

Aareal Bank Group – Interim Financial Information

1 January to
30 September 2022

Contents

2	Key Indicators
4	Business Development
4	Key Events and Transactions
4	Report on the Economic Position
4	Financial Performance
6	Financial Position – Assets
7	Financial Position – Equity and Liabilities
8	Report on Changed Forecasts
9	Events after the Reporting Date
10	Segment Results
11	Financial Calendar
11	Imprint

Business Development

Key Events and Transactions

The course of the 2022 financial year and the forecast continue to be significantly influenced by the macro-economic and geopolitical environment: besides the development of the Covid-19 pandemic, the war in Ukraine has evolved into an additional uncertainty factor for the forecast. We refer to our comments in the Report on Changed Forecasts.

Nonetheless, our business performed well in all segments.

Thanks to the good opportunities presented in the Structured Property Financing segment and strong new business of € 6.9 billion, our property financing portfolio volume amounts to € 31.9 billion. We have therefore already achieved the year-end target for a portfolio size of around € 31 to € 32 billion which we increased during the course of the year. Growth was supported by corresponding funding activities and a high average deposit volume of € 13.3 billion in the Banking & Digital Solutions segment.

Aareon was successful in growing sales revenue, despite its transformation to a SaaS company. M&A transactions closed in the previous year also contributed to this rise.

Report on the Economic Position

Financial Performance

€ mn	1 Jan - 30 Sep 2022	1 Jan - 30 Sep 2021
Net interest income	514	435
Loss allowance	170	79
Net commission income	199	174
Net derecognition gain or loss	24	15
Net gain or loss from financial instruments (fvpl)	22	-7
Net gain or loss from hedge accounting	-6	-4
Net gain or loss from investments accounted for using the equity method	-2	-1
Administrative expenses	423	393
Net other operating income/expenses	-1	-17
Operating profit	157	123
Income taxes	57	67
Consolidated net income	100	56
Consolidated net income attributable to non-controlling interests	0	2
Consolidated net income attributable to shareholders of Aareal Bank AG	100	54

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	1 Jan - 30 Sep 2022	1 Jan - 30 Sep 2021
Earnings per share (Eps)		
Consolidated net income attributable to shareholders of Aareal Bank AG ¹⁾	100	54
of which: allocated to ordinary shareholders	89	44
of which: allocated to AT1 investors	11	10
Earnings per ordinary share (€) ²⁾	1.49	0.73
Earnings per AT1 unit (€) ³⁾	0.11	0.10

¹⁾ The allocation of earnings is based on the assumption that net interest payable on the AT1 bond is recognised on an accrual basis.

²⁾ 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.

³⁾ 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.

Consolidated operating profit amounted to € 157 million in the first nine months of the 2022 financial year and was thus in line with expectations and significantly higher than in the previous year (€ 123 million) as a result of the strong operating performance and even though we recognised loss allowance of € 126 million for our exposure to Russia, which is being run down.

Net interest income of € 514 million was significantly higher than in the previous year (€ 435 million), mainly due to the expected year-on-year increase in the credit portfolio and first positive effects from higher market interest rates on the deposit-taking business.

Loss allowance totalled € 170 million (9m 2021: € 79 million). This includes an addition to loss allowance of € 126 million for the Bank's exposure to Russia which is currently being run down, bringing the coverage of the outstanding exposure (of around € 210 million) to approximately 60%. The exposure could not be serviced due to the sanctions imposed in Russia (transfer risk), even though the borrower is willing and able to pay. The potential additional impact of the war in Ukraine and the economic consequences of the mutual sanctions imposed are very difficult to estimate at this point in time.

Furthermore, we moved a new LGD model for our commercial property finance portfolio (which complies with new EBA guidelines for rating procedures) into production as at the end of the first half of the year; this new model also serves as a basis for model-based Stage 1 and 2 loss allowance. The model effect due to this conversion was approximately € 10 million.

Other net additions reflected the impact of current macro-economic scenarios deployed; given the outbreak of war, these are markedly worse than at the turn of the year and are only partially offset by positive portfolio effects (maturity effects in particular). The risk of Russia potentially stopping gas deliveries to the EU altogether has been incorporated into deteriorated macro-economic forecasts.

Net commission income increased to € 199 million (9m 2021: € 174 million) on the back of higher sales revenue at Aareon and the performance of the Banking & Digital Solutions segment. Despite its transformation to a SaaS company, Aareon's sales revenue increased to € 221 million (9m 2021: € 195 million).

Aareon's adjusted EBITDA¹⁾ amounted to € 47 million (9m 2021: € 42 million). M&A activities contributed to growth in both segments.

The net derecognition gain of € 24 million (9m 2021: € 15 million) was attributable to market-driven effects from early loan repayments, and to income from the securities portfolio. De-risking measures of € 3 million had burdened results from the securities business in the previous year.

Net gain or loss from financial instruments (fvpl) and net gain or loss from hedge accounting in the aggregate amount of € 16 million (9m 2021: € -11 million) was mainly incurred by positive valuation effects resulting from market developments for currency and interest rate hedging derivatives, due to the strong market dynamics and coming from negative values at the beginning of the year. To reduce volatility in the income statement brought about by these items, the Bank had concluded additional hedging transactions in the first half of 2022.

Administrative expenses rose to € 423 million (9m 2021: € 393 million), as expected and as a result of two factors: on the one hand, business expansion, especially at Aareon; on the other hand, transaction costs incurred by the successful completion of the voluntary public offer made by Atlantic BidCo. The Bank's costs remain stable as a result of its strict cost discipline. The cost/income ratio in the banking business (which, in line with common practice in the banking sector, does not include the bank levy and contributions to the deposit guarantee scheme) improved to 39% and demonstrates Aareal Bank's high cost efficiency, even in a European comparison.

Net other operating income/expenses amounted to € -1 million (9m 2021: € -17 million). In the previous year, it was burdened by € 11 million in interest on tax back payments, as well as lower rental income on properties held by the Bank, as a result of Covid-19.

Overall, this resulted in consolidated operating profit of € 157 million (9m 2021: € 123 million). Taking into consideration income taxes of € 57 million (9m 2021: € 67 million) and non-controlling interest income of € 0 million (9m 2021: € 2 million), consolidated net income attributable to shareholders of Aareal Bank AG amounted to € 100 million (9m 2021: € 54 million). In the previous year, income taxes were burdened by a non-recurring tax effect. Earnings per ordinary share (EpS) amounted to € 1.49 (9m 2021: € 0.73), and RoE after taxes to 4.3% (9m 2021: 2.3%).

Financial Position – Assets

€ mn	30 Sep 2022	31 Dec 2021
Assets		
Financial assets (ac)	46,693	42,345
Cash funds	8,323	6,942
Loan receivables	30,753	29,434
Money market and capital market receivables	7,532	5,884
Receivables from other transactions	85	85
Loss allowance (ac)	-627	-492

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¹⁾ "Earnings before interest, taxes, depreciation and amortisation" before new products, Value Creation Programme (VCP), ventures, M&A activities and non-recurring effects.

€ mn	30 Sep 2022	31 Dec 2021
Financial assets (fvoci)	3,172	3,753
Money market and capital market receivables	3,170	3,749
Equity instruments	2	4
Financial assets (fvpl)	2,425	1,734
Loan receivables	555	598
Money market and capital market receivables	5	4
Positive market value of designated hedging derivatives	1,211	900
Positive market value of other derivatives	654	232
Investments accounted for using the equity method	21	19
Intangible assets	550	394
Property and equipment	266	278
Income tax assets	65	66
Deferred tax assets	114	168
Other assets	589	463
Total	53,268	48,728

At € 53.3 billion, Aareal Bank Group's consolidated total assets increased in comparison to the previous year-end. The property financing volume rose to € 31.9 billion (31 December 2021: € 30.0 billion). This increase was achieved in particular on the back of strong new business of € 6.9 billion (9m 2021: € 6.1 billion) generated during the first nine months of 2022 and included an amount of approximately € 620 million for "green" financings¹⁾. The volume of green financings increased to a total of € 1.9 billion (9m 2021: € 0.4 billion); in this context, some existing clients also issued the required undertaking and the related certificates for the first time.

Financial Position – Equity and Liabilities

€ mn	30 Sep 2022	31 Dec 2021
Equity and liabilities		
Financial liabilities (ac)	45,123	43,017
Money market and capital market liabilities	31,756	30,597
Deposits from the housing industry	12,814	11,717
Liabilities from other transactions	93	94
Subordinated liabilities	460	609
Financial liabilities (fvpl)	4,394	1,882
Negative market value of designated hedging derivatives	2,267	971
Negative market value of other derivatives	2,127	911
Provisions	278	558
Income tax liabilities	22	17
Deferred tax liabilities	59	56
Other liabilities	126	137

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¹⁾ "Green" financings meet the high energy efficiency requirements of the Aareal Green Finance Framework and the client undertakes to meet these requirements throughout the term of the loan.

€ mn	30 Sep 2022	31 Dec 2021
Equity	3,266	3,061
Subscribed capital	180	180
Capital reserves	721	721
Retained earnings	2,023	1,937
AT1 bond	300	300
Other reserves	-22	-143
Non-controlling interests	64	66
Total	53,268	48,728

At € 53.3 billion, Aareal Bank Group's consolidated total equity and liabilities increased in comparison to the previous year-end. The average deposit volume from the housing industry increased to € 13.3 billion in the first nine months of the year (9m 2021: € 11.9 billion).

Aareal Bank Group raised € 4.5 billion on the capital markets during the first nine months of 2022. This included six benchmark transactions: two € 750 million Pfandbrief issues, one € 625 million Pfandbrief issue and one Pfandbrief issue in the amount of € 500 million. Aareal Bank Group raised a total of € 1.3 billion in senior unsecured funding, including two 'green' senior preferred issues¹⁾ of € 500 million each.

Report on Changed Forecasts

Besides the strategic initiatives and measures within the framework of "Aareal Next Level", Aareal Bank Group's focus in the 2022 financial year will remain on coping with the impact of the Covid-19 pandemic in the best way possible – together with its clients.

A further uncertainty factor is the potential impact of the war in Ukraine, which is currently very difficult to estimate – in relation to our limited exposure in Russia as well as to the economic consequences of the imposed sanctions and escalated geopolitical tensions.

Given the strong operating performance during the first nine months of the year, Aareal Bank currently maintains its forecast for 2022 consolidated operating profit at the lower end of the range (€ 210 million to € 250 million; 2021: € 155 million) despite loss allowance of € 126 million for the exposure to Russia (currently being run down) and the impact of the ECB Governing Council's decisions on the TLTRO programme. The same applies to earnings per share (EpS), forecast in a range between € 2.00 and € 2.50 (2021: € 0.89) and RoE after taxes (4.5 % to 6 %; 2021: 2.1 %). Loss allowance (including credit risk-induced adjustments to the measurement of defaulted property loans, which are reported in net gain or loss from financial instruments (fvpl)) is projected to come out at the upper end of the range between € 140 million and € 180 million (2021: € 169 million) due to the addition to loss allowance for the exposure to Russia (currently being run down).

¹⁾ The requirements for "green" issues are set out in the Aareal Green Finance Framework.

Aareal Bank Group expects income to continue to rise significantly vis-à-vis the previous year. Net interest income is anticipated to continue its upwards trend as a result of the increase in the credit portfolio and positive effects from higher market interest rates on the deposit-taking business, thus ranging between € 660 million and € 690 million (original range: € 600 million to € 630 million; 2021: € 597 million). Net commission income should also rise significantly, thanks in particular to Aareon's growth, to between € 270 million and € 290 million (2021: € 245 million).

Due to Aareon's strong growth, administrative expenses are expected to rise above the previous year's level. As a matter of course, the original Group target did not incorporate transaction costs related to the successful completion of the voluntary public offer made by Atlantic BidCo to the shareholders, which were largely incurred during the first half of 2022. Administrative expenses are therefore expected in a range of between € 550 million and € 580 million (original range: € 540 million to € 570 million; 2021: € 528 million).

New business in the Structured Property Financing segment is still expected within the increased range of between € 7.5 billion and € 8.5 billion (previously: between € 7 billion and € 8 billion) in the 2022 financial year, so that Aareal Bank Group's property financing portfolio should amount to between € 31 billion and € 32 billion at the end of 2022, market conditions permitting and subject to exchange rate fluctuations (previously: around € 31 billion).

For the Banking & Digital Solutions segment, Aareal Bank assumes slight growth in net commission income for the core activities and continues to expect an average deposit volume from the housing industry of above € 12 billion (previously: around € 12 billion).

Aareon is expected to see a marked increase in sales revenue in the region of € 305 million to € 325 million for the current year (2021: € 269 million). Adjusted EBITDA¹⁾ is also likely to see a further increase to between € 73 million and € 78 million (2021: € 67 million).

With regard to capitalisation, Aareal Bank expects a CET1 ratio (Basel IV (phase-in)) markedly above 16 % by the end of the year, despite the planned portfolio growth and subject to further regulatory changes.

Events after the Reporting Date

On 27 October 2022, the ECB Governing Council decided to recalibrate the conditions of the existing third series of targeted longer-term refinancing operations (TLTRO III). Aareal Bank thus plans to repay around € 4.3 billion of the total amount of TLTRO refinancing of € 5.3 billion as early as in November 2022. As a result of the unilateral amendment to the contractual terms, the Bank must realise a measurement loss in a low to mid-double-digit million range in net interest income and net derecognition gain or loss, due to the interest rate hedges entered into in connection with TLTRO. However, despite these negative TLTRO implications, Aareal Bank is able to confirm the full-year operating profit forecast for 2022 amid the Bank's strong operating performance.

No other material events occurred after the end of the reporting period that need to be disclosed at this point.

¹⁾ "Earnings before interest, taxes, depreciation and amortisation" before new products, Value Creation Programme (VCP), ventures, M&A activities and non-recurring effects.

Segment Results

	Structured Property Financing		Banking & Digital Solutions		Aareon		Consolidation/ Reconciliation		Aareal Bank Group	
	1 Jan – 30 Sep 2022	1 Jan – 30 Sep 2021	1 Jan – 30 Sep 2022	1 Jan – 30 Sep 2021	1 Jan – 30 Sep 2022	1 Jan – 30 Sep 2021	1 Jan – 30 Sep 2022	1 Jan – 30 Sep 2021	1 Jan – 30 Sep 2022	1 Jan – 30 Sep 2021
€ mn										
Net interest income	475	406	49	33	-10	-4	0	0	514	435
Loss allowance	170	79	0		0	0			170	79
Net commission income	5	6	23	20	180	157	-9	-9	199	174
Net derecognition gain or loss	24	15							24	15
Net gain or loss from financial instruments (fvpl)	22	-7	0		0				22	-7
Net gain or loss from hedge accounting	-6	-4							-6	-4
Net gain or loss from investments accounted for using the equity method	0		-1	-1	-1	0			-2	-1
Administrative expenses	200	193	54	53	178	156	-9	-9	423	393
Net other operating income/expenses	-4	-21	-1	0	4	4	0	0	-1	-17
Operating profit	146	123	16	-1	-5	1	0	0	157	123
Income taxes	52	68	6	-1	-1	0			57	67
Consolidated net income	94	55	10	0	-4	1	0	0	100	56
Consolidated net income attributable to non-controlling interests	0	0	0	0	0	2			0	2
Consolidated net income attributable to shareholders of Aareal Bank AG	94	55	10	0	-4	-1	0	0	100	54
Allocated equity ¹⁾	1,622	1,677	289	260	37	38	838	562	2,786	2,537
RoE after taxes in % ²⁾³⁾	6.9	3.6	4.5	-0.1	-13.9	-3.1			4.3	2.3

¹⁾ Allocated equity is calculated for all segments on the basis of standardised capital requirements pursuant to Basel IV (phase-in) of 15%. Reported equity on the statement of financial position differs from this. Aareon's total equity as disclosed in the statement of financial position amounts to € 138 million (31 December 2021: € 143 million).

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.

Financial Calendar

2 March 2023	Preliminary results for the 2022 financial year
30 March 2023	Publication of annual report as at 31 December 2022
11 May 2023	Publication of results as at 31 March 2023
10 August 2023	Publication of results as at 30 June 2023
9 November 2023	Publication of results as at 30 September 2023

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The German version shall be authoritative.



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Group**

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