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2013

Aareal Bank AG – Annual Report 2013

Aareal Bank

Management Report

Fundamental information about the Group

The Group's business model

Aareal Bank AG, headquartered in Wiesbaden, Germany, is the parent company of the Group. Its shares are admitted to listing and trading on the regulated market (*Geregelter Markt*) of the Frankfurt Stock Exchange, and are included in the mid-cap MDAX® index. Aareal Bank Group provides financing as well as advisory and other services to the housing industry and the commercial property sector. It supports German and international clients, as a financing partner and service provider.

Aareal Bank is a member of the Association of German Banks (BdB) and the Association of German Pfandbrief Banks (vdp).

Aareal Bank Group's business model comprises two segments:

Structured Property Financing

The Structured Property Financing segment comprises all of the property financing and refinancing activities.

In this segment, Aareal Bank facilitates property projects for its domestic and international clients, and is active in this respect in Europe, North America and Asia. It offers commercial property financing solutions, especially for office buildings, hotels as well as retail, logistics and residential properties. The Bank's particular strength lies in it successfully combining local market expertise and sector-specific know-how. In addition to local experts, the Bank also has industry specialists at its disposal, to create financing packages for logistics properties, shopping centres and hotels. This enables Aareal Bank to offer tailor-made financing concepts that meet the special requirements of our national and international clients. What makes Aareal Bank special are its direct client relationships, which – in very many cases – it has maintained for many years.

Aareal Bank has a broad and solid refinancing base. It has established itself as an active issuer of Pfandbriefe, which account for a major share of the Bank's long-term funding. The quality of the cover assets pools is also confirmed by the "AAA"- rating of Aareal Bank's Pfandbrief issues. To cater to a broad investor base, Aareal Bank covers a wide range of other refinancing tools, including promissory notes and debt securities. Private placements are the focal point of our capital market activities. These are complemented by larger, public placements that are issued depending on market conditions. The Bank also generates deposits from the housing industry, which represent a strategically important additional source of funding. Furthermore, it has recourse to institutional money market investor deposits. The success of our capital and money market activities, and the business with housing industry clients, are the results of a combination of a sustainable business model with a sound understanding of the capital markets, and the quality of the cover assets pool.

Consulting/Services

The Consulting/Services segment offers the housing industry and the commercial property sector services and products for managing property portfolios and processing payment flows. Within this segment, our subsidiary Aareon AG and the Bank's Housing Unit work together closely.

We operate the IT systems consultancy and related advisory services for the housing industry and the commercial property sector through our Aareon AG subsidiary, which looks back at almost 60 years of experience. Aareon pursues a multi-product strategy that covers the requirements of all client groups in this segment. It is active in many European countries, with Germany being its core market. The ERP (enterprise resource planning) product portfolio for efficient process planning comprises Wodis Sigma, SAP® solutions and Blue Eagle, as well as the GES system. Aareon's international subsidiaries also offer ERP systems that are tailored to meet the needs of the respective market. These are Prem'Habitat and PortalImmo Habitat in France, QL in UK and SG|tobias and the new product generation SG|tobias^{AX} in the Netherlands. Sweden's Incit AB, which is also represented in the Netherlands and in Norway, offers the ERP system Incit Xpand. Clients can use Aareon's ERP solutions in different operating systems, depending on the product: software as service provided through the exclusive Aareon Cloud, ASP (application service providing), hosting and in-house. ERP solutions and integrated services, together with additional services, support the process-efficient cooperation between property companies and their business partners. The integrated services are incorporated directly in the ERP solutions and use the same database. These include the Mareon service portal, the Aareon invoicing service, Aareon Archiv kompakt, insurance management with BauSecura, CRM (customer relationship management) solutions and mobile services. This range is complemented by sector-specific advisory services for all products and services.

In the Housing Unit, Aareal Bank operates the automated mass payments system BK01, where it assumes management of the payment transactions and account maintenance for its clients in Germany, integrating both within their IT systems. The Housing Unit's clients are from the residential and commercial property sector, as well as from the utilities and waste disposal industry. The settlement of payment transactions via Aareal Bank generates deposits that contribute significantly to Aareal Bank Group's refinancing base.

Management system

Aareal Bank Group is managed with the aid of indicator-based management tools that are designed and differentiated specifically by segment.

In addition to return and productivity management tools and the risk management system described in the risk report, we particularly use the equity base and profitability at Group level as central performance parameters to manage and monitor our business. Our extensive risk management system is of great importance to us.

Aareal Bank Group manages its Group entities and their individual risk positions centrally. All management-relevant information is systematically collected and analysed to develop suitable strategies for risk management and monitoring. We also employ forecasting models for balance sheet structure, liquidity and portfolio development for strategic business and revenue planning.

In addition to business-related management tools, we also use other instruments to optimise our organisation and workflows. These include comprehensive cost management, centralised management of project activities and Human Resources controlling, for example.

Structured Property Financing also deploys supplementary management tools and indicators. For example, we manage our new lending business in this segment using lending policies which are specific to property type and country, and which are monitored during the lending process.

The property financing portfolio as a whole is actively managed throughout Aareal Bank Group, with the aim of optimising its risk diversification and profitability. To develop risk and return-oriented strategies for our portfolio, we evaluate market and business data, using this as a basis to simulate potential lending strategies, and to identify a target portfolio, which is part of Group planning. This helps us to identify – and to respond to – market changes at an early stage. Active portfolio management makes it possible for us to optimally allocate equity to the most attractive products and regions from a risk/return perspective, within the scope of our three-continent strategy. By taking into consideration maximum allocations to individual countries, products and property types, we ensure a high level of diversification and avoid risk concentrations.

In the Consulting/Services segment, management of the Group entities allocated to the segment is oriented on specific indicators, primarily earnings before interest and taxes (EBIT), depending on each entity's business focus. We also use specific performance indicators that are typical for consulting and services in the IT business, the focus of this segment. These include indicators relating to regular client satisfaction surveys, as well as capacity utilisation indicators in the consultancy business. The volume of deposits is a key performance parameter in the Housing Unit.

Report on the economic position

Macro-economic environment

The macro-economic environment in 2013 was defined by muted economic development. The easing on the financial and capital markets that had already started in the previous year continued. The willingness of the ECB – already stated in 2012 – to buy bonds on the secondary market under certain conditions largely contributed to this recovery. However, uncertainty remained about the further development of the European sovereign debt crisis. Cautious investment activities of companies and reluctance in private household consumption burdened economic development, particularly in Europe.

Economy

At 2.2 %, global economic growth in 2013 was marginally lower than the year before (2.3 %), albeit with considerable differences amongst the individual regions.

Real economic output in the euro zone fell slightly in the year under review; the start of the year in particular was defined by a negative economic trend. Although the economic situation improved during the remainder of the year and the euro zone succeeded in emerging from recession in the second quarter, economic development remained muted. Private consumption as well as corporate investments in the euro zone declined in the year under review. However, exports generated slightly positive impulses. Besides uncertainty in conjunction with the European sovereign debt crisis, a restrictive fiscal policy and the high level of unemployment in numerous countries particularly hampered macro-economic demand. In addition, demand in various countries such as the Netherlands, Spain and Portugal was burdened by private household efforts to lower debt levels. Falling housing prices also impacted on consumption in some countries, such as the Netherlands.

The recession experienced in the previous year by the southern member states, which were particularly affected by the sovereign debt crisis and the measures taken to consolidate the budgets continued. This included Italy and Spain. However, a trend towards stabilisation emerged in Italy and Spain in the second half of the year. In Finland and the Netherlands, real gross domestic product fell in 2013, as was the case the year before. In Belgium and France, real economic output was virtually stable, while the economies of Germany, Luxembourg and Austria grew marginally.

In contrast, the economy in various countries outside the euro zone was more positive. Real gross domestic product increased slightly to moderately in UK, Poland, Sweden and Switzerland. It improved slightly in Denmark. Even though real economic output in the Czech Republic fell significantly year-on-year, the recession was overcome in the course of the year. Russia experienced slight economic growth, albeit at a significantly lower rate than the year before. At the same time, the Turkish economy grew faster than in the previous year.

Real economic output rose moderately in the US and was supported by increases in private consumption, investments and exports. Recovery trends on the housing markets and the highly expansive monetary policy are likely to have supported the economy. At the same time, public sector demand had a dampening effect. The economy in Canada also grew moderately. Mexico's economic output increased slightly year-on-year but experienced interim periods of weakness.

Real economic output in China grew at the same pace as the year before. Housing prices rose again significantly, which is why the government intervened with, for example, a ban on second home ownership in certain cities. Real gross domestic product grew moderately in Japan. The expansive monetary and financial policy, as well as improved international competitiveness brought about by exchange rate effects, played a role here.

Annual rate of change in real gross domestic product in %

	2013	2012		2013	2012		2013	2012
Europe						***North America***		
			Other european countries					
Euro zone	-0.4	-0.6	Czech Republic	-1.4	-0.9	Canada	1.7	1.7
Austria	0.3	0.7	Denmark	0.4	-0.4	Mexico	1.3	3.7
Belgium	0.2	-0.1	Poland	1.4	2.0	USA	1.7	2.8
Finland	-0.9	-0.8	Russia	1.2	3.5			
France	0.1	0.0	Sweden	0.8	1.3	***Asia***		
Germany	0.5	0.9	Switzerland	1.9	1.0			
Italy	-1.8	-2.6	Turkey	4.2	2.2	China	7.6	7.7
Luxembourg	0.8	0.3	United Kingdom	1.9	0.3	Japan	1.7	1.4
Netherlands	-1.0	-1.3				Singapore	3.7	1.3
Portugal	-1.5	-3.2						
Spain	-1.2	-1.6						

The situation on the labour markets remained difficult in many European Union (EU) countries. Unemployment rose again in the euro zone, particularly at the start of the year. A trend towards stabilisation was evident as the year progressed, and the unemployment rate had increased only slightly to 12.1 % by the year-end. At 27 %, unemployment was particularly high in Spain, although the increase levelled off during the year. The unemployment rate in Italy was clearly lower at 12.7 %, but it rose continuously over the course of the year. At 10.8 % and 10.2 % respectively (each at year-end), France and Poland also featured high unemployment rates. Unemployment was low, however, in Germany, Luxembourg and Austria.

The unemployment rate steadily declined in the US during the year to reach 7.0 % at year end. The trend in unemployment showed a slight fall, with minor fluctuations, in Japan.

Sovereign debt crisis

The sovereign debt crisis eased in individual European countries during 2013. Still, it remained a key issue in the macroeconomic environment, where it not only impacted on the economy but also on the financial and capital markets.

As a consequence of the sovereign debt crisis, we have seen – for quite some time now – a segmentation of financial and capital markets in the euro zone into countries with low sovereign bond yields and those in the periphery with significantly higher yields. This did not change in the year under review, although the yield differentials decreased considerably. Yields on both Italian and even more so on Spanish government bonds fell significantly. At the same time, low-yielding countries such as Germany and France saw slightly rising yields. The reduction in risk premiums was a clear sign for an easing of the sovereign debt crisis, whereby the ECB's willingness to buy government bonds under certain circumstances, contributed significantly. Italy and Spain also succeeded in placing rather significant volumes of bonds on the financial and capital markets.

In spring, the focus had shifted to the issue of providing support to Cyprus and measures to save the country from bankruptcy. As a consequence, Cyprus was provided with support in the form of loans from the European Stability Mechanism (ESM) funds and the International Monetary Fund (IMF). During the latter part of the year, Greece's high debt level revived the discussion about further support measures for the country. Ireland exited the European rescue programme in December 2013. Having succeeded in expanding its capital market access already in the second half of 2012, it now fully refinances itself independently on the capital markets.

By mid-year, the euro zone representatives agreed on regulations on how to recapitalise banks directly from the ESM. This regulation would only apply to systemically relevant banks that can be restructured, that no longer have access to private capital, and whose home country could not provide the aid alone.

In the US, the government debt ceiling was once again a very important issue in the year under review. In mid-October, the parties succeeded in arriving at a compromise, only shortly before this limit was reached. This compromise provided for a short-term suspension of the limit until 7 February 2014 and a subsequent increase in the liabilities that have meanwhile accumulated.

Financial and capital markets, monetary policy and inflation

The situation on the financial and capital markets eased noticeably in the year under review compared with previous years. This afforded banks, companies and countries the opportunity to place securities at favourable terms.

Pfandbrief issues and other European covered bonds benefited from the steady recovery of the markets. Investor demand was strong already at the beginning of the year and certain risk premiums fell by the end of the year, in some cases sharply. In particular, covered bonds from the periphery countries benefited from this spread tightening, with Spain achieving the best performance amongst these countries.

The volume of outstanding German Pfandbriefe has fallen since 2000 and new issuance in this product has declined significantly for some years now, driven by the development concerning Public Sector Pfandbriefe. A reason for the declining volume was the greater reduction of assets and the decision taken by some competitors to suspend business activities entirely. The latter particularly affected the public sector finance business segment, which was due in part to regulatory requirements. At the same time, the volume of outstanding and new Mortgage Pfandbrief issues was almost stable.

Another trend seen in 2013 was smaller issue sizes. The share of issues sized at less than € 1 billion increased to almost 60 % in the year under review, compared with a figure of only approximately 40 % in 2012. This was due to, among other things, stricter asset/liability and rating requirements, as well as the still-high level of liquidity provided by the ECB.

Of late, the rating agencies' requirements were raised continuously and have become much more complex: the risk of mismatching between the payment flows from the outstanding covered bonds and the cover asset pools, which the agencies have frequently criticised as material, has led to higher over-collateralisation requirements in the recent past.

In the year under review, numerous commercial banks repaid significant sums from the ECB's three-year refinancing operations. Aareal Bank also took advantage of the good liquidity situation to repay the € 1 billion raised within the scope of the ECB's three-year tender – in full – during the first quarter of 2013. Funds held by commercial banks with the ECB or the euro zone's national central banks fell considerably during the course of the year. This also reflects the easing situation on the financial and capital markets.

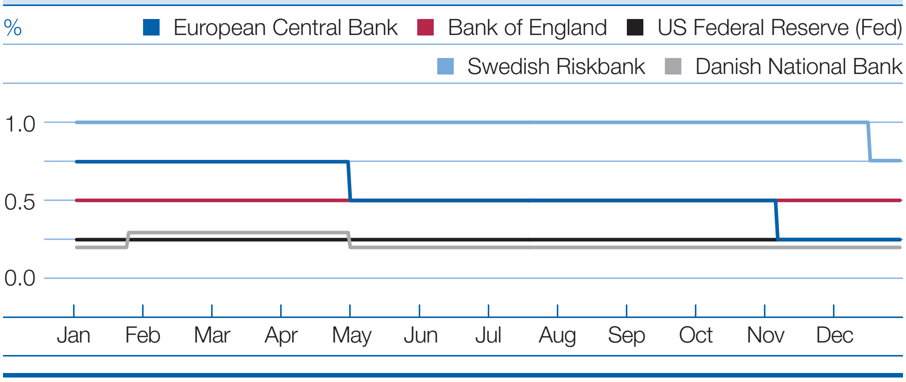
Compared to the beginning of the year, the euro exchange rate – associated with some fluctuation in the course of the year – was higher at year-end against almost all the important currencies in which we are active. These include the pound sterling, the Swedish krona and the US dollar. Euro appreciation against the Japanese yen and the Canadian dollar was particularly pronounced. As an exception to this trend, the euro exchange rate changed little against the Danish krone, as the Danish central bank aims to maintain a stable krone against the euro.

The aforementioned segmentation of the financial and capital markets between the individual countries must be taken into consideration when analysing interest rate developments. Long-term interest rates[1] rose in almost all the important currencies we are active in. The greatest increases were seen in pound sterling, Canadian dollar and US dollar. However, interest rates could still be classified as low in the various currencies. Long-term interest rates in Japan – which are close to zero – hardly changed. Short-term interest rates[2] were largely stable for most of the currencies observed. Only the Swedish krona eased slightly.

Most central banks continued to pursue an expansive monetary policy during the year under review. In this context, we would like to mention the extensive purchases by the Fed of mortgage-backed notes from state-supported issuers and longer-term US Treasuries, which continued throughout the entire year. Market participants' expectations as to whether a reduction ('tapering') of such purchases would take place during 2013 led to higher interest rates, especially in the US, but in other markets as well. In the UK, the Bank of England's Funding for Lending scheme (FLS), which was launched in 2012 to support the private housing property market, came to an end. However, the lending programme for corporate financing was extended until the start of 2015.

Numerous central banks held their key interest rates unchanged or marginally changed at a low level. The ECB lowered the key interest rate by 0.25 percentage points at both the start of May and in November to a level of 0.25 %. The applicable rate of interest for the deposit facility was left unchanged at 0.00 %. Denmark's central bank lowered its key interest rate by 0.10 percentage points to 0.20 %, having increased the rate by the same amount in January. The Swedish Riksbank reduced its key rate by 0.25 percentage points to 0.75 % in mid-December.

Key rate developments in 2013



Inflation was moderate in many countries. Annual average inflation in the euro zone fell considerably, both during the year under review and in comparison with the previous year, to 1.4 %. Inflation in the US was at a similar level, while it hovered close to the zero per cent mark in Japan. Higher rates of inflation were registered in the emerging economies. At 2.7 %, Chinese inflation was at the previous year's level, while it reached levels of 6 % and 7 % respectively in Russia and Turkey.

Regulatory environment

The emphasis in the banking sector remains on the various regulatory and reform measures. Many measures were adopted during the period under review, while others were still being discussed or prepared. The question as to what the cumulative impact will be for banks and the real economy has yet to be answered. The focus shifted in particular to the extensive ECB comprehensive assessment, which includes a regulatory risk assessment, an asset quality review and a stress test. The implementation of the assessment at all banks which will come under direct ECB supervision began before the responsibility for supervision was transferred to the ECB; the assessment will last until autumn 2014.

[1] Calculated on the basis of the 10-year swap rate
[2] Calculated on the basis of the 3-month Euribor/LIBOR, or comparable rates (depending on the currency)

The environment in which the banks were operating continued to be defined in recent years by a rapid rise in regulatory requirements. These include the comprehensive Basel II framework and its implementation in the EU (CRD I), the implementation of the "Sydney Press Release" in the EU and the revision of the regulation on large-volume loans (CRD II), the implementation of the short-term package of measures of the Basel Committee (CRD III) and the Basel III reform package (CRR/CRD IV), their implementation in national law, as well as the various amendments to the Minimum Requirements for Risk Management (MaRisk).

Sector-specific and business developments

Structured Property Financing segment

During the year under review, we continued to adhere to our risk-aware approach to lending, whilst also consistently managing our credit portfolio.

New business originated amounted to € 10.5 billion (2012: € 6.3 billion) and therefore significantly exceeded the original target of € 6 billion to € 7 billion. This was against a background of a more active transaction environment, characterised by higher liquidity than we had originally expected. This presented greater opportunities for new business on the one hand, of which we took advantage from the start of the year onwards. On the other hand, it was associated with higher and partially early repayments[3]. Repayments amounted to € 4.5 billion in the 2013 financial year (2012: € 3.0 billion). Based on the portfolio at year-end 2012, this represents a repayment ratio of 19.1 % (2012: 12.5 %).

A portion of the property financing portfolio has been committed in foreign currencies. Exchange rate fluctuations impacted on the performance of the euro equivalent of the portfolio volume. The property finance portfolio fell by approximately € 380 million during 2013, due to such fluctuations.

On account of this development, the volume of Aareal Bank Group's property finance portfolio rose by 5.3 % to € 24.5 billion as at 31 December 2013 (2012: € 23.3 billion).

The volume of loans included in cover for Pfandbriefe increased further during the year under review. It amounted to € 11.5 billion as at 31 December 2013 (2012: € 10.7 billion). This equates to an increase of approx. 7.5 %.

The share of newly-originated loans in total new business amounted to 61.6 % in the year under review (2012: 47.2 %).

At 75.7 % (2012: 75.5 %), we achieved the highest share of new business in Europe, followed by North America with 20.7 % (2012: 22.0 %) and Asia with 3.6 % (2012: 2.5 %)[4]. We generate new business through our regional sales units as well as through our teams of sector specialists covering financing solutions for shopping centres, logistics and hotel properties.

Our new business in 2013 was also broadly diversified in terms of property type. Office properties accounted for the largest share with 36.4 % (2012: 39.8 %), followed by retail properties with 26.5 % (2012: 22.1 %) and hotels with 21.2 % (2012: 20.0 %). The shares of logistics properties at 7.9 % (2012: 10.1 %), housing properties at 5.7 % (2012: 5.2 %) and other financings at 2.3 % (2012: 2.8 %) were considerably lower than the aforementioned property types.

Competition on the market for commercial property finance intensified noticeably compared with the previous year and increased during the course of the year under review.

Particularly in the business of financing first-class properties in corresponding locations and with low loan-to-value ratios, competition was pronounced for many markets in Western and Northern Europe. In addition, there was a marked increase in the willingness to fund project developments, large-volume projects and properties outside of the prime locations, even though competition was less intense in these areas. In general, the finance providers proved more willing to accept higher loan-to-value ratios and lower margins from the clients. Competition in Eastern Europe was not quite as intense, although there was still evidence of greater competitive pressure. Lenders took a reluctant stance, however, when it came to funding commercial property in Southern Europe. The corresponding market environment in Asia was competitive.

In the US, the market for commercial property finance was defined by a high degree of liquidity and strong competition which even became more intense in the course of the year. The willingness to accept higher loan-to-value ratios and lower client margins, as well as financings outside of the prime locations, grew here, too. Not only banks, but also life

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[3] Repayments on the property financing portfolio include all types of scheduled and unscheduled principal payments by clients.

[4] New business is allocated to the individual regions on the basis of the location of the property(ies) used as collateral. For exposures not collateralised by property, the allocation is based on the borrower's country of domicile.

insurers, which have been active in commercial property financing in the US for many years, and a marked increase in securitisations (commercial mortgage-backed securities – "CMBS") generated intense competition.

All in all, the rental performance[5] for first-class commercial properties was largely stable to slightly positive. Investors' yield requirements mainly declined slightly in the premium segment[6].

The volume of commercial property traded (the transaction volume) increased substantially on a global level over the previous year. Investors continued to focus on first-class properties in the corresponding locations. However, in view of the growing competition for these properties and a greater readiness to assume risk, there was evidence of a growing interest in secondary markets and in properties with a higher risk profile.

Developments in the commercial property markets in the individual regions

Europe

Rental development was largely stable to rising on the markets for first-class commercial properties in the European economic centres. In contrast, the number of markets with falling rents for high-quality properties was comparatively low.

Rents for retail properties in the premium segment increased in many economic centres, and varied greatly by region. Rents in this segment increased, for example, in London's West End, Istanbul, Moscow, Paris, Stockholm, the leading German centres, as well as in the Italian centres of Milan and Rome. At the same time, rents were virtually stable in the big Spanish cities of Barcelona and Madrid, and in Brussels, Prague and Warsaw. Only very few economic centres, notably in the Netherlands, registered falling rents on the markets for premium retail properties.

Rental activities for office properties were largely moderate, but picked up somewhat during the year. Rental development on the markets for high-quality office properties was somewhat less uniform than on the markets for prime retail properties. Rents for first-class office properties were stable in various economic centres, such as Amsterdam, Brussels, The Hague, Frankfurt, Hamburg, Moscow and Stockholm. However, a number of markets posted rising rents in this segment, including for example Berlin, Dusseldorf, Gothenburg, Helsinki, Munich and London. Examples of falling office rents were found in the Southern European economic centres, such as Barcelona, Madrid, Milan and Rome. However, office rents in the high-quality segment fell in other economic centres too, such as Copenhagen, Paris, Prague and Warsaw. Rent-free periods of use must be taken into account, particularly for Paris.

In contrast, a stable rental development clearly prevailed for first-class logistics properties.

The rents for properties that are not included in the first-class segment in terms of their quality and location, however, lagged behind the overall development and came under pressure.

The hotel markets of the big European cities – in terms of average revenues per available hotel room, an important indicator in this industry – were rather more inconsistent. Numerous centres recorded rising average revenues, including for example, the German centres of Frankfurt, Hamburg and Munich, but also the Southern European centres of Barcelona, Milan and Rome, as well as Brussels, Copenhagen and Paris. Falling average revenues, however, were recorded in Amsterdam, Madrid and Warsaw, for example. Average revenues per available hotel room were almost stable in Berlin, London and Prague.

In the year under review, investors particularly remained on the lookout for first-class commercial property in corresponding locations and with stable cash flows. However, the supply on various markets dwindled while the willingness to invest in properties with a higher risk profile, e.g. outside of the prime locations, increased. Transaction volumes in commercial property in Europe rose markedly in comparison with the previous year. The regional focal points were still the UK – especially London – and Germany. Transaction volumes increased in other markets too, such as Italy and Spain, albeit coming from a low prior year level.

In the European economic centres, a slightly falling trend in yields for properties in the premium segments clearly prevailed. Yields were lower for both office and retail as well as for logistics properties across the regions. Yields were stable, however, on the office markets of – for example – Barcelona, Milan, Moscow, Paris and Stockholm, the retail markets of Moscow, Prague and Stockholm, and the logistics markets of Amsterdam, Brussels, Rotterdam and Prague. Rising yields were only registered in a few of the economic centres, such as the office market in Rome, the retail markets

[5] It is characteristic of commercial property markets that they are not homogeneous. The individual properties differ, even within a regional market, with regard to the factors that determine their value and rents, such as construction quality, modernity, floor space and energy efficiency, flexibility and property management. The location – within regional or local markets – is of course an important factor as well. Hence, rents and values of individual properties from the same regional market can develop differently. This must be taken into account when analysing the following market trends.

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

in the Dutch centres, and the logistics markets of The Hague and Barcelona. The development of properties in peripheral locations or of lesser quality lagged behind that of high-quality properties.

Aareal Bank manages its sales activities in the individual regions via a network of sales centres (hubs). We have five regional hubs in Europe. Our sales activities are complemented by our teams of sector specialists covering financing solutions for hotels, shopping centres and logistics properties at the Wiesbaden location. As of the 2013 financial year, we merged the two hubs for Northwest Europe and Northern Europe. Management of this merged hub was assumed by our London branch, which has been responsible for the UK and the Netherlands, and now is also for the Northern European countries. The Stockholm branch and the representative office in Copenhagen remained in place. The other regional distribution centres are our national sales unit in Wiesbaden for Germany, the Paris branch for the other Western European countries including Spain, the Rome branch for Italy and the branch in Warsaw for Eastern Europe. The business in Turkey is allocated to the distribution centre of the sector specialists, as this is where international investors are active, especially in shopping centres and hotels, and our market activity in Turkey is greatest in these segments.

The volume of new business we achieved in Europe in the year under review amounted to € 7.9 billion, with Western Europe[7] accounting for the highest share thereof at € 4.8 billion. Western European markets also recorded the highest transaction volumes by far in commercial property within Europe. We originated € 1.4 billion in new business in Eastern Europe, earning this region the second place, followed by Southern Europe with € 0.9 billion and Northern Europe with € 0.8 billion.

North America (NAFTA states)

The commercial property markets in the US recorded a moderately positive rental development, on a national average. This applied to office and retail, as well as to the logistics markets. The increase in logistics property was strongest in relative terms, followed by office and retail property. Rental increases prevailed on the leading regional markets, too, and was fairly strong in the office, retail and logistics markets of New York and San Francisco, the retail market of Boston and the logistics market of Los Angeles. The office market in Washington D.C. and the retail market in Los Angeles were examples of on average virtually stable rents in the leading cities. In line with these rent increases, all three property types registered slightly falling vacancy ratios on a national average.

The hotel sector in the US was in an upside trend, with average revenues per available hotel room rising year-on-year. Higher revenues were due to both an increase in occupancy ratios and average room rates. Average revenues per available hotel room also improved in Canada and Mexico.

The volume of commercial property transactions in North America increased significantly. Against the background of high levels of liquidity held by investors and strong competition for first-class properties in prime locations, investors' readiness to assume risk increased in the US as well, and demand for properties with a higher risk profile rose. This heightened investor demand was reflected in the yields for newly acquired properties. These fell slightly on a national average on the US markets for retail and logistics properties, and for office properties in the business centres, while increasing marginally for office buildings in the suburbs.

We have an active presence in North America through our subsidiary Aareal Capital Corporation, which has an office in New York and also manages our new business activities locally. We originated new business in the amount of € 2.2 billion in North America in 2013, which was accounted for almost exclusively by the US.

Asia

Rental development for first-class commercial properties was inconsistent among the big Asian cities. Rents for office properties remained constant in the premium segment in the big Chinese cities of Beijing and Shanghai, while rising in the Beijing sub-market of the financial district. However, office rents fell in Singapore and Tokyo, but stabilised as the year progressed. On the retail markets, rents for prime properties rose slightly in Singapore and Tokyo, and remained stable for the high-quality shopping centres in Beijing and Shanghai. Rising rents were evident on the markets for high-quality logistics properties in Beijing, Shanghai, Singapore and particularly in Tokyo.

There was no uniform trend either on the hotel markets of these four big cities. Average revenues per available hotel room fell in Beijing and Singapore. They remained nearly constant in Shanghai while increasing sharply in Tokyo.

Transaction volumes increased noticeably in Asia too. Yields for high-quality commercial properties remained stable in Beijing and Shanghai. In Tokyo, they were stable on the markets for office and logistics properties but eased slightly for retail properties. Yields on office and logistics properties fell slightly in Singapore, but increased marginally on the market for prime retail properties.

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[7] The breakdown of the regions in the new business reporting deviates from the distribution structure described above. The volume of new business reported here also includes new business originated by our sector specialists.

Our subsidiary Aareal Bank Asia in Singapore manages our market activities in Asia. We also have a local presence with our representative office in Shanghai. Our new business in Asia amounted to € 0.4 billion, largely accounted for by China and Japan.

Acquisition of Corealcredit Bank AG

During the year under review, 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 22 December 2013 with the previous owner, a company of US financial investor Lone Star. The purchase price amounts to € 342 million, subject to contractually-agreed adjustments until the closing date. The closing – which is still subject to the approval of the respective authorities – is expected to be completed during the first half of 2014. At the time of closing, Corealcredit Bank will be included in the consolidated financial statements of Aareal Bank Group for the first time (initial consolidation). As at 30 June 2013, Corealcredit Bank's total assets amounted to € 7.6 billion, with € 3.6 billion in commercial property financings.

Consulting/Services segment

Housing Unit

Developments in the German housing industry remained stable overall in 2013, too. This was supported mainly by robust rents and long-term financing structures. Investments in property management companies continued to focus on the maintenance and modernisation of the housing stock. The housing and property companies that are organised in the German Federation of German Housing and Real Estate Enterprises (Bundesverband deutscher Wohnungs- und Immobilienunternehmen – "GdW") and its regional federations invested more than € 10 billion in the future of their portfolios.

The housing market was largely immune to short-term economic fluctuations, since market developments here tend to be determined for the most part by long-term factors such as population and income perspectives. Rents offered were some 3 % higher throughout Germany than in the previous year's level. The increase in advertised rents offered for new builds was higher in the major cities than in rural areas. The rental development was a result of the low new construction activity in recent years and the growing demand for residential properties, especially in prospering economic centres and university cities.

The housing market in Germany continued to develop heterogeneously. Demand for housing was higher in the economically strong urban areas, while rural areas, in particular, experienced a population decline and the associated falling demand for housing. The vacancy ratio on the housing market was moderately lower at less than 3 % in the former West German Federal states and approx. 8 % in Eastern Germany.

Investors continued to focus on residential property in 2013. The key reasons for the ongoing investment demand were the low yields offered by alternative investments and the positive development on the housing market. Transaction volumes increased again by around 29 % over the previous year (€ 11.4 billion) to € 14.7 billion, mostly on account of large-volume deals.

Based on the origins of the buyer groups, German investors once again dominated the transaction market. International investors accounted for only 18 % of investment volumes in 2013, so that their share of the transaction market fell again by a third compared with the previous year (27 %). Overall, various investor groups showed great interest, with listed property companies dominating the market, followed by pension funds and special funds.

The Bank's Housing Unit further strengthened its market position in 2013, acquiring new clients and intensifying business relationships with existing clients, bringing in more business partners for the payments and deposit-taking businesses. These partners manage around 290,000 units. Existing business partners in commercial property management connected more managed units to our payment processes than in the previous year. Once again, additional companies from the utilities and waste disposal industry opted for our payment systems and/or investment products. We meanwhile have an established customer base from this sector and thus a solid base for further growth.

Against the background of introducing the Single European Payments Area (SEPA) at the start of 2014, we started to convert our systems ahead of schedule by introducing the relevant SEPA credit transfers and direct debit payment methods. Having comprehensively informed our clients though workshops, brochures, cover letters and personal discussions, we supported them in the conversion to the new SEPA payment processes.

We also extended the newly-developed application for calculating usage and billing data in the BK01 sector solution for the utilities and waste disposal industry.

This brings the number of business partners currently using our process-optimising products and banking services to more than 2,900. Despite continued intense competition, the volume of deposits from the housing industry increased significantly to € 7.2 billion on average in the 2013 financial year (2012: € 5.6 billion). Deposits averaged € 7.7 billion in the fourth quarter of 2013. This reflects the strong trust clients place in Aareal Bank.

The marked increase was particularly evident in current account balances, which also increased by more than one third compared with the previous year, in line with call money. With an increase of around 15 % in 2013, we once again increased the volume of rent deposits over the previous year significantly.

Aareon AG

Aareon recorded a positive business development in 2013 in its business segments – ERP Products, Integrated Services and International Business. Overall, sales revenues rose from € 165 million to € 173 million. Despite considerable investments, earnings before interest and taxes (EBIT) were € 27 million and therefore slightly above the previous year's level of € 26 million. This yielded an EBIT margin of 16 %.

In the area of ERP Products, the number of Wodis Sigma clients increased further in 2013 to more than 500 (2012: 477). Since 2011, Aareon has offered – besides Wodis Sigma as an in-house solution – Wodis Sigma as a service from the exclusive Aareon Cloud. The majority of new clients for ERP products opted for this secure and pioneering operating mode. The new Wodis Sigma Release 5 was presented at the annual Wodis Sigma Forum held in Bochum in November, including key functional enhancements concerning the mobile property inspection and integration of the Aareon CRM portal.

Demand was particularly strong in the ERP product line – SAP® solutions and Blue Eagle – in Aareon's advisory solutions for SAP® and for consultancy services. Aareon's successful partnership with SAP continues: since 1 January 2013, Aareon has participated as an SAP Services Partner in the SAP PartnerEdge Program of SAP Deutschland AG & Co. KG. This new agreement replaced the previous status as SAP channel partner, which had expired at the end of 2012 after ten years of successful cooperation.

The volume of business with the established GES ERP system, which is available in the ASP operating mode, was stable.

In order to convert the national payment systems to the single euro payments area (SEPA) as at 1 February 2014, Aareon had integrated the necessary functions in all ERP systems. Acceptance among the clients is high.

Development in integrated services remained positive. Demand was particularly strong for the Mareon service portal, the BauSecura insurance management and the Aareon invoicing services.

As planned, Aareon introduced Aareon Archiv kompakt in early 2013. This digital archiving solution is met with strong demand. In addition, Aareon launched Mareon FM (facility management), a development of the Mareon service portal for FM providers that has been tried and tested for more than ten years.

Two new features of the Mareon service portal were released on schedule in 2013: the "Supply and Demand" module for property management companies, which makes it easier to compare prices and automates a standard process, and the web app for tradesmen.

Aareon's invoicing service continued to penetrate the market in 2013 and Aareon entered into several strategic partnerships, for example with SEEBURGER AG, Bretten, a global specialist for the integration of internal and external business processes. The goal of this partnership is to integrate Aareon's invoicing service in the SEEBURGER Business Integration Suite Utilities.

At the Aareon Congress, which was held in Garmisch-Partenkirchen in May 2013 and was characterised by digitalisation, Aareon presented its CRM offer for the first time, the result of the internal Aareon development project. The Aareon CRM portal is one of its main components and was rolled out with the first clients. Further introductory projects are about to be concluded.

International business remained positive during the period under review. Its share in Aareon Group's share of total sales revenue increased to 31 % (2012: 29 %). Within the scope of its research and development activities, Aareon Group benefits from the constant exchange of information on an international level. Synergies in the areas of business models, technologies and cooperation partners are systematically identified and exploited.

In the financial year under review, the Dutch subsidiary SG|automatisering bv, Emmen, rolled out an important client – the important property management company De Key, Amsterdam (35,700 rental units) – with the ERP product generation SG|tobias^{AX} based on Microsoft® Dynamics®AX.

The CRM solutions of the French subsidiary Aareon France SaaS, Meudon-la-Forêt, triggered positive client reactions. Aareon France is a forerunner in the area of client management systems for the commercial housing sector, which optimise and complement the processes and improve the rental service. Aareon France incorporates its expertise into the research and development activities of Aareon Group. The property management company Promologis, Toulouse (22,000 rental units) opted in favour of the CRM solutions. Erilia, Marseille, (89,000 rental units) is the first Aareon France client to use the Aareon data centre for hosting its CRM solution. The property management company Adoma, Paris (80,000 rental units), appointed Aareon France to develop a CRM web-based solution for prospective tenants.

Aareon France also acquired additional clients for the Prem'Habitat and PortalImmo Habitat ERP solutions. The new release 3.0 of PortalImmo Habitat was developed on schedule and launched in the third quarter of 2013.

Several products were rolled out in the UK, with the ERP solution QL and the mobile solution 1st Touch – for example for the important property management company Together Housing Group, Halifax (35,000 rental units). 1st Touch, which was acquired in 2012, was successfully integrated into Aareon Group. Aareon is further developing the mobile solutions offered, so that they can also be marketed internationally. One result was the development of the mobile property inspection for Wodis Sigma Release 5.0.

In the course of its growth strategy, Aareon further extended its market position in Europe and took a 100 % stake in the Swedish company Incit AB, Mölndal, with effect from 1 July 2013. The Scandinavian market is important for Aareon because of its high share of institutional property investors. Incit AB is a leading provider of ERP property management software in Scandinavia. The financial and property management system Incit Xpand offers comprehensive property management functions, ranging from accounting to management information. The ERP solutions of Incit AB are based on Microsoft® technology, as is the case with most of Aareon Group's solutions. They are designed for multi-currency and country application, ideally complementing Aareon's service range. In addition to Sweden, Incit AB is represented with subsidiaries in Norway (Incit AS, Oslo) and in the Netherlands (Incit Nederland B.V., Gorinchem).

Net assets, financial position and financial performance

Financial performance

Aareal Bank AG closed the financial year 2013 – which was characterised by a challenging market and competitive environment, as in the previous year – with an operating profit (excluding loan loss provisions) of € 248.6 million (2012: € 225.6 million).

The aggregate of net interest income and net commission income amounted to € 475.2 million, up € 32.2 million compared to the previous year. Interest income from lending and money-market transactions fell by € 33.1 million year-on-year, whilst interest income from securities declined by € 34.3 million. Interest expenses were down by € 128.7 million. Current income totalled € 3.5 million during the year under review (2012: € 0.2 million). Net commission income of € 21.5 million was down € 32.4 million year-on-year.

Administrative expenses (including depreciation and amortisation of intangible assets and tangible fixed assets) of € 232.5 million were € 16.5 million higher than in the previous year. One reason for this were measurement effects in conjunction with share-based variable remuneration components, owing to the positive performance of the Aareal Bank share, and to higher expenses for projects compared to the previous year.

Net other operating income and expenses improved to € 5.9 million year-on-year (2012: -€ 1.4 million), due to lower expenses for subsidiaries.

The balance of provisions for loan losses and the result from securities held as liquidity reserve amounted to -€ 130.0 million (2012: -€ 215.7 million). This figure includes expenditure for specific and general loan loss provisions. Securities held as liquidity reserve were revalued strictly at the lower of cost or market; the item also includes capital gains and losses realised on this portfolio.

Net other income and expenses of -€ 42.5 million (2012: -€ 20.3 million) includes the results and revaluation of subsidiaries, as well as the results from investment securities.

Taking into account a tax liability of -€ 26.2 million (2012: tax refund claim of € 15.4 million), the Bank posted net income of € 49.9 million (2012: € 5.0 million).

Net assets

Aareal Bank AG's total assets as at 31 December 2013 amounted to € 42.0 billion, after € 43.2 billion as at 31 December 2012. This decline was largely due to a lower level of short-term cash and cash equivalents.

Net assets are dominated by the property financing business and securities investments. Aareal Bank holds liquidity reserves – in the form of a high-quality securities portfolio – in view of the still-volatile market environment and in order to comply with future regulatory requirements.

As at 31 December 2013, the nominal volume of the securities portfolio was € 10.8 billion (31 December 2012: € 12.1 billion). Key aspects taken into account for new investments are good credit quality and the related value stability, as well as a high degree of liquidity, particular with regard to Basel III criteria. The securities portfolio comprises four asset classes: public-sector borrowers, covered bonds and Pfandbriefe, bank bonds and asset-backed securities (ABS). 97 % of the overall portfolio is denominated in euros. 98 % of the portfolio has an investment grade rating[8].

Public-sector borrowers are the largest asset class held, accounting for a share of approx. 82 %. These include securities and promissory note loans that qualify as ordinary cover for Public Sector Pfandbriefe. 97 % of these issuers are domiciled in the EU. Approx. 76 % are rated “AAA”or “AA” and a further 4 % are rated “A”. Overall, 98 % have an investment grade rating.

The share of Pfandbriefe and covered bonds at year-end was 11 %. 96 % consists of European covered bonds, with the remainder invested in Canadian covered bonds. Around 44 % have an “AAA” rating and a further 25 % are rated “A”. The remainder are rated “BBB”.

The bank bond asset class is made up predominantly of European issuers with high credit quality. The share of this asset class was approx. 5 % at year-end. A total of around 98 % were rated at least “A”.

The securities portfolio also contains ABS securities that account for a share of approx. 2 %. Of this amount, European mortgage-backed securities account for approx. 91 %. The asset class comprises 77 % RMBS, 14 % CMBS and 9 % asset-backed securities on car and student loans.

Property financing portfolio

Portfolio structure

Aareal Bank AG's volume of property financings rose from € 21.8 billion to € 22.6 billion in 2013. On a consolidated level, the volume of Aareal Bank Group's property financing portfolio stood at € 24.5 billion as at 31 December 2013. This represents an increase of 5.3 % over the 2012 year-end figure of € 23.3 billion. The international share of the portfolio fell slightly to 84.7 % (2012: 85.8 %).

The allocation of the portfolio by region and continent changed only marginally in 2013, compared with the end of the previous year. Whilst the portfolio shares of exposures in Germany, Western Europe and North America rose slightly, they were slightly lower in Asia, Southern Europe and Northern Europe; the portfolio share of East European exposures remained stable.

The allocation of the portfolio by property type remained more or less unchanged during the year under review, whereby the share of retail property financings was increased. In contrast, the shares of office properties, hotels and logistics properties in the overall portfolio declined slightly, while those of housing properties and other financings remained stable.

All in all, the high degree of diversification by region and property type within the property financing portfolio was maintained in the 2013 financial year.

Financial position

Interbank and repo business

Generally, in addition to customer deposits, Aareal Bank Group uses interbank and repurchase transactions for short-term refinancing, the latter being used primarily to manage liquidity and cash positions.

Aareal Bank participated in the European Central Bank's long-term refinancing operations (LTRO) during recent years. The Bank fully repaid the amounts drawn of € 1 billion on 27 February 2013. There were no liabilities vis-à-vis Deutsche Bundesbank or the ECB as at 31 December 2013.

Customer deposits

As part of our business activities, we generate deposits from housing clients, and from institutional investors. The volume of deposits from the housing industry increased during the reporting period. As at 31 December 2013, they amounted to € 7.0 billion (2012: € 6.3 billion) According to plan, the Bank reduced the volume of deposits from investors during 2013; these deposits amounted to € 4.8 billion as at 31 December 2013 (2012: € 5.2 billion).

[8] The rating details are based on the composite ratings.

Long-term funding and equity

Funding structure

Aareal Bank Group's funding remains very solid, as evidenced by the high proportion of long-term refinancing. This encompasses registered and bearer Pfandbriefe, promissory note loans, medium-term notes, other bonds and subordinate issues. The latter include subordinated liabilities, profit-participation certificates, silent participations and trust preferred securities. As at 31 December 2013, the long-term refinancing portfolio amounted to € 26.0 billion. Mortgage Pfandbriefe (*Hypothekenpfandbriefe*) comprised € 10.6 billion and Public Sector Pfandbriefe (*Öffentliche Pfandbriefe*) € 2.8 billion, whilst € 11.1 billion was made up of unsecured bonds, and € 1.5 billion was in subordinated bonds.

In 2013, Mortgage Pfandbriefe accounted for a total share of 41 % of long-term refinancing.

Refinancing activities

During the period under review, Aareal Bank succeeded in raising a total of € 4.1 billion of medium- and long-term funds on the capital market. The issue volume of our unsecured funds amounted to € 1.0 billion. In addition, subordinated debt (LT2) has been issued with a volume of € 0.1 billion. Mortgage Pfandbriefe made up € 3.0 billion of the total volume. This highlights how very important the Pfandbrief remains to Aareal Bank's funding mix.

Of the various privately- and publicly-placed issues, the two benchmark Mortgage Pfandbriefe placed in January and June 2013, with issue volumes of € 625 million and € 500 million respectively have to be highlighted. Moreover, the Bank increased two outstanding € 500 million Aareal Bank Mortgage Pfandbriefe by € 125 million each. We also successfully placed two syndicated Mortgage Pfandbrief issues – in March (€ 200 million) and October 2013 (€ 250 million) – as well as Aareal Bank's debut sterling Mortgage Pfandbrief in April 2013, with an issue size of GBP 200 million. Owing to the strong demand for Pfandbriefe and unsecured bonds from solid issuers, we were able to successfully execute all of our planned funding activities as planned.

Equity

Key indicators pursuant to AIRBA[9]

	31 Dec 2013 [2)]	31 Dec 2012
€ mn		
Tier 1 capital	2.437	2.430
Total own funds	3.081	2.991
Risk-weighted assets (incl. market risk)	13.150	14.513
%		
Tier 1 ratio	18,5	16,7
Total capital ratio	23,4	20,6

[2)] After confirmation of the financial statements 2013 of Aareal Bank AG.
The Management Board‘s proposal for the appropriation of profit for the 2013 financial year – which is subject to approval by the General Meeting – was taken into account when calculating equity.

[9] Aareal Bank AG has opted to determine regulatory indicators at Group level only since 2007, applying the regulation of section 2a (6) of the German Banking Act (KWG). In this respect, the following disclosures relate to Aareal Bank Group.

Our employees

Personnel data as at 31 December 2013

	31 Dec 2013	31 Dec 2012	Change
Number of employees of Aareal Bank Group	2.375	2.289	3,8 %
Number of employees of Aareal Bank AG	874	875	-0,1 %
of which: outside Germany	92	92	
of which: Proportion of women	46,3 %	45,0 %	
Proportion of women in executive positions	25,6 %	26,2 %	
No. of years service	13,3 years	13,5 years	-0,2 years
Average age	44,7 years	44,5 years	0,2 years
Staff turnover rate	1,4 %	2,7 %	
Part-time ratio	19,7 %	19,0 %	
Retired employees and surviving dependants	544	577	-4,0 %

Age structure and fluctuation

Aareal Bank's fluctuation ratio for 2013 was 1.4 %. The average number of years in service for the Company is 13.3. These two figures are a reflection of the strong relationship of the employees with the Company. The average age of our employees is 44.7 years.

Remuneration system

The remuneration systems are based on remuneration principles that apply throughout Aareal Bank Group. When the German Ordinance on Remuneration in Financial Institutions,(Institutsvergütungsverordnung), as amended on 6 October 2010, came into force, the remuneration structures at Aareal Bank AG and Bank-related subsidiaries were adjusted, incorporating external advisors and the employee representative bodies. The modified systems came into effect as at 1 January 2011.

In addition to the fixed remuneration that is paid in twelve monthly instalments, all employees receive a variable remuneration. These variable remuneration components are performance-related and are generally paid directly with the salary for the month of April. The variable remuneration of a limited number of employees (senior executives and so-called risk takers) comprises a short-term and a long-term component. The limitation of variable remuneration components is designed to avoid negative incentives for taking disproportionately high risks.

Salaries are reviewed annually, to ensure that individual remuneration packages are appropriate. The objective is to offer a remuneration level that is both appropriate and attractive to all Group employees.

Qualification and training programmes

A company's success largely depends on its employees. Qualified and motivated employees make a decisive contribution to a company's economic performance and are thus a key factor to its success as well as a competitive advantage. For this purpose, Aareal Bank Group operates a human resources approach aimed at the further qualification of its managers, experts and employees.

Aareal Bank invests in its employees on an ongoing basis, and in a targeted manner. The emphasis is on supporting specialist, entrepreneurial and communicative skills over the long term. The international orientation is particularly important to the Bank in relation to continuing professional development (CPD). Specifically, this involves training to achieve and expand linguistic and cultural competencies.

Aareal Bank believes that promoting qualification and continued professional development (CPD) is one of the fundamental principles of professional development. This is underlined by a broad range of management, qualification and training programmes offered by the internal corporate university "Aareal Academy", which are available to the employees at all locations. It offers the employees a broad range of internal and external seminars, language and IT training courses, vocational qualifications and training courses, which are complemented by the opportunity for individual development planning.

Aareal Academy's specialist seminars were established in cooperation between Human Resources and the Bank's specialist divisions. Within the scope of the strategic personnel development programme, Human Resources thus developed tailor-made training programmes that were adjusted to meet the Bank's various functions and requirements. The development of new, internal training measures follows the principle of "colleagues learn from colleagues". In line with this principle, experts are called in as advisors, thus guaranteeing that current professional topics are dealt with and new knowledge is imparted.

The main focus during the 2013 financial year was on supplementary training and workshop offers on Company Health Management. In addition to the existing training and coaching measures, the Bank's managers are supported through another training programme called "Healthy Leadership". Carrying on from this, a workshop format on the issue of stress management was established for employees. In addition, health management was integrated within the scope of a sub-module in the new format "Office Congress of Aareal Bank Group" for assistants and employees working in support functions.

Aareal Bank Group views its training and CPD activities as an investment in its own employees, and therefore in the future of the entire Group. The "Structured Appraisal and Target Setting Dialogue", Aareal Bank's employee review, is the starting point for the individual development plans. Every year, each employee discusses his or her personal development with the responsible manager, agreeing upon concrete measures. Once again, more than 1,000 development measures were agreed in this manner at the start of 2013. As a result of these plans, 2,611 employees participated in Aareal Bank's training measures during the year under review.

The outcome of this systematic Human Resources development approach is that Aareal Bank employees invested an average of 3.51 days in professional development seminars and workshops during 2013.

The procedure for assessing potential, which was introduced already in the 2010 financial year and updated in 2013, is conducted in the Bank as a standard tool prior to the transfer of a management duty or specialist expert position. This tool systematically selects employees and guides them to new areas of responsibility.

The long-standing cooperation with the European Business School (EBS) and its Real Estate Management Institute (REMI) continued during the year under review. Within the scope of the cooperation, Aareal Bank Group's employees are offered the chance to participate in the executive courses of study that are specific to the property sector, or in events arranged by this partner institute of higher education. Aareal Bank also supports the institute with the "Aareal Foundation Chair for Property Investment and Financing" at the EBS-REMI.

Subsidiary Aareon AG also continued to focus on the CPD of its managers during the 2013 financial year. Within the scope of the *Professional individual executive development ("ProFI"),* the managers were offered training (including labour law for managers), diagnostics (including development centre for new executives) and advisory measures (including individual coaching and managerial circles). Another focus was on supporting the international profile of Aareon by means of language courses and training sessions to expand inter-cultural competencies. The training programme to become a certified property manager at the Hochschule für Wirtschaft und Umwelt in Nürtingen-Geislingen was also continued in 2013.

Promoting the next generation

Promoting the next generation through training is a central element of the HR work of Aareal Bank Group. The specialist knowledge required in our business divisions requires us to invest continuously – and in a targeted manner – in training the next generation. To this end, Aareal Bank has been offering a tailored trainee programme for university graduates since 2000, which provides comprehensive development opportunities within the Company. The programme concentrated on the Housing Business during the year under review.

Besides Aareal Bank's trainee programme and the restoration of Aareon's trainee programme in 2013, new entrants starting out in Aareal Bank Group can avail of a range of training programmes. Aareon AG offers vocational training in various careers: office administrator, IT applications developer, IT system integrator. It also offers the dual course of study: "Business Administration - Property Manager" in cooperation with the College of Advanced Vocational Studies in Leipzig and the technical institute "Duale Hochschule" in Baden-Württemberg (DHBW) in Mannheim. Aareon also cooperated with DHBW Mannheim for the first time in 2013 on the "Business Administration - Exhibition, Congress and Event Management" course of study.

Aareal Bank and Aareon held the Girls' Day and Boys' Day as part of its measures for promoting the next generation. The Girls Day was held at Aareon for the sixth consecutive year, where 17 female students aged between 11 and 15 were given an insight into the wide variety of careers in IT. A further 20 students aged between 11 and 14 years took the opportunity presented by the Girls' and Boys' Day at Aareal Bank to gain more comprehensive impressions of occupations that they would have not taken into account in their choice of career otherwise.

A total of 68 boys and girls visited the first Aareon kids & friends science camp. Employees' children and their friends aged between 8 and 12 years participated in the workshops, which aim at stimulating and promoting technical interest at an early stage.

Within the scope of promoting the next generation, Aareal Bank Group also offers students the opportunity to gain their first impressions of the professional world and Group divisions by actively participating in internships. The work placement programme was continued successfully during the year under review.

Work-life balance

Aareal Bank Group places great importance on supporting its employees to achieve compatibility of career and family. Employees are supported in many ways.

Since July 2012, the Bank cooperates with the non-profit organisation "Fit For Family Care", which operates two childcare facilities in Wiesbaden. This cooperation agreement offers employees childcare places for children aged between ten months and six years. Aareal Bank also cooperates with the City of Wiesbaden to offer childcare facilities to its employees during the school holidays, and since summer 2013 has cooperated with the Biberbau children and youth farm in Wiesbaden, where employees' children can take advantage of educational and leisure opportunities. These offers are supplemented by flexible working hours, part-time work or the possibility to incorporate home working into their working hours – provided the respective position allows it. During the year under review, 172 employees (19.7 %) worked part-time (2012: 166 or 19 %), and 31 employees (3.5 %) worked from home during parts of their working hours (2012: 26 or 3.0 %).

Another component for improving the work-life balance of Aareal Bank's staff is the range of advisory and support services offered where close relatives are ill or in need of care, the opportunity to use statutory family caregiver leave and the constantly changing offer within the scope of the company health management, together with the various measures surrounding health protection and preventative healthcare for all employees.

For the last six years, Aareon has been certified as a family-friendly company by berufundfamilie gemeinnützige GmbH, a non-profit organisation. Aareon's staff policy services include the promotion of workplace flexibility through part-time work and home working. At the end of 2013, Aareon had 123 (16.0 %) part-time positions (2012: 128, 16.8 %) and 85 (10.9 %) home working places (2012: 82, 10.7 %). Aareon also works together with a family service company that supports employees on matters relating to childcare as well as onset of a care situation, and, together with another company, offers places at a day nursery and nursery school at a daycare centre in Mainz, where the nursery school places are free of charge for Aareon employees.

Besides the various measures for promoting the compatibility of career and family, parent/child offices have been set up at Aareal Bank in Wiesbaden and at various locations of Aareon. The objective is to support employees that are faced with short-term bottlenecks in the provision of care for their children.

Diversity

The Management Board has made an express commitment to diversity in Aareal Bank Group and has published this on the internet and intranet. This defines diversity as follows:

- An appreciation for the uniqueness of every individual and respect for their differences
- Equal opportunities at all levels
- The prevention of discrimination of any kind
- The belief that diversity enriches corporate culture and also represents a success factor in reaching strategic goals

To this end, the attractiveness of Aareal Bank Group as a modern employer is intended to be promoted, employee loyalty strengthened and employee motivation enhanced, while performance-oriented and individual promotion of abilities and competencies are intended to be guaranteed. Furthermore, the Group intends to react to demographic change and an ageing employee base, as well as taking into account the individual situations and phases in the employees' lives.

In order to highlight the significance of diversity and document the fact that the concept of diversity is very important to Aareal Bank Group, the Bank signed the Charter of Diversity (an initiative launched by German industry in 2006) during the reporting period.

Aareal Bank Group currently has employees from 30 different nations. It makes sure that its international operations are filled by mainly local nationalities.

The share of female employees in Aareal Bank Group was 46.3 % in 2013, with women accounting for 25.6 % of executive positions. The share of female employees in Aareon Group was 32.3 %, with 21.9 % holding executive positions.

With effect from 1 June 2013, the Supervisory Board appointed Ms Dagmar Knopek as a member of the Management Board of Aareal Bank.

Severely-disabled persons made up 3.3 % of Aareal Bank's staff base in 2013. This employee group is represented in the Group's German entities by a disability representative.

Equal treatment

Aareal Bank Group attaches great importance to the equal treatment of men and women in the Company, both with regard to staff appointment decisions and in terms of continuing professional development and remuneration. As a rule, all vacant positions below executive staff level are filled within the scope of an internal recruitment procedure. All employees may apply for the advertised positions. The employees' remuneration is, so to speak, not differentiated by gender, but – aside from the individual performance – solely on the basis of aspects such as qualification, experience and education.

The employee representative bodies regularly check within the scope of their co-determination rights that qualification is the decisive criteria for filling positions. In addition, recruitment decisions at Management Board and executive staff levels must take into account primarily the qualifications and experience at international level, when selecting a suitable candidate.

In Germany, Aareal Bank and Aareon apply the German General Equal Treatment Act (Allgemeines Gleichbehandlungsgesetz – "AGG"), with specially-appointed AGG Officers overseeing compliance. At the same time, AGG training is held for all employees. In the United States, the employee manual contains anti-harassment rules to avoid harassment and discrimination at the workplace.

Report on material events after the reporting date

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

Risk Report

Risk management at Aareal Bank AG

The ability to correctly assess risks, and to manage them in a targeted manner, is a core skill in banking. Accordingly, being able to control risks in all their relevant variations is a key factor for a bank's sustainable, commercial success. Besides this purely economic motivation for a highly-developed risk management system, extensive regulatory requirements apply to the risk management as well. We therefore continued to drive the development of our processes for identifying, measuring, limiting and managing risks in the financial year under review too.

Risk management – scope of application and areas of responsibility

Overall responsibility for risk management and risk monitoring remains with the Management Board and the Supervisory Board of Aareal Bank AG. The adjacent diagram provides an overview of the responsibilities assigned to the respective organisational units.

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

Type of risk		Risk management	Risk monitoring
Market price risks		Treasury; Dispo Committee	Risk Controlling
Liquidity risks		Treasury	Risk Controlling
Credit risks	Property Finance Single exposures	Credit Business Market, Credit Management	Risk Controlling, Credit Management
Credit risks	Property Finance Portfolio risks	Credit Management	Risk Controlling
Credit risks	Treasury business	Treasury; Counterparty and Country Limit Committee	Risk Controlling
Credit risks	Country risks	Treasury, Credit Management, Counterparty and Country Limit Committee	Risk Controlling
Operational risks		Process owners	Risk Controlling
Investment risks		Corporate Development	Risk Controlling, Finance, Corporate Development, Controlling bodies

Process-independent monitoring: Audit

Strategies

The business policy set by the Management Board, and approved by the Supervisory Board, provides the conceptual framework for risk management at Aareal Bank AG. 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 strategies are designed to ensure a professional and conscious management of risks. Accordingly, these strategies include general policies, to ensure a uniform understanding of risks across all parts of the Bank. They also provide a cross-sectional, binding framework applicable to all divisions. The Bank has implemented adequate risk management and risk control processes to implement these strategies, and to safeguard the Bank's risk-bearing capacity. During the financial year under review, risk strategies as well as the Bank's business strategy were adapted to the changed environment, and the new strategies adopted by the Management Board and the Supervisory Board.

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 AG 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 German Solvency Regulation (SolvV). Aareal Bank has decided to considerably exceed this minimum requirement, and to prudently apply a minimum core Tier 1 ratio (calculated in accordance with Basel III) of 8 %. Only free own funds exceeding this level are applied as potential risk cover, of which a further 28 % 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 core Tier 1 ratio of 8 %, the value-at-risk models used to quantify 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.

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".

Stress testing

Stress testing, and the analysis of stress test results, form an additional focal aspect of our risk management system. This involves conducting stress tests for all material risks, using both plausible historical parameters as well as hypothetical stress testing scenarios. To also be able to assess cross-relationships between the various types of risk, we have defined multi-factor stress scenarios, so-called "global" stress tests. For instance, the impact of a crisis affecting financial markets and the economy on individual types of risk and aggregate risk is analysed within the scope of a historical scenario. An escalation of the financial markets and economic crisis is modelled as a hypothetical scenario. The stress testing methodology implemented also takes into account the impact of any risk concentrations. We compare the aggregate risk cover available in a stress situation with the result of stress tests, thus assessing Aareal Bank's ability to bear risk in a stressed environment. Regular quarterly reports on the results of such stress analyses are submitted to the Management Board.

Approval to apply the internal ratings-based advanced approach (AIRBA)

Since 31 December 2010, Aareal Bank has applied the internal ratings-based Advanced Approach (AIRBA) to calculate regulatory capital requirements for counterparty credit risk in commercial property financings. We applied for approval by the German Federal Financial Supervisory Authority (BaFin) to also use the AIRBA to counterparty credit risk vis-à-vis institutions. Following a successful review, BaFin has granted its approval in a letter dated 29 November 2013. Since then, we have also been applying internal ratings for institutions for the purpose of calculating regulatory capital requirements for counterparty credit risk exposure. The risk classification procedures we have implemented represent a central element of our risk management process.

Organisational structure and workflows

Lending business

Division of functions and voting

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

Processes in the credit business are designed to consistently respect the clear functional division of Sales units ("Markt") and Credit Management ("Marktfolge"), up to and including senior management level. In addition, the Risk Controlling division, which is not involved in making lending decisions, is responsible for monitoring all material risks whilst ensuring an adequate and targeted risk reporting system at a portfolio level.

Lending decisions regarding credit business classified as relevant for the Bank's risk exposure require two approving votes submitted by a Sales unit and a Credit Management unit. The Bank's Assignment of Approval Powers defines the relevant lending authorities within Sales units and Credit Management. Where authorised persons are unable to come to a unanimous lending decision, the loan involved cannot be approved, or must be presented to the next-highest decision-making level for a decision.

The Counterparty and Country Limit Committee (CCC), which consists of executives from non-Sales units is responsible for the Credit Management vote regarding the approval of counterparty, issuer, or country limits.

We have implemented and documented the clear separation of Sales and Credit Management processes across all relevant divisions.

Process requirements

The credit process comprises the credit approval and further processing phases, each governed by a control process. Credit exposures subject to increased risks involve supplementary processes for intensified handling, the handling of problem loans, and – if necessary – for recognising allowance for credit losses. The corresponding processing principles are laid down in the Bank's standardised rules and regulations. Important factors determining the counterparty credit risk of a credit exposure are identified and assessed on a regular basis, adequately taking into account sector and (where appropriate) country risks. Critical issues regarding an exposure are highlighted, and analysed assuming different scenarios where appropriate.

Suitable risk classification procedures are applied to evaluate risks for lending decisions, as well as for regular or event-driven monitoring of exposures. This classification scheme is reviewed at least once a year; depending on the risk situations, the review cycle may be significantly shortened. Furthermore, the risk assessment results are taken into account for pricing purposes.

The organisational guidelines contain provisions governing escalation procedures and further handling in the event of limit breaches, or of a deterioration in individual risk parameters. Measures involved may include the provision of extra collateral, or an impairment test.

Early risk detection procedures

The early identification of credit risk exposure, using individual or combined (early warning) criteria is a core element of our risk management approach.

In particular, the procedures applied for the early detection of risks serve the purpose of identifying borrowers or exposures where higher risks start emerging, at an early stage. For this purpose, we generally monitor individual exposures and the parties involved (such as borrowers or guarantors) regularly throughout the credit term, assessing quantitative and qualitative factors, using instruments such as periodic monitoring and internal ratings. The intensity of the ongoing assessments is based on the risk level and size of the exposure. The Group's risk management processes ensure that counterparty credit risk is assessed at least once a year.

An "On-watch Committee" has been established in order to enhance the Bank's procedures for the early detection of risks. Whenever there are indications of specific risks, this Committee has global authority – regardless of exposure size – to classify exposures as “normal” or “subject to intensified handling”, and to decide on the measures to be taken as well as the composition of the Deal Team handling the exposure. The transfer of know-how between various markets is enhanced through the cross-divisional representation on the Committee.

Extensive IT resources are deployed to identify risk positions, and to monitor and measure risks. Overall, the existing set of tools and methods enable the Bank to adopt suitable risk management measures, where required, at an early stage.

Actively managing client relationships is crucially important in this context: approaching clients in time to jointly develop a solution to any problems which may arise. Where necessary, we muster the support of experts from the independent restructuring and recovery functions.

Risk classification procedures

Aareal Bank employs risk classification procedures tailored to the requirements of the respective asset class for the initial, regular, or event-driven assessment of counterparty credit risk. The rating scales and exposure definitions have been customised to match the respective methods. Responsibility for development, quality assurance, and monitoring implementation of risk classification procedures, is outside the Sales units. These units are responsible for the annual validation of the risk classification procedure.

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

Property financing business

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

In a first step, the client's probability of default (PD) is determined using a rating procedure. The method used in this context comprises two main components, a property rating and a corporate rating.

The relative impact of the two components on the rating result is determined by the structure of the exposure concerned. The client's current and future default probability is determined based on specific financial indicators, together with qualitative aspects and expert knowledge.

The second step involves calculating the loss given default (LGD). The LGD estimates the extent of the economic loss in the event of a borrower defaulting. In simple terms, this is the amount of the claim not covered by the proceeds from the realisation of collateral.

When evaluating collateral, haircuts are applied or recovery rates used, depending on the type of collateral involved and specific realisation factors. For financings of domestic properties, recovery rates are taken from a pool of data used across the Bank, whilst recovery rates for international properties are derived using statistical methods, given the low number of realisations.

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

Financial institutions

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

Sovereign states and local authorities

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

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

Trading activities

Functional separation

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

On the Sales side, the processing chain comprises the Treasury division, whilst Credit Management tasks are carried out by the independent Operations and Risk Controlling divisions. Beyond this, Finance and Audit are responsible for tasks not directly related to processes.

We have laid down organisational guidelines providing for binding definitions of roles and responsibilities along the processing chain; with clearly defined change processes.

The detailed assignment of responsibilities is outlined below.

Treasury is responsible for risk management and trading activities as defined by the Minimum Requirements for Risk Management ("MaRisk") set out by BaFin. Treasury is also responsible for asset/liability management, and for managing the Bank's market and liquidity risk exposures. In addition, we have established a Transaction Committee, to develop strategies for the Bank's asset/liability management and proposals for their implementation. The Committee, which comprises the Management Board member responsible for Treasury, the Head of Treasury, and other members appointed by the Management Board, meets on a weekly basis.

Operations is responsible for controlling trading activities, confirming trades to counterparties, and for trade settlement. The division is also responsible for verifying that trades entered into are in line with prevailing market conditions, as well as for the legal assessment of non-standard agreements, and of new standard documentation/master agreements.

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

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

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

Process requirements

Processes are geared towards ensuring end-to-end risk management, from conclusion of the trade right through to monitoring portfolio risk. The monitoring and reporting function comprises deploying adequate risk measurement systems, deriving limit systems, and ensuring the transparency of Aareal Bank AG's overall risk exposure from trading activities, in terms of scope and structure.

Moreover, processes and systems are designed in a way that allows to incorporate new products into the risk monitoring system swiftly and adequately, in order to ensure the flexibility of the Sales units in their business activities.

A standardised process exists for the intensified handling of counterparties and issuers, and for dealing with problems. This process comprises identifying early warning indicators, applying them for the purposes of risk analysis, and determining further action to be taken. In the event of counterparty or issuer default, the Counterparty and Country Limit Committee will coordinate an action plan in cooperation with the Bank's divisions involved.

Escalation and decision-making processes have been set out to deal with limit breaches.

Risk exposure by type of risk

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.

Credit risk strategy

Based on the Bank's overall business strategy, Aareal Bank AG's credit risk strategy sets out all material aspects of the Bank's credit risk management and policies. Proposals for the credit risk strategy are prepared jointly by Sales units and Credit Management, and adopted by the entire Management Board and the Supervisory Board. The credit risk strategy will be reviewed, at least once a year, as to its suitability regarding the Bank's risk-bearing capacity and its business environment; amendments will be made as necessary. This process is instigated by management, and implemented by the Sales units and Credit Management, who submit a proposal (on which they both agreed) to management. Designed in principle for a medium-term horizon, the credit risk strategy is adapted when necessary to reflect material changes in the Group's credit risk and business policies, or in the Group's business environment (as in the case of the financial markets crisis).

Aareal Bank's credit risk strategy comprises the Group credit risk strategy (as a general guideline) plus individual sub-strategies called Lending Policies. Given the hierarchical structure of the credit risk strategy, the Group Credit Risk Strategy overrides individual sub-strategies. These rules serve as a guideline for generating new business.

Risk measurement and monitoring

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

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

The Bank focuses in particular on the identification, monitoring and management of risk concentrations, where both quantitative and qualitative methods are being used. With regard to counterparty credit risk, these include for example, the regular analysis of our largest borrower units and the analysis of the portfolios by countries (covering risk classes and categories of collateral). Thresholds are set within this system for individual sub-markets and product groups. Risk Controlling uses a "red-amber-green" indicator system to assess the utilisation of the limits on a monthly basis, which it submits to the Management Board. The thresholds are reviewed annually within the scope of the target portfolio and Group planning.

The model-based review and monitoring of risk concentrations is carried out on the basis of the credit risk models used in the Bank. The models in question allow the Bank to include in particular, rating changes and diversification effects in the model-based assessment of the risk concentrations.

Within the process-oriented monitoring of individual exposures, the Bank uses specific tools to monitor exposures on an ongoing basis: besides the tools already described, this includes rating reviews, monitoring of construction phase loans or residential property developers, the monitoring of payment arrears, and the regular, individual analysis of the largest exposures.

A risk report that complies with the Minimum Requirements for Risk Management (MaRisk) is prepared and submitted to the Bank's senior management 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 types of collateral), with a particular focus on risk concentrations.

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

All trades are immediately taken into account for the purposes of borrower-related limits. Compliance with limits is monitored in real time by Risk Controlling. Any limit breaches are documented, together with action taken in response. Where limit transgressions exceed an amount defined in line with risk considerations, these are escalated to the responsible members of senior management, using a standardised escalation process.

Credit risk mitigation

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

As an international property finance house, Aareal Bank AG focuses on property when collateralising loans and advances. Loans are granted and the security interest perfected in accordance with the jurisdiction in which the respective property is located.

Market values and mortgage lending values are set in accordance with the responsibilities for decision-making on lending, and form an integral part of the lending decision. The values to be determined by the Bank are generally pegged on the valuation prepared by an independent appraiser; any discrepancies must be substantiated in writing. In any case, the market and mortgage lending values determined by the Bank must not exceed the values assessed by independent internal or external appraisers.

To mitigate credit risk, the Bank also accepts collateralisation through a pledge of shareholdings in property companies or special-purpose entities not listed on a stock exchange. The Bank has set out detailed provisions governing the valuation of such collateral.

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

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

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

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

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

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

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

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

Only cash collateral is accepted for derivatives, whereas collateral for repos can be provided in cash or in securities. Some of the collateral agreements the Bank has entered into provide for a higher amount of collateral to be provided in the event of a downgrade of the Bank's external rating.

In principle, Aareal Bank AG 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. Loan syndication is used as an active element of portfolio management.

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

Country risk

Definition

When defining country risk, in addition to the risk of sovereign default or default of state entities, Aareal Bank AG also considers the risk that a counterparty could become unable to meet its payment obligations as a result of government action, despite being willing and able to pay, due to restrictions being imposed on making payments to creditors (transfer risk). These types of risks arise only if the borrower is located in a different country from the lender, or if the financed property is located in another country. The Bank always complied with the country limits defined in accordance with its ability to carry and sustain risk throughout the financial year under review.

Country risk measurement and monitoring

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

Market price risks

Definition

Market price risk is broadly defined as the threat of losses due to changes in market parameters. Aareal Bank's market price risk exposure predominantly comprises interest rate risks, whilst currency risks are largely eliminated through hedges. Commodity and other price risks are irrelevant for the Bank's business. Hence, the primary market price risk exposures are related to the 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 counter-measures take effect. Since this is a statistical approach, the forecast for the potential loss that may be incurred within a specific period of time is for a given confidence interval only.

A variance-covariance approach (delta-normal method) is used throughout the Group to determine the VaR indicator. Determined on a daily basis for the Group and all its operating units, 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 two years, using the average residual amount of deposits observed in the past. Loans are taken into account using their fixed-interest period (for fixed-rate exposures), or using their expected maturity (variable-rate exposures). Aareal Bank's 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.

Limits were unchanged during the financial year under review. No limit breaches were detected. The overall average utilisation of the value-at-risk limit – which we have defined for the aggregate exposure to market price risk and specific risk – was 68.1 % for the year.

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). No negative outliers at Group level occurred during the last 250 trading days, affirming the high forecasting quality of the VaR model we use.

Stress testing

Although VaR has become a standard tool, the concept may fail to adequately project the actual risk in extreme situations – for example, the end-2008 phase of the financial markets crisis. For this reason, the VaR projection is supplemented by simulating stress scenarios on a monthly basis.

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

The worst-case scenario used in the financial year under review was a hypothetical scenario, where a deteriorating financial markets crisis caused bond and CDS spreads to widen due to rating downgrades, combined with an appreciation of the euro and unchanged interest rate markets. This scenario implied a present value loss of 20 % of the stressed aggregate risk cover limit as at year-end 2013. No breach of set limits occurred during the year under review.

Interest rate sensitivity

An additional instrument used to quantify interest rate risk exposure is the calculation of interest rate sensitivity, expressed by the so-called "delta" parameter. The first step to determine this parameter requires calculating the present values of all asset and equity/liability items on the statement of financial position. In a second step, the interest rates of yield curves used for this calculation are subjected to a one basis point parallel shift up (a method known as the "key rate method"). Delta is the present value of the profit or loss resulting from this yield curve change.

Interest rate gap analysis
Further, the gap analysis per currency provides information on all of the Bank's positions in respect of which the interest rate has been fixed. In addition to disclosing the net gap positions in the respective maturity bucket, this data allows for specific analyses concerning the risks and returns from the current portfolio.

Trading book
Being authorised to maintain a trading book, Aareal Bank AG is the Group entity that is in a position to assign transactions to the trading portfolio as defined by the German Banking Act. Given that no such trades were concluded during 2013, trading book risks played a negligible role in the overall risk scenario.

Liquidity risks

Definition
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'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.

Risk measurement and monitoring
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 following tools are used for this purpose:

a) Cash flow forecast
We have developed a cash flow forecast, tracking cash flows from all balance sheet items and derivatives, on a daily basis, over a ten-year period. This liquidity risk information helps to assess the Bank's short-term liquidity position, broken down by currency or product. Strategic liquidity is taken into account using this ten-year cash flow profile. We use statistical modelling to incorporate the cash flow profile of products without a fixed contractual lifetime.

b) Liquidity run-off profile
The appropriateness of the Bank's liquidity is assessed using a liquidity run-off profile: the aggregate of all potential cash inflows and outflows over a three-month period is compared to the liquidity stock. This liquidity stock comprises all assets that can be liquidated at very short notice. The difference of both figures (in absolute terms) indicates excess liquidity, once all claims assumed in the run-off profile have been fulfilled through the liquidity stock. There were no liquidity shortages throughout the period under review.

Further details are provided in the comments on the Bank's liquidity in the section on "Refinancing and Equity".

c) Funding profile
Diversifying the Bank's refinancing profile by type of investor, and by product, represents a further key aspect of our approach to liquidity risk management. Core sources of funding such as customer deposits and funds invested by institutional clients – alongside covered and uncovered bond issues – constitute the foundation of our liability profile.

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

We generally consider the withdrawal of customers' current account balances as the most significant scenario. Even in this stress scenario, liquidity is sufficient to cover the expected liquidity needs under stress conditions.

Liquidity Ordinance
The requirements of the liquidity ratio in accordance with the Liquidity Ordinance, which is relevant to liquidity management, were always complied with throughout the year 2013, as were the limits set by reference to the liquidity run-off profile.

Operational risks

Definition

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

Risk measurement and monitoring

It is the objective of the policy pursued by Aareal Bank AG to achieve a risk-minimising or loss-limiting effect at an early stage by employing a pro-active approach.

The Bank currently uses the following tools to manage operational risks:

- Self assessments: analysis thereof can provide management with indicators of any potential risks within the organisational structure.
- Risk inventories that include a periodic systematic identification and compilation of all relevant risks.
- A loss database, in which relevant damages incurred are reported, and in which they can be monitored until they are officially closed.

By means of this control toolkit, decentralised data capture as well as centralised and timely compilation of all material operational risks are ensured.

The three tools described above are used to prepare the regular risk reporting to the Bank's senior management. The responsibility for implementing operative risk-reducing measures rests with those responsible for the Bank's risk management.

In addition to the reports prepared from the tools stated above, suitable and plausible stress tests are conducted every quarter. These are hypothetical scenarios and sensitivity analyses on the risk inventories. The results of the stress tests are reported regularly to the Management Board and serve as an indicator for potential developments within the operational risks that could jeopardise the continued existence of the Group.

Analyses conducted using the instruments employed have shown that the Bank is not exposed to disproportionate operational risks; nor did they indicate any material risk concentration. There were cases reported in the loss database during the financial year under review, but there were no losses involving significant monetary damages.

Further to these tools, the Bank reviews relevant individual scenarios, and implements any measures required, on the basis of external data. Taken together, these tools for managing operational risks result in an integrated control circuit which leads to risk identification, evaluation, and management – through to risk control.

Tools to control operational risk are supplemented by a system to manage and monitor outsourced activities and processes (outsourcing), whereby the relevant organisational units regularly assess the performance of outsourcing providers, using defined criteria. The results of this process, and actions taken, are communicated to the Bank's senior management within the scope of operational risk reporting, thus allowing for risk-mitigating steps to be taken where needed.

Investment risks

Aareal Bank AG's risk exposure is largely concentrated on risks generally associated with banking, such as credit risk, market price risk, liquidity risk, and operational risk. Some Group subsidiaries, however, are exposed to a variety of other types of risk outside typical banking risk, which we include in our centralised risk management system through an Investment Risk Control concept.

Aareal Bank Group acquires equity investments strictly for the purpose of positioning the Group as an international property financing specialist and provider of property-related services.

Definition

Aareal Bank defines 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.

Risk measurement and monitoring

All relevant Group entities are subject to regular audits, including a review and assessment of their risk situation within the framework of risk measurement and monitoring. Due to the special character of some exposures (e.g. marketing risks), special methods and procedures are employed to deal with investment risk. The Bank uses an internal valuation method to quantify investment risk, and to include it in the calculations of the Bank's ability to carry and sustain risk, and for the purpose of limitation. The limit defined for investment risk was always complied with during the financial year under review.

The existing procedures used to measure and monitor risk exposure are supplemented by subjecting the equity portfolio to regular stress testing.

The Corporate Development, Finance and Risk Controlling divisions are jointly responsible for measuring and monitoring investment risk exposure.

Corporate Development and Finance hold the functional and organisational authority regarding investment controlling.

Risk Controlling is responsible for submitting a quarterly equity investment risk report to the Bank's Management Board.

Other risks

Definition

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

Reputational risk is defined as the risk of events that negatively affect the Bank's reputation with investors, analysts, or clients.

Strategic risk is typically associated with the threat of incorrect assumptions regarding market developments, burdening a bank's performance as a result.

Risk measurement and monitoring

The Bank has defined a suitable early-warning system – focusing on media observation/social media, client/staff and investors/analysts – that is designed to assess reputational risks. By analysing the early-warning indicators and deploying experiences already gained by the Bank, the Management Board can take a proactive stance in relation to potential reputational risks.

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

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

Accounting-related Internal Control and Risk Management System

Tasks of the accounting-related Internal Control System (ICS) and the Risk Management System (RMS)

The accounting-related Internal Control and Risk Management System includes principles, procedures and measures to ensure the effectiveness and the efficiency of internal and external accounting, in accordance with applicable legal provisions. Pursuant to section 289 (2) no. 5 of the German Commercial Code (HGB), the tasks of the accounting-related Internal Control System mainly include ensuring proper conduct of business activities, guaranteeing proper internal and external accounting, as well as ensuring compliance with relevant statutory and legal requirements applicable to the Company.

The objective of the accounting-related Risk Management System is to identify, assess and limit risks which may impede the compliance of the financial statements with applicable rules and regulations, and to ensure that such risks are properly reflected in the financial statements. As with any other internal control system, the accounting-related ICS and RMS may only provide reasonable – but not absolute – assurance with regard to achieving this objective, regardless of how much care is used to design this system.

Organisation of the accounting-related ICS and RMS

The Internal Control System of Aareal Bank AG takes into account the principles established by the Minimum Requirements for Risk Management (MaRisk) related to company-specific design of the ICS. The design of this Internal Control System comprises organisational and technical measures to control and monitor the Company's activities. The Management Board of Aareal Bank AG is responsible for designing, implementing, applying and developing/reviewing an appropriate accounting-related internal control system. The Management Board makes decisions as regards the scope and the design of specific requirements; it has defined the responsibilities for the individual process steps in connection with accounting by means of organisational guidelines, and has delegated these responsibilities to individual organisational units.

Primary responsibility for accounting and financial reporting lies with the Finance division. Finance manages the centralised processes for preparing Aareal Bank AG's annual and interim financial statements. Amongst other tasks, Finance is responsible for preparing the financial statements (including the management report) in accordance with the German Commercial Code (German GAAP – "HGB"), and monthly reporting packages; the division is also responsible for developing accounting guidelines in accordance with the HGB, and IT guidelines.

The number of employees within Aareal Bank AG's Finance division is adequate, as are their qualifications. Furthermore, they possess the necessary knowledge and experience relevant for their functions.

The Supervisory Board is responsible for monitoring the Management Board. It approves both the single-entity financial statements of Aareal Bank AG and the consolidated financial statements. Measures taken by the Supervisory Board to ensure an efficient performance of its control functions include the establishment of an Accounts and Audit Committee, which is primarily responsible for financial reporting issues and monitors the effectiveness of Aareal Bank AG's Internal Control System. The committee analyses and assesses the financial statements submitted to it, the internal risk reports, and the annual Internal Audit report. In addition, the Committee is responsible for determining the focal points of the audit, as well as for evaluating the auditors' findings. The Accounts and Audit Committee includes an independent finance expert, pursuant to section 100 (5) of the German Public Limited Companies Act (Aktiengesetz – “AktG”).

Internal Audit also has a process-independent monitoring function. It reports directly to the Management Board, and provides objective and risk-oriented auditing and consulting services which are designed to optimise Aareal Bank AG's business processes with regard to accuracy, safety and efficiency. The Internal Audit division supports the Management Board by evaluating the effectiveness and appropriateness of the process-dependent iInternal Control System and of the risk management system in general. The review of the risk management's effectiveness and appropriateness covers the risk management and risk control systems, reporting, information systems, and the accounting process. Any detected weaknesses regarding the identification, evaluation and reduction of risks are reported and addressed within the context of specific action plans.

To perform its tasks, Internal Audit has full and unrestricted information rights with respect to activities, processes and IT systems of Aareal Bank AG. Internal Audit is informed on a regular basis about material changes related to the Internal Control and Risk Management System.

The review of process-integrated controls conducted by Internal Audit is based on a set of internal regulations, procedural instructions and guidelines of Aareal Bank AG. The audit activities of Internal Audit comprise all of the Group's operational and business processes (including the accounting and financial reporting process), and are carried out using a risk-based approach.

Components of the accounting-related ICS and RMS

Within Aareal Bank AG, various measures related to the Bank's organisational structures and workflows help to fulfil the monitoring duties concerning the accounting and financial reporting process within the framework of its Internal Control System.

A prerequisite for the monitoring system to work efficiently is a written set of procedural rules governing the distribution of tasks between the individual divisions and the scope of the respective activities. The organisational structure of the Finance division is set out in the Bank's organisational guidelines. Aareal Bank AG's accounting system is structured observing the principle of separation of functions. The functional separation makes for a split between operative and administrative roles, and is designed to ensure a sufficient level of control. In addition, the preparation of the single-entity and the consolidated financial statements is carried out in distinct units.

Various guidelines exist for activities and processes. These guidelines are set out in the Written Set of Procedural Rules of Aareal Bank AG and available for inspection for all employees. There are requirements as regards data entry and control – as well as data storage – which have to be observed in general by all of the Bank's posting units. If necessary, results are reconciled across divisions or companies.

Activities required within the scope of preparing the financial statements are defined by internal accounting instructions. Aareal Bank AG's voucher documentation rules set out the rules governing accounting vouchers for all of the Bank's posting entities. Legal requirements and the relevant accounting standards are set out in detail in the accounting instructions, and by reference to the plan of accounts. The Finance division regularly reviews these documents, and updates them if necessary. The valuation techniques used, as well as the underlying parameters, are controlled regularly, and adjusted if necessary. Where valuation units (Bewertungseinheiten) are used for measurement purposes, defined criteria are reviewed on a regular basis. For further information on measurement, please refer to the relevant notes to the consolidated financial statements.

In addition, the Bank's Risk Manual summarises the material elements of Aareal Bank Group's Risk Management System. Specifically, the Manual describes the organisational workflows as well as methods and instruments used in the context of risk management. In this context, reference is made to our explanations in the Risk Report.

Clearly-defined rules as regards delegation of authorities facilitating the allocation of professional responsibilities also contribute to reliable financial reporting. Any decisions taken are always based on relevant authorities. Internal controls defined on the basis of risk considerations are embedded in the accounting process. Compliance with the principle of dual control in all material processes is one of the principles for ensuring accurate accounting. Where no integrated approval system/dual control feature has been implemented in the accounting IT systems for material transactions, this has been integrated and documented in the workflows for material manual processes.

Adherence of accounting to generally accepted accounting principles is ensured by both preventive and detective controls within the accounting process itself, as well as through a comprehensive review of processed data. The preparation of the consolidated financial statements is characterised by multiple analyses and plausibility checks. Besides the evaluation of individual accounting issues, these include comparisons of periods, and between plan and actual data. Reconciliation of balances and positions with clients and counterparties is carried out in line with existing regulations. Control processes in accordance with MaRisk have been implemented for credit risk provisioning. Reconciliations take place between the main ledger and upstream position-management systems, as well as on the level of individual accounts. Adequate control processes have been implemented for both manual and automated accounting transactions. Additional control processes are in place to ascertain the complete recording of all transactions in the Bank's accounting systems.

In order to increase the level of control quality, all relevant divisions are involved in the reconciliation process. An example of cross-divisional reconciliation is the process for the preparation of annual and interim reports. All divisions involved must ensure and (prior to preparation by the Management Board) confirm the quality of the sections of the reports they are responsible for. This represents an additional control level for the data to be disclosed.

In terms of organisational workflows, the accounting-related Internal Control and Risk Management System is based on a comprehensive standardisation of processes and software. Aareal Bank AG uses both standard and customised software. The Bank's accounting-related IT systems were designed in such a way that both manual controls and automatic plausibility checks are performed for material technical and procedural system steps of the applications used. The controls in relation to processing within the IT systems are also integrated in the processes, as well as being independently performed. Process-integrated controls comprise, for example, the review of error and exception reports or the regular analysis of internal service quality. In contrast, IT reviews are conducted independently from processes, by Internal Audit.

Data and IT systems must be protected from unauthorised access. A differentiated access authorisation concept is in place for the systems used for finance and accounting, preventing any unauthorised access. Authorisations are allocated to responsible employees, reviewed regularly, and adjusted if necessary in accordance with internal criteria.

Aareal Bank AG reviews its accounting-related Internal Control and Risk Management System on an ongoing basis. Necessary adjustments are made with respect to the accounting process based on the Bank's reviews. Adjustments may have to be made, for example, in connection with changes in the Bank's organisational structure, to the business model, or new legal requirements.

Aareal Bank AG has to comply with legal requirements. If these requirements change, for example in the form of new laws or changes in accounting standards, the processes or IT systems will be adjusted as required in separate projects across divisions – based on a clearly-defined allocation of functions, and the accounting-related Risk Management System will be adjusted to take the amended rules into account. Current developments of statutory and legal provisions applicable for Aareal Bank AG are constantly monitored and reported, not only by the responsible division, but also by a steering committee established by the Bank. This committee also initiates any required adjustments to be made to systems and processes, and reports the results to the Management Board.

Report on Expected Developments

Macro-economic environment

Economy

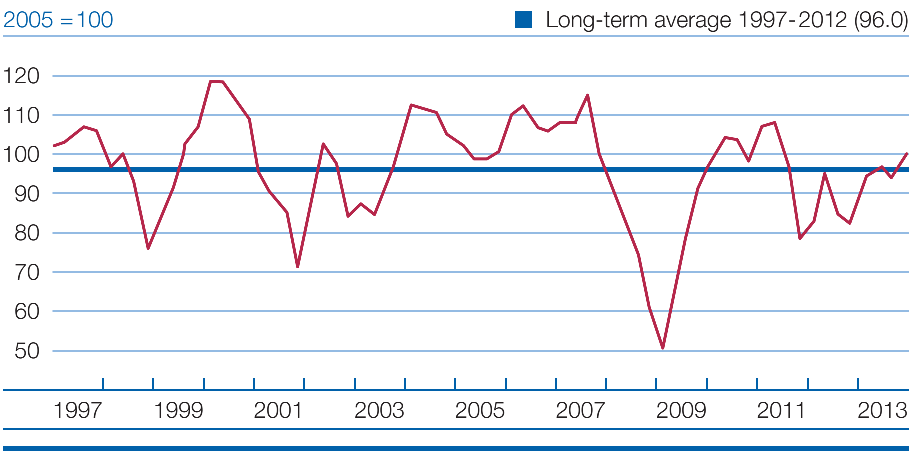
There are indications for a slight recovery in the global economy in the year 2014. Sentiment has improved in some regions, both amongst businesses and private households – and this is expected to gradually feed into demand. Likewise, slowly diminishing uncertainty concerning the development of the European sovereign debt crisis might also have a positive impact. However, material burdening factors persist in many economies; any recovery is thus likely to take place in a slight and reluctant manner. We therefore anticipate the global economy to grow at a slightly faster rate than last year, with continued noticeable differences regarding economic developments in different regions.

In the euro zone, uncertainty in connection with the European sovereign debt crisis has been declining for some time now. This is expected to have a positive impact on the economy – however, high unemployment, low wage growth in the previous year and a persistently restrictive fiscal policy – albeit less pronounced than in the previous years – have a dampening effect on macro-economic demand. Against this background, we expect real economic output in the euro zone to rise only slightly and slowly, for example, in Belgium, Finland and France. Growth rates are likely to be somewhat higher, even though still to a moderate extent, in Germany and Austria. The economies in Italy, the Netherlands and Spain, which were still in recession last year, are expected to continue stabilising this year. We anticipate real gross domestic product figures to rise marginally to slightly. For numerous European countries outside the euro zone, a more pronounced increase in economic output is likely, and we believe this will be the case in the UK, Poland, Sweden and Switzerland, as well as in the Czech Republic – which had been in recession for two years. We envisage a moderate recovery for the Danish economy. Whilst the Russian economy is also expected to grow at a slightly stronger rate than last year, the growth rate is likely to remain low compared to historical levels. Turkey is likely to have a moderate growth rate, albeit somewhat lower than in the previous year.

The economic environment in the United States has improved: private household debt is down significantly, the market for residential property shows equally significant signs of recovery, and unemployment has declined continuously. Against this background, the US economy is expected to show a pronounced growth rate, exceeding the previous year's figure. A moderate increase in interest rates is likely to follow the expected reduction ("tapering") of the US Federal Reserve's extensive bond purchases respectively their expiry. The economic forecast for the US is based on the assumption that these interest rate rises will not compromise investments to a major extent – nonetheless, this represents a risk to economic development. In the US, uncertainty continues to exist in particular with respect to fiscal policy. We assume the growth rate of real gross domestic product to accelerate compared with the previous year – to a slight extent for Canada, and to a stronger extent for Mexico.

The Japanese economy is likely to grow moderately, given Japan's enhanced competitiveness (due to exchange rate fluctuations) and accelerating global trade. At the same time, budget consolidation measures which are about to take effect, such as the planned value-added tax increases, need to be taken into account: hence, we believe that Japan's growth rate will be on the same level as in the previous year. The Chinese economy will continue to post high growth rates by international standards. In our view, this year's growth rate will be marginally lower than in 2013. We believe Singapore's economy will grow with rates comparable to those of 2013.

ifo Global Economic Climate*



* Arithmetic mean oft he assessment oft he current situation and expected developments.
Source: ifo World Economic Survey (WES) IV/2013

Looking at the slow economic recovery in Europe, we expect unemployment to remain virtually unchanged – or perhaps to fall slightly at best – in many European countries this year. Accordingly, tensions will remain high, especially on labour markets in Southern Europe. Stronger economic growth in the US gives reason to expect the pronounced reduction in unemployment to continue.

Future economic development, and hence the forecasts, are subject to material risks and uncertainty – whereby the European sovereign debt crisis is a key factor. Even though uncertainty in this respect has declined in the meantime and financial and capital markets have seen significant relief, a renewed deterioration and escalation of the sovereign debt crisis cannot be excluded. Such a development might lead to distortions on the financial and capital markets, causing a deeper recession that could spread on a global scale, through channels of trade. Even though we do not consider such a deep global recession to be the most likely outcome, the risk still exists. Fiscal developments in the US pose another material risk.

Likewise, a quick exit from expansive monetary policy – particularly by the Fed – constitutes a risk for the global economy as related interest rate increases might burden corporate investments more strongly than is currently assumed. Furthermore, the tapering of US bond purchases holds the threat of investors withdrawing capital from emerging markets – which would burden their economies. Conversely, the expansive effects of lower interest rates on the global economy might be amplified in an environment of decreasing uncertainty. Right now, it is still unclear what effect the liquidity created through the massive expansion in central bank money supply will have, especially over the longer term. This constitutes an additional risk to economic developments.

Financial and capital markets, monetary policy and inflation

Financial and capital markets – including government bond and interbank markets – have continued to calm down notably during the year under review. There are no signs for any material changes to this situation in the current year. Whilst the impact of the European sovereign debt crisis on financial and capital markets has thus declined, related risks remain in this context. The financial and capital markets may still be very susceptible to shocks, should the sovereign debt crisis escalate. A positive factor in this connection is the fact that Spain left the rescue facility in January 2014, which it had drawn upon in an amount of € 41.3 billion to recapitalise banks.

Risks for the financial and capital markets also exist in connection with fiscal policy developments in the US.

In view of the expected low inflationary pressure, we believe that most central banks will keep their key interest rates low. Consequently, under current conditions, short-term interest rates are also expected to remain at low levels. However, the US Federal Reserve is likely to further reduce ("taper") or even exit its bond purchases this year – which might trigger moderate increases in long-term interest rates, particularly in the US but also in other regions. The Fed already cut back its bond purchases several times at the beginning of 2014.

Whilst risk premiums for euro zone periphery states are likely to remain in place, a marked narrowing might be possible as long as uncertainty in connection with the European sovereign debt crisis is not renewed.

In view of a slight, reluctant economic recovery, we believe inflationary pressure this year to be rather low. However, this forecast is subject to uncertainty caused by the development of oil prices, a key component of inflation developments. Besides economic factors, oil prices are also driven by political developments. In our view, this year's average inflation rate in the euro zone will be marginally lower than in 2013. For most European countries outside the euro zone – such as Denmark, the UK and Sweden – inflation is expected to be low to moderate. Russia and Turkey, in contrast, are likely to experience markedly higher inflation rates compared to other European countries. In the US, we anticipate moderate inflation, roughly in line with the previous year's level. In Japan, a noticeable increase in inflation, at least compared to the zero inflation rate seen over previous years, can be expected given the planned VAT increases and the central bank's stated inflation target of 2 %, In China, we expect inflation to be still moderate during the year.

Regulatory environment

The trend towards a tighter regulatory framework in the banking business is set to persist during the coming years. Accordingly, Aareal Bank will also focus on the related measures for implementation and how these will affect the Bank’s business activities.

In addition to the core elements of the Basel III regime, which include enhancing the quality and quantity of regulatory capital, as well as the introduction of international liquidity standards and a leverage ratio, requirements are set to tighten further due to the ECB's Comprehensive Assessment – this will tie up additional resources. Furthermore, additional new regulatory requirements will need to be implemented. These include, on a national level, the Minimum Requirements for the Design of Recovery Plans ("MaSan"), as well as the establishment of a framework for the restructuring and resolution of banks and securities firms on a European level, in order to ensure effective crisis management and orderly resolution.

Regulators have yet to come up with final details for a large portion of these additional requirements, and adopt them. The final draft of the various technical standards that are essential for implementation is still pending. To nevertheless facilitate the timely implementation, we have already started to deal with and pursue the various issues in numerous projects – devoting considerable resources to this task.

Sector-specific and business developments

Structured Property Financing segment

During the year under review, competition on the market for commercial property financings in Europe has clearly intensified compared with the previous year. We expect competition to remain intense during 2014. This might also be driven by an expansion of financing activities from non-bank competitors, such as insurance companies, pension funds and debt funds. In general, the willingness of finance providers to accept lower margins and higher loan-to-value ratios is likely to noticeably increase further, especially in European core markets such as Germany, France and the UK. Yet we also anticipate competition to palpably intensify in other West European countries, as well as in Northern and Eastern Europe. Finance providers are expected to be more reluctant when it comes to Southern Europe, yet it is fair to expect a slight loosening in lending standards there – especially if uncertainty in connection with the European sovereign debt crisis continues to decline. Financings of first-class commercial properties in corresponding locations are likely to remain in focus. We expect to see a continued notable increase in financing offers for properties with a higher risk profile, and for large-volume projects.

For commercial property financings in the US, competition is set to remain strong and market liquidity to remain high, as was the case in the previous year. Insurance companies have played a major role on these markets for many years now. The volume of CMBS transactions may continue to grow strongly. We believe that the financing markets in China and Japan will also remain highly competitive.

Developments on the commercial property markets[10] are influenced on the one hand by the expected slight economic recovery – accompanied in Europe by high unemployment in many countries – and by the high degree of investor liquidity on the other hand. For investors holding significant liquidity and chasing yield in a low interest rate environment, commercial property might become attractive as a form of investment, which would stimulate demand on commercial property markets.

[10] Assessments of individual sub-markets and properties may deviate from the general description of developments on commercial property markets outlined below.

In Europe, taking the slight, slow economic recovery into consideration, we anticipate largely stable property values and rents in most countries during 2014. The high level of unemployment in numerous countries might have a burdening effect. On average, we assume values and rents to remain virtually stable in Belgium, the Czech Republic, Finland, Poland, Russia, Sweden and Turkey. Market values and rents should stabilise in Spain and Italy as their respective economies improve. However, the national averages for market values and rents in France – and to a somewhat greater extent in the Netherlands, given the historically high levels of unemployment together with subdued economic development – are expected to decline slightly. Thanks to the forecast for more dynamic economic development and brisk demand for commercial property, Germany and the UK are expected to see notable increases in values and rents. We anticipate a slight increase for Denmark.

Combined with a high degree of investor liquidity, the positive outlook for the US economy and labour markets point towards moderate increases in rents and property values, despite the expected moderate rise in long-term interest rates. We expect a stable performance in Canadian property values. Against the background of expected interest rate rises, we remain cautious regarding the development of the commercial property markets in China and anticipate a slight decline in values on average. Whilst we expect a stable performance in Singapore, our forecast for Japan is a markedly positive trend.

The developments outlined above should, in our view, tend to apply to office, retail and logistics property markets. On the hotel markets, we expect average revenues per available hotel room to remain roughly in line with the previous year, especially in Europe and Asia. Of course, diverging levels on individual markets are always a possibility. On the North American hotel markets, however, we think that a slightly positive trend – on average – is possible.

Investors were already increasingly looking for properties with a higher risk profile last year – a trend that may continue and strengthen somewhat this year. First-class properties in the corresponding locations, offering secure cash flows, will continue to be of particular interest. Yet, a shortage in such properties should direct more and more liquidity to markets outside the premium segment.

Macro-economic risks and uncertainty factors will continue to be relevant for the further development of the commercial property markets. Events such as an escalation of the European sovereign debt crisis or a deep recession would likely lead to significant declines in property values and rents. As another risk factor, in the wake of an exit by the US Federal Reserve from its bond-buying programme, long-term interest rates – especially in the US – might rise noticeably beyond the anticipated scope, which would clearly burden the development of property values. Conversely, limited supply – due to the low level of completions over recent years, particularly in the US but also in Europe – might provide support to commercial property markets.

Aareal Bank takes property market developments into account for its ongoing risk assessment, as well as, within the framework of its lending policies, expected diverging developments in different countries.

We have determined our target for new business in line with market conditions, including the competitive environment, forecast investor behaviour, and expected economic developments. Our target for aggregate new business originated this year is between € 8 billion and € 9 billion.

We want to continue to use club deals and syndicated financing in the future too, to allow us to participate in large-volume financings and to diversify risk. In this context, a significant change came into force in Germany on 1 January 2014: insurance companies, pension funds and pension schemes domiciled in a country of the European Economic Area (EEA) are now also eligible as beneficiaries to be entered into the funding register. This has facilitated cooperation with these market participants within the scope of syndications.

These forecasts are based on the assumption that there will be no protracted recession, and no escalation of the European sovereign debt crisis. Such events might burden new business, leading to a marked reduction especially in the case of newly-originated loans.

Consulting/Services segment

Housing Unit

For the housing industry in Germany, we expect a solidly positive development during the current year, thanks to stable rents and a high degree of stability in property values.

Expectations for residential space have become more differentiated, as a consequence of demographic change and the trends towards a more individual and differing lifestyle. This means that, going forward, housing industry enterprises will need to continue increasing their investments. The future development of the industry will be shaped by issues such as energy-efficient renovation and appropriate living conditions for families and the elderly.

The housing industry will continue to pursue a sustainable development of their portfolios; in addition, they will expedite new housing construction projects in order to modernise their holdings. Energy-efficiency requirements for new construction projects are expected to increase by 25 % in the spring of 2014, which will drive up construction costs. Expected investments in the industry are closely connected with the political environment and its impact on the profitability of any projects undertaken. High construction costs, exacerbated by discussions concerning a cap on rent levels, might have a dampening effect upon investment activities.

From a demographic and overall economic perspective, we anticipate a stable development of the residential property market in the 2014 financial year. In spite of the higher housing construction activity seen in 2013, the increased supply will not be sufficient to cover expected demand. Rental growth will continue to be highest in cities with growing populations and high economic output. This trend will be beneficial to property investors and potential sellers within the housing industry.

We expect investment demand for residential property to remain intact throughout 2014. Key factors driving the persistent investor interest are the favourable interest rate environment, the stability of the housing market, and sound fundamental data emanating from the German economy. However, investment activity will be limited by a lack of core investments on offer and the restricted number of potential large-scale portfolios available for sale. Against this background, we anticipate a noticeable decline in transaction volumes next year.

We see good opportunities during 2014 to acquire new clients and to further intensify the business relationships with our existing client base. This also applies to our payments services for utilities and the waste disposal industry. We see further growth potential in payment support services and process optimisation. At present, therefore, we invest particularly in the further development of our products designed for the management and settlement of rental deposits.

Looking at the volume of deposits taken, we expect the positive trend to continue, particularly in relation to current account balances and rent deposits. 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 AG

The digitalisation of communication in the property management sector, and the related use of CRM solutions and mobile applications, are becoming increasingly important. In this context, the IT trend of cloud computing will become further established on the market for property management software.

For 2014, Aareon expects a slight increase in earnings before interest and taxes (EBIT), primarily driven by the acquisition of Sweden's Incit AB in 2013, the continued migration of GES clients to Wodis Sigma, and strong growth among its international subsidiaries.

EBIT in Aareon's domestic operations is forecast to remain virtually unchanged from 2013's levels. A slight increase in sales revenues will be offset by higher personnel and other staff-related costs, as well as higher project-related costs.

Aareon expects unchanged sales revenues and EBIT in its ERP products segment in 2014, with a strong increase in sales revenues anticipated for the Wodis Sigma product line. Decisive factors will be activities that are designed to gradually increase the level of migrations, and to boost the need for consultancy services – with a view to growing advisory and licence fees. Business in the GES product line during the financial year under review was largely characterised by major one-off projects, and the implementation of SEPA. Given the non-recurring character of these effects and the continued migration of GES clients to Wodis Sigma, Aareon expects markedly lower product revenues in 2014.

The company continues to expect stable sales revenues from the SAP®solutions and Blue Eagle product line.

Significant sales revenue growth is expected in the Integrated Services segment; contributing factors include demand for the Aareon CRM and Mobile Services solutions (launched in 2013) and the Aareon Archiv kompakt product. In this context, Aareon also anticipates a positive development of sales revenues in Integrated Services consulting. Thanks to a high level of development work, EBIT in this segment is set to remain at the previous year's level.

In its International Business segment, Aareon expects significant EBIT growth, also reflecting the acquisition of Sweden’s Incit AB. At the same time, we also forecast significant increases in sales revenues and results for Aareon's other international subsidiaries.

Overall, Aareon forecasts a marked increase in sales revenues for the next year, EBIT of around € 28 million, slightly higher year-on-year, and an EBIT margin of around 16 %.

Group targets

Aareal Bank Group draws up its corporate planning in accordance with IFRSs. Hence, no single-entity planning is being made for Aareal Bank AG, which is why the following statements on Group targets refer to Group planning in accordance with IFRSs.

Aareal Bank Group's positive development is expected to continue during the current year. The Group's forecasts for the 2014 financial year include, for the first time, projected figures for Corealcredit Bank AG – assuming the closing of the transaction on 31 March 2014. The exact contribution of Corealcredit Bank depends on the closing date for the transaction, which is still expected to be in the course of the first half-year. Aareal Bank announced the acquisition of Corealcredit Bank on 22 December 2013.

We expect net interest income in the 2014 financial year to rise to between € 610 and € 640 million. Net interest income is set to benefit from good margins from the previous year’s lending business, low funding costs, and the acquisition of Corealcredit Bank AG. The low interest rate environment continues to have negative implications for net interest income, both in relation to the deposit-taking business and because of the lack of attractive investment opportunities for the liquidity reserves.

Despite a larger loan portfolio, Aareal Bank forecast allowance for credit losses in a slightly more optimistic range of € 100 million to € 150 million. As in the previous years, the Bank cannot rule out additional allowance for unexpected credit losses that may be incurred during 2014.

Net commission income is projected to increase slightly, to between € 170 million and € 180 million.

Administrative expenses are expected in a range of € 430 to 450 million. A material reason for the projected increase over the previous year is the acquisition of Corealcredit Bank.

Overall, we believe there is a good chance to achieve a consolidated operating profit of between € 370 million and € 390 million for the current financial year, including the non-recurring effect (due to negative goodwill) from the acquisition of Corealcredit Bank. Adjusted for this non-recurring effect, we anticipate consolidated operating profit of between € 220 million and € 240 million.

Excluding said non-recurring effect, return on equity (RoE) before taxes is projected to be around 9 %.

New business of between € 8 billion and € 9 billion is expected for the Structured Property Financing segment in 2014.

In the Consulting/Services segment, we anticipate a slightly higher result before taxes for Aareon of around € 28 million.

Corporate Governance Statement pursuant to section 289a of the HGB

The Corporate Governance Statement, including the Declaration of Compliance pursuant to section 161 of the German Public Limited Companies act (Aktiengesetz – “AktG”), disclosures regarding Corporate Governance standards, the description of work processes for the Management Board and the Supervisory Board, as well as Aareal Bank AG's Corporate Governance Report, are publicly available on the Company's website, at http://www.aareal-bank.com/investor-relations/corporate-governance/. Reference is made to the details disclosed there.

Principles of remuneration of members of the Management Board and the Supervisory Board

The Supervisory Board determines the structure and amount of remuneration for members of the Management Board. Aareal Bank AG has entered into fixed-term service contracts with the members of its Management Board.

In addition to their fixed annual salary components, Management Board members receive a performance-related bonus (variable remuneration) that is determined using an assessment basis extending over several years. The level of this performance-related bonus is determined by reference to the personal performance of each Management Board member which is measured by the degree to which targets set in advance by the Supervisory Board are achieved, based on contractually agreed initial values. The targets which are relevant for performance-related bonuses include annual targets and three-year targets. The weighting of annual to three-year targets is fixed for each financial year, with a 60 % / 40 % weighting taken as a guideline.

The annual and three-year targets are derived from the Bank’s overall strategy and the annual and medium-term planning of Aareal Bank Group, each of which are agreed upon with the Supervisory Board. The targets comprise quantitative components and qualitative components, with latter being also related to non-financial parameters. In this context, the Bank's overall performance, the performance of the relevant section, and the individual performance contributions of the Management Board member concerned are all taken into consideration.

The amount of the initial value of the performance-related bonus increases – depending on the Management Board member's degree of target achievement – up to a maximum of 200 %. If the target achievement exceeds a level of 200 %, the initial value of the performance-related bonus will not increase any further (cap). If target achievement is 0 %, no performance-related bonus will be awarded for the financial year concerned. The initial value is fixed at 100 % for target achievement levels between 90 % and 110 %.

To ensure that the remuneration system provides long-term incentive effects, performance-related bonuses are awarded at the end of the financial year, according to the following principles:

20 % of the performance-related bonus is paid as a cash bonus directly after theend of the financial year. A further 20 % of the performance-related bonus is awarded as a share bonus[11] in the form of phantom shares directly after the end of the financial year and are the subject of the Share Bonus Plan. 30 % of the performance-related bonus is deferred as a cash deferral (Cash Deferral). The remaining 30 % of the performance-related bonus is deferred as a share deferral[11] and is the subject of the Share Deferral Plan.

With regard to the portion of the performance-related bonus that is deferred initially as a cash deferral or a share deferral, the Supervisory Board makes a decision regarding the granting of one third of the amount, as well as the associated interest, in the three years following the determination of the performance-related bonus (retention period). If the deferred remuneration components for the Management Board members are actually awarded, the cash deferral is paid out in cash and the share deferral is converted into virtual shares, subject to a two-year holding period.

In making its determination about the amount to be awarded, the Supervisory Board particularly takes into account any negative aspects of the Management Board member's performance, his section, as well as any weakness in the performance of Aareal Bank AG or the Group as a whole. The final amount may be awarded in full, partially, or not at all. If theaward is not made in its full amount, the remainder is forfeited, i.e. it is not carried forward into subsequent years. No bonus may be awarded if BaFin makes an official ruling against the Bank pursuant to section 45 (2) of the German Banking Act (KWG) due to shortcomings relating to capital adequacy or liquidity issues. If a case of serious individual misconduct by a member of the Management Board is identified afterwards in the financial year in which the remuneration components were awarded as a cash deferral and share deferral, the retained remuneration components are cancelled in full. Members of the Management Board may not undertake to limit or override the risk orientation of the performance-related bonus by initiating personal protection measures or countermeasures (hedging ban).

Remuneration for the services of the Supervisory Board members is specified in Article 9 of the Memorandum and Articles of Association of Aareal Bank AG. The Annual General Meeting held on 18 May 2011 made the most recent adjustments to the system for the remuneration of the Supervisory Board.

Since that date, the remuneration system for the Supervisory Board has only comprised a fixed remuneration system, as well as a compensation for attending meetings. In addition, the Supervisory Board members will be reimbursed for their expenses. Where membership in the Supervisory Board falls short of an entire financial year, said remuneration shall be paid on a pro rata temporis basis. Any value-added tax invoiced will also be deemed to be a refundable expense.

The fixed remuneration is € 30,000 p.a. for each Supervisory Board member. The Chairman of the Supervisory Board shall receive two and a half times this amount, while the deputy shall receive one and a half times as much as a normal member. The fixed remuneration is increased by € 15,000 p.a. for each membership in a committee (with the exception of the Nomination Committee, which is an exclusively advisory committee, and the Committee for Urgent Decisions, which is part of the Risk Committee). The fixed remuneration is increased by € 30,000 p.a. for the chairmanship of a committee (with the exception of the Nomination Committee and the Committee for Urgent Decisions).

The meeting attendance compensation amounts to € 1,000.00 for each meeting attended (except for meetings of the Nomination Committee and the Committee for Urgent Decisions).

The remuneration for any financial year shall be due and payable one month after the end of the respective financial year.

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

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[11] Please refer to the subsection "Cash-settled share-based remuneration" in the remuneration report, which is part of the Notes to the Financial Statements, for details concerning the specifications of the Share Bonus Plan and the Share Deferral Plan.

Disclosures in accordance with section 289 (4) of the German Commercial Code (HGB)

Composition of subscribed capital

The composition of Aareal Bank AG's subscribed capital is shown in the notes to the financial statements. Each share casts one vote at a General Meeting. There are no shares with special rights granting supervisory powers to any shareholder or shareholder group. The Company currently does not hold any treasury shares, which would not be entitled to vote.

Restrictions affecting voting rights or the transfer of shares

The German Financial Markets Stabilisation Fund (SoFFin) agreed to provide a stabilisation measure to the Bank in March 2009, in the form of a silent participation. In the context of this stabilisation measure, SoFFin and the Bank's main shareholder, Aareal Holding Verwaltungsgesellschaft mbH ("Aareal Holding") entered into an agreement under which Aareal Holding has undertaken to maintain its stake in the Bank's capital (currently 15,916,881 shares) throughout the term of the recapitalisation, and to act in SoFFin's interest when casting certain votes during the General Meeting (or to seek SoFFin's opinion prior to such a poll). Furthermore, Aareal Holding has undertaken to exercise its voting rights for resolutions to be adopted by a General Meeting in such a way that Aareal Holding will retain its blocking minority.

In all other respects, the transfer and exercise of voting rights is governed exclusively by legal restrictions. Voting rights are not limited to a certain number of shares, or of votes. All shareholders who have registered to attend a General Meeting in good time, and who have provided the Company with evidence of their shareholding and their right to vote, are entitled to attend the General Meeting, and to exercise their voting rights from all shares held and so registered. The exercise of voting rights from the shares concerned is precluded by law in the cases where section 136 of the AktG applies. Where the company holds treasury shares, section 71b of the AktG prohibits the exercise of rights vested in such shares. We are not aware of any other restrictions affecting voting rights or the transfer of shares.

Shareholdings exceeding 10 % of voting rights

Details regarding any shareholdings exceeding 10 % of voting rights are provided in the notes to the financial statements.

Shares with special rights granting the holder supervisory powers

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

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

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

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

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

Pursuant to section 179 of the AktG, the Memorandum and Articles of Association may be amended by way of resolution passed by the General Meeting. Resolutions of the General Meeting regarding amendments to the Memorandum and Articles of Association are passed by a simple majority of the votes cast, or – to the extent permitted by law – by the majority of the issued share capital present at the Meeting. In accordance with section 181 (3) of the AktG, such amendments become effective upon their entry in the company's Commercial Register. In the event of a capital change, the Supervisory Board is authorised to modify the wording of the Articles of Association in line with the amount of the capital change (Article 5 (7) of the Memorandum and Articles of Association).

Authorisation of the Management Board to issue or repurchase shares

Authorised capital

The Annual General Meeting held on 23 May 2012 resolved to authorise the Management Board to increase, on one or more occasions, the Company's share capital by up to a maximum total amount of € 89,785,830 (Authorised Capital) by issuance of new shares for contribution in cash or in kind. This authorisation will expire on 22 May 2017. The shareholders must be granted subscription rights in the event of a capital increase against cash contributions. The Management Board is authorised to exclude shareholders' pre-emptive subscription rights in the event of a capital increase not exceeding 10 % of the issued share capital at the time of the authorisation becoming effective or being exercised, subject to approval by the Supervisory Board and provided that the issue price is not significantly lower than the prevailing market price of shares already listed, at the time of final determination of the issue price. Article 5 (4) lit. b) to d) of the Memorandum and Articles of Association sets out further conditions for excluding shareholders' pre-emptive subscription rights. The Management Board may exclude shareholders' pre-emptive subscription rights in the event of a capital increase against contributions in kind. When exercising this authorisation, the Management Board will restrict the exclusion of shareholders' pre-emptive rights to a total of 20 % of the Company's issued share capital. Accordingly, the aggregate exclusion of shareholders' subscription rights upon exercise of this authorisation must not exceed 20 % of the registered share capital at the time said authorisation comes into effect or is exercised. This limit also includes shares that are issued based on the authorisation passed by the General Meeting on 23 May 2012 as a result of convertible bonds and/or bonds with warrants issued subject to exclusion of shareholders' pre-emptive rights.

The authorised capital has not been utilised.

Conditional capital

Pursuant to Article 5 (5) of the Memorandum and Articles of Association, the share capital is subject to a conditional capital increase of up to € 30 million by means of issuing up to 10 million new notional no-par value bearer shares. The purpose of the conditional capital increase is the granting of shares to holders or creditors of convertible bonds and/or bonds with warrants issued in accordance with the authorisation by the General Meeting held on 19 May 2010. Under this authorisation, bonds with warrants or convertible bonds with an aggregate nominal amount of up to € 600 million may be issued until 18 May 2015. Under the authorisation, subsidiaries of Aareal Bank AG may also issue convertible bonds and / or bonds cum warrants, and subject to approval by the Supervisory Board allows the company to guarantee such issues as well as to issue shares to fulfil the resulting conversion or option rights. Subject to the approval of the Supervisory Board, the Management Board may exclude shareholders' pre-emptive rights in the certain cases. Notwithstanding the provisions of section 9 (1) of the AktG, in certain circumstances holders of conversion or option rights are entitled to be protected against dilution. The new shares will be issued at the conversion or option price to be set as defined in the resolution passed by the General Meeting on 19 May 2010. The conditional capital increase will be executed only to the extent that holders of conversion or option rights exercise such rights or any conversion obligation from such convertible bonds and/or bonds with warrants is performed, and to the extent that treasury shares are not utilised to service such convertible bonds and/or bonds cum warrants. The new shares will be entitled to a share in the profits from the beginning of the financial year in which they come into existence, by way of exercise or conversion. The Management Board is authorised to determine any further details of the conditional capital increase, subject to approval by the Supervisory Board. The purpose of this authorisation to issue convertible bonds and/or bonds cum warrants (where the issue of shares to honour the obligations under such convertible bonds and/or bonds cum warrants is covered by the conditional capital) is to provide the Management Board with the flexibility to act swiftly when raising finance, in the interests of the Company. The Management Board has not yet exercised this authorisation.

Authorisation to purchase treasury shares

The General Meeting held on 19 May 2010 authorised the Management Board, pursuant to section 71 (1) No. 7 of the AktG, to purchase and sell treasury shares for the purposes of securities trading, at a price not falling below or exceeding the average closing price of the Company's share in Xetra trading (or a comparable successor system) during the three trading days on the Frankfurt Stock Exchange prior to the relevant transaction by more than 10 %. This authorisation expires on 18 May 2015. The volume of shares acquired for this purpose must not exceed 5 % of the issued share capital of Aareal Bank AG at the end of any given day.

The General Meeting held on 19 May 2010 authorised the Management Board, pursuant to Section 71 (1) No. 8 of the AktG, up to 18 May 2015, to acquire and sell treasury shares for purposes other than securities trading, up to a maximum volume of 10 % of the issued share capital at the time of passing the resolution or – if this value is lower – of the share capital existing at the time of exercising this authorisation for purposes other than securities trading. Shares may be acquired via the stock exchange or by means of a public offer to buy, directed at all shareholders. Where acquisition is effected via the use of derivatives in the form of put or call options, or a combination of both, the option terms must ensure that said options are only serviced with shares that were purchased, in accordance with the principle of equal treatment, at the stock exchange at the prevailing share price of the Company's share in Xetra trading (or a comparable successor system) at the time of the purchase on the stock exchange.

The Management Board is authorised to effect the sale of any treasury shares acquired in accordance with this authorisation, subject to approval by the Supervisory Board, via channels other than the stock exchange or an offer to all shareholders, provided that the sale is carried out at a price that is not significantly lower than the stock exchange price of the Company's shares at the time of sale. This authorisation is subject to the proviso that the aggregate value of shares sold under this authorisation and of shares issued to the exclusion of shareholders' subscription rights, in accordance with section 186 (3) sentence 4 of the AktG, shall not exceed 10 % of the issued share capital at the time of said authorisation becoming effective or being exercised. Subject to approval by the Supervisory Board, pre-emptive subscription rights on the sold shares may also be excluded in the event of a sale against contributions in kind, or if the sold shares are given to the holders of conversion or option rights in lieu of new shares from a contingent capital increase. The Management Board is also authorised to exclude the pre-emptive subscription rights to the extent required to grant subscription rights to new shares to owners of convertible bonds or bonds cum warrants which were issued in the meantime in such an amount as would be due to them once they exercised their option rights. The Management Board is authorised to call in any of the shares acquired under this authorisation, without any further resolutions by the General Meeting being necessary. The Company did not exercise this authorisation to purchase or dispose of treasury shares during the year under review.

The authorisation to purchase treasury shares is granted for a five-year period; it is in line with widely accepted practice of German listed companies. In line with authorised capital and conditional capital, this serves the company's interest of having access to flexible financing options.

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

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

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

For details regarding compensation agreements entered into with members of the Management Board or employees in the event of a takeover bid, please refer to the Remuneration Report, which forms part of the notes to the financial statements.

Annual Financial Statements

Income statement of Aareal Bank AG for the period from 1 January to 31 December 2013

€ mn			2013		2012
Expenses					
Interest expenses			**982.9**		1,111.6
Commission expenses			**8.3**		12.0
General administrative expenses					
a) Staff costs					
aa) Wages and salaries	96.6			89.3	
ab) Social security contributions, pensions and other employee benefits	17.8	114.4		17.2	
including for pensions 7.8 (2012: 6.9)					
b) Other administrative expenses		114.3	**228.7**	105.5	212.0
Amortisation, depreciation and write-downs of intangible and tangible fixed assets			**3.7**		4.0
Other operating expenses			**12.7**		20.9
Write-downs and valuation allowances of loans and advances and specific securities, as well as additions to loan loss provisions			**130.0**		215.7
Amortisation and write-downs on participations, interests in affiliated companies, and investment securities			**13.8**		-
Expenses for assumption of losses			**33.6**		23.1
Net income taxes			**26.2**		-15.4
Other taxes not reported under other operating expenses			**0.4**		0.2
Net income			**49.9**		5.0
Total expenses			**1,490.2**		**1,589.1**
Net income / net loss			**49.9**		5.0
Profit carried forward from the previous year			**-**		-
Withdrawals from retained earnings					
from the reserve for shares in a parent or majority investor			**-**		-
from other retained earnings			**-**		-
Transfer to retained earnings					
to the reserve for shares in a parent or majority investor			**-**		-
to other retained earnings			**-**		-
Net retained profit			**49.9**		**5.0**

€ mn		2013		2012
Income				
Interest income from				
a) Lending and money market transactions	1,068.5		1,101.6	
b) Fixed-income securities and debt register claims	364.6	**1,433.1**	398.9	1,500.5
Current income from				
a) Equities and other non-fixed-income securities	-		0.2	
b) Participating interests	0.0		0.0	
c) Interests in affiliated companies	3.5	**3.5**		0.2
Income from profit pools, profit transfer agreements and partial profit transfer agreements		**5.2**		0.8
Commission income		**29.8**		65.9
Income from write-ups to participating interests, shares in affiliated companies and securities held as fixed assets		**-**		2.1
Other operating income		**18.6**		19.6
Total income		**1,490.2**		**1,589.1**

Balance sheet of Aareal Bank AG as at 31 December 2013

€ mn			2013		2012
Assets					
Cash funds					
a) Cash on hand		0.0		0.0	
b) Balances with central banks		1,223.0	**1,223.0**	3,666.7	3,666.7
including: with Deutsche Bundesbank 1,196.1 (2012: 3,639.0)					
Loans and advances to banks					
a) Loans secured by charges on real property		8.6		9.0	
b) Loans to local authorities		102.2		112.3	
c) Other loans and advances		2,639.5	**2,750.3**	1,639.7	1,761.0
including: payable on demand 743.8 (2012: 1,239.1)					
Loans and advances to customers					
a) Loans secured by charges on real property		21,670.0		20,851.0	
b) Loans to local authorities		1,212.1		1,329.1	
c) Other loans and advances		2,613.7	**25,495.8**	2,139.5	24,319.6
Debt and other fixed-income securities					
a) Money market instruments		-		-	
b) Bonds and notes					
ba) Public-sector issuers	7,575.3			7,583.9	
including: with Deutsche Bundesbank 6,646.1 (2012: 7,190.9)					
bb) Other issuers	2,084.0	9,659.3		3,304.5	
including: with Deutsche Bundesbank 1,917.9 (2012: 2,691.9)					
c) Own bonds		1,416.8	**11,076.1**	1,416.5	12,304.9
Nominal amount: 1,409,2 (2012: 1,411.8)					
Equities and other non-fixed income securities			**141.6**		145.7
Participating interests			**1.3**		1.4
including: interests in banks 0.8 (2012: 0.8)					
interests in financial services providers - (2012: -)					
Interests in affiliated companies			**710.0**		645.7
including: interests in banks 8.8 (2012: 9.0)					
interests in financial services providers - (2012: -)					
Trust assets			**73.3**		102.8
including: Trustee loans 71.8 (2012: 101.2)					
Intangible assets					
a) Internally generated industrial property rights and similar rights and assets		-		-	
b) Purchased concessions, industrial property rights and similar rights and assets as well as licences in such rights and assets		2.0		2.1	
c) Goodwill		-		0.0	
d) Advance payments made		-	**2.0**	-	2.1
Tangible fixed assets			**11.3**		10.8
Other assets			**136.1**		31.7
Prepaid expenses			**203.5**		89.6
Deferred tax assets			**171.0**		120.0
Total assets			**41,995.3**		**43,202.0**

€ mn			2013		2012
Equity and liabilities					
Liabilities to banks					
a) Outstanding registered mortgage Pfandbriefe		237.9		251.8	
b) Outstanding registered public sector Pfandbriefe		42.8		82.9	
c) Other liabilities		1,462.2	**1,742.9**	3,116.0	3,450.7
including: payable on demand 775.3 (2012: 914.3)					
Liabilities to customers					
a) Outstanding registered mortgage Pfandbriefe		2,998.9		3,252.1	
b) Outstanding registered public sector Pfandbriefe		2,231.2		2,807.0	
c) Savings deposits					
ca) With an agreed notice period of three months	-			-	
cb) With an agreed notice period of more than three months	-	-		-	
d) Other liabilities		19,556.5	**24,786.6**	19,928.9	25,988.0
including: payable on demand 5,009.5 (2012: 5,226.2)					
Certificated liabilities					
a) Bonds issued					
aa) Mortgage Pfandbriefe	8,150.8			6,637.5	
ab) Public sector Pfandbriefe	35.0			35.0	
ac) Other debt securities	3,413.8	11,599.6		3,033.6	
b) Other certificated liabilities		-	**11,599.6**	-	9,706.1
including: money market instruments - (2012: -)					
Trust liabilities			**73.3**		102.8
including: Trustee loans 71.8 (2012: 101.2)					
Other liabilities			**175.2**		358.4
Deferred income			**109.3**		83.3
Deferred tax liabilities			**18.7**		22.0
Provisions					
a) Provisions for pensions and similar obligations		86.1		82.2	
b) Tax provisions		31.7		8.1	
c) Other provisions		102.9	**220.7**	99.1	189.4
Subordinated liabilities			**752.2**		780.9
including: maturing within two years 37.5 (2012: 136.3)					
Profit-participation certificates			**157.0**		210.5
including: maturing within two years 102.0 (2012: 135.0)					
Fund for general banking risks			**167.6**		167.6
Equity					
a) Subscribed capital		179.6		179.6	
Contributions by silent partners		520.2		520.2	
b) Capital reserve		727.8		727.8	
c) Retained earnings					
ca) Legal reserve	4.5			4.5	
cb) Reserve for treasury shares	-			-	
cc) Statutory reserves	-			-	
cd) Other retained earnings	710.2	714.7		705.2	
d) Net retained profit		49.9	**2,192.2**	5.0	2,142.3
Total equity and liabilities			**41,995.3**		**43,202.0**

€ mn		2013		2012
Contingent liabilities				
a) Contingent liabilities from discounted forwarded bills	-		-	
b) Liabilities from guarantees and indemnity agreements	205.0		626.5	
c) Liability from the pledging of collateral for third-party liabilities	-	**205.0**	-	626.5
Other commitments				
a) Repurchase obligations from securities repurchase agreements	-		-	
b) Placement and underwriting obligations	-		-	
c) Irrevocable loan commitments	1,186.7	**1,186.7**	2,234.0	2,234.0

Notes

Basis of accounting

The financial statements of Aareal Bank AG for the financial year 2013 were prepared in accordance with the provisions of the German Commercial Code (Handelsgesetzbuch – ”HGB”) and the supplementary regulations of the German Public Limited Companies Act (Aktiengesetz – ”AktG”) and the German Accounting Directive for Banks and Financial Services Providers (Verordnung über die Rechnungslegung der Kreditinstitute und Finanzdienstleistungsinstitute – ”RechKredV”).

Accounting and valuation principles

Loans and advances

Loans and advances to banks and customers are carried at amortised cost, including deferred interest. Premiums and discounts are shown under deferred items, in accordance with section 340e (2) of the HGB. Credit risks are accounted for by setting aside provisions in the amount of the expected loss, using prudent estimates.

Portfolio-based valuation allowances are recognised for risks which have already materialised, but which cannot be allocated to individual loans and advances due to lack of knowledge. For this purpose, groups of financial assets with comparable default risk profiles are combined in portfolios and reviewed for impairment. The valuation allowances are calculated using a formula-based procedure based on the following Basel II parameters used in the advanced IRB Approach: expected loss given default (LGD) and probability of default (PD). The transition of the one-year probability of default, which represents the basis for the concept of expected loss pursuant to the German Solvency Regulation (Solvabilitätsverordnung), to the concept of incurred loss is made using the LIP (Loss Identification Period) factor. The LIP factor is a correction factor to adjust the one-year probability of default to the estimated time period, from the date the loss is incurred up to the identification of the actual loss.

Securities

Bonds and other fixed-income securities, as well as equities and other non-fixed income securities, are measured strictly at the lower of cost or market value, as prescribed for current assets, taking into account hedging instruments. Where the reasons for the write-down no longer apply, write-ups are made in accordance with section 253 (5) of the HGB. Investment securities are valued at the lower of cost or market. Differences between cost and amounts repayable are amortised in income.

Participating interests, interests in affiliated companies, intangible assets and tangible assets

Participating interests and interests in affiliated companies are stated at cost. Tangible assets and purchased intangible assets are stated at cost less depreciation/amortisation. Write-downs are required in the event of impairments in value deemed to be other than temporary.

Where the reasons for the write-down no longer apply, write-ups are recognised for participating interests, interests in affiliated companies, intangible assets and tangible assets in accordance with section 253 (5) of the HGB. Where land and buildings were acquired to salvage loans and have been in the possession of the Bank for more than five years, these are reported under tangible fixed assets. Additions of low-value commercial goods ("geringwertige Wirtschaftsgüter") not exceeding € 150 are fully written off in the year of acquisition, and accounted for as disposals. In addition, Aareal Bank AG made use of the simplification rule pursuant to section 6 (2a) of the German Income Tax Act (Einkommensteuergesetz – "EStG").

The option to disclose a net amount, pursuant to section 340c (2) of the HGB has been exercised.

Deferred taxes

If there are differences between the book value of assets, liabilities, deferred income and prepaid expenses and their related tax bases, which are expected to be reversed in later financial years, any resulting net tax burden is recognised as a deferred tax liability and any resulting net tax benefit is recognised as a deferred tax asset, in accordance with section 274 of the HGB. Tax loss carryforwards are taken into account in the calculation of deferred tax assets, based on the level of the potential losses to be offset within the next five years. Deferred taxes are measured using the company- and country-specific tax rates expected to apply at the time of the realisation of temporary differences and the offsetting of loss carryforwards. The Bank discloses deferred taxes on a gross basis, in accordance with section 274 (1) sentence 3 of the HGB.

Liabilities

Liabilities are shown on the balance sheet at the settlement amount. The difference between the settlement amount and the initial book value of liabilities is recognised under deferred items, and amortised over the term of the liability.

Provisions

Provisions are recognised in the amount of the required settlement amount, as determined based on prudent commercial judgement. Pursuant to section 253 (2) sentence 1 of the HGB, provisions with a remaining term of more than one year have to be discounted using the market interest rate of the past seven years applicable for their average remaining term.

Provisions for pensions and similar obligations are determined in accordance withactuarial principles. Provisions for pensions are recognised at thesettlement amount taking into account future wage, salary and pension trends and applying the average market interest rate applicable for an assumed remaining term of 15 years as disclosed by Deutsche Bundesbank, except where the applicable remaining term of the respective pension plan is shorter.

Provisions for taxes and other provisions have been set aside for existing legal or constructive obligations in the settlement amount, as required by prudent commercial judgement.

Currency translation

Currency translation complies with the principles set out in sections 256a and 340h of the HGB.

The Bank has classified all foreign exchange transactions as “specific cover“ and measured these using the middle spot rate (ECB reference middle rate) in accordance with section 340h of the HGB. Hence, income and expenses from currency translation were recognised in the income statement.

The Bank decomposes foreign exchange forward transactions which are used to hedge interest-bearing balance sheet items into an agreed spot base and the swap rate, recognising a deferred asset or liability equivalent to the net aggregate difference between the spot base and the exchange rates prevailing on the reporting date. Forward premiums or discounts are amortised in net interest income over the term of the transaction.

Currency translation income and expenses are reported in net other operating income/expense.

Trading portfolio

There were no financial instruments of the trading portfolio as at the balance sheet date.

Hedging relationships

The Bank establishes hedging relationships within the meaning of section 254 of the HGB. Accordingly, fixed-income securities of the liquidity reserve in the amount of € 4,877.66 million are hedged against changes in value attributable to interest rate risk, on the basis of so-called "micro hedges". In this context, the underlying transaction and the hedge generally are acquired within the framework of so-called "asset swap packages", i.e. they are so-called "perfect hedges" where all value-affecting factors between the hedged portion of the underlying transaction substantially correspond to the hedging portion of the hedge. The prospective effectiveness of the hedging relationship, which refers to the period until the security's final maturity, is proven, based on the so-called "critical terms match method". Regression and correlation coefficients are used as criteria to measure retrospective effectiveness.

This is presented in the financial statements using the so-called "net hedge presentation method" (Einfrierungsmethode). Under this method, the cumulative changes in the value of the underlying transaction is determined on the basis of the hedged risk, and compared to the changes in the value of the hedge. The hedged risk amounts to € 448.37 million and corresponds to the cumulative increase of the fair value of assets since inception of the hedging relationship. This increase is not shown in the income statement on a net basis, after including hedge transactions. Any previously existing ineffectiveness based on the hedged risk is reflected in a provision for hedging relationships. The changes in value attributable to the hedged risk are reflected on a portfolio basis, in the form of a write-down on the security concerned.

The Bank continues to establish hedging relationships between repurchased own bonds in a nominal amount of € 1,411.23 million and the corresponding securitised liabilities.

Fair value measurement of interest rate instruments of the banking book

In addition, the Bank uses derivative financial instruments of the banking book (non-trading book), above all interest rate swaps, for the purpose of controlling interest rate risk (interest spread risk) as part of overall management of the Bank. In accordance with HGB, these instruments represent "pending transactions" which are not recognised in the balance sheet. They form a "hedging relationship", together with the recognised interest-bearing assets and liabilities of the banking book. In accordance with IDW RS BFA 3, this hedging relationship has to be reviewed as to whether losses are anticipated, taking into account expenses expected to be required for funding, risk management and administration in relation to managing the banking book. Currently, the Bank has two equal methods available to determine provisions for anticipated losses: the (P&L based) approach referring to certain time periods, and the (static) present value method. The Bank uses the present value method. Under this method, a provision has to be recognised when the book value of the banking book exceeds the present value of the banking book, i.e. if there are net unrealised losses in the banking book. The present value is derived from the cash flows of the financial instruments included in the banking book, discounted to the balance sheet date. Potential future risk costs are considered by adjusting the applicable interest rate used for the discounting of cash flows. The administrative expenses relating to the banking book are derived from cost accounting and deducted on a lump-sum basis. No provision for anticipated losses had been recognised as at the balance sheet date since the present value of the banking book is higher than the book value as at 31 December 2013.

Derivatives

Derivative financial instruments are considered pending transactions, and are therefore generally not recorded in the balance sheet.

Exchange-traded derivatives are measured at their quoted market price. The market price of over-the-counter (OTC) derivatives is determined using standard valuation models commonly accepted in the financial industry, such as the present value technique and option pricing models. The fair value of foreign exchange forwards is generally based on current forward exchange rates.

Acquired as well as issued structured products are generally accounted for as groups of uniform assets and liabilities in accordance with IDW RS HFA 22.

Structured products subject to significantly higher or additional risks or rewards are accounted for separately as individual receivables or liabilities.

Notes to the income statement

Income by geographical segment

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

€ mn	2013	2012
Germany	1,387.1	1,430.2
Europe / Americas / Asia	97.9	156.0
Total	**1,485.0**	**1,586.2**

Administration and intermediation services rendered to third parties

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

Other operating income and expenses

Other operating income totals € 18.6 million (2012: € 19.6 million) and comprises income from the reversal of provisions in the amount of € 9.3 million, the result from currency translations in the amount of € 2.5 million (2012: € 1.6 million), and income from tax refunds amounting to € 2.5 million. In addition, income under agency contracts for other Group subsidiaries in the amount of € 1.7 million is also recognised.

Other operating expenses total € 12.7 million (2012: € 20.9 million) and include expenses for subsidiaries in the amount of € 6.9 million, of which € 5.2 million is attributable to agency contracts for other Group companies. In addition, the item includes expenses in the amount of € 4.9 million from unwinding of the discount of provisions, after offsetting with income from plan assets used for pension obligations pursuant to section 246 (2) sentence 2 of the HGB.

Net income taxes

The net income tax position amounts to an expense of € 26.2 million (2012: income of € 15.4 million), of which an expense of € 71.5 million included in current taxes is payable in Germany: this figure comprises € 33.3 million in corporation tax and solidarity surcharge and € 34.3 million in trade tax payable for the current year, as well as € 3.9 million in tax expense for previous years. The net income tax position also includes € 38.1 million in income from the capitalisation of deferred taxes and € 7.2 million in expenses for the Bank's foreign branch offices.

The tax reconciliation is used to determine why the tax expense (current taxes and deferred taxes) reported in the income statement differs from the expense calculated using the expected tax rate of 31.2 % (2012: 31.2 %), which represents the current tax rate in Germany (trade tax rate of 15.4 %, corporation tax rate of 15 % and solidarity surcharge of 5.5 %).

€ mn	31 Dec 2013	31 Dec 2012
Income before income taxes	76.1	-10.4
Expected income tax expenses; tax rate: 31.2% (unchanged yoy)	23.8	-3.3
Reconciliation		
Different foreign tax burden	-1.3	-4.3
Tax attributable to tax-exempt income	-18.1	-17.0
Tax attributable to non-deductible expenses	14.1	17.9
Remeasurement of deferred taxes	2.4	2.2
Prior-period actual taxes	5.3	-10.9
Reported income tax expenses	26.2	-15.4
Effective tax rate (%)	34.4	147.9

Prohibition of distribution

A total amount of € 156.3 million in profits is subject to a prohibition of distribution, pursuant to section 268 (8) of the HGB, of which € 152.3 million is attributable to the balance resulting from recognised deferred tax assets and recognised deferred tax liabilities. A prohibition of distribution applies to a net amount of € 4.0 million (after fair-value netting of assets), pursuant to section 246 (2) sentence 2 of the HGB.

Notes to the balance sheet

Securities negotiable at a stock exchange

Analysis of securities negotiable at a stock exchange in the balance sheet line items shown below (excluding pro-rata interest):

€ mn	Listed 31 Dec 2013	Unlisted 31 Dec 2013
Debt and other fixed-income securities	10,885.7	0.0
Equities and other non-fixed income securities	0.4	0.0
Participating interests	-	-
Interests in affiliated companies	0.0	0.0

Hedging relationships as defined by section 254 of the HGB have been created with respect to negotiable securities in an aggregate amount of € 6,288.9 million (2012: € 6,193.4 million).

Bonds and notes of € 11,076.1 million (2012: € 12,304.9 million) (including accrued interest) reported under debt and other fixed-income securities include € 1,475.0 million (2012: € 1,005.6 million) in securities which are not eligible as collateral with Deutsche Bundesbank. Of that amount, € 290.8 million (2012: € 342.9 million) relate to sovereign foreign-currency bonds, which are eligible for securities lending.

Bonds of selected European countries

The following table is an overview of the bonds issued by public-sector entities and bank bonds of selected European countries, included in the item "debt securities and other fixed-income securities":

Bond values as at 31 Dec 2013

€ mn		Greece	Ireland	Italy	Portugal	Spain	Total
Bonds issued by public-sector entities (liquidity reserve)*							
	Nominal amount			430		25	**455**
	Book value			415		26	**441**
	Fair value			462		30	**492**
Bonds issued by public-sector entities (securities held as fixed assets) *							
	Nominal amount			839	155	312	**1,306**
	Book value			859	156	314	**1,329**
	Fair value			900	144	266	**1,310**
Covered bank bonds (liquidity reserve)							
	Nominal amount			70	60	195	**325**
	Book value			71	57	204	**332**
	Fair value			74	64	210	**348**
Covered Bank Bonds (securities held as fixed assets)							
	Nominal amount					353	**353**
	Book value					363	**363**
	Fair value					379	**379**
Senior unsecured bank bonds (liquidity reserve)							
	Nominal amount			13			**13**
	Book value			12			**12**
	Fair value			13			**13**
Senior unsecured bank bonds (securities held as fixed assets)							
	Nominal amount			0			**0**
	Book value			0			**0**
	Fair value			0			**0**
Total	**Nominal amount**		**0**	**1,352**	**215**	**885**	**2,452**

* All bonds issued by public-sector debtors, including government-guaranteed bonds.

Bond values as at 31 Dec 2012

€ mn		Greece	Ireland	Italy	Portugal	Spain	Total
Bonds issued by public-sector entities (liquidity reserve)*							
	Nominal amount			410		25	**435**
	Book value			368		26	**394**
	Fair value			424		27	**451**
Bonds issued by public-sector entities (securities held as fixed assets) *							
	Nominal amount			839	155	312	**1,306**
	Book value			859	156	314	**1,329**
	Fair value			856	135	233	**1,224**
Covered bank bonds (liquidity reserve)							
	Nominal amount			70	60	100	**230**
	Book value			70	49	100	**219**
	Fair value			73	58	105	**236**
Covered Bank Bonds (securities held as fixed assets) *							
	Nominal amount					501	**501**
	Book value					514	**514**
	Fair value					512	**512**
Senior unsecured bank bonds (liquidity reserve)							
	Nominal amount			13			**13**
	Book value			12			**12**
	Fair value			13			**13**
Senior unsecured bank bonds (securities held as fixed assets) *							
	Nominal amount			23			**23**
	Book value			23			**23**
	Fair value			24			**24**
Total	**Nominal amount**			**1,355**	**215**	**938**	**2,508**

* All bonds issued by public-sector debtors, including government-guaranteed bonds.

Investment fund units

€ mn	Book value 31 Dec 2013	Market value 31 Dec 2013	Book value 31 Dec 2012	Market value 31 Dec 2012
DBB INKA	100.4	100.4	101.5	101.5
Arsago Multistrategie	40.7	40.7	40.7	40.7
Balance as at 31 Dec 2013	**141.1**	**141.1**	**142.2**	**142.2**

DBB INKA is an investment fund as defined under German law (Sondervermögen) which invests in assets permitted under the German Investment Act (Investmentgesetz – "InvG"), observing the principle of risk diversification. The Arsago Multistrategie fund is a multi-strategy hedge fund which uses derivative instruments to gain exposure to various interest rate, currency and macro strategies.

Daily fund unit redemption is subject to certain restrictions. The value of investment fund units as defined by section 36 of the InvG is € 141.1 million. During the financial year under review, no distributions were made under the funds.

Subordinated assets

The following items comprise subordinated assets in the amount shown:

€ mn	31 Dec 2013	31 Dec 2012
Loans and advances to banks	-	-
Loans and advances to customers	4.6	10.5
Debt and other fixed-income securities	-	-
Equities and other non-fixed income securities	0.4	0.4
Other assets	-	-

Movements in fixed assets:

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

The values shown for debt and other fixed-income securities include additions and disposals, as well as changes in inventory due to the amortisation of premiums and discounts (excluding accrued interest).

	Debt and other fixed-income securities	Participating interests	Interests in affiliated companies	Intangible assets	Tangible assets	
€ mn					Office furniture and equipment	Land and buildings
Cost						
Balance as at 1 Jan 2013	5,325.8	2.5	716.0	37.5	34.7	0.1
Additions	0.0	0.0	64.3	1.0	3.2	0.0
Disposals	1,342.8	0.0	0.0	0.6	4.3	0.0
Changes in inventory / transfers	0.0	-0.2	0.2	0.0	0.0	0.0
As at 31 Dec 2013	**3,983.0**	**2.3**	**780.5**	**37.9**	**33.6**	**0.1**
Depreciation, amortisation and write-downs						
Balance as at 1 Jan 2013	**0.0**	**1.1**	**70.4**	**35.4**	**24.0**	0.0
Depreciation and amortisation	0.0	0.0	0.0	1.1	2.5	0.0
Write-downs	0.0	0.0	0.2	0.0	0.0	0.0
Disposals	0.0	0.1	0.0	0.6	4.1	0.0
Transfers	0.0	0.0	0.0	0.0	0.0	0.0
Write-ups	0.0	0.0	0.1	0.0	0.0	0.0
As at 31 Dec 2013	**0.0**	**1.0**	**70.5**	**35.9**	**22.4**	**0.0**
Book value as at 31 Dec 2013	**3,983.0**	**1.3**	**710.0**	**2.0**	**11.2**	**0.1**
Book value as at 31 Dec 2012	5,325.8	1.4	645.7	2.1	10.7	0.1

As at 31 December 2013, the securities held as fixed assets include an ABS portfolio of high credit quality, bonds of North American financial institutions as well as securities issued by Eastern and Southern European debtors. The following performance was recognised:

€ mn	Book value 31 Dec 2013	Market value 31 Dec 2013	Book value 31 Dec 2012	Market value 31 Dec 2012
Asset-backed securities	162.5	141.8	262.9	206.5
Bank bonds	489.8	518.5	743.2	785.0
Covered bonds	722.6	764.6	995.3	1,033.5
Public-sector issuer	2,608.1	2,781.1	3,324.4	3,476.4
Total	**3,983.0**	**4,206.0**	**5,325.8**	**5,501.4**

Securities with a nominal amount of € 3,991.9 million were not measured at the lower of cost or market. For some of the securities issued by public-sector entities and the ABS portfolio, the book value in the amount of € 629.0 million and € 162.5 million respectively is higher than the market value of € 556.6 million and € 141.8 million respectively. An examination of cost vs. market values as at 31 December 2013 did not indicate any permanent impairment.

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

The Bank has rented the majority of business land and buildings used for its business operations from one of its subsidiaries.

Other assets

Other assets include, in particular, € 111,9 million recognised from currency translation, receivables from profit and loss transfer agreements as well as receivables from profit distributions of € 5.1 million and € 18.5 million in tax receivables.

In the previous year, other assets included, in particular, € 23.8 million in tax receivables and € 1.2 million in receivables from profit and loss transfer agreements.

Deferred taxes

As at 31 December 2013, € 171.0 million (2012: € 120.0 million) in deferred tax assets and € 18.7 million (2012: € 22.0 million) in deferred tax liabilities were reported on the balance sheet. Deferred taxes are recorded in the amount of the assumed tax burden or relief in coming financial years, and are measured using the company- and country-specific tax rates expected to apply at the time of the realisation of temporary differences and the offsetting of loss carryforwards.

For Germany, we generally used a corporate income tax rate (including solidarity surcharge) of 15.8 % and a municipal trade tax rate, depending on the multiplier set by the relevant local authorities. This results in a tax rate of 31.2 % for Germany.

Deferred tax assets were largely recognised for valuation differences for debt and fixed-income securities as well as loans and advances to customers compared to their tax base, provisions for impending losses from executory contracts, as required under German commercial law, prepaid expenses for collected loan fees as well as on provisions for pensions. Deferred tax assets in the amount of € 6.8 million (2012: € 6.4 million) were recognised for loss carryforwards.

Deferred tax liabilities were recognised primarily for flat-rate specific provisions on receivables of the permanent establishment in Rome.

Other liabilities

Other liabilities include profit entitlements from silent participations in the amount of € 39.5 million, of which € 6.3 million become legally payable only after the balance sheet date, with the profit appropriation decision of the Annual General Meeting. In addition, € 35.3 million in liabilities from profit and loss transfer agreements and tax liabilities of € 16.2 million are recognised.

In the previous financial year, other liabilities included, in particular,€ 270.8 million in liabilities recognised from currency translation, and € 37.4 million in liabilities from profit entitlements from silent participations.

Provisions for pensions and similar obligations

The values determined in the actuarial pension report are based on the following methods and assumptions:

	31 Dec 2013	31 Dec 2012
Actuarial method applied:	Projected unit credit method	Projected unit credit method
Fundamental assumptions for calculation:		
Discount rate in %	4.90	5.06
Expected wage and salary increases in %	2.25	2.25
Mortality tables used	"Richttafeln 2005G" mortality tables by Prof Dr Klaus Heubeck	"Richttafeln 2005G" mortality tables by Prof Dr Klaus Heubeck

Assets which are held exclusively for the purpose of fulfilling pension obligations are netted against provisions for pensions, within the framework of a Contractual Trust Agreement (CTA) where the trustee is acting on behalf of both parties (in the capacity of an administrative trustee and security trustee).

€ mn	31 Dec 2013	31 Dec 2012
Pension obligation	135.2	126.5
Fair value of plan assets	49.1	44.3
Cost of plan assets	45.1	40.4
Provisions for pensions and similar obligations	**86.1**	**82.2**

The plan assets comprise the following items, all of which are exclusively reserved to meet Aareal Bank AG's pension obligations vis-à-vis its active and retired employees in Germany.

€ mn	31 Dec 2013	31 Dec 2012
Fund units	13.1	11.5
Bonds	15.6	13.5
Reinsurance cover	20.4	19.3
Fair value of plan assets	**49.1**	**44.3**

The following table shows the income and expenses in relation to pension obligations and the associated plan assets that were offset and recognised in the income statement of the reporting year.

€ mn	31 Dec 2013	31 Dec 2012
Interest cost on pension obligations	6.3	6.0
Income from plan assets	2.0	3.8
Net interest cost	**4.3**	**2.2**

Subordinated liabilities

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

Total interest expenses for subordinated liabilities of € 42.6 million include € 12.7 million in deferred interest not yet due.

Aareal Bank AG has € 250.0 million in subordinated equity from Aareal Capital Funding LLC, Wilmington, USA, at its disposal. The amount exceeds 10 % of the aggregate nominal value of all subordinated liabilities; this bears an interest of 7.135 %. These subordinated funds are due for repayment on 31 December 2026. The Bank has had a right to terminate, on a quarterly basis, since 31 December 2006; the creditors do not have any early termination rights.

Profit-participation certificates

Profit-participation certificates issued comprises the following certificates issued by Aareal Bank AG.

The profit-participation certificates recognised on the balance sheet are eligible as liable equity capital pursuant to section 10 (5) of the KWG in the amount of € 46.0 million (2012: € 63.0 million).

€ mn	Nominal amount	Issue currency	Interest rate (% p.a.)	Maturity
Bearer profit-participation certificates:	60.0	EUR	6.125	2003 - 2013
	60.0			
Registered profit-participation certificates:	5.0	EUR	7.220	2002 - 2016
	5.0	EUR	7.220	2002 - 2016
	5.0	EUR	6.080	2003 - 2013
	20.0	EUR	6.120	2003 - 2013
	5.0	EUR	6.310	2003 - 2017
	10.0	EUR	5.750	2004 - 2014
	2.0	EUR	5.470	2004 - 2014
	5.0	EUR	5.480	2004 - 2014
	5.0	EUR	5.380	2004 - 2016
	20.0	EUR	5.950	2004 - 2016
	6.0	EUR	5.830	2005 - 2017
	88.0			

Pursuant to the terms and conditions of issue, holders of profit-participation certificates have a claim on interest payments which takes precedence over the profit entitlements of shareholders. Where a distribution during the term of the profit-participation certificates would cause a net loss, said interest claim would be reduced, possibly down to zero, creating a claim for backpayment during the term of the certificates at the same time.

Repayment takes place at the nominal amount (subject to any loss sharing), after the Annual General Meeting passing resolutions regarding the relevant financial year.

€ 10.8 million in interest expenses were incurred in 2013 with respect to profit-participation certificates issued.

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

Purchase of treasury shares

The Management Board was authorised by the Annual General Meeting held on 19 May 2010 pursuant to section 71 (1) no. 7 of the German Public Limited Companies Act (AktG) to purchase and sell treasury shares until 18 May 2015 for the purposes of securities trading at prices that may not be higher or lower than 10 % than the average closing price of the shares in Xetra (or a comparable successor system) of the Frankfurt Stock Exchange during the three trading days prior to purchase. The volume of shares acquired for this purpose must not exceed 5 % of the share capital of Aareal Bank AG at the end of any day.

The General Meeting held on 19 May 2010 also authorised the Management Board, pursuant to Section 71 (1) No. 8 of the AktG, up to 18 May 2015, to acquire and sell treasury shares for purposes other than securities trading, up to a maximum volume of 10 % of the issued share capital at the time of passing the resolution or – if this value is lower – of the share capital existing at the time of exercising this authorisation for purposes other than securities trading. Shares may be acquired via the stock exchange or by means of a public offer to buy, directed at all shareholders. Where acquisition is effected via the use of derivatives in the form of put or call options, or a combination of both, the option terms must ensure that said options are only serviced with shares that were purchased, in accordance with the principle of equal treatment, at the stock exchange at the prevailing share price of the Company's share in Xetra trading (or a comparable successor system) at the time of the purchase on the stock exchange.

The Management Board is authorised – subject to certain conditions and subject to exclusion of shareholders' pre-emptive rights – to effect the sale of any treasury shares acquired in accordance with this authorisation, via channels other than the stock exchange or an offer to all shareholders. The Management Board is authorised to call in any of the shares acquired under this authorisation, without any further resolutions by the General Meeting being necessary.

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

Development of shareholders' equity reported on the balance sheet

€ mn	Subscribed capital	Capital reserves	Retained earnings: Legal reserve	Retained earnings: Other retained earnings	Net retained profit	Equity
Balance as at 1 Jan 2013	**699.8**	**727.8**	**4.5**	**705.2**	**5.0**	**2,142.3**
(of which: contributions by silent partners)	(520.2)	-	-	-	-	(520.2)
Transfer from net retained profit 2012	-	-	-	5.0	-5.0	-
Transfer from net income 2013	-	-	-	0.0	49.9	49.9
As at 31 Dec 2013	**699.8**	**727.8**	**4.5**	**710.2**	**49.9**	**2,192.2**
(of which: contributions by silent partners)	(520.2)	-	-	-	-	(520.2)

Subscribed capital amounts to € 179.6 million (2012: € 179.6 million) and is divided into 59,857,221 (2012: 59,857,221) bearer shares with a proportionate share in the nominal share capital of € 3.00 per share.

On 31 March 2009, the German Financial Markets Stabilisation Fund (SoFFin) provided the € 525.0 million silent participation to Aareal Bank AG, agreed upon as part of the package of support measures on 15 February 2009. This perpetual silent participation bears interest at 9 % p.a. On 16 July 2010, Aareal Bank AG repaid a first tranche of € 150.0 million of the € 525.0 million silent participation provided by the German Financial Markets Stabilisation Fund (SoFFin). On 28 April 2011, Aareal Bank AG made a second partial repayment, in the amount of € 75.0 million.

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

Authorised capital

Aareal Bank has authorised capital pursuant to the resolution by the Annual General Meeting held on 23 May 2012. Accordingly, the Management Board is authorised to increase, on one or more occasions, the Company's share capital by up to a maximum total amount of € 89,785,830 (Authorised Capital 2012) by issuance of new bearer shares for contribution in cash or in kind, subject to the approval of the Supervisory Board; this authority will expire on 22 May 2017. In the event of a capital increase against cash contributions, the shareholders shall be granted a subscription right, unless the Management Board exercises its authority to exclude shareholder's pre-emptive subscription rights. The Management Board may exclude shareholders' subscription rights, subject to approval by the Supervisory Board and the conditions set out below:

a) In the event of a capital increase against cash contributions, provided that the issue price of the new shares is not significantly below the prevailing stock exchange price of the Company's listed shares at the time of the final determination of the issue price. However, this authorisation shall be subject to the proviso that the aggregate value of shares sold to the exclusion of shareholders' subscription rights, in accordance with section 186 (3) sentence 4 of the German Public Limited Companies Act (*Aktiengesetz* – "AktG"), shall not exceed ten per cent (10 %) of the registered share capital at the time said authorisation comes into effect or – in case such amount is lower – is exercised. Any shares that were issued or sold during the term and prior to the exercising of said authorisation, in direct or analogous application of section 186 (3) sentence 4 of the AktG, shall count towards the above threshold of ten per cent (10 %) of the registered share capital. Said ten-per-cent threshold shall also include shares the issuance of which is required under the terms of debt securities with embedded conversion or option rights on shares issued pursuant to section 186 (3) sentence 4 of the AktG (excluding shareholders' subscription rights), which were (or may be) issued during the validity of this authorisation;
b) For fractional amounts arising from the determination of the applicable subscription ratio;
c) Where this is necessary to grant subscription rights to the holders of bonds with warrants or convertible bonds issued (or to be issued) by the Company or its affiliated companies, which subscription rights are required to entitle these holders to the same extent as they would have been entitled to upon exercising their conversion or option rights or upon performance of a conversion obligation, if any, thus protecting such holders against dilution;
d) For an amount of up to € 4,000,000, to offer employees (of the Company or its affiliated companies) shares for subscription.

In the event of a capital increase against contributions in kind, the Management Board is authorised to exclude shareholders' subscription rights, subject to the approval by the Supervisory Board.

When exercising this authorisation, the Management Board will restrict the exclusion of shareholders' pre-emptive rights to a total of 20 % of the Company's registered share capital. Accordingly, the aggregate exclusion of shareholders' subscription rights upon exercise of this authorisation must not exceed 20 % of the registered share capital at the time said authorisation comes into effect or is exercised. This limit also includes shares issued by the Company on the basis of the authorisation by the General Meeting on 23 May 2012, under convertible bonds and/or bonds with warrants issued excluding the pre-emptive rights of shareholders.

The authorised capital has not been utilised.

Conditional capital

The share capital is subject to a conditional capital increase of up to € 30 million by means of issuing up to ten million new no-par value bearer shares, with a share in the Company's share capital of € 3.00 each. Such conditional capital increase serves to enable the Company to service convertible bonds and/or bonds with warrants on the basis of the authorisation resolution of the Annual General Meeting held on 19 May 2010. Said resolution authorised the Management Board, subject to the consent of the Supervisory Board, to issue, on one or more occasions until 18 May 2015, convertible bonds and/or bonds with warrants with a limited or an unlimited term in an aggregate nominal amount of € 600 million and to grant option and/or conversion rights to bearers or holders of bonds with regard to no-par value bearer shares of the Company, equivalent to a share in the share capital of up to € 30 million.

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

The conditional capital increase will be executed only to the extent that holders of conversion or option rights exercise such rights or any conversion obligation from such convertible bonds and/or bonds with warrants are performed, and to the extent that treasury shares are not utilised to service such convertible bonds and/or bonds with warrants. The new shares will be entitled to a share in the profits from the beginning of the financial year in which they come into existence through the exercise of conversion or option rights or the performance of conversion obligations.

No convertible bonds or warrants were in issue as at the balance sheet date. Neither said authorisation nor conditional capital were exercised or utilised in the year under review.

Contingent liabilities and other commitments

The Bank has off-balance contingent liabilities and irrevocable loan commitments. During the term of these obligations, the Bank regularly reviews whether any losses can be expected from the utilisation of such contingent liabilities. This assessment is primarily made due to the credit risk analysis. Any losses that can be expected according to this analysis are recognised in the balance sheet as provisions.

The contingent liabilities primarily result from guarantee and indemnity agreements with banks in the amount of € 107.1 million (2012: € 380.3 million). These include € 37.0 million (2012: € 40.7 million) in maximum default guarantees extended to DEPFA Deutsche Pfandbriefbank AG (within the scope of splitting the former DEPFA Group), for the purpose of providing cover against risks of default with respect to the property loan portfolio held by pbb Deutsche Pfandbriefbank AG.

Liabilities did not have to be recognised for obligations from indemnity agreements vis-à-vis third parties and other obligations, which were entered into in favour of affiliated companies, as the underlying liabilities are likely to be fulfilled by the affiliated companies. Therefore, we do not expect any utilisation in this regard.

Irrevocable loan commitments are made up of credit and loan commitments, of which € 72.0 million (2012: € 234.6 million) are granted to domestic borrowers and € 1,114.7 million (2012: € 1,999.4 million) to foreign borrowers.

Unrecognised transactions (section 285 no. 3 of the HGB)

Leasing: Aareal Bank AG is the lessee mainly of operating leases. Rental and lease contracts relate to the buildings of the Bank's head office in Wiesbaden used for the Bank's operations and of the foreign branch offices and representative offices as well as to the vehicle fleet and certain operating and office equipment. In all cases, the contracts are so-called operating leases which are not recognised in the Bank's financial statements. The key benefit of such contracts is a lower amount of capital lock-up compared to an acquisition and the elimination of the realisation risk. At the moment, there are no indications that risks may result from the lease term.

Disclosures on repurchase agreements and derivatives are presented in the following section of the notes.

Remaining terms

€ mn	31 Dec 2013	31 Dec 2012
Loans and advances to banks	**2,750.3**	**1,761.0**
Payable on demand	743.8	1,239.1
Up to 3 months	1,534.9	-
Between 3 months and 1 year	25.6	9.8
Between 1 year and 5 years	86.0	99.3
More than 5 years	8.6	17.9
Pro rata interest	351.4	394.9
Loans and advances to customers	**25,495.8**	**24,319.6**
Payable on demand	115.8	107.8
Up to 3 months	725.8	1,522.4
Between 3 months and 1 year	3,049.1	2,939.5
Between 1 year and 5 years	16,385.5	15,581.2
More than 5 years	5,072.5	4,028.0
Indefinite maturity	-	-
Pro rata interest	147.1	140.7
Debt and other fixed-income securities maturing in the following year (nominal amount)	**1,226.3**	**1,313.2**
Liabilities to banks	**1,742.9**	**3,450.7**
Payable on demand	775.3	914.3
Up to 3 months	141.1	361.4
Between 3 months and 1 year	69.2	262.9
Between 1 year and 5 years	291.3	1,275.6
More than 5 years	218.6	337.6
Pro rata interest	247.4	298.9
Savings deposits with agreed notice period	**0.0**	**0.0**
Up to 3 months	0.0	0.0
Between 3 months and 1 year	0.0	0.0
Between 1 year and 5 years	0.0	0.0
Pro rata interest	0.0	0.0
Other deposits from customers	**24,786.6**	**25,988.0**
Payable on demand	5,009.5	5,226.2
Up to 3 months	4,165.2	3,773.3
Between 3 months and 1 year	3,778.1	3,808.6
Between 1 year and 5 years	4,063.7	4,347.0
More than 5 years	7,492.8	8,501.9
Pro rata interest	277.3	331.0
Bonds issued maturing in the following year (nominal amount)	**2,415.0**	**1,314.4**
Other certificated liabilities	**0.0**	**0.0**

Prepaid expenses and deferred income

Prepaid expenses and deferred income primarily include upfront payments as well as any premiums and discounts on registered bonds, claims under promissory note loans, issued bonds and other loans as well as fee portions with interest-paying characteristics, which have been amortised over the relevant terms.

Prepaid expenses in the amount of € 203.5 million (2012: € 89.6 million) primarily include € 4.8 million (2012: € 6.8 million) in premiums on originated loans, in accordance with section 340e (2) sentence 3 of the HGB and € 148.8 million (2012: € 34.8 million) in discounts on bonds issued and borrowings pursuant to section 250 (3) of the HGB. The item also includes € 45.6 million (2012: € 46.1 million) from upfront payments/option premiums in connection with derivatives.

€ 62.5 million (2012: € 66.6 million) of deferred income (total 2013: € 109.3 million; total 2012: € 83.3 million) refers to upfront payments/option premiums in connection with derivatives, while € 6.8 million (2012: € 14.7 million) refers to discounts on originated loans, in accordance with section 340e (2) sentence 2 of the HGB, and to fee portions with interest-paying characteristics in the amount of € 39.6 million. In order to provide a true and fair view of the financial position and performance, the fees with interest-paying characteristics have been amortised in net interest income over the relevant terms since the financial year 2013 (in previous periods, these charges were directly absorbed in net commission income).

Trust business

€ mn	Trust assets 31 Dec 2013
Loans and advances to banks	0,0
Loans and advances to customers	71.8
Equities and other non-fixed income securities	1.5
Total	**73.3**

€ mn	Trust liabilities 31 Dec 2013
Liabilities to banks	18.8
Liabilities to customers	54.5
Total	**73.3**

€ mn	Trust assets 31 Dec 2012
Loans and advances to banks	-
Loans and advances to customers	101.3
Equities and other non-fixed income securities	1.5
Total	**102.8**

€ mn	Trust liabilities 31 Dec 2012
Liabilities to banks	24.4
Liabilities to customers	78.4
Total	**102.8**

Notes on affiliated companies and enterprises with a participatory interest

	Affiliated companies 2013		Enterprises with a participatory interest 2013		Affiliated companies 2012		Enterprises with a participatory interest 2012	
	Certificated	Not certificated	Certificated	Not certificated	Certificated	Not certificated	Certificated	Not certificated
€ mn								
Loans and advances to banks	-	-	-	-	-	-	-	-
Loans and advances to customers	-	2,561.0	-	-	-	1,680.8	-	-
Debt and other fixed-income securities	-	-	-	-	-	0.0	-	-
Liabilities to banks	-	-	-	-	-	0.0	-	-
Liabilities to customers	-	408.1	-	0.0	-	353.2	-	0.1
Certificated liabilities	-	-	-	-	-	-	-	-
Subordinated liabilities	-	250.0	-	-	-	250.0	-	-

Transactions with related parties are carried out on an arm's length basis. Our relationships to related parties are detailed in the section "Loans to executive bodies of Aareal Bank AG" as well as in the Remuneration Report.

Shareholdings

The following disclosures are made pursuant to section 285 (11) of the HGB:

No.	Company name	Registered office	Share in capital in %	Equity € mn	Results € mn
1	Aareal Bank AG	Wiesbaden	100.0		
2	1st Touch Ltd	Southampton	100.0	GBP 2.2 mn	GBP 1.1 mn
3	Aareal Bank Asia Limited	Singapore	100.0	SGD 17.4 mn	SGD 0.3 mn [1]
4	Aareal Bank Capital Funding LLC	Wilmington	100.0	250.0	0.0
5	Aareal Bank Capital Funding Trust	Wilmington	100.0	0.0	0.0
6	Aareal Capital Corporation	Wilmington	100.0	USD 203.6.mn	USD 6.4 mn [1]
7	Aareal Estate AG	Wiesbaden	100.0	2.8	0.0 [3]
8	Aareal First Financial Solutions AG	Mainz	100.0	3.2	0.0 [3]
9	Aareal Gesellschaft für Beteiligungen und Grundbesitz Erste mbH & Co. KG	Wiesbaden	94.9	2.1	0.1 [1]
10	Aareal Immobilien Beteiligungen GmbH	Wiesbaden	100.0	167.6	0.0 [3]
11	Aareal IT Beteiligungen GmbH	Wiesbaden	100.0	145.5	0.0 [3]
12	Aareal Partecipazioni S.p.A.	Rome	100.0	6.8	0.0 [1]
13	Aareal Property Services B.V.	Amsterdam	100.0	29.4	0.6 [1]
14	Aareal Valuation GmbH	Wiesbaden	100.0	0.5	0.0 [3]
15	Aareon AG	Mainz	100.0	75.4	14.0
16	Aareon Deutschland GmbH	Mainz	100.0	32.2	0.0 [3]
17	Aareon France S.A.S.	Meudon-la Forêt	100.0	4.2	1.3
18	Aareon Immobilien Projekt GmbH	Essen	51.0	0.9	0.6
19	Aareon UK Ltd.	Coventry	100.0	GBP 4.3 mn	GBP 1.1 mn
20	Aareon Wodis GmbH	Dortmund	100.0	2.0	0.0 [3]
21	Aqvatrium AB	Stockholm	100.0	SEK 383.1 mn	SEK 2.2 mn [1]
22	arsago Alternative Investments SPC	Grand Cayman	67.0	n/a	n/a
23	Aufbaugesellschaft Prager Straße mbH	Wiesbaden	100.0	0.0	0.0 [1]
24	BauContact Immobilien GmbH	Wiesbaden	100.0	27.9	1.0
25	BauGrund Immobilien-Management GmbH	Bonn	100.0	0.5	0.0 [3]
26	BauGrund TVG GmbH	Munich	100.0	0.1	0.0
27	BauSecura Versicherungsmakler GmbH	Hamburg	100.0	2.8	2.7
28	berlinbiotechpark Management GmbH	Berlin	100.0	0.1	0.1 [2]
29	berlinbiotechpark Verwaltung GmbH	Berlin	89.6	0.2	0.0 [2]
30	Capital Funding GmbH & Co. KG	Frankfurt	100.0	0.0	0.0 [5]
31	Deutsche Bau- und Grundstücks-Aktiengesellschaft	Berlin	100.0	1.5	-0.6
32	Deutsche Structured Finance GmbH	Frankfurt	100.0	2.6	0.8 [1]
33	Deutsche Structured Finance GmbH & Co. Alphard KG	Frankfurt	100.0	0.5	0.2 [1]
34	Deutsche Structured Finance GmbH & Co. Deneb KG	Frankfurt	100.0	0.6	-1.1 [1]
35	DSF Anteils GmbH	Frankfurt	100.0	0.1	0.0 [1]
36	DSF berlinbiotechpark Verwaltungsgesellschaft mbH	Frankfurt	50.0	0.1	0.0 [2]

[1] Preliminary figures as at 31 December 2013; [2] Equity and results as at 31 December 2012; [3] Profit transfer agreement / control and profit transfer agreement
[4] Different financial year; [5] 10% of voting rights, diverging from the equity interest held; n/a no data

No.	Company name	Registered office	Share in capital in %	Equity € mn	Results € mn
37	DSF Dritte Verwaltungsgesellschaft mbH	Frankfurt	100.0	0.0	0.0 [2]
38	DSF Elfte Verwaltungsgesellschaft mbH	Frankfurt	100.0	0.0	0.0 [1]
39	DSF Energia Naturale S.r.l.	Rome	100.0	0.0	0.0 [1]
40	DSF Flugzeugportfolio GmbH	Frankfurt	100.0	0.0	0.0 [3]
41	DSF Fünfzehnte Verwaltungsgesellschaft mbH	Frankfurt	100.0	0.1	0.0 [2]
42	DSF German Office Fund GmbH & Co. KG	Frankfurt	94.0	0.6	-1.4 [1]
43	DSF Immobilienverwaltung GmbH	Frankfurt	100.0	0.0	0.0 [2]
44	DSF Neunte Verwaltungsgesellschaft mbH	Frankfurt	100.0	0.0	0.0 [2]
45	DSF Solar Italien GmbH & Co. KG	Frankfurt	100.0	0.0	0.0 [4]
46	DSF Treuhand GmbH	Frankfurt	100.0	0.1	0.0 [2]
47	DSF Verwaltungsgesellschaft mbH	Frankfurt	100.0	0.0	0.0 [2]
48	DSF Vierte Verwaltungsgesellschaft mbH	Wiesbaden	100.0	2.2	0.0 [3]
49	DSF Vierzehnte Verwaltungsgesellschaft mbH	Frankfurt	100.0	0.2	0.0 [2]
50	DSF Zwölfte Verwaltungsgesellschaft mbH	Frankfurt	100.0	0.3	0.0 [2]
51	GEV GmbH	Wiesbaden	100.0	52.9	0.0 [3]
52	IMMO Consulting S.r.l.	Rome	100.0	0.7	0.2 [1]
53	Incit AB	Mölndal	100.0	SEK 23.2 mn	SEK 4.5 mn
54	Incit AS	Oslo	100.0	NOK 1.0 mn	NOK 0.3 mn
55	Incit Nederland B.V.	Gorinchem	100.0	-0.6	0.1
56	IV Beteiligungsgesellschaft für Immobilieninvestitionen mbH	Wiesbaden	100.0	2.1	0.1 [1]
57	Izalco Spain S.L.	Madrid	100.0	11.1	0.0 [3]
58	Jomo S.p.r.l.	Brussels	100.0	11.6	-1.1 [2]
59	La Sessola Holding GmbH	Wiesbaden	100.0	42.1	-7.3 [1]
60	La Sessola S.r.l.	Rome	100.0	54.9	-5.7 [1]
61	La Sessola Service S.r.l.	Rome	100.0	1.8	-0.6 [1]
62	Main Triangel GmbH	Frankfurt	94.0	79.1	6.3 [1]
63	Main Triangel Gastronomie GmbH	Wiesbaden	100.0	0.4	-0.1 [1]
64	Mercadea S.r.l.	Rome	100.0	4.3	0.1 [1]
65	Mirante S.r.l.	Rome	100.0	13.1	-0.3 [1]
66	PLP Holding GmbH	Wiesbaden	100.0	12.3	-14.7 [1]
67	Real Verwaltungsgesellschaft mbH	Schönefeld	100.0	27.9	0.8 [1]
68	Rehabilitationsklinik Barby Besitzgesellschaft mbH	Wiesbaden	100.0	-4.6	1.0 [1]
69	Rehabilitationsklinik Templin Besitzgesellschaft mbH	Wiesbaden	100.0	-3.7	0.0 [1]
70	SG Automatisering B.V.	Emmen	100.0	16.8	3.2
71	SG | Facilitor B.V.	Enschede	100.0	0.9	0.6
72	SG | stravis B.V.	Emmen	100.0	0.1	0.0
73	Sole Giano S.r.l. & Co. S.a.s.	Rome	100.0	-0.2	-0.1 [2]
74	Sustainable Solar Future - Hellas Limited Liability Company	Athens	99.0	0.0	0.0 [2]
75	Sustainable Solar Future Northern - Hellas Limited Liability Company	Athens	99.0	0.0	0.0 [2]
76	Sustainable Solar Thermal Future East - Crete Limited Liability Company	Heraklion	99.0	0.5	0.0 [2]
77	Terrain-Aktiengesellschaft Herzogpark	Wiesbaden	99.9	4.7	0.0 [3]

[1] Preliminary figures as at 31 December 2013; [2] Equity and results as at 31 December 2012; [3] Profit transfer agreement / control and profit transfer agreement

[4] Different financial year; [5] 10% of voting rights, diverging from the equity interest held; n/a no data

No.	Company name	Registered office	Share in capital in %	Equity € mn	Results € mn
78	Bavaria Solar I Verwaltungsgesellschaft mbH	Frankfurt	24.0	0.0	0.0 [1]
79	Deutsche Operating Leasing AG i.L.	Frankfurt	19.2	0.9	-0.1 [4]
80	DSF PP Justizzentrum Thüringen GmbH & Co. KG	Frankfurt	48.4	0.4	0.0 [2]
81	DSF Zehnte Verwaltungsgesellschaft mbH	Frankfurt	50.0	0.1	0.0 [2]
82	Rehabilitationsklinik Uckermark GmbH i.L.	Templin	49.0	n/a	n/a
83	SG2ALL B.V.	Huizen	50.0	0.4	0.2
84	Westhafen Haus GmbH & Co. Projektentwicklungs KG	Frankfurt	25.0	-0.2	0.0 [2]
85	Westhafen-Gelände Frankfurt am Main GbR	Frankfurt	33.3	0.1	0.0 [2]
86	Windpark Ahlerstedt Verwaltungsgesellschaft mbH	Frankfurt	20.0	0.0	0.0 [1]
87	Windpark Borsum Verwaltungsgesellschaft mbH	Frankfurt	20.0	0.0	0.0 [1]
88	Windpark Portfolio Verwaltungs GmbH	Freiburg	20.0	0.0	0.0 [1]

[1] Preliminary figures as at 31 December 2013; [2] Equity and results as at 31 December 2012; [3] Profit transfer agreement / control and profit transfer agreement
[4] Different financial year; [5] 10% of voting rights, diverging from the equity interest held; n/a no data

Assets pledged as collateral

Assets in the amount stated were pledged for the following liabilities:

€ mn	31 Dec 2013	31 Dec 2012
Liabilities to banks	1,976.8	4,059.3
Liabilities to customers	0.0	0.0
Total	**1,976.8**	**4,059.3**

Repurchase agreements

As at 31 December 2013, no bonds were used as part of repurchase agreements (2012: nil).

Assets and liabilities in foreign currencies

The aggregate equivalent amount of assets denominated in foreign currencies was € 10,337.2 million (2012: € 9,783.4 million) at the balance sheet date, while liabilities totalled € 669.6 million (2012: € 415.9 million). Foreign currency balances are partly offset by equivalent foreign exchange forwards and currency swaps.

Forward transactions

The following forward transactions had been entered into as at 31 December 2013:

- **Transactions based on interest rates**
  Caps, floors, swaptions, interest rate swaps

- **Transactions based on exchange rates**
  Spot and forward foreign exchange transactions, cross-currency interest rate swaps

- **Other transactions**
  Credit default swaps, other forward transactions

Interest-rate based transactions and cross-currency interest rate swaps are primarily used to hedge against interest rate and exchange rate fluctuations. Spot and forward foreign exchange transactions are almost exclusively used for refinancing purposes. Credit derivatives are primarily used to assume credit risks for the purpose of portfolio diversification. The credit default swaps entered into for that purpose are reviewed as to whether a provision for anticipated losses shall be recognised based on pre-determined criteria.

Remaining terms and future cash flows of derivatives are broken down in the following table:

€ mn	Up to 3 months	3 months to 1 year	1 year to 5 years	More than 5 years	Total 31 Dec 2013
31 Dec 2013					
Interest rate instruments					
Interest rate swaps					
Cash inflows	228.6	638.4	2,473.4	939.0	4,279.4
Cash outflows	222.5	420.3	2,169.6	980.9	3,793.3
Swaptions					
Cash inflows	-	-	-	-	0.0
Cash outflows	-	-	-	-	0.0
Caps, floors					
Cash inflows	0.7	4.4	10.0	1.5	16.6
Cash outflows	0.7	4.4	10.0	1.5	16.6
Currency-related instruments					
Spot and forward foreign exchange transactions					
Cash inflows	2,871.4	17	-	-	2,888.8
Cash outflows	2,847.8	17	-	-	2,865.2
Cross-currency swaps					
Cash inflows	540.8	2,020.5	4,955.1	106.0	7,622.4
Cash outflows	548.8	2,033.9	4,976.2	107.7	7,666.6
Other transactions					
Credit default swaps					
Cash inflows	0.1	0.4	0.9	-	1.4
Cash outflows	-	-	-	-	-
Total cash inflows	**3,641.6**	**2,681.1**	**7,439.4**	**1,046.5**	**14,808.6**
Total cash outflows	**3,619.8**	**2,476.0**	**7,155.8**	**1,090.1**	**14,341.7**

€ mn	Up to 3 months	3 months to 1 year	1 year to 5 years	More than 5 years	Total 31 Dec 2012
31 Dec 2012					
Interest rate instruments					
Interest rate swaps					
Cash inflows	244.8	714.7	2,138.5	863.4	3,961.4
Cash outflows	233.8	453.1	1,779.2	884.2	3,350.3
Swaptions					
Cash inflows	-	-	-	-	0.0
Cash outflows	-	-	-	-	0.0
Caps, floors					
Cash inflows	0.7	4.9	10.9	1.3	17.8
Cash outflows	0.7	4.9	10.9	1.3	17.8
Currency-related instruments					
Spot and forward foreign exchange transactions					
Cash inflows	1,539.0	-	-	-	1,539.0
Cash outflows	1,527.5	-	-	-	1,527.5
Cross-currency swaps					
Cash inflows	571.3	1,874.6	5,290.8	404.0	8,140.7
Cash outflows	623.8	1,979.8	5,546.6	401.2	8,551.4
Other transactions					
Credit default swaps					
Cash inflows	0.3	0.7	2.5	-	3.5
Cash outflows	-	-	-	-	-
Total cash inflows	**2,356.1**	**2,594.9**	**7,442.7**	**1,268.7**	**13,662.4**
Total cash outflows	**2,385.8**	**2,437.8**	**7,336.7**	**1,286.7**	**13,447.0**

The following table shows positive and negative market values, aggregated by product level (without taking into account collateral or netting agreements):

Unless a quoted market price is available, derivatives are measured using generally accepted methods on the basis of current market parameters (yield curves, volatility factors, etc.). Methods used include standard methods and models such as discounted cash flow analyses and option pricing models. Structured products are measured after they have been split into their individual components. Fair values including accrued interest are given for derivative financial instruments not recognised at fair value as at 31 December 2013.

	Nominal amount as at 31 Dec 2013	Market value as at 31 Dec 2013		Market value as at 31 Dec 2012	
€ mn		positive	negative	positiv	negativ
Interest rate instruments					
OTC products					
Interest rate swaps	44,829.1	1,931.4	1,706.1	2,849.9	2,372.0
Swaptions	176.1	-	0	-	-
Caps, floors	4,715.8	16.2	16.1	17.3	17.3
Total interest rate instruments	**49,721.0**	**1,947.6**	**1,722.2**	**2,867.2**	**2,389.3**
Currency-related instruments					
OTC products					
Spot and forward foreign exchange transactions	2,885.7	31.1	7.2	13.1	1.2
Cross-currency swaps	7,553.8	166.4	158.2	60.8	435.2
Total currency-related instruments	**10,439.5**	**197.5**	**165.4**	**73.9**	**436.4**
Other transactions					
OTC products [1]					
Credit default swaps	75.0	0.1	1.1	0.1	15.8
Total other transactions	**75.0**	**0.1**	**1.1**	**0.1**	**15.8**
Total	**60,235.5**	**2,145.2**	**1,888.7**	**2,941.2**	**2,841.5**

[1] This includes derivatives subject to the country risk of Hungary and embedded in an Austrian bank bond.

Derivatives have been entered into with the following counterparties:

	Market value as at 31 Dec 2013		Market value as at 31 Dec 2012	
€ mn	positiv	negativ	positiv	negativ
OECD public-sector authorities				
OECD banks	1,921.4	1,837.9	2,542.8	2,815.0
Non-OECD banks				
Companies and private individuals	223.8	50.8	398.3	26.4
Total	**2,145.2**	**1,888.7**	**2,941.1**	**2,841.4**

Remuneration Report

Remuneration of the Board of Managing Directors

Principles of remuneration

The Supervisory Board determines the structure and amount of remuneration for members of the Management Board. Aareal Bank AG has entered into fixed-term service contracts with the members of its Management Board.

In addition to their fixed annual salary components, Management Board members receive a performance-related bonus (variable remuneration) that is determined using an assessment basis extending over several years. The level of this performance-related bonus is determined by reference to the personal performance of each Management Board member which is measured by the degree to which targets set in advance by the Supervisory Board are achieved, based on contractually agreed initial values. The targets which are relevant for performance-related bonuses include annual targets and three-year targets. The weighting of annual to three-year targets is fixed for each financial year, with a 60 % / 40 % weighting taken as a guideline.

The annual and three-year targets are derived from the Bank's overall strategy and the annual and medium-term planning of Aareal Bank Group, each of which are agreed upon with the Supervisory Board. The targets comprise quantitative components and qualitative components, with latter being also related to non-financial parameters. In this context, the Bank's overall performance, the performance of the relevant section, and the individual performance contributions of the Management Board member concerned are all taken into consideration.

The amount of the initial value of the performance-related bonus increases – depending on the Management Board member's degree of target achievement – up to a maximum of 200 %. If the target achievement exceeds a level of 200 %, the initial value of the performance-related bonus will not increase any further (cap). If target achievement is 0 %, no performance-related bonus will be awarded for the financial year concerned. The initial value is fixed at 100 % for target achievement levels between 90 % and 110 %.

To ensure that the remuneration system provides long-term incentive effects, performance-related bonuses are awarded at the end of the financial year, according to the following principles:

20 % of the performance-related bonus is paid as a cash bonus directly after the end of the financial year.

A further 20 % of the performance-related bonus is awarded as a share bonus[12] in the form of phantom shares directly after the end of the financial year and are the subject of the Share Bonus Plan.

30 % of the performance-related bonus is deferred as a cash deferral[12] (Cash Deferral).

The remaining 30 % of the performance-related bonus is deferred as a share deferral[12] and is the subject of the Share Deferral Plan.

With regard to the portion of the performance-related bonus that is deferred initially as a cash deferral or a share deferral, the Supervisory Board makes a decision regarding the granting of one third of the amount, as well as the associated interest, in the three years following the determination of the performance-related bonus (retention period). If the deferred remuneration components for the Management Board members are actually awarded, the cash deferral is paid out in cash and the share deferral is converted into virtual shares, subject to a two-year holding period.

In making its determination about the amount to be awarded, the Supervisory Board particularly takes into account any negative aspects of the Management Board member's performance, his section as well as any weakness in the performance of Aareal Bank AG or the Group as a whole. The final amount may be awarded in full, partially, or not at all. If the award is not made in its full amount, the remain is forfeited, i.e. it is not carried forward into subsequent years. No bonus may be awarded if BaFin makes an official ruling against the Bank pursuant to section 45 (2) of the German Banking Act (KWG) due to shortcomings relating to capital adequacy or liquidity issues. If a case of serious individual misconduct by a member of the Management Board is identified afterwards in the financial year in which the remuneration components were awarded as a cash deferral and share deferral, the retained remuneration components are cancelled in full. Members of the Management Board may not undertake to limit or override the risk orientation of the performance-related bonus by initiating personal protection measures or countermeasures (hedging ban).

[12] Please refer to the subsection "Cash-settled share-based payment" in this Remuneration Report for further explanations related to the structure of the Share Bonus Plan, the Share Deferral Plan and the Cash Deferrals.

Remuneration

Remuneration of the members of the Management Board can be broken down as follows:

€	Year	Fixed remuneration	Variable remuneration: Cash component – Cash bonus	Cash component – Cash deferral	Share-based component – Share bonus	Share-based component – Share deferral	Other [1]	Total remuneration
Dr Wolf Schumacher	2013	1,100,000.00	363,000.00	544,500.00	363,000.00	544,500.00	27,751.91	2,942,751.91
	2012	1,100,000.00	330,000.00	495,000.00	330,000.00	495,000.00	26,026.59	2,776,026.59
Dirk Große Wördemann[2]	2013	270,833.35	330,833.00	-	-	-	14,607.20	616,273.55
	2012	650,000.00	158,800.00	238,200.00	158,800.00	238,200.00	31,189.76	1,475,189.76
Dagmar Knopek[3]	2013	408,333.33	125,510.00	188,265.00	125,510.00	188,265.00	17,291.18	1,053,174.51
	2012	-	-	-	-	-	-	-
Hermann J. Merkens	2013	700,000.00	215,160.00	322,740.00	215,160.00	322,740.00	55,758.86	1,831,558.86
	2012	700,000.00	195,600.00	293,400.00	195,600.00	293,400.00	53,909.48	1,731,909.48
Thomas Ortmanns	2013	700,000.00	215,160.00	322,740.00	215,160.00	322,740.00	28,418.29	1,804,218.29
	2012	700,000.00	195,600.00	293,400.00	195,600.00	293,400.00	26,695.09	1,704,695.09
Total	**2013**	**3,179,166.68**	**1,249,663.00**	**1,378,245.00**	**918,830.00**	**1,378,245.00**	**143,827.44**	**8,247,977.12**
	2012	**3,150,000.00**	**880,000.00**	**1,320,000.00**	**880,000.00**	**1,320,000.00**	**137,820.92**	**7,687,820.92**

[1] Other remuneration includes payments (in particular for company cars) in the amount of € 85,318.84 in 2013 (2012: € 85,521.76) as well as benefits related to social security contributions totalling € 49,219.20 for 2013 (2012: € 45,231.36).
[2] Mr Große Wördemann resigned as at 31 May 2013. The annual variable remuneration 2013 was paid on a pro-rata basis. No further remuneration was granted to Mr Große Wördemann. The remaining cash and share deferrals will be managed according to the terms as set out in Mr Wördemann's service contract. Going forward, Mr Große Wördemann will be available to the Bank as a consultant.
[3] Ms Knopek was appointed member of the Management Board as at 1 June 2013.

The following initial values for the performance-related bonus at an overall target achievement level of 100 % were agreed upon in the service contracts of the Management Board members:

€	Reference values for variable remuneration 2013	Reference values for variable remuneration 2012
Dr Wolf Schumacher	1,650,000.00	1,650,000.00
Dirk Große Wördemann [1]	794,000.00	794,000.00
Dagmar Knopek [2]	978,000.00	-
Hermann J. Merkens	978,000.00	978,000.00
Thomas Ortmanns	978,000.00	978,000.00
Total	**5,378,000.00**	**4,400,000.00**

[1] Mr Große Wördemann resigned as at 31 May 2013.
[2] Ms Knopek was appointed member of the Management Board as at 1 June 2013.

No benefits were granted to any member of the Management Board by third parties with respect to his/her Management Board activities during the year under review.

The following table shows the portion of the variable component attributable to share-based payment arrangements as well as the corresponding number of virtual shares granted:

	Year	Share-based payment Value (€)	Share-based payment Quantity (number)[1]
Dr Wolf Schumacher	2013	907,500.00	31,521.36
	2012	825,000.00	50,274.24
Dirk Große Wördemann [2)]	2013	-	-
	2012	397,000.00	25,270.53
Dagmar Knopek [3)]	2013	313,775.00	10,898.75
	2012	-	-
Hermann J. Merkens	2013	537,900.00	18,683.57
	2012	489,000.00	29,798.89
Thomas Ortmanns	2013	537,900.00	18,683.57
	2012	489,000.00	29,798.89

[1)] The stated number of virtual shares granted for 2013 is a preliminary figure, based on the price of Aareal Bank AG's share on 31 December 2013 (€ 28.79). The final conversion rate may only be determined after publication of the 2013 annual report.
[2)] Mr Große Wördemann resigned as at 31 May 2013.
[3)] Ms Knopek was appointed member of the Management Board as at 1 June 2013.

Pensions, retirement benefits and severance pay

The benefit regulations as agreed in the employment contract apply to the members of the Management Board of Aareal Bank AG. Accordingly, they are entitled to receive pension payments after completing their 60th year of age, or earlier in case of a permanent disability of service. For members of the Management Board appointed on or after 1 November 2010, this rule applies only from the beginning of the second term of office, and they are only entitled to pension payments after completion of their 62nd year of age.

The following overview shows the pension claims of the members of the Management Board and the changes of the corresponding pension provisions during the period under review:

	2013			2012		
€ 000`s	Pension claims p.a.[1)]	Balance of pension obligations as at 31 Dec 2013	Increase of pension obligations in 2013	Pension claims p.a.[1)]	Balance of pension obligations as at 31 Dec 2012	Increase of pension obligations in 2012
Dr Wolf Schumacher	379	3,840	761	364	3,079	675
Dagmar Knopek[2)]	-	229	229	-	-	-
Hermann J. Merkens	220	1,721	334	209	1,387	261
Thomas Ortmanns	220	1,881	424	210	1,457	376
Total	**819**	**7,671**	**1,748**	**783**	**5,923**	**1,312**

[1)] Pension claims are calculated based on the earliest possible pension payment.
[2)] Ms Knopek currently does not meet the vesting criteria for the pension claims.

The pension claims are adjusted to take account of the development of standard wages within the private banking sector as from the beginning of actual payments of pensions, to the extent that these are based on defined benefit plans. If the payments refer to defined contribution plans, the guaranteed amount is adjusted by 1 % p.a. The pension paid to widows amounts to 60 % of the pension of the member of the Management Board, while pensions to half-orphans and orphans amount to 10 % and not more than 25 %, respectively. Service cost incurred in the financial year 2013 in connection with the pension claims of members of the Management Board totalled € 1.4 million (2012: € 1.3 million). The pension obligations for current members of the Management Board as well as for former members of the Management Board and their surviving dependants increased by € 1.7 million in the year under review (2012: € 1.8 million). The total present value of the pension obligations amounts to € 22.9 million (2012: € 21.2 million). Of that amount, € 15.4 million relate to former members of the Management Board and their surviving dependants (2012: € 15.0 million). Payments to former Management Board members and their surviving dependants totalled € 0.8 million (2012: € 0.8 million) during the period under review.

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

In the case of a retirement due to a change of control, the members affected receive, in settlement of their total remuneration a monthly payment, as agreed in their employment contracts, as well as a contractually agreed fixed one-off payment. Depending on the type of the change of control – termination by the Company or termination by the respective Board member – the agreed benefits are as follows:

€ per month of remaining contract term[1)]	Terminated by the company	Terminated by the Board member
Dr Wolf Schumacher	141,667.00	70,833.00
Dagmar Knopek	120,833.00	54,167.00
Hermann J. Merkens	120,833.00	54,167.00
Thomas Ortmanns	120,833.00	54,167.00

1) Upon request of the Board member, the benefits may be paid in form of a one-off payment. In this case, the amount is discounted using the interest rate of the ECB for one-year deposits of private households in the month of payment.

The claims resulting from the early termination of the Board activities due to a change of control are capped to an equivalent of three years' remuneration.

During the term of a SoFFin stabilisation measure, Management Board members are not entitled to any severance pay in the event of an early termination or a change of control. The fulfilment of a Management Board member's contractual remuneration claims arising from the employment contract are not limited by the framework agreement entered into with SoFFin.

Remuneration of the Supervisory Board

Remuneration for the services of the Supervisory Board members is specified in Article 9 of the Memorandum and Articles of Association of Aareal Bank AG. The Annual General Meeting held on 18 May 2011 made the most recent adjustment to the system for the remuneration of the Supervisory Board.

Since that date, the remuneration system for the Supervisory Board has only conprised a fixed remuneration system, as well as compensation for attending meetings. In addition, the Supervisory Board members will be reimbursed for their expenses. Where membership in the Supervisory Board falls short of an entire financial year, said remuneration shall be paid on *a* pro rata temporis basis. Any value-added tax invoiced will also be deemed to be a refundable expense.

The fixed remuneration is € 30,000 p.a. for each Supervisory Board member. The Chairman of the Supervisory Board shall receive two and a half times this amount, while the deputy shall receive one and a half times as much as a normal member. The fixed remuneration shall be increased by € 15,000 p.a. for each membership in a committee (with the exception of the Nomination Committee, which is an exclusively advisory committee, and the Committee for Urgent Decisions, which is part of the Risk Committee). The fixed remuneration shall be increased by € 30,000 p.a. for the chairmanship of a committee (with the exception of the Nomination Committee and the Committee for Urgent Decisions).

The meeting attendance compensation amounts to € 1,000.00 for each meeting attended (except for meetings of the Nomination Committee and the Committee for Urgent Decisions).

The remuneration for any financial year shall be due and payable one month after the end of the respective financial year.

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

€	Year	Fixed remuneration	Attendance fees	Total remuneration
Hans W. Reich,	2013	70,408.33	9,520.00	79,928.33
Chairman (until 22 May 2013)	2012	178,500.00	26,180.00	204,680.00
Marija G. Korsch, Member (since 11 July 2012),	2013	122,570.00	19,040.00	141,610.00
Chairman (since 22 May 2013)	2012	16,759.16	4,760.00	21,519.16
Erwin Flieger,	2013	89,250.00	19,040.00	108,290.00
Deputy Chairman	2012	89,250.00	19,040.00	108,290.00
York-Detlef Bülow,	2013	89,250.00	20,230.00	109,480.00
Deputy Chairman	2012	89,250.00	21,420.00	110,670.00
Christian Graf von Bassewitz	2013	71,400.00	17,850.00	89,250.00
	2012	71,400.00	21,420.00	92,820.00
Manfred Behrens	2013	35,700.00	4,760.00	40,460.00
	2012	35,700.00	5,950.00	41,650.00
Thomas Hawel	2013	35,700.00	5,950.00	41,650.00
	2012	35,700.00	9,520.00	45,220.00
Dieter Kirsch	2013	53,550.00	11,900.00	65,450.00
	2012	53,550.00	14,280.00	67,830.00
Dr Herbert Lohneiß	2013	53,550.00	11,900.00	65,450.00
	2012	53,550.00	13,090.00	66,640.00
Joachim Neupel	2013	89,250.00	19,040.00	108,290.00
	2012	89,250.00	21,420.00	110,670.00
Richard Peters,	2013	21,717.50	3,570.00	25,287.50
Member (since 22 May 2013)	2012	-	-	-
Prof Dr Stephan Schüller	2013	71,400.00	20,230.00	91,630.00
	2012	71,400.00	19,040.00	90,440.00
Wolf R. Thiel,	2013	-	-	-
Member (until 31 March 2012)	2012	13,387.50	3,570.00	16,957.50
Helmut Wagner	2013	35,700.00	7,140.00	42,840.00
	2012	35,700.00	8,330.00	44,030.00
Total	**2013**	**839,445.83**	**170,170.00**	**1,009,615.83**
	2012	**833,396.66**	**188,020.00**	**1,021,416.66**

The members of the Supervisory Board did not provide any consulting or agency services, or other personal services in 2013. Therefore, no additional remuneration was paid.

Cash-settled share-based payment

a) Description of cash-settled share-based payment

Within Aareal Bank AG, there are various forms of share-based payment arrangements. Among other things, differences between these plans can be found as regards their term and the vesting conditions as well as regarding the group of beneficiaries.

Management Board

Share Bonus Plan

According to the rules for the Share Bonus Plan, a portion of the variable remuneration will be converted into an equivalent number of virtual shares and credited to the beneficiary. The calculation of the number of virtual shares is based on the weighted average price on the basis of five trading days (Xetra) after publication (ad-hoc release) of the annual financial statements adopted by the Supervisory Board (subscription price). The date of publication of the respective financial statements is used as the reference date. Not earlier than three years after the reference date, the beneficiary may exercise the virtual shares granted either in whole or in part within five business days after the publication of the quarterly report (holding period). Any virtual shares not exercised may be exercised either in whole or in part at a later date, in each case within five business days after the publication of a quarterly report. Upon exercise, the relevant proportion of virtual shares is converted at the weighted average price as reported by Bloomberg on the exercise date. If dividends are paid on the Company's shares during the time period between the reference date and the exercise date, a payout is made as a salary component in an amount equivalent to the dividends and the proportion of the virtual shares.

Share Deferral Plan

Under the Share Deferral Plan, a portion of the variable remuneration is converted into an equivalent number of virtual shares and credited to the beneficiary. This credit, however, does not convey an entitlement or a claim regarding a later payout or grant of virtual shares. Interest accrues on the amount credited in the form of a share deferral to the beneficiary. The reference rate is the interest rate of the European Central Bank for deposits from private households with a term of up to one year. As above, the credit of interest does not convey an entitlement or a claim regarding the interest amount. In the three years following the credit (retention period), the Supervisory Board decides whether in each case a third of the share deferral, including interest, should be converted. The question, whether a third of the phantom shares is converted and, if yes, in which amount, is based on the following principles:

Negative performance contributions of the beneficiary or of the organisational units for which he is responsible for or a negative overall performance of Aareal Bank Group lead to a reduction of the payout, in some cases even to zero. No bonus may be awarded if BaFin makes an official ruling against the Bank pursuant to section 45 (2) of the KWG.

If less than 100 % of the third of the share deferral eligible for conversion (including interest) is converted into virtual shares, the amount not converted is forfeited and is not carried forward to future years. The rules for the calculation of the number of virtua sharesl, their exercise and the other rights and obligations associated with the granting of virtual shares correspond to those applicable for share bonuses, with the exception that (instead of three-year holding period) a holding period of two years applies.

Phantom Share Plan

The Phantom Share Plan applied to virtual shares granted until (and including) the financial year 2011.

According to the rules for the Phantom Share Plan, a portion of the variable remuneration will be converted into an equivalent number of virtual shares. The conversion is based on the weighted average price (XETRA) of Aareal Bank AG's share as notified by Bloomberg, on the five trading days following the publication (ad-hoc release) of the financial statements as approved by the Supervisory Board. The entitlement to the remuneration, i.e. the award, arises after the Supervisory Board has used its discretion with regard to the amount of variable remuneration within the applicable range. One fourth of the awarded virtual shares become exercisable each year. This also applies for the year in which they are awarded. Virtual shares not exercised in a particular year are accumulated. The phantom shares may be exercised either in whole or in part within five business days after the publication of a quarterly report. The relevant price for exercising these phantom shares is the weighted average price according to Bloomberg on the exercise date.

There are no exercise hurdles in form of a minimum stock price appreciation target or other market or performance-related criteria. Virtual shares that have not been exercised carry full dividend rights, i.e. the beneficiaries receive for each virtual share not yet exercised a cash payment equivalent to the amount of the approved dividend. The term of the plan is not limited.

Further share-based payment models

Virtual shares are granted to senior executives and the so-called "risk takers" of Aareal Bank AG, as defined by the German Ordinance Governing Supervisory Requirements for Remuneration Systems of Institutions (Instituts-Vergütungsverordnung – "InstitutsVergV"), as well as to Managing Directors and Management Board members of Aareal Bank AG's subsidiaries on the basis of the following share-based payment models.

Share Bonus Plan

According to the rules for the share bonus plan, a portion of the variable remuneration will be converted into an equivalent number of virtual shares. The conversion is based on the weighted average price (XETRA) of Aareal Bank AG's share according to Bloomberg, on the five trading days following the publication of the annual report for the reference period. Entitlement to the remuneration occurs at the end of the reference period. The share bonus is paid out after a minimum holding period of two years, beginning on the date on which entitlement arose. The payout amount is calculated by multiplying the number of virtual shares allocated with the share price upon payout. The share price upon payout corresponds to the weighted average price on XETRA of Aareal Bank AG's share according to Bloomberg, on the five trading days following the publication of the annual report for the financial year preceding the payout date. The actual payout date for the share bonus may be determined individually, based on an option right. For this purpose, the beneficiary must inform the Bank whether he will use the option right by notifying the Bank accordingly not later than the tenth day following the publication of the annual report for the financial year preceding the planned payout date. The option right expires after not less than three years, from the end of the calendar quarter of the earliest payout date. The option right may only be exercised as at 31 March, 30 June or 30 September of a calendar year; exercise of the option has to be notified to the Bank not later than at the tenth day after publication of the quarterly financial results. The conversion of the virtual shares for the purpose of determining the payout amount is made at the weighted average price on XETRA according to Bloomberg, for the five trading days following the publication of the latest quarterly financial results for the selected option date.

There are no exercise hurdles in form of a minimum stock price appreciation target or other market or performance-related criteria. Virtual shares carry fully dividend rights, i.e. the beneficiaries receive for each virtual share not yet exercised a cash payment equivalent to the amount of the approved dividend. The maximum term of the plan – in relation to the grant date – is three years (six years in case of an option for late payout).

Restricted Virtual Share Award Plan

According to the rules for the Restricted Virtual Share Award (RVSA), a portion of the variable remuneration will be converted into an equivalent number of virtual shares. The conversion is based on the weighted average price (XETRA) of Aareal Bank AG's share according to Bloomberg, on the five trading days following the publication of the annual report for the reference period. The amount granted within the scope of the RVSA is only awarded on a provisional basis. Entitlement to the RVSA vests over a period of three years at one third of the original award each year, starting one year after the end of the reference period, provided that certain conditions (penalty rules) are met. The RVSA is paid out after a holding period of one year starting on the date on which entitlement arose. When the holding period is expired, the beneficiary has an option right to postpone the RVSA payout by not more than three years. The payout may only be made as at 31 March, 30 June or 30 September of a calendar year; exercise of the option has to be notified to the Bank not later than at the tenth day following the publication of the quarterly financial results.

The payout amount is calculated by multiplying the number of the exercised virtual shares with the weighted average price on XETRA of Aareal Bank AG's share according to Bloomberg, on the five trading days following the publication of the quarterly financial results.

According to the penalty rules, the Bank is entitled to reduce the amount of the portion of the RVSA for which no entitlement has been earned in an appropriate manner, possibly down to zero. The reasons for a reduction of the RVSA are described in section 45 of the German Banking Act (Kreditwesengesetz, KWG): when, until the relevant payout date, Aareal Bank's regulatory capital does not meet the requirements of section 10 (1) and (1b) or of section 45b (1) of the KWG or the investment of its funds does not comply with the requirements of section 11 (1) of the KWG or the development of Aareal Bank AG's financial position and financial performance justifies the assumption that it will not be able to meet these requirements permanently. The reasons for a reduction of the RVSA also exist when cases of serious individual misconduct prior to the entitlement of the RVSA, or parts of it, are identified afterwards. Examples are cases of misconduct which give rise to extraordinary termination of employment relationships, a breach of the prohibition of hedge transactions, even after the termination of the employment relationships, as well as a material breach of internal guidelines (e.g. Code of Conduct or compliance rules).

In addition, the amount of the RVSA for which no entitlement has arisen may be reduced when the so-called success factor for determining the bonus pool for variable remuneration for the employees of Aareal Bank AG is below zero. The success factor is determined based on the target planned and agreed by Aareal Bank AG's Management Board and Supervisory Board for the operating result before taxes of Aareal Bank Group, net of non-recurring effects. The basis for the determination of the target is the Bank's medium-term planning, taking into account capital employed. The success factor may range from -0.7 and +2.0.

There are no further exercise hurdles, other than the penalty rules, in form of a minimum stock price appreciation target or other market or performance-related criteria. Virtual shares carry full dividend rights, i.e. the beneficiaries receive for each virtual share not yet exercised a cash payment equivalent to the amount of the approved dividend. The maximum term of the plan – in relation to the grant date – is five years (eight years in case of an option for late payout).

Virtual share plan

According to the rules for the virtual share plan, a portion of the variable remuneration will be converted into an equivalent number of virtual shares. The conversion rate corresponds to the weighted average price (XETRA) of Aareal Bank AG's share according to Bloomberg, on the four trading days following the publication of the annual report for the reference period.

The virtual shares are automatically exercised in the three years following the reference year, with one third being exercised in each year. The exercise is based on the weighted average price on XETRA of Aareal Bank AG's share according to Bloomberg, on the publication date of the annual report for the financial year preceding the exercise and the four following trading days. For virtual shares granted from 1 January 2011, the beneficiary has an option right to postpone the payout of the virtual shares by not more than three years. The payout may only be made as at 31 March, 30 June or 30 September of a calendar year; exercise of the option has to be notified to the Bank not later than at the tenth day following the publication of the quarterly financial results.

There are no exercise hurdles in form of a minimum stock price appreciation target or other market or performance-related criteria. With respect to virtual shares that have not been exercised, the beneficiaries receive for each virtual share a cash payment equivalent to the amount of the approved dividend. The maximum term of the plan – in relation to the grant date – is four years (seven years in case of an option for late payout).

b) Valuation model and valuation assumptions

The obligations resulting from all of the described share-based payment arrangements as of the balance sheet date correspond to the remuneration granted, discounted to the balance sheet date. The discount period corresponds to the period from the balance sheet date to the earliest exercise or payout date per plan and per tranche. The discount is based on the average market interest rate of the previous seven financial years as published by the German Federal Ministry of Justice applicable as at the relevant balance sheet date, depending on the term. These interest rates in turn are based on the zero-coupon euro swap curve.

c) Amount of cash-settled share-based payment transactions

The total amount of outstanding virtual shares in relation to the above mentioned share-based payment arrangements changed as follows:

Quantity (number)	2013	2012
Balance (outstanding) at 1 January	**622,495**	**406,431**
Granted	328,513	284,856
of which: vested	136,816	210,848
of which: awarded on a provisional basis	191,697	74,008
Expired	-	-
Exercised	160,832	68,792
Balance (outstanding) at 31 December	**790,176**	**622,495**
of which: exercisable	130,227	290,478

Remuneration for key executives

The definition of executives in key positions within Aareal Bank Group includes members of management or supervisory bodies of Aareal Bank AG and its subsidiaries, plus first-level managers and experts of Aareal Bank AG (other related parties).

Total remuneration of executives in key positions of Aareal Bank AG is analysed below:

€ 000's	1 Jan-31 Dec 2013	1 Jan-31 Dec 2012
Short-term employee benefits	14,101	13,787
Post-employment benefits	2,285	2,033
Other long-term benefits	2,325	2,204
Termination benefits	-	580
Share-based payment	4,009	3,826
Total	**22,720**	**22,430**

Other disclosures

Disclosures in accordance with the German Pfandbrief Act (section 28)

Total amount and related cover assets pool of outstanding mortgage Pfandbriefe and public-sector Pfandbriefe

€ mn	Cover assets pool	Pfandbriefe outstanding	Excess cover
31 Dec 2013			
Mortgage Pfandbriefe			
Nominal value	12,953.3	10,599.2	2,354.1
Present value	13,877.7	11,085.2	2,792.5
Public-sector Pfandbriefe			
Nominal value	2,534.1	2,256.7	277.4
Present value	3,039.5	2,807.2	232.3

€ mn	Cover assets pool	Pfandbriefe outstanding	Excess cover
31 Dec 2012			
Mortgage Pfandbriefe			
Nominal value	11,819.5	9,555.2	2,264.3
Present value	12,675.2	10,563.3	2,111.9
Public-sector Pfandbriefe			
Nominal value	3,176.0	2,859.5	316.5
Present value	3,849.8	3,565.2	284.6

€ mn	Share of derivatives in cover assets pool 2013	Share of derivatives in cover assets pool 2012	Share of derivatives in covered bonds 2013	Share of derivatives in covered bonds 2012
Nominal value				
Mortgage Pfandbriefe	64.6	19.7	48.4	160.8
Public-sector Pfandbriefe	0.0	0.0	0.0	0.0
Present value				
Mortgage Pfandbriefe	178.2	129.5	0.0	0.0
Public-sector Pfandbriefe	131.7	130.7	0.0	0.0

€ mn	Share of further cover assets 2013	Share of further cover assets 2012
Mortgage Pfandbriefe	1,379.4	1,104.4
Public Sector Pfandbriefe	0.0	0.0

€ mn	Cover assets pool	Pfandbriefe outstanding	Excess cover
31 Dec 2013			
Risk-adjusted net present value			
Mortgage Pfandbriefe	14,138.6	11,441.7	2,696.9
Public Sector Pfandbriefe	3,039.4	2,807.2	232.2

€ mn	Cover assets pool	Pfandbriefe outstanding	Excess cover
31 Dec 2012			
Risk-adjusted net present value			
Mortgage Pfandbriefe	12,808.6	10,896.2	1,912.4
Public Sector Pfandbriefe	3,849.8	3,565.2	284.6

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

€ mn	Cover assets pool	Pfandbriefe outstanding
31 Dec 2013		
Mortgage Pfandbriefe		
Up to 1 year	2,263.2	1,501.5
Between 1 year and 2 years	1,606.9	1,172.4
Between 2 year and 3 years	2,796.0	2,283.6
Between 3 year and 4 years	1,859.9	1,349.6
Between 4 year and 5 years	1,963.1	1,685.7
Between 5 years and 10 years	2,187.8	2,362.9
More than 10 years	276.4	243.5
Total	**12,953.3**	**10,599.2**
Public Sector Pfandbriefe		
Up to 1 year	158.5	210.6
Between 1 year and 2 years	172.6	72.1
Between 2 year and 3 years	186.2	97.2
Between 3 year and 4 years	233.1	164.3
Between 4 year and 5 years	316.0	378.2
Between 5 years and 10 years	662.0	610.9
More than 10 years	805.7	723.4
Total	**2,534.1**	**2,256.7**

€ mn	Cover assets pool	Pfandbriefe outstanding
31 Dec 2012		
Mortgage Pfandbriefe		
Up to 1 year	2,155.1	1,833.8
Between 1 year and 2 years	2,212.9	1,524.1
Between 2 year and 3 years	1,598.8	1,172.8
Between 3 year and 4 years	2,478.7	1,468.8
Between 4 year and 5 years	1,228.1	1,131.0
Between 5 years and 10 years	2,092.4	2,138.6
More than 10 years	53.5	286.1
Total	**11,819.5**	**9,555.2**
Public Sector Pfandbriefe		
Up to 1 year	525.9	625.3
Between 1 year and 2 years	242.9	210.6
Between 2 year and 3 years	172.0	72.1
Between 3 year and 4 years	185.8	97.2
Between 4 year and 5 years	137.4	164.3
Between 5 years and 10 years	871.6	794.8
More than 10 years	1,040.4	895.2
Total	**3,176.0**	**2,859.5**

Loans and advances used to cover mortgage Pfandbriefe

€ mn	Cover assets pool 2013	Cover assets pool 2012
Distribution of the amounts measured at nominal value by volume		
Up to € 300 thousand	13.8	14.6
Between € 300 thousand and € 5 million	459.8	584.6
More than € 5 million	11,035.6	10,096.2
Total	**11,509.2**	**10,695.4**

As at the balance sheet date, the loans and advances used for lending against Mortgage Pfandbriefe included payment arrears of 90 days or more in the amount of € 0.7 million (2012: € 9.7 million), of which € 0.7 million refer to Italy and € 0.0 million to Germany. In the comparable period of the previous year, payment arrears of 90 days or more referred to Germany (€ 0.0 million) and Italy (€ 9.7 million).

Distribution of the amounts measured at nominal value and used to cover mortgage Pfandbriefe by countries in which the real property collateral is located:

	Commercial property							Residential property						
€ mn	Building plots only	New buildings not yet yielding returns	Office buildings	Retail property	Industrial	Other	Total	Building plots only	New buildings not yet yielding returns	Single family homes	Multi family homes	Flats/apartments	Total	Total cover assets pool
31 Dec 2013														
Belgium			139.1	95.2	9.0	38.9	282.2							282.2
Denmark		1.6	81.7	10.4	5.7	52.1	151.5		16.6				16.6	168.1
Germany			583.6	242.3	456.1	250.7	1,532.7	0.8		3.9	539.5	0.5	544.7	2,077.4
Estonia				26.8			26.8							26.8
Finland			20.9	166.4	5.4	20.5	213.2							213.2
France		48.2	887.0	66.9	227.6	329.0	1,558.7				4.7		4.7	1,563.4
United Kingdom			344.7	645.0	116.3	302.4	1,408.4							1,408.4
Italy			689.0	383.8	46.7	69.1	1,188.6				82.4		82.4	1,271.0
Canada			45.5			50.4	95.9							95.9
Netherlands			145.9	174.4	91.9	239.9	652.1				155.0		155.0	807.1
Austria				47.9			47.9							47.9
Poland		41.1	303.8	429.1	100.8	11.0	885.8							885.8
Sweden			203.6	244.1	213.5	47.3	708.5							708.5
Switzerland						159.2	159.2							159.2
Slovakia					2.2		2.2							2.2
Spain		20.6	40.0	446.1	20.5	62.4	589.6							589.6
Czech Republic	3.8		65.9		14.5	59.1	143.3							143.3
USA	25.3	212.0	188.1	347.0		225.0	997.4				61.8		61.8	1,059.2
Total	**29.1**	**323.5**	**3,738.8**	**3,325.4**	**1,310.2**	**1,917.0**	**10,644.0**	**0.8**	**16.6**	**3.9**	**843.4**	**0.5**	**865.2**	**11,509.2**

	Commercial property							Residential property						
€ mn	Building plots only	New buildings not yet yielding returns	Office buildings	Retail property	Industrial	Other	Total	Building plots only	New buildings not yet yielding returns	Single family homes	Multi family homes	Flats/apartments	Total	Total cover assets pool
31 Dec 2012														
Belgium			172.6	96.6	9.0	30.9	309.1							309.1
Denmark	3.7		70.3	13.2	5.7	67.2	160.1	2.3	1.6		8.7	4.2	16.8	176.9
Germany			349.4	176.6	468.0	228.7	1,222.7	0.8		4.7	634.7	0.9	641.1	1,863.8
Estonia				26.8			26.8							26.8
Finland			28.6	215.8	5.4	20.5	270.3							270.3
France		83.0	523.9	72.2	190.7	283.2	1,153.0				4.7		4.7	1,157.7
United Kingdom			180.1	469.7	158.9	307.1	1,115.8							1,115.8
Italy	74.5	9.0	712.9	390.3	50.9	107.2	1,344.8				83.6		83.6	1,428.4
Japan						56.5	56.5							56.5
Canada			50.8			90.1	140.9							140.9
Luxembourg			4.5				4.5							4.5
Netherlands			190.1	41.2	152.3	168.7	552.3				155.0		155.0	707.3
Poland		9.1	314.7	188.7	105.5	-	618.0							618.0
Sweden			367.1	126.4	237.4	33.1	764.0							764.0
Switzerland			20.0	16.8		185.2	222.0							222.0
Slovakia					6.6	-	6.6							6.6
Spain		20.6	40.0	475.1	21.1	50.2	607.0							607.0
Czech Republic	3.8		99.6	10.2	15.7	62.6	191.9							191.9
USA		188.4	326.2	247.4	19.2	163.3	944.5				83.4		83.4	1,027.9
Total	**82.0**	**310.1**	**3,450.8**	**2,567.0**	**1,446.4**	**1,854.5**	**9,710.8**	**3.1**	**1.6**	**4.7**	**970.1**	**5.1**	**984.6**	**10,695.4**

In the financial year 2013, the Bank did not acquire any properties for the purpose of loss prevention (2012: none).

As at 31 December 2013, there were no foreclosures or forced administration procedures pending, and neither had any foreclosures been carried out (2012: none).

As at 31 December 2013, interest payments were overdue in the amount of € 3.7 million (2012: € 6.2 million) for commercial property and in the amount of € 0.0 million (2012: € 0.1 million) for residential property.

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

€ mn	Sovereigns	Public-sector entities regional	Public-sector entities municipal	Other	Total
31 Dec 2013					
Germany	13.0	1,385.6	18.7	426.2	1,843.5
EU institutions	-	-	-	111.4	111.4
France	105.0	-	-	-	105.0
Italy	114.0	-	-	-	114.0
Japan	-	-	20.0	-	20.0
Austria	150.2	25.0	-	-	175.2
Poland	25.0	-	-	-	25.0
Sweden	25.0	-	-	-	25.0
Spain	-	115.0	-	-	115.0
Total	**432.2**	**1,525.6**	**38.7**	**537.6**	**2,534.1**

€ mn	Sovereigns	Public-sector entities regional	Public-sector entities municipal	Other	Total
31 Dec 2012					
Germany	13.7	1,770.5	26.9	574.3	2,385.4
EU institutions	-	-	-	111.4	111.4
France	-	-	-	100.0	100.0
Italy	114.0	-	-	-	114.0
Japan	-	-	20.0	50.0	70.0
Austria	125.2	25.0	-	80.0	230.2
Poland	50.0	-	-	-	50.0
Spain	-	115.0	-	-	115.0
Total	**302.9**	**1,910.5**	**46.9**	**915.7**	**3,176.0**

Neither at the balance sheet date nor in the comparable period of the previous year did loans and advances used for lending against public-sector Pfandbriefe include any items with payment arrears of 90 days or more.

Contingencies

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

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

Due to its participating interest in Liquiditäts-Konsortialbank GmbH, Frankfurt/Main, in the nominal amount of € 1 million, Aareal Bank AG has call commitments of up to € 6 million. In addition, Aareal Bank AG has a pro-rata principal liability in the event of non-fulfilment of call commitments by other co-shareholders, who hold aggregate interests of € 63 million.

Consolidated financial statements

As the parent company of Aareal Bank Group, Aareal Bank AG, Wiesbaden, prepares consolidated financial statements. The consolidated financial statements will be deposited with the Register of Companies at the Wiesbaden District Court (Amtsgericht, HRB 13 184) and will also be available from Aareal Bank AG in Wiesbaden, Germany.

Loans to executive bodies of Aareal Bank

Throughout the financial year 2013, the Bank has reported transactions subject to reporting requirements within the meaning of section 15a of the German Securities Trading Act (WpHG) to BaFin, the German financial services regulatory agency, without delay, and also published such details on its website. Furthermore, Aareal Bank AG has undertaken in its extended principles related to the German Corporate Governance Code to disclose on its website, without delay, each reported purchase or sale of the shares of the Company and its subsidiaries as well as options and other derivatives related to these by members of the Management Board or the Supervisory Board.

The following list provides an overview of existing loans to related parties:

€ mn	31 Dec 2013	31 Dec 2012
Management Board	-	-
Supervisory Board	0.5	0.6
Other related parties	-	1.6
Total	0.5	2.2

Loans extended to members of the Supervisory Board generally have a term between 10 and 18 years, and bear interest at (nominal) rates between 4.71 % and 5.66 %. Collateral was provided in line with usual market practice. In the year under review, repayments amounted to € 0.1 million.

Employees

The average staffing level is shown below:

Yearly average	1 Jan-31 Dec 2013	1 Jan-31 Dec 2012
Salaried employees	840	893
Executives	27	28
Total	**867**	**921**
of which: Part-time employees	168	167

Auditors' fees

The total fees charged by the auditor are as follows:

€ 000's	
Category	
Audit services	2,768.0
Other assurance services	52.8
Tax advisory services	63.1
Other services	1,952.9
Total	**4,836.8**

Notices pursuant to section 21 (1) of the German Securities Trading Act (WpHG)

Pursuant to the WpHG, any investor whose shareholding in a listed company reaches, exceeds or falls short of certain threshold values in terms of voting rights (whether by purchase, sale or by any other means) must notify the Company and the German Federal Financial Supervisory Authority. The lowest threshold for this notification requirement is 3 %. 71.1 % of Aareal Bank AG shares are held in free float. The largest shareholder of the Company is Aareal Holding Verwaltungsgesellschaft mbH, Düsseldorf, with an interest of 28.9 %.

During the year, we received several notifications on voting rights from Fidelity Group, Boston, Massachusetts, USA. The notification made by this group of companies referred to the fact that, as at 30 June 2013, the shares held by FMR LLC, Boston, Massachusetts, USA exceeded the 3 % threshold, amounting to 3.01 % (1,801,832 voting rights). Attribution of all the voting rights is based on section 22 (1) sentence 1 No. 6 in conjunction with sentence 2 of the WpHG.

Allianz Global Investors Europe GmbH, Frankfurt issued several notifications of voting rights during 2013. The last notification, which was issued on 30 May 2013, reported a share of voting rights of 4.97 % (2,972,198 voting rights). Of this share of voting rights, 0.98 % of the total number of voting rights (corresponding to 583,910 of a total of 59,857,221 voting rights) are attributable to it pursuant to section 22 (1) sentence 1 No. 6 of the WpHG.

Dimensional Group, Austin, Texas, USA, notified us on 4 June 2012 that, as at 29 May 2012, it held the following amount of voting rights:

- Dimensional Fund Advisors LP, Austin, Texas, USA, 3.04 % (1,820,026 voting rights); attribution of all voting rights pursuant to section 22 (1) sentence 1 No. 6 of the WpHG.
- Dimensional Holdings Inc., Austin, Texas, USA, 3.04 % (1,820,026 voting rights); attribution of all voting rights pursuant to section 22 (1) sentence 1 No. 6 in conjunction with section 22 (1) sentence 2 of the WpHG.

In 2013, we did not receive any further notifications on voting rights from Dimensional Group.

BlackRock Group, USA, issued several notifications of voting rights in 2013 pursuant to which its share of voting rights fell below the threshold of 3.00 %.The following entities were affected:

- BlackRock, Inc., New York, USA, 2.97 % (1,779,715 voting rights) as at 21 August 2013, attribution of all voting rights pursuant to section 22 (1) sentence 1 No. 6 in conjunction with section 22 (1) sentence 2 of the WpHG.
- BlackRock HoldCo 2, Inc., Wilmington, Delaware, USA, 2.9995 % (1,795,424 voting rights) as at 19 August 2013, attribution of all voting rights pursuant to section 22 (1) sentence 1 No. 6 in conjunction with section 22 (1) sentence 2 of the WpHG.

Norges Bank, Oslo, Norway, issued two notifications of voting rights during 2013. The last notification, which was issued on 17 December 2013, reported a share of voting rights of 2.99 % (1,790,459 voting rights of a total of 59,857,221 voting rights).

The Norwegian Ministry of Finance, Oslo, Norway, for and on behalf of the government of Norway, issued two notifications of voting rights during 2013. The last notification, which was issued on 17 December 2013, reported a share of voting rights of 2.99 % (1,790,459 voting rights of a total of 59,857,221 voting rights). All of these voting rights can be attributed to the government of Norway, pursuant to section 22 (1) sentence 1 no. 1 of the WpHG.

Corporate Governance Code

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

Proposal on the appropriation of profits

The Management Board of Aareal Bank AG proposes to the Annual General Meeting that a partial amount of € 44,892,915.75 of Aareal Bank AG's net retained profit of € 49,892,915.75 for the financial year 2013, as reported under the German Commercial Code (HGB), be used to distribute a dividend of € 0.75 per notional no-par value share.

The Management Board also proposes to the Annual General Meeting to transfer the remaining distributable profit of € 5,000,000.00 to other retained earnings.

Executive bodies of Aareal Bank AG
Offices held in accordance with section 285 no. 10 of the German Commercial Code (HGB) in conjunction with section 125 (1) sentence 5 of the German Public Limited Companies Act (AktG)

Supervisory Board

Hans W. Reich, Chairman of the Supervisory Board (until 22 May 2013)		
Chairman of the Supervisory Board of Citigroup Global Markets Deutschland AG		
Aareal Bank AG	Chairman of the Supervisory Board	until 22 May 2013
Citigroup Global Markets Deutschland AG	Chairman of the Supervisory Board	
Marija G. Korsch, Chairman of the Supervisory Board (since 22 May 2013)		
Former Executive at Bankhaus Metzler seel. Sohn & Co. Holding AG		
Aareal Bank AG	Member of the Supervisory Board	
Just Software AG	Member of the Supervisory Board	
Erwin Flieger, Deputy Chairman of the Supervisory Board		
Chairman of the Supervisory Boards of Bayerische Beamten Versicherungsgruppe		
Aareal Bank AG	Deputy Chairman of the Supervisory Board	
Bayerische Beamten Lebensversicherung a.G.	Chairman of the Supervisory Board	
Bayerische Beamten Versicherung AG	Chairman of the Supervisory Board	
BBV Holding AG	Chairman of the Supervisory Board	
DePfa Holding Verwaltungsgesellschaft mbH	Chairman of the Supervisory Board	
MEAG MUNICH ERGO Kapitalanlagegesellschaft mbH	Member of the Supervisory Board	
Neue Bayerische Beamten Lebensversicherung AG	Chairman of the Supervisory Board	
York-Detlef Bülow *, Deputy Chairman of the Supervisory Board		
Aareal Bank AG		
Aareal Bank AG	Deputy Chairman of the Supervisory Board	
Christian Graf von Bassewitz,		
Banker (ret'd.); former Spokesman of the General Partners of Bankhaus Lampe KG		
Aareal Bank AG	Member of the Supervisory Board	
Bank für Sozialwirtschaft Aktiengesellschaft	Member of the Supervisory Board	
Deutscher Ring Krankenversicherungsverein a.G.	Deputy Chairman of the Supervisory Board	
OVB Holding AG	Deputy Chairman of the Supervisory Board	until 20 June 2013
OVB Vermögensberatung AG	Member of the Supervisory Board	until 20 June 2013
SIGNAL IDUNA Allgemeine Versicherung AG	Member of the Supervisory Board	
SIGNAL IDUNA Holding AG	Member of the Supervisory Board	
Societaet CHORVS AG	Member of the Supervisory Board	

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

Manfred Behrens		
CEO/Chairman of the Management Board of Swiss Life Deutschland Holding GmbH		
Aareal Bank AG	Member of the Supervisory Board	
Swiss Life Select Schweiz AG (former AWD Allgemeiner Wirtschaftsdienst AG)	President of the Board of Directors	until 29 April 2013
tecis Finanzdienstleistungen AG	Chairman of the Supervisory Board	
Thomas Hawel *		
Aareon Deutschland GmbH		
Aareal Bank AG	Member of the Supervisory Board	
Aareon Deutschland GmbH	Deputy Chairman of the Supervisory Board	
Dieter Kirsch *		
Aareal Bank AG		
Aareal Bank AG	Member of the Supervisory Board	
Dr Herbert Lohneiß		
Former Chief Executive Officer of Siemens Financial Services GmbH (ret'd)		
Aareal Bank AG	Member of the Supervisory Board	
UBS Global Asset Management (Deutschland) GmbH	Member of the Supervisory Board	
Joachim Neupel, Chairman of the Accounts and Audit Committee		
German Chartered Accountant, tax consultant		
Aareal Bank AG	Member of the Supervisory Board	
Richard Peters (since 22 May 2013)		
President and Chairman of the Management Board of Versorgungsanstalt des Bundes und der Länder		
Aareal Bank AG	Member of the Supervisory Board	since 22 May 2013
DePfa Holding Verwaltungsgesellschaft mbH	Member of the Supervisory Board	
Prof Dr Stephan Schüller		
Spokesman of the General Partners of Bankhaus Lampe KG		
Aareal Bank AG	Member of the Supervisory Board	
DePfa Holding Verwaltungsgesellschaft mbH	Deputy Chairman of the Supervisory Board	
Universal-Investment-Gesellschaft mbH	Member of the Supervisory Board	
Helmut Wagner *		
Aareon Deutschland GmbH		
Aareal Bank AG	Member of the Supervisory Board	
Aareon Deutschland GmbH	Member of the Supervisory Board	

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

Management Board

Dr Wolf Schumacher, Chairman of the Management Board		
Corporate Communications, Investor Relations, Corporate Development, Human Resources, Legal, Compliance, Audit and Operations		
Aareon AG	Member of the Supervisory Board	
EBS European Business School gGmbH	Member of the Supervisory Board	
Dirk Große Wördemann, Member of the Management Board (until 31 May 2013)		
Sales Units Structured Property Financing		
Aareal Bank Asia Limited	Member of the Board of Directors	until 31 May 2013
Aareal Bank Asia Limited	CEO (Chairman)	until 31 May 2013
Aareal Capital Corporation	Chairman of the Board of Directors	until 31 May 2013
Aareal Financial Service spol. s r.o. i.L.	Member of the Supervisory Board	until 31 May 2013
Aareon AG	Member of the Supervisory Board	until 31 May 2013
Deutsche Bau- und Grundstücks-Aktiengesellschaft	Deputy Chairman of the Supervisory Board	until 31 May 2013
Dagmar Knopek, Member of the Management Board (since 1 June 2013)		
Sales Units Structured Property Financing		
Aareal Bank Asia Limited	Member of the Board of Directors	since 1 June 2013
Aareal Bank Asia Limited	CEO (Chairman)	since 1 June 2013
Aareal Capital Corporation	Chairman of the Board of Directors	since 1 June 2013
Aareon AG	Member of the Supervisory Board	since 24 June 2013
Hermann Josef Merkens, Member of the Management Board		
Finance, Risk Controlling, Credit Management and Workout		
Aareal Estate AG	Chairman of the Supervisory Board	
Aareal Bank Asia Limited	Member of the Board of Directors	
Aareal Capital Corporation	Member of the Board of Directors	
Aareal First Financial Solutions AG	Member of the Supervisory Board	
Aareon AG	Member of the Supervisory Board	
CredaRate Solutions GmbH	Deputy Chairman of the Supervisory Board	
Thomas Ortmanns, Member of the Management Board		
Institutional Housing Unit, Treasury, Organisation, Information Technology		
Aareal First Financial Solutions AG	Chairman of the Supervisory Board	
Aareon AG	Chairman of the Supervisory Board	
Deutsche Bau- und Grundstücks-Aktiengesellschaft	Chairman of the Supervisory Board	
HypZert GmbH	Member of the Supervisory Board	

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

Ulf Ekelius, Bank Director		
Aareal Financial Service spol. s r.o. i.L.	Member of the Supervisory Board	until 27 June 2013
Dunya Heß		
Aareal Property Services B.V.	Member of the Supervisory Board	
Uli Gilbert		
Terrain-Aktiengesellschaft Herzogpark	Member of the Supervisory Board	
Hans-Ulrich Kron, Bank Director		
Aareal Estate AG	Deputy Chairman of the Supervisory Board	
Terrain-Aktiengesellschaft Herzogpark	Deputy Chairman of the Supervisory Board	
Dr Stefan Lange, Bank Director		
Aareal Estate AG	Member of the Supervisory Board	
Aareal First Financial Solutions AG	Member of the Supervisory Board	
Terrain-Aktiengesellschaft Herzogpark	Chairman of the Supervisory Board	
Dirk Pasewald		
Aareal Property Services B.V.	Member of the Supervisory Board	
Markus Schmidt		
Aareal Property Services B.V.	Member of the Supervisory Board	
Christine Schulze Forsthövel, Bank Director		
Aareal-Financial Service spol. s r.o. i.L.	Member of the Supervisory Board	until 27 June 2013

Composition of Supervisory Board's committees

Executive Committee	
Marija G. Korsch	Chairman
Erwin Flieger	Deputy Chairman
York-Detlef Bülow	Deputy Chairman
Prof Dr Stephan Schüller	

Committee for Urgent Decisions	
Marija G. Korsch	Chairman
Christian Graf von Bassewitz	
Erwin Flieger	
Dr Herbert Lohneiß	
Joachim Neupel	

Accounts and Audit Committee	
Joachim Neupel	Chairman
Prof Dr Stephan Schüller	Deputy Chairman
Christian Graf von Bassewitz	
York-Detlef Bülow	
Marija G. Korsch	

Nomination Committee
Marija G. Korsch
Erwin Flieger

Risk Committee	
Marija G. Korsch	Chairman
Dr Herbert Lohneiß	Deputy Chairman
Christian Graf von Bassewitz	
Erwin Flieger	
Dieter Kirsch	
Joachim Neupel	

Responsibility statement

Statement pursuant to section 37v (2) No.3 of the WpHG

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

Wiesbaden, 26 February 2014

The Management Board

Dr Wolf Schumacher	**Dagmar Knopek**	**Hermann J. Merkens**	**Thomas Ortmanns**

Auditors' Report

We have audited the annual financial statements, comprising the balance sheet, the income statement and the notes to the financial statements, together with the bookkeeping system, and the management report of Aareal Bank AG, Wiesbaden, for the business year from 1 January to 31 December, 2013. The maintenance of the books and records and the preparation of the annual financial statements and management report in accordance with German commercial law are the responsibility of the Company's Board of Managing Directors. Our responsibility is to express an opinion on the annual financial statements, together with the bookkeeping system, and the management report based on our audit.

We conducted our audit of the annual financial statements in accordance with § (Article) 317 HGB ("Handelsgesetzbuch" – "German Commercial Code") and German generally accepted standards for the audit of financial statements promulgated by the Institut der Wirtschaftsprüfer (Institute of Public Auditors in Germany) (IDW). Those standards require that we plan and perform the audit such that misstatements materially affecting the presentation of the net assets, financial position and results of operations in the annual financial statements in accordance with (German) principles of proper accounting and in the management report are detected with reasonable assurance. Knowledge of the business activities and the economic and legal environment of the Company and expectations as to possible misstatements are taken into account in the determination of audit procedures. The effectiveness of the accounting-related internal control system and the evidence supporting the disclosures in the books and records, the annual financial statements and the management report are examined primarily on a test basis within the framework of the audit. The audit includes assessing the accounting principles used and significant estimates made by the Company's Board of Managing Directors, as well as evaluating the overall presentation of the annual financial statements and management report. We believe that our audit provides a reasonable basis for our opinion.

Our audit has not led to any reservations.

In our opinion based on the findings of our audit, the annual financial statements comply with the legal requirements and give a true and fair view of the net assets, financial position and results of operations of the Company in accordance with (German) principles of proper accounting. The management report is consistent with the annual financial statements and as a whole provides a suitable view of the Company's position and suitably presents the opportunities and risks of future development.

Frankfurt/Main, 28 February 2014

PricewaterhouseCoopers
Aktiengesellschaft
Wirtschaftsprüfungsgesellschaft

Stefan Palm	**ppa. Kai Böhm**
Wirtschaftsprüfer	**Wirtschaftsprüfer**
German Public Auditor	**German Public Auditor**

Report of the Supervisory Board of Aareal Bank AG, Wiesbaden

Dear shareholders,

During the financial year 2013, Aareal Bank AG once again performed successfully, mastering the challenges presented by the demanding market environment. Aareal Bank achieved consolidated operating profit which exceeded both the results posted in 2011 and the previous year's figures.

The Supervisory Board considers Aareal Bank AG's consistently positive results as evidence for the viability and operative strength of the Group's business model.

During the financial year under review, the Supervisory Board continually advised, monitored, and supervised the management of the Company. The Management Board informed the Supervisory Board regularly, without delay and comprehensively, both orally and in writing, of all 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 – until 22 May 2013, Mr Hans Reich, and from 22 May 2013 onwards, Ms Marija G. Korsch – 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 Chairmen of the Supervisory Board, in order to discuss key issues and important decisions personally.

Activities of the plenary meeting of the Supervisory Board

Six 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 by the members of the Management Board, and discussed these in detail. Proceedings and reports during all scheduled meetings focused on the way the Bank dealt with the challenges posed by the European sovereign debt crisis, and the resulting effects upon Aareal Bank AG.

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 regulations implementing the Basel III framework (the Capital Requirements Regulation (CRR) and the Capital Requirements Directive (CRD IV)).

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 the European sovereign debt crisis, and from other market developments.

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. Within 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:

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

During the extraordinary meeting in March, the Chairman of the Supervisory Board declared that he would resign from his chairmanship and from membership of the Supervisory Board, with effect from the end of the Annual General Meeting on 22 May 2013. During the same meeting, the Supervisory Board accepted the proposal to elect Ms Marija G. Korsch as the Chairman of the Supervisory Board, succeeding Mr Reich.

During an additional, scheduled meeting in March, the Supervisory Board concerned itself in detail with the financial statements and consolidated financial statements presented for the 2012 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 2013 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 2013. This meeting also discussed the annual reports submitted by Internal Audit and by the Compliance Officer. Furthermore, the proposals submitted by the Nomination Committee to fill the vacancy as a result of Mr Reich's retirement were discussed, and the Supervisory Board decided to propose Mr Richard Peters as a candidate for election to the Supervisory Board to the Annual General Meeting.

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.

During the September meeting, corporate governance issues were presented and discussed, alongside other regulatory issues.

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. The meeting also discussed corporate governance issues, as well as the requirements of the amendments to the German Banking Act concerning the structure of the Supervisory Board committees. 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 (AktG), which was subsequently published on the Bank's website. Moreover, the Supervisory Board concerned itself with the latest amendments to the German Ordinance on Remuneration in Financial Institutions (InstVergV). With the support of external advisors, the Supervisory Board discussed individual items where action was required with respect to the remuneration concept, in the context of the corresponding governance structure, and adopted proposed resolutions where possible. The Supervisory Board duly noted a related implementation schedule, taking coordination with the Works Council and the Executive Staff Representative Committee into account.

In accordance with good corporate governance practice, the Supervisory Board also regularly examines the efficiency of its activities in order to identify any areas requiring improvement. The results of the efficiency examination conducted during the 2013 financial year were acknowledged by the members of the Supervisory Board, and were discussed in detail. No concrete need for action was identified.

Strategy documents were regularly submitted to, and discussed by the Supervisory Board, in accordance with the Minimum Requirements for Risk Management in Banks (MaRisk). In this context, the Supervisory Board received a report on the status and implementation of the latest amendments to the 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.

This meeting provided the opportunity for a more detailed analysis and discussion of key topics, outside the regular work of the Supervisory Board.

Activities of Supervisory Board committees

The Supervisory Board has established five committees in order to perform its supervisory duties in an efficient manner: the Executive Committee, the Risk Committee, the Committee for Urgent Decisions, the Accounts and Audit Committee, and the Nomination Committee. Explanations concerning the new structure of Supervisory Board committees in accordance with section 25d of the KWG are provided in the Corporate Governance Statement.

The Executive Committee of the Supervisory Board convened for three scheduled meetings and three extraordinary meetings. In the scheduled meetings, the Executive Committee prepared the proposed resolutions of the plenary meetings of the Supervisory Board. Strategic options of Aareal Bank were discussed during the extraordinary meetings; this included the acquisition of all shares in Corealcredit Bank AG, which was agreed upon on 22 December 2013.

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 environment and the situation of the Bank's competitors. 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. Also, detailed reports were given regarding the Bank's liquidity status and 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 discussed in detail the developments of the debt crisis and their implications for the business environment of Aareal Bank, the consideration of Aareal Bank's risk-bearing capacity and the detailed account of its capital ratios, as well as the implementation of the requirements in accordance with Basel III. 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 Accounts and Audit Committee held six meetings during the year under review. During its meeting in February 2013, the Accounts and Audit Committee received and discussed the preliminary results for the 2012 financial year. During its March meeting, the committee received the external auditors' report on the 2012 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 extensive discussions with the external auditors. In accordance with its duties under the Memorandum and Articles of Association, the Accounts and Audit Committee also discussed the selection of external auditors and the focal aspects of the audit for 2013 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 2013, the Management Board presented the quarterly results for the financial year, as well as the preliminary full-year results for 2012 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 2013 were discussed at a meeting in February 2014.

In its meeting on 19 March 2014, the Audit Committee received the external auditors' detailed report on the audit and audit results for the 2013 financial year, and discussed these results extensively with the auditors and the Management Board.

The Nomination Committee convened once in 2013. The task of the committee is to coordinate and carry out the search for new shareholder representatives on the Supervisory Board, if a member representing shareholders retires from the

Supervisory Board. Hans W. Reich resigned from his office with effect from 22 May 2013 during the financial year under review.

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.

Member of the Supervisory Board	Number of meetings attend / number of meetings (plenary and committee meetings)
Hans W. Reich **	9 of 9
Marija G. Korsch	16 of 17
Erwin Flieger	17 of 17
York-Detlef Bülow *	17 of 18
Christian Graf von Bassewitz	15 of 16
Manfred Behrens	4 of 6
Thomas Hawel *	5 of 6
Dieter Kirsch *	10 of 10
Dr Herbert Lohneiß	10 of 10
Joachim Neupel	16 of 16
Richard Peters **	3 of 3
Prof Dr Stephan Schüller	17 of 18
Helmut Wagner *	6 of 6

* employee representative
** member of the Supervisory Board for only part of the financial year

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 2013, 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 and the Group Management Report 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 IFRS and the proposal of the Management Board regarding the appropriation of profit and the audit report were examined in detail. No objections were raised to the audit results. In its meeting on 26 March 2014, 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.

Personnel matters

Hans W. Reich retired from his office as Chairman and as a member of the Supervisory Board, with effect from the end of the Annual General Meeting of Aareal Bank AG on 22 May 2013. Hans W. Reich's tenure was shaped by a number of key challenges for Aareal Bank, which the Bank mastered during his chairmanship of the Supervisory Board. The Supervisory Board regrets that the Bank has lost a renowned expert in international banking, and would like to sincerely thank Mr Reich for his long-standing and successful service on the Bank's Supervisory Board.

At the same time, the Supervisory Board welcomes new member Richard Peters and looks forward to a fruitful and successful cooperation. Mr Peters is President and Chairman of the Versorgungsanstalt des Bundes und der Länder – ("VBL"). He has been a member of VBL's Management Board since 1998, first with responsibility for VBL's investments and subsequently for VBL's insurance business and benefits. The Supervisory Board is delighted to have won a capital markets expert and wishes Mr Peters every success for his mandate. Dirk Große Wördemann resigned from Aareal Bank at his own request, with effect from 31 May 2013, in order to focus more on real estate investments, as he had done prior to joining Aareal Bank. He will continue to work for the Bank, as an advisor. Mr Große Wördemann had been a member of Aareal Bank's Management Board since November 2010. The Supervisory Board thanks Mr Große Wördemann for his contributions to the Bank.

The Bank's Supervisory Board appointed Ms Dagmar Knopek as a member of the Management Board with effect from 1 June 2013. The Supervisory Board is delighted that it was able to appoint Ms Knopek, who has been working for Aareal Bank for many years and commands extensive experience in the international commercial property finance business. The Supervisory Board wishes Ms Knopek every success in her new area of responsibility.

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 2013 financial year, which was once again eventful. The commitment and strong motivation of 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.

Special transactions

During the year under review, 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 22 December 2013 with the previous owner, a company of US financial investor Lone Star. The Supervisory Board has been involved in the entire process and was always comprehensively kept informed by the Management Board. The Supervisory Board has approved the transaction; with the acquisition, Aareal Bank AG further expands its position in commercial property finance.

Frankfurt, March 2014

For the Supervisory Board

Korsch

Marija G. Korsch (Chairman)

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Financial Calendar

7 May 2014	Presentation of interim report as at 31 March 2014
21 May 2014	Annual General Meeting – Kurhaus Wiesbaden
12 August 2014	Presentation of interim report as at 30 June 2014
11 November 2014	Presentation of interim report as at 30 September 2014

Structured Property Financing (North America)

Structured Property Financing (Europe)

Structured Property Financing (Asia)

Consulting / Dienstleistungen

Aareal Bank, Real Estate Structured Finance: Brussels, Copenhagen, Dublin, Istanbul, London, Madrid, Moscow, New York, Paris, Rome, Shanghai, Singapore, Stockholm, Warsaw, Wiesbaden | **Aareal Valuation GmbH:** Wiesbaden | **Aareal Estate AG:** Wiesbaden

Aareal Bank, Housing Unit: 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 | **Deutsche Bau- und Grundstücks-AG:** Berlin, Bonn, Moscow, Munich | **Aareal First Financial Solutions AG:** Mainz

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