

## Report of the Supervisory Board of Aareal Bank AG, Wiesbaden

Dear shareholders,

For Aareal Bank, the 2014 financial year was characterised by a series of positive events: the Bank passed the European Central Bank's Comprehensive Assessment, fully repaid the residual amount of the silent participation provided by the German Financial Markets Stabilisation Fund (SoFFin), and further strengthened its capitalisation through the placement of Additional Tier 1 capital. Aareal Bank also successfully completed the acquisition of Corealcredit.

The Supervisory Board believes that these steps demonstrate Aareal Bank AG's solid position and affirm the Company's strength. Consolidated operating profit for the 2014 financial year – including € 154 million in negative goodwill from the acquisition of Corealcredit – was € 436 million and therefore more than double the previous year's figure.

The Supervisory Board again considers Aareal Bank AG's repeated positive results as evidence for the long-term viability of the Group's business model and its operative strength.

During the financial year under review, the Supervisory Board continually advised, monitored, and supervised the management of the Company. The Management Board informed the Supervisory Board regularly, without delay and comprehensively, both orally and in writing, upon all the issues important to the Bank. The Management Board reported on the Group's situation, business development, key financial indicators and market developments. In addition, detailed reports and explanations were given to the Supervisory Board regarding the current liquidity status and liquidity management

measures taken, the prevailing risk situation, and on risk control and risk management measures taken within the Group. The Supervisory Board also received comprehensive reports on the development of business segments, and on operative and strategic planning. The Supervisory Board was informed about, and involved in, all important decisions. All material events were discussed and examined in detail; where a Supervisory Board resolution was required, the decision proposals were submitted to the Supervisory Board and a decision taken. In cases where resolutions needed to be passed in between scheduled Supervisory Board meetings, such resolutions were passed by way of circulation or via conference calls.

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

## Activities of the plenary meeting of the Supervisory Board

Seven plenary meetings of the Supervisory Board were held during the year under review, of which five were scheduled meetings. During the meetings, the members of the Supervisory Board received reports and explanations from the members of the Management Board, and discussed these in detail. One of the focal working and reporting aspects during all scheduled meetings was the approach to be taken by the Bank towards the changing market environment.

In its discussions, the Supervisory Board also concerned itself with changes to the regulatory framework, in great detail. During the year under review, this included the decisions to establish a uniform European Banking Authority under the auspices of the European Central Bank and the previous Comprehensive Assessment as well as the amendment of the German Regulation on Remuneration in Financial Institutions (Instituts-Vergütungsverordnung – "InstVergV").

Throughout the financial year, in the course of all meetings as well as during the periods between meetings, the Management Board informed the Supervisory Board about economic and market developments and their potential impact on Aareal Bank Group, in a timely, complete and comprehensible manner. This included detailed explanations of the appropriate measures taken in response to the challenges arising from general market developments, in particular the prevailing low interest rate environment.

During the scheduled plenary meetings of the Supervisory Board, the Management Board reported to the Supervisory Board regularly and comprehensively; these reports also covered the development of the Structured Property Financing and Consulting/Services segments, focusing on current economic developments. At regular intervals, the Supervisory Board was informed of the Bank's liquidity status and the related steps taken by the Bank's Treasury. In addition, the Supervisory Board was informed about the business development

of the entire Aareal Bank Group, on the basis of actual figures and projections. The Management Board also reported regularly on the quality of the property financing portfolio, against the background of general market trends and expected changes on the various property markets.

The focal points of the various Supervisory Board meetings are presented below:

The extraordinary meeting in January focused on the implementation of the amendments to the German Regulation on Remuneration in Financial Institutions (InstVergV). Matters pertaining to the financial statements were discussed in the extraordinary meeting in February.

In the March meeting, the Supervisory Board concerned itself in detail with the financial statements and consolidated financial statements presented for the 2013 financial year, and with the auditors' report. The relevant facts were presented in the Supervisory Board report for the previous year. In addition, the proposal regarding the selection and subsequent appointment of the external auditor for the Annual General Meeting was discussed. This also included the scope and focal points of the audit for the 2014 financial year, as defined by the Supervisory Board. Other issues covered in the meeting in March included the preparations for the Annual General Meeting in May 2014. This meeting also discussed the annual reports submitted by Internal Audit and by the Compliance Officer.

The purpose of the May meeting of the Supervisory Board was to follow up on the Annual General Meeting of Aareal Bank AG, which preceded the meeting.

One meeting in July focused mainly on Aareal Bank Group's strategic options, and on the challenges presented in the prevailing market environment.

During the September meeting, corporate governance issues were presented and discussed, alongside other regulatory issues. The discussions on the Bank's strategic options were continued.

In the December meeting, the Management Board reported on the Group's corporate planning. The Management Board submitted and explained the corporate planning in detail to the Supervisory Board. Corporate governance issues were discussed as well: The requisite resolutions were passed and implemented. Furthermore, the Supervisory Board adopted the regular Declaration of Compliance, pursuant to section 161 of the German Public Limited Companies Act (Aktiengesetz – "AktG"), which was subsequently published on the Bank's website.

Following the new regulations of sections 25c and d of the German Banking Act (Kreditwesengesetz – "KWG"), the Supervisory Board carried out the required evaluations. The results of the evaluation conducted during the 2014 financial year were acknowledged by the members of the Supervisory Board, and were discussed in detail.

Strategy documents were regularly submitted to, and discussed by the Supervisory Board, in accordance with the Minimum Requirements for Risk Management in Banks (MaRisk). The results of the regular review of the Company's remuneration system were reported to the Supervisory Board. The Supervisory Board determined that the Company's remuneration system is appropriate.

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

Any Supervisory Board decisions which were taken by way of circulation were discussed at the subsequent meeting, to ensure that the members were able to reconcile the implementation of such decisions.

As part of preparing Supervisory Board decisions, a routine examination is carried out as to whether there are any conflicts of interest. No potential conflicts of interest that would need to be considered in the context of decision-making processes were identified during the financial year under review. The members of the Supervisory Board have declared

in writing that no conflicts of interest pursuant to section 5.5.2 of the Corporate Governance Code arose during the financial year under review.

In addition to its regular meetings, the Supervisory Board convened for a separate meeting during which auditors PricewaterhouseCoopers provided information on current changes and deliberations in the regulatory and legal framework.

### Activities of Supervisory Board committees

The Supervisory Board has established five committees in order to perform its supervisory duties in an efficient manner: the Executive and Nomination Committee, the Risk Committee, the Committee for Urgent Decisions, the Audit Committee, and the Remuneration Control Committee.

The Executive and Nomination Committee of the Supervisory Board convened for seven scheduled meetings and two extraordinary meetings. In the scheduled meetings, the Executive and Nomination Committee prepared the proposed resolutions of the plenary meetings of the Supervisory Board. The ATI bond issue was discussed in one of the extraordinary meetings. Three meetings were held without the participation of the employee representative and the Management Board, since these meetings were concerned with the nomination process of shareholder representatives on the Supervisory Board to be elected at the 2015 Annual General Meeting.

The Risk Committee held four meetings during the year under review. The Management Board submitted detailed reports to the committee, covering all markets in which the Bank is active in the property finance business, as well as supplementary reports regarding the Bank's investments in securities portfolios. The committee members discussed these reports and market views in detail. The committee discussed the banking and regulatory environment of the Bank. The committee also regularly dealt with loans requiring approval, and transactions subject to reporting requirements.

The committee discussed individual exposures of material importance to the Bank, which were presented and explained by the Management Board. In addition, reports on current political developments were provided to the committee, together with appropriate responses. Also, detailed reports were given regarding the Bank's liquidity status and management as well as its funding.

The committee regularly discussed reports on the Bank's risk situation, which were submitted and explained by the Management Board. Having discussed the contents with the Management Board, these were duly noted and approved by the members of the committee. Besides credit and country risks, the committee concerned itself with market risks, liquidity risks, and operational risks. The committee concerned itself with the risk-bearing capacity and the capital ratios of Aareal Bank, as well as with the introduction of a Single Supervisory Mechanism (SSM) under the auspices of the ECB. The committee also decided on any other transactions requiring the Supervisory Board's approval pursuant to the Company's Memorandum and Articles of Association or the internal rules of procedure.

The Committee for Urgent Decisions is a sub-committee of the Risk Committee. It approves loans subject to approval requirements by way of circulation; for this reason, it did not hold any meetings. Any decisions which were taken between meetings of the Risk Committee were discussed at the subsequent meeting.

The Audit Committee held six meetings during the year under review. During its meeting in February 2014, the Audit Committee received and discussed the preliminary results for the 2013 financial year. During its March meeting, the committee received the external auditors' report on the 2013 financial year and discussed the results with the auditors in detail. The committee members read the audit reports provided; they formed their own judgement of the audit results on the basis of these reports, and by way of meetings held with the external auditors. In accordance with its duties under the Memorandum and Articles of Association, the

Audit Committee also discussed the selection of external auditors and the focal aspects of the audit for 2014 during the same meeting.

Proceedings at the meetings in August and November included information given to the committee on supplementary topics, such as measures to implement changed regulatory requirements. In addition to a report on the audit progress, the Management Board presented and explained the updated Group planning to the committee during its December meeting. The committee also received reports submitted by Internal Audit and by the Compliance Officer, requesting and receiving detailed explanations. It discussed and duly noted the review of the internal control system, which was carried out in accordance with applicable law.

Furthermore, during the committee meetings in February, May, August and November 2014, the Management Board presented the quarterly results for the financial year, as well as the preliminary full-year results for 2013 prior to publication, in accordance with the German Corporate Governance Code; the committee members discussed the reports with the Management Board. As in the financial year under review, the preliminary results for 2014 were discussed at a meeting in February 2015.

In its meeting on 19 March 2015, the Audit Committee received the external auditors' detailed report on the audit and audit results for the 2014 financial year, and discussed these results extensively with the auditors and the Management Board.

During its nine meetings, the Remuneration Control Committee discussed the implementation of the amendments to the German Regulation on Remuneration in Financial Institutions (InstVergV) as well as all issues related to remuneration, fulfilling its original assignment.

Where members of the Supervisory Board were unable to attend a meeting, they had announced their absence in advance, giving reasons. If material decisions were on the agenda, these Supervisory Board members submitted written instructions for

the casting of their votes, or cast their votes afterwards, in writing. Attendance of Supervisory Board members at meetings is shown in the table below.

<b>Member of the Supervisory Board</b>	<b>Number of meetings attended/ number of meetings (plenary and committee meetings)</b>
Marija G. Korsch	35 of 35
Erwin Flieger	29 of 29
York-Detlef Bülow *	28 of 28
Christian Graf von Bassewitz	15 of 17
Manfred Behrens	7 of 7
Thomas Hawel *	7 of 7
Dieter Kirsch *	20 of 20
Dr Herbert Lohneiß	11 of 11
Joachim Neupel	17 of 17
Richard Peters	7 of 7
Prof Dr Stephan Schüller	23 of 31
Helmut Wagner *	7 of 7

\* employee representative

## **Financial statements and consolidated financial statements**

The Supervisory Board instructed PricewaterhouseCoopers Aktiengesellschaft Wirtschaftsprüfungsgesellschaft, Frankfurt/Main, who were elected as auditors by the Annual General Meeting 2014, with the audit of the financial statements. The external auditors appointed submitted a statement regarding their independence to the Supervisory Board, who duly noted it. The Supervisory Board has no reason to doubt the accuracy of this statement of independence. Fulfilling their duties as commissioned by the Supervisory Board, PricewaterhouseCoopers Aktiengesellschaft Wirtschaftsprüfungsgesellschaft audited the financial statements prepared in accordance with the German Commercial Code (HGB) and the consolidated financial statements prepared in accordance with IFRSs, as well as the Management Report and the Group Management Report. Based on the results of their audit, PricewaterhouseCoopers Aktiengesellschaft Wirtschaftsprüfungsgesellschaft issued an unqualified audit

opinion for the financial statements and consolidated financial statements.

All members of the Supervisory Board received the audit reports regarding the financial statements and the consolidated financial statements, including all annexes thereto, in good time before the meeting during which the audit results were discussed. Having examined the documents provided, the Supervisory Board members formed their own judgement of audit results. The representatives of the external auditor participated in the meeting of the Supervisory Board, during which the financial statements were discussed, and gave a detailed account of the results of their audit. The representatives of PricewaterhouseCoopers Aktiengesellschaft Wirtschaftsprüfungsgesellschaft were available to the Supervisory Board to answer further questions, and to provide additional information. All questions were answered to the full satisfaction of the Supervisory Board.

The financial statements and management report of Aareal Bank AG, prepared in accordance with the HGB, and the consolidated financial statements prepared in accordance with IFRSs, and the proposal of the Management Board regarding the appropriation of profit, and the audit report, were all examined in detail. No objections were raised to the audit results. In its meeting on 25 March 2015, the Supervisory Board approved the results of the audit. The Supervisory Board approved the financial statements and Management Report of Aareal Bank AG, prepared in accordance with the HGB, together with the consolidated financial statements and the Group Management Report prepared in accordance with IFRSs, and thus confirmed the financial statements of Aareal Bank AG. The Supervisory Board examined and discussed with the Management Board its proposal regarding the appropriation of profit. On the basis of the discussion, the Supervisory Board endorsed the proposal for the appropriation of profit submitted by the Management Board.

## Special transactions

On 22 December 2013, Aareal Bank Group acquired all of the shares of Corealcredit Bank AG, Frankfurt/Main, which specialises in commercial property financing in Germany. A corresponding agreement was concluded on 31 March 2014 (closing). The integration of Corealcredit into Aareal Bank Group was largely completed by year-end 2014.

Another important milestone was BaFin's consent to the Bank fully repaying the remaining SoFFin silent participation. The Bank thus repaid the residual amount of €300 million to SoFFin on 30 October. With the full repayment of the silent participation, SoFFin's support to Aareal Bank has therefore come to an end. The Management Board and Supervisory Board are deeply grateful to the German Federal Government, the German parliament, and to SoFFin. The decision, taken in the year 2009, to support our work in times of great uncertainty, contributed to secure the Bank's fully viable business model, in a difficult market phase. This allowed Aareal Bank – as a perfectly healthy institution, as it was back then, and continues to be – to remain on its successful path undeterred, even in a market situation that had dramatically intensified at times.

On 3 February 2015, Aareal Holding Verwaltungsgesellschaft mbH placed its 28.9 % stake in Aareal Bank AG's issued share capital with investors, in an accelerated book-building process. Market interest was very high, offering clear proof of the investment attraction of Aareal Bank shares. With the full repayment of the remaining SoFFin silent participation at the end of October 2014, the Holding's formal requirement to hold a blocking minority interest was terminated. The Supervisory Board fully confirms the Management Board's gratitude regarding the shareholders of Aareal Holding Verwaltungsgesellschaft, appreciating their constructive support of Aareal Bank over the years, in particular during the turbulent times following the financial crisis in 2007.

On 22 February 2015, Aareal Bank Group announced the acquisition of all of the shares of Westdeutsche ImmobilienBank AG ("WestImmo"), which specialises in commercial property financing. Following the acquisition of Corealcredit in the spring of 2014, Aareal Bank has once again effected a targeted investment in its core Structured Property Financing business by acquiring WestImmo, expanding its strong position on key target markets. The Supervisory Board is convinced that the Bank exploited another promising opportunity with this acquisition.

In conclusion, the Supervisory Board would like to thank the Management Board and all of the Group's employees for their strong commitment during the eventful 2014 financial year. That commitment – and strong motivation – from all employees of Aareal Bank Group made the Company's success possible, and thus enabled the Bank to successfully master the challenges of recent months.

**Frankfurt, March 2015**

**For the Supervisory Board**



**Marija G. Korsch (Chairman)**