1 Jan-30 Jun 2015 |
|---|---|---|---|
| Interest income | | 440 | 490 |
| Interest expenses | | 83 | 121 |
| **Net interest income** | 1 | **357** | **369** |
| Allowance for credit losses | 2 | 31 | 49 |
| **Net interest income after allowance for credit losses** | | **326** | **320** |
| Commission income | | 112 | 97 |
| Commission expenses | | 19 | 14 |
| **Net commission income** | 3 | **93** | **83** |
| Net result on hedge accounting | 4 | 1 | 8 |
| Net trading income/expenses | 5 | 17 | -5 |
| Results from non-trading assets | 6 | 61 | -2 |
| Results from investments accounted for using the equity method | | 0 | 0 |
| Administrative expenses | 7 | 290 | 268 |
| Net other operating income/expenses | 8 | -1 | 10 |
| Negative goodwill from acquisitions | | – | 150 |
| **Operating profit** | | **207** | **296** |
| Income taxes | | 65 | 46 |
| **Consolidated net income** | | **142** | **250** |
| Consolidated net income attributable to non-controlling interests | | 10 | 10 |
| Consolidated net income attributable to shareholders of Aareal Bank AG | | 132 | 240 |
| **Earnings per share (EpS)** | | | |
| Consolidated net income attributable to shareholders of Aareal Bank AG[2)] | | 132 | 240 |
| of which: allocated to ordinary shareholders | | 124 | 232 |
| of which: allocated to AT1 investors | | 8 | 8 |
| Earnings per ordinary share (€)[3)] | | 2.08 | 3.87 |
| Earnings per AT1 unit (€)[4)] | | 0.08 | 0.08 |

1) Adjustment of previous year's figures due to completion of purchase price allocation for WestImmo, in accordance with IFRS 3

2) The allocation of earnings is based on the assumption that net interest payable on the AT1 bond is recognised on an accrual basis.

3) Earnings per ordinary share are determined by dividing the earnings allocated to ordinary shareholders of Aareal Bank AG by the weighted average of ordinary shares outstanding during the financial year (59,857,221 shares). Basic earnings per ordinary share correspond to diluted earnings per ordinary share.

4) Earnings per AT1 unit (based on 100,000,000 AT1 units with a notional amount of € 3 each) are determined by dividing the earnings allocated to AT1 investors by the weighted average of AT1 units outstanding during the financial year. Earnings per AT1 unit (basic) correspond to (diluted) earnings per AT1 unit.

# Statement of Comprehensive Income

## Reconciliation from Consolidated Net Income to Total Comprehensive Income

| € mn | 1 Jan-30 Jun 2016 | 1 Jan-30 Jun 2015 |
|---|---|---|
| **Consolidated net income** | **142** | **250** |
| Items that will not be reclassified subsequently to profit or loss | | |
| **Changes in the reserve from defined benefit plans** | **-47** | **16** |
| Remeasurements | -68 | 24 |
| Taxes | 21 | -8 |
| Items that are reclassified subsequently to profit or loss | | |
| **Changes in revaluation surplus** | **3** | **23** |
| Gains and losses on remeasuring AfS financial instruments | 5 | 22 |
| Reclassifications to the income statement | -1 | 10 |
| Taxes | -1 | -9 |
| **Changes in hedging reserves** | **9** | **18** |
| Profit/loss from derivatives used to hedge future cash flows | 11 | 27 |
| Reclassifications to the income statement | 2 | – |
| Taxes | -4 | -9 |
| **Changes in currency translation reserves** | **-2** | **4** |
| Profit/loss from translating foreign operations' financial statements | -3 | 4 |
| Reclassifications to the income statement | 1 | – |
| Taxes | – | – |
| **Other comprehensive income** | **-37** | **61** |
| **Total comprehensive income** | **105** | **311** |
| Total comprehensive income attributable to non-controlling interests | 10 | 10 |
| Total comprehensive income attributable to shareholders of Aareal Bank AG | 95 | 301 |

# Statement of Comprehensive Income

## Income Statement (Quarterly Development)

| € mn | Quarter 2 2016 | Quarter 2 2015 |
|---|---|---|
| Interest income | 214 | 246 |
| Interest expenses | 37 | 55 |
| **Net interest income** | **177** | **191** |
| Allowance for credit losses | 29 | 31 |
| **Net interest income after allowance for credit losses** | **148** | **160** |
| Commission income | 57 | 50 |
| Commission expenses | 10 | 8 |
| **Net commission income** | **47** | **42** |
| Net result on hedge accounting | 0 | -3 |
| Net trading income/expenses | 8 | 2 |
| Results from non-trading assets | 61 | 1 |
| Results from investments accounted for using the equity method | 0 | 0 |
| Administrative expenses | 144 | 136 |
| Net other operating income/expenses | 0 | 13 |
| Negative goodwill from acquisitions | – | 150 |
| **Operating profit** | **120** | **229** |
| Income taxes | 38 | 24 |
| **Consolidated net income** | **82** | **205** |
| Consolidated net income attributable to non-controlling interests | 5 | 5 |
| Consolidated net income attributable to shareholders of Aareal Bank AG | 77 | 200 |

# Statement of Comprehensive Income

## Reconciliation from Consolidated Net Income to Total Comprehensive Income (Quarterly Development)

| € mn | Quarter 2 2016 | Quarter 2 2015 |
|---|---|---|
| **Consolidated net income** | **82** | **205** |
| Items that will not be reclassified subsequently to profit or loss | | |
| **Changes in the reserve from defined benefit plans** | **-25** | **48** |
| Remeasurements | -36 | 70 |
| Taxes | 11 | -22 |
| Items that are reclassified subsequently to profit or loss | | |
| **Changes in revaluation surplus** | **6** | **-24** |
| Gains and losses on remeasuring AfS financial instruments | 9 | -33 |
| Reclassifications to the income statement | -1 | -1 |
| Taxes | -2 | 10 |
| **Changes in hedging reserves** | **0** | **0** |
| Profit/loss from derivatives used to hedge future cash flows | 0 | 0 |
| Reclassifications to the income statement | 0 | – |
| Taxes | 0 | 0 |
| **Changes in currency translation reserves** | **0** | **1** |
| Profit/loss from translating foreign operations' financial statements | -1 | 1 |
| Reclassifications to the income statement | 1 | – |
| Taxes | – | – |
| **Other comprehensive income** | **-19** | **25** |
| **Total comprehensive income** | **63** | **230** |
| Total comprehensive income attributable to non-controlling interests | 5 | 5 |
| Total comprehensive income attributable to shareholders of Aareal Bank AG | 58 | 225 |

# Segment Reporting

## Segment Results[1)]

| € mn | Structured Property Financing | | Consulting/Services | | Consolidation/Reconciliation | | Aareal Bank Group | |
|---|---|---|---|---|---|---|---|---|
| | 1 Jan-30 Jun 2016 | 1 Jan-30 Jun 2015 | 1 Jan-30 Jun 2016 | 1 Jan-30 Jun 2015 | 1 Jan-30 Jun 2016 | 1 Jan-30 Jun 2015 | 1 Jan-30 Jun 2016 | 1 Jan-30 Jun 2015 |
| Net interest income | 363 | 370 | 0 | 0 | -6 | -1 | 357 | 369 |
| Allowance for credit losses | 31 | 49 | | | | | 31 | 49 |
| **Net interest income after allowance for credit losses** | **332** | **321** | **0** | **0** | **-6** | **-1** | **326** | **320** |
| Net commission income | 3 | 2 | 85 | 81 | 5 | 0 | 93 | 83 |
| Net result on hedge accounting | 1 | 8 | | | | | 1 | 8 |
| Net trading income/expenses | 17 | -5 | 0 | | | | 17 | -5 |
| Results from non-trading assets | 61 | -2 | | | | | 61 | -2 |
| Results from investments accounted for using the equity method | | | 0 | 0 | | | 0 | 0 |
| Administrative expenses | 189 | 173 | 102 | 96 | -1 | -1 | 290 | 268 |
| Net other operating income/expenses | -1 | 9 | 0 | 1 | 0 | 0 | -1 | 10 |
| Negative goodwill from acquisitions | | 150 | | | | | | 150 |
| **Operating profit** | **224** | **310** | **-17** | **-14** | **0** | **0** | **207** | **296** |
| Income taxes | 71 | 50 | -6 | -4 | | | 65 | 46 |
| **Consolidated net income** | **153** | **260** | **-11** | **-10** | **0** | **0** | **142** | **250** |
| Consolidated net income attributable to non-controlling interests | 8 | 8 | 2 | 2 | | | 10 | 10 |
| Consolidated net income attributable to shareholders of Aareal Bank AG | 145 | 252 | -13 | -12 | 0 | 0 | 132 | 240 |
| | | | | | | | | |
| Allocated equity | 1,614 | 1,593 | 114 | 124 | 728 | 550 | 2,456 | 2,267 |
| Cost/income ratio (%) | 42.4 | 45.3 | 120.2 | 117.6 | | | 54.9 | 57.9 |
| RoE before taxes (%)[2) 3)] | 25.4 | 36.5 | -33.3 | -26.2 | | | 15.1 | 24.2 |
| | | | | | | | | |
| **Employees (average)** | **1,058** | **972** | **1,764** | **1,634** | | | **2,822** | **2,606** |
| | | | | | | | | |
| **Segment assets** | **41,284** | **45,993** | **9,641** | **9,504** | | | **50,925** | **55,497** |

[1)] Adjustment of previous year's figures due to completion of purchase price allocation for WestImmo, in accordance with IFRS 3
[2)] On an annualised basis.
[3)] The allocation of earnings is based on the assumption that net interest payable on the AT1 bond is recognised on an accrual basis.

# Segment Reporting

## Segment Results (Quarterly Development)[1)]

| | Structured Property Financing | | Consulting/Services | | Consolidation/ Reconciliation | | Aareal Bank Group | |
|---|---|---|---|---|---|---|---|---|
| | Quarter 2 2016 | Quarter 2 2015 | Quarter 2 2016 | Quarter 2 2015 | Quarter 2 2016 | Quarter 2 2015 | Quarter 2 2016 | Quarter 2 2015 |
| € mn | | | | | | | | |
| Net interest income | 181 | 192 | 0 | 0 | -4 | -1 | 177 | 191 |
| Allowance for credit losses | 29 | 31 | | | | | 29 | 31 |
| **Net interest income after allowance for credit losses** | **152** | **161** | **0** | **0** | **-4** | **-1** | **148** | **160** |
| Net commission income | 1 | 2 | 43 | 40 | 3 | 0 | 47 | 42 |
| Net result on hedge accounting | 0 | -3 | | | | | 0 | -3 |
| Net trading income/expenses | 8 | 2 | 0 | | | | 8 | 2 |
| Results from non-trading assets | 61 | 1 | | | | | 61 | 1 |
| Results from investments accounted for using the equity method | | | 0 | 0 | | | 0 | 0 |
| Administrative expenses | 94 | 89 | 51 | 48 | -1 | -1 | 144 | 136 |
| Net other operating income/expenses | 0 | 12 | 0 | 1 | 0 | 0 | 0 | 13 |
| Negative goodwill from acquisitions | | 150 | | | | | | 150 |
| **Operating profit** | **128** | **236** | **-8** | **-7** | **0** | **0** | **120** | **229** |
| Income taxes | 41 | 26 | -3 | -2 | | | 38 | 24 |
| **Consolidated net income** | **87** | **210** | **-5** | **-5** | **0** | **0** | **82** | **205** |
| Consolidated net income attributable to non-controlling interests | 4 | 4 | 1 | 1 | | | 5 | 5 |
| Consolidated net income attributable to shareholders of Aareal Bank AG | 83 | 206 | -6 | -6 | 0 | 0 | 77 | 200 |
| | | | | | | | | |
| Allocated equity | 1,614 | 1,593 | 114 | 124 | 728 | 550 | 2,456 | 2,267 |
| Cost/income ratio (%) | 37.2 | 42.7 | 118.0 | 117.4 | | | 49.0 | 55.2 |
| RoE before taxes (%)[2) 3)] | 29.5 | 56.8 | -30.7 | -26.2 | | | 17.9 | 38.5 |

[1)] Adjustment of previous year's figures due to completion of purchase price allocation for WestImmo, in accordance with IFRS 3

[2)] On an annualised basis.

[3)] The allocation of earnings is based on the assumption that net interest payable on the AT1 bond is recognised on an accrual basis.

# Segment Reporting

## Consulting / Services segment – Reconciliation of the Income Statement

### Reconciliation of the segment result from the income statement classification aligned to an industrial enterprise to a bank income statement classification (which is used for the purposes of segment reporting)

| € mn | | | Income statement classification – bank | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | | | Net interest income | Net commission income | Net trading income/ expenses | Results from investments accounted for using the equity method | Administrative expenses | Net other operating income / expenses | Impairment of goodwill | **Operating profit** | Income taxes | **Segment result** |
| | **Q2 2016** | | 0 | 43 | 0 | 0 | 51 | 0 | | **-8** | -3 | **-5** |
| | **Q2 2015** | | 0 | 40 | | 0 | 48 | 1 | | **-7** | -2 | **-5** |
| **Income statement classification – industrial enterprise** | | | | | | | | | | | | |
| Sales revenue | Q2 2016 | 52 | | 52 | | | | | | | | |
| | Q2 2015 | 47 | | 47 | | | | | | | | |
| Own work capitalised | Q2 2016 | 2 | | | | | 2 | | | | | |
| | Q2 2015 | 1 | | | | | 1 | | | | | |
| Changes in inventory | Q2 2016 | 0 | | | | | | 0 | | | | |
| | Q2 2015 | 0 | | | | | | 0 | | | | |
| Other operating income | Q2 2016 | 0 | | | 0 | | | 0 | | | | |
| | Q2 2015 | 2 | | | | | | 2 | | | | |
| Cost of materials purchased | Q2 2016 | 9 | | 9 | | | | | | | | |
| | Q2 2015 | 7 | | 7 | | | | | | | | |
| Staff expenses | Q2 2016 | 35 | | | | | 35 | | | | | |
| | Q2 2015 | 33 | | | | | 33 | | | | | |
| Depreciation, amortisation and impairment losses | Q2 2016 | 3 | | | | | 3 | | | | | |
| | Q2 2015 | 3 | | | | | 3 | | | | | |
| Results from investments accounted for using the equity method | Q2 2016 | 0 | | | | 0 | | | | | | |
| | Q2 2015 | 0 | | | | 0 | | | | | | |
| Other operating expenses | Q2 2016 | 15 | | | | | 15 | 0 | | | | |
| | Q2 2015 | 14 | | | | | 13 | 1 | | | | |
| Interest and similar income / expenses | Q2 2016 | 0 | 0 | | | | | | | | | |
| | Q2 2015 | 0 | 0 | | | | | | | | | |
| **Operating profit** | **Q2 2016** | **-8** | **0** | **43** | **0** | **0** | **51** | **0** | | | | |
| | **Q2 2015** | **-7** | **0** | **40** | | **0** | **48** | **1** | | | | |
| Income taxes | Q2 2016 | -3 | | | | | | | | | -3 | |
| | Q2 2015 | -2 | | | | | | | | | -2 | |
| **Segment result** | **Q2 2016** | **-5** | | | | | | | | | | |
| | **Q2 2015** | **-5** | | | | | | | | | | |

# Statement of Financial Position

| € mn | Note | 30 Jun 2016 | 31 Dec 2015 |
|---|---|---|---|
| **Assets** | | | |
| Cash funds | | 1,051 | 1,282 |
| Loans and advances to banks | 9 | 1,787 | 1,893 |
| Loans and advances to customers | 10 | 33,864 | 34,566 |
| Allowance for credit losses | 11 | -538 | -528 |
| Positive market value of derivative hedging instruments | | 2,937 | 2,498 |
| Trading assets | 12 | 711 | 638 |
| Non-trading assets | 13 | 10,215 | 10,507 |
| Investments accounted for using the equity method | | 1 | 1 |
| Intangible assets | 14 | 123 | 126 |
| Property and equipment | 15 | 268 | 267 |
| Income tax assets | | 30 | 20 |
| Deferred tax assets | | 243 | 239 |
| Other assets | 16 | 233 | 439 |
| **Total** | | **50,925** | **51,948** |
| **Equity and liabilities** | | | |
| Liabilities to banks | 17 | 2,143 | 1,898 |
| Liabilities to customers | 18 | 30,236 | 30,360 |
| Certificated liabilities | 19 | 9,479 | 10,819 |
| Negative market value of derivative hedging instruments | | 2,827 | 2,720 |
| Trading liabilities | 20 | 702 | 663 |
| Provisions | 21 | 824 | 783 |
| Income tax liabilities | | 74 | 102 |
| Deferred tax liabilities | | 34 | 34 |
| Other liabilities | 22 | 158 | 114 |
| Subordinated capital | 23 | 1,423 | 1,411 |
| Equity | 24, 25, 26 | | |
| Subscribed capital | | 180 | 180 |
| Capital reserves | | 721 | 721 |
| Retained earnings | | 1,651 | 1,633 |
| AT1 bond | | 300 | 300 |
| Other reserves | | -69 | -32 |
| Non-controlling interests | | 242 | 242 |
| Total equity | | 3,025 | 3,044 |
| **Total** | | **50,925** | **51,948** |

# Statement of Changes in Equity

| € mn | Subscribed capital | Capital reserves | Retained earnings | AT1 bond | Other reserves: Reserve from remeasurements of defined benefit plans | Other reserves: Revaluation surplus | Other reserves: Hedging reserves | Other reserves: Currency translation reserves | Total | Non-controlling interest | Equity |
|---|---|---|---|---|---|---|---|---|---|---|---|
| **Equity as at 1 Jan 2016** | **180** | **721** | **1,633** | **300** | **-80** | **28** | **13** | **7** | **2,802** | **242** | **3,044** |
| Total comprehensive income for the period | | | 132 | | -47 | 3 | 9 | -2 | **95** | 10 | **105** |
| Payments to non-controlling interests | | | | | | | | | | -10 | **-10** |
| Dividends | | | -99 | | | | | | **-99** | | **-99** |
| AT1 coupon | | | -16 | | | | | | **-16** | | **-16** |
| Other changes | | | 1 | | | | | | **1** | | **1** |
| **Equity as at 30 Jun 2016** | **180** | **721** | **1,651** | **300** | **-127** | **31** | **22** | **5** | **2,783** | **242** | **3,025** |

| € mn | Subscribed capital | Capital reserves | Retained earnings[1)] | AT1 bond | Other reserves: Reserve from remeasurements of defined benefit plans | Other reserves: Revaluation surplus | Other reserves: Hedging reserves | Other reserves: Currency translation reserves | Total | Non-controlling interest | Equity |
|---|---|---|---|---|---|---|---|---|---|---|---|
| **Equity as at 1 Jan 2015** | **180** | **721** | **1,357** | **300** | **-95** | **15** | **-1** | **4** | **2,481** | **242** | **2,723** |
| Total comprehensive income for the period | | | 240 | | 16 | 23 | 18 | 4 | **301** | 10 | **311** |
| Payments to non-controlling interests | | | | | | | | | | -10 | **-10** |
| Dividends | | | -72 | | | | | | **-72** | | **-72** |
| AT1 coupon | | | -7 | | | | | | **-7** | | **-7** |
| Other changes | | | | | | | | | | | |
| **Equity as at 30 Jun 2015** | **180** | **721** | **1,518** | **300** | **-79** | **38** | **17** | **8** | **2,703** | **242** | **2,945** |

[1)] Adjustment of previous year's figures due to completion of purchase price allocation for WestImmo, in accordance with IFRS 3

# Statement of Cash Flows (condensed)

| € mn | 2016 | 2015 |
|---|---|---|
| **Cash and cash equivalents as at 1 January** | **1,282** | **184** |
| Cash flow from operating activities | -423 | -694 |
| Cash flow from investing activities | 295 | 859 |
| Cash flow from financing activities | -103 | -165 |
| **Total cash flow** | **-231** | **0** |
| Effect of changes in exchange rates | 0 | 0 |
| **Cash and cash equivalents as at 30 June** | **1,051** | **184** |

# Notes (condensed)

## Basis of Accounting

### Legal framework

Aareal Bank AG is a listed public limited company incorporated under German law, with its registered office in Wiesbaden, Germany. It is the parent company of an international property finance and services group.

This half-yearly financial report for the period ended 30 June 2016 was prepared pursuant to the provisions of section 37w of the German Securities Trading Act (Wertpapierhandelsgesetz – "WpHG") in conjunction with section 37y no. 2 of the WpHG. It comprises the present interim condensed consolidated financial statements (also referred to as the "Consolidated Financial Statements"), as well as an interim group management report (also referred to as the "Group Management Report") and was approved for publication by the Management Board on 2 August 2016.

Aareal Bank AG prepares its condensed interim consolidated financial statements in accordance with International Financial Reporting Standards (IFRSs) applicable within the European Union (EU) as at the reporting date, in connection with the provisions pursuant to section 315a (1) of the German Commercial Code (Handelsgesetzbuch – "HGB"). In particular, the interim consolidated financial statements comply with the requirements for interim financial reporting set out in IAS 34. The reporting currency is the euro (€).

### Reporting entity structure

Subsidiaries of Aareal Bank AG are included in the consolidated financial statements by way of full consolidation. Companies over which Aareal Bank AG may exercise a significant influence ("associates") are included in the consolidated financial statements, using the equity method.

Apart from the disposal of all shares in Aareal Bank's wholly-owned subsidiary Aqvatrium, there were no other material changes to the scope of consolidation during the period under review.

### Accounting Policies

Unless specifically indicated otherwise, the accounting policies applied in the preparation of the consolidated financial statements 2015 were also applied in the preparation of these condensed interim consolidated financial statements, including the calculation of comparative figures.

The following financial reporting standards (IASs/IFRSs) were required to be applied for the first time in the reporting period:

#### IAS 19 Defined Benefit Plans: Employee Contribution

The amendments to IAS 19 include a clarification regarding the recognition of employee contributions made to defined benefit plans paid by the employees themselves for service elements. Contributions by employees or third parties reduce the ultimate costs of benefit commitments and are therefore accounted for on the basis of accounting policies for benefit commitments.

### Annual Improvements Cycle 2010-2012

The Annual Improvements Cycle 2010-2012 resulted in a collection of clarifications and minor amendments to different standards. The amendment to IFRS 2 mainly consists of a clarification of the definition for "vesting condition" by adding definitions for "service condition" and "performance condition" to Appendix A of the standard. The amendments to IFRS 3 related to the classification of contingent consideration as debt or equity pursuant to IFRS 3.40. According to the latest amendments, only contingent consideration transferred as part of a business combination and fulfilling the definition of a financial instrument shall be considered for classification, while the reference to "other applicable IFRSs" was deleted. If a contingent consideration is classified as a financial liability, it shall be recognised at fair value through profit or loss. The amendments to IFRS 8 clarified the aggregation of operating segments and the reconciliation of segments' assets to the entity's assets as disclosed in the statement of financial position. The amendment to IFRS 13 clarified that short-term receivables and liabilities may not be subject to discounting if the effect of not discounting is immaterial. The amendments to IAS 16 and 38 provide clarification on the restatement of accumulated depreciation in case of a revaluation of assets. The amendment to IAS 24 broadens the definition of "related parties" to include entities (and group companies of such entities) providing key management personnel services to the reporting entity, without any other form of close relationship in place between the two companies within the meaning of IAS 24 (so-called "management entities").

### IFRS 11 Accounting for Acquisitions of Interest in Joint Operations

The amendments to IFRS 11 govern the recognition of acquisitions of interests in joint operations in which the activity constitutes a business within the meaning of IFRS 3 Business Combinations. In such cases, the acquirer has to apply the principles on business combinations accounting set out in IFRS 3. Moreover, disclosure requirements of IFRS 3 apply in these cases. In addition, the amendment clarifies that, in the context of the acquisition of additional interests, previously held interests in a joint operation are not remeasured if joint control is retained.

### IAS 16 und IAS 38 Clarification of Acceptable Methods of Depreciation and Amortisation

The amendments include guidance for determining an acceptable method of depreciation and amortisation. The amendments clarify that depreciation of property, plant and equipment on the basis of revenue from the goods produced by such property, plant and equipment is not appropriate. In addition, rules are introduced pursuant to which future reductions in the selling price of goods and services are an indication of their economic obsolescence and, therefore, an indication for the decline of potential future economic benefits of the assets required for the production of such goods or services.

### IAS 16 und IAS 41 Agriculture: Bearer Plants

In accordance with the amendments, bearer plants – such as grape vines, rubber trees and oil palms – which are used to harvest the produce of biological assets over several accounting periods, without being sold as agricultural produce, have to be accounted for in the same way as property, plant and equipment pursuant to IAS 16, since their use is similar. However, the produce growing on bearer plants continues to be accounted for in accordance with IAS 41 in future.

### IAS 27 Equity Method in Separate Financial Statements

As a result of the amendment, the equity method is re-introduced as an accounting option for interests in subsidiaries, joint ventures and associates in separate financial statements of an investor. The existing options for measurement at cost or in accordance with IAS 39/IFRS 9 continue to apply.

#### Annual Improvements Cycle 2012-2014

The Annual Improvements Cycle 2012-2014 resulted in a collection of clarifications and minor amendments to different standards. The amendments to IFRS 5 include guidance for cases in which an entity reclassifies an asset directly from "held for sale" to "held for distribution to owners". The presentation and measurement requirements as described in IFRS 5 still apply after direct reclassification. A further amendment concerns IFRS 7, clarifying in which cases servicing contracts – where the selling entity retains any of the contractual rights or obligations inherent in the transferred financial asset – form the basis for continuing involvement within the meaning of IFRS 7. The amendments also specify that there is no explicit disclosure requirement regarding the offsetting of financial assets and liabilities in condensed interim financial statements. The amendment to IAS 19 relates to the interest rate used for discounting defined benefit pension obligations. The amendment clarifies that the depth of the market for high quality corporate bonds should be assessed "at currency level", i.e. corporate bonds from the entire euro zone should be taken into account for assessments relating to the euro zone. The amendment to IAS 34 affects disclosures "elsewhere in the interim report". Such information may be provided directly in the respective interim report (chapter reference required), or in other documents, and shall always be subject to a cross-reference provided in the interim report.

#### Amendments to IAS 1: Disclosure Initiative

The amendments refer to clarifications of the concept of materiality in relation to the presentation of items in the statement of financial position, the statement of comprehensive income, the statement of cash flows and the statement of changes in equity as well as regarding the Notes. Immaterial disclosures are not required to be made. This also applies when the disclosure is explicitly required pursuant to other standards. In addition, rules for the presentation of subtotals, the systematic ordering or grouping of the Notes, as well as the disclosures of accounting policies, have been added to IAS 1, and previous requirements have been clarified. Moreover, the amendment clarifies the separate presentation of the share of investments accounted for using the equity method in other comprehensive income in the statement of comprehensive income by items that are subsequently reclassified to the income statement and those which are not reclassified to the income statement.

The revised standards do not have any material consequences for the consolidated financial statements of Aareal Bank Group.

In the reporting period, the following financial reporting standards (IASs/IFRSs) to be applied in future financial years were published by the International Accounting Standards Board (IASB) or endorsed by the EU Commission:

| New International Financial Reporting Standards | Issued | Endorsed | Effective date |
|---|---|---|---|
| IFRS 16 Leases | January 2016 | | Financial years beginning on or after 1 January 2019 |

| Revised International Financial Reporting Standards | | Issued | Endorsed | Effective date |
|---|---|---|---|---|
| IAS 12 | Recognition of Deferred Tax Assets for Unrealised Losses | January 2016 | | Financial years beginning on or after 1 January 2017 |
| IAS 7 | Disclosure Initiative | January 2016 | | Financial years beginning on or after 1 January 2017 |
| IFRS 15 | Revenue from Contracts with Customers | April 2016 | | Financial years beginning on or after 1 January 2018 |
| IFRS 2 | Classification and Measurement of Share-based Payment Transactions | June 2016 | | Financial years beginning on or after 1 January 2018 |

**IFRS 16: Leases**

The new financial reporting standard IFRS 16, regarding lease accounting, will replace IAS 17 as well as the related interpretations IFRIC 4, SIC 15 and SIC 7. IFRS 16 introduces a single lessee accounting model and requires a lessee to recognise (in the statement of financial position) any leases and the related contractual rights and obligations with a term of more than twelve months, unless the underlying asset is of low value. The lessee recognises a right-of-use asset (representing its right to use the underlying leased asset) and also a lease liability (representing its obligation to make lease payments). Similar to the previous rules set out in IAS 17, the lessor continues to classify its leases as finance or operating leases. The criteria for classification under IFRS 16 equal those of IAS 17. In addition, IFRS 16 sets outs a number of further rules for presentation, disclosures in the Notes and sale-and-lease-back transactions.

**Amendments to IAS 12: Recognition of Deferred Tax Assets for Unrealised Losses**

The amendment to IAS 12 clarifies that an impairment of a debt instrument measured at fair value, resulting from changes in market interest rates, leads to deductible temporary differences. The IASB also clarifies that an entity has to assess for all of its deductible temporary differences whether taxable profits are expected to be available in future, in order to utilise and recognise these. Only if and to the extent that tax laws make a distinction between different types of taxable profits, these different types have to be assessed separately. Moreover, IAS 12 introduces rules and examples which clarify how future taxable income has to be determined for the recognition of deferred tax assets.

**Amendments to IAS 7: Disclosure Initiative**

Within the scope of the disclosure initiative, amendments to IAS 7 Statement of Cash Flows were issued. The objective is to improve information about changes in an entity's liabilities. In future, an entity has to provide disclosures about the changes in financial liabilities whose cash receipts and cash payments are reported in the statement of cash flows as cash flows from financing activities. The related financial assets also have to be disclosed (e.g. assets from hedging transactions). The IASB suggests presenting the disclosures in the form of a reconciliation between the opening and closing balances in the statement of financial position, but also permits other forms of presentations.

**Clarifications to IFRS 15: Revenue from Contracts with Customers**

In April 2016, the IASB issued the final version of the amendment standard IFRS 15. The amendment includes clarifications regarding various rules set out in IFRS 15, and also simplifications concerning the transition to the new standard. The clarifications refer to the identification of the service obligations from a contract, the assessment as to whether a company acts as principal or agent of a transaction, and the assessment as to whether revenue from a licence granted has to be recognised either as at a particular reporting date or during a specific period. The simplifications refer to options regarding the presentation of contracts that are either completed at the beginning of the earliest period presented, or which were modified prior to the beginning of the earliest period presented. This is to reduce the complexity and costs of the transition to the new standard.

**Amendments to IFRS 2: Classification and Measurement of Share-based Payment Transactions**
In June 2016, the IASB issued amendments to IFRS 2 that clarify classification and measurement of share-based payment transactions. The amendments relate to the following areas: (i) accounting for cash-settled share-based payment transactions that include a performance condition, (ii) the classification of share-based payment transactions with a settlement feature for withholding tax obligations and (iii) accounting for modifications of share-based payment transactions that change the classification from ”cash-settled” to ”equity-settled”.

Aareal Bank Group did not opt for early application of these standards, which are required to be applied in future financial years.

Aareal Bank Group is currently reviewing the effects of the application of the new and amended financial reporting standards on the consolidated financial statements.

# Notes to the Statement of Comprehensive Income

## (1) Net interest income

| € mn | 1 Jan-30 Jun 2016 | 1 Jan-30 Jun 2015 |
|---|---|---|
| Interest income from | | |
| Property loans | 386 | 429 |
| Public-sector loans | 4 | 7 |
| Other lending and money market operations | 33 | 22 |
| Debt securities and other fixed-income securities | 17 | 32 |
| Current dividend income | 0 | 0 |
| **Total interest income** | **440** | **490** |
| Interest expenses for | | |
| Bonds issued | 19 | 39 |
| Registered mortgage bonds | 7 | 11 |
| Promissory note loans | 22 | 31 |
| Subordinated capital | 16 | 18 |
| Money market transactions | 9 | 19 |
| Other interest expenses | 10 | 3 |
| **Total interest expenses** | **83** | **121** |
| **Total** | **357** | **369** |

Net interest income totalled € 357 million, which represents a slight reduction over the previous year (€ 369 million), which was particularly due to lower early loan repayments. The increase in lending volume – due to the acquisition of WestImmo – was largely offset by the planned reduction of non-strategic portfolios.

Interest income includes expenses of € 5 million from cash investments as well as money market and securities repurchase transactions; interest expenses include income in the amount of € 1 million from money market and securities repurchase transactions.

## (2) Allowance for credit losses

| € mn | 1 Jan-30 Jun 2016 | 1 Jan-30 Jun 2015 |
|---|---|---|
| Additions | 37 | 113 |
| Reversals | 9 | 59 |
| Direct write-offs | 14 | 0 |
| Recoveries on loans and advances previously written off | 11 | 5 |
| **Total** | **31** | **49** |

Allowance for credit losses amounted to € 31 million (H1 2015: € 49 million) and was thus in line with our expectations. The allowances mainly comprise € 21 million in net additions to the specific allowance for credit losses and € 11 million in net additions to the newly-recognised portfolio-based allowance for credit losses. Please also refer to our explanations in note (11).

### (3) Net commission income

| € mn | 1 Jan-30 Jun 2016 | 1 Jan-30 Jun 2015 |
|---|---|---|
| Commission income from | | |
| Consulting and other services | 102 | 89 |
| Trustee loans and administered loans | 1 | 1 |
| Securities transactions | – | – |
| Other lending and money market operations | 4 | 4 |
| Other commission income | 5 | 3 |
| **Total commission income** | **112** | **97** |
| Commission expenses for | | |
| Consulting and other services | 15 | 11 |
| Securities transactions | 1 | 1 |
| Other lending and money market transactions | 1 | 0 |
| Other commission expenses | 2 | 2 |
| **Total commission expenses** | **19** | **14** |
| **Total** | **93** | **83** |

Net commission income increased to € 93 million (H1 2015: € 83 million), which was mainly due to higher sales revenue at Aareon.

Commissions from consulting and services primarily include commissions for IT services.

### (4) Net result on hedge accounting

| € mn | 1 Jan-30 Jun 2016 | 1 Jan-30 Jun 2015 |
|---|---|---|
| Ineffective portion of fair value hedges | 0 | 7 |
| Ineffective portion of cash flow hedges | 1 | 1 |
| Ineffective portion of net investment hedges | – | 0 |
| **Total** | **1** | **8** |

### (5) Net trading income/expenses

| € mn | 1 Jan-30 Jun 2016 | 1 Jan-30 Jun 2015 |
|---|---|---|
| Net income/expenses from positions held for trading | 14 | 7 |
| Currency translation | 3 | -12 |
| **Total** | **17** | **-5** |

Net trading income/expenses are primarily attributable to the measurement and close-out of derivatives used to hedge interest rate and currency risks.

### (6) Results from non-trading assets

| € mn | 1 Jan-30 Jun 2016 | 1 Jan-30 Jun 2015 |
|---|---|---|
| Result from debt securities and other fixed-income securities | 0 | -2 |
| of which: Loans and receivables (LaR) | – | 6 |
| Held to maturity (HtM) | – | – |
| Available for sale (AfS) | 0 | -8 |
| Result from equities and other non-fixed income securities | 0 | 0 |
| of which: Available for sale (AfS) | 0 | 0 |
| Designated as at fair value through profit or loss (dFVtPL) | 0 | – |
| Results from equity investments (AfS) | 61 | 0 |
| **Total** | **61** | **-2** |

The results from non-trading assets arise from the completion of the sale of all of the shares held in the wholly-owned Group company Aqvatrium, which is the owner of a commercial property in Stockholm. The sale was announced on 8 December 2015.

### (7) Administrative expenses

| € mn | 1 Jan-30 Jun 2016 | 1 Jan-30 Jun 2015 |
|---|---|---|
| Staff expenses | 170 | 145 |
| Other administrative expenses | 110 | 114 |
| Depreciation, amortisation and impairment of property and equipment and intangible assets | 10 | 9 |
| **Total** | **290** | **268** |

At € 290 million (H1 2015: € 268 million), administrative expenses exceeded the level of the corresponding previous year's period, as expected. The increase was due particularly to running costs for WestImmo as well as integration costs.

## (8) Net other operating income/expenses

| € mn | 1 Jan-30 Jun 2016 | 1 Jan-30 Jun 2015 |
|---|---|---|
| Income from properties | 15 | 25 |
| Income from the reversal of provisions | 2 | 9 |
| Income from goods and services | 0 | 1 |
| Miscellaneous | 8 | 8 |
| **Total other operating income** | **25** | **43** |
| Expenses for properties | 17 | 22 |
| Expenses for services used | 0 | 0 |
| Write-downs of trade receivables | 0 | 0 |
| Expenses for other taxes | 2 | 3 |
| Miscellaneous | 7 | 8 |
| **Total other operating expenses** | **26** | **33** |
| **Total** | **-1** | **10** |

## Notes to the Statement of Financial Position

### (9) Loans and advances to banks

| € mn | 30 Jun 2016 | 31 Dec 2015 |
|---|---|---|
| Money market receivables | 1,634 | 1,509 |
| Promissory note loans | 140 | 192 |
| Securities repurchase agreements | – | 150 |
| Other loans and advances | 13 | 42 |
| **Total** | **1,787** | **1,893** |

Loans and advances to banks are allocated to the measurement category ”Loans and receivables” (LaR).

### (10) Loans and advances to customers

| € mn | 30 Jun 2016 | 31 Dec 2015 |
|---|---|---|
| Property loans[1)] | 28,902 | 29,344 |
| Promissory note loans | 1,524 | 1,457 |
| Other loans and advances | 3,438 | 3,765 |
| **Total** | **33,864** | **34,566** |

1) Excluding € 1.3 billion in private client business (31 December 2015: € 1.5 billion) and € 0.6 billion in local authority lending business by WestImmo (31 December 2015: € 0.6 billion)

Loans and advances to customers are allocated to the measurement category ”Loans and receivables” (LaR).

### (11) Allowance for credit losses

**30 June 2016**

| € mn | Specific valuation allowances | Portfolio impairment allowance | Total allowance for credit losses for recognised items | Provisions in the lending business for unrecognised items | Total allowance for credit losses and provisions in the lending business |
|---|---|---|---|---|---|
| **Allowance for credit losses as at 1 January** | **412** | **116** | **528** | **14** | **542** |
| Additions | 26 | 11 | **37** | 0 | **37** |
| Write-downs | 6 | – | **6** | – | **6** |
| Reversals | 5 | – | **5** | 4 | **9** |

>

| € mn | Specific valuation allowances | Portfolio impairment allowance | Total allowance for credit losses for recognised items | Provisions in the lending business for unrecognised items | Total allowance for credit losses and provisions in the lending business |
|---|---|---|---|---|---|
| Unwinding | 16 | – | **16** | – | **16** |
| Changes in basis of consolidation | – | – | **–** | – | **–** |
| Currency adjustments | -1 | 1 | **0** | 0 | **0** |
| **Balance as at 30 June** | **410** | **128** | **538** | **10** | **548** |

**30 June 2015**

| € mn | Specific valuation allowances | Portfolio impairment allowance | Total allowance for credit losses for recognised items | Provisions in the lending business for unrecognised items | Total allowance for credit losses and provisions in the lending business |
|---|---|---|---|---|---|
| **Allowance for credit losses as at 1 January** | **333** | **147** | **480** | **18** | **498** |
| Additions | 113 | – | **113** | – | **113** |
| Write-downs | 12 | – | **12** | – | **12** |
| Reversals | 9 | 47 | **56** | 3 | **59** |
| Unwinding | 10 | – | **10** | – | **10** |
| Changes in basis of consolidation[1] | – | 19 | **19** | – | **19** |
| Currency adjustments | 3 | 0 | **3** | 0 | **3** |
| **Balance as at 30 June** | **418** | **119** | **537** | **15** | **552** |

[1] Adjustment of previous year's figures due to completion of purchase price allocation for WestImmo, in accordance with IFRS 3

The allowance for risks associated with unrecognised items relates to loans and advances to customers, and loans and advances to banks classified as "Loans and receivables" (LaR). These allowances are reported under allowance for credit losses on the asset side of the statement of financial position. The provisions for risks associated with unrecognised items relate to contingent liabilities and loan commitments. These provisions are reported under provisions on the liability side of the statement of financial position.

### (12) Trading assets

| € mn | 30 Jun 2016 | 31 Dec 2015 |
|---|---|---|
| Positive market value of trading assets | 711 | 638 |
| **Total** | **711** | **638** |

Trading assets are allocated to the measurement category "Held for trading" (HfT). They are mainly used to hedge economic market price risks.

### (13) Non-trading assets

| € mn | 30 Jun 2016 | 31 Dec 2015 |
|---|---|---|
| Debt securities and other fixed-income securities | 10,209 | 10,499 |
| of which: Loans and receivables (LaR) | 3,554 | 3,630 |
| Held to maturity (HtM) | 622 | 604 |
| Available for sale (AfS) | 6,033 | 6,265 |
| Equities and other non-fixed income securities | 5 | 7 |
| of which: Available for sale (AfS) | 5 | 7 |
| Designated as at fair value through profit or loss (dFVtPL) | – | – |
| Interests in affiliated companies (AfS) | – | – |
| Other investments (AfS) | 1 | 1 |
| **Total** | **10,215** | **10,507** |

The item "Debt and other fixed-income securities" mainly consists of public-sector bonds as well as asset-covered bonds (Pfandbriefanleihen) and bank bonds.

### (14) Intangible assets

| € mn | 30 Jun 2016 | 31 Dec 2015 |
|---|---|---|
| Goodwill | 75 | 75 |
| Proprietary software | 20 | 19 |
| Other intangible assets | 28 | 32 |
| **Total** | **123** | **126** |

### (15) Property and equipment

| € mn | 30 Jun 2016 | 31 Dec 2015 |
|---|---|---|
| Land and buildings and construction in progress | 246 | 245 |
| Office furniture and equipment | 22 | 22 |
| **Total** | **268** | **267** |

### (16) Other assets

| € mn | 30 Jun 2016 | 31 Dec 2015 |
|---|---|---|
| Properties | 53 | 263 |
| Trade receivables (LaR) | 47 | 42 |
| Miscellaneous | 133 | 134 |
| **Total** | **233** | **439** |

The decrease in property arises from the completion of the sale of all of the shares held in the wholly-owned Group company Aqvatrium, which is the owner of a commercial property in Stockholm. The sale was announced on 8 December 2015.

### (17) Liabilities to banks

| € mn | 30 Jun 2016 | 31 Dec 2015 |
|---|---|---|
| Money market liabilities | 1,205 | 925 |
| Promissory note loans | 374 | 414 |
| Registered mortgage Pfandbriefe | 511 | 457 |
| Registered public-sector Pfandbriefe | 24 | 51 |
| Other liabilities | 29 | 51 |
| **Total** | **2,143** | **1,898** |

Liabilities to banks are allocated to the measurement category "Liabilities measured at amortised cost" (LaC).

### (18) Liabilities to customers

| € mn | 30 Jun 2016 | 31 Dec 2015 |
|---|---|---|
| Money market liabilities | 13,604 | 13,179 |
| Promissory note loans | 6,884 | 7,038 |
| Registered mortgage Pfandbriefe | 6,566 | 6,852 |
| Registered public-sector Pfandbriefe | 3,182 | 3,291 |
| Other liabilities | 0 | 0 |
| **Total** | **30,236** | **30,360** |

Liabilities to customers are allocated to the measurement category "Liabilities measured at amortised cost" (LaC).

### (19) Certificated liabilities

| € mn | 30 Jun 2016 | 31 Dec 2015 |
|---|---|---|
| Bearer mortgage Pfandbriefe | 7,021 | 8,529 |
| Bearer public-sector Pfandbriefe | 45 | 71 |
| Other debt securities | 2,413 | 2,219 |
| **Total** | **9,479** | **10,819** |

Certificated liabilities are allocated to the measurement category "Liabilities measured at amortised cost" (LaC).

### (20) Trading liabilities

| € mn | 30 Jun 2016 | 31 Dec 2015 |
|---|---|---|
| Negative market value of trading assets | 702 | 663 |
| **Total** | **702** | **663** |

Trading liabilities are allocated to the measurement category "Held for trading" (HfT). They are mainly used to hedge economic market price risks.

### (21) Provisions

| € mn | 30 Jun 2016 | 31 Dec 2015 |
|---|---|---|
| Provisions for pensions and similar obligations | 402 | 333 |
| Other provisions and contingent liabilities | 422 | 450 |
| **Total** | **824** | **783** |

The change in provisions for pensions and similar obligations were largely attributable to a changed discount rate and the resulting revaluation of the amount of obligations. The change is recognised directly in Other Comprehensive Income, under Changes in the reserve from defined benefit plans.

### (22) Other liabilities

| € mn | 30 Jun 2016 | 31 Dec 2015 |
|---|---|---|
| Liabilities from outstanding invoices | 10 | 12 |
| Deferred income | 19 | 14 |
| Liabilities from other taxes | 14 | 18 |
| Trade payables (LaC) | 10 | 16 |
| Other liabilities (LaC) | 105 | 54 |
| **Total** | **158** | **114** |

### (23) Subordinated capital

| € mn | 30 Jun 2016 | 31 Dec 2015 |
|---|---|---|
| Subordinated liabilities | 1,180 | 1,164 |
| Profit-participation certificates | 52 | 53 |
| Contributions by silent partners | 191 | 194 |
| **Total** | **1,423** | **1,411** |

Items of subordinated capital are allocated to the measurement category "Liabilities measured at amortised cost" (LaC).

### (24) Equity

| € mn | 30 Jun 2016 | 31 Dec 2015 |
|---|---|---|
| Subscribed capital | 180 | 180 |
| Capital reserves | 721 | 721 |
| Retained earnings | 1,651 | 1,633 |
| AT1 bond | 300 | 300 |
| Other reserves | | |
| Reserve from remeasurements of defined benefit plans | -127 | -80 |
| Revaluation reserve | 31 | 28 |
| Hedging reserves | 22 | 13 |
| Currency translation reserves | 5 | 7 |
| Non-controlling interests | 242 | 242 |
| **Total** | **3,025** | **3,044** |

### (25) Treasury shares

No treasury shares were held during the period under review.

### (26) Distributions

The Annual General Meeting of Aareal Bank AG on 25 May 2016 resolved to pay a dividend of € 1.65 per no-par value share, totalling € 98,764,414.65, from net retained profit (Bilanzgewinn) of € 99,264,414.65 as reported under the German Commercial Code (HGB) for the financial year 2015.

In accordance with the terms and conditions of the bond, the Management Board resolved to make a distribution on the AT1 bond, effective 30 April 2016.

Within Aareal Bank Group's consolidated statement of financial position, a dividend payment and a distribution on the AT1 bond reduce the retained earnings item within consolidated equity.

## Notes to the Financial Instruments

### (27) Presentation of the fair value hierarchy in accordance with IFRS 13

The following table shows the carrying amounts of financial instruments held by Aareal Bank Group which are reported at fair value in the statement of financial position, according to the three-tier fair value hierarchy pursuant to IFRS 13.72 et seq. The classification into individual hierarchy levels is based on the inputs used for fair value measurement.

**30 June 2016**

| € mn | Fair value total | Fair value level 1 | Fair value level 2 | Fair value level 3 |
|---|---|---|---|---|
| **Positive market value of derivative hedging instruments** | **2,937** | **–** | **2,937** | **–** |
| **Assets held for trading** | **711** | **–** | **711** | **–** |
| Trading derivatives | 711 | – | 711 | – |
| **Non-trading assets available for sale** | **6,038** | **6,008** | **30** | **–** |
| Fixed-income securities | 6,033 | 6,003 | 30 | – |
| Equities/funds | 5 | 5 | 0 | – |
| **Negative market value of derivative hedging instruments** | **2,827** | **–** | **2,827** | **–** |
| **Liabilities held for trading** | **702** | **–** | **702** | **–** |
| Trading derivatives | 702 | – | 702 | – |

**31 December 2015**

| € mn | Fair value total | Fair value level 1 | Fair value level 2 | Fair value level 3 |
|---|---|---|---|---|
| **Positive market value of derivative hedging instruments** | **2,498** | **–** | **2,498** | **–** |
| **Assets held for trading** | **638** | **–** | **638** | **–** |
| Trading derivatives | 638 | – | 638 | – |
| **Non-trading assets available for sale** | **6,272** | **6,240** | **32** | **–** |
| Fixed-income securities | 6,265 | 6,235 | 30 | – |
| Equities/funds | 7 | 5 | 2 | – |
| **Negative market value of derivative hedging instruments** | **2,720** | **–** | **2,720** | **–** |
| **Liabilities held for trading** | **663** | **–** | **663** | **–** |
| Trading derivatives | 663 | – | 663 | – |

The fair value of financial instruments is allocated to Level 1 of the fair value hierarchy if it is determined on the basis of unadjusted quoted prices in active markets for identical assets or liabilities. The determination of the fair value is based on the principal market for the asset or liability or, in the absence of a principal market, the most advantageous market for the asset or liability. Another factor to be taken into account is whether Aareal Bank can enter into a transaction for the relevant asset or liability at the price in that market at the measurement date.

Fair values determined using inputs other than quoted prices included within Level 1 that are observable for the financial instrument, either directly or indirectly, are included in Level 2 of the fair value hierarchy. Financial instruments whose fair value is allocated to Level 2 of the fair value hierarchy are measured using various valuation techniques.

In case of fixed-income securities or equities for which no current market price is available, the fair value is determined on the basis of comparable market prices to the extent possible. To this end, quoted prices on active markets for largely identical or quoted prices on inactive markets for identical or similar securities are used by adjusting the last available market price or the current fair value of another largely identical instrument, to take into account any changes in risk or new information known as at the measurement date. In the absence of comparable market prices for securities, they are measured through an analysis of future payments using the fully-capitalised earnings value approach, where the inputs are based on observable market data. These approaches include the discounted cash flow (DCF) method which is used to determine the present value of contractual cash flows until the expected end of the term. The present value is determined based on the benchmark curve applicable for the relevant market, taking into account mark-ups based on credit quality and liquidity. The valuation model used for options included in the transaction is the commonly used Black-Scholes model or appropriate numerical procedures.

The fair value of OTC derivatives included in the trading portfolio, as well as of OTC hedging derivatives, is determined on the basis of sector-specific standardised measurement models, such as the present value method or option pricing models. These techniques are based on inputs quoted on active markets, such as interest rates, yield curves and credit spreads. The fair value of foreign exchange forwards is generally based on current forward exchange rates quoted on active markets. Fair values determined using valuation techniques where one or more material inputs are not based on observable market data are assigned to Level 3 of the fair value hierarchy. Products that are allocated to this level are currently not held by Aareal Bank Group.

In the first six months of 2016, there were no material transfers between the hierarchy levels for the various financial instruments.

Aareal Bank reviews the allocation of a financial instrument in the fair value hierarchy on the previous year's balance sheet date of the preceding quarter, in comparison with the allocation on the current reporting date, to determine whether reclassifications occurred between the individual levels of the fair value hierarchy. The date for recognising reclassifications into the hierarchy levels and for recognising reclassifications from the hierarchy levels is the same.

### (28) Comparison of carrying amounts and fair values of the financial instruments

The following table is a comparison of the fair values of the financial instruments with their carrying amounts. The presentation is made for each class of financial instrument.

| € mn | Carrying amount 30 Jun 2016 | Fair value 30 Jun 2016 | Carrying amount 31 Dec 2015 | Fair value 31 Dec 2015 |
|---|---|---|---|---|
| Cash on hand and balances with central banks (LaR) | 1,051 | 1,051 | 1,282 | 1,282 |
| Loans and advances to banks (LaR) | 1,787 | 1,791 | 1,893 | 1,896 |
| Loans and advances to customers (LaR) | 33,326 | 35,572 | 34,038 | 36,156 |
| Non-trading assets (LaR) | 3,554 | 3,442 | 3,630 | 3,586 |
| Other assets (LaR) | 107 | 105 | 93 | 92 |
| **Total loans and receivables** | **39,825** | **41,961** | **40,936** | **43,012** |
| **Non-trading assets held to maturity** | **622** | **625** | **604** | **606** |
| **Non-trading assets available for sale** | **6,038** | **6,038** | **6,272** | **6,272** |
| **Positive market value of derivative hedging instruments** | **2,937** | **2,937** | **2,498** | **2,498** |
| **Assets held for trading** | **711** | **711** | **638** | **638** |
| Liabilities to banks (LaC) | 2,143 | 2,162 | 1,898 | 1,912 |
| Liabilities to customers (LaC) | 30,236 | 30,323 | 30,360 | 30,335 |
| Certificated liabilities (LaC) | 9,479 | 9,516 | 10,819 | 10,870 |
| Other liabilities (LaC) | 125 | 122 | 82 | 82 |
| Subordinated capital (LaC) | 1,423 | 1,427 | 1,411 | 1,441 |
| **Total liabilities measured at amortised cost** | **43,406** | **43,550** | **44,570** | **44,640** |
| **Negative market value of derivative hedging instruments** | **2,827** | **2,827** | **2,720** | **2,720** |
| **Liabilities held for trading** | **702** | **702** | **663** | **663** |

### (29) Day-one profit or loss

Aareal Bank Group has entered into transactions that were not effected on the principal market or the most advantageous market for the asset or liability concerned. In these cases, the transaction price does not correspond to the fair value of the asset or liability, because determination of fair value using a valuation technique which assumes a transaction on a principal market results in a fair value that deviates from the transaction price. The financial instruments are carried at the transaction price upon initial recognition. The difference between the transaction price and the fair value measured based on the valuation model (the so-called day-one profit or loss) is amortised over the term of the transaction in the income statement, since the fair value of these financial instruments of the trading portfolio is determined using valuation models whose inputs are not fully based on observable market factors.

The table below shows the development of the day-one profit or loss during the period under review. The day-one profit or loss is recognised as an item to be deducted from the carrying amount of the respective underlying derivative position:

| € mn | 2016 | 2015 |
|---|---|---|
| **Balance as at 1 January** | **27** | **43** |
| Additions from new transactions | 0 | 2 |
| Reversals through profit or loss in the period | 10 | 8 |
| Changes in basis of consolidation | – | 4 |
| **Balance as at 30 June** | **17** | **41** |

### (30) Reclassification of financial assets

In 2008 and 2009, Aareal Bank Group took advantage of the opportunity to reclassify financial assets into another measurement category. Specifically, securities with an aggregate volume of € 6.2 billion were reclassified from the IFRS measurement categories "Available for sale" (AfS) and "Held for trading" (HfT), to "Loans and receivables" (LaR). In all cases, we opted for reclassification since there was no longer an active market for the securities concerned (in spite of their good quality), and due to our intention to hold these issues for a longer term. Depending on prevailing market conditions, Aareal Bank Group may use this reclassification option again in the future.

The following table compares the carrying amounts of the reclassified assets to their fair values:

| € mn | Carrying amount 30 Jun 2016 | Fair value 30 Jun 2016 | Carrying amount 31 Dec 2015 | Fair value 31 Dec 2015 |
|---|---|---|---|---|
| **from AfS to LaR** | **3,200** | **3,074** | **3,262** | **3,202** |
| Asset-backed securities | 24 | 24 | 27 | 27 |
| Senior unsecured bank bonds | 47 | 48 | 138 | 140 |
| Covered bank bonds | 240 | 245 | 298 | 304 |
| Public-sector issuers | 2,889 | 2,757 | 2,799 | 2,731 |
| **from HfT to LaR** | **77** | **82** | **85** | **91** |
| Asset-backed securities | 77 | 82 | 85 | 91 |
| **Total** | **3,277** | **3,156** | **3,347** | **3,293** |

If the Bank had not opted for reclassification, this would have resulted in a € 1 million loss (before taxes) for the first six months of the current financial year (H1 2015: € 0 million), and € -54 million (after taxes) (H1 2015: € 20 million) would have been recognised in the revaluation surplus.

## (31) Bond and property financing portfolio in selected European countries

The following table is a breakdown of the bonds issued by public-sector entities and bank bonds of selected European countries, included in non-trading assets:

### Bond portfolio as at 30 June 2016

| | Carrying amount | | | Revaluation surplus[1] | | | Unrealised gains / losses[1] |
|---|---|---|---|---|---|---|---|
| | LaR + HtM | AfS | Total | LaR | AfS | Total | |
| € mn | | | | | | | |
| Greece | – | – | – | – | – | – | – |
| Ireland | – | – | – | – | – | – | – |
| Italy | 1,321 | 321 | 1,642 | -41 | 18 | -23 | -83 |
| Portugal | 68 | 109 | 177 | 0 | 0 | 0 | -8 |
| Spain | 550 | 63 | 613 | 0 | 4 | 4 | -12 |
| **Total** | **1,939** | **493** | **2,432** | **-41** | **22** | **-19** | **-103** |
| Total as at 31 Dec 2015 | 1,884 | 579 | 2,463 | -43 | 33 | -10 | -50 |

[1] Figures given on an after-tax basis

The revaluation surplus for bonds of the "Loans and receivables" (LaR) category is attributable to securities which were reclassified in the years 2008 and 2009 from the measurement category "Available for sale" (AfS) to the measurement category "Loans and receivables" (LaR). Unrealised gains and losses refer to securities accounted for at amortised cost (LaR + HtM). When determining such unrealised gains and losses, the effects from interest rate-driven measurement of hedged securities were taken into account.

The maturities of the bonds set out above are mainly within the long-term range.

The presented AfS securities with a carrying amount of € 493 million (31 December 2015: € 579 million) were allocated to Level 1 of the fair value hierarchy, and measured based on quoted prices on active markets.

The following table is a breakdown of property financing in selected European countries included in loans and advances to customers:

### Property financing portfolio as at 30 June 2016

| | Carrying amount[1] | Average LTV[2] | of which: subject to specific valuation allowances |
|---|---|---|---|
| | € mn | % | € mn |
| Greece | – | | – |
| Ireland | – | | – |
| Italy | 3,292 | 72,0 | 832 |
| Portugal | – | | – |
| Spain | 1,103 | 66,8 | 88 |
| **Total** | **4,395** | | **920** |
| Total as at 31 Dec 2015 | 4,335 | | 924 |

[1] Not including valuation allowances; [2] Performing loans only

## Other Notes

### (32) Contingent liabilities and loan commitments

| € mn | 30 Jun 2016 | 31 Dec 2015 |
|---|---|---|
| Contingent liabilities | 154 | 162 |
| Loan commitments | 1,325 | 1,227 |
| of which: irrevocable | 895 | 797 |

### (33) Employees

The number of Aareal Bank Group employees[1] at 30 June 2016 is shown below:

| | 30 Jun 2016 | 31 Dec 2015 |
|---|---|---|
| Salaried employees | 2,652 | 2,695 |
| Executives | 161 | 166 |
| **Total** | **2,813** | **2,861** |
| of which: part-time employees | 520 | 514 |

The average number of Aareal Bank Group employees in 2016[2] is shown below:

| | 1 Jan-30 Jun 2016 | 1 Jan- 31 Dec 2015 |
|---|---|---|
| Salaried employees | 2,659 | 2,557 |
| Executives | 163 | 162 |
| **Total** | **2,822** | **2,719** |
| of which: part-time employees | 518 | 487 |

### (34) Related party disclosures in accordance with IAS 24

In the first six months of the 2016 financial year there were no material transactions with related parties that would have to be reported here.

### (35) Events after the interim reporting period

There have been no material events subsequent to the end of the interim reporting period under review that need to be disclosed at this point.

[1] This number does not include 238 employees of the hotel business La Sessola Service S.r.l. (31 December 2015: 41 employees).
[2] This number does not include 171 employees of the hotel business La Sessola Service S.r.l. (31 December 2015: 132 employees).

## Executive Bodies of Aareal Bank AG

### Supervisory Board

**Marija Korsch** [1) 2) 3) 4) 5) 6)]
Chairman of the Supervisory Board
Former partner of Bankhaus Metzler seel.
Sohn & Co. Holding AG

**Prof. Dr Stephan Schüller** [1) 2) 3)]
Deputy Chairman of the Supervisory Board
Spokesman of the General Partners of
Bankhaus Lampe KG

**York-Detlef Bülow** [1) 2) 3) 7)]
Deputy Chairman of the Supervisory Board
Aareal Bank AG

**Thomas Hawel** [6) 7)]
Aareon Deutschland GmbH

**Dieter Kirsch** [2) 4) 5) 7)]
Aareal Bank AG

**Richard Peters** [1) 3) 6)]
President and Chairman of the Management Board
of Versorgungsanstalt des Bundes und der Länder

**Dr Hans-Werner Rhein** [1) 4) 5)]
German Lawyer (Rechtsanwalt)

**Sylvia Seignette** [4) 5)]
Former CEO of Calyon in Germany/Austria

**Elisabeth Stheeman** [4) 5) 6)]
Senior Advisor, Bank of England, Prudential
Regulation Authority

**Hans-Dietrich Voigtländer** [2) 3) 6)]
Senior Partner at BDG Innovation +
Transformation GmbH & Co. KG

**Prof. Dr Hermann Wagner** [3) 4) 5)]
Chairman of the Audit Committee
German Chartered Accountant, Tax Consultant

**Beate Wollmann** [7)]
Aareon Deutschland GmbH

### Management Board

**Hermann Josef Merkens**
Chairman of the Management Board

**Dagmar Knopek**
Member of the Management Board

**Christiane Kunisch-Wolff**
**(since 15 March 2016)**
Member of the Management Board

**Thomas Ortmanns**
Member of the Management Board

**Christof Winkelmann (since 1 July 2016)**
Member of the Management Board

[1)] Member of the Executive and Nomination Committee; [2)] Member of the Remuneration Control Committee; [3)] Member of the Audit Committee;
[4)] Member of the Risk Committee; [5)] Member of the Committee for Urgent Decisions; [6)] Member of the Technology and Innovation Committee;
[7)] Employee representative

## Responsibility Statement

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

**Wiesbaden, 2 August 2016**

**The Management Board**

**Hermann J. Merkens** **Dagmar Knopek** **Christiane Kunisch-Wolff**

**Thomas Ortmanns** **Christof Winkelmann**

# Review Report

## To Aareal Bank AG, Wiesbaden

We have reviewed the condensed consolidated interim financial statements – comprising the statement of financial position, statement of comprehensive income, condensed statement of cash flows, statement of changes in equity and selected explanatory notes – and the interim group management report of Aareal Bank AG, Wiesbaden for the period from 1st of January 2016 to 30th of June 2016 which are part of the half-year financial report pursuant to § (Article) 37w WpHG ("Wertpapierhandelsgesetz": German Securities Trading Act). The preparation of the condensed consolidated interim financial statements in accordance with the IFRS applicable to interim financial reporting as adopted by the EU and of the interim group management report in accordance with the provisions of the German Securities Trading Act applicable to interim group management reports is the responsibility of the parent Company's Board of Managing Directors. Our responsibility is to issue a review report on the condensed consolidated interim financial statements and on the interim group management report based on our review.

We conducted our review of the condensed consolidated interim financial statements and the interim group management report in accordance with German generally accepted standards for the review of financial statements promulgated by the Institut der Wirtschaftsprüfer (Institute of Public Auditors in Germany) (IDW) and additionally observed the International Standard on Review Engagements "Review of Interim Financial Information Performed by the Independent Auditor of the Entity" (ISRE 2410). Those standards require that we plan and perform the review so that we can preclude through critical evaluation, with moderate assurance, that the condensed consolidated interim financial statements have not been prepared, in all material respects, in accordance with the IFRS applicable to interim financial reporting as adopted by the EU and that the interim group management report has not been prepared, in all material respects, in accordance with the provisions of the German Securities Trading Act applicable to interim group management reports. A review is limited primarily to inquiries of company personnel and analytical procedures and there-fore does not provide the assurance attainable in a financial statement audit. Since, in accordance with our engagement, we have not performed a financial statement audit, we cannot express an audit opinion.

Based on our review, no matters have come to our attention that cause us to presume that the condensed consolidated interim financial statements have not been prepared, in all material respects, in accordance with the IFRS applicable to interim financial reporting as adopted by the EU nor that the interim group management report has not been prepared, in all material respects, in accordance with the provisions of the German Securities Trading Act applicable to interim group management reports.

**Frankfurt/Main, 2 August 2016**

**PricewaterhouseCoopers**
**Aktiengesellschaft**
**Wirtschaftsprüfungsgesellschaft**

| | |
|---|---|
| **Stefan Palm** | **ppa. Kay Böhm** |
| **Wirtschaftsprüfer** | **Wirtschaftsprüfer** |
| **(German Public Auditor)** | **(German Public Auditor)** |

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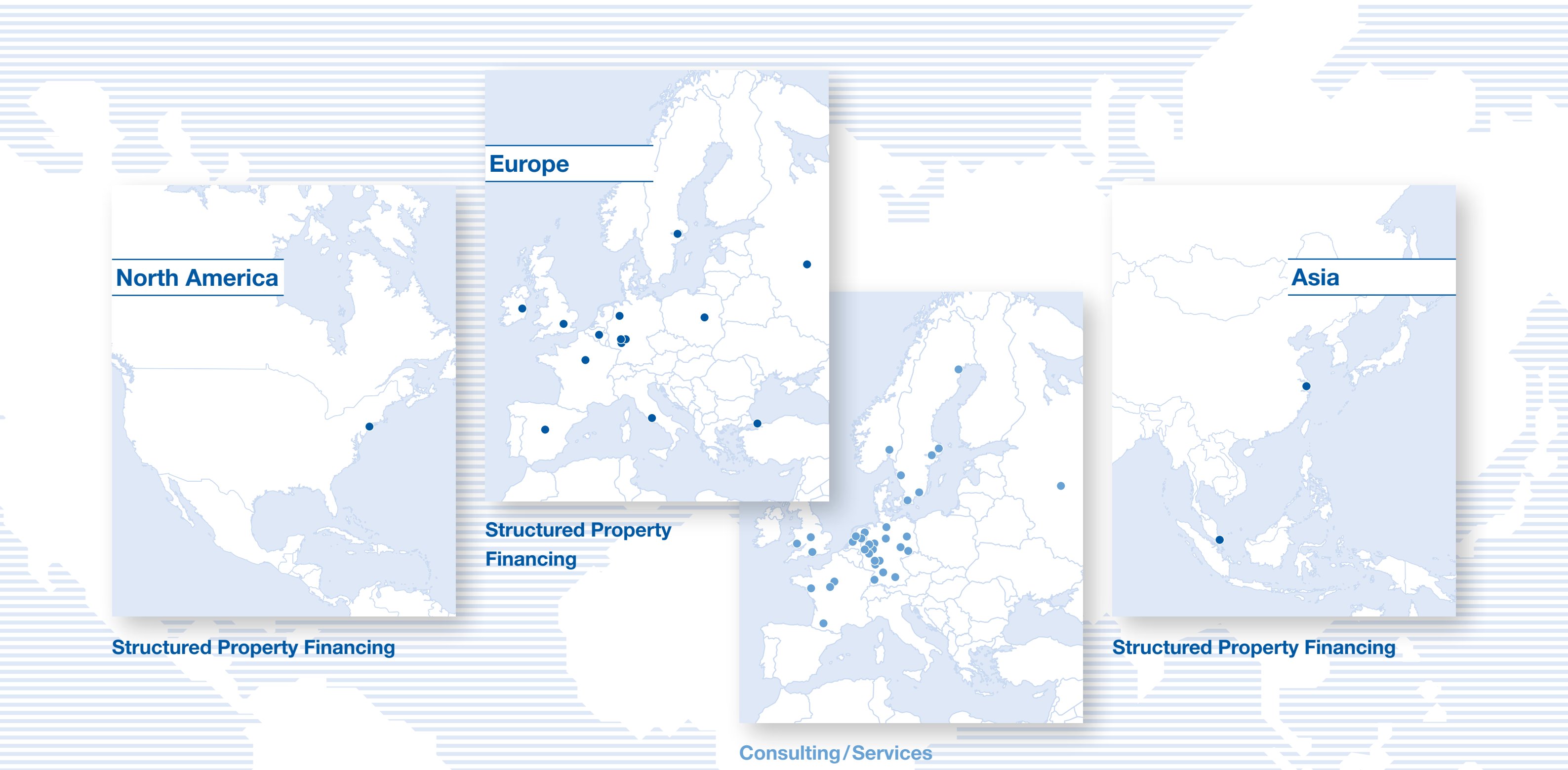
# Financial Calendar

| | |
|---|---|
| 10 November 2016 | Presentation of interim report as at 30 September 2016 |
| 31 May 2017 | Annual General Meeting – Kurhaus, Wiesbaden |

# Locations




**Aareal Bank, Real Estate Structured Finance:** Brussels, Dublin, Frankfurt/Main, Istanbul, London, Madrid, Moscow, New York, Paris, Rome, Shanghai, Singapore, Stockholm, Warsaw, Wiesbaden | **Aareal Estate AG:** Wiesbaden | **Aareal Valuation GmbH:** Wiesbaden | **Westdeutsche ImmobilienBank AG:** Mainz, Münster

**Aareal Bank, Housing Industry:** Berlin, Essen, Hamburg, Leipzig, Munich, Stuttgart, Wiesbaden | **Aareon AG:** Berlin, Coventry, Dortmund, Emmen, Enschede, Essen, Gorinchem, Hamburg, Hilversum, Hückelhoven, Karlskrona, Leipzig, Lund, Mainz, Meudon-la-Forêt, Mölndal, Munich, Nantes, Norrtälje, Orléans, Oslo, Piteå, Southampton, Stockholm, Stuttgart, Swansea, Toulouse | **Aareal First Financial Solutions AG:** Mainz | **Deutsche Bau- und Grundstücks-AG:** Berlin, Bonn, Dresden, Düsseldorf, Frankfurt/Main, Freiburg, Hanover, Leipzig, Moscow, Munich, Wuppertal

as at 30 June 2016

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08/2016

Aareal Bank Group