ANNUAL REPORT 2020

new perspectives

Aareal

YOUR COMPETITIVE ADVANTAGE.

Key Indicators

	1 Jan - 31 Dec 2020	1 Jan - 31 Dec 2019
Results		
Operating profit (€ mn)	-75	248
Consolidated net income (€ mn)	-69	163
Consolidated net income allocated to ordinary shareholders (€ mn)[1]	-90	145
Cost/income Ratio (%)[2]	44.2	37.3
Dividend per share (€)[3]	1.50	–
Earnings per ordinary share (€)[1]	-1.50	2.42
RoE before taxes (%)[1) 4]	-4.1	8.9
RoE after taxes (%)[1) 4]	-3.6	8.8

	31 Dec 2020	31 Dec 2019
Statement of financial position		
Property finance (€ mn)[5]	27,181	25,882
Equity (€ mn)	2,967	2,861
Total assets (€ mn)	45,478	41,137
Regulatory indicators[6]		
Risk-weighted assets (€ mn)	12,138	11,195
Common Equity Tier 1 ratio (CET1 ratio) (%)	18.8	19.6
Tier 1 ratio (T1 ratio) (%)	21.3	22.3
Total capital ratio (TC ratio) (%)	28.0	29.9
Common Equity Tier 1 ratio (CET1 ratio) (%) – Basel IV (phased-in) –[7]	17.3	17.1
Employees	2,982	2,788

	31 Dec 2020	31 Dec 2019
Moody's[8]		
Issuer rating	A3	A3
Bank deposit rating	A3	A3
Outlook	negative	stable
Mortgage Pfandbrief Rating	Aaa	Aaa
Fitch Ratings[9]		
Issuer default rating	BBB+	A-
Senior Preferred	A-	A
Senior Non Preferred	BBB+	A-
Deposit ratings	A-	A
Outlook	negative	negative
Sustainability ratings[10]		
MSCI	AA	AA
ISS-ESG	prime (C+)	prime (C+)
CDP	Awareness Level C	Awareness Level C

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

2) Structured Property Financing segment only; in line with common practice in the banking sector, bank levy and contributions to the deposit guarantee scheme are not included; otherwise, the cost/income ratio would have amounted to 48.1 %. The previous year's figure was adjusted accordingly.

3) 2020: Dividend payments of € 1.50 for 2020 (to be effected in 2021) would need to be made in two steps. In compliance with the requirements published by the European Central Bank (ECB) on 15 December 2020, the distributable amount is calculated at € 0.40 per share. The Management Board plans to submit a corresponding proposal for the appropriation of profits to the ordinary Annual General Meeting in May 2021. Depending on further economic developments, regulatory requirements, the Bank's capital position and its risk situation, an extraordinary Annual General Meeting, which could possibly take place during the fourth quarter of 2021, could then decide on the intended remaining payout of € 1.10 per share.
2019: Following a request of the ECB to refrain from distributing dividends, the AGM decided that net retained profit for 2019 be transferred to retained earnings.

4) "Other reserves" were included in equity, in line with the further development of segment reporting; the previous year's figure was adjusted accordingly.

5) Excluding € 0.3 billion in private client business (31 December 2019: € 0.4 billion) and € 0.3 billion in local authority lending business by the former Westdeutsche ImmobilienBank AG (WestImmo) (31 December 2019: € 0.4 billion)

6) 31 December 2019: excluding dividend for 2019 from initial proposal on the appropriation of net retained profit and including a pro-rata temporis deferral of net interest on the AT1 bond
31 December 2020: including dividend for 2019 from initial proposal on the appropriation of net retained profit and less a proposed dividend of € 1.50 per share in 2021 and pro-rata temporis deferral of net interest on the AT1 bond. Dividend payments of € 1.50 for 2020 (to be effected in 2021) would need to be made in two steps. In compliance with the requirements published by the European Central Bank (ECB) on 15 December 2020, the distributable amount is calculated at € 0.40 per share.The Management Board plans to submit a corresponding proposal for the appropriation of profits to the ordinary Annual General Meeting in May 2021. Depending on further economic developments, regulatory requirements, the Bank's capital position and its risk situation, an extraordinary Annual General Meeting, which could possibly take place during the fourth quarter of 2021, could then decide on the intended remaining payout of € 1.10 per share.
The SREP recommendations concerning the NPL inventory and the ECB's NPL guidelines for exposures newly classified as NPLs, as well as the "CRR Quick fix" as of 30 September 2020, were taken into account.

7) Underlying RWA estimate, incorporating the higher figure determined using the revised AIRBA or the revised CRSA (phased-in), based on the final Basel Committee framework dated 7 December 2017; the calculation of the material impact upon Aareal Bank is subject to the outstanding EU implementation as well as the implementation of additional regulatory requirements (CRR II, EBA requirements etc.). The Bank's Basel IV (fully phased-in) CET1 ratio stood at 13.1 % at the year-end (2019: 13.5 %).

8) Moody's Investors Service confirmed the issuer rating and bank deposit rating on 21 April 2020. At the same time, Moody's set the outlook for the issuer rating and bank deposit rating to "negative", given deterioration in the operating environment on account of the Covid-19 pandemic.

9) The ratings reported as at 31 December 2019 were published on 10 January 2020. Fitch Ratings had changed the outlook to "negative" in connection with the introduction of revised bank rating criteria. On 27 March 2020 the rating was changed, as expected. Due to the Covid-19 pandemic, Fitch Ratings lowered its rating outlook to negative (RWN – Rating Watch Negative), also on 27 March 2020.

10) Please refer to our website (www.aareal-bank.com/en/responsibility/reporting-on-our-progress/) for more details.

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

Contents

New perspectives

To our Shareholders

Group Management Report

Consolidated Financial Statements

Transparency

Our online Annual Report:
ar2020.aareal-bank.com


new
perspectives
Aareal
YOUR COMPETITIVE ADVANTAGE.


AROUND
THE
WORLD

GROUP

Overview of Aareal Bank Group and its three business segments

Aareal Bank Group is a leading international provider of smart financing, software products, digital solutions and payment transaction applications in the property sector and related industries. Aareal Bank AG is the Group's parent entity, headquartered in Wiesbaden.

We strive to offer our clients pioneering solutions which help them explore competitive advantages and enable long-term business success. Because our vision is not limited to traditional banking, we can assess key developments, opportunities and risks reliably and early on, and very quickly bring what we discover to bear in the interests of our clients. We have bundled our portfolio of services into three business segments.

Structured Property Financing

In the Structured Property Financing segment, we support our clients in making large-volume commercial property investments. The investment properties mostly comprise office buildings, hotels, shopping centres, logistics and residential property, as well as student apartments. The regional focus of our activities is on Europe and North America as well as on the Asia-Pacific region. Our local staff, in close coordination with our sector experts at the Group's head office, ensure that the full scope of requisite know-how is available for every transaction. Our clients include institutional investors, private equity firms, family offices, financial institutions, private individuals, listed property companies, pension funds, and investors with a focus on a particular sector.

Banking & Digital Solutions

In the Banking & Digital Solutions segment, we are partners to companies from the housing and property sectors and related industries, offering them extensive consulting services and digital product solutions, which we bundle with traditional corporate institutional banking and our deposit-taking business. An important part of our services in this respect is connecting the housing and property sectors with related industries. We also ensure that our clients have optimised, efficient business processes and payment transaction systems, and we offer comprehensive tenancy bond solutions.

Aareon

Our subsidiary Aareon, the leading provider of ERP software and digital solutions for the European property sector and its partners, represents our third business segment. It offers pioneering and trusted consulting, software and service solutions to optimise IT-supported business processes and business model development. With our international research & development, including cross-border know-how transfer, clients benefit from the entire Group's expertise. Aareon's staff combine property sector expertise and comprehensive IT skills. The Aareon Smart World product portfolio connects property companies and their employees with clients, business partners and technical devices in apartments and buildings. At the heart of this digital ecosystem are Aareon's ERP systems, which can be seamlessly combined with additional digital solutions to meet individual companies' needs.

Profitable growth in all segments

STRATEGY

Aareal Bank Group's strategy focuses on sustainable business success: we want to continue our long track record of success in the German banking sector in the future whilst generating value for all of our stakeholders.

By successfully implementing our "Aareal 2020" programme for the future, we managed to not only achieve our targets for the year, but also to reposition ourselves substantively, organisationally and culturally. Our Group is now higher performing, more robust, efficient and agile.

Under the guiding principle of "Aareal Next Level", we continue to evolve the strategic positioning we had been implementing for the Bank since spring 2020, to confront the immense challenges facing the entire financial services sector.

Aareal Next Level: geared towards sustainable business performance

Activate! Elevate! Accelerate!

Our goal with "Aareal Next Level" is to advance Aareal Bank Group to the next stage of its development. This remains unchanged, despite the coronavirus pandemic. The essential results of the 360-degree review that was concluded in early 2021 have confirmed that our strategy and our business model remain viable in a normalised environment, once the pandemic has been overcome. Our focus in future, however, will be even more firmly directed than previously at exploring new potential for growth and greater strategic opportunities, whilst maintaining our proven business model. Excluding any potential acquisitions, this should allow us to generate consolidated operating profit in the range of €300 million in 2023, provided the pandemic has been fully overcome by then and the risk situation has returned to normal again.

We see opportunities for profitable growth in all our three business segments. Given that these have different operating frameworks and growth potentials, however, we have also defined different strategic focal points in "Aareal Next Level". The Structured Property Financing segment is guided by the motto "Activate!", the Banking & Digital Solutions segment by "Elevate!" and Aareon by "Accelerate!".

Structured Property Financing

In the Structured Property Financing segment, the controlled, ESG-compliant expansion of the portfolio volume – adopting a flexible approach with regard to countries, asset classes and financing structures – is aimed at making better use of the existing platform. In part, that means systematically using the flexibility developed in recent years in terms of regions, asset classes, structures and exit channels. It also involves expanding our activities along the value creation chain, for example in servicing property financing. We also want to enhance the efficiency of our processes.

Overall, we seek to maintain our significance – which is quite high – as a property financing provider in the most important markets whilst more closely aligning our business with the changing needs of our clients and markets, in line with business cycles and in a flexible manner. In addition, our goal is to realise the potential of digital business models in the Structured Property Financing segment even further.

We are targeting a portfolio volume of around €29 billion by the end of 2021 and of approximately €30 billion by the end of 2022 – with positive effects for net interest income, which is expected to rise noticeably already in the current year. For the post-Covid period, we anticipate enhanced opportunities for high-margin business whilst maintaining our conservative risk standards.

Banking & Digital Solutions

Under the motto "Elevate!", we want to significantly expand the Banking & Digital Solutions segment in the years ahead, which combines our activities for the institutional housing industry and related sectors. We are planning to grow our product portfolio and expand into new markets where there is demand for specific expertise in payment transactions.

Aareal Next Level

ACTIVATE!

Structured Property Financing

- Controlled expansion of the portfolio volume
- Adopting a flexible approach with regard to countries, asset classes and financial structures

ELEVATE!

Banking & Digital Solutions*

- Expanding the product range, in particular in the digital arena, and through further strategic partnerships
- Continue with the deposit-taking business as an attractive additional source of funding

* Formerly known as Consulting/Services Bank: segment has been renamed effective from Jan. 2021

Our goal is a controlled, ESG-compliant expansion of the portfolio.

In the process, we intend in particular to take advantage of our deep understanding of our clients' infrastructures and processes. In addition to the deposit-taking business, we also aim to increase our focus on generating commission income, and to further harness the opportunities that arise there to develop business models together with our clients and other market participants.

A marked increase in net commission income is envisaged between now and 2025. We want to achieve this mainly by expanding the product range,

Progressive urbanisation and digitalisation are triggering numerous growth impulses in the property industry.

ACCELERATE!

Aareon

- Further intensify Aareon's pace of growth, organically as well as through further related acquisitions
- Aareon set to achieve "Rule of 40" performance by 2025

With "Aareal Next Level", we will develop our three business segments in a targeted manner.

We expand our digital product offering, and anticipate further growth.

in particular in the digital arena and through further strategic partnerships. We want to continue with our deposit-taking business as an attractive additional source of funding for the Group, with volumes projected to remain above €11 billion over the medium term.

Along the way, we will increase the recognition of the different products and lines of business. In specific terms, this means that Aareal Bank, as the leading provider of payment transaction services for the housing industry, will be expanding. This will enhance transparency of our products and services.

Strategic partnerships open up new potential, paving the way for new business models.

Aareon

The Aareon business segment is a material growth driver for Aareal Bank Group. Aareon AG is recognised as a pioneer in the digitalisation of the European property industry. Under the "Accelerate!" motto, we intend to once again significantly intensify the pace of growth in this segment in the years ahead, organically growing Aareon's business for this purpose. Targeted M&A activities are expected to generate additional growth. Throughout this process, we intend to not only secure the loyalty of our existing client base with an expanded range of products, but also to reach related client groups and target them with our established product portfolio. In addition, we are planning to develop new products for adjacent client groups.

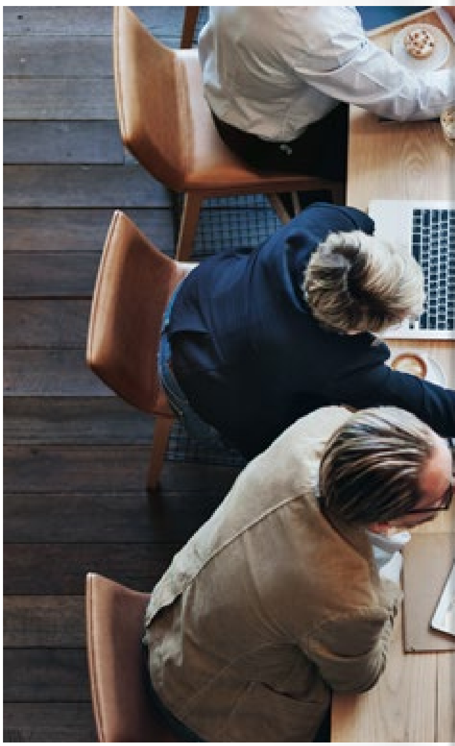
In order to further bolster Aareon's growth prospects and implement its growth programme more quickly, we entered into a long-term partnership in August 2020 with the financial investor Advent. Within the scope of this agreement, we have sold a 30 per cent minority stake in Aareon to Advent International. Joining forces with Aareal Bank, Advent is set to help further strengthen Aareon's market position as a leading provider of ERP systems and digital solutions for the European property industry and its partners, and to accelerate Aareon's value appreciation. The common goal is for Aareon to achieve "Rule of 40" performance by 2025 (meaning that the sum of Aareon's EBITDA margin and revenue growth rate should exceed 40 per cent). Based on the Value Creation Programme jointly developed with Advent – excluding any potential acquisitions – an increase in adjusted EBITDA to around € 135 million by 2025 is targeted.

Additional levers to sustainably raise profitability

Besides the growth initiatives for the three segments, Aareal Bank Group will use additional levers to sustainably raise its profitability, including an optimisation of the funding mix and the capital structure. In addition, numerous measures are being implemented to enhance the efficiency of the organisational structure, processes and infrastructure. As an example, the "IT Next Level" initiative will reduce complexity in the IT infrastructure, expanding cloud-based applications. In addition, the Group plans to streamline management structures across divisions.

All of the measures combined are projected to lead to a cost/income ratio below 40 per cent in the Bank's Structured Property Financing segment by 2023, which is in line with a best-in-class ratio on an international level as well. Aareal Bank has budgeted total expenses of around € 10 million in its banking business for implementing the strategic adjustments in the years 2021 to 2023; these are however offset by one-off income in a similar magnitude. Aareon expects expenses of approximately €8 million in 2021 for implementing its Value Creation Programme.

We want to create competitive advantages for our clients.



Successful together: combining different skills and expertise leads to the best results.

New brand positioning

Our new brand positioning, introduced in 2020, also serves to highlight the objectives we are pursuing with "Aareal Next Level". Our key objective: we want to make our clients more successful, creating a competitive advantage for them. To do so, we are using our extensive expertise and experience, as well as our wide-ranging service portfolio, to offer our clients optimum services that secure long-term competitive advantages for them. We develop integrated offers, tailor-made from scratch to meet our clients' specific demands, and targeting maximum realisation of our clients' potential. This is based on our unique combination of financing services and innovative digital products.

Especially in conurbations, there is a growing need for digital and sustainable solutions.

Transaction highlights 2020

Aareal Bank has once again successfully financed numerous international property projects in various asset classes in the financial year under review. The highlights of 2020 include:

TISHMAN SPEYER

EUR 210,000,000

for the financing of **"Espace Lumière", an office building** in Boulogne-Billancourt, France

Arranger, agent, and lender for **Tishman Speyer and an institutional investor**

scape

GBP 54,000,000

for the financing of **"Scape London Canalside", a student accommodation facility** in London, UK

Arranger and lender for **Scape Living Student Accommodation**

ctp

EUR 403,500,000

for the refinancing of
two logistics and industrial parks
in Bor and near Brno, Czech Republic

Lead arranger, sole lender, facility and security agent for the **property developer CTP**

Logistics properties – dynamic, high-yielding, crisis-resistant

Logistics has become one of the most important global sectors. As a result, such properties are no longer a niche product, but have evolved into an established and very popular asset class, offering institutional investors not only low volatility, a high degree of predictability, and great flexibility, but also a low level of risk.

Take a peek at our **"Logistics properties" white paper** to find out why logistics properties will continue to offer high potential for investors.

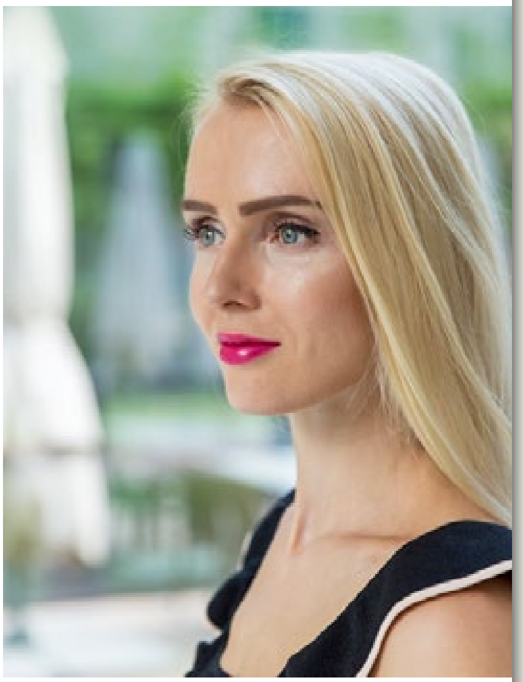
For an overview of additional financing projects, please take a look online:
www.aareal-bank.com/transactions

CHANGE AT AAREAL BANK

Sustainable economic activity

Sustainability, digitalisation, new technologies: the financial sector is undergoing profound changes.

Alice Haupt from our Strategy team helped to establish Aareal Bank's Sustainability Management initiative in 2012. With our ESG@Aareal initiative launched in 2020, we are now firmly and systematically embedding ESG aspects in all our processes.



A sustainable transformation is underway in our society and the economy, at top speed. Companies are working around the clock, and around the globe, to adjust their value chains to meet the requirements of sustainability. Clients and investors, shareholders and employees, social stakeholders and political decision-makers alike expect companies and other organisations to help build a future in which economic, ecological and social issues fit together harmoniously.

Through comprehensive sustainability management, Aareal Bank Group attuned itself to these trends years ago. As a bank and partner to the property industry, we are active in two sectors that are instrumental as the economy transforms – the financial sector, which has a key role to play in promoting sustainable development, and the property industry, which is of tremendous importance to achieving the climate targets set by the EU.

Embedding ESG even deeper

As a major player in the market, we are aware of our special responsibility. It is our ambition to help shape ESG developments in our market, i.e. concerning environmental, social and governance criteria. This is reflected in our business strategy: With Aareal Next Level, we have formulated a sustainable strategy that purposefully takes up and integrates ESG requirements.

But we are not yet where we want to be. Going forward, we want to combine financial and non-financial objectives to an even greater extent for our corporate management, and systematically embed ESG aspects in our mindset and all our processes. Our goal is to continue to receive good rating results and awards for our approach to sustainability, as we have done in the past.

The increasing importance of sustainability is also enhancing the requirements for climate-friendly building operations. This applies to shopping centres, hotels, logistics properties and offices as well as to residential units.

ESG@Aareal

That is why we will continue to pursue a stronger integration of ESG in our business strategy with Aareal Next Level, and why we launched ESG@Aareal in 2020. ESG@Aareal serves to systematically gather the current and future sustainability expectations of our clients and other stakeholders, and match them with our own ambitions. This allows us to identify the changes our strategy, our products, our risk management, our communications, IT and reporting require. Above and beyond this, we have a focus on ESG regulation and what this means for our business models.

One of the most important goals of ESG@Aareal is systematically identifying ESG business potential: we want to seize the many opportunities that the sustainable transformation of society and economy holds for us. This includes developing new products, adjusting existing offerings and providing ESG-oriented financial instruments, e.g. green lending products. ESG@Aareal will not only enable a full integration of ESG requirements into our processes, but also make a significant contribution to Aareal Bank Group's future viability, together with our Aareal Next Level strategy.

As the growing importance of ESG factors triggers numerous and profound changes, ESG@Aareal will have an impact on nearly all of Aareal Bank Group's value creation processes. ESG@Aareal therefore follows a holistic approach, integrating almost every division. This serves to ensure that we will achieve our goal of embedding ESG even further, as an integral part of our strategy and our DNA.

Core action areas

Our sustainability strategy comprises the following core action areas:

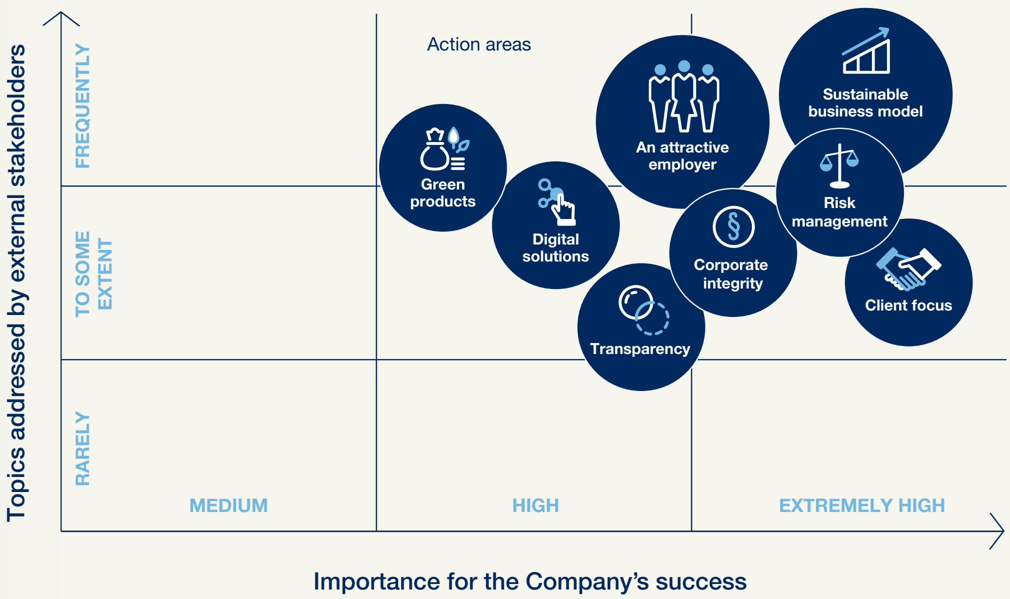
- Sustainable business model,
- Client focus,
- Risk management,
- Corporate integrity,
- Attractive employer,
- Transparency,
- Digital solutions,
- Green products.

These topics are of particular importance to us. To determine, cluster, and prioritise them, we regularly hold structured discussions with both our stakeholders and representatives from different divisions of the Group, which we then use to build our materiality matrix.

The following sections will deal with the topics that hold the greatest relevance for both our stakeholders and us ("extremely high" importance). We aim to show

- the trends we are looking at ("sustainable business model"),
- how we develop pioneering solutions ("client focus"),
- how we ensure ethical conduct ("integrity"),
- how we respond to new risks ("risk management"), and
- how we want to work going forward ("attractive employer").

Our materiality matrix



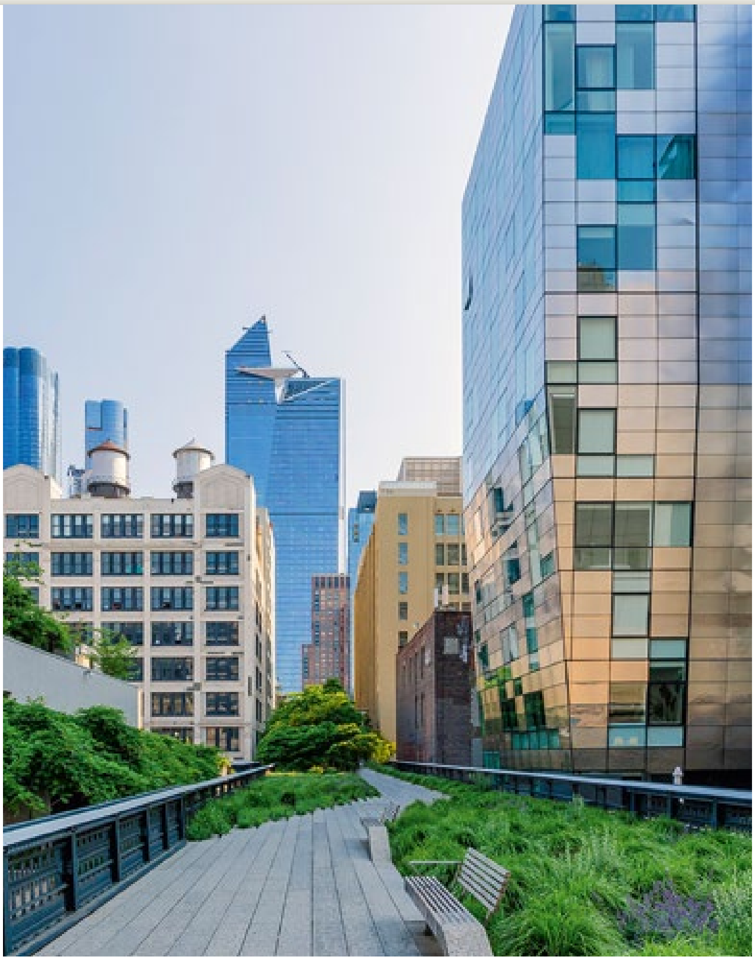
The materiality matrix shows the core action areas of our approach to sustainability.

SUSTAINABLE BUSINESS MODEL

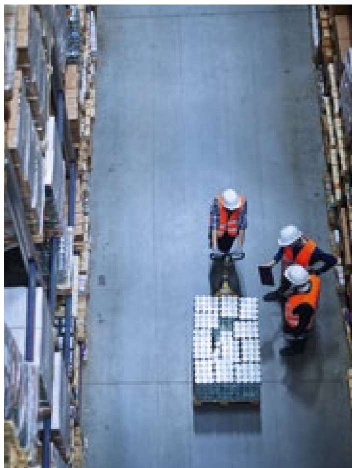
Keeping up with

the trends

The economy and society are undergoing profound change. Aareal Bank is actively helping to shape this transformation process.



Work life and home life are increasingly merging. This calls for new property concepts.



The financial services sector is facing tremendous challenges: new technologies, new ways of working and new market participants, not to mention new regulations that change the financial markets in lasting and profound ways. More than ever before, banks are being called upon to question their business models, and to continuously develop them in light of sustainability considerations.

That is why we are following the changes on our markets – and the trends that go hand-in-hand with them – very closely, and are considering their implications seriously. It is only by anticipating developments at an early stage and by translating them into innovative products and services for our clients that we can attain the market position we are striving for and rise to the challenge we have set for ourselves.

The many issues that we are currently considering include, for example:

- what are the developments on the property markets – particularly in terms of ESG – and how can we benefit from them,
- how can we take greater advantage of data by using artificial intelligence and in so doing add value for our clients, and
- what opportunities does the platform economy hold and what products and services can we use to cater for this trend.

During recent decades, the logistics sector has evolved from a set of pure transport and storage processes into a global network of production and distribution centres.

Property trends

The Covid-19 pandemic has influenced the property markets considerably over the past financial year and created a great deal of uncertainty. It can be assumed that this uncertainty will persist for some time to come. However, we are confident that the property markets will normalise again as soon as the economy returns to its usual rate of growth. Ultimately, the demand for property remains intact.

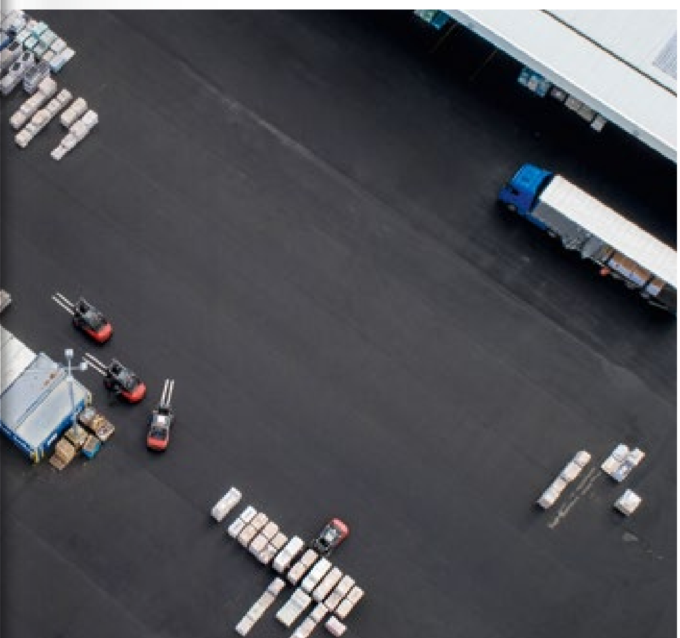
Individual asset classes will perform differently in the years ahead, however. Yet these differences are not so much a result of the pandemic than an expression of trends that emerged some time ago and merely gained momentum as a result of the Covid-19 crisis.

Logistics is a growth market with great potential. As such, the logistics sector will continue to play a decisive role in shaping the economy in the future. That means rising demand for logistics properties – especially those that are centrally located with good infrastructure. The rising demand is also being met with a limited supply of space, creating attractive growth prospects for investors.

Even though **hotel properties** were hit hardest by the coronavirus pandemic, in terms of occupancy, they remain amongst the most sought-after investment asset classes. We do not believe that this is a structural crisis. In the future, we will once again travel and take advantage of the services of hotels. That is why hotels are amongst the properties that will recover the fastest once the economy normalises.

"Our strategy in the Structured Property Financing segment is in touch with these trends on the property markets. We will continue to implement our financing policy – which was conservative to begin with – and focus predominantly on first-class assets and professional clients, and a broadly diversified and sustainable portfolio in our financing projects."

Severin Schöttmer
Managing Director Special Property Finance, Aareal Bank



A video clip in our Online Annual Report showcases what makes us special when it comes to financing logistics properties.

An information chart in the Online Annual Report outlines key drivers for the logistics sector.

**Expert dialogue:
Prof Dr Kerstin Hennig (EBS) and Severin Schöttmer (Aareal Bank) discuss trends on the property markets.**

Prime properties in very good locations continue to offer opportunities.

In the **retail** asset class, the Covid-19 pandemic has acted as a catalyst, accelerating changes that had been emerging for quite some time, particularly due to e-commerce. Once the coronavirus pandemic has been overcome, consumers will once again focus on professionally managed, prime brick-and-mortar retail properties offering an experience in top locations. Hence, this segment will continue to hold opportunities.

Office buildings have experienced many changes. The lines between "life", "home" and "work" are being increasingly blurred, creating new challenges for office buildings. Properties with future-proof designs in attractive locations continue to offer strong potential in this asset class.

Artificial intelligence

Artificial intelligence (AI), along with blockchain technologies, is one of the key future technologies within the financial services industry. In combination with structured data analysis, it presents banks with numerous different possibilities to unlock new revenue streams and provide even better quality services at a lower cost.

We see a variety of different application areas for AI: it can help to increase efficiency, improve risk management, support lending decisions, identify new findings about sectors and markets and enhance how our products and services perform. That is why we are already employing certain smart tools that use AI technology, especially with regard to clustering and structuring large amounts of data.

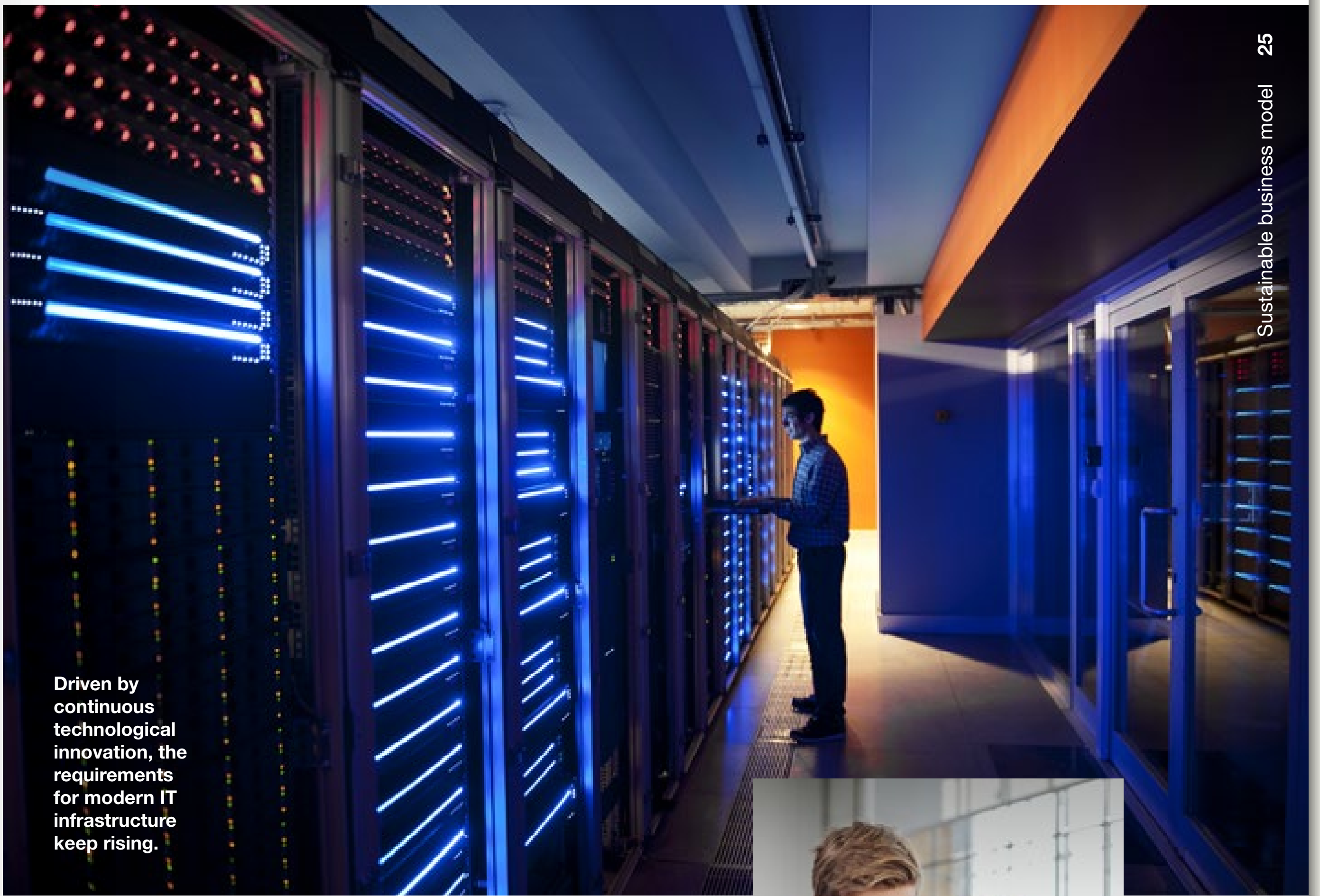
To take advantage of the vast array of opportunities, we have been working with a range of AI experts for several years, including our partnership with Rocketloop, a start-up specialising in individual machine learning and AI. As part of our collaboration, we developed an innovative news crawler in 2020 that scans available property markets information on the web and provides it, bundled with different analysis tools, to our Credit Risk department. We are currently using this AI tool to help support our retail property financing activities in the UK.

"There's hardly any issue that will have a bigger impact on both FinTech companies and the established financial sector over the next several years as data. To be able to develop application areas and ultimately business models based on that, we need to stop siloed thinking and act in a coordinated fashion as a whole company. That is the foundation for AI's success."

Dr Sebastian Schäfer
Managing Director, TechQuartier and Co-Initiator of the Financial Big Data Cluster

"For us, Neela's added value is not a purely cost-related consideration. We want to use her to boost our brand – to provide a better, wider-ranging service for tenants and offer a customer touch point far superior to the norm."

Pernilla Fröden
IT Business Developer, Stena Fastigheter



Driven by continuous technological innovation, the requirements for modern IT infrastructure keep rising.

At present we are prioritising other potential applications for AI and are adapting our existing data architecture. At the same time, we are constantly developing our IT infrastructure through targeted sub-projects so that it not only provides the appropriate performance level and flexibility for AI solutions to be widely used, but also so that it can live up to the needs of a modern banking IT landscape overall. It is just as important, however, that our employees have the right mindset and the necessary qualifications. That is why we will be tailoring staff development and collaborations with technology partners in this area in the years to come.

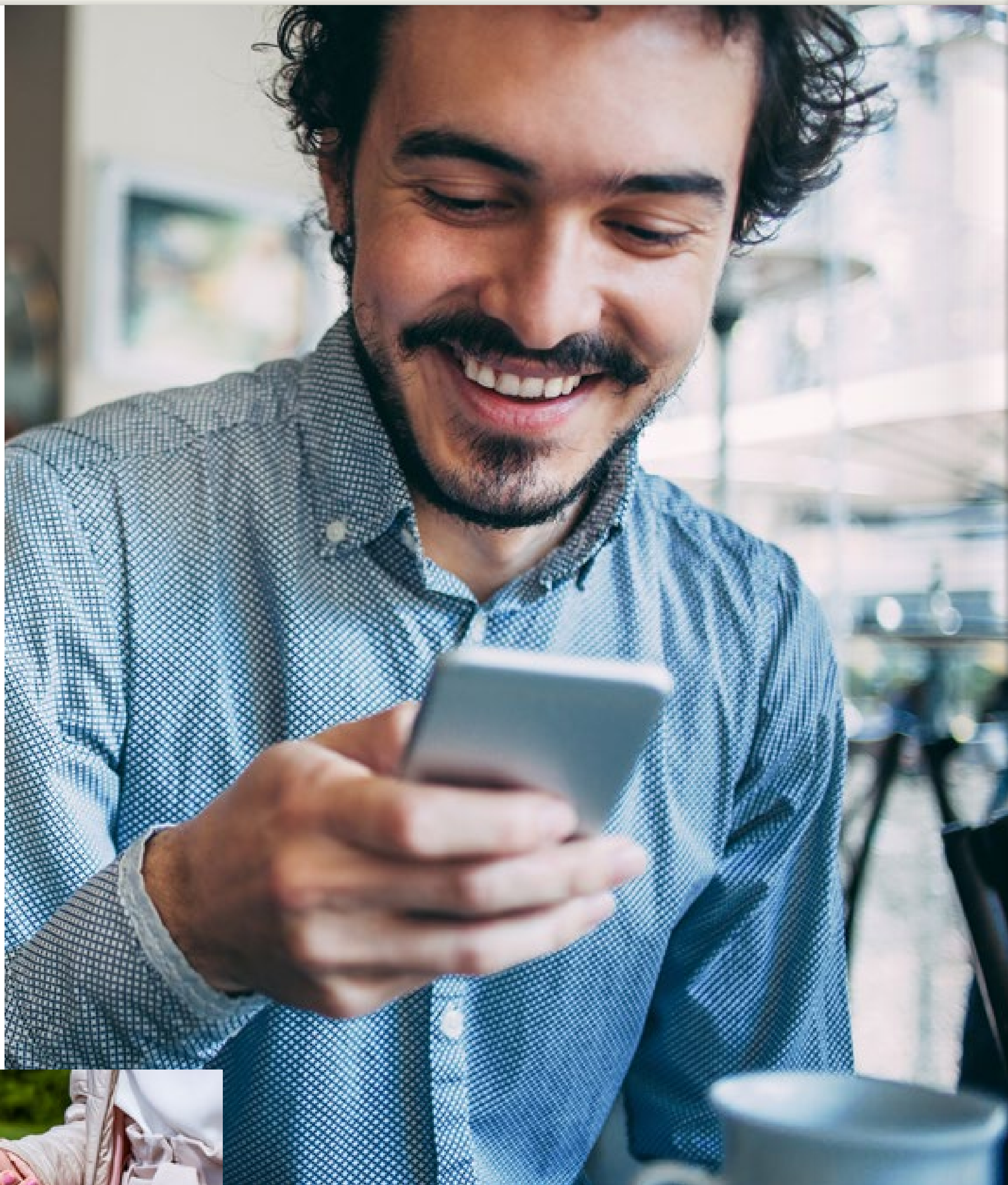
In 2020, Aareon's AI-based virtual assistant Neela was introduced to the market. As part of the initial launch phase, Neela was introduced as a chatbot. The functionality enables property companies in particular to automatically answer their clients' frequently asked questions. The benefits: clients can get answers quickly and conveniently, employees are freed up by not having to answer frequently asked questions and therefore have more time for complex issues.

In

2020

Aareon's AI-based virtual assistant Neela was introduced to the market.

A brief audio clip in our Online Annual Report summarises our cooperation with e-mobility platform provider smartlab (in German only).



As e-mobility gains in importance, the focus is increasingly on efficient settlement of payments to different charging point providers – with the goal of offering maximum convenience to end-customers.

"We entered into a pioneering partnership with Aareal Bank that we can thank for making client processes considerably more efficient. Customers are left with minimum effort and costs, and we are able to focus on our core expertise, i.e. developing services surrounding e-mobility for municipal utilities and business partners."

Dr Mark Steffen Walcher
Managing Director, smartlab

Platform economy

Over the past several years, platform companies have been amongst the fastest growing enterprises. Their business model is based primarily on making selling, buying or creating products and services simpler and bringing together market participants on a platform. These platforms, which become more attractive the more offerings and users they unite, are becoming more successful in the financial services sector as well as the property and housing industry.

Aareon is a pioneer in the provision of B2B platforms for the property sector. Roughly 20 years ago, Mareon was launched as a way to connect property companies and tradespeople and Mieter Portal has been on the market for over five years. Aareon Smart Platform was introduced in 2019: as an open platform, this allows clients and partners to develop solutions and transfer them into Aareon Smart World.

Aareal Exchange & Payment Platform is Aareal Bank Group's trailblazing platform solution. The focus of this B2B platform solution is optimising processes between housing companies and different payment services. With its help, payments in the property and housing industry can be transacted on one common platform using internet-based payment methods Barzahlen / viacash, PayPal or credit cards in addition to traditional options like cash, bank transfers or direct debit. The central integration of different payment services into the underlying ERP processes efficiently allows to pay for various housing services using alternative payment methods, which means housing companies can expand the range of services they offer to their tenants. Surveys very clearly indicate growing demand and expectation for these payment services in the property and housing sectors.

In addition, with Aareal Connected Payments, we partnered with the platform provider smartlab to develop an automated invoicing procedure which is initially being used in the e-mobility arena. The procedure makes it easier to manage the invoices for complex payment flows between different partners, so-called multi-party payments, on a shared platform. Aareal Connected Payments is used on the ladenetz.de platform. It enables electric car owners to charge their vehicles with a single charging card across Germany and makes it possible for the more than 220 connected municipal utilities to automatically and simply settle accounts amongst themselves.

Discover our info chart on the future of payments in our Online Annual Report (in German only).

"Customers want to have a range of simple and secure payment methods when it comes to paying their rent too. Integrating PayPal into the Aareal Exchange & Payment Platform enables companies to connect with more than 370 million PayPal clients worldwide and offer their clients the option of paying the way they want to."

Christina Moritz
Director Sales, Paypal Germany, Austria and Switzerland

"Sometimes, it is necessary to be able to integrate new solutions quickly. That's precisely what the Aareon Smart Platform makes possible. It enables us to add value for our customers and their partners; and we derive benefit too from using the service ourselves and being able to enhance the loyalty of our customers."

Hervé Cliquet
Manager Digital Platform & Innovation Lab, Aareon France

Cooperation as a

driver of success

CLIENT FOCUS

No success without cooperation – whether in the form of dialogue rooted in partnership, co-creation, intensive communication with start-ups, or in many other ways.

"Within a few weeks, after a host of different Covid-19-related global restrictions were introduced in mid-March, we had worked with our clients to formulate short-term strategies for dealing with the exceptional situation. By engaging in a regular and frequent dialogue with our clients, we can adjust these strategies together to adapt to constantly changing conditions. This measure helped considerably to stabilise the situation – and at the same time fostered a long-term relationship based on trust between Aareal Bank and its clients."

Bettina Graef-Parker
Managing Director Special Property Finance, Aareal Bank

Never before have industries undergone such a rapid transformation process as today. Within just a few decades, entire sectors have changed radically and profoundly. In this process, not only have new business models and providers emerged, but the needs and expectations of clients have also changed at a swift pace.

We believe that in an increasingly digitalised world that is constantly presenting new opportunities and perspectives, it is no longer enough for a company to merely anticipate needs and expectations to remain viable. Rather, it is necessary to place clients' success at the centre of the Company's business activities, and enhance clients' competitive edge for the long term. To underscore this challenge, we evolved our brand in 2020 and defined a new brand claim: "Aareal – Your Competitive Advantage."

We are now closely looking at:
- how we can expand individual dialogue with our clients, and bring our partnership-based approach more fully to bear,
- when and how we can get creative in collaboration with our clients and what the success factors are in this respect, and
- how we get inspired to develop new products and services while simultaneously securing new markets.

A dialogue rooted in partnership

We see it as our calling to be a partner to our clients. We leverage our comprehensive expertise and experience, and our broad range of services, with the objective of offering our clients the best possible services for their long-term competitive edge. We do not see ourselves merely as a provider of products and services, but rather as a company whose pioneering solutions mean we serve as an advisor, guide and facilitator for our clients.

That is why we believe it is so important to understand market connections, think in a cross-sector way and put ourselves in our client's position to understand the challenges they are facing. As such, we maintain in-house expert teams for logistics, shopping centre and hotel financings in our Structured Property Financing segment. These expert teams provide us with valuable market insights that we can take advantage of to add value for our clients.

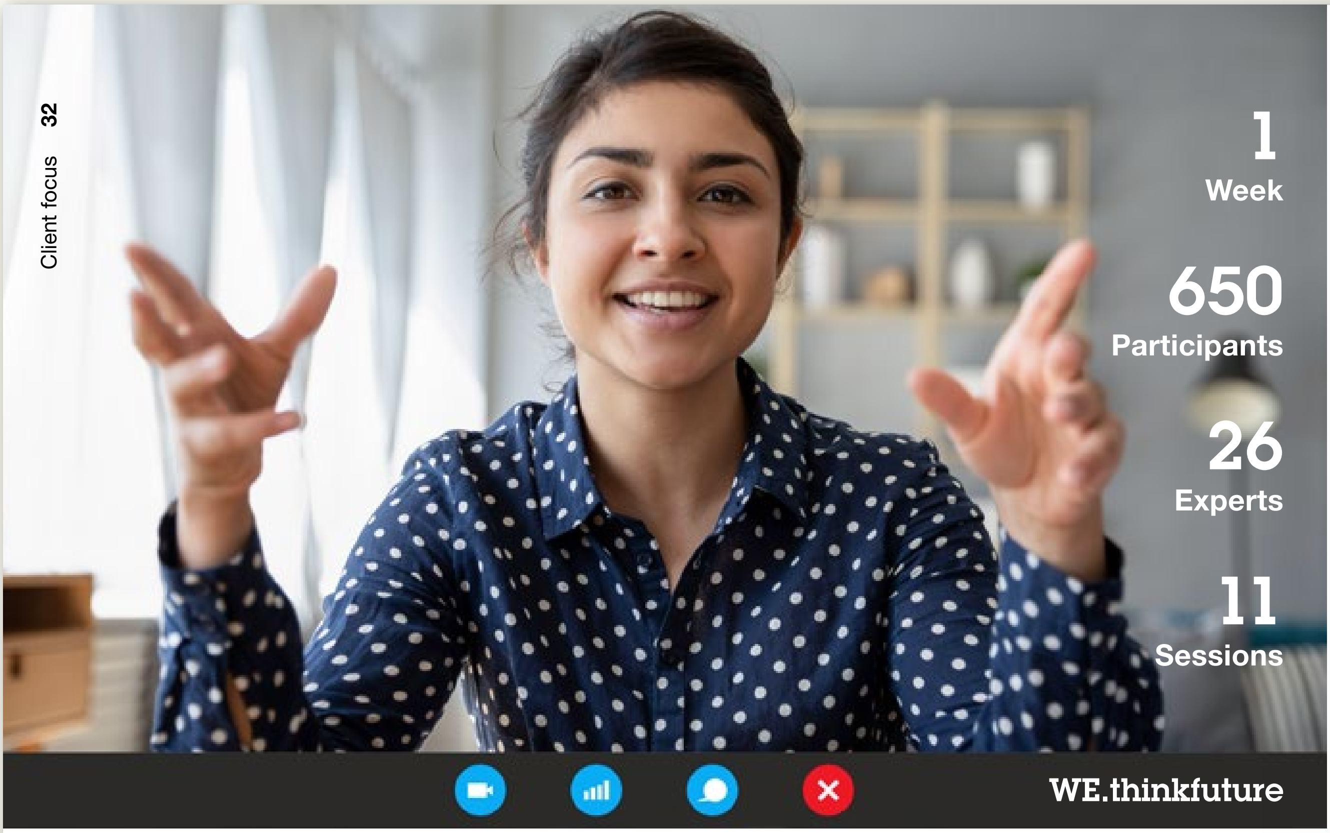
"Naturally, we want to stand by our clients' sides, particularly during challenging times," says Steffen Bruns, Managing Director Business Development & Strategy at Aareal Bank. "Because that's when one needs powerful partners the most. That is why, for example, we approached our clients in the Structured Property Financing segment shortly after the outbreak of the Covid-19 crisis to discuss their particular situations and, where necessary, show them what options they had."

Management Board member Christof Winkelmann describes how clients benefit from our special sector expertise in a video interview, to be found in our Online Annual Report.

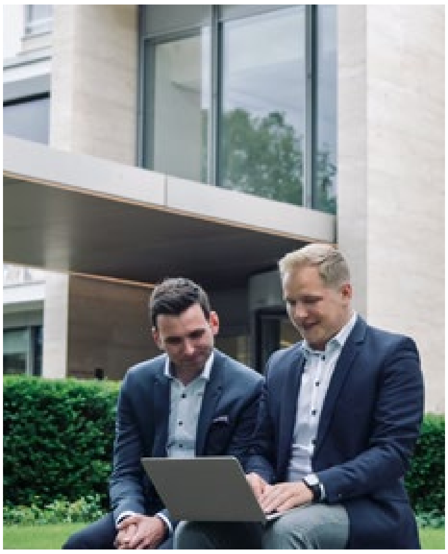
"Despite all the turmoil that 2020 brought there were some successes. Probably our company's biggest achievement was the € 380 million portfolio financing with Aareal Bank. We don't believe it would have been possible without the shared trust and sense of partnership that our respective organisations have built over the years. Thank you to the entire Aareal Team!"

Dominic Seyrling
Director – Investments,
Archer Hotel Capital

Our teams of experts provide advice for all our financing projects – on an equal footing and in a spirit of partnership.



We have made a short film that summarises the key findings of our WE.thinkfuture 2020 digital conference, which can be found in our Online Annual Report.


Stefan Rohmann from our Human Resources department and IT application specialist Phil Rüdiger agree: nothing is more constructive than direct dialogue.

It is also important to us to spark ideas and contribute to a deeper exchange between players. That applies especially to clients from the housing and energy sectors that we provide services to in the Banking & Digital Solutions segment, and at Aareon. Which is why we launched the WE.thinkfuture initiative in 2020. Its aim is to establish a cross-sector dialogue that connects the housing and energy industries, fosters innovation and exchanges with start-ups, identifies change processes at an early stage and actively influences the future. One of the central facets of this work is the client as a driver of innovation.

The feedback that we received from this initiative has been very positive. Over the course of a week, more than 650 participants and 26 experts considered future challenges and current trends in 11 sessions: from the prevailing tension between the drive to innovate and cost pressure, to success factors such as networking and the willingness to cooperate, to the significance of an infrastructure approach that starts small but is aimed at comprehensive framework solutions that propel the development of e-mobility or smart districts. We set a discussion about the future in motion that we will continue and develop in the years to come.

Co-creation

Clients know best what they want. And increasingly, they demand products and services that meet their individual expectations. That is why it simply makes sense to involve clients in the product development process early on, and to systematically take into account their needs and expectations during the design phase of a solution.

We rely on the co-creation approach when developing new products and services, particularly in our Banking & Digital Solutions and Aareon segments, and increasingly so. This entails, for example, using agile, iterative and client-centred methods, such as design thinking.

A good example is Aareon's development of Wodis Yuneo. Wodis Yuneo is the new product generation of the Wodis Sigma ERP system which enables the use of new technologies such as business intelligence, artificial intelligence, big data and robotics. This makes it possible to automate a lot of routine tasks, give users tips and recommendations and make use of intelligent tools and analytics components.

By involving users in many of the product development stages, an ERP system was developed that accommodates a diverse range of different needs. Users can personalise their cockpits and individually tailor how they navigate the system, for example by using a mouse, keyboard, touchscreen or voice commands. Wodis Yuneo also answers users' demands for greater flexibility. Users will be ale to access all the data at any time, whether at the office, when working from home or using mobile devices; the ERP system can be run as a Software-as-a-Service (SaaS) solution, or as an inhouse solution. Thanks to the way it seamlessly communicates with BK01, the leading process for payment transactions for the housing sector, users can use Wodis Yuneo to automate their mass payments.

For more information on Wodis Yuneo, please refer to the video in our Online Annual Report (in German only).

"Wodis Yuneo will inspire many employees to embrace innovation. This is precisely the sort of momentum required for the implementation of what can be complex digitalisation processes in the company."

Ulf Momsen
Authorised Officer (Prokurist), Flensburger Arbeiter-Bauverein

"With Aareon Wodis Yuneo, we have expanded the ERP system to efficiently meet the challenges of the industry with modern technology. It is a dynamic product that we will continue to develop in collaboration with our clients. That will ensure that it is future-proof and a safe investment for property companies for the long term."

Dr André Rasquin
Chief Operations Officer, Aareon

Young companies are often creative, agile, and very open to technological innovation, which is why we are also targeting collaborations with start-ups.

We followed a similar co-creation approach when developing Aareal Meter. Aareal Meter will help companies from the energy and housing industries as well as municipalities and other involved service providers to digitalise meter readings, thus boosting efficiency in what used to be a time-consuming and error-prone exercise to date. This solution emerged as a result of a strategic collaboration between Aareal Bank Group and pixolus, a start-up specialised in mobile data collection, and from systematically incorporating client requests in every major phase of product development. This constellation and the use of one of pixolus's existing products as a starting point meant that a shared idea became a market-ready product within twelve months, and it is already being used by the first customers.

Cooperations with start-ups

In the search for new ideas and innovative approaches, we are also looking to give a leg up to younger companies. They often have the courage and creativity to radically challenge established business models and to test the potential of the latest technologies. In addition, start-up companies generally exhibit a highly agile corporate culture that enables comparatively fast product development timelines.

With our start-up programme, we are targeting different types of collaborations with FinTechs, PropTechs and other start-ups. We are supporting accelerator programmes, entering into cooperations with start-ups and investing in young promising companies, and the Aareon subsidiary Ampolon Ventures is founding its own start-ups.

The goal of these activities is to better understand what drives digital development and how trends can be translated into pioneering solutions. We want to further enhance our innovative force and offer our clients the greatest added value. It is also important to us that we challenge ourselves, and question how future-proof our culture and our processes are.

In our collaborations with PropTechs and FinTechs, which increasingly are turning into important industry experts, it is vital to be intellectually invested. We deliver sector know-how, provide infrastructure and contribute our contacts to the partnership. This is due to our conviction that sometimes the decisive innovative spark is just a collaboration away.

We have high expectations for our most recent investment in objego; objego specialises in the development and operation of a web-based digital platform for managing property portfolios for private landlords of up to 250 units. With the joint venture in objego and the associated partnership with the energy service provider ista, we are not only driving the expansion of our software solution-based product offering, but also expanding into new markets such as the B2C business for private landlords. Our investment in objego is an expression of our strategy to steadily grow our product and service offering in the Banking & Digital Solutions segment, to close attractive market gaps and increase commission income.

Expert dialogue:
Philip Rodowski (objego) and Henning Zander (Aareal Bank) discuss the success factors for a start-up collaboration.

"Innovation is not something new but it is getting more complex every day. Collaboration needs, more than ever, to be intrinsic within a corporation's strategy and cultural mindset. Banks shouldn't be trying to conquer the market by themselves, instead, finding the right partner for it is essential either with a start-up, scale-up, SME, or another corporation."

Fernando Zornig
Director, Plug and Play

"As a young and innovative company in the property segment, our goal is to develop ventures with trailblazing solutions. With Ophigo, foxxbee and Ecaria, we are involved in three ventures with future potential."

Arash Houshmand
Managing Director, Ampolon Ventures

INTEGRITY

Responsibility is not a buzzw

Ethics and yield are closely linked. Long-term success is only open to those treating humans and nature with respect.

Frederick Schönig
Managing Director, Transaction
Legal & Operations, Aareal Bank

Running a business means assuming responsibility, for society, the environment, employees, and owners. Today, in a world that is increasingly interconnected, this is truer than ever. That is why the requirements for an effective integrity and risk culture and corresponding incentive and sanctions mechanisms have significantly increased in recent years.

For many years, our Code of Conduct has been the foundation of our business practices. The Code of Conduct sets out binding rules for legal and ethical conduct, and defines our fundamental understanding of how we work together, corporate and social responsibility, as well as fair employment and working conditions. At the same time, the Code of Conduct serves as the basis for many other policies and measures at our Company to help ensure that we conduct ourselves in a way that is ethically and morally right. This includes safeguarding fair working conditions and respecting human rights.

Our Code of Conduct is the foundation of our business practices.

A confidential (and anonymous) whistle-blowing channel also exists that can be used to report suspected breaches of the rules, fraudulent behaviour, or white-collar crime to the Compliance department. This guarantees whistle-blowers confidentiality and protection. In addition, an externally run whistle-blower system was established as a separate process for Aareal Bank in 2020. Employees can use this voluntary, confidential reporting system to raise concerns online or by phone – including anonymously, if desired.

To continue to meet the ever increasing requirements for upright conduct and integrity, we are currently working on:

- further strengthening our risk culture,
- connecting our ESG targets more strongly with our remuneration systems, and
- implementing our diversity values in our workforce by taking appropriate measures.

Risk culture

Banks live on trust. To retain this trust and prevent illegal or illegitimate business practices in the financial sector, regulators have made risk culture and reputational risk a top priority for all financial institutions. A company's risk culture is defined by four factors in particular: leadership culture, employee accountability, open communication/critical dialogue and appropriate incentives.

We are currently refining our approaches to all four of these factors. Over the past two years, we have revised and further fleshed out all of the relevant processes and underlying guidelines, for example by reviewing our Code of Conduct and preparing Human Rights Guidelines. Furthermore, risk culture has been added to the Group strategy as a key element and made an objective for all members of the Management Board.

"In 2020, Aareal Bank ranked first among MDAX companies in the DVFA Scorecard for Corporate Governance and came in third in the overall ranking. In our communications with shareholders, we rely on transparency and plausibility. This recognition motivates us to continue with our efforts for good corporate governance."

Holger Lehnen
Remuneration Officer, Corporate Lawyer
Corporate Affairs, Aareal Bank

Risk culture

Management culture (tone from the top)

- Management Board and senior management as role models
- Clear communication of Company values

Accountability of employees

- Code of Conduct in accordance with section AT 5, no. 3 of the MaRisk
- All members of staff are responsible for implementing the risk culture within the scope of their duties

Effective communication and challenge

- Open dialogue, across all levels of hierarchy
- Ongoing development of an error culture
- Bi-directional communications – 'top-down' and 'bottom-up'

Appropriate incentives

- Encourage employees' orientation on the risk culture
- Create appropriate material and non-material incentives

An adequate risk culture provides a key foundation for executives and employees to deal with company-specific risks in an appropriate manner.

Sevan Ghazarian
Solution Architect, Banking Transformation – Business Analytics & Projects, Aareal Bank

Julia Issel
Lead Consultant, Banking Transformation – Business Analytics & Projects, Aareal Bank

Carolin Kuhaupt
SAP-Consultant, Banking Operations – Business Applications, Aareal Bank

Zaman Kakhki
Business Consultant, Banking Transformation – Business Analytics & Projects, Aareal Bank

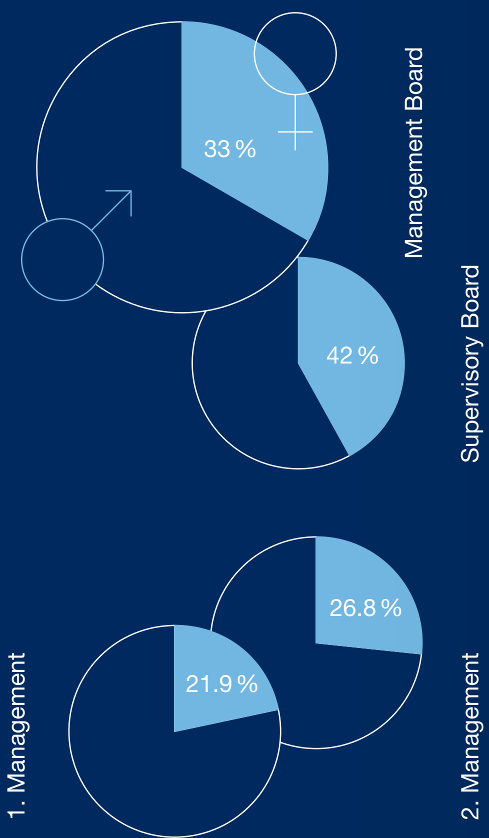
We rely on people who want to get involved, and who contribute a variety of skills and experience.

We are also looking closely into the question of how we can further improve the way we review, measure and then tailor how we strengthen our risk culture. At the same time, we are working on using different event formats to raise awareness amongst our executives and employees about the heightened requirements surrounding our risk culture and to align questions of integrity with our process of cultural change.

Setting ESG targets

Studies and experience have demonstrated time and again: people are particularly motivated to pursue targets, and to do so systematically, if these targets are linked to a variable remuneration component. Target-based variable remuneration not only provides those responsible with a clear orientation framework and incentives, it also has powerful management and steering implications. Furthermore, this type of target setting shows the importance that is attributed to certain targets in a company.

Because the significance of ESG targets is increasing in our industry, we have decided to take a first step towards systematically anchoring ESG criteria in our Management Board remuneration. To this end, our Management Board remuneration system was refined in 2020 and will be presented to our shareholders for adoption at the next Annual General Meeting.



Going forward, our Annual Report will include the specific ESG targets influencing our Management Board remuneration, together with other parameters. The targets we choose are clearly defined and measurable. To measure and monitor target achievement, KPIs are determined annually for the targets, and their degree of achievement is assessed at the end of the financial year.

As part of our ESG@Aareal initiative, we are currently developing a system of ESG indicators that build upon each other for our Group, analysing our stakeholders' expectations, and the regulatory changes that are becoming apparent with regard to our sustainability performance. The formulated KPIs serve as the foundation for effectively and comprehensively embedding ESG targets in our executives' variable remuneration.

Diversity

The Boston Consulting Group has spoken: Aareal Bank Group is a diverse company. For years, we have been at the top end of the consultancy's Gender Diversity Index, ranking first in 2019 and second in 2020.

The main reason behind our strong performance is our high share of women at the executive level: on our Management Board, one in three members is female and on our Supervisory Board 42 per cent are women. On the first management level below the Management Board, 21.9 per cent of managers are women. On the second management level, this share rises to 26.8 per cent.

"The refined remuneration system for the Management Board of Aareal Bank acts as an incentive for aligning the Group's development more closely with long-term sustainable criteria. A major change in the remuneration system is that sustainability criteria are better integrated with compensation to reflect the growing importance of ESG issues."

Marija Korsch
Chairman of the Supervisory Board, Aareal Bank

"I highly appreciate the many options Aareal Bank has offered me to help coordinate work and family, including flexible working hours and part-time arrangements, various work-from-home models, support with day care, or a parent-child office."

Annette Korioth
Director Finance & Controlling – Financial Instruments, Aareal Bank

Constructive cooperation and a strong team spirit are what drives successful teams. This is the only way to achieve top performance – regardless of whether you're working at a desk or in our staff restaurant.

"What could be more sustainable in HR than hiring and promoting young talent? In 2020, almost half of all hires at Aareal Bank were young talents. I am one of them and I think it's great that I am being supported in my development and that Aareal Bank is recognising the value of investing in young talent."

Stefanie Schweitzer
Assistant Manager Group Human Resources & Infrastructure – Center of Expertise, Aareal Bank

There is a positive correlation between diversity and innovation.

For us, however, diversity does not end with gender. We believe it is important to tackle the wide-ranging challenges we have to meet with wide-ranging experiences and perspectives. We are active internationally – we need international teams. We aim to offer comprehensive consultancy – we need employees from different age groups. We offer a broad range of services – we need employees who bring different professional, personal and cultural backgrounds to the table.

Studies have shown time and again There is a positive correlation between diversity and innovation. In particular where the tasks at hand are complex, such as sustainable or digital transformation, heterogeneous teams are more successful than their homogeneous counterparts because they come up with more and better solutions. And for truly fresh ideas to come into being, people with different ways of life and experiences need to join forces to develop solutions.

Against this background, we are committed not only to paying attention to diversity when recruiting and developing talent, but to setting up our operational processes in such a way that we succeed in including different personalities. Our managers play an important role in this – it is their job to transform people with different experiences and profiles into a powerful team. Going forward, we will pay even closer attention to how successful our managers are at doing so. At the same time, we are offering numerous measures for flexible working arrangements to facilitate reconciling work and family needs, supporting our employees whatever their life situation is. We consider diversity management a core discipline of future-oriented human resources management, and as a key success factor in further expanding our market position.

"The capital markets have responded very well to our diversity efforts at Aareal Bank Group. In 2020, we joined the Bloomberg Gender Equality Index. This index is limited to only 325 companies from around the world that exceed a globally established threshold defined by Bloomberg to measure gender equality in five areas: female leadership and talent pipeline, equal pay and gender pay parity, inclusive culture, sexual harassment policies and pro-women brand."

Jürgen Junginger
Managing Director Investor Relations, Aareal Bank

RISK MANAGEMENT

Con trolled

Seizing opportunities – without losing sight of the risks. The more complex the world becomes, the more efficient risk management must be.

The ability to correctly identify, assess and manage risk is one of the most important foundations of our business model. For many years, we have pursued a conservative risk policy, ensuring a clear, sustainable risk culture. Over the past two years, we successfully implemented an accelerated de-risking programme, which we will continue, on a selective basis, in 2021, in order to further enhance the Bank's stability – not least due to the impact of the Covid-19 pandemic.

offensive

Risk management requirements have increased considerably for banks over the last several years. A number of different market and technology trends have contributed to this, as well as a variety of laws, regulations and administrative rules. The challenge in all of this is not only that the number of possible risks has increased, but also the interdependencies, the volatility of the risk situation and the usability of available data and information.

That is why our risk management is constantly evolving and we are increasingly using automated processes for identifying and evaluating risks to efficiently collect data and allow analysts more time to assess risks. Alongside implementing current and upcoming regulatory requirements, right now we are especially concerned with how we can expand our risk management to include factors that are relevant in the context of ESG.

Integration of ESG risks
The growing importance of ESG topics for the financial services sector holds manifold opportunities, yet also involves risks. Banks therefore need to analyse ESG risks holistically and integrate them into their risk management framework. By this we mean things like the drivers of regulatory risk that create and/or increase established risks in our business.

As part of our ESG@Aareal project we are currently building a high-performance ESG risk management system. The aim of these activities is to systematically integrate ESG considerations into our risk strategy and risk processes, methods and instruments, and to develop an ESG risk management framework. To do this, we analysed the status quo over the past financial year, defined ambition levels and derived measures to be taken from these.

We are currently working to develop a risk governance policy defining the relevant responsibilities, as well as transitioning to the implementation phase, and documenting the results in an ESG manual.

We determined the relevant ESG risk factors for Aareal Bank Group back in 2019, in a Group-wide initiative that used a combination of a bottom-up and a top-down approach. After that, we compared the results of these two perspectives so as ensure that we have identified all ESG risk factors impacting our existing risk types as comprehensively as possible.

We consider the relevant ESG risk categories to be (physical) climate risks, changes in stakeholder requirements, competitive and market pressure, business ethics and compliance, and uncertainty regarding ESG regulations relating to Aareal Bank Group. They affect our credit risks in particular, but also our strategic and operational risks.

Expert dialogue:
Matthias Arnheiter (Head of Corporate Strategy at Berlin Hyp) and Christoph Reitze (Aareal Bank) discuss the challenges and solutions of integrating ESG into business strategy and risk management.

"To analyse climate and environmental risks, we rely primarily on scenario analyses and stress tests. As part of ESG@Aareal, we are currently developing a stress scenario that takes into account the relevant physical and transitory climate risks for Aareal's portfolio."

Ronny Hahn
Managing Director Risk Controlling, Aareal Bank

"Comprehensively dealing with ESG risk leads to new perspectives on known risks and the complex context of their causes and effects. Effectively managing ESG risks therefore requires a holistic approach across every area of the bank."

Prof Dr Thomas Kaiser
House of Finance, Goethe-Universität Frankfurt

Threats often lurk where you cannot directly see them. This is why forward-looking and effective risk management is indispensable, especially for banks.


Dr Kirsten Appel, General Counsel, Corporate Affairs – Legal, Aareal Bank
Dominik Brieler, Managing Director, plusForta
Michele Cicland, Assistant Manager Group Technology, Aareal Bank
Manfred Over, Director Real Estate Investment Consulting, Aareal Bank
Senay Azak-Matt, Director Second Line of Defence, Aareal Bank
Carolin Kuhaupt, SAP-Consultant, Banking Operations – Business Applications, Aareal Bank
Patrick Samaan, Senior Manager Sales Management, Aareal Bank
Dr Julia Körner, Company Lawyer, Corporate Affairs-Legal, Aareal Bank

AN ATTRACTIVE EMPLOYER

Living differently, working differently

Re-defining work. Aareal Bank not only addresses innovative working models and continuous learning – but also the issue of carbon emissions.

Working environments are changing fast, with new technologies opening up opportunities for collaboration and offering fresh perspectives to employers and employees. An open opportunity is a call to action, it needs to be seized – and seizing it requires the courage to embrace change, a mind open to new ways of working, and the willingness to keep learning.

Aareal Bank Group has taken its first steps into the workplace 4.0. Over the past years, we have adjusted our structures and processes, and aligned our working conditions with new working environments. At the same time, we have expanded our relevant training programmes and launched a process of continuous transformation.

We want to make even greater use of the potential that tomorrow's working environments hold. That is why we currently have a particular focus on the following themes:

- What opportunities do fresh, innovative forms of work offer us, and how do we want to make use of them?
- What are the environmental and social benefits to digital work?
- How can we meet the rising demand in continuing professional development, and which measures do we want to adopt for this?

An open opportunity is a call to action; it needs to be seized.

Modern forms of work

The way we work has developed rapidly over the past years and gained further momentum with the COVID-19 pandemic. This change has been driven to a significant extent by digitalisation: automated business processes, additional networking opportunities and new requirements for our staff – as well as their new expectations – are key results of the shifting work culture, adding to new working models such as agile working or work-life blending, the integration of work and life.

We are looking deep into the forms of work of tomorrow to be able to adapt and use them as quickly as possible, both in collaboration with our clients and within our own organisation. Against this background, our working environments keep evolving. This includes using new communication channels, expanding the digital

"I am convinced that hybrid working models will shape the workplace in the long term. We support our financial sector clients in the technological and cultural change that this requires to their organisation. In this effort, collaborative cloud-based solutions such as Microsoft Teams are key. They allow institutions such as Aareal Bank to react to changing requirements swiftly and flexibly."

Christine Haupt
Chief Operating Officer,
Microsoft Germany

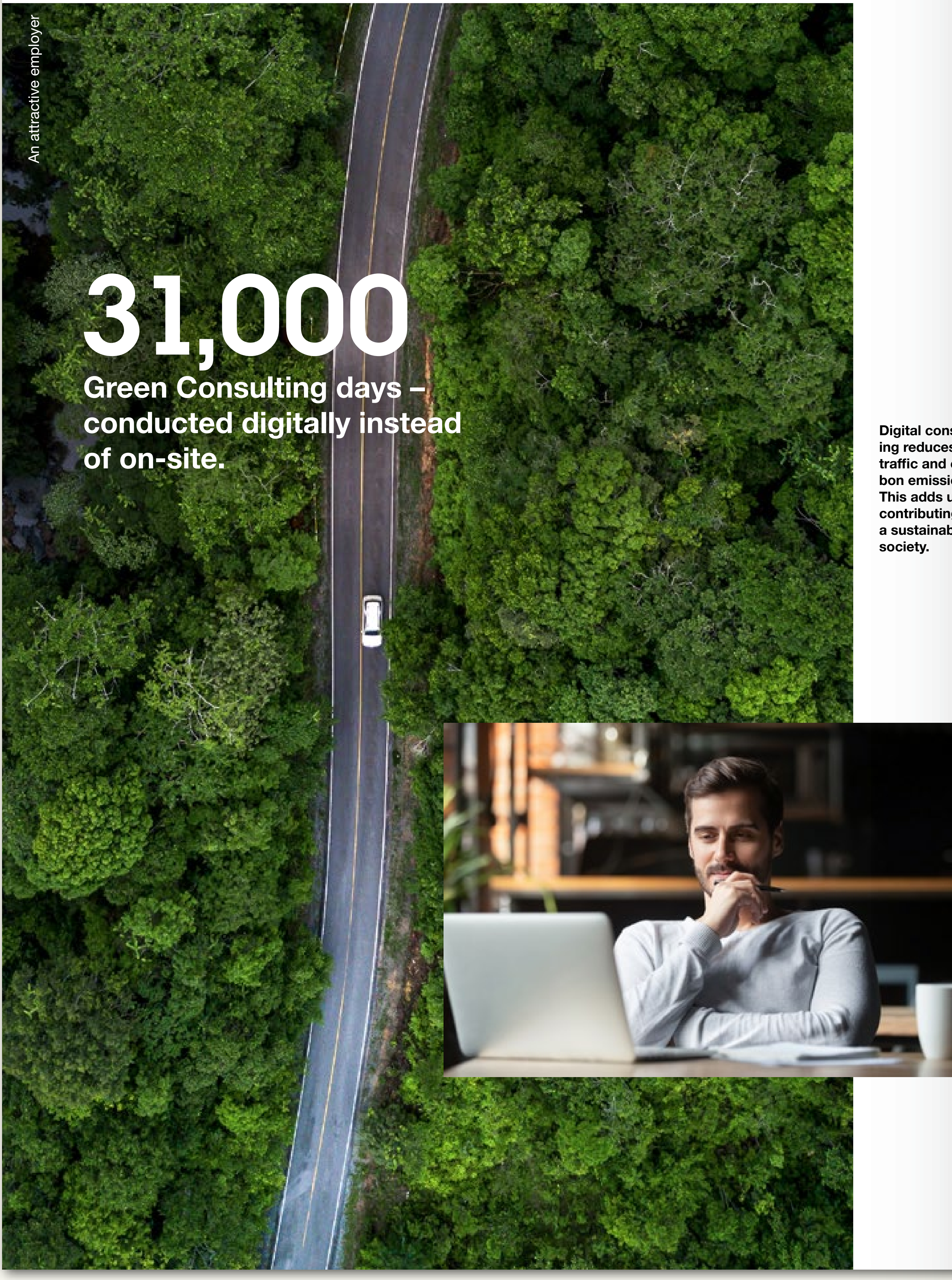
However, the horseshoe-shaped table setting is not yet entirely obsolete: increasingly, modern working spaces emerge which offer new opportunities for managers and employees alike to let their creative juices flow.

"The short-term roll-out of Microsoft Teams was due to the situation at the time. Microsoft Teams has since established itself as a key component to providing our employees with an expanding range of cloud-based digital workplace services across different devices, in particular MS Azure, and doing so in a future-proof way. At the same time, we are reducing our administrative IT workload."

Mathias Magold
Director IT Services,
Aareal Bank

workplace and advancing our leadership culture. Modern spaces that foster new work and create room for new ideas provide further support in this respect. We are in a process of continuous transformation, raising awareness amongst our employees for the potential and opportunities of new work.

The COVID-19 pandemic has clearly shown that this strategy is successful. In a matter of days, the majority of our employees had to make the switch from their office to a home office and thanks to the structures for mobile work already in place, the move was successful within a very short period of time. In this, we benefitted from a highly flexible IT infrastructure; this flexibility will be expanded even further in the coming years.



31,000

Green Consulting days – conducted digitally instead of on-site.

Digital consulting reduces traffic and carbon emissions. This adds up, contributing to a sustainable society.

Green Consulting

Seizing the opportunities of digital working while helping the environment – our Aareon segment has wedded these two objectives in its "Green Consulting" offering. The principle behind it: by providing our IT consulting services online, we not only save on time and money as there is no need to travel, but we also save on carbon emissions.

Our clients have welcomed this offering with open arms, with more than 31,000 "Green Consulting" days being mandated by the end of 2020 – more than double the number of 2019.

Learning@Aareal

In a professional environment undergoing an ever-stronger transformation, lifelong learning is indispensable. In this context, it is not only about continuously acquiring new skills and qualifications. Good continuing professional development also means giving every employee the opportunity to develop at a personal, individual level.

This means that our new job training and CPD initiative Learning@Aareal does not follow a prescriptive approach; rather, it is based on personal initiative and lets our employees decide for themselves which areas they would like to focus on in their development. The starting point for this question is always their current role and function within the Company. Therefore, we have designed a skills matrix determining which expertise our employees should have in which position. The matrix forms the basis for Learning@Aareal, ensuring that every employee finds him-/herself in the programme, regardless of their individual needs.

New ways of learning in a multimedia setting allow Learning@Aareal to provide comprehensive and well-structured CPD offering. The programme includes a few dozen different learning methods. Increased usage of digital channels and so-called blended learning, which combines the benefits of in-person trainings and e-learning, allows for a high degree of flexibility: the online lessons available on the curated learning platform can be accessed from any location and at any time; users can take a break whenever they need and resume at the exact same spot. These are ideal conditions for our employees to be able to continue their education flexibly according to their needs.

Expert dialogue:
Christian Friedrich (Haufe Akademie) and Birgid Schlasius (Aareal Bank) discuss innovative methods in personnel qualification.

"The strong demand for our 'Green Consulting' online services underscores that our strategy is right."

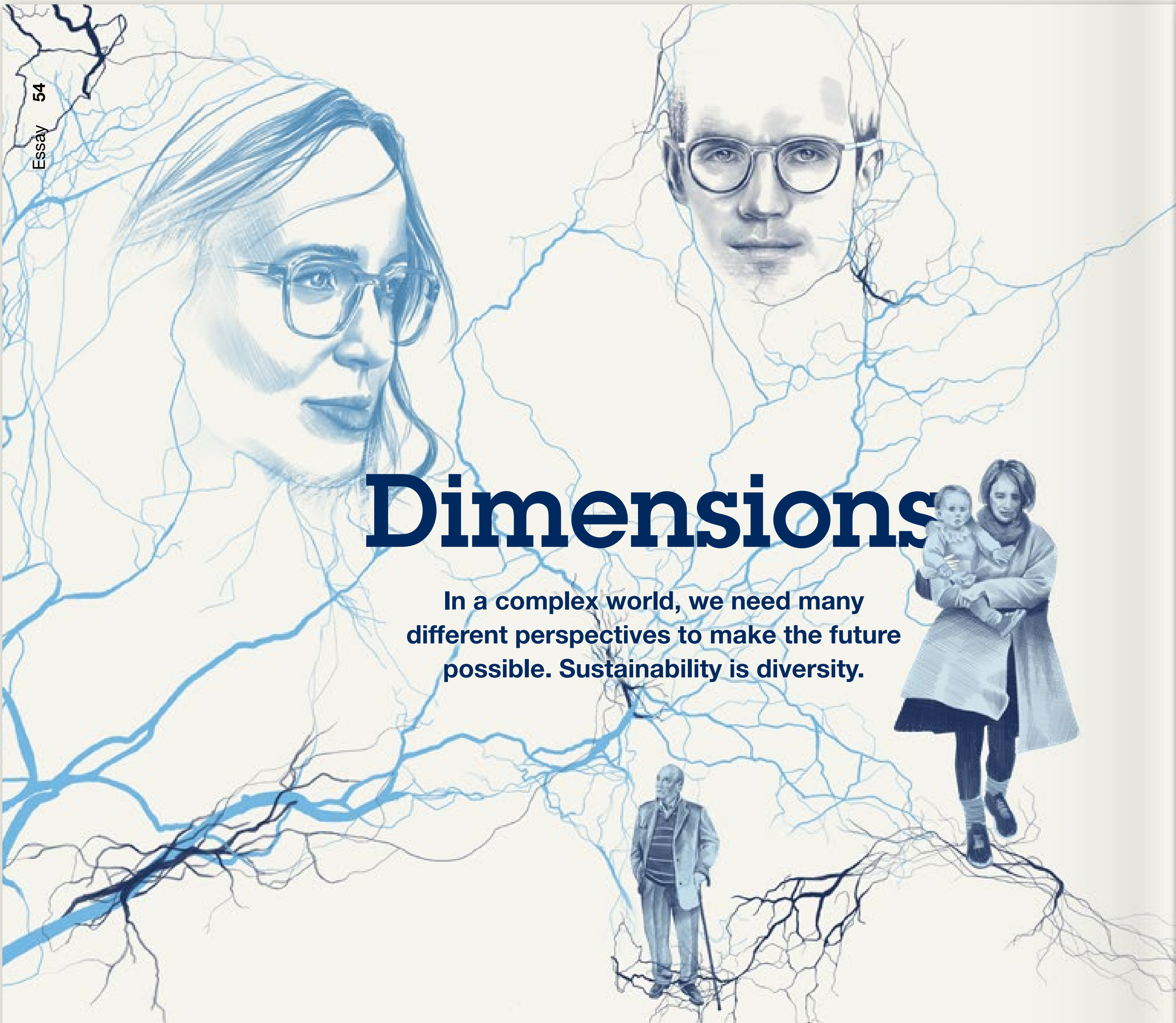
Thomas Lauer
Director Consulting, Aareon

"We pay close attention to sustainability in all of our corporate activities. It's nice to be supported in this by a partner such as Aareon."

Elwira Meid
Digitalisation Officer,
Koblenzer Wohnungsbaugesellschaft

"Learning@Aareal supports employees in performing their current role through targeted learning offerings – 50 per cent of which are available in the digital realm – that are based on our corporate and HR strategy, as well as Aareal Bank's USP."

Jens Huchting
Managing Director Group Human Resources & Infrastructure, Aareal Bank



Dimensions

In a complex world, we need many different perspectives to make the future possible. Sustainability is diversity.

What does one need to do to make tomorrow the best it can be? Since the Second World War, these are the sorts of questions that have occupied futurologues, future researchers and, above all, western nations that have grown affluent. The future had economic boom times, forged by man's will, but not nearly enough – everything needed to keep going that way forever, eternally more of the same – that was the plan for the consumer society of yesterday. And not without reason – many people had nothing or very little. Material needs determined the view of the future, and they still do today, certainly. But at that point, the affluent society was still in its infancy, it had yet to hit puberty, which happened politically, culturally and socially around 1968. And tomorrow was an endless extension of the present, merely more of it. New perspectives – they were like the old viewpoints, only richer. Technicians and managers – people who were capable of generating wealth and organising it – were the model for the age.

But then people started to have doubts about the endless progression of more, and higher, faster. No, the point is not a mere critique of economic growth; it is not that simple. The point, in the transition to an information society – that is to say in the transformation we are currently in the midst of – is that the need for greater quantity gradually gave rise to the desire for greater quality, and increasingly often. Quality is a personal matter. People used to say, "our children should have it better," and what they meant was more of what we did not have enough of. Of all the things parents want for their children today, they want them to be able to lead a successful life that suits them. The new perspective is human in the truest sense. It revolves around the individual, the most important resource of the information society, and of the 21st century.

What profession should one strive for? What about a forester? It sounds a little like running away, but maybe it is exactly the opposite. The forester can conceive of the whole picture – the wood – and the important detail – the tree – without contradiction. Foresters do not think in terms of uniformity, but rather in differentiation, not in one solution, but in the manifold. Foresters are experts at thinking in context. That is exactly what sustainability has to be in order for us to solve the problems of today and tomorrow.

Sustainability, originally a term from forestry, means that we not simply act, but also consider the repercussions of our actions. This does not mean eternal strife and indecision, quite the contrary. It is about the constructive doubt that the father of the Enlightenment, René Descartes, called "the beginning of wisdom". Sustainability is not a managed economy. We do not know what will happen tomorrow, and we should not actually need to have a crisis like the pandemic behind us to know that.

Plans are justified, but in a world where complexity becomes the most important resource for innovation and problem solving, their strict limits are quite clear. Critically doubting what is should not distract us, but rather open the door to new possibilities. That is an important and fundamental principle of the Enlightenment and therefore also of the information society and its economy, which is part of that tradition. One must see the wood and the trees, and one must not fear the apparent thicket, its complexity, but rather use it, truly comb it. Because it is precisely at the point at which the future seems to be nothing but a threat that tremendous perspectives suddenly arise.

No, we do not know all of the answers to the questions about the problems of today and tomorrow, but we know about constructive doubt. Sustainable

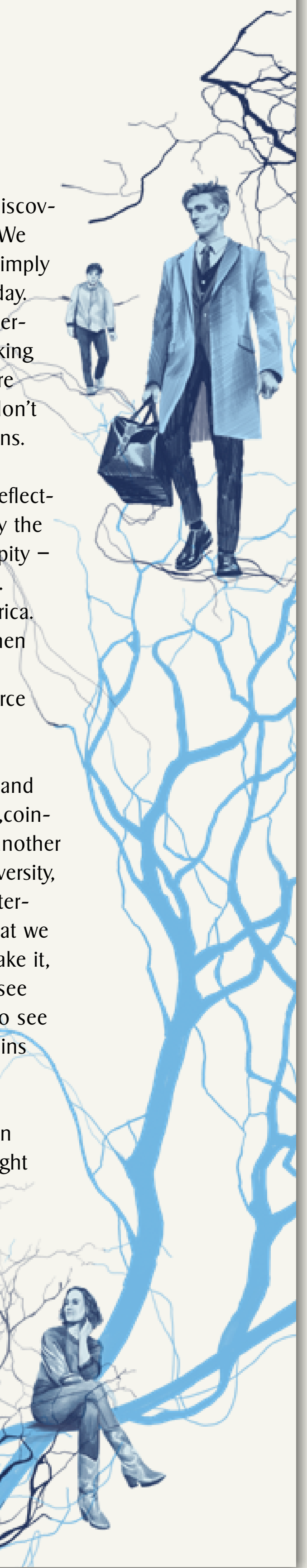
Wolf Lotter
Business journalist
and book author

thinking means that we prepare ourselves for discoveries and new perspectives as best as we can. We have to be capable of handling surprises, not simply working off a blueprint of the future drafted today. That will end in failure. What works is encountering the world with open eyes. Sustainable thinking means flexible thinking, critical questions, where something leads, what we do today, what we don't do – something lacking from a lot of discussions.

The principle of sustainable critical thinking is reflected in the term serendipity, which was coined by the American psychologist Robert Merton. Serendipity – it means something akin to happy coincidence. Columbus tries to find India, but lands in America. We make discoveries that improve our lives when we keep our eyes open, when we do not treat the thicket as an obstacle but rather as a resource for new ideas.

The forester in all of us, as we learn to understand and shape our information society, he knows: „coincidence favours the prepared mind." To put it another way, we prepare ourselves by being open to diversity, to the manifold, to complexity, to numerous alternative answers, to open critical questions so that we can recognise a discovery as such when we make it, and to not leave anything by the wayside. We see context when we have learned to see details, to see quality. Sustainability, critical thinking, it underpins differentiation and understanding context.

We are better able to make it in the world when we conceive of it in human proportions. The right sustainable perspective is not a highway into the future, but rather a network of roads and streets, a warren of paths and connections to what matters to people and to where the individual wants to go. The new perspective has open horizons. That is the very reason we find ourselves within it again. It is not a norm. And that is why it has human proportions.



Aareal

YOUR COMPETITIVE ADVANTAGE.

To our Shareholders

New perspectives

from left:

Thomas Ortmanns
Member of the Management Board

Dagmar Knopek
Member of the Management Board

Marc Hess
Member of the Management Board

Hermann J. Merkens
Chairman of the Management Board

Christiane Kunisch-Wolff
Member of the Management Board

Christof Winkelmann
Member of the Management Board

Letter from the Management Board

Dear shareholders, business associates and staff members,

Aareal Bank Group is looking back at a very challenging 2020 financial year. The global spread of the coronavirus has drastically impacted economic activity around the globe, plunging the global economy into the deepest crisis in decades. Direct and indirect effects of the pandemic, namely the lockdowns in numerous countries, have hit many of our clients' businesses; thus, we have also felt a considerable impact. As a reliable, long-term partner, we have helped our clients get through these difficult times in the best way possible, whilst also having to take account of our own changed risk situation and the increased uncertainty that still prevails.

The pandemic has especially led to higher loss allowance in the Structured Property Financing segment. Based on the global lockdown measures – extended and further tightened at the end of the year – and the resulting deterioration in the economic outlook, we have generally classified as stage 2 all loans for which liquidity support measures were granted in our annual financial statements 2020 – thus recognising loss allowance for default risks which are possible but have not yet materialised. In addition, stage 3 allowance for loans which are potentially or actually non-performing was also raised. Overall, we booked loss allowance of € 344 million in the 2020 financial year, thus comprehensively covering all Covid-19-related risks conceivable at the time of preparing the annual financial statements.

Massively increased loss allowance is the main reason for Aareal Bank Group having reported a loss in the past financial year – for the first time in many years. Consolidated operating profit amounted to € -75 million. After taxes, consolidated net income allocated to ordinary shareholders was € -90 million. The deteriorated risk situation contrasted with a successful operating performance. Thanks to lively new business almost on a par with the previous year, we expanded our credit portfolio to the upper end of the € 26 billion to € 28 billion target corridor. Our subsidiary Aareon also demonstrated its potential and resilience to a crisis with renewed growth in sales revenue.

In light of provisions recognised for the pandemic effects, the solid operating performance in all segments, and our solid capitalisation, we are looking ahead with confidence – and already beyond the current crisis. We feel well positioned for the economic recovery set to begin in the current year and to gradually improve thereafter. On the one hand, this allows us to distribute a dividend – despite the negative result. In the current year, we intend to pay a dividend of € 1.50 per share in two steps, subject to the approval of the supervisory authority and economic conditions permitting. On the other hand, we now have scope to pursue the opportunities arising in the changed environment.

Our fundamentally optimistic stance is also supported by results from the 360-degree review of our "Aareal Next Level" strategic framework which we performed in the past months. The key finding: Aareal Bank Group's business model and strategy remain viable in a normalised environment, once the pandemic has been overcome. However, adjustments will be made within "Aareal Next Level" in order to be able to fully exploit the opportunities arising from changes induced by Covid-19, and to retain the Bank's successful and efficient performance in the future.

By adjusting the strategy, we will be able to generate consolidated operating profit in the range of € 300 million – excluding effects of potential acquisitions – as early as 2023, provided the pandemic has been fully overcome by then and the risk situation has returned to normal. In the recent past, we were only able to achieve a similar level of results in exceptional years that featured strong one-off effects due to acquisitions, accompanied by a significantly more favourable interest rate environment than we expect for 2023.

We will make use of all available levers to realise this significant increase in profitability. We will optimise our funding mix and our capital structure, and also launch a bundle of additional measures aimed at enhancing the efficiency of the organisational structure, processes and infrastructure. Earnings, however, are our main focus: we see opportunities for profitable growth in all our business areas.

In our Structured Property Financing segment, we want to continue controlled expansion of the credit portfolio, in order to improve usage of the existing platform. By year-end 2022 we will achieve a figure of around € 30 billion, whilst adhering to our conservative risk standards – with positive effects for net interest income, which is expected to rise sharply already in the current year.

Growth is also our aim in the Consulting/Services segment. To clarify the main thrusts here, the segment has been renamed "Banking & Digital Solutions" with retroactive effect from 1 January 2021. Our focus will lie on expanding our digital product range and forging further strategic partnerships – alongside the deposit-taking business which we will continue to operate on a similar level as before. A separate innovation budget is at our disposal to achieve these goals. We expect significantly increased net commission income in this segment as a result of the various growth initiatives.

Our IT subsidiary Aareon has been on a profitable growth journey for quite some time. Working side by side with our partner Advent International, we aim to accelerate Aareon's growth momentum – both organically and via further acquisitions. To finance the latter, Aareon not only has equity at its disposal; we will also be able to mobilise a significant amount of debt capital, thus continuing to drive Aareon's inorganic growth together with Advent. Yet even without M&A effects, we are targeting a rise in Aareon's adjusted EBITDA to approximately € 135 million by 2025 based, on the jointly developed Value Creation Programme. The gem within our portfolio that is Aareon is shining brighter and brighter. And with Aareal Bank as majority owner, shareholders will continue to benefit from Aareon's value appreciation.

Aareal Bank Group's medium-term growth prospects are sound – as are short-term prospects, with the picture materially improving in our view. We anticipate a clearly visible macro-economic recovery as early as this year, and therefore plan to return to profitability. The extent of the turnaround will depend primarily on how quickly the recovery gains traction, and how loss allowance develops. From today's perspective, we expect loss allowance for 2021 to fall significantly to between € 125 million and € 200 million, albeit still remaining above its long-term average. Based on a strong operating performance, we are projecting a consolidated operating profit in a broad range of € 100 million to € 175 million, taking into account the uncertainties that currently prevail.

The 2021 financial year will be an important interim step on the path that we have embarked upon with the evolutionary development of our strategy. We have set out a clear plan, showing how we can exploit opportunities for profitable growth in all our segments. This will not only allow us to substantially increase our results – we will also be able to free up capital for the purposes of active capital management, or for selected acquisitions. In the years to come, Aareal Bank Group will thus not only become stronger and more profitable than we are today, but more sustainable too.

We look forward to your continued support and thank you for your trust. I hope you will stay with us in the future too!

On behalf of the entire Management Board

Marc Hess **Thomas Ortmanns**

The Aareal Bank Share

Investor Relations activities

In the financial year under review, the Covid-19 pandemic impacted the economy to an unprecedented extent; the resulting burdens touched all aspects of public and private life. Despite this, Aareal Bank, as a listed public limited company, remains subject to numerous disclosure obligations. Especially in such challenging times, Aareal Bank sees these as an opportunity not only to enter into a consistently open and constructive dialogue with analysts, investors and clients, as well as with the media – but also to intensify this dialogue.

Especially given the more difficult environment and the uncertainty amid the pandemic, the dialogue has become all the more detailed and intensive: in fact, it is a prerequisite for a listed public company to be successful over the long term. Only when company developments are communicated and – if needed – also discussed with Aareal Bank in a timely, open and transparent manner can market participants evaluate potential opportunities and risks that may result from the pandemic and market developments as well as from regulatory changes.

To this end, two face-to-face conferences are held, among other things, in Frankfurt each year for investors, analysts and the media. Back at Aareal Bank's conference in February 2020, the Management Board was still able to personally present the results of the previous financial year in great detail, and also provided a strategic outlook for the future, comprising the current financial year as well as the medium-term horizon ("Aareal Next Level"). Aareal Bank also uses the quarterly publications conference calls as an opportunity to inform investors, analysts and the media about current Group developments.

In the course of the financial year under review, the Investor Relations team took part in eight international capital markets conferences. After three successful conferences in Asia, Europe and the US, all conferences from the second quarter onwards were held online, due to the pandemic. With only nine (partly virtual) roadshows, significantly fewer of these events were hosted than in previous years. As face-to-face meetings were impossible in 2020, one-on-one discussions were replaced by virtual meetings that could also be scheduled more flexibly. These individual online meetings more than made up for the fewer roadshows, so that market communications – by and large – remained at a high level throughout 2020. The fact that the members of the Management Board also attend online conferences, roadshows, and one-on-one meetings on a regular basis, and are available for discussions, is highly appreciated by investors.

In order to ensure access to timely, open and transparent information of relevance to the capital markets, Aareal Bank provides shareholders and analysts with detailed information on Aareal Bank Group and its three segments Structured Property Financing, Consulting/Services Bank (renamed Banking & Digital Solutions with effect from 1 January 2021), and Aareon on its website at www.aareal-bank.com. Furthermore, published ad-hoc disclosures and press releases, financial reports, as well as current Investor Relations presentations, are available for download from our Investor Relations portal. The financial calendar offers an overview of the most important dates in the Company's calendar.

Key data and indicators of the Aareal Bank share

	2020	2019
Share price (€)[1]		
Year-end price	19.550	30.250
High	31.690	31.200
Low	13.670	22.710
Book value per ordinary share (€)	43.54	42.77
Dividends per ordinary share (€)[2]	1.50	./.
Earnings per ordinary share (€)	-1.50	2.42
Price/earnings ratio[3]	-13.03	12.50
Dividend yield (%)[3]	7.67	./.
Market capitalisation (€ mn)[3]	1.170	1.811

ISIN	DE 000 540 811 6
German Securities ID (WKN)	540 811
Mnemonic	
Deutsche Börse	ARL
Bloomberg (Xetra)	ARL GY
Reuters (Xetra)	ARL.DE
Issued share capital (number of bearer unit shares)	59.857.221

[1] XETRA® closing prices
[2] Dividend payments of € 1.50 for 2020 (to be effected in 2021) would need to be made in two steps. In compliance with the requirements published by the European Central Bank (ECB) on 15 December 2020, the distributable amount is calculated at € 0.40 per share. The Management Board plans to submit a corresponding proposal for the appropriation of profits to the ordinary Annual General Meeting in May 2021. Depending on further economic developments, regulatory requirements, the Bank's capital position and its risk situation, an extraordinary Annual General Meeting, which could possibly take place during the fourth quarter of 2021, could then decide on the intended remaining payout of € 1.10 per share. 2019: following a request of the ECB to refrain from distributing dividends, the AGM decided that net retained profit for 2019 be transferred to retained earnings.
[3] Based on XETRA® year-end closing prices

Shareholder structure

since 3 February 2015

To further strengthen shareholders' confidence in the sustainable performance of Aareal Bank Group's business model, we will not waver in our efforts to make our strategic course transparent during the financial year 2021. We continue to actively seek the dialogue with our investors and analysts – using all modern communications channels as a substitute to personal discussions, to the extent possible.

Analysts' opinions

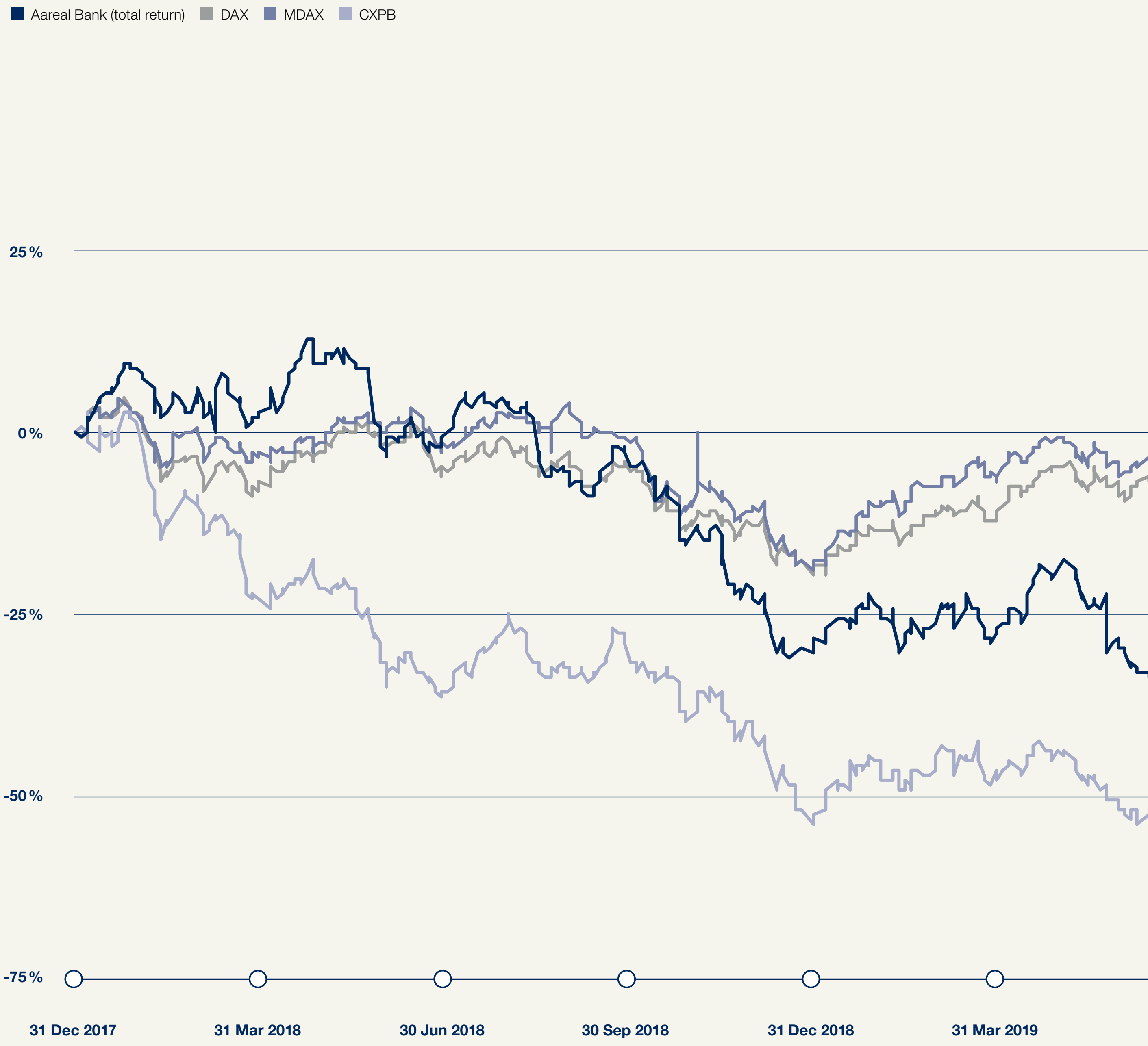
Of the 15 brokerages and analyst firms that regularly covered Aareal Bank at the start of the financial year, two firms stopped and one firm temporarily suspended coverage of Aareal Bank in the course of the year, so that at the end of 2020, a total of 12 brokerages and analyst firms published independent studies and comments about developments at Aareal Bank Group.

Having finished the 2019 financial year on a positive note, in 2020, Aareal Bank needed to meet expectations by market participants and analysts in the light of the Covid-19 pandemic. Four "buy" and five "neutral" recommendations compared to three "sell" recommendations.

We regularly update and publish the analysts' recommendations on our website www.aareal-bank.com on the Investor Relations page.

Relative performance of the Aareal Bank share price

2017-2019



1 **26 February 2020**
Following a strong performance in the 2019 financial year, Aareal Bank Group expects stable 2020 consolidated net income

2 **26 March 2020**
Aareal Bank Group publishes its Annual Report 2019

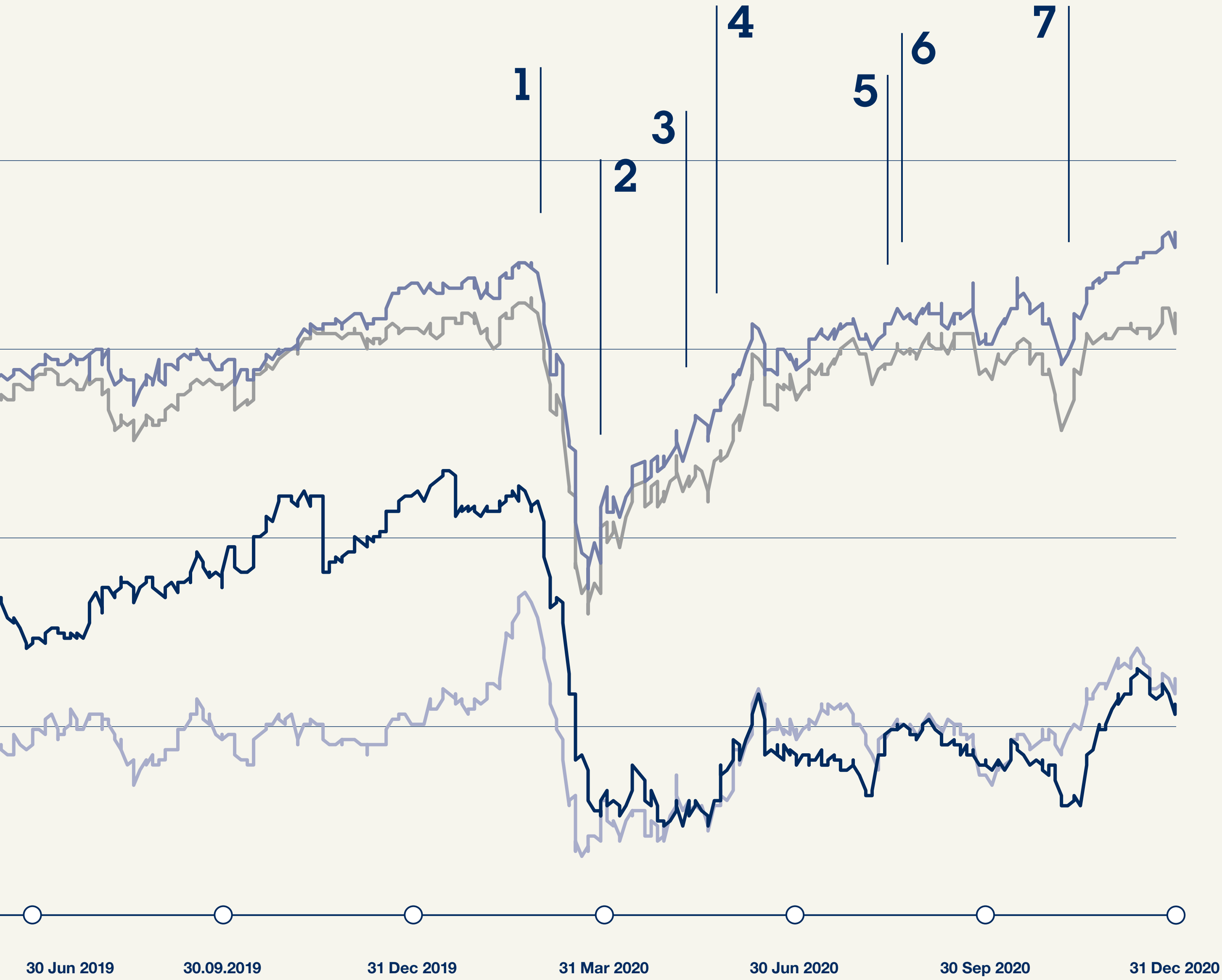
3 **12 May 2020**
Aareal Bank Group delivers positive results for the first quarter of 2020, having accounted for effects of Covid-19

4 **27 May 2020**
Annual General Meeting of Aareal Bank AG approves dividend waiver recommended by the ECB by a large majority

5 **13 August 2020**
Aareal Bank Group posts positive results for the second quarter of 2020 as well, despite burdens of Covid-19 and a successful de-risking

6 **14 August 2020**
Aareal Bank sells 30 per cent stake in IT subsidiary Aareon to Advent International – long-term partnership agreed upon

7 **12 November 2020**
Aareal Bank Group once again posts positive consolidated operating profit in the third quarter, despite persistent significant burdens due to Covid-19



Aareal Bank Group is a leading provider of smart financing, software products and digital solutions for the property sector and related industries. It is active in more than 20 countries across three continents – in Europe, North America and Asia/Pacific.

Group Management Report

New perspectives

Group Management Report

Aareal Bank Group is an international property specialist. It is active in more than 20 countries across three continents – in Europe, North America, and in the Asia/Pacific region.

Fundamental Information about the Group

Business model

Aareal Bank AG, headquartered in Wiesbaden, Germany, is the parent company of the Group. Its shares are admitted to trading on the regulated market (geregelter Markt) of the Frankfurt Stock Exchange.

The strategic business segments of Aareal Bank Group are commercial property financing and services, software products and digital solutions for the property sector and related industries. The strategic business segments are broken down into the three segments Structured Property Financing, Consulting/Services Bank and Aareon.

Structured Property Financing

In the Structured Property Financing segment, Aareal Bank facilitates property investments for its domestic and international clients, and is active in this respect in Europe, North America and the Asia/Pacific region. Aareal Bank finances commercial property investments, especially for office buildings, hotels, retail, logistics and residential properties, with a focus on existing buildings. By combining local market expertise with sector-specific know-how from the Group's head office, Aareal Bank can offer financing concepts that meet the special requirements of its national and international clients, as well as concluding structured portfolio and cross-border financings.

Aareal Bank manages its sales activities in the individual regions worldwide via a network of sales centres (hubs). In addition to the locally-based experts, the distribution centres for sector specialists covering hotels, retail and logistics properties, as well as those catering to the specific needs of investment fund clients, are located in Wiesbaden.

There are two regional hubs in Europe: one hub combines sales activities for the euro zone, with a focus on the Benelux countries, France, Germany, Italy and Spain. An additional hub focuses on sales activities outside the euro zone, with a focus on the UK and Central and Eastern Europe. Distribution in Northern Europe is managed from the head office in Wiesbaden. As before, the hubs have a network – comprising branches in London, Paris, Rome, Stockholm and Warsaw – at their disposal. Furthermore, the Dublin branch holds securities. Representative offices are located in Istanbul, Madrid, and Moscow.

Aareal Bank Group's activities on the North American market are carried out through the subsidiary Aareal Capital Corporation, operating from New York City. The Singapore subsidiary Aareal Bank Asia Limited conducts the sales activities in the Asia/Pacific region.

Funding

Aareal Bank is an active issuer of Pfandbriefe, which account for a major share of its long-term funding. Moody's Aaa rating of the Pfandbriefe confirms the quality of the cover assets pool. To cater to a broad investor base, Aareal Bank uses a wide range of other refinancing tools, including senior preferred and senior non-preferred bonds, as well as other promissory notes and bonds. Depending on market conditions, the Bank places large-sized public issues or private placements. In the Consulting/Services Bank segment, the Bank also generates bank deposits from the housing industry, which represent a strategically important additional source of funding. Furthermore, it has recourse to institutional money market investor deposits.

Consulting/Services Bank

In the Consulting/Services Bank segment (formerly: Bank division Housing Industry, as of 1 January 2021: Banking & Digital Solutions), Aareal Bank Group offers its clients from the institutional housing industry, commercial property companies, as well as the energy and utilities industry, services for the management of properties used for residential purposes and the integrated processing of payment flows, as well as other services. With its BK 01 software, it operates a procedure for the automated settlement of mass payments, in the German property industry. The procedure is integrated in licensed bookkeeping systems. In conjunction with payment transactions processed via Aareal Bank's systems, deposits are generated that contribute significantly to Aareal Bank Group's refinancing base. Besides the German property industry, the German energy sector forms a second major client group of the segment for the services mentioned above. This enables the offer of further products, facilitating the cross-sector cooperation of client groups and realising synergies via end-to-end digital processes. Aareal Bank is further strengthening its market position with its growing range of digital products and invoicing solutions within this segment. These products include mobile solutions for recording and processing meter readings, a platform solution for managing B2B payment processes and services, as well as a solution for simplifying invoice management of complex payment flows, whose first application was in e-mobility.

Aareon

In the Aareon segment, the Aareon sub-group offers its customers consulting, software and services solutions to optimise IT-supported business processes and to expand business models in the digital age. Aareon is present at 39 locations in Germany, Finland, France, the UK, the Netherlands, Norway, Austria, Romania (development business), Sweden and Switzerland. Aareon Smart World's portfolio of products, comprising ERP (enterprise resource planning systems) and digital solutions, networks property companies and their employees with clients, business partners as well as technical equipment in apartments and buildings. The ERP systems ensure recurring sales revenue and are a starting point for cross-selling activities for the digital solutions. The portfolio of digital solutions is being steadily expanded by the international research and development teams and through cooperations with PropTech enterprises. Aareon benefits from a cross-border transfer of know-how, leveraging the respective country-specific focal areas of digitalisation to expand its range of products and services. Aareon offers software solutions both in the DACH region (Germany, Austria and Switzerland) and abroad that may be used in various types of operating environments: in-house services, hosting and Software as a Service (SaaS) from the exclusive Aareon Cloud.

Management system

Aareal Bank Group is managed using key financial performance indicators, taking the Group's risk-bearing capacity into account. Management takes place primarily at Group level, and is additionally differentiated by business segment. Group management is based on medium-term Group planning, prepared annually, which is geared towards the Group's long-term business strategy. An extensive (management) reporting system regularly provides the information required for management and monitoring purposes.

The following indicators implemented within the scope of business and return management are Aareal Bank Group's key financial indicators. As well as the designation of the Consulting/Services Bank segment, they were revised at the turn of the year as part of the strategic review. Given its relevance for management purposes, the Common Equity Tier I Capital Ratio is based on the so-called "phased-in" ratio pursuant to Basel IV:

- **Group/consolidated:**
  - Net interest income (in accordance with IFRSs)
  - Net commission income (in accordance with IFRSs)
  - Loss allowance (in accordance with IFRSs)
  - Administrative expenses (in accordance with IFRSs)
  - Operating profit (in accordance with IFRSs)

  - Return on equity (RoE) before taxes[1] (up to 31 December 2020) RoE after taxes[2] (from 1 January 2021)
  - Consolidated net income allocated to ordinary shareholders of Aareal Bank[3] (up to 31 December 2020)
  - Earnings per ordinary share (EpS)[4]
  - Common Equity Tier 1 ratio (CET1 ratio) (%) – Basel IV (estimate) – (phased-in from 1 January 2021)

- **Structured Property Financing segment**
  - New business[5]
  - Credit portfolio of Aareal Bank Group

- **Consulting/Services Bank segment (as of 1 January 2021: Banking & Digital Solutions)**
  - Average deposit volume from the housing industry
  - Net commission income (in accordance with IFRSs)

- **Aareon segment**
  - Sales revenue (in accordance with IFRSs)
  - Adjusted EBITDA[6]

The Group's existing risk management system is used to manage and monitor the various risk exposures of Aareal Bank Group entities, in a centralised manner. 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 various 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. The property financing portfolio 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 strategy. By taking into consideration maximum allocations to individual countries, products and property types in the portfolio, we ensure a high level of diversification and avoid risk concentrations.

The Consulting/Services Bank and Aareon segments also have specific management indicators typical for the respective business. The deposit volume from the housing industry and net commission income are key financial performance indicators for the Consulting/Services Bank segment. Aareon is managed on the basis of target figures commonly applied to software companies, such as sales revenue and adjusted EBITDA[6].

---

[1] RoE before taxes = $\frac{\text{Operating profit ./. consolidated net income attributable to non-controlling interests ./. AT1 coupon}}{\text{Average equity (IFRS) excluding non-controlling interests, other reserves, AT1 bond, and dividends}}$

[2] RoE after taxes = $\frac{\text{Operating profit ./. income taxes ./. consolidated net income attributable to non-controlling interests ./. AT1 coupon (net)}}{\text{Average equity (IFRS) excluding non-controlling interests, other reserves, AT1 bond, and dividends}}$

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

[4] EpS = $\frac{\text{Operating profit ./. income taxes ./. consolidated net income attributable to non-controlling interests ./. AT1 coupon (net)}}{\text{Number of ordinary shares}}$

[5] New business = newly-originated loans plus renewals

[6] "Earnings before interest, taxes, depreciation and amortisation" excluding strategic investments (venture and M&A activities) and non-recurring effects

Report on the Economic Position

Macro-economic environment

The Covid-19 pandemic, which spread worldwide in the first quarter of 2020, and the measures taken in this context, resulted in a drastic collapse in economic output within a very short timeframe. Numerous economies faced enormous challenges in the first half of the year, some of which have not been seen since WWII. As a result of the measures taken to protect against the spread of the infection, which brought public life to a complete standstill in numerous countries and temporarily prohibited various services, as well as the collapse of various supply chains, the global economy plunged into a deep recession from March onwards. The second half of the year showed a marked recovery, which eased over time and ground to a halt as a result of renewed lockdowns imposed in many countries at the end of the year. State aid measures and a very loose monetary policy mitigated some of the negative effects this had on the economic players.

Economy

As a result of the Covid-19 pandemic, economic output in the euro zone in 2020 fell by 7.1 % compared with 2019. The year-on-year decline was still 15.0 % in the first half of 2020. In the third quarter of 2020, the economy improved by 12.5 % over the second quarter. New lockdowns in the fourth quarter of 2020 led to a renewed decline in individual euro zone countries. The services sector was hardest hit, while industrial production proved more stable. Governments implemented different aid and support measures – ranging from payment moratoriums to direct aid payments – to mitigate the consequences. While these measures varied from country to country, the aid provided totalled 4.5 % of gross domestic product in the euro zone. As a result, the government debt ratios in the euro zone increased.

The downturn was somewhat milder in some non-euro zone countries. The decline in Sweden's economic output, in particular, was less severe than in the rest of the EU. Economic output in Poland was down 2.9 % on the previous year. In contrast, the Czech Republic was harder hit by the pandemic than Poland or Sweden in 2020, with its economic output falling by 6.8 %.

In addition to the pandemic, Brexit also left its mark in the UK. The transition phase following the UK's exit from the EU on 31 January 2020 ended at the end of 2020. A trade deal was reached with the EU at the end of December 2020, thus avoiding a hard Brexit with numerous restrictions on trade. The deal also secures zero tariffs and unlimited movement of goods, albeit with greater bureaucratic hurdles to be overcome. Furthermore, the UK also ended the year 2020 with a hard lockdown, with the resultant negative effects. Overall, gross domestic product fell by 10.3 % during the course of 2020 compared with 2019.

Economic output in the US was 3.5 % lower in 2020 as a result of the Covid-19 pandemic, but made a marked recovery, especially in the third quarter of 2020. Several state aid programmes were rolled out during 2020, the last of which was launched towards the end of December. Uncertainty surrounding the presidential election also had a negative impact before easing at the end of 2020. In Canada, gross domestic product at the end of the year 2020 was down by 5.5 % on the same period of the previous year.

The pandemic had already started in China at the end of 2019, where it was brought under control much earlier than in the rest of the world. This meant that measures to ease restrictions took effect earlier, with positive knock-on effects for economic output, which showed no signs of a decline for the year as a whole. Exports, which are important for China, increased again in the second half of 2020.

In Australia, economic output in 2020 was 2.8 % lower than in the previous year, due to lower domestic consumption as a result of the Covid-19 pandemic.

The recession led to a sharp decline in employment across the globe. Whilst short-working programmes and other state measures tempered the rise in unemployment in many of the developed economies, large-scale redundancies have been seen in countries that did not have such programmes in place. In the US in particular, the number of people registering as unemployed for the first time rose dramatically within a short period. In April 2020, for example, the unemployment rate came to 14.7 % compared with 3.5 % at the end of 2019. However, the figure fell again to below 7.0 % by the end of 2020.

Annual rate of change in real gross domestic product

%	2020[1]	2019[2]
Europe		
Euro zone	-7.1	1.3
Austria	-7.5	1.4
Belgium	-7.1	1.7
Finland	-3.2	1.1
France	-9.1	1.5
Germany	-5.3	0.6
Italy	-9.0	0.3
Netherlands	-3.9	1.6
Spain	-11.1	2.0
Other European countries		
Poland	-2.9	4.6
Russia	-3.8	1.3
Sweden	-3.0	1.4
Switzerland	-3.1	1.1
United Kingdom	-10.3	1.4
North America		
Canada	-5.5	1.9
USA	-3.5	2.2
Asia/Pacific		
Australia	-2.8	1.9
China	2.1	6.0

[1] Preliminary figures; [2] Adjusted to final results

Financial and capital markets, monetary policy and inflation

The Covid-19 pandemic was the dominant topic on the financial markets, too. In the short term, the crisis triggered higher volatility and pushed up interest rates. Fast action taken by central banks in and extensive response to the crisis, however, increasingly reassured the markets.

In 2020, the European Central Bank (ECB) adjusted its monetary policy several times to promote favourable financing conditions for the real economy in times of heightened uncertainty. While the key interest rate remained unchanged at zero per cent during the year, in March the Asset Purchase Programme (APP), which was launched back in September 2019 for an indefinite period, was ramped up by € 120 billion until the end of 2020. It will run from 2021 onwards on a monthly base level of € 20 billion. Additionally, a pandemic emergency purchase programme (PEPP) for public and private-sector issuers of securities was launched in March. This programme's volume was gradually increased during the year in several stages from € 750 billion originally to € 1.85 trillion. Its duration was also extended, most recently in December, to March 2022 at the earliest. The ECB will be maturing principal payments from securities purchased under the PEPP at least until the end of 2023. The terms for TLTRO 3 (Targeted Long-term Refinancing Operations 3) were also eased in March 2020 and extended in December, encouraging banks to maintain their lending policies. If the banks participating in these refinancing operations realise positive net lending to non-financial companies and private individuals in the euro zone in a reference period, this provides an attractive refinancing option with a negative interest rate that exceeds the ECB's deposit rate. There are also a number of other conditions attached to this programme.

The US Federal Reserve (FED) also took extensive measures in 2020 to support lending to households and the corporate sector, and to free up liquidity in the banking system. Two interest rate cuts implemented on 3 and 15 March lowered the key interest rate by a total of 150 basis points to a corridor of 0 – 0.25 %. As further stimulus, the FED made the decision on 15 March to increase its purchase programme for government bonds and mortgage-backed securities to an unlimited volume. Numerous lending programmes were also launched in the first half-year, to provide private and public-sector borrowers alike with liquidity and to help ensure that the credit markets could continue to function. As part of this programme only applies to 2020, it will be subsequently discontinued. On 27 August, the forward guidance was changed, whereby the current low interest rate policy is likely to remain in place in the medium term. This resets the inflation rate target at 2 % on average. The conversion to an average horizon suggests that exceeding the 2 % target slightly would be tolerated. Instead of taking deviations from the maximum employment level into account when setting monetary policy, a shortfall only will now be considered.

The Bank of England lowered the base rate to 0.1 % in two interest rate cuts in March 2020. The purchase programme for UK government and corporate bonds was also increased in several steps to a target value of GBP 895 billion.

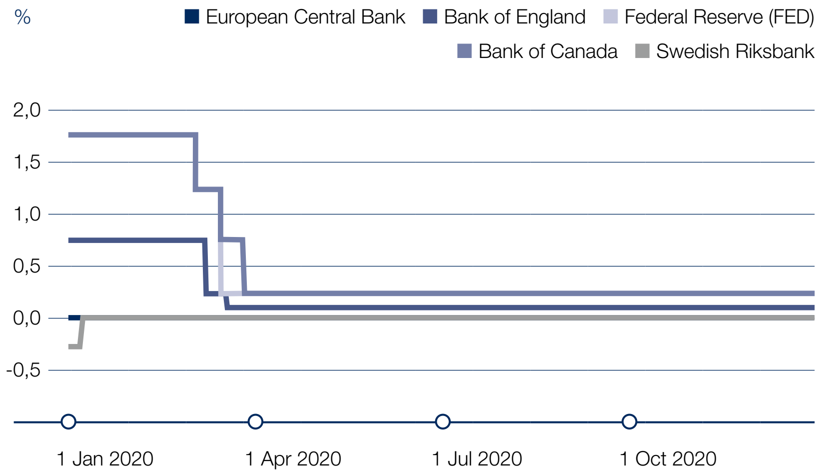
At year-end 2020, short-term interest rates[1] were 15 basis points lower year-on-year in the euro zone and 25 basis points lower in Swedish krona. In US dollars and Canadian dollars, they fell by around 160 basis points. The decline was around 75 and 90 basis points respectively for pound sterling and Australian dollars.

Long-term interest rates[2] fell initially at the start of the year in all of the currency areas that are relevant to Aareal Bank. As a direct consequence of the pandemic, they rose in April 2020 in all relevant currencies by around 40 to 50 basis points. Measured in euros, they then fell continuously to end roughly 50 basis points lower compared with the start of the year. Measured in USD, they fell up to mid-2020, before rising again by the end of the year. At the end of the year 2020, they were around 90 basis points below the 2019 year-end value. Long-term GBP interest rates developed in a similar manner; at the end of 2020 they remained around 60 basis points below the previous year's figure. They fell to a lesser extent in Swedish krona, at roughly 30 basis points less year-on-year at the end of 2020.

Government bonds with a ten-year maturity painted a mixed picture in the full-year 2020. While yields in the countries considered as safe havens fell in the course of the Covid-19 pandemic, they rose initially in Italy and Spain. Yields in the US, Sweden and the UK rose further in the second half of 2020, but declined again in Italy and Spain. At the end of 2020, yields in all the observed countries were down compared with the end of 2019.

Despite the current Covid-19 pandemic, the primary market in the euro zone's covered bond segment was defined by falling yields in 2020 due to the ECB's expansive monetary policy. Senior preferred bonds of many European banks were also trading at negative yields. Monetary policy taken, such as the ECB's TLTRO, also led to a significant reduction in the volume of new Pfandbriefe issued compared to 2019.

Key rate developments in 2020[3]



[3] The upper level of the corridor for Fed key rates is shown in the chart.

[1] Calculated on the basis of 3-month Euribor or the corresponding Libor or other comparable rates for other currencies

[2] Calculated on the basis of swaps in the respective currencies

Regulatory environment

The environment in which banks are operating continues to be defined by highly dynamic regulatory requirements, as well as by changes in banking supervision. This includes, in particular, the implementation of the final draft of the Basel III framework into EU law (known as "Basel IV"), which was endorsed by the Basel Committee's Group of Governors and Heads of Supervision (GHOS). Furthermore, the EU Commission's revision of supervisory regimes (CRR II, CRD V, BRRD II and SRMR II) at EU level as well as the EBA documents (Guidelines on PD and LGD estimation, treatment of defaulted exposures, and determination of downturn LGD), brought about further regulatory changes. The provisions put forward by the ECB, EBA and the EU Commission on the treatment of non-performing loans must also be taken into account. With regard to Covid-19, the IASB and relevant regulatory authorities such as the EBA, the ECB and ESMA formulated recommendations for implementation in the processes and for risk quantification, which we have taken into consideration accordingly. In addition, new reporting requirements were implemented, such as Covid-19 reporting, as well as relief measures such as the CRR Quick Fix, in which the date of application for selected topics, such as the SME Supporting Factor, were brought forward.

Moreover, both national and European regulators are imposing various new requirements – including in connection with IT/information security risks, or regarding the prevention of money laundering, tax evasion and terrorist financing. Furthermore, politics and the banking supervision deem it necessary to establish sustainability more strongly with society, and as a regulatory requirement within the economy. As such, the EU's Technical Expert Group on Sustainable Finance published the "Taxonomy Technical Report", and BaFin issued its "Guidance Notice on Dealing with Sustainability Risks" at the end of 2019. The ECB also published its guide on climate-related and environmental risks, setting out its expectations relating to risk management and disclosure.

The ECB's Supervisory Review and Evaluation Process (SREP) ensures a common approach on the supervisory review of banks, within the framework of Pillar 2. The SREP is built around a business model analysis, an assessment of governance, as well as of the capital and liquidity risks. The results of the individual areas are aggregated in a score value, from which the ECB derives supervisory measures on holding additional capital and/or additional liquidity buffers. In the past year, ECB took a pragmatic SREP approach, which was mainly focused on the assessment of Covid-19-related risks. As a result, the score values and the requirements for additional capital and liquidity buffers remained unchanged except in justified individual cases. The assessment of Aareal Bank remained unchanged compared to the previous year.

Sector-specific and business developments

Structured Property Financing segment

Transaction volumes in 2020 declined substantially from the previous year, with notable difference in the regions. While volumes fell by around 40 % in North America, it was lower in Europe and the Asia/Pacific region at around 30 %. Transactions were delayed especially by measures taken to protect against the spread of the infection, while investor demand on the other hand remained intact. The latter can be assumed, given the virtually unchanged long and short positions of the investors. Property types varied; demand for logistics properties in particular remained strong, while fewer hotels and retail property changed hands, as a result of being directly affected by the government restrictions due to the measures taken to protect against the spread of the infection. The longer-term trend and radical changes brought about by online trading also impacted on retail property.

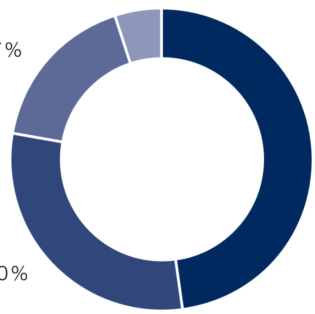
Measures imposed by various governments to protect against the spread of the infection in relation to the Covid-19 pandemic limited the operation of retail properties, hotels and student accommodation over a longer period of time in 2020 in many markets, resulting in lower revenues and rental income. Office properties were impacted rather indirectly by the measures, leading to greater uncertainty about future rental demand. Logistics properties, on the other hand, recorded higher rental demand.

In spite of the Covid-19 pandemic, market participants remained willing to provide financing for most types of property and locations in 2020. There were only partial restrictions, for example for retail properties in peripheral locations or some hotel properties. As a result, and with a smaller number of transactions, competition for commercial property financing remained intense. Margins increased in the course of the Covid-19 pandemic as refinancing rates rose. However, this trend reverted again as the situation eased in the course of the year. Refinancing costs and customer margins fell again, albeit not quite to the previous year's level. Loan-to-value ratios for new business declined.

In an environment influenced by the pandemic with high levels of uncertainty, Aareal Bank generated new business[1)] of € 7.2 billion (2019: € 7.7 billion) and was therefore within the original target corridor of € 7 billion to € 8 billion, despite the adverse circumstances related to the pandemic. The estimated share of newly-originated loans was 75.6 % (2019: 80.1 %) or € 5.5 billion (2019: € 6.2 billion). Renewals amounted to € 1.7 billion (2019: € 1.5 billion). At 58.7 % (2019: 60.1 %), Europe accounted for the largest share of the financings, followed by North America with 36.6 % (2019: 35.1 %) and the Asia/Pacific region with 4.7 % (2019: 4.8 %).

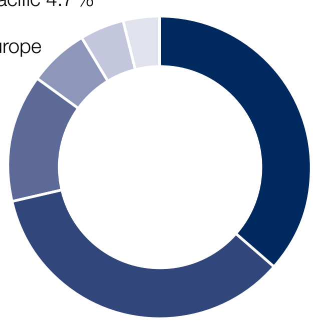
Share of transaction volume observed worldwide in 2020

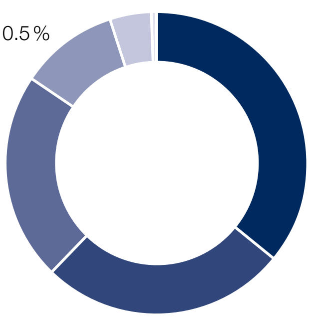
%



New business[1)] 2020

by regions | by type of propert (%)





* Incl. Germany

1) New business, excluding former WestImmo's private client business and local authority lending business.

With a share of 36.1 % (2019: 49.5 %), office property accounted for the largest share in new business in terms of property type, followed by logistics property at 26.5 % (2019: 9.9 %), whose share of new business increased appreciably, ahead of hotel property at 22.2 % (2019: 24.0 %) and retail property at 10.5 % (2019: 13.3 %). The share of residential property was 4.5 % (2019: 2.8 %), while other property and financings accounted for 0.2 % (2019: 0.5 %). Special attention was paid to the financing of modern, high-quality logistics properties in 2020.

Europe

Transaction volumes fell by around 30 % in Europe. The decline was lower in the UK and Poland. In Sweden, volumes even increased over the previous year. Investor positions changed only marginally compared with the previous year. Cross-border institutional investors were on the buy side for the most part, while REIT structures and private investors tended to be sellers.

Top yields[1] for office properties changed only marginally year-on-year and remained low. Top yields on European logistics properties decreased by 25 to 50 basis points. On contrast, top yields for retail and hotel properties rose between 50 and 125 basis points, especially in the UK. The development on the retail property market varied between shopping centres and retail parks, with the latter posting a lower rise of 25 to 50 basis points on average. In some markets, such as Germany and Sweden, they remained unchanged for retail parks.

The scenario during the year was similar for top rents. While they tended to remain rather stable for logistics properties, they fell by between 10 % and 20 % for retail property, whereby there were differences between shopping centres and retails parks. The latter were affected to a lesser extent by the measures taken to protect against the spread of the infection and remained open to a greater extent. Top rents for office properties fell by a few percentage points. With hotel properties, the lockdown led to a decline of around 50 % in average revenues per available hotel room, with income temporarily coming to a complete standstill. In contrast, occupancy improved significantly in part when measures taken to protect against the spread of the infection were eased. However, the higher levels of new infections at the end of the year and renewed lockdown measures had negative impact again.

The Bank originated new business of € 4.2 billion (2019: € 4.6 billion) in Europe during the year under review. As in the previous years, Western Europe accounted for the largest share of € 2.5 billion (2019: € 3.2 billion). This was followed by Eastern Europe, where new business of € 1.0 billion (2019: € 0.5 billion) was generated almost exclusively in Poland and the Czech Republic, Northern Europe with € 0.5 billion (2019: € 0.3 billion) and Southern Europe with € 0.2 billion (2019: € 0.6 billion).

North America

In North America, transaction volumes in 2020 were down by around 40 % year-on-year following an increase in the first quarter. The consequences of the Covid-19 pandemic were still being clearly felt at the end of the year. In terms of quantity, only half as many properties changed hands as in the previous year. This was particularly the case for retail and hotel property. Unlike in previous years, private investors were clearly on the seller side, whereas cross-border investors had almost balanced positions. Institutional investors were mainly on the buy side.

In 2020, rents offered for first-class offices in US metropolitan areas averaged 1.2 % lower compared with the end of the previous year. Developments did, however, vary from market to market. Rents in San Francisco fell by nearly 9 %. They were 4 % lower in New York, while remaining stable in Philadelphia. The development in rents for prime retail properties varied depending on the property subtype. Shopping malls, which were already under intense competitive pressure before the Covid-19 pandemic hit, reported a further

[1] Falling yields are usually associated with rising property market values, all other things remaining equal.

drop in rent and revenues, although this trend was also influenced by the pandemic. Local suppliers and retailers stocking everyday consumer goods, on the other hand, proved to be robust.

The pandemic impacted to a lesser extent on yields for first-class offices in the US in the year as a whole, thanks to high levels of liquidity and readiness to provide financing. Despite this, yields rose by just short of 20 basis points. Yields for malls also increased by around 20 basis points on average compared with the start of the year.

In North America, too, official restrictions led to the closure of almost all hotels from mid-March onwards, with only a slow trend towards subsequent relaxations. Although improvements in occupancy rates and average revenue per available room were starting to emerge at year-end, an increase in the number of new Covid-19 infections once again put a damper on the trend later in the year.

In North America, the Bank originated new business of € 2.7 billion (2019: € 2.7 billion) in 2020, almost all of which was attributable to the US.

Asia/Pacific region

Transaction volumes for commercial property in the Asia/Pacific region were roughly one third lower than in the same period of the previous year, owing to the Covid-19 pandemic. Fewer retail and hotel properties, in particular, changed hands in Asia/Pacific, too, while the number of logistics properties increased. Investor positions were similar to the previous year, with cross-border and institutional investors tending to be on the buy side, while REIT structures and private investors were more likely to be the sellers.

The development of top rents for office properties in Australia, China and Singapore showed a declining trend. Rents for logistics properties increased in Australia and China. However, rents for retail properties fell in all markets, due to the measures taken to protect against the spread of the infection, among other things. Rents for logistics properties rose.

Yields for top office properties rose by an average of 10 basis points in the Asia/Pacific region. While yields for shopping centres rose by up to 30 basis points, yields on logistics properties decreased by an average of 30 basis points.

Given that China represented the starting point for the pandemic, hotels there and in other Asian countries were impacted early in the year by the almost complete closure brought about by the measures taken to protect against the spread of the infection. This also meant, however, that relaxation measures were taken earlier than in other regions. While occupancy rates in China showed a rising trend thanks to domestic demand, they were still down noticeably year-on-year. Overall, average occupancy rates reached nearly 50 % in the Asia/Pacific region in 2020.

The Bank originated new business of € 0.3 billion in the Asia/Pacific region in 2020 (2019: € 0.4 billion).

Consulting/Services Bank segment

The residential and commercial property sectors in Germany are proving to be stable market segments, even in light of the Covid-19 pandemic. In general, steady rental income generated from a high occupancy status continues to guarantee a secure foundation. New-build rents rose by 3.7 % compared with the previous year (the third quarter is the comparative figure). Despite individual rent deferrals, no significant decline in rental income has therefore been witnessed on the housing market so far.

The shortage of residential space, which was the key driver of rental prices, eased. Construction in the most popular cities ("Schwarmstädte") is meanwhile nearly adequate, especially given that the trend to relocate here has eased off. Because of the high rents in city centres, people searching for accommodation have turned increasingly to the outskirts, with the resultant higher increase in rent prices there. This trend was reinforced by the Covid-19 pandemic, as the daily commute was no longer as important given the greater numbers working from home.

Group Management Report
Consolidated Financial Statements
Transparency

The 2020 financial year saw the Consulting/Services Bank segment strengthen its market position again via the acquisition of new clients. We also consistently intensified the cross-sector collaboration with our clients from the energy and waste disposal industry. This is accomplished especially through interface products such as BK 01 eConnect and BK 01 immoconnect, which extend across sectors and can be linked to housing industry products, such as the BK 01 Invoice Data Processing, in order to facilitate for example accounting documentation and invoicing of energy supplies. This brought in more clients from the housing industry – managing more than 200,000 residential units between them – for the payments and deposit-taking businesses.

We once again strengthened our range of property industry services this year and at the same time extended the range of digital solutions for the housing industry and its clients.

With the Aareal Exchange & Payment Platform (AEPP), we offer a solution that enables companies to integrate alternative payment methods in the automatic administrative processes. AEPP also opens up the opportunity to implement new customer services and to invoice efficiently.

With Aareal Meter, we have developed a product together with pixolus GmbH that, based on mobile scanning of energy meters, automates and speeds up clients' meter reading processes.

Aareal Connected Payments acts as a new invoicing solution to support e-mobility. Aareal Bank co-operates here with the platform provider smartlab.

In collaboration with the Group company plusForta GmbH, we have extended our total offering in rental security deposits to include the tenant deposit guarantee alternative. All the variants for managing rental security deposits are digitally available and integrated in our processes.

The digital solutions also include the acquisition of joint control of the objego start-up, a joint venture with ista Deutsche GmbH, offering software to private landlords with up to 250 units, allowing them to manage their rented apartments in an efficient and straightforward manner.

At present, around 4,000 corporate clients throughout Germany are using our process-optimising products and banking services. The segment's volume of deposits averaged at € 11 billion in the 2020 financial year (2019: € 10.7 billion) and was thus in line with our expectations. All in all, this reflects the strong trust our clients continue to place in Aareal Bank. Additionally, despite the challenging environment we were able to increase net commission income in the Consulting/Services Bank segment as planned to € 26 million (2019: € 23 million).

Aareon segment

Aareon is a provider of ERP software and digital solutions for the European property sector and their partners in Europe. It pursues a growth strategy. Key factors to its success are client orientation, the growth in digital solutions, further strengthening of the ERP systems and exploration of new relevant markets and related sectors associated with the property industry. In the course of Aareon's forward-looking orientation and further intensification of research and development, the focus will be on digital solutions.

The 2020 financial year – in particular the second quarter – was dominated by the Covid-19 pandemic. Aareon supported its clients throughout the crisis – also by providing special product and service offerings, as well as numerous webinars – enabling them to continue their business operations in digital form. Clients with a high level of digitalisation were already at an advantage here. Client events were conducted successfully online, to the extent possible, while larger events, such as the Aareon Congress in particular, as a German industry event, were cancelled and adapted to digital formats. In September, Aareal held the online industry event Aareon Live in Germany, with more than 1,600 registered participants. Despite the Covid-19 pandemic, sales revenue including the CalCon Group was increased to € 258 million (2019:

€ 252 million). At € 62 million, an adjusted EBITDA[1] was achieved that was more or less on a par with the prior-year level (2019: € 64 million) The original forecast (which excluded Covid-19 effects and the consolidation of CalCon Group) had targeted revenue of € 272 million to € 276 million and an adjusted EBITDA of between € 68 million and € 71 million. Compared to the original forecast, the Consulting business in particular declined due to Covid-19, which could only partially be offset by sales revenues of acquired CalCon Group. Maintenance and Software as a Service (SaaS) businesses were material drivers of revenue growth. Revenue growth for digital solutions totalled 19 % compared to the previous year. This marked increase is due, among other things, to further market penetration and to the acquisition of CalCon Group as at 1 January 2020.

Additional clients were acquired in the Germany, Austria and Switzerland (DACH) region for the Wodis Sigma ERP solution and for the new Aareon Wodis Yuneo product generation, which was launched in September. This resulted in higher licence revenues, even though the favoured version continues to be the one that uses Wodis Sigma and Wodis Yuneo as a service from the exclusive Aareon Cloud. Additional licenses for SAP® solutions and Blue Eagle also led to high licence revenues. Migration projects were continued remotely during the Covid-19 pandemic. The last migration projects from GES to other ERP solutions were concluded on 1 July 2020. As at 31 December 2020, Aareon discontinued GES operations in the Aareon IT centre as planned. Additional commercial property clients were acquired for the RELion ERP solution, resulting in higher licence and consulting revenue. The business with Aareon Cloud Services continued on its positive trajectory. BauSecura's insurance business was up on the previous year's level. In the international ERP business, recurring revenues in particular from maintenance and Software-as-a-Service-(SaaS) increased further as a result of client rollouts. This is reflected especially in the Netherlands, where the transformation of the business model to an SaaS operation gained momentum. The Dutch REMS ERP solution for the commercial property business was stable in terms of sales revenue and an important new client was rolled out as scheduled. The new release of Prem'-Habitat was launched on the market in France, with clients – including one major client – having opted for it already. Many sales successes were reported in the UK with new and existing clients – including one major key client. Sales activities were stepped up in the Nordic countries to acquire new clients. Consulting revenue was down on the previous year due to the Covid-19 pandemic, despite the growing demand for the "green" online consulting offering.

Digitalisation is becoming increasingly important for the property industry. The Covid-19 pandemic acted as a catalyst in this respect, with a growing number of clients enhancing their ERP systems with the addition of integrated digital solutions, thus developing their own digital ecosystem, so that business volumes with digital solutions continued to rise in 2020.

Demand remains strong in the DACH region and in the international business for the WRM (Workforce Relationship Management), CRM (Customer Relationship Management) and SRM (Supplier Relationship Management) solutions. The marketing of the Aareon Smart Platform, which was rolled out in the fourth quarter of 2019, continued. In the second quarter of 2020, Aareon announced the AI-based virtual assistant Neela (CRM solution) in Germany, and started marketing activities in the Netherlands, the UK and the Nordics. In a first stage, Neela was introduced as a chatbot. Neela facilitates an even more comfortable relationship between customers and property companies. In November 2019, Aareon had signed the contract to acquire CalCon with effect from 1 January 2020. The project for integrating the CalCon group was concluded in the first half of 2020.

With a view to potential inorganic growth, Aareon's management conducted a comprehensive screening process looking at potential acquisition targets

[1] "Earnings before interest, taxes, depreciation and amortisation" excluding strategic investments (venture and M&A activities) and non-recurring effects

and identified opportunities that are being pursued systematically with the Value Creation Programme. On 23 December 2020, Aareon announced the acquisition of 100 % of the shares in Arthur Online Ltd., London (Arthur). Arthur offers a cloud-based software solution for property management focused on the UK, which brings together property managers, property owners, tenants and contractors on a single platform. The company was acquired with effect from 29 January 2021.

Financial Position and Financial Performance

Financial performance

Group

Consolidated operating profit for the 2020 financial year came to € -75 million due to the impact of the Covid-19 pandemic and was thus significantly below our original forecast and the previous year's level of € 248 million.

At € 512 million, net interest income was down on the previous year (€ 533 million) and our original forecast of a slightly declining net interest income, mainly due to a decline in the loan and securities portfolios in the course of the year. This was attributable to the previous year's accelerated de-risking involving defaulted loans, a larger exposure to a single borrower and securities in Italy, as well as to lower new business in the first half of the year on account of the Covid-19 pandemic. In parallel with the portfolio growth, net interest income rose again at the end of the year and also includes a pro rata interest benefit from the TLTRO programme in the amount of € 11 million.

Loss allowance amounted to € 344 million and was therefore significantly higher than the previous year's figure (€ 90 million) and our original forecast of a slightly declining loss allowance, largely because of the adverse economic effects related to the Covid-19 pandemic. Based on the extended and further tightened global lockdown measures, the Bank has generally classified all loans for which liquidity support measures (payment deferrals and liquidity facilities) were granted as stage 2 as at 31 December 2020 and recognised loss allowance in the amount of the losses expected for the entire remaining term. The assumption that no signifi-

Consolidated net income of Aareal Bank Group

€ mn	1 Jan - 31 Dec 2020	1 Jan - 31 Dec 2019
Net interest income	512	533
Loss allowance	344	90
Net commission income	234	229
Net derecognition gain or loss	28	64
Net gain or loss from financial instruments (fvpl)	-32	1
Net gain or loss from hedge accounting	6	-4
Net gain or loss from investments accounted for using the equity method	1	1
Administrative expenses	469	488
Net other operating income/expenses	-11	2
Operating profit	**-75**	**248**
Income taxes	-6	85
Consolidated net income	**-69**	**163**
Consolidated net income attributable to non-controlling interests	5	2
Consolidated net income attributable to shareholders of Aareal Bank AG	-74	161

cant decrease in credit quality within the meaning of IFRS 9 has occurred is only made in exceptional cases when this is justified based on supportable information. Stage 3 loss allowance increased due to new loan defaults; causes for increases with respect of existing exposures included a deterioration of market values, particularly affecting shopping centres in the UK and individual exposures in the US. The scope of current valuation reviews within the portfolio particularly affected by the Covid-19 pandemic (including property types such as retail, hotels, and student housing) for the purpose of year-end valuation covered this portfolio almost completely; external valuations accounted for approximately 85 % of the lending volume. Overall, the valuation reviews were in line with our expectations from the third quarter of 2020, except for a few NPL cases (non-performing loans). No management overlay was required by the year-end. Moreover, the accelerated de-risking burdened the loss allowance in the second quarter with € 9 million.

Net commission income increased to € 234 million (2019: € 229 million) on the back of higher sales revenue at Aareon and in the Consulting/Services Bank segment. However, due to the Covid-19 pandemic, the increase was below our original forecast.

The net derecognition gain of € 28 million (2019: € 64 million) was attributable to market-driven effects from early loan repayments, and to repurchases in the Treasury business within the scope of market support. The higher figure for the previous year reflected structural adjustments to our securities portfolio following the acquisition of former Düsseldorfer Hypothekenbank AG (Düsselhyp).

At € -26 million (2019: € -3 million), the net result from financial instruments (fvpl) and from hedge accounting was also burdened by Covid-19. The decline was largely due to credit-risk induced measurement losses of defaulted property loans, which are reflected in the net gain or loss from financial instruments (fvpl).

In spite of rising expenses in connection with Aareon's growth, administrative expenses declined to € 469 million (2019: € 488 million), also due to cost savings incurred in connection with the Covid-19 pandemic, meaning that it came in below our original forecast of slightly increasing administrative expenses. The previous year's figure still included running costs and integration expenses in the amount of € 11 million incurred in conjunction with the integration of Düsselhyp.

Net other operating income/expenses of € -11 million (2019: € 2 million) was burdened by write-downs on properties held by the Bank in the amount of € -33 million, as a result of Covid-19.

All in all, the consolidated operating loss for the 2020 financial year totalled € 75 million, after a profit of € 248 million in 2019. Taking into consideration income from income taxes of € -6 million (positively influenced by the capitalisation of deferred taxes) and non-controlling interest income of € 5 million, consolidated net income attributable to shareholders of Aareal Bank AG amounted to € -74 million (2019: € 161 million). Assuming the pro rata temporis accrual of net interest payments on the AT1 bond, consolidated net income allocated to ordinary shareholders stood at € -90 million (2019: € 145 million). Earnings per ordinary share (EpS) amounted to € -1.50 (2019: € 2.42), and RoE before taxes -4.1 % (2019: 8.9 %). In our original forecast, we had assumed stable consolidated net income allocated to ordinary shareholders and EpS as well as RoE before taxes more or less on the same level as in the previous year.

Structured Property Financing segment

Operating profit in the Structured Property Financing segment amounted to € -99 million, due to the effects of the Covid-19 pandemic (2019: € 276 million).

Net interest income in the segment of € 474 million was down on the previous year (€ 549 million), mainly due to a year-on-year decline in the loan and securities portfolios. This was attributable to the previous year's accelerated de-risking involving defaulted loans, a larger exposure to a single borrower and securities in Italy, as well as to lower new business in the first half of the year on account of the Covid-19 pandemic. In parallel with the portfolio growth, net interest income rose again at the end of the year and also includes a pro rata interest benefit from the TLTRO programme in the amount of € 11 million. The adjusted transfer pricing and the increased interest rate on residual deposits of the Consulting/Services Bank segment from 1 January 2020 onwards led to a decline in net interest income in the Structured Property Financing segment (see Note 71 of the consolidated financial statements).

Loss allowance of € 344 million (2019: € 90 million) was recognised, largely due to the adverse economic effects related to the Covid-19 pandemic. Based on the extended and further tightened global lockdown measures, the Bank has generally classified all loans for which liquidity support measures (payment deferrals and liquidity facilities) were granted as stage 2 as at 31 December 2020 and recognised loss allowance in the amount of the losses expected for the entire remaining term. The assumption that no significant decrease in credit quality within the meaning of IFRS 9 has occurred is only made in exceptional cases when this is justified based on supportable information. Stage 3 loss allowance increased due to new loan defaults; causes for increases with respect of existing exposures included a deterioration of market values, particularly affecting shopping centres in the UK and individual exposures in the US. The scope of current valuation reviews within the portfolio particularly affected by the Covid-19 pandemic (including property types such as retail, hotels, and student housing) for the purpose of year-end valuation covered this portfolio almost completely; external valuations accounted for approximately 85 % of the lending volume. Overall, the valuation reviews were in line with our expectations from the third quarter of 2020, except for a few NPL cases. No management overlay was required by the year-end. Moreover, the accelerated de-risking burdened loss allowance in the second quarter with € 9 million.

The net derecognition gain of € 28 million (2019: € 64 million) was attributable to market-driven effects from early loan repayments, and to repurchases in the Treasury business within the scope of market support. The higher figure for the previous year reflected structural adjustments to our securities portfolio following the acquisition of former Düsseldorfer Hypothekenbank AG (Düsselhyp).

Structured Property Financing segment result

€ mn	1 Jan - 31 Dec 2020	1 Jan - 31 Dec 2019
Net interest income	474	549
Loss allowance	344	90
Net commission income	8	10
Net derecognition gain or loss	28	64
Net gain or loss from financial instruments (fvpl)	-32	1
Net gain or loss from hedge accounting	6	-4
Net gain or loss from investments accounted for using the equity method	2	1
Administrative expenses	227	254
Net other operating income/expenses	-14	-1
Operating profit	**-99**	**276**
Income taxes	-14	95
Segment result	**-85**	**181**

At € -26 million (2019: €- 3 million), the net result from financial instruments (fvpl) and from hedge accounting was also burdened by Covid-19. The decline was largely due to credit-risk induced measurement losses of defaulted property loans, which are reflected in the net gain or loss from financial instruments (fvpl).

Administrative expenses declined to € 227 million (2019: € 254 million), due to cost savings in connection with the Covid-19 pandemic. The previous year's figure still included running costs and integration expenses in the amount of € 11 million incurred in conjunction with the integration of Düsselhyp.

Net other operating income/expenses of € -14 million (2019: € -1 million) was burdened by write-downs on properties held by the Bank in the amount of € -33 million, as a result of Covid-19.

Overall, operating profit for the Structured Property Financing segment was € -99 million (2019: € 276 million). Taking into consideration income from income taxes of € -14 million (2019: € 95 million), which were positively impacted by the capitalisation of deferred taxes, the segment result amounted to € -85 million (2019: € 181 million).

Consulting/Services Bank segment

The year-on-year improvement in net interest income to € 39 million (2019: € -15 million) for the Consulting/Services Bank segment was due primarily to adjusted transfer pricing and the increased interest rate on residual deposits from 1 January 2020 onwards (see Note 71 of the consolidated financial statements). Net interest income continues to be burdened by the negative margins from the deposit-taking business due to the persistently low level of interest rates.

As planned, net commission income of € 26 million showed positive development (2019: € 23 million).

As a result of Covid-19, administrative expenses fell slightly to € 68 million (2019: € 73 million).

Overall, segment operating profit was € -3 million (2019: € -65 million). Taking income taxes into consideration, the segment result amounted to € -2 million (2019: € -44 million).

Aareon segment

Net commission income in the Aareon segment was € 213 million and increased slightly (including CalCon Group) despite the Covid-19 pandemic (2019: € 208 million).

Administrative expenses rose to € 188 million (2019: € 173 million), due to business expansion (including the CalCon Group) and strategic investments.

Consulting/Services Bank segment result

€ mn	1 Jan - 31 Dec 2020	1 Jan - 31 Dec 2019
Net interest income	39	-15
Loss allowance	0	0
Net commission income	26	23
Administrative expenses	68	73
Net other operating income/expenses	0	0
Operating profit	**-3**	**-65**
Income taxes	-1	-21
Segment result	**-2**	**-44**

Aareon segment result

€ mn	1 Jan - 31 Dec 2020	1 Jan - 31 Dec 2019
Net interest income	-1	-1
Loss allowance	0	0
Net commission income	213	208
Net gain or loss from financial instruments (fvpl)	0	0
Net gain or loss from investments accounted for using the equity method	-1	0
Administrative expenses	188	173
Net other operating income/expenses	4	3
Operating profit	**27**	**37**
Income taxes	9	11
Segment result	**18**	**26**

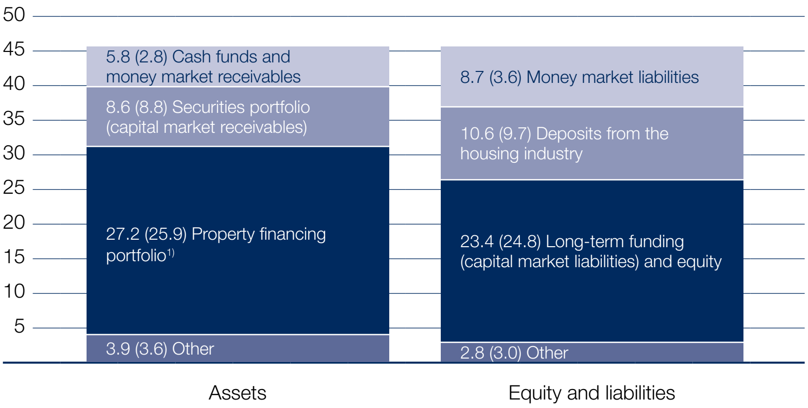
Overall, segment operating profit was € 27 million (2019: € 37 million). Taking income taxes into consideration, the segment result amounted to € 18 million (2019: € 26 million).

Financial position

Consolidated total assets of Aareal Bank Group increased to € 45.5 billion as at 31 December 2020 (31 December 2019: € 41.1 billion), especially reflecting the use of targeted longer-term refinancing operations (TLTROs): this led to increases in cash funds and money-market liabilities.

Statement of financial position – structure as at 31 Dec 2020 (31 Dec 2019)

€ bn



[1] Excluding € 0.3 billion in private client business (31 December 2019: € 0.4 billion) and € 0.3 billion in local authority lending business by the former Westdeutsche ImmobilienBank AG (WestImmo) (31 December 2019: € 0.4 billion), and excluding loss allowance

Cash reserve and money market receivables

The cash reserve and money market receivables position contains excess liquidity invested at short maturities. As at 31 December 2020, this comprised predominantly cash funds and deposits with central banks and money-market receivables from banks.

Property financing portfolio

As at 31 December 2020, the volume of Aareal Bank Group's property financing portfolio[2] stood at € 27.2 billion (2019: € 25.9 billion). Including former WestImmo's private client and local authority lending businesses, it amounted to € 27.8 billion. After a marked increase in the second half of the year, the volume was thus at the upper end of our target corridor of € 26 billion to € 28 billion.

Portfolio allocation by region and continent did not change significantly compared with the end of the previous year. Whilst the portfolio share of exposures in Eastern Europe rose by around 1.9 percentage points, it was down by around

[1] Excluding former WestImmo's private client business and local authority lending business

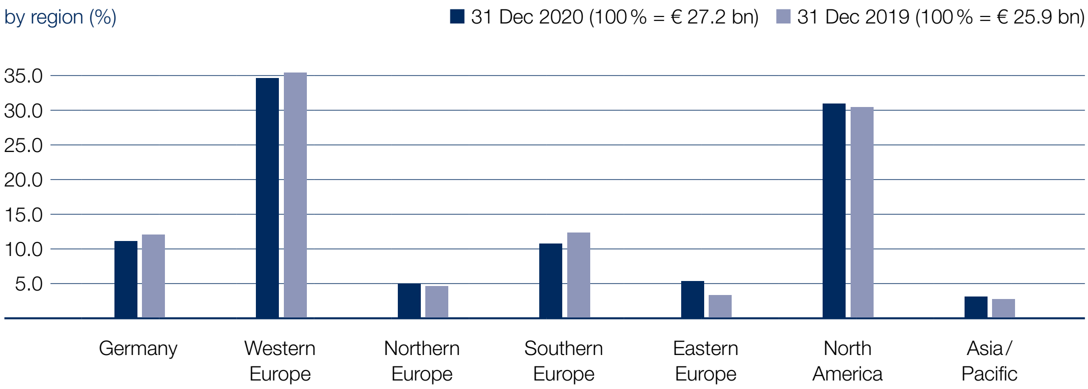
1.6 percentage points for Southern Europe, due to accelerated de-risking in Italy. It remained relatively stable for all other regions. The Covid-19 pandemic led to higher LtVs in most regions, especially in North America.

The breakdown of the portfolio by property type did not change significantly during the reporting period. The share of logistics properties increased by 3.3 percentage points compared to year-end 2019, whilst the share of retail properties was reduced by 2.7 percentage points. The share of office, hotel and residential properties, as well as other financings in the overall portfolio remained almost unchanged compared to year-end 2019. The Covid-19 pandemic led to higher LtVs, especially for hotel and retail property.

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

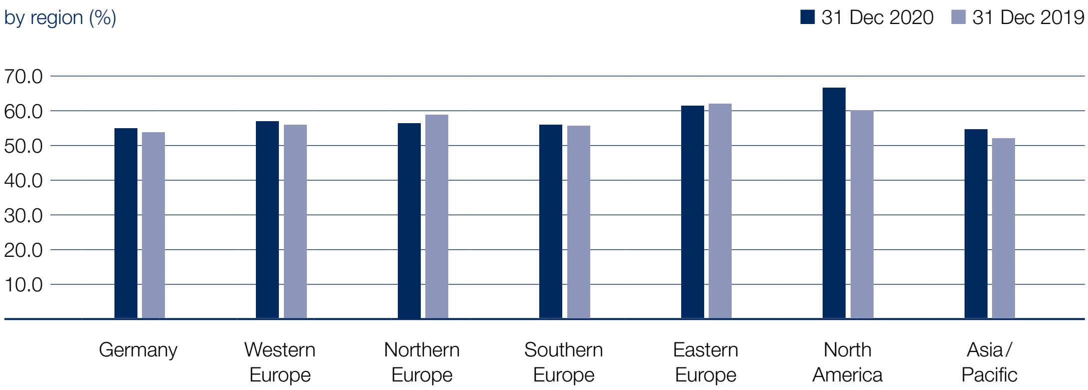
Property financing volume[1] (amounts drawn)

by region (%)



Average LTV of property financing[1]

by region (%)

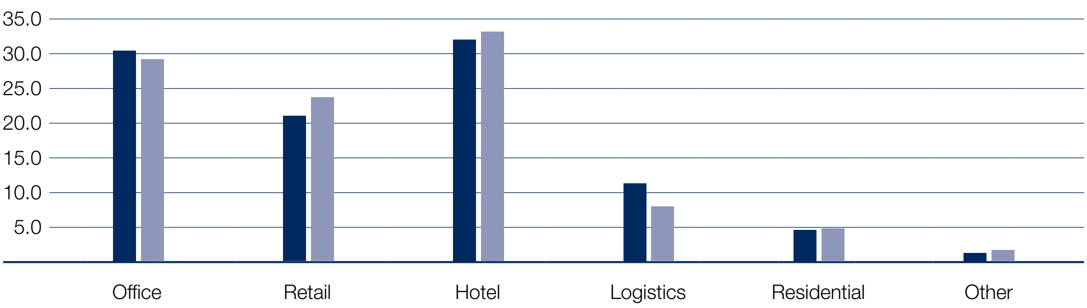


Note that the loan-to-value ratios are calculated on the basis of drawdowns and market values, including supplementary collateral with sustainable value, excluding defaulted property financings.

[1] Excluding former WestImmo's private client business and local authority lending business

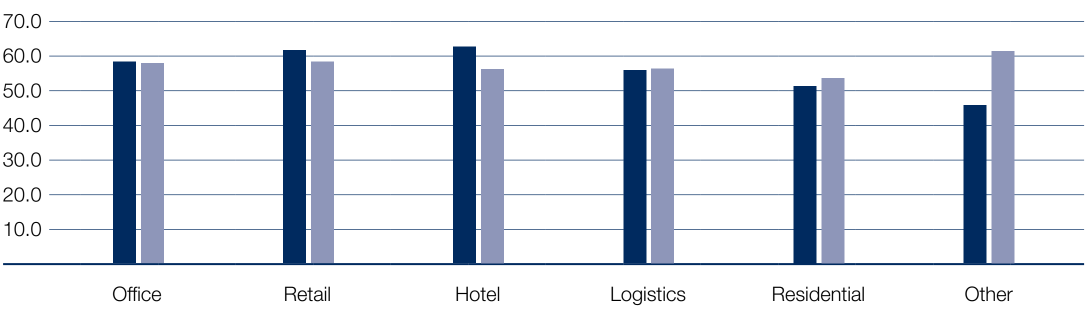
Property financing volume[1] (amounts drawn)

by type of property (%)



Average LTV of property financing[1)]

by type of property (%)



Note that the loan-to-value ratios are calculated on the basis of drawdowns and market values, including supplementary collateral with sustainable value, excluding defaulted property financings.

[1)] Excluding former WestImmo's private client business and local authority lending business

Treasury-Portfolio

As explained below, Aareal Bank holds a high-quality portfolio, which fulfils two major tasks as part of the overall management of the Bank. On the one hand, the bulk of the securities are held for the liquidity portfolio, which accounts for a major part of the liquidity reserve from both the economic and normative perspective of risk-bearing capacity. In addition to the liquidity portfolio, part of the Treasury portfolio is also used as a collateral portfolio. We define this mainly as the securities and promissory note loans that are used as collateral for the two Pfandbrief programmes.

Key aspects taken into account for portfolio management are good credit quality and the related value stability, as well as a high degree of liquidity, depending on the intended use.

As at 31 December 2020, the total nominal volume of the Treasury portfolio[2)] was € 7.2 billion (31 December 2019: € 7.3 billion).

The portfolio comprises the asset classes public-sector borrowers, covered bonds and bank bonds (financials), with the public-sector asset class accounting for the biggest portion of the portfolio (currently approximately 98 %).

[2)] As at 31 December 2020, the securities portfolio was carried at € 8.6 billion (31 December 2019: € 8.8 billion).

The high creditworthiness requirements are also reflected in the rating breakdown in the portfolio. 99.9 % of the portfolio has an investment grade rating[1], and 83 % of the positions have an AAA to AA- rating (2019: 78 %).

The portfolio currently comprises almost exclusively (98 %) securities denominated in euros and its average remaining term on the reporting date was 6.2 years.

Given the high requirements as regards the liquidity of the positions as part of their use for the liquidity portfolio, 94 % of the portfolio can be pledged as collateral with the ECB and 79 % fulfils the requirements for "High Quality Liquid Assets" (as defined in the Liquidity Coverage Ratio (LCR)).

Financial position

Money-market liabilities and deposits from the housing industry

Generally, in addition to deposits from housing industry clients and institutional investors, Aareal Bank also uses interbank and repo transactions for short-term refinancing, the latter being used primarily to manage liquidity and cash positions.

As at 31 December 2020, Aareal Bank had € 10.6 billion at its disposal in deposits generated from the business with the housing industry (31 December 2019: € 9.7 billion). Money market liabilities, including targeted longer-term refinancing operations (TLTROs) of Deutsche Bundesbank, amounted to € 8.7 billion (31 December 2019: € 3.6 billion).

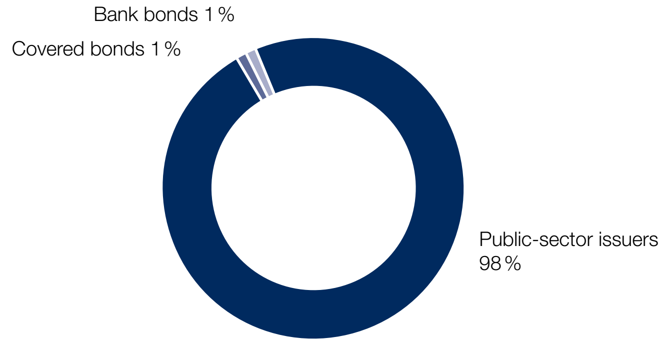
Long-term funding and equity

Funding structure

Aareal Bank Group continues to be solidly funded, a development visible by its major share of long-term funding. This encompasses registered and bearer Pfandbriefe, promissory note loans, medium-term notes, other bonds and subordinated issues. The latter include subordinated liabilities and Additional Tier 1 (AT1) bond.

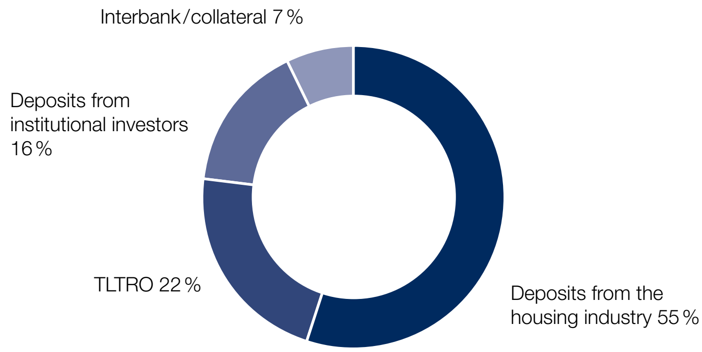
Treasury portfolio as at 31 December 2020

%　　Total volume (nominal): € 7.2 bn



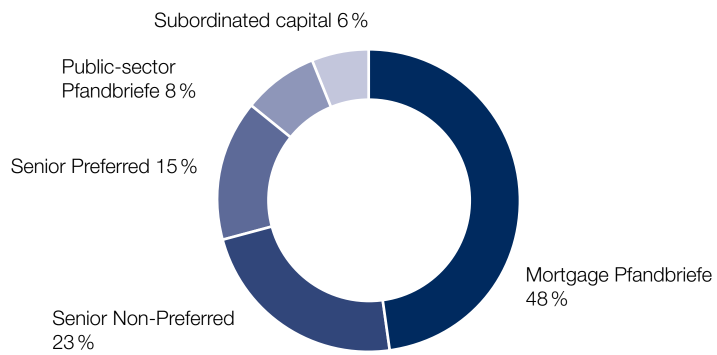
Money market funding mix as at 31 December 2020

%　　Total volume: € 19.3 bn



Capital market funding mix as at 31 December 2020

%　　Total volume: € 19.1 bn

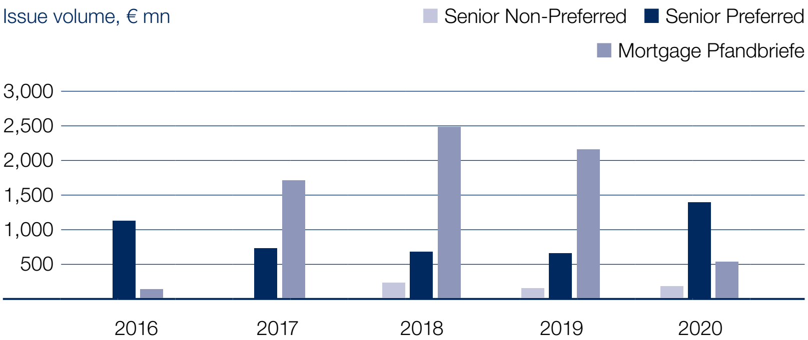


[1] The rating details are based on the composite ratings.

As at 31 December 2020, the notional volume of the long-term refinancing portfolio was € 19.1 billion. The book values of the long-term refinancing portfolio totalled € 20.7 billion.

Issuing activities – 2016 to 2020

Issue volume, € mn



Refinancing activities

Throughout the financial year 2020, Aareal Bank Group was able to place € 2.1 billion on the capital market, comprising € 0.5 billion of Pfandbrief, € 1.4 billion of senior preferred and € 0.2 billion of senior non-preferred issues. In addition, the bank issued Pfandbriefe in the amount of € 0.9 billion which it took onto its own books. Aareal Bank Group raised € 4.3 billion as part of TLTRO 3.

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

Equity

Aareal Bank Group's total equity as disclosed in the statement of financial position amounted to € 2,967 million as at 31 December 2020

Regulatory indicators[1)]

	31 Dec 2020[2)]	31 Dec 2019
€ mn		
Common Equity Tier 1 (CET 1)	2,286	2,191
Tier 1 (T1)	2,586	2,491
Total capital (TC)	3,395	3,343
%		
Common Equity Tier 1 ratio (CET 1 ratio)	18.8	19.6
Tier 1 ratio (T1 ratio)	21.3	22.3
Total capital ratio (TC ratio)	28.0	29.9
Common Equity Tier 1 ratio (CET 1 ratio) – Basel IV (fully phased-in) –[3)]	13.1	13.5
Common Equity Tier 1 ratio (CET 1 ratio) – Basel IV (phased-in) –[3)]	17.3	17.1

[1)] Aareal Bank AG utilises the rules set out in section 2a of the KWG in conjunction with Article 7 of the CRR, pursuant to which regulatory indicators of own funds may only be determined at Group level. In this respect, the following disclosures relate to Aareal Bank Group.

[2)] 31 December 2019: excluding dividend for 2019 from initial proposal on the appropriation of net retained profit and including a pro-rata temporis deferral of net interest on the AT1 bond
31 December 2020: including dividend for 2019 from initial proposal on the appropriation of net retained profit and less a proposed dividend of € 1.50 per share in 2021 and pro-rata temporis deferral of net interest on the AT1 bond. The 2021 dividend payment of € 1.50 for 2020 would need to be made in two steps. In compliance with the requirements published by the European Central Bank (ECB) on 15 December 2020, the distributable amount is calculated at € 0.40 per share. The Management Board plans to submit a corresponding proposal for the appropriation of profits to the ordinary Annual General Meeting in May 2021. Depending on further economic developments, regulatory requirements, the Bank's capital position and its risk situation, a subsequent Annual General Meeting, which could possibly take place during the fourth quarter of 2021, could then decide on the intended remaining payout of € 1.10 per share.
The SREP recommendations concerning the NPL inventory and the ECB's NPL guidelines for exposures newly classified as NPLs, as well as the "CRR Quick fix" as of 30 September 2020, were taken into account.

[3)] Underlying RWA estimate, incorporating the higher figure determined using the revised AIRBA or the revised CRSA (phased-in), based on the final Basel Committee framework dated 7 December 2017; the calculation of the material impact upon Aareal Bank is subject to the outstanding EU implementation as well as the implementation of additional regulatory requirements (CRR II, EBA requirements etc.).

(31 December 2019: € 2,861 million), comprising € 300 million for the Additional Tier 1 (AT 1) bond. Retained earnings increased especially due to the sale of a minority stake in Aareon and the fact that no dividend was paid for the previous year. Please also refer to the statement of changes in equity, and to our explanations in Note 58 of the consolidated financial statements.

The Common Equity Tier 1 ratio (CET1 ratio) – Basel IV (estimated) – continued to lie above the target value of 12.5% in the year under review.

Our Employees

The year under review brought major changes for our employees too. As a part of the Business Continuity Management, the pandemic led to the announcement of a mandatory working-from-home order at all German locations in March 2020 as part of the emergency planning due to the Covid-19 pandemic. Following a first working-from-home test phase in mid-March 2020, almost all employees were able to continue working seamlessly from home, thus maintaining operations in this way throughout the entire lockdown. Since the end of the first lockdown, we introduced a rolling attendance system. Implemented together with a strict hygiene concept, this allowed employees to work partially at the office again. Where appropriate and compatible with the local regulations, the emergency planning was implemented at our international locations correspondingly. At the start of the first lockdown, our employees quickly organised themselves with digital tools to facilitate cooperation. These experiences have shown us that we can successfully make it through the crisis using new ways of cooperation.

Qualification and training programmes

Qualified and motivated employees make a decisive contribution to our Company's economic performance and are thus a key factor in 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. In line with the corporate strategy, the human resources policy is continuously developed in a targeted way. Aareal Bank Group supports employees in change processes, and promotes lifelong professional learning.

The Bank's training and education programme was restructured in the year under review. The result of this restructuring is Learning@Aareal – a learning provision of which 50% the content is available in digital format, therefore facilitating permanent learning regardless of time or location. Learning@Aareal supports employees in performing their current tasks through targeted offers that are focused on the company and personal strategy, Aareal Bank's USP (unique selling point) and a consistent skill matrix. Learning@Aareal also helps to improve the balance between work and family life, which is one of Aareal Bank's core concerns. Learning@Aareal is integrated in Aareal Bank's strategic development approach, which uses a skill matrix as the basis

Employee data as at 31 December 2020

	31 Dec 2020	31 Dec 2019	Change
Number of employees at Aareal Bank Group	2,982	2,788	7.0%
Years of service	10.8 years	11.6 years	-0.8 years
Staff turnover rate	4.5%	4.6%	-2.2%

The overview of employee key indicators in the "Responsibility" section of the Company's website (www.aareal-bank.com/en/responsibility/reporting-on-our-progress/) provides more information, including the breakdown by gender, age and region.

for talent development at an organisational level. By linking skill matrix, Learning@Aareal, clear selection procedures and management and expert career paths, we are facilitating the sustainable development of our employees. Networking knowledge contributes to the permanent development of the organisation and guarantees that specialist knowledge is secured to sustainable succession planning. Besides the conceptual new approach, tried and tested formats for specific and generic training measures – for example, in the form of qualification programmes for (agile as well as traditional) project management, were pursued as well as supporting measures related to organisational and team development. A programme for newly appointed executive staff was also launched for the first time.

Personnel development at Aareon continued in digital format during the Covid-19 pandemic. An e-learning management system was introduced, which offered training on housing industry topics from EBZ Bochum and on management, agile project management, soft skills, communication and health. Other training measures included an IT security boot camp and special consulting training sessions.

A digital language learning portal helped to further build language and communications skills on both Aareal Bank and Aareon, within the scope of internationalisation. This learning portal allows all employees throughout the Group to improve their language skills, anywhere (even at home) and at any time.

The fourth cross-mentoring programme was initiated at Aareal Bank and Aareon. Cross-mentoring describes the targeted exchange of employees from different companies; it is a personnel development measure aimed at promoting knowledge transfer.

Promoting the next generation

Promoting the next generation through training is a central element of Human Resources work at Aareal Bank Group. The specialist knowledge required in our business segments requires us to invest continuously – and in a targeted manner – in training the next generation.

Aareal Bank's programme aimed at promoting the next generation comprises not only trainee programmes, but also the dual studies Business Informatics and Business Administration in cooperation with DHBW Mannheim and RheinMain University, as well as the on-the-job Bachelor's degree Business Administration in cooperation with the University of Applied Sciences Mainz. For the first time, Aareal Bank offered vocational training in IT application development in 2020, in cooperation with other companies in the region. Aareal Bank closely collaborates with universities in the region through various initiatives. In addition to the successful transfer of specialist knowledge and the gathering of new perspectives, the specific measures taken at Aareal Bank to empower young professionals have already reduced the average age.

Besides training programmes, Aareon offers the dual courses of study "Business information systems" and "Media, IT and management" as well as various vocational training opportunities for office managers, IT applications developers, or IT systems integrators.

In the course of the measures for promoting the next generation, Aareon supported the JOBLINGE initiative aimed at socially deprived young citizens. First participants of this programme have meanwhile embarked on their training. Aareon also held two applicant training courses for participants of the JOBLINGE initiative. To promote trainees and science, Aareon is cooperating with several universities, offers placements and supports students as part of the German scholarship of the Johannes Gutenberg University in Mainz.

Remuneration system

In addition to a fixed remuneration component, all permanent employees receive performance-based variable remuneration. 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.

Work-life balance

Aareal Bank Group places great importance on supporting its employees to achieve compatibility between career and family. This is emphasised by a broad range of dedicated support services such as partnerships with childcare institutions or service providers for the provision of private childcare, holiday programmes for employees' children, the availability of parent-child workrooms, flexible working policies, part-time positions and the option of mobile working or alternating teleworking for all employees. Another component of improving the work-life balance of the employees consists of services that make it easier to combine working life with the care of close relatives. This includes, among other things, the offer of counselling and support in the event of illness as well as nursing care for close relatives (available throughout Germany), as well as the option of participating in various training courses in the Bank for better compatibility between family, care and work.

As an innovative company that promotes the digital transformation process holistically and manages the related process of change for its employees, Aareon had already numerous measures as part of the "work4future" project concluded in 2020. The works agreement on mobile working was implemented in 2019, increasing our employees' work flexibility. A digital collaboration tool was introduced for internal communications, which brought employees even closer together in the Covid-19 pandemic, despite social distancing. This was supported through various campaigns and regular posts by members of the Management Board. The room concepts were developed further in line with the requirements of day-to-day cooperation, to become even more innovative and successful in this context.

Health

In order to verify the effectiveness and continuous improvement of occupational safety management, occupational safety committees meet quarterly. These include the respective company doctor and occupational safety specialists, in addition to various company officers.

In order to protect and promote the health of its employees in a targeted manner, Aareal Bank Group offers a comprehensive range of health-promoting measures in the areas of information, prophylaxis, exercise and ergonomics, nutrition, mental health and relaxation that are always based on employees' current needs. Despite the restrictions imposed by the pandemic in the reporting year, successful formats continued to be applied in the Bank. These included preventative, individual health consultations on various topics, consultations with the company doctor including screenings, flu vaccinations, skin screenings, colorectal cancer screening and ergonomics advice at the work place, massages (until the lockdown), as well as business yoga that was continued digitally. In company health management, Aareon implemented numerous measures for supporting employees in the digital working worlds in 2020 – this was particularly relevant against the background of the Covid-19 pandemic.

Risk Report

Aareal Bank Group Risk Management

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. This economic motivation for a highly-developed risk management system is continuously increased by extensive regulatory requirements for risk management.

Aareal Bank regularly reviews the appropriateness and effectiveness of its corporate governance systems (including risk governance systems).

Given the Covid-19 pandemic, the various processes and systems affected were reviewed right at the start of the pandemic. Management has thus responded to the Covid-19 crisis in a comprehensive manner. The Pandemic Committee established continuously ascertained (IT) operations, including required hygiene and distancing rules. Technical equipment has proven to be effective during the crisis, which involved longer periods of working from home. Specific Covid-19 scenarios were developed at an early stage, in order to simulate the potential impact applying different parameters. Besides an event-driven review of the Risk Appetite Framework and the credit risk strategies, methods used to determine scenario assumptions for risk management of the property finance portfolio were extended. Reporting frequencies were adjusted as required. The prevailing situation was discussed continuously with all affected stakeholders in the respective bodies.

Aareal Bank also includes sustainability risks – so-called ESG risks (environmental, social and governance) – in its risk management. Fundamentally, Aareal Bank considers sustainability risks to include cross-species risks and risk drivers that are influenced directly or indirectly by environmental or social issues, or by monitoring processes. All material sustainability risks were able to be classified as a form of existing financial and non-financial risks. In line with this, they are managed implicitly as part of the risk types under which they are classified.

Risk management – scope of application and areas of responsibility

Aareal Bank AG, as the parent entity of the Group, has implemented extensive systems and procedures to monitor and manage the Group's risk exposure.

Uniform methods and procedures are deployed to monitor material risks generally associated with banking business across all entities of Aareal Bank Group. Specific risk monitoring methods have been developed and deployed to suit the relevant risk exposure at the subsidiaries. In addition, risk monitoring for these subsidiaries is carried out at Group level via the relevant control bodies of the respective entity, and equity investment risk controlling.

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

The Management Board formulates the business and risk strategies, as well as the so-called Risk Appetite Framework. For this purpose, "risk appetite" means the maximum risk exposure where the Bank's continued existence is not threatened, even in the event of risks materialising. For individual business units (the "First Line of Defence"), the Risk Appetite Framework defines guidelines for the independent and responsible handling of risks.

The risk monitoring function (the "Second Line of Defence") regularly measures utilisation of risk limits, and reports on the risk situation. In this context, the Management Board is supported by the Risk Executive Committee (RiskExCo). The RiskExCo develops proposals for resolutions in line with delegated tasks, and promotes risk communications and a risk culture within the Bank. The risk management system was supplemented by a recovery plan, in line with regulatory requirements, which comprises the definition of threshold values for key performance indicators – both from an economic and a normative perspective. These are designed to ensure that any negative market developments having an impact upon our business model are identified at an early stage and corresponding action is taken in order to safeguard the sustained continuation of business operations. Risk Controlling is responsible for monitoring financial risks at portfolio level, whilst the Non-Financial Risk division exercises this function for non-financial risks. Both divisons report directly to the Group Chief Risk Officer (GCRO).

On top of this, Group Internal Audit (as the "Third Line of Defence") reviews the organisational structure and procedures, as well as risk processes

Type of risk	Risk management	Risk monitoring
Overall responsibility: Management Board and Supervisory Board of Aareal Bank AG		
Loan loss risks		
Property Financing	Loan Markets & Syndication Credit Risk Project & Credit Portfolio Management Credit Transaction Management Workout	Risk Controlling Second Line of Defence (NPL)
Treasury business	Treasury	Risk Controlling
Country risks	Treasury Credit Risk Credit Transaction Management	Risk Controlling
Interest rate risk in the banking book (IRRBB)	Treasury, Asset-Liability Committee	Risk Controlling Finance & Controlling
Market risks	Treasury, Asset-Liability Committee	Risk Controlling
Operational risks	Process owners	Non-Financial Risks
Investment risks	Group Strategy	Risk Controlling Finance & Controlling Controlling bodies
Property risks	Aareal Estate AG	Risk Controlling
Business and strategic risks	Group Strategy	Risk Controlling
Liquidity risks	Treasury	Risk Controlling
Process-independent monitoring: Internal Audit		

– including the Risk Appetite Framework – and assesses their appropriateness. Moreover, internal processes provide for the involvement of the Compliance function whenever there are facts which are compliance-relevant.

In order to efficiently perform its control function, amongst other measures, the Supervisory Board has established a Risk Committee, whose responsibility includes the risk strategies as well as the management and monitoring of all material types of risk.

Strategies

The business policy set by the Management Board, and duly acknowledged by the Supervisory Board, provides the conceptual framework for Aareal Bank Group's risk management. The Risk Appetite Framework, which also outlines the key elements of the risk culture put in place, is defined consistently with the business strategy and building on the defined risk appetite. Taking the Risk Appetite Framework as a basis, and strictly considering the Bank's risk-bearing capacity, we have formulated detailed strategies for managing the material types of risk, in terms of capital as well as liquidity. Taken together, these represent the Group's risk strategy. 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 Group. 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.

The business strategy, the Risk Appetite Framework and the risk strategies are subject to review on an ongoing basis, and are updated if necessary. In the wake of the pandemic and the associated macro-economic impact, an extraordinary review of risk strategies was carried out in 2020. Besides the regular review (and, if appropriate, adjustment) of the business strategy (and consequently, the Group risk strategy), the Bank's risk-bearing capacity and its material risk models are validated at least once a year. For this purpose, the appropriateness of risk measurement methods, processes, and risk limits is examined in particular. During the financial year under review, the strategies were adopted by the Management Board, duly noted, and approved by the Supervisory Board.

The Bank has defined escalation and decision-making processes to deal with limit breaches. Risk Controlling prepares timely and independent risk reports for the management.

Aareal Bank Group maintains a decentralised Internal Control System (ICS), with control activities and results being outlined in the Written Set of Procedural Rules. These describe individual processes of divisions, subsidiaries, or other units. Internal controls may run upstream, downstream, or in parallel to workflows; this applies both to automatic control and monitoring functions as well as to the respective manual steps. Accordingly, the ICS comprises the entire universe of control activities; its objective is to ensure that qualitative and quantitative standards are adhered to (compliance with legal or regulatory requirements, with limits etc.).

The appropriateness and effectiveness of controls is reviewed on an event-driven basis; in any case, at least once a year. The results are discussed with the corresponding units within the Second and Third Lines of Defence (Risk Controlling, Compliance and Internal Audit), and reported to the Management Board and the Supervisory Board. In the event of any irregularities or violations, depending on the severity of the event, the Management Board (as well as the Supervisory Board, if appropriate) must be notified without delay, so that adequate measures or audit activities can be initiated at an early stage.

Risk-bearing capacity and risk limits

The Bank's ability to carry and sustain risk (as determined within the framework of the Internal Capital Adequacy Assessment Process (ICAAP)) is a core determining factor governing the structure of its risk management system. To ensure its uninterrupted risk-bearing capacity, Aareal Bank Group has adopted a dual management approach comprising two complementary perspectives: the normative and the economic perspective.

The normative perspective aims to ensure Aareal Bank Group's ability to fulfil all of its regulatory requirements over a multi-year period. This perspective thus accounts for all material risks which may impact upon relevant regulatory indicators over the multi-year planning period.

The normative ICAAP perspective is embedded into Aareal Bank Group's planning process, which – in particular – also includes capital planning. Group planning covers three planning years, it comprises both baseline and adverse scenarios. Results of Group planning are shown as a projected consolidated income statement for Aareal Bank Group. Planning also encompasses the balance sheet structure, as well as key regulatory indicators, plus additional internal management indicators.

Besides the planning process itself, intra-year computation adjustments to Aareal Bank Group's planning process also included the ongoing monitoring of management indicators as well as checking whether limits in the normative perspective were being complied with. Management indicators in the normative perspective (which are being monitored, and for which limits have been set) comprise various regulatory ratios.

We are using the ICAAP economic perspective, whose purpose is to safeguard Aareal Bank Group's economic substance and thus, in particular, to protect creditors against economic losses. We predominantly employ proprietary procedures and methods (agreed upon with regulators) in order to identify and quantify potential economic losses, and to determine the required capital backing.

The purpose of internal capital is to serve as a risk-bearing component under the economic perspective. Within Aareal Bank Group, the current regulatory Tier I capital serves as the basis for determining economic aggregate risk cover. Accordingly, available internal capital comprises Common Equity Tier I (CET1) capital, supplemented by Additional Tier I (AT1) capital. Tier 2 capital, as well as projected results to be incurred during the risk analysis horizon, are not taken into account.

Moreover, the value-oriented approach adopted under the economic perspective requires suitable adjustments to be made to regulatory Tier I capital, in order to bring aggregate risk cover into line with the economic assessment. Specifically, this may entail adjustments regarding conservative valuation, hidden encumbrances, or a management buffer.

Aareal Bank Group consistently applies a period of 250 trading days as a risk analysis horizon, as well as for the holding period as part of risk models under the economic perspective. To the extent that risks are measured on the basis of quantitative risk models, a uniform observation period of at least 250 trading days (or at least one year) is applied to the risk parameters used. The appropriateness of model assumptions is verified within the scope of validating the corresponding risk models and parameters.

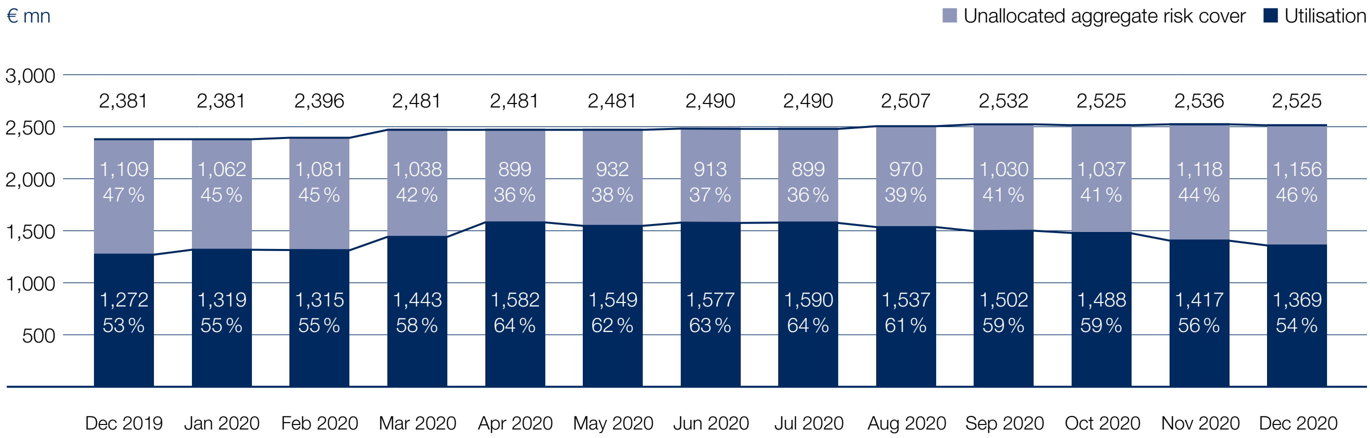
Looking at correlation effects between material types of risk within the framework of the economic ICAAP perspective, Aareal Bank Group has prudently opted for aggregation of risk levels; accordingly, no risk-mitigating correlation effects are being taken into account. Where we measure risks on the basis of quantitative risk models for the purposes of calculating risk-bearing capacity, these are based on a confidence interval of 99.9 %.

Limits for specific risk types are determined in such a manner that aggregate limits do not exceed economic aggregate risk cover, less a risk buffer designed to cover risks not explicitly covered by limits (e.g. those risks which cannot be sensibly quantified), and to also absorb other fluctuations of internal capital over time. Individual limits are set on the basis of existing risk exposures and historical levels of potential risks, and to an extent that is in line with the Bank's business and risk strategy. Specific limits have been set in a way that

Risk-bearing capacity of Aareal Bank Group (ICAAP – economic perspective)

€ mn	31 Dec 2020	31 Dec 2019
Tier 1 (T1) capital	2,586	2,491
Economic adjustments	-61	-110
Aggregate risk cover	**2,525**	**2,381**
Utilisation of aggregate risk cover		
Loan loss risks	637	525
Interest rate risk in the banking book (IRRBB)	68	93
Market risks	415	360
Operational risks	102	123
Investment risks	35	30
Property risks	76	60
Business and strategic risks	36	81
Total utilisation	**1,369**	**1,272**
Utilisation (% of aggregate risk cover)	**54 %**	**53 %**

Utilisation of aggregate risk cover during the course of 2020



each limit is sufficient for utilisation in line with planned business development, as well as for common market fluctuations.

A detailed monthly report provides information regarding the utilisation of individual limits for the material types of risk, as well as on the overall limit utilisation. These are being monitored as part of daily reporting. No limit breaches were detected during the period under review. Higher market volatility caused by the Covid-19 pandemic triggered isolated transgressions of early warning thresholds: this indicates that the limit system is adequately calibrated and shows its steering effect, in the sense of being responsive to significant changes in overall conditions. Corresponding countermeasures have been taken; the overall utilisation of risk cover shows that capitalisation is adequate.

Utilisation of aggregate risk cover developed during the period under review as shown above.

Since risk cover potential is an inadequate measure to assess the risk-bearing capacity for liquidity risk, we have defined special tools within the framework of the Internal Liquidity Adequacy Assessment Process (ILAAP) for managing this type of risk. These tools are described in detail in the section "Liquidity risks".

Stress testing

Within the scope of ICAAP and ILAAP, scenario analyses are carried out in all perspectives, as a core element of our risk management system. This involves conducting stress tests for all material risks, using both 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 the crisis affecting financial markets and the economy, which broke out in 2007, on individual types of risk and aggregate risk is analysed within the scope of a historical scenario. In the hypothetical scenario, current potential developments are derived from factors such as political developments, and are combined with significant macro-economic deterioration. The stress testing methodology implemented also takes into account the impact of any risk concentrations. Stress scenarios are analysed both from an economic and a normative perspective, with the respective cross-relationships being taken into consideration – meaning that any economic risks which may materialise (from a normative view) over the analysis period being incorporated in the normative perspective, unless they are sufficiently covered already.

The Management Board and the Supervisory Board are informed of the results issued by the stress analyses on a quarterly basis.

Lending business

Division of functions and voting

Aareal Bank Group's structural organisation and business processes consider regulatory requirements regarding the organisational structure and procedures 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 Schedule of 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 RiskExCo, which has delegated authority to the Heads of Risk Controlling, Credit Transaction Management and Credit Portfolio Management (organisational units which are independent of Sales units), is responsible for 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, 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 shortened significantly. Furthermore, the risk assessment results influence pricing.

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.

A CRE Credit Risk Committee (CRC) has been established in order to enhance the Bank's procedures for the early detection of risks. The CRC promotes the risk culture by identifying and addressing risk-relevant issues concerning individual credit exposures; the committee is also involved in each credit exposure with mandatory rating that is subject to higher risk exposure. Specifically, the CRC decides upon the exercise of discretion regarding classification of exposures as "normal", "intensified" or "problem loan" handling, as well as approval of action plans. The transfer of know-how is enhanced through the cross-divisional representation on the CRC. Contractual measures related to Covid-19 – such as the waiver of certain agreements, deferrals of repayments, or the provision of liquidity facilities – are being reported to the Management Board on a regular basis, and closely monitored.

Extensive IT resources are deployed to identify risk positions, and to monitor and assess risks. Overall, the existing set of tools and methods enables the Bank to adopt 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. Responsibility for development, quality assurance, and monitoring implementation of risk classification procedures, and for annual validation, lies with two separate divisions outside the Sales units which are independent from each other.

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

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.

In this context, PD and LGD procedures are also applied for accounting purposes, for determining model-based loss allowance. Concerning the scenario analyses to be taken into account when determining individual LGDs, we applied an updated scenario mix, going beyond the customary process. This probability-weighted scenario mix reflects the uncertainties as to how the Covid-19 pandemic will develop further and supplements our baseline scenario (swoosh) with the addition of divergent developments over an observation period of three years.

The expected loss (EL) in the event of default of an exposure is determined as the product of PD, LGD and EAD. 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 Group 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 Group 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 Credit Transaction Management and Risk Controlling divisions. Beyond this, Finance & Controlling 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"). Treasury is also responsible for asset/liability management, and for managing the Bank's market and liquidity risk exposures. In addition, we have established an Asset-Liability Committee (ALCO), to develop strategies for the Bank's asset/liability management and proposals for their implementation. The ALCO, 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.

Credit Transaction Management 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/master agreements.

To assess counterparty credit risk in the trading business, Credit Transaction Management 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 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 Group's overall risk exposure from trading activities, in terms of scope and structure.

Change processes (as defined in section AT 8 of the MaRisk) are consistently measured via Group-wide framework directives, with the RiskExCo involved in all cases. 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, as well as determining further action to be taken. In the event of counterparty or issuer default, the RiskExCo will be involved in devising 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.

Loan loss risks

Definition

Aareal Bank defines loan loss risk as the risk of losses being incurred due to (i) a deterioration in a business partner's credit quality (migration risk); (ii) a business partner defaulting on contractual obligations; (iii) collateral being impaired; or (iv) 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's credit risk strategy sets out all material aspects of the Group's credit risk management and policies. The credit risk strategy serves as a strategic guideline for dealing with each respective category of risk within Aareal Bank Group; it also provides a binding, overarching framework applicable to all divisions.

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. The Bank also includes sustainability risks, to the extent that they are relevant for the assessment. The associated process is instigated by senior management, and implemented by Risk Controlling, which submits a proposal, which has been agreed upon with all divisions to senior management. The credit risk strategy adopted is subsequently discussed by the Supervisory Board.

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. Given the changed economic conditions due to the Covid-19 pandemic, we have thus completed an event-driven review and update, which included stricter requirements for new business involving those types of property particularly affected by the Covid-19 pandemic.

Risk measurement and monitoring

Regulatory requirements are taken into account for the organisation of operations and workflows in the credit and trading businesses.

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

Aareal Bank employs different risk classification procedures tailored to the requirements of the respective type of business for the initial, regular, or event-driven assessment of counterparty credit risk. Forward-looking as well as macro-economic information is taken into consideration for risk classification procedures, and in the valuation of collateral. The respective procedures and parameters are subject to regular review and adjustment. Responsibility for development, quality assurance, and monitoring implementation of procedures, is outside the Sales units.

Against the background of the Covid-19 pandemic, special attention is currently paid to macro-economic forecasts. In the context of this ongoing review, we also rely on projections published by the ECB, apart from those issued by our usual data providers. Yet estimation uncertainties are currently much higher than usual, as the pandemic has provoked a situation unprecedented in recent history. Data and experience are therefore both lacking.

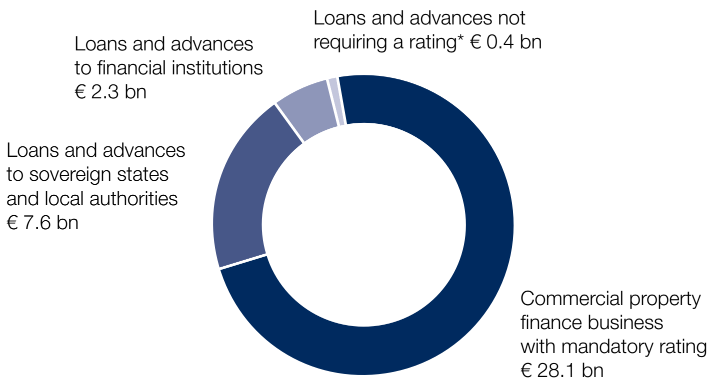
Methods used to measure, control and monitor concentration and diversification effects on a portfolio level include two different credit risk models. Based on these models, the Bank's decision-makers are regularly informed of the performance and risk content of property financing exposures, and of business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

Within the process-oriented monitoring of individual exposures, the Bank uses various tools to monitor exposures on an ongoing basis: besides the tools already described, this includes rating reviews, the monitoring of payment arrears, and the regular, individual analysis of the largest exposures. The intensity of loan coverage is oriented upon the credit risk exposure.

Against the background of the Covid-19 pandemic, Aareal Bank was in close contact with most property financing clients with mandatory rating, and has amended contractual arrangements to clients' updated business plans to the extent necessary and possible. Given the lockdown, this primarily affected financings of hotels and shopping centres, as well as involving waivers of certain contractual agreements without impact on payments (covenants). Our clients and sponsors have provided a significant portion of the required liquidity from their own resources. In addition, funds obtained from government assistance were used and a few

Breakdown of on-balance sheet and off-balance sheet business

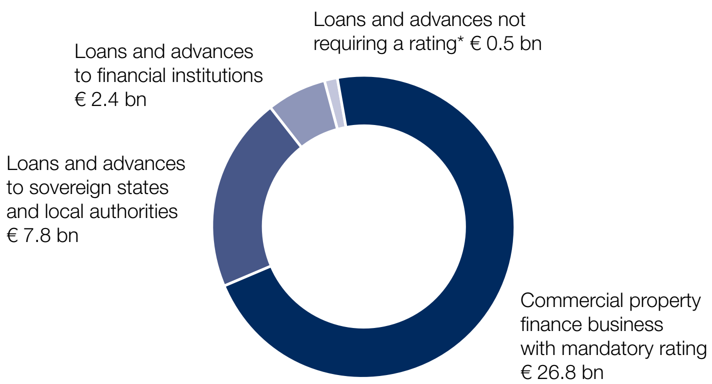
by rating procedure, € bn 31 Dec 2020



* Including the private client business of former WestImmo

Breakdown of on-balance sheet and off-balance sheet business

by rating procedure, € bn 31 Dec 2019



* Including the private client business of former WestImmo

clients reduced their exposures. Aareal Bank supported clients through deferrals of repayments totalling € 120 million as well as liquidity facilities of € 146 million. The gross carrying amount of the on-balance-sheet lending business under government moratoria amounted to € 49 million, whilst the gross carrying amount of on-balance sheet lending business subject to Covid-19-related forbearance measures amounted to € 6.5 billion. Measures related to Covid-19 – such as deferrals of repayments, or the provision of liquidity facilities – are being reported to the Management Board on a regular basis, and closely monitored.

On top of existing processes, additional measures were implemented during the year under review for those portfolios particularly affected by the Covid-19 pandemic, such as retail, hotels, and student housing. These portfolios were subject to particular monitoring (regardless of whether liquidity facilities were provided), including ad-hoc valuation reviews of the financed properties, which were increasingly backed by external appraisals. The frequency for periodic monitoring and internal rating (which also comprise a detailed target/actual comparison of the business plan) was adjusted to a semi-annual cycle. The CRE Credit Risk Committee was closely involved in evaluating and assessing all credit or monitoring decisions. A separate reporting system was established for the affected portfolios, enabling follow-ups of individual exposures and providing credit-relevant information, in order to be able to derive suitable measures at portfolio level, at an early stage.

When accounting for these measures, we have taken the recommendations made by the IASB, and by relevant regulatory authorities such as the EBA, the ECB and ESMA, into consideration – with the objective of providing a realistic assessment of expected losses. Intensified handling triggers recognition of loss allowance, in the amount of lifetime expected credit loss for the financial instrument concerned (Stage 2). The same applies for financings for which a forbearance measure has been granted. As at 31 December 2020, we assume recovery to kick in later (compared to expectations in the third quarter of 2020) due to the pandemic developments. These prospective changes in estimates result in such Covid-19-related liquidity measures no longer being of a temporary nature, but lead to a significant deterioration of credit quality in general. The assumption that no significant decrease in credit quality has occurred is only made in exceptional cases when this is justified based on supportable information.

The following tables provide a breakdown of gross carrying amounts of on-balance sheet as well as off-balance sheet credit business, money-market business, and capital markets business, by rating classes and loss allowance stages, in line with credit risk management at Group level. The impact of the Covid-19 pandemic has led to an increase in Stage 2 loss allowance. Figures are based on Aareal Bank Group's internal default risk rating classes. The default definition follows the definition pursuant to Article 178 of the CRR, which is decisive for management purposes.

Monthly reporting covers the material aspects of credit risk; it is supplemented by detailed information – which also fully covers specific credit portfolio developments (broken down by country, property and product type, risk classes, and collateral categories, for example), in line with regulatory requirements – at least on a quarterly basis. Risk concentrations are being taken into account in particular.

Trading activities are restricted to counterparties for whom the requisite limits are in place. All trades are immediately taken into account for the purposes of borrower-related limits. Compliance with limits is monitored in real time by Risk Controlling. Persons holding position responsibility are informed about relevant limits and their current usage, regularly and without delay.

In principle, Aareal Bank pursues a "buy and manage" strategy in managing its credit portfolio – with the primary objective of holding the majority of loans extended on its balance sheet until maturity; at the same time, targeted exit measures are deployed for actively managing the portfolio and the risks involved.

On-balance sheet commercial property finance business with mandatory rating

	31 Dec 2020					31 Dec 2019				
	Stage 1	Stage 2	Stage 3	fvpl[1]	Total	Stage 1	Stage 2	Stage 3	fvpl[1]	Total
€ mn										
Class 1										
Class 2	73				**73**	62				**62**
Class 3	249	4			**253**	430			2	**432**
Class 4	1,142				**1,142**	1,368				**1,368**
Class 5	3,684	9		249	**3,942**	3,447			495	**3,942**
Class 6	3,920	426		184	**4,530**	4,300	20		64	**4,384**
Class 7	2,991	297		253	**3,541**	3,872			75	**3,947**
Class 8	3,140	574		38	**3,752**	6,051	35		209	**6,295**
Class 9	2,565	1,271		14	**3,850**	2,936			56	**2,992**
Class 10	707	2,961		17	**3,685**	860	344			**1,204**
Class 11	453	514			**967**	174				**174**
Class 12	1	16			**17**	1	16			**17**
Class 13							60			**60**
Class 14										
Class 15										
Defaulted			1,547	95	**1,642**			935	149	**1,084**
Total	**18,925**	**6,072**	**1,547**	**850**	**27,394**	**23,501**	**475**	**935**	**1,050**	**25,961**

[1] fvpl = at fair value through profit and loss (in accordance with IFRSs)

Off-balance sheet commercial property finance business with mandatory rating

	31 Dec 2020					31 Dec 2019				
	Stage 1	Stage 2	Stage 3	fvpl[1]	Total	Stage 1	Stage 2	Stage 3	fvpl[1]	Total
€ mn										
Classes 1-2										
Class 3						22				**22**
Class 4	29				**29**	25				**25**
Class 5	69			10	**79**	63			17	**80**
Class 6	168				**168**	117				**117**
Class 7	87	0		14	**101**	141			25	**166**
Class 8	123	9			**132**	271	4			**275**
Class 9	158	41			**199**	101				**101**
Class 10	12	80			**92**	34				**34**
Class 11	30	11			**41**	1				**1**
Classes 12-15										
Defaulted			1	5	**6**			2		**2**
Total	**676**	**141**	**1**	**29**	**847**	**775**	**4**	**2**	**42**	**823**

[1] fvpl = at fair value through profit and loss (in accordance with IFRSs); commitments for loan portions earmarked for syndication

On-balance sheet loans and advances to financial institutions

€ mn	31 Dec 2020 Stage 1	Stage 2	Stage 3	fvpl[1]	Total	31 Dec 2019 Stage 1	Stage 2	Stage 3	fvpl[1]	Total
Class 1	853				**853**	815				**815**
Class 2	213				**213**					
Class 3	26				**26**	172				**172**
Class 4	108				**108**	82				**82**
Class 5	48				**48**	49				**49**
Class 6	26				**26**					
Class 7	677				**677**	836				**836**
Class 8	320				**320**	417				**417**
Class 9						35				**35**
Class 10	33				**33**	26				**26**
Classes 11-18										
Defaulted										
Total	2,304	–	–	–	2,304	2,432	–	–	–	2,432

[1] fvpl = at fair value through profit and loss (in accordance with IFRSs)

On-balance sheet loans and advances to sovereign states and local authorities

€ mn	31 Dec 2020 Stage 1	Stage 2	Stage 3	fvpl[1]	Total	31 Dec 2019 Stage 1	Stage 2	Stage 3	fvpl[1]	Total
Class 1	3,622				**3,622**	2,505				**2,505**
Class 2	1,674			26	**1,700**	2,680			65	**2,745**
Class 3	778			62	**840**	739			67	**806**
Class 4	76				**76**	100				**100**
Class 5	36				**36**	176				**176**
Class 6	177				**177**	262				**262**
Class 7	151				**151**	189				**189**
Class 8	1				**1**	6				**6**
Class 9	404	556			**960**	925	125			**1,050**
Classes 10-20										
Defaulted										
Total	6,919	556	–	88	7,563	7,582	125	–	132	7,839

[1] fvpl = at fair value through profit and loss (in accordance with IFRSs)

In summary, during the period under review, the existing set of tools and methods continued to enable the Bank to adopt suitable risk management or risk mitigation measures, where required, without any undue delay.

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 focuses on property when collateralising loans and advances. As a rule, loans are granted and the security interest perfected in accordance with the jurisdiction in which the respective property is located.

Mortgage lending values or fair values are set or determined 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 a valuer, which is subject to an internal plausibility check. Any diverging assessment 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 valuers.

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 defined credit processes provide for the regular review of collateral value. The risk classification is adjusted in the event of material changes in collateral value. 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.

Due to Covid-19, the associated lockdowns, and the increased number of enquiries, there were delays in obtaining external appraisals for properties which showed evidence of fluctuations in value. During the reporting year, Aareal Bank accounted for this by means of internal appraisals and management overlays. The scope of current valuation reviews within the portfolio particularly affected by the Covid-19 pandemic (including property types such as retail, hotels, and student housing) for the purpose of year-end valuation covered this portfolio almost completely. External valuations accounted for approximately 85 % of the lending volume. Overall, the valuation reviews were in line with our expectations from the third quarter of 2020, except for a few NPL cases. No management overlay was required by the year-end.

Credit risk mitigation for trading activities

To reduce counterparty risk in Aareal Bank's trading business, the master agreements for financial derivatives and master agreements for securities repurchase transactions (repos) used by the Bank[1)]

[1)] Any comments below referring to the German Master Agreement on Financial Derivatives (Deutscher Rahmenvertrag für Finanztermingeschäfte – "DRV") also pertain to the master agreement issued by the International Swaps and Derivatives Association Inc. (ISDA) (the "ISDA Master Agreement"). Both agreements are standardised agreements recommended by leading associations – among others, by the Association of German Banks (Bundesverband deutscher Banken – "BdB").

provide for various credit risk mitigation techniques, via mutual netting framework agreements.

The master agreements for financial derivatives used by the Bank contain netting framework agreements at a single transaction level (so-called "payment netting"), and arrangements for the termination of individual transactions under a master agreement (so-called "close-out netting").

In general, all master agreements are based on the principle of a common agreement. This means that, in the case of a termination, the individual claims are netted, and that only such net amount can and may be claimed with regard to the defaulted counterparty. This claim must not be affected by any insolvency, i.e. it must be legally valid and enforceable. This, in turn, means that the jurisdictions concerned must recognise the concept of a common agreement which protects the net amount of the claim from imminent access by the insolvency administrator.

Above all, the close-out netting is subject to (international) legal risks. The Bank reviews these legal risks by reference to legal opinions regarding the validity and enforceability of mutual netting framework agreements in the case of a counterparty's insolvency. These legal opinions are evaluated based on various criteria such as product type, jurisdiction of the registered office and branch office of the counterparty, individual contract supplements and other criteria, and using a database developed for this purpose. In doing so, the Bank decides for each individual transaction whether or not netting is possible. The Bank uses eligible bilateral netting framework agreements within the meaning of the CRR for all transactions with financial institutions; in many cases there are additional collateral agreements which further reduce the relevant credit risk.

The Bank enters into repo transactions both on a bilateral basis and via Eurex Clearing AG as a central counterparty. For repo transactions, depending on the counterparty, payment or delivery netting is agreed upon. Master agreements for repo transactions generally contain provisions on close-out netting. The Bank does not use the option permitted by regulatory authorities to reduce capital requirements for repo transactions.

Furthermore, counterparty risk is reduced through derivatives settlement via central counterparties (CCPs): Aareal Bank uses Eurex Clearing AG and LCH.Clearnet Limited.

The Bank uses an internal rating system to assess the credit quality of counterparties. Credit Transaction Management is responsible for the daily valuation of the Bank's trades, including collateral accepted or pledged, and using validated valuation procedures.

Collateral for derivative transactions is usually provided in cash. Repo transactions are usually collateralised through securities, pledged on a daily basis.

Some collateral agreements provide for higher collateral levels in the event of material downgrade to a contracting party's rating.

Country risks

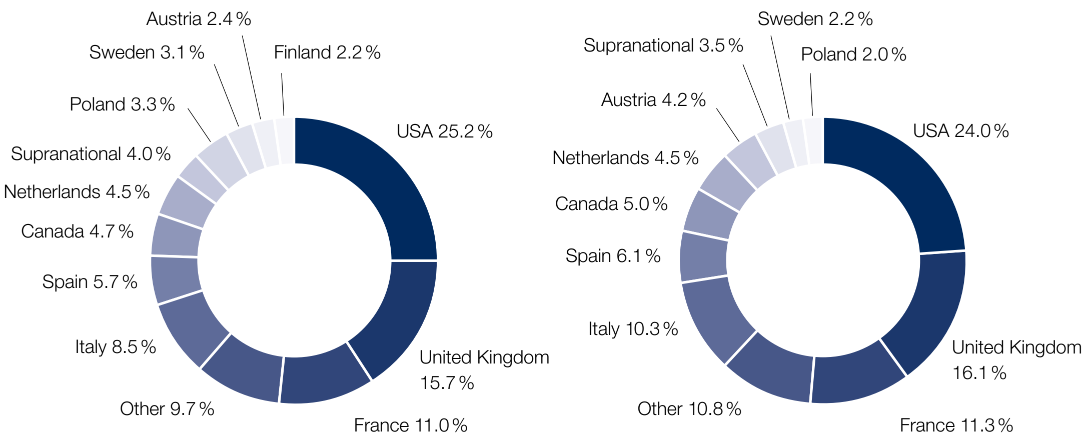
Our comprehensive approach to risk management also includes measuring and monitoring country risk exposure. When defining country risk, in addition to the risk of sovereign default or default of state entities, Aareal Bank also considers the risk that a counterparty could become unable to meet its payment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

The diagram below illustrates the risk exposure by country (comprising receivables and off-balance sheet obligations) in the Bank's international busi-

Breakdown of country exposure in the international business

%

31 Dec 2020 | 31 Dec 2019



ness, at year-end. In the property financing business, country exposures are allocated by location of the property used as collateral. For exposures not collateralised by property, the allocation is based on the borrower's country of domicile. This reflects the exposure of the property finance business, as well as the activities of Treasury.

Interest rate risk in the banking book

Definition

Interest rate risk in the banking book (IRRBB) is defined as the risk exposure of instruments held in the banking book which are sensitive to changes in interest rates, caused by yield curve shifts.

Specifically, for Aareal Bank this includes:

- risks arising from maturity transformation in the event of yield curve shifts (so-called gap risk), which, in turn, are broken down into:
  - risks from cash flows which are sensitive to interest rates, relative to the general yield curve (interest rate risk or repricing risk);
  - risks arising from the valuation of future cash flows, relative to the general yield curve (yield curve risk);
- risks from cash flows which are sensitive to interest rates, in terms of spreads to the general yield curve (basis risk);
- risks from explicit and implied options (option risk);
- risks arising from changing valuation of pension liabilities (pension risk);
- risks from fluctuations in the value of fund assets (fund risk); and
- risks from changes in Aareal Bank's specific funding spreads (funding risk).

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 exposure to interest rate risk in the banking book on a daily basis.

The VaR concept has been broadly accepted as the predominant method for measuring economic interest rate risk in the banking book. VaR quantifies risk as the maximum loss that will occur within a certain period of time, and given a defined probability.

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, 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 99.9 % confidence interval under the economic perspective.

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 and deposits at notice which are factored into calculations for a period of up to ten years, using the average residual amount of deposits observed in the past. Loans are taken into account using their fixed-interest period (for fixed-rate exposures), or using their expected maturity (variable-rate exposures). Aareal Bank Group's consolidated equity is not taken into account as a risk-mitigating item. This tends to overstate VaR, demonstrating our goal to pursue a conservative approach adopted in our risk measurement processes.

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.

Present-value impact of an interest rate shock

The following tables show the changes in present value as prescribed by BaFin circular 06/2019, applying EBA guidelines EBA/GL/2018/02 on controlling interest rate risk in the banking book (IRRBB).

The standard test prescribed therein outlines present value changes in the banking book in the event of a maximum 200 basis point parallel shift for each currency. As in the previous years, the ratio of the aggregate results to Aareal Bank Group's regulatory capital is clearly below the prescribed threshold of 20 %.

Furthermore, present value changes are determined (and their ratio to Tier 1 capital shown) for six early-warning indicators, applying the prescribed scenarios. The ratio of the aggregate result

Changes in present value

	31 Dec 2020		31 Dec 2019	
	-200 bp	+200 bp	-200 bp	+200 bp
€ mn				
EUR	9	49	5	37
GBP	19	-21	21	-20
USD	62	-39	18	-28
Sonstige	8	-18	8	-13
Total	**98**	**-29**	**52**	**-24**
Percentage ratio to regulatory capital	**2.9**	**0.9**	**1.6**	**0.7**

€ mn	31 Dec 2020	31 Dec 2019
Parallel shock up	-32	-30
Interest rate coefficient for parallel shock up (%)	1.2	1.2
Parallel shock down	98	52
Interest rate coefficient for parallel shock down (%)	3.8	2.1
Steepener shock	50	38
Interest rate coefficient for steepener shock (%)	1.9	1.5
Flattener shock	2	-44
Interest rate coefficient for flattener shock (%)	0.1	1.8
Short rates shock up	-39	-40
Interest rate coefficient for short rates shock up (%)	1.5	1.6
Short rates shock down	92	51
Interest rate coefficient for short rates shock down (%)	3.6	2.0
Tier 1 (T1) capital	**2,586**	**2,491**

to Aareal Bank Group's Tier I capital is clearly below the prescribed threshold of 15 %.

Market risks

Definition

Market risks are broadly defined as the threat of losses due to changes in market parameters; this refers to market risks which are not assigned to the IRRBB. In particular, this also encompasses any type of spread risk exposure of instruments held in the banking book which are sensitive to changes in interest rates, and which are neither included in IRRBB nor in counterparty credit risk. Specifically, for Aareal Bank this includes:

- risks resulting from fluctuations of spot foreign exchange (FX) rates (spot FX risk);
- risks resulting from fluctuations of forward foreign exchange rates (forward FX risk); and
- risks from the regulatory review of the trading book (Financial Risk in the Trading Book – FRTB).

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

Commodities are irrelevant for the Bank's business. Exchange rate risks are largely eliminated through hedges.

Additional elements of market risk are:

- valuation risks due to changes in credit spreads (credit spread risk);
- specific price risks from the bond portfolio, wherein the bonds are mainly sovereign bonds (sovereign risk);
- risks from adjustments to the credit valuation of OTC – derivatives (CVA risk).

To differentiate spread risks (credit spread risk and sovereign risk) in terms of their credit risk exposure, reported market risk is adjusted accordingly.

Risk measurement and monitoring

Risk Controlling informs the members of the Management Board responsible for Treasury and risk monitoring about the risk position and exposure to other market risks on a daily basis.

The VaR concept has been broadly accepted as the predominant method for measuring economic market risk. VaR quantifies risk as the maximum loss that will occur within a certain period of time, and given a defined probability.

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, the VaR figure takes into account the correlation between individual risk types. Statistical parameters used in the VaR model are calculated directly from a historical data pool maintained within the Bank, which covers at least 250 days.[1] The loss potential is determined applying a 99.9 % confidence interval.

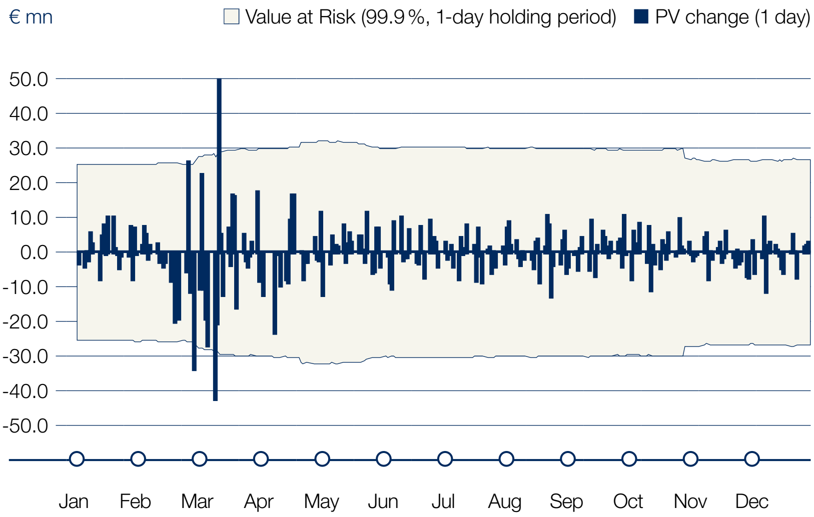
Backtesting

The quality of forecasts made using statistical models is checked through a monthly 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 99.9 %, only a small number of events are expected to break out of the VaR projection.

The backtesting exercise shown below comprises all risk positions subject to daily changes from the "Market risks" category.

Two negative outliers were observed at Group level during the past 250 trading days, also as a result of volatility induced by Covid-19 in March; this does not refute the long-term forecasting quality of the VaR model we use.

Present values and 1-day VaR during the course of 2020



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. To the extent that they are caused by operational risks, model and reputational risks are also taken into consideration within this type of risk. Systemic risks (or their impact on operational risks) are not affected by this.

Risk measurement and monitoring

It is the objective of the policy pursued by Aareal Bank 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 risk control tools to manage operational risks:

[1] Historical data covering two years is used for the sub-risk type of credit spread risk.

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

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

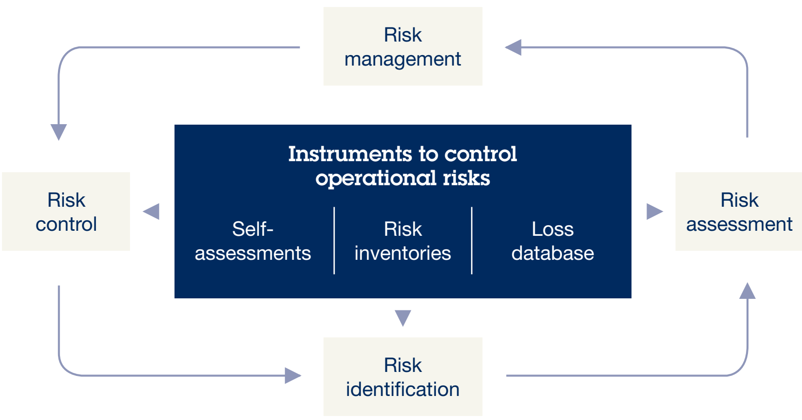
The three tools described above are used to prepare the regular risk reporting to the Bank's senior management. The responsibility for implementing operative risk-reducing measures rests with those responsible for the Bank's risk management. The utilisation of freely available funds for operational risks – as part of the Bank's risk-bearing capacity – are determined using the regulatory standardised approach.

In addition to the reports prepared from the tools stated above, suitable and plausible stress tests are conducted every quarter. These are hypothetical and historical scenarios as well as 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.

Aareal Bank's legal department deals with any litigation the Bank is involved in, as well as with any legal issues of fundamental importance – where necessary, using the support of external lawyers.

Legal also compiles all information concerning any legal disputes involving Aareal Bank Group, whether in or out of court. To this extent, the involvement of the legal department is based on corresponding Group-wide guidelines. The Bank's decentralised operating legal entities, as well as

Management of operational risks



the legal departments of subsidiaries submit quarterly reports on legal risks identified to Aareal Bank's legal department; where particular risks have occurred, such reports are submitted on an event-driven basis. When required, Aareal Bank's legal department discusses and coordinates any concrete measures with the reporting unit.

The legal department reports to the Management Board, (at least) on a quarterly basis, as well as on an event-driven basis. Moreover, information about legal risks is included in operational risk reporting.

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. Even though loss cases are recorded in the loss database on an ongoing basis, the aggregate impact of such losses during the year under review amounted to less than 10 % of the regulatory capital to be maintained for operational risks.

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

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.

Strategy Development, as well as Finance & Controlling and Risk Controlling, are responsible for measuring and monitoring investment risk exposure. Risk Controlling is responsible for submitting a quarterly equity investment risk report to the Bank's Management Board.

Property risks

Definition

We define property risk as the threat of unexpected losses arising from changes in the value of property held by the Bank, or by fully-consolidated subsidiaries.

Due to the special character of property risk (involving marketing risks, for example), special methods and procedures are employed to deal with investment risk. All relevant property holdings are subject to regular audits, including a review and assessment of their risk situation. The effects of the Covid-19 pandemic required a valuation review for some properties. This required write-downs to be recognised for properties held by the Bank. Property risks increased during the period under review, as a result of the acquisition of a property SPV from an Italian credit exposure.

Risk measurement and monitoring

In order to measure and monitor risks, property yields are analysed for different regions, and over the time horizons available: on this basis, potential yield increases over a one-year horizon are determined applying a 99.9 % confidence interval. A property's risk contribution results from the difference between the current market value and the property value adjusted for the yield increase.

Business and strategic risks

Definition

Business and strategic risk is defined as the risk of unexpected losses, usually brought about by a decline in profits due to income falling short of expectations, whereby the shortfall cannot be compensated for by cost reductions. Strategic risk may emerge from changes in the competitive or regulatory environment, or due to unsuitable positioning in the macro-economic environment.

Risk measurement and monitoring

In this context, we distinguish between investment risk and allocation risk, whereby allocation risk is already covered by various planning scenarios, and is thus incorporated in aggregate risk cover.

Investment risk is measured across segments: it is quantified assuming that additional upfront investment is required to establish an investment opportunity which was previously unavailable. Such upfront investment is assumed to represent potential risk.

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 Group's liquidity risk management system is designed to ensure that the Bank has sufficient cash and cash equivalents to honour its payment obligations at any future point in time. The risk management and monitoring processes have been designed to cover refinancing and market liquidity risks in addition to liquidity risk in the narrower sense. All elements have been integrated in an overarching ILAAP, which maps liquidity risks in both the normative and the economic perspective. Within the framework of Group planning, in addition to ICAAP risk parameters taken into account for capital planning purposes, ILAAP risk parameters for a three-year horizon are also considered.

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:

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 expected cash flow profile of products without a fixed contractual lifetime.

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.

Stress testing

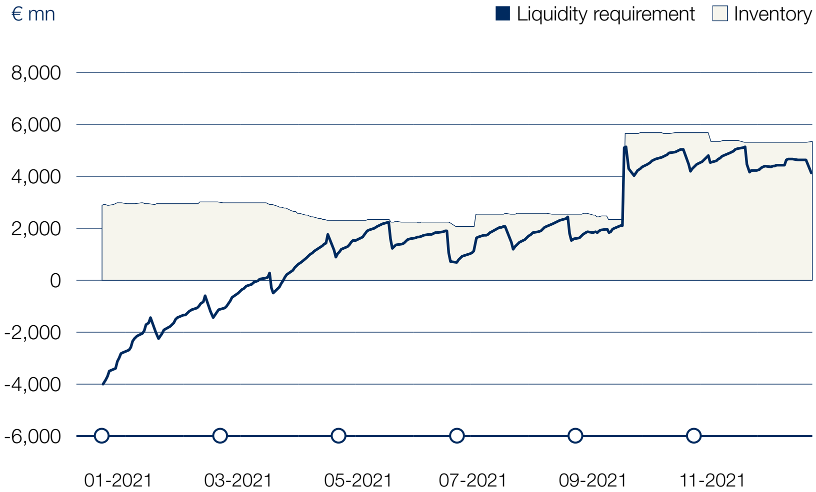
Moreover, we employ stress tests and scenario analyses to assess the impact of sudden stress events onto the Bank's liquidity situation. The various standardised scenarios used are evaluated on the basis of the liquidity run-off profile.

We generally consider the withdrawal of deposits from the housing industry as the most significant scenario. Even in this stress scenario, liquidity is sufficient to cover the expected liquidity needs under stress conditions.

Time to illiquidity

To safeguard adequate liquidity beyond the three-month horizon covered by the liquidity run-off profile, we use the concept of time to illiquidity as a parameter. For this purpose, a liquidity run-off profile was developed which compares liquidity requirements occurring with the liquidity stock, for a one-year period. Time to illiquidity ("TtI") denotes the remaining period (expressed in days) during which Aareal Bank Group can be regarded

Liquidity development



as sufficiently liquid, even under adverse conditions. In other words, liquidity requirements (including security add-on for adverse future events) do not exceed the liquidity stock.

The calculations are based on contractual cash flows and the short-term risk assessment methodology (liquidity run-off profile), as well as the portfolio development within the current plan scenario.

The following chart shows the projected development of the liquidity stock, together with aggregate liquidity requirements (incorporating planned portfolio developments, and including security add-ons for adverse future events) until the end of 2021. The chart demonstrates that the liquidity stock will always exceed liquidity requirements, even under adverse conditions. The increase in the liquidity stock from September 2021 onwards reflects the maturity of Targeted Longer-Term Refinancing Operations (TLTROs), together with related collateral.

Further details are provided in the comments on the Bank's liquidity in the section on the "Financial position".

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. In this context, we refer to the comments regarding the breakdown of funding between money markets and capital markets, as set out in the description of financial position.

Concentration limits

Besides the pure measurement of risk indicators, we also monitor concentrations of liquid assets and of funding sources, determining the percentage share of the ten largest counterparties and/or positions, relative to the total portfolio.

A limit is set for each indicator in order to restrict the dependency upon individual positions or counterparties.

LCR forecast

We have developed the LCR forecast as a measurement tool designed to ensure that we maintain compliance with the regulatory Liquidity Coverage Ratio. A preview of the Liquidity Coverage Ratio is calculated over a horizon of up to three years, determining the ratio of highly liquid assets to cumulative net cash outflows for various end-of-month dates – thus identifying any potential liquidity shortfalls or reserves.

NSFR forecast

The NSFR forecast, which is a projection of the Net Stable Funding Ratio over a period of up to three years, represents another important component of our liquidity management. This measurement tool allows us to forecast the regulatory Net Stable Funding Ratio for future dates, thus identifying any potential liquidity shortfalls or eserves in terms of the NSFR at an early stage.

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. 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. 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 and operate this system.

Organisation of the accounting-related ICS and RMS

The Internal Control System of Aareal Bank takes into account the principles established by the Minimum Requirements for Risk Management (MaRisk) related to the 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, covering all entities of Aareal Bank Group. The Management Board of Aareal Bank AG is responsible for designing, implementing, applying, further developing and 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.

Aareal Bank prepares its financial statements in accordance with the provisions of the German Commercial Code (Handelsgesetzbuch – "HGB") and its consolidated financial statements in accordance with International Financial Reporting Standards (IFRSs) as applicable in the European Union. The Finance & Controlling division controls accounting processes and is responsible for ensuring conformity with legal requirements, as well as with any further internal and external provisions. The accounting-related requirements that have to be applied are documented in guidelines and IT requirements.

For the consolidated financial statements in accordance with IFRSs, the companies that form part of the Group create an IFRS package as at the respective reporting date. This includes financial statements prepared under IFRSs and in accordance with the IFRS Group Accounting Manual, as well as the Notes and consolidation information (intercompany balances). All packages are recorded by the Finance & Controlling division in a consolidation software and aggregated for the purpose of preparing the consolidated financial statements. The Supervisory Board is responsible for monitoring the Management Board. Within the scope of financial reporting, it approves the single-entity financial statements of Aareal Bank AG as well as the consolidated financial statements and group management report. Measures taken by the Supervisory Board to ensure an efficient performance of its control functions include the establishment of an Audit Committee, which is primarily responsible for financial reporting issues and monitors the effectiveness of Aareal Bank's Internal Control System. It analyses and assesses the presented financial statements and internal risk reports as well as the annual report submitted by Internal Audit. In addition, the Audit Committee is responsible for determining the focal points of the audit, as well as for evaluating the auditors' findings. The Audit Committee includes an expert in the fields of accounting or auditing, pursuant to section 100 (5) of the German Public Limited Companies Act (Aktiengesetz – "AktG").

Internal Audit also assumes a monitoring function not related to the process. It reports directly to the Management Board, and provides auditing and consulting services which are designed to optimise Aareal Bank'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 Internal Control System and of the Risk Management System in general. Any detected weaknesses regarding the identification, evaluation and reduction of risks are reported and addressed within the context of specific action plans.

Internal Audit also performs Group audit functions for Aareal Bank's subsidiaries, within the context of the Group's risk management. 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. To perform its tasks, Internal Audit has full and unrestricted information rights with respect to activities, processes and IT systems of Aareal Bank AG and its subsidiaries. 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 Group. The audit activities of Internal Audit comprise all of the Group's operational and business processes, and are carried out using a risk-based approach.

Components of the accounting-related ICS and RMS

Within Aareal Bank, various measures related to the Bank's organisational structures and procedures help to fulfil the monitoring duties 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 & Controlling division is set out in the Bank's organisational guidelines. Aareal Bank's accounting system is structured observing the principle of separation of functions, which makes for a split between operative and administrative roles, and is designed to ensure a sufficient level of control.

Various guidelines exist for activities and processes. These guidelines are set out in the Written Set of Procedural Rules of Aareal Bank and available for inspection to 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. Uniform accounting methods and measurement techniques are guaranteed through guidelines applicable throughout the Group. The requirements of these Group-wide guidelines substantiate legal provisions, and are adjusted on an ongoing basis to take current standards into account. The valuation techniques used, as well as the underlying parameters, are controlled regularly, and adjusted if necessary.

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 manual process workflows.

Adherence of accounting to generally accepted accounting principles is ensured by both preventive and detective controls, as well as through a 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. Control processes have been implemented for both manual and automated accounting transactions.

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 Group uses both standard and customised software. The consolidation software provides technical support to the reconciliation of Group-internal relationships, in a clearly-defined process. The data of the units included is reported using a uniform standardised chart of accounts. The Group'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, Internal Audit conducts IT reviews independently from processes.

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 manipulation of data. Authorisations are allocated to the responsible employees, reviewed regularly, and adjusted if necessary in accordance with internal criteria.

Aareal Bank 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 Group structure, to the business model, or due to new legal requirements. The Covid-19 pandemic has not required any material adjustments to the accounting-related Internal Control System.

Aareal Bank 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 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 and Opportunities

Macro-economic environment

The economy, financial markets and commercial properties are subject to a series of risks, whereby some downside risks – such as the risk of a no-deal Brexit or uncertainties in the course of the US presidential election – were not triggered until the end of 2020. Nonetheless, 2021 will continue to be exposed to other risks that could have negative implications. These include the ongoing Covid-19 pandemic and its economic burdens, protectionist tendencies, doubt about the cohesion of the European Union, higher public and private borrowing and other geopolitical risks.

An ongoing Covid-19 pandemic due to further new infections or the failure of the vaccines to deliver the anticipated success could halt or even stop the recovery of the global economy. An extension or reintroduction of protective measures against the infection – also due to newly emerging Covid strains – could have negative consequences for demand and for the services sector.

A resurgence of the European sovereign debt crisis also has to be considered a threat. Sovereign debt is rising in many places, whilst the legal situation in the euro zone materially increases the risk of a crisis, which could resurge, for example, due to higher debt levels resulting from the Covid-19 pandemic or because of doubts as to solidarity within the euro zone. Political uncertainty in Spain also needs to be mentioned in this context. A separation of the Autonomous Community of Catalunya from the Kingdom of Spain might have negative economic consequences, which are as yet difficult to assess. Spain and Italy, among others, pose another risk with their high number of Covid-19 infections. Although the EU's rescue package announced in July 2020 is aimed in particular at supporting these countries, there is still a risk that the measures will not be quite enough to stem the negative consequences.

The reform backlog and structural economic problems in some euro zone countries, in particular following the government crisis in Italy, geopolitical risks (e.g. armed conflicts, terrorism) represent further uncertainties, risks and stress factors.

Non-financial enterprises in many of the developed countries have increased their borrowings significantly, especially by issuing bonds. In many instances, these bonds are just about rated in investment grade territory. An ongoing pandemic or other risks could be a reason for downgrading the rating of these bonds. The ending of special regulations and state aid represents a risk for higher insolvency rates among non-financial enterprises.

Relating to macro-economic development, these factors are also significant for the financial and capital markets, and could trigger further disruption on these markets if they were to materialise to a considerable extent. Volatility on these markets is thus set to remain noticeable going forward.

There are several risks for commercial property resulting from the Covid-19 pandemic: bans on contact, travel restrictions and business closures of a temporary nature to begin with are likely to have a marked negative impact on cash flows in 2021 too, particularly for hotel and retail properties. They are exposed to the risk of continuing constraints and the resulting follow-on risks, which might reduce cash flows over the longer term. Furthermore, the Bank cannot exclude that the pandemic's economic impact – particularly due to new protective measures against the spread of the infection – will continue to have a negative effect upon property values.

The Bank expects competition in the commercial property financing markets to remain intense, particularly in regions and for property types that were less adversely affected by the pandemic. While loan-to-value ratios for new business look set to remain virtually stable, changes in the market environment could put direct pressure on margins, or result in higher loan-to-value ratios.

Economy

The rapid development and approval of Covid-19 vaccines support the assumption that the global economy will recover by a strong 5.0% on 2021. As pre-crisis levels will not be reached everywhere, even at the end of the year, the recovery is therefore expected to be largely gradual. Various measures taken at the end of 2020 to protect against the spread of the infection are likely to dampen the recovery.

Gross domestic product in the euro zone is expected to increase by 4.2 % in 2021. This is based on expectations that retail sales will remain solid, exports increase and investments recover at a slower pace. The funds from the EU support packages are also likely to provide support in the second half of the year. Given that the respective member states have formulated different support packages, the recovery with definitely be heterogeneous.

With gross domestic product forecast to grow by 4.5 % in 2021, the UK is expected to recover. The trade agreement reached with the EU is likely to support the recovery and reduce uncertainty, albeit not entirely.

We expect economic growth of 4.2 % for the US in 2021, especially due to fiscal support towards mid-year. Despite high Covid-19 numbers, the economic situation should gradually return to normal. The economy in Canada is expected to grow by 4.4 % in 2021, with accelerating growth anticipated from mid-year onwards.

China was already showing signs of recovery at the end 2020, which should continue into 2021. However, we will see a shift in the growth drivers from infrastructure investment and exports to consumption and corporate investments.

Based on consumption and a positive trend on the labour market, Australia's economy is expected to grow by 3.1 % in 2021. The pre-crisis level should therefore be reached in the second half of the year.

Financial and capital markets, monetary policy and inflation

The risks and uncertainties referred to above are also significant for the financial and capital markets and could continue to create considerable disruption. Given these circumstances, we can expect sharply rising or falling equity and bond prices overall in 2021.

Due to the uncertainty, especially regarding the impact of the Covid-19 pandemic on the economy, we expect to see strongly expansionary monetary and fiscal policy measures and continued low interest rates in 2021. However, the persistent low interest rate environment might impair the effect of central banks' traditional policy.

Several factors are likely to drive up inflation in 2021 over the levels seen in 2020. On the one hand, energy prices have increased year-on-year, while the pandemic-induced tax relief will be abolished in part on the other. All in all, weaker demand in the services sector will probably curb core inflation.

Regulatory environment

The Covid-19 pandemic impacted on the regulatory environment as well. Various regulatory initiatives were deferred and temporary relief resolved for financial institutions. Nonetheless, the trend towards a tighter regulatory framework is set to persist in the years ahead, too. For instance, the finalisation of the Basel III framework, adopted by the Basel Committee's Group of Governors and Heads of Supervision (GHOS), will bring about extensive changes to the approaches used for determining risk-weighted capital requirements (a concept known as "Basel IV"). In the course of the Covid-19 pandemic, the Basel Committee has deferred the date of application by one year to 1 January 2023. A second consultation on implementing Basel IV at a European level, taking into account the experience gathered from the Covid-19 pandemic, is anticipated and likely to start during the first half of 2021.

The EBA guidelines on granting and monitoring loans will place further demands on the banks' internal governance (incl. in risk culture and strategy) and on the credit processes (incl. documentation, credit rating review) as well as the monitoring framework (e.g. ongoing monitoring of the credit terms).

The requirements are supplemented at a European level by another MaRisk amendment at national level, which is due to come into force in 2021.

Sector-specific and business developments

Structured Property Financing segment

Demand for commercial properties will vary in 2021, depending on the region and property type. This is an area in which developments surrounding the Covid-19 pandemic and the form of economic recovery will be decisive, especially given that some regions and types of property were more severely affected by the pandemic than others.

Moreover, other uncertainty factors and risks in the macro-economic environment are also relevant for commercial property markets.

It is expected that various factors will have an impact on how commercial property values develop this year. While historically low interest rates support property values, political uncertainty, economic downturns or restraint among investors can have an adverse impact on property values.

With regard to commercial property, we expect stable to rising average market values over the next few years. All in all, commercial properties should have reached or overcome the performance low. Considering the assumed recovery, most commercial properties should return to their pre-crisis values in the years to come. With a view to retail properties, we expect the situation to ease more slowly, as the structural change in buying behaviour is having a dampening effect on the outlook of value-driving rental revenues, depending on location and segment. Also depending on location and segment, we see hotel properties recovering in the years to come. As travel activities gradually increase, we expect a recovery at least to pre-crisis levels. We expect a similar development for student housing activities, where demand by international students should recover. We expect the values of office properties to rise slower compared to the previous year, due to the Covid-19 pandemic. Logistics properties continue to be assessed positively, as we expect the trend of rising market values of these properties to prevail. Individual properties may generally deviate from this estimate, depending on the different regional economic impacts of the Covid-19 pandemic.

As a matter of principle, it is worth noting that estimation uncertainty – concerning the economy, markets, and the impact upon Aareal Bank – is currently much higher than usual, as the pandemic has provoked a situation unprecedented in recent

%	2020	2021	2022	2023
"Swoosh" scenario				
Gross domestic product (year-on-year change in %)				
Euro zone	-7.1	4.2	4.9	2.2
US	-3.5	4.2	3.4	2.0
UK	-10.3	4.5	6.4	2.3
Unemployment (%)				
Euro zone	8.0	9.1	8.4	7.9
US	8.1	6.2	5.2	4.7
UK	6.1	7.4	5.5	4.6
Portfolio-weighted property price development (2020 basis = 100 %)		104.2	107.5	108.2

>

%	2020	2021	2022	2023
"Bad case" scenario				
Gross domestic product (year-on-year change in %)				
Euro zone	-7.1	-0.9	5.6	2.3
US	-3.5	0.0	4.2	1.7
UK	-10.3	-1.1	6.0	2.4
Unemployment (%)				
Euro zone	8.0	11.0	10.2	9.4
US	8.1	6.9	5.8	5.3
UK	6.1	10.8	9.2	7.8
Portfolio-weighted property price development (2020 basis = 100 %)		97.6	102.3	103.4

history. Data and experience are therefore both lacking. Against this background, the impact of worsening macro-economic factors (compared to the "swoosh" scenario underlying our forecast) was examined. In the so-called "bad case" scenario, loss allowance for the overall portfolio increases by approximately 20 basis points compared to our "swoosh" scenario in 2021. The scenarios are based on the macro-economic factors shown above.

In the Structured Property Financing segment, we aim to originate new business of between € 7 billion and € 8 billion for the 2021 financial year, so that Aareal Bank Group's property financing portfolio is expected to be at € 29 billion at the end of the 2021 financial year, subject to exchange rate fluctuations. To manage our portfolio and risk exposure, we also use syndications.

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

Banking & Digital Solutions segment

The segment description Consulting/Services Bank was changed to Banking & Digital Solutions at the turn of the year as part of the strategic review.

The German housing and commercial property industries are expected to remain solid in 2021, in spite of the Covid-19 pandemic. We expect property values to be very stable and rental income to remain largely steady. Following a long growth phase, rental income is expected to stagnate at average levels in the long term, due to regulatory requirements such as the caps on rent levels and also against the background of the Covid-19 pandemic. Further rent deferrals or defaults due to rising unemployment are also to be expected, especially among freelancers and the self-employed. At present, it is impossible to seriously forecast just how serious the impact is going to be – this will largely depend upon the further development of the Covid-19 pandemic.

The companies will continue to optimise and develop existing portfolios, driven especially by socio-political consideration, such as refurbishing buildings to make them suitable for the elderly, district development or new-build projects. The demands of climate protection targets for Germany, and the decisive pressure on the property industry to achieve them, is putting serious demands on resources.

Even though the Bank's market share in the institutional housing industry is already high based on the number of residential units, we see good opportunities in the 2021 financial year to acquire new clients and to intensify the business relationships with our existing client base. We plan to achieve this through the expansion of the "Housing Industry Ecosystem", the cross-sector development of interface products, and the expansion to adjacent ecosystems, such as companies from the utilities and waste disposal industries. The focus here remains on, for example, the functional expansion of the Aareal Portal corporate client platform as regards the digitalisation of client communication and account processing.

In our view, the range of services that connect alternative online payment solutions to existing systems, thus helping to overcome process breaks (even across industry sectors), are particularly interesting. The Aareal Exchange & Payment Platform, which integrates alternative payment methods in existing accounting systems, is available since 2020 with an interface to barzahlen/viacash, with further payment methods such as PayPal and credit cards being added in 2021. We also see potential in technical solutions for automating billing processes as part of electromobility in the network of charging stations. The corresponding Aareal Connected Payments product was launched successfully on the market in 2020. Further growth should be generated by the integrated rental security product Aareal Aval and Aareal Meter, a solution that uses mobile meter reading to provide a digital solution to a labour-intensive analogous product.

Against this background, we are aiming for renewed net commission income growth over the previous year (2020: € 26 million) and expect the average deposit volume from the housing industry to remain around € 11 billion. The persistently low interest rate environment, which is relevant for the results from our deposit-taking business, will continue to burden 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, stable and alternative source of funding for Aareal Bank.

Aareon segment

Aareon will continue to implement and accelerate its growth strategy in the 2021 financial year. In this context, Aareon Flight Plan 2021 was developed and launched on the fourth quarter of 2020. This plan integrates measures from a Value Creation Programme, including inorganic growth projects, as well as investments in existing and new products.

The Covid-19 pandemic will continue to have an impact on Aareon in 2021 – especially on the consultancy business. The Covid-19 pandemic is expected to result in greater digitalisation needs in the medium term and therefore to an increase in the demand for digital solutions and advisory services. In this context, Aareon expects double-digit growth rates of over 20 % in digital solutions in the 2021 financial year (2020: 19 %). Sales revenue generated from ERP products is expected to grow in the lower single-digit range. Overall, a marked increase in consolidated sales revenue is expected for 2021. As a result of the aforementioned expenses for investments (including the Value Creation Programme), we anticipate an increase in adjusted EBITDA[1]. Aareon will become a "Rule of 40" entity in the medium term. This indicator is widely used in the software industry to identify efficient growth companies whose revenue growth and EBITDA margin add up to at least 40 %.

Demand for the new product generation Aareon Wodis Yuneo, which was introduced in 2020, will be important for the ERP business in the DACH region. Market response has been very positive up to now, so that Aareon expects revenues to increase further in 2021. Aareon also anticipates growth for the ERP solution RELion, which is focused on the commercial property market. The business volume generated from Aareon Cloud Services and BauSecura insurance management will be up slightly on the previous year. The acquisition of Arthur Online Ltd., London, which complements

[1] "Earnings before interest, taxes, depreciation and amortisation" excluding strategic investments (venture and M&A activities) and non-recurring effects

Aareon's product portfolio from 1 February 2021 onwards, will also contribute to this growth. Arthur offers a cloud-based software solution for property management focused on the UK, which brings together property managers, property owners, tenants and contractors on a single platform. On the other hand, the number of client projects migrating to the new ERP product generation will rise significantly for the Tobias solution. It is expected that 2020 sales revenue levels will be reached again in France. On the UK market, client acquisitions in 2020 in particular are expected to have a positive impact on recurring revenues in 2021. The acquisition of new ERP clients should also lead to growing licence revenues. Aareon also expects to generate higher revenues from licenses and SaaS with new and existing clients in the Nordic countries.

The digital solutions will make a decisive contribution towards realising the growth potential in the DACH region and in the international business. Aareon anticipates strong licence business from the BRM solution of the CalCon company acquired at the beginning of the year under review. SaaS revenues are expected to increase for the WRM and CRM products due to additional products being rolled out. Higher sales revenues with SRM products should be achieved thanks to a greater number of tradesmen' orders that are settled via Mareon.

Looking at the Consulting business, Aareon expects demand for green consulting services in particular to remain strong against the backdrop of the Covid-19 pandemic. Traditional consulting offerings are also expected to be used increasingly during the year; nonetheless, renewed lockdowns will also impact on consulting revenue in 2021.

Aareon will continue in 2021 with the development drive in new products and services that was launched in 2019. The virtual assistant Neela and the Aareon Smart Platform and Smart Partner solutions will be developed further and new functional features added. Further product developments are planned in preventive maintenance and in networking clients, public offices and utilities, among others, on a digital platform and for mobile solutions. Aareon is also investing in developing new lines of business by co-founding start-ups. Capacities were also extended to drive Aareon's inorganic growth.

Based on the explanations outlined above, Aareon envisages a marked overall increase in sales revenue to between € 276 million and € 280 million in the year ahead (2020: € 258 million). Adjusted EBITDA[1] is likely to further increase to between € 63 million and € 65 million (2020: € 62 million). The forecast does not include any effects from future M&A transactions.

Business strategy

Aareal Bank Group's strategy focuses on sustainable business success. Environmental, social and governance aspects are therefore key elements of its business strategy. The medium-term strategic development is therefore being pursued under the guiding principle of "Aareal Next Level". The general strategic orientation will continue – with large-volume, international commercial property financing on the one hand and consulting and services for the housing sector in Europe and related industries on the other. The individual business activities will be developed in a targeted manner, in order to sharpen their own independent profiles, accelerate the Group's growth overall and create value for the shareholders and other stakeholders.

The emphasis in the Structured Property Financing segment is to ensure the Bank's success of previous years and secure its existing position in an adverse environment, but also to exploit growth opportunities while adhering to our risk standards. To do so, Aareal Bank makes systematic use of the flexibility gained in recent years regarding regions, asset classes, structures, and exit channels, as well as expanding the activities along the value creation chain. The Consulting/Services Bank and Aareon segments are expected to continue to grow in the years ahead. The objective is to gradually reduce

[1] "Earnings before interest, taxes, depreciation and amortisation" excluding strategic investments (venture and M&A activities) and non-recurring effects

the overlaps and cross-dependencies, while strengthening the independence of the individual brands and business models – whilst securing existing synergies at the same time.

Within the scope of strategic initiatives and measures implemented within "Aareal Next Level", Aareal Bank agreed on a long-term partnership with financial investor Advent International ("Advent") on 14 August 2020, to significantly further strengthen the growth momentum of its subsidiary Aareon. The agreement was concluded following anti-trust approvals on 31 October 2020, with the sale of a 30 % minority stake in Aareon to Advent. The financial terms and conditions of the disposal are based on an enterprise value for Aareon of approximately € 960 million. This corresponds to an equity value of approximately € 860 million, leading to a purchase price for the 30 per cent stake of € 258 million, which was paid in cash. With the new partnership agreed with Advent, Aareal Bank has swiftly brought the structured process for the sale of a significant minority stake in Aareon to a successful conclusion, benefiting from the currently very favourable market environment for resilient software-centric businesses.

Within the scope of a strategic review, Aareal Bank also examined whether Aareal Bank Group's business model remains viable in a normalised environment, once the pandemic has been overcome. Some adjustments will be made within the existing "Aareal Next Level" strategic framework in order to be able to fully exploit the opportunities arising from changes induced by Covid-19, and to retain the Bank's successful performance in the future. The Bank will continue to pursue its risk-conscious, organic expansion of the financing business in its Structured Property Financing segment. Furthermore, the inherent profitability in this business is set to be further enhanced, including through the optimisation of the funding mix and capital structure. In the Consulting/Services Bank segment, the opportunities should be used for expanding the product range, and for entering into further partnerships, with a particular focus on strengthening commission-based business. We envisage even stronger profit momentum through the implementation of the Value Creation Programme for Aareon, which was prepared together with partner Advent. Measures are also being implemented to enhance the efficiency in the organisation, of processes and infrastructure.

Given the general market environment, regulatory dividend restrictions and the perspectives that the results of our strategic review process, including the Value Creation Programme for Aareon, have opened up, our shareholder group and its expectations have already changed, with further changes possibly arising in this respect. One indicator of this is the significant interest that financial investors have been showing in companies operating in the financial sector for some time now. Should new investors acquire substantial stakes in Aareal Bank, further strategic options could arise.

Group targets

Besides the strategic measures and initiatives within the framework of "Aareal Next Level", Aareal Bank Group's focus in the 2021 financial year will be on coping with the impact of the Covid-19 pandemic in the best way possible – together with its clients. In this context, it will be crucial how quickly the emerging recovery of the real economy will gain momentum. With a view to the economic development, Aareal Bank Group continues to anticipate a "swoosh-shaped" trend and expects a marked recovery during this year and 2022[1].

Based on this assumption and current insights, Aareal Bank Group expects a clearly positive consolidated operating profit in a range of between € 100 million and € 175 million for 2021 as a whole (2020: € -75 million), despite high loss allowance. Earnings per share (EpS) are therefore expected to be in the region of € 0.70 to € 1.50 (2020: € -1.50) and the RoE after taxes between 1.5 % and 4 % (2020: -3.6 %). Naturally, in the

[1] For details please refer to our explanations and the description of the macro-economic influencing factors in the Report on Expected Developments and Opportunities of the Structured Property Financing segment.

current environment, this forecast is subject to significant uncertainty, especially with regard to the assumed duration and intensity of the crisis, the pace of recovery and the associated effects on our clients, as well as prevailing uncertainty concerning regulatory and accounting provisions, and the possibility that individual loan defaults cannot be reliably predicted. Effects from a potential, selective continuation of accelerated de-risking activities are not included either.

Income is expected to rise significantly over the previous year. Net interest income should rise to between € 550 million and € 580 million (2020: € 512 million), reflecting the higher (and further growing) loan portfolio. Net commission income should rise further, thanks in particular to Aareon's growth, to between € 250 million and € 270 million (2020: € 234 million). Based on our "swoosh" scenario, we estimate the allowance for credit losses to be in a range to between € 125 million to € 200 million (2020: € 344 million). However, this item is subject to considerably higher uncertainty than usual, due to the Covid-19 pandemic. Administrative expenses should amount to between € 520 million and € 540 million (2020: € 469 million). Besides the non-recurrence of the previous year's cost savings due to Covid-19, this reflects the planned growth of Aareon and the initiatives launched on the basis of the strategic review.

In the Structured Property Financing segment, a portfolio size of around € 29 billion is envisaged by the end of the year, market conditions permitting and subject to exchange rate fluctuations. Aareal Bank plans new business volume of € 7 billion to € 8 billion on this basis.

For the Banking & Digital Solutions segment, we are aiming at further slight net commission income growth (2020: € 26 million) and expect an average deposit volume from the housing industry of around € 11 billion.

It is expected that Aareon will see a marked increase in sales revenue in the region of € 276 million to € 280 million for the current year (2020: € 258 million). Adjusted EBITDA[1)] is likely to further increase to between € 63 million and € 65 million (2020: € 62 million). The forecast does not include any effects from future M&A transactions.

Aareal Bank envisages to achieve consolidated operating profit in an amount of approximately € 300 million already in 2023. This is of course provided the pandemic has been fully overcome by then.

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

Remuneration Report

Review

Aareal Bank AG's Management Board remuneration system proved to be balanced in the exceptional environment created by the Covid-19 pandemic. One key component of the Management Board remuneration system is the definition of ambitious quantitative and qualitative targets and corresponding robust measurement criteria in advance. The calculation of the variable remuneration is then based on the established target achievement level, which largely prevents any leeway for purely discretionary decisions in accordance with the regulatory requirements

In the Supervisory Board's opinion, the Management Board achieved excellent performance in the reporting year and steered Aareal Bank safely through the Covid-19 pandemic. From the Supervisory Board's perspective, the Bank did not lose sight of its strategic objectives at any point in time, key objectives of the Bank were met despite the challenging overall environment, and the sale of a

1) "Earnings before interest, taxes, depreciation and amortisation" excluding strategic investments (venture and M&A activities) and non-recurring effects

minority stake in Aareon also served to significantly strengthen Aareal Bank's equity resources.

Notwithstanding these achievements, however, the effects that the pandemic has had on the Bank's operating profit have a significant impact on the variable remuneration payable to Management Board members and employees, due to the close links between the overall target achievement level of the Management Board members and the overall performance of Aareal Bank Group.

The operating profit for 2020, which was impacted to a considerable degree by the Covid-19 pandemic, means, in terms of remuneration for Management Board members and employees, that the target achievement level for the Group component in 2020, which accounts for what is by far the largest share of the overall target achievement level, was set at only 20 %. As a result, the annual target achievement level of each individual Management Board member, which also comprises the achievement levels for the sectional and individual targets, is approx. 50 % for the 2020 financial year. Since the previous years are included in the Management Board remuneration due to the three-year observation period, this leads to an overall target achievement level of around 70 % for each Management Board member in 2020. What proves to be a positive aspect for the overall target achievement level in 2020 will turn into a negative one in the years that follow, as the significantly reduced annual target achievement level for 2020 will also have a negative impact on any variable remuneration for 2021 and 2022.

In addition, the large proportion of share-based remuneration means that the Management Board members have been affected by the drop in the share price during the Covid-19 crisis. Specifically, the value of more than 250,000 virtual shares held by the members of the Management Board which are subject to deferral/holding periods, was down year-on-year in line with share price performance.

Outlook

Various adjustments to the remuneration system were adopted by the Supervisory Board in 2020 following intensive discussions with Aareal Bank's shareholders in order to achieve an increased focus on the sustainable development of Aareal Bank Group in the long run. For the variable remuneration from the 2021 financial year onwards, this will, in particular, include establishing the systematic requirement for at least 15 % of the targets set to be based on quantifiable ESG criteria in the future. In addition, the proportion of share-based remuneration was already increased to 55 % for the 2020 variable remuneration (with the exception of the Chairman of the Management Board, Hermann Merkens, who was released from his duties at the end of the reporting year). There is still no need for any agreement requiring Management Board members to enter into any proprietary investments in Aareal Bank shares, since the existing system meets the purpose of such an investment. By granting 55 % of variable remuneration in the form of virtual shares, together with the fact that variable remuneration – assuming a target achievement level of 100 % – is nearly equivalent to the fixed annual salary, Management Board members will have regularly earned virtual shares equivalent to a fixed annual salary level after three years. Given the long deferral periods and the holding periods, this is a value which they usually retain until the end of their term on the Management Board (cf. section "(Virtual) shareholdings of Management Board members and share-based remuneration").

The enhanced Management Board remuneration system will be put to the vote at this year's Annual General Meeting, the aim being for it to apply as of the 2021 reporting year.

Remuneration system for the Management Board

Remuneration element	Description	Reference to strategy and long-term development
Fixed remuneration elements		
Fixed annual salary + ancillary benefits = basic remuneration	– Fixed contractually agreed remuneration in line with standard market conditions, paid monthly – Ancillary benefits in line with standard market conditions, in particular a company car that can also be used for private purposes or a lump-sum payment for members who decide against a company car; certain costs for security expenses, including the taxes and social security contributions payable on these amounts; (substitute) social security contribution corresponding to 50 % of the contributions due under the statutory social security scheme – The resulting basic remuneration accounts for around 45 % of the total target remuneration for Management Board members	Guaranteeing the fixed income in the form of a fixed annual salary and ancillary benefits equivalent to scope and complexity of the business and the role and responsibility of the individual members of the Management Board, and competitive on the market.
Pension obligations	– Defined contribution commitment with guaranteed interest – Annual contributions of around 15 % of the total target remuneration for Management Board members – Management Board members are entitled to pension payments when they reach a defined age – In the event of permanent disability, Management Board members are entitled to invalidity benefits even before they reach this defined age	Granting of pension commitments for financial security in retirement and protection in case of death and disability that are in line with market requirements.
Variable remuneration elements		
	– The target variable remuneration corresponds to around 40 % of the Management Board members' total target remuneration – Variable remuneration is determined via the achievement of targets derived from the business and risk strategies, and which are in line with Aareal Bank's corporate and risk culture – Group (70 %), sectional (15 %) and individual (15 %) targets – Group targets usually correspond to the financial KPIs used in the management system, while sectional and individual targets can include both financial and non-financial KPIs. At least 15 % of the target achievement will be based on quantitative ESG targets from the 2021 financial year onwards. – Performance measurement based on criteria whose achievement is determined over a three-year period – No discretionary components besides the targets derived from the strategy – Breakdown of variable remuneration via four components (as per regulatory requirements) – At least 55 % of variable remuneration is share-based – At least 80 % of the variable remuneration is paid out on a deferred basis (20 % as a share bonus with one-year retention period, plus 60 % cash and share deferral) – Maximum overall target achievement level is capped at 150 % of the target value – Maximum variable remuneration cannot exceed fixed remuneration – No compensation is granted in the form of special bonuses extending over and above the components referred to above.	Calculation of variable remuneration on the basis of annual financial and non-financial performance criteria that promote the achievement of the strategic objectives. Provides incentives to Management Board members for implementing the business priorities of Aareal Bank and to act in the interest of the long-term and sustainable positive business development. Group performance targets account for 70 % of overall target achievement, hence prioritising the entire Company's interest, including shareholder expectations. By granting the variable remuneration, Aareal Bank meets the regulatory requirements to which it is subject.

Remuneration element	Description	Reference to strategy and long-term development
Other rules		
Risk-bearing capacity	– Before disbursing the variable remuneration, the Supervisory Board reviews it regarding its compatibility with the risk-bearing capacity.	Disbursing variable remuneration is not meant to threaten Aareal Bank's financial solidity.
Penalty and clawback	– All components of the variable remuneration are subject to penalty and clawback provisions. – Admission of an adjustment to outstanding remuneration and/or clawback of remuneration already disbursed in case of clawback events.	Within the meaning of responsible and sustainable corporate governance, and for the purpose of implementing the regulatory requirements, penalty and clawback rules are a mandatory part of good corporate governance, which in turn is firmly enshrined in Aareal Bank's strategy.
Consideration of extraordinary developments	– (Modifier) adjustment of Group target achievement level by 20 percentage points possible in cases involving exogenous circumstances. – In principle, no subsequent adjustments to remuneration targets, unless extraordinary developments result in the business strategy being adjusted during the year.	In order to ensure that the remuneration system provides incentives for the actual performance of the Management Board member with regard to the sustainable and long-term development of Aareal Bank Group, adjustments can be made subject to pre-defined and very restrictive conditions.
From the 2021 reporting year onwards: Maximum remuneration of € 5.5 million per Management Board member (within the meaning of section 87a of the German Public Limited Companies Act (Aktiengesetz – "AktG")	– Maximum expense amount for the financial year which includes the fixed annual salary, variable remuneration elements (incl. the development of the virtual shares over the next six years), ancillary benefits and pension obligations (service cost). Severance payments are excluded from this amount as a non-standard remuneration component. – The maximum remuneration is stated individually for each member of the Management Board and applies until the next proposal is made to the Annual General Meeting. It is calculated based on the maximum possible values for the abovementioned remuneration components, plus a buffer for fluctuations in the share price, for example.	In order to define absolute values to ensure the proportionality of the amount of Management Board remuneration, the maximum remuneration sets a specific upper limit. This theoretical maximum value is based on a maximum possible target achievement level over the entire three-year assessment period and maximum share price performance. This means that the maximum remuneration can be clearly distinguished from the total target remuneration.

Remuneration structure

Total target remuneration comprises a fixed component (fixed annual salary plus ancillary benefits (= "basic remuneration") and annual retirement benefits) and a variable component, the structure of which is subject to regulatory requirements.

The fixed annual salary plus ancillary benefits accounts for approximately 45 % of the total target remuneration, with the fixed annual salary determining the vast majority. The ancillary benefits generally amount to a share of between one and two percentage points. In order to be able to report a proportion of retirement benefits that is as stable as possible, the information presented is based on the annual pension contributions, which, unlike the IAS 19 disclosures, do not differ depending on the member's age and length of service on the Management Board. The maximum remuneration is still based on the expenses according to IAS 19, which are also shown in the corresponding remuneration tables. The target variable, performance-related remuneration comprises approx. 40 % of the total target remuneration.

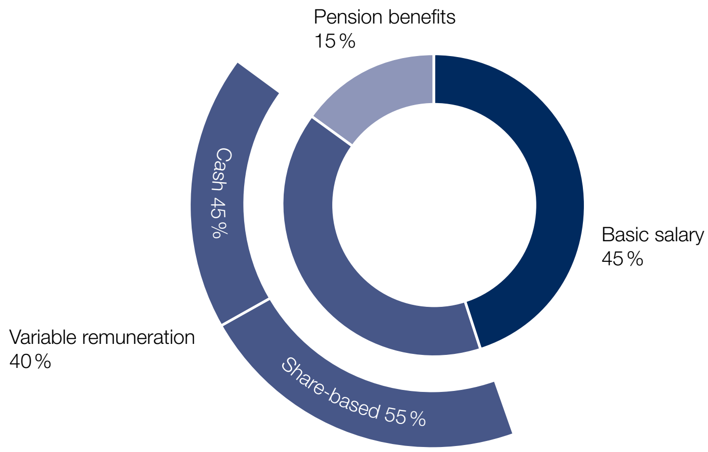
In line with the "1:1 rule" that applies to credit institutions, the maximum variable remuneration must not exceed the fixed remuneration component. In order to allow target overfilling in the first place, the share of total target remuneration attributable to the target variable remuneration must be below the fixed remuneration share. In order not to motivate Management Board members to take inappropriate risks in line with Aareal Bank Group's risk culture, no use was made of the option to adjust the 1:1 rule via the Annual General Meeting.

The relative shares referred to above can shift by a few percentage points due to fluctuating ancillary benefits.

The Supervisory Board can adjust the reference values for the fixed and variable remuneration components in the context of the defined maximum remuneration while maintaining the relative proportions of fixed and variable components provided for in this remuneration system. Until further notice, however, the reference values for fixed and variable, performance-related remuneration components set out below apply.

Management Board remuneration structure

%



Fixed remuneration component

The fixed remuneration component of a Management Board member consists of three components – the fixed annual salary, ancillary benefits, and contributions to retirement provisions.

Fixed annual salary

Within Aareal Bank's corporate governance system, the members of the Bank's Management Board discharge operative functions in addition to their managerial duties. They prepare and implement strategic objectives in cooperation with their employees. Management Board members are remunerated in line with this comprehensive set of duties.

The fixed annual salary currently amounts to € 1,425,000 for the Chairman of the Management Board and to € 900,000 for ordinary Management Board members.

Ancillary benefits

As well as paying a fixed annual salary, Aareal Bank grants the members of the Management Board ancillary benefits in line with standard market conditions.

For example, Aareal Bank provides a company car to Management Board members, which may also be used for private purposes. If Management Board members decide against a company car, they receive a lump-sum compensation payment instead.

Management Board members also receive an amount equivalent to up to 50 % of the contributions to the statutory social security system.

They also receive certain insurance benefits/insurance compensation benefits. In addition, Aareal Bank bears the costs incurred for certain security expenses.

The members of the Management Board are also granted insurance cover in line with standard market conditions, such as D&O insurance (subject to the statutory deductible), group accident insurance or health insurance for travel abroad.

The Supervisory Board can grant other or additional ancillary benefits that are customary on the market, such as the assumption of costs for trips home to see family.

In principle, all members of the Management Board are equally entitled to the ancillary benefits. The benefits can, however, vary in terms of their type and amount depending on the member's personal situation. They can also fluctuate considerably from year to year. This is particularly true with regard to security expenses, which are not usually incurred in similar amounts every year.

Pensions and retirement benefits

The benefit regulations as agreed in the service contracts apply to the members of the Management Board. All members of the Management Board are granted a defined contribution commitment:

This currently amounts to a total of € 464,000 p.a. for the Chairman of the Management Board and € 293,000 p.a. for ordinary members of the Management Board, and thus accounts for around 15 % of the target remuneration structure of the Management Board members. The contributions bear interest at a guaranteed rate of 4 %. In addition, members of the Management Board can make use of a deferred compensation system.

Members of the Management Board are entitled to pension payments when they reach a defined age. This is age 60 for members appointed before 1 January 2013 and currently age 62 for all other members. In the event of permanent disability, Management Board members are entitled to invalidity benefits even before they reach this defined age.

The amounts are subject to a guarantee adjustment of 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.

Performance-related variable remuneration

Long-term and sustainable focus of the targets

The structure of the variable remuneration system is subject to detailed requirements set out in the bank regulatory provisions. The calculation of the variable remuneration is generally split into two phases. In the first phase, the achievement of targets derived from the strategy is determined over a period of three years at three levels: Group, sectional and individual. The target achievement level is multiplied by the reference value and produces the amount calculated (e.g. for an ordinary member of the Management Board: 780,000 x 90% = € 702,000). The amount calculated is then paid out in the second phase in four different components, including 80 % that is paid out on a deferred basis and at least 55 % paid out in virtual shares over a period spanning several years (see "Deferred disbursement, through retention of variable remuneration components and virtual shares (phase 2)").

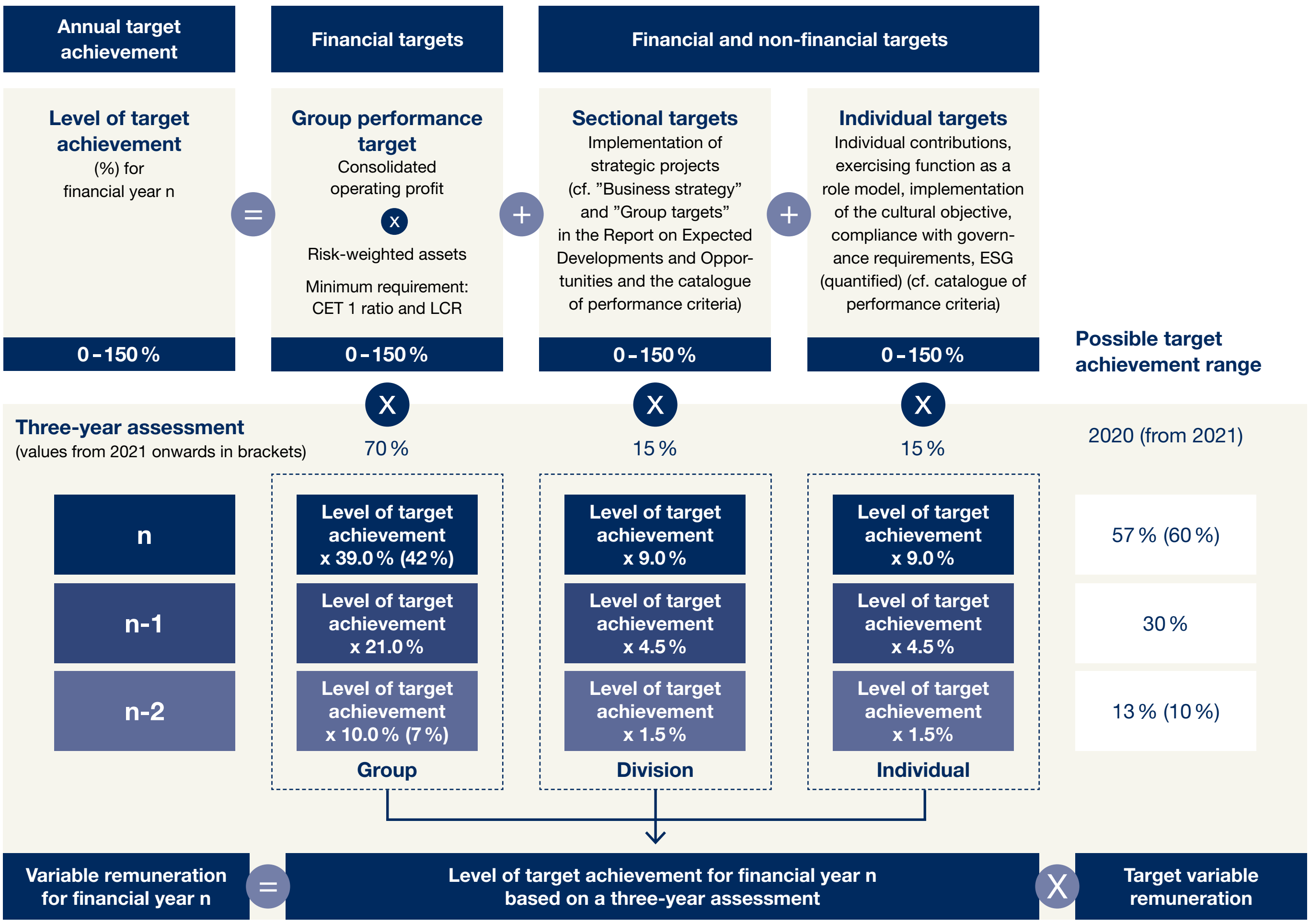
Among other things, the fact that the targets are geared towards the strategy and the subsequent adjustment based on share price performance over the next six years promotes sustainable and long-term company development while at the same time taking the interests of the shareholders into account. This is also achieved through the penalty, clawback, modifier rules and the check to ensure compatibility with sufficient risk-bearing capacity.

Multi-year performance measurement across different target levels (phase 1)

A significant part of Aareal Bank's variable remuneration is governed by law: besides the general requirement – pursuant to theAktG – that the remuneration system be focused on a sustainable company development, sections 19 and 20 of the German Regulation on Remuneration in Financial Institutions (Institutsvergütungsverordnung – "InstVergV") require that target achievement be determined on the basis of at least three target levels, and over a minimum assessment period of three years. Accordingly, Aareal Bank's remuneration system for the Management Board provides for three target levels of:

- Group performance;
- sectional performance; and
- individual performance.

Target achievement and variable remuneration for financial year n

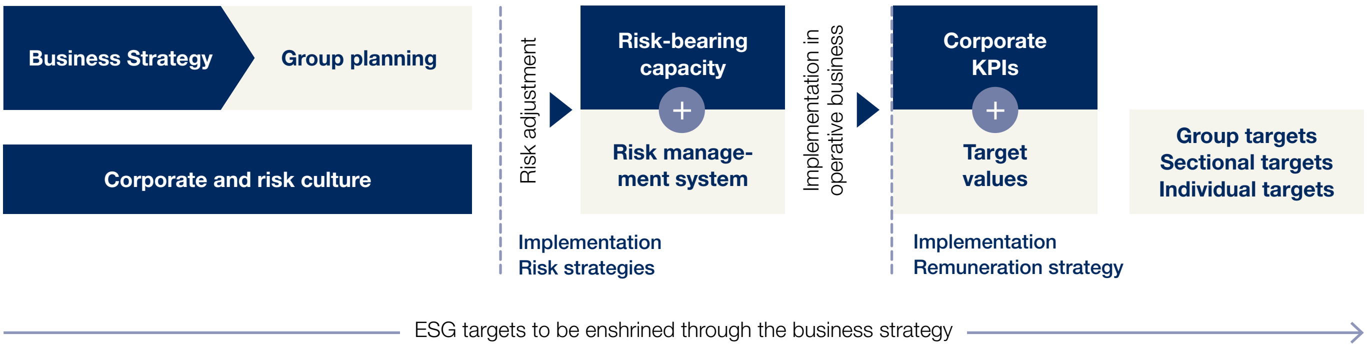


Target achievement for each target level is determined on the basis of a three-year assessment period.

The targets set at all three levels are focused on sustainable and long-term growth and are designed to be forward-looking. To measure and monitor target achievement, various KPIs are determined annually for targets, and their degree of achievement is assessed at the end of the financial year. The target achievement level for each target level is thus determined by the respective KPI achievement of the past financial year and by the degrees of KPI achievement of the two previous financial years **(three-year assessment basis).**

The members of the Management Board are responsible – and epitomise – the Company's success. This is also reflected in the **weighting of the target levels.** Accordingly, achieving Group performance targets accounts for the clear majority (generally 70 %) of target achievement. This target level is determined solely on a quantitative basis; performance is therefore calculated based on whether the target value specified by the Supervisory Board for the components consolidated operating profit and RWA, or for other corporate financial indicators defined annually by the Supervisory Board, has been achieved. The other two target levels, the sectional and individual target levels, are generally weighted at 15 % each. The Supervisory Board

System for defining targets



reserves the right to adjust the weightings attached to the performance levels annually.

To set ambitious targets and a strong incentive for successful Management Board work, target achievement levels are incorporated at different levels over time. The target achievement level is calculated by looking at performance in more than one year at all target levels. This means that, generally speaking, the most recent reporting year is weighted at 60 %, the preceding one at 30 %, and the oldest year in the assessment period at 10 %. A transitional rule applies for the 2020 reporting period, whereby the reporting years 2020, 2019 and 2018 are weighted at 57 %, 30 % and 13 %, respectively.

Pursuant to section 25c (4a) of the German Banking Act (Kreditwesengesetz – "KWG"), the strategy is to be geared towards the Bank's sustainable development. As early on as during the development process, the business strategy is reviewed as to its compatibility with the corporate and risk culture, the risk strategies and the Bank's sustainability approach, and is adjusted if necessary. This means that the remuneration targets and KPIs derived from the strategy do not promote short-term successes, but rather support the Company in its long-term and sustainable development **(pay-for-performance principle).** As a result, they serve the interests of the shareholders, employees and other stakeholders of Aareal Bank Group.

Remuneration parameters (ex-ante risk adjustment)

The targets are made up of quantitative and qualitative components. A target value for 100 per cent target achievement, a minimum ambition level and a maximum achievable value are set for quantitative criteria. Qualitative values are measured using different formats that suit the corresponding target parameters. These can include comparisons with project targets, internal and external studies, section-specific reports, as well as statistics on how the Bank is perceived by its employees or clients. Specific target achievement is reported on an ex-post basis (cf. "Target achievement" section).

Amongst other things, the Company's interests are duly taken into account by the fact that **Group targets** are geared towards the KPIs used for corporate management purposes. These KPIs are generally based directly on the Group's performance indicators, which are defined in the Group Management Report. In order to reduce the influence of one-off effects and to ensure that the KPIs fulfil their purpose in terms of measuring the actual performance of Management Board members, certain effects are already excluded from target achievement when the targets are set, e.g. changes due to external regulatory requirements, M&A transactions, or comparable effects. The Supervisory Board sets target values for the Group on the basis of the consolidated operating profit, risk-weighted assets (RWAs) and/or other indicators that it defines based on the performance indicators (cf. the "Management system" section of the Group Management Report), and determines the result that constitutes achievement of each target. Consolidated operating profit is chosen as the income target, whereas RWA is used as a risk-adjusted target. The 100 % targets set for the target parameters complied with the corporate objectives communicated to the capital markets in the past, and will continue to do so in the future, too. The maximum achievement level for target consolidated operating profit is 150 %; for the RWA target, it is 125 %. The overall target achievement level is calculated by multiplying all target values; it is capped at a target achievement level of 150 %.

Sectional targets are related to the respective Management Board member's area of responsibility pursuant to the schedule of responsibilities. Accordingly, the Supervisory Board sets targets which the organisational units assigned to the respective Management Board members need to fulfil in order to achieve the strategic objectives of the Company as a whole. Between two and four targets are determined for each Management Board member. The Supervisory Board uses the sectional component to measure the contribution to the implementation of the strategy made by the units for which the individual Management Board member is responsible. Based on the strategic framework (currently "Aareal Next Level"), the Supervisory Board selects certain initiatives and assigns those initiatives to the individual members of the Management Board. The KPIs used by the Supervisory Board typically include qualitative and quantitative criteria, as shown in the catalogue of performance criteria. In line with Aareal Bank Group's management system, sectional targets for Management Board members responsible for Sales units comprise growth and development of main strategic fields of business and are measured, for example, by the level of specific property portfolio increases or the revenue generated with digital products.

Individual targets refer to the Management Board members' individual performance as role models for the organisation ("tone from the top"). A maximum of two individual targets are determined for each Management Board member. As with the other targets, the individual Management Board member is set targets that promote the implementation of Aareal Bank Group's strategic objectives, but are primarily to be fulfilled by him/her.

Catalogue of possible performance criteria (financial/non-financial, quantitative as well as qualitative)

Key performance indicators used in the Group management system	Strategic project (Aareal Next Level)
Increasing flexibility	Sustainability of the organisation
Increase in growth	Establishing sustainability in the core business
Capital market target	Expansion of sustainable products
Market expansion	Innovative power
Budget target	Client satisfaction
Efficiency enhancement	Dialogue with employees
Liquidity planning	Empowering the next generation
Targets for risk indicators	Safeguarding expertise
Effectiveness of the organisation	Transparency
Scaling client relationships	

ESG targets can be established at both sectional and individual level. The specific ESG target parameters are disclosed as part of the reporting process (annual report for the year concerned) together with the other parameters used. In order to ensure that the increased importance of ESG aspects in Aareal Bank's strategy are adequately reflected in the remuneration system, quantifiable ESG targets will be included in the overall target calculation with a minimum weighting of 15 % from the 2021 financial year onwards, and are covered, in particular, by the individual component. The use of quantitative ESG targets allows for a high level of transparency regarding Aareal Bank AG's ESG focal areas and at the same time creates targeted incentives for a long-term sustainable strategy. In addition to the individual level, the sectional level can also include ESG targets to add more weight to ESG aspects.

In its ESG targets, Aareal Bank does not separately reflect compliance with statutory regulations, since adherence to internal and external provisions is deemed to be a necessary condition for confidential cooperation; as such, separate target-setting within the scope of variable remuneration is obsolete. Wilful breaches of internal and external rules may rather trigger a so-called **penalty-triggering event** which in turn can lead to variable remuneration no longer being paid at all or to retained remuneration components being reduced ex post, and can even result in the **clawback** of remuneration components that have already been granted.

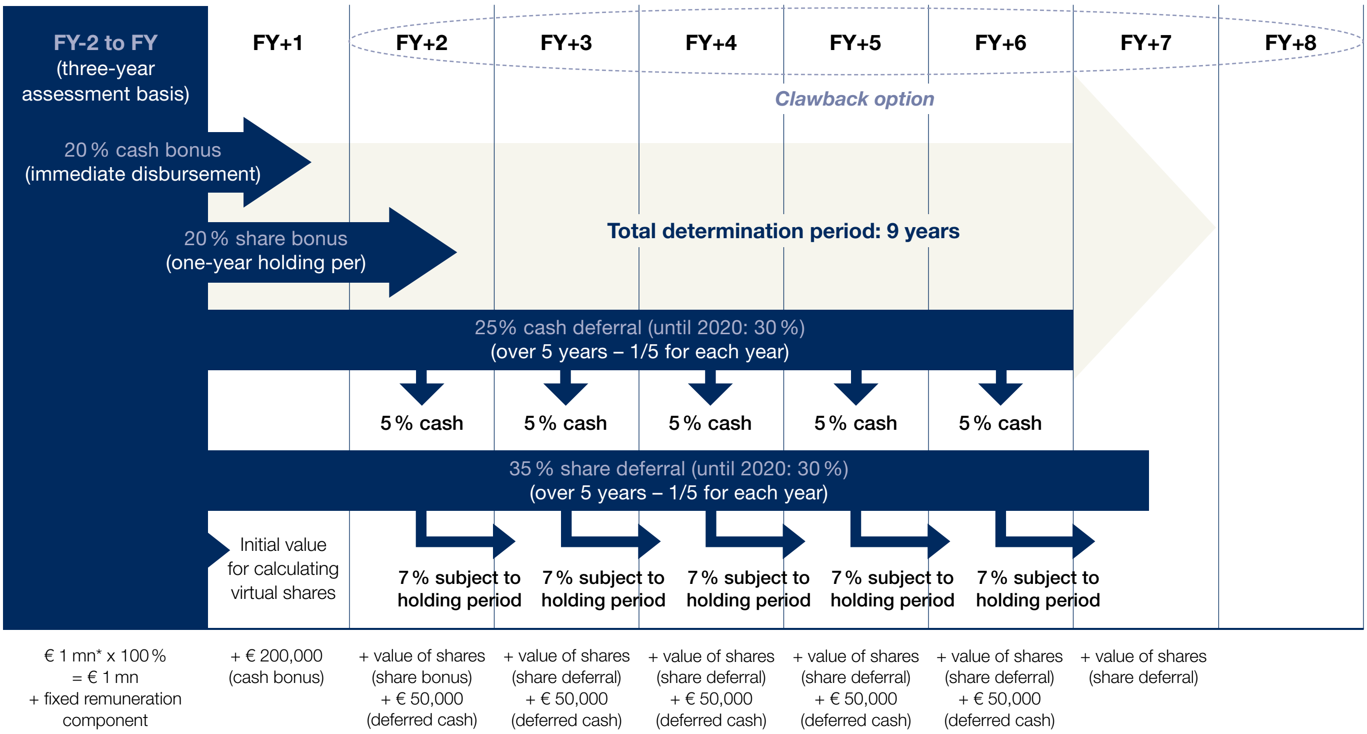
Deferred disbursement, through retention of variable remuneration components and virtual shares (phase 2)

To ensure that the remuneration system provides long-term incentives, the initial value for variable remuneration – as determined according to the principles set out above – is awarded at the end of the financial year, according to the following principles:

- After confirmation of the total target achievement level by the Supervisory Board, 20 % of the variable remuneration are disbursed in cash **(cash bonus).**
- After confirmation of the total target achievement level by the Supervisory Board, a further 20 % of the variable remuneration is granted in the form of virtual shares **(share bonus with holding period)** and forms part of the share bonus plan.
- 25 % of the variable remuneration is retained **(cash deferral),** and disbursed in cash – pro rata temporis – over a five-year deferral period.
- The remaining 35 % of the variable remuneration forms part of the Share Deferral Plan **(share deferral with holding period).**

Sample disbursement methodology, based on 100% target achievement for the financial year

The Supervisory Board regularly examines, at the beginning of each year and prior to disbursement or conversion into virtual shares, whether the original target achievement still applies, and whether a penalty-triggering event has occurred which requires reduction or clawback of variable remuneration.



*For the sake of simplicity of this sample presentation, variable remuneration for a 100 % target achievement level was set to a notional value of € 1 million.

Consequently, 60 % of the variable remuneration is granted on a deferred basis, supporting the long-term focus of the variable remuneration system. This means that deferred disbursement applies to a total of 80 % of variable remuneration determined, for up to six years. 55 % of the variable remuneration is granted as share-based remuneration and has a holding period of one year, which applies to both the share bonus and the individual tranches of the share deferral. The fact that the variable component is predominantly share-based helps to ensure the sustainability, as well as the long-term focus, of the remuneration system and promotes alignment with shareholder interests.

Five-year retention period

For the portion of performance-related remuneration that is deferred initially as a cash deferral or a share deferral (60 %), the Supervisory Board makes a decision regarding the granting of one fifth of the amount in the five years following the determination of the performance-related remuneration (cf. the sub-section ”Ex-post review of target achievement and behaviour of the Management Board”).

Until the end of each respective deferral period, there is no right to the relevant remuneration components. No interest or dividends will accrue. Once the deferred remuneration components for Management Board members are vested, the cash deferral is paid out in cash and the share deferral is converted into virtual shares subject to a one-year holding period, in line with regulatory requirements.

Share bonus with holding period (20 %)

The portion of the performance-related remuneration which is subject to the share bonus plan will be converted into an equivalent number of virtual shares. The calculation of the number of virtual shares is based on the weighted average price on the basis of five (Xetra®) exchange trading days after publication of the preliminary results for the financial year for which the share bonus is granted (subscription price). The date of publication of the preliminary results is used as the reference date.

The virtual shares so determined are posted to a virtual account and are held for one year. They will be converted, automatically and without delay, into a cash amount and disbursed immediately after the Supervisory Board meeting which passes the resolution on the adoption of the annual financial statements for the first financial year following the financial year for which the virtual shares were granted (“holding period”). The conversion will be effected using the weighted average price calculated on the basis of the five (Xetra®) exchange trading days following the publication of the preliminary results for the year preceding the payout.

The payout amount of the share bonus of a given financial year may vary depending on the share price development and has been limited to a maximum of 300 % of the agreed initial value (ceiling).

Share Deferral Plan (35 %)

In the five years following determination of performance-related remuneration (deferral period), the Supervisory Board decides whether in each case a fifth of the share deferral should be converted into virtual shares.

The rules of the Share Bonus Plan are applicable to the calculation of the number of virtual shares, subject to the proviso that the weighted average price calculated on the basis of the five (Xetra) exchange trading days following the publication of the preliminary results for the financial year in respect of which variable remuneration was determined. This is designed to preserve the reference to the original assessment period.

The ceiling value is applicable for the conversion of the virtual shares, with the proviso that the payout amount following the conversion of the virtual shares of a tranche into a cash payment must not exceed 300 % of the share deferral (35 % of the initial value of performance-related remuneration) set for the financial year in question (which may have been reduced following the application of a penalty rule or as a result of an instruction by BaFin).

With regard to the deviation from the recommendation set out in the German Corporate Governance Code regarding the four-year holding period that we have declared as a precaution, we refer to our Declaration of Compliance with the German Corporate Governance Code at www.aareal-bank.com/en/about-us/corporate-overnance/declaration-of-compliance/

Ex-post review of target achievement and behaviour of the Management Board

Backtesting regarding retained remuneration components

Before the Supervisory Board decides on conversion or disbursement of retained remuneration components, it reviews whether the target achievement level originally agreed upon is still held to be correctly determined, based on current knowledge. For example, where an indicator used to determine remuneration needs to be adjusted ex-post, this can also reduce the variable remuneration determined – and hence, result in a reduction in the amount retained. If it turns out, at a later date, that a target was not achieved or if the assessment of qualitative targets shows a negative deviation when the target achievement measurement is repeated as part of a retrospective review, the variable remuneration can also be reduced ex-post.

Penalty review

When determining variable remuneration, as well as prior to every disbursement of cash components or conversion into virtual shares, the Supervisory Board verifies whether there are any reasons, besides the achievement of targets, justifying a reduction in, or even the loss of, variable remuneration.

Such **penalty-triggering events** include inappropriate behaviour, behaviour in breach of duties, or negative performance contributions of Management Board members, which cannot be offset through positive performance contributions at other levels. They include, for example, wilful breaches of the Code of Conduct and/or internal and/or external rules, conduct that damages the Bank's reputation, or other misconduct. If any retained performance-related remuneration components are not awarded, or only in part, the remaining sum is forfeited, i. e. it is not carried forward into subsequent years. The variable remuneration must be reduced to zero in the event of **negative performance** contributions. In accordance with the regulatory requirements governing remuneration, negative performance contributions refer to a scenario in which the Management Board member was significantly involved in, or responsible for, any behaviour which led to considerable losses, or material regulatory sanctions, for the Bank.

Clawback

Agreements reached with the Management Board members ensure that variable remuneration already paid out has to be clawed back in the event of negative performance contributions (see Penalty review). The amounts can be clawed back until two years have expired since the end of the last retention period for the variable remuneration paid for the financial year in question.

Allocation to appropriate periods

The penalty review and backtesting processes are applied to the appropriate periods. Missed targets/penalty-triggering events defined as part of the penalty review are allocated to a particular assessment period. They are allocated to the year in which the target was missed/the penalty-triggering event occurred, meaning that the variable remuneration is also adjusted for the corresponding year.

Restrictions and additional provisions

Impact of special external conditions (modifiers)

The Supervisory Board is entitled to increase or decrease the level of target achievement for the Group component by up to 20 percentage points (a so-called modifier) in the event of unforeseeable changes to the economic environment which are beyond the Management Board's influence or control (i. e. only on the basis of external conditions). This will not affect the 150 % cap, which cannot be circumvented by the modifier.

Subsequent adjustments to targets and target values (KPIs) are generally not permitted. Such adjustments may be made as an exception if extraordinary developments require adjustments to be made to the business strategy and the remuneration targets or parameters have to be adjusted accordingly in order to maintain the long-term and sustainable focus.

Maximum remuneration

Pursuant to section 87a (1) sentence 2 no. 1 of the AktG, the Supervisory Board has set an upper limit for the total amount of all remuneration elements in a given year, i.e. currently consisting of the fixed annual salary, ancillary benefits, the annual pension expenses pursuant to IAS 19, and variable remuneration (maximum remuneration). The maximum remuneration limits the maximum total remuneration (sum of the individual components based on maximum target achievement) that can be granted for one year. The maximum remuneration amounts to € 5.5 million (gross) for each Management Board member.

This upper limit refers to the total benefits granted to a member of the Management Board for his/her work on the Management Board in the financial year in question. Payments of long-term variable remuneration components, i.e. those that are paid out on a deferred basis, are attributed to the year of vesting. Ancillary benefits are recognised based on the non-cash benefit amount used for tax purposes. The maximum remuneration defined in this remuneration system does not release the Supervisory Board from its obligation to review the appropriateness of the specific upper remuneration limits when determining individual remuneration.

In contrast to remuneration systems featuring what are known as share ownership rules, in which Management Board members commit to holding a certain proportion of physical shares, the share price performance of virtual shares has to be included in the maximum remuneration. Standard practice in the market involves accounting for expenses for pension commitments in accordance with IAS 19. This figure is not, however, based on the annual contribution, but is largely determined by the age of the Management Board members and their length of service, and is subject to fluctuations.

Any severance payments paid in the event of premature termination of Management Board activities are not included in the maximum remuneration. The regulatory requirements that apply to severance payments remain unaffected.

Remuneration when positions in executive bodies are assumed

The assumption of paid or unpaid forms of secondary employment, honorary positions, supervisory board, advisory board or similar mandates, as well as work on expert opinions, require the prior written consent of the Supervisory Board's Executive and Nomination Committee. If and to the extent that the paid forms of secondary employment are directly related to the Bank (e.g. in cases involving mandates within the Group), the remuneration paid for these activities is offset against the individual's fixed annual salary. In the event that members of the Management Board assume positions in executive bodies outside of the Group, the Supervisory Board is responsible for deciding whether to offset the remuneration earned by the Management Board member in question against the total remuneration from his or her Management Board position.

Hedging ban

The contracts of Management Board members prohibit them from undertaking to limit or override the risk orientation of their remuneration by initiating personal protection or countermeasures (hedging ban).

Risk-bearing capacity and parallel interest with shareholders

To preserve the Company's continued survival (and hence, shareholders' investment), variable remuneration is generally subject to a review performed by the Supervisory Board pursuant to section 7 of the InstVergV. This review is based on the Recovery Plan (which is mandatory for Aareal Bank as a significant institution) and the thresholds defined therein. These thresholds include achieving minimum profitability indicators such as the return on equity. In the event of these so-called "early warning thresholds" being reached, the Supervisory Board will decide, in its reasonable discretion, whether variable remuneration for the Management Board needs to be reduced. The total amount of variable remuneration is set to zero if Aareal Bank's risk-bearing capacity is no longer sufficiently ensured. In addition, pursuant to section 45 (2) nos. 10 and 11 of the KWG, the German Federal Financial Supervisory Authority (BaFin) may impose further conditions or restrictions, or may instruct that the total amount of variable remuneration be cancelled.

The provisions enacted by the German Risk Reduction Act (Risikoreduzierungsgesetz – "RiG") (section 45 (2) and (7) of the KWG) allow the competent supervisory authority to prohibit the payment of variable remuneration if state support measures are used or if the remuneration system is assessed as being inappropriate. The Supervisory Board will observe any corresponding regulatory restrictions.

Additional conditions for achievement of Group targets

In addition to ensuring sufficient risk-bearing capacity, the Supervisory Board defines additional conditions that would lead to the forfeiture of the Group component in the event of non-fulfilment. These additional conditions are set via specific indicators of sufficient capital and liquidity resources, and usually relate to CET1 and LC ratios that exceed the minimum thresholds.

Benefits paid in the event of temporary, non-permanent incapacity for work

In the event of temporary, non-permanent incapacity for work, members continue to receive their fixed annual salary for a period of up to six months. The Supervisory Board can decide at its own discretion whether the variable remuneration components are also granted in full or in part for the periods in which continued salary payments are made.

Contractual terms; permanent disability; death

The Management Board employment contracts are concluded for the duration of the appointment period in each case. This is usually three years for an initial appointment and five years for each subsequent appointment. In accordance with the German Public Limited Companies Act, the employment contracts do not provide for any option for termination for convenience; the right of both parties to terminate the employment contract without notice for good cause remains unaffected.

The Management Board employment contract ends automatically if the member becomes permanently incapacitated for work. In such cases, the Management Board employment contracts provide for the continued payment of the fixed annual salary (plus (substitute) social security contributions) from the beginning of the permanent disability and for a period of up to six months (taking into account the periods for which continued salary payments were already made), but not extending beyond the point in time at which the employment contract would have ended normally.

The contracts of employment may state that, if a member of the Management Board dies during the term of his/her contract, widows, widowers or civil partners and legitimate children (provided they have not yet turned 27 and are still in vocational training/further education) are entitled, as joint and several creditors, to continued fixed salary payments for the month of death and the following six months, but until the contract ends at the latest. In such cases, the variable remuneration is calculated pro rata for the period leading up to the member's death.

Rules governing severance pay

The Management Board employment contracts do not (with the exception of the provisions that apply in the event of a change of control) include any obligation to make severance payments in cases involving the early termination of employment relationships **(rescission of the agreement without good cause).** However, severance payments may be included in individual termination agreements, provided that these are specified in accordance with regulatory requirements, in particular with the InstVergV. The agreements concluded with members of the Management Board state that, in the event of the premature termination of their term on the Management Board without good cause, payments, including ancillary benefits, made to the Management Board member in question must not exceed twice the annual remuneration and must not constitute remuneration for more than the remaining term of the employment contract (severance cap).

In the event of the loss of a Management Board position due to a **change of control** (i. e. essentially in cases of involuntary loss), the Management Board employment contracts may state that the members are to be paid the fixed remuneration component, the performance-related remuneration as well as the contractually agreed ancillary benefits for the remainder of the term of the contract. In such cases, the performance-related remuneration is subject to the above-mentioned conditions; that is, in particular the deferral periods, the holding periods and the penalty rules are applicable. In cases like these, the extent to which sectional and individual targets were achieved on average during the last three financing years prior to the termination of the Management Board position is used as a basis to determine the target achievement level for the individual and sectional targets for the remaining term of the contract.

In the event of resignation from the Management Board within a certain period after a change of control, the Management Board employment contracts may state that the members are only to receive the fixed remuneration and the contractually agreed ancillary benefits for the remainder of the term of the contract. In this case, the contracts do not provide for any entitlement to the variable remuneration component.

The total amount of the payments made to a member who has left due to a change of control is also limited to the severance cap of a maximum of two years' remuneration/remuneration for the remaining term of the contract.

Newcomer rule

The Supervisory Board can remunerate newly-appointed members who have not previously held a position on the Management Board of a comparable institution in line with an entry level of 80% of fixed and variable remuneration for ordinary members of the Management Board, reflecting lack of experience. If the Management Board member is re-appointed, the Supervisory Board will also decide upon the potential increase of remuneration to the normal level. However, since the Supervisory Board decides upon the specific selection as well as remuneration of individual Management Board members, within its reasonable discretion, and taking the Company's specific needs and the general appropriateness review into account, it is possible to diverge from this rule.

The Supervisory Board has decided to only gradually build up the three-year period for measuring remuneration targets (phase 1) for newly appointed Management Board members. In the Supervisory Board's view, newly-appointed members of the Management Board should not be held accountable for past developments. In accordance with the regulatory requirements pursuant to the InstVergV, the deferral period is extended correspondingly for periods with a shortened assessment period. Hence, for the first year, the assessment period is only one year, with the deferral period being extended from five to seven years. For the second year, the assessment period is extended to two years and the deferral period shortened to six years. The remuneration system for the Management Board will be applied, as provided, from the third year onwards.

Post-contractual non-compete clause

The Supervisory Board can agree a post-contractual non-compete clause for a period of up to 24 months. For this period, appropriate compensation to be determined on a case-by-case basis is agreed. Furthermore, if such a non-compete clause is agreed, the employment contracts generally state that the compensation is to be paid in monthly instalments, offsetting any severance payments.

Appropriateness review

In accordance with section 12 of the German Ordinance on Remuneration in Financial Institutions (Institutsvergütungsverordnung – InstVergV), the Supervisory Board regularly (at least annually) checks whether Management Board and employee remuneration is appropriate.

The appropriateness of the remuneration paid to the Management Board is assessed in particular in view of the remit and performance of the Management Board member, as well as the Bank's situation. The function, area of responsibility and experience of the individual Management Board members are taken into account when determining the amount of the total target remuneration. As a result, the Supervisory Board can set different remuneration levels for different Management Board members at its own due discretion, taking into account criteria such as standard market practice, the experience of the Management Board member, his/her length of service on the Management Board and the Management Board members area of responsibility.

When assessing whether the Management Board remuneration is in line with standard market practice, both vertical compatibility with peer group companies and horizontal compatibility with the remuneration structures for the employees of Aareal Bank AG in Germany are taken into account.

The vertical comparison involves looking at how the Management Board remuneration relates to the remuneration paid to the senior management team, and how it relates to the remuneration paid to the workforce as a whole. For the purposes of the vertical comparison, the workforce as a whole refers to all employees of Aareal Bank AG and its German Group companies working in Germany. As well as looking at how the remuneration paid to the two comparison groups currently relates to the remuneration paid to the Management Board, the Supervisory Board also looks at the development of the remuneration paid to the groups described over time.

When setting the Management Board remuneration, the Supervisory Board also ensures that the remuneration system for Management Board members is compatible with the system used for employees who are not covered by a collective agreement. This is achieved, among other things, by ensuring that the structure of the variable remuneration system – apart from regulatory requirements – is essentially the same for the Management Board and the Bank's employees: the incentives set for the Management Board and employees are focused on the Group's performance, and individual employee targets are developed based on the Management Board's sectional targets, which are, as a result, also closely linked to the corporate strategy. The pension benefits for employees are also aligned with the system that applies to the Management Board members, which is reflected, by way of example, in the fact that the same interest rate applies.

In addition, a full review is conducted at least every four years and at the latest before the remuneration system is resubmitted to the Annual General Meeting for approval. In addition to reviewing the amount of remuneration paid to the Management Board members, this review also takes into account employees' remuneration and employment conditions.

To evaluate whether the Management Board's specific total remuneration is in line with common practice/that of other companies, the Supervisory Board has set two horizontal comparison groups. The comparison group companies are selected based on Aareal Bank's market position (in particular: sector, size, country). Therefore, the comparison groups are companies listed in the relevant stock exchange indices (currently the DAX, MDAX und SDAX), as well as banks of a similar size. The composition of the peer groups is reviewed on a regular basis as part of the full appropriateness review process.

Right to allow temporary deviations from the remuneration system

The Supervisory Board is entitled to temporarily deviate from the remuneration system for Management Board members pursuant to section 87a (2) of the AktG if it is necessary for the sake of the Company's long-term wellbeing.

This can prove necessary, for example, in the event of far-reaching and extraordinary changes in the economic situation, such as the occurrence of a severe economic crisis. Similarly, a significant change in corporate strategy may require a deviation from this remuneration system in order to ensure that appropriate incentives are set.

Deviations from the remuneration system are only possible by way of a corresponding Supervisory Board resolution based on a proposal put forward by the Remuneration Control Committee confirming the need for the deviation.

The option of deviating from the remuneration system for the Management Board temporarily is limited to the following components: the amount of the fixed maximum remuneration, the performance criteria for variable remuneration, ranges for possible target achievement levels for the variable remuneration parameters, the specific remuneration components and the relative shares of fixed and variable remuneration components. Deviations can also be made by temporarily granting additional remuneration components, for example in the form of extraordinary ancillary and special benefits.

Remuneration of the Management Board

Measures in the 2020 financial year

Absence of Hermann J. Merkens due to ill health

The Chairman of the Management Board of Aareal Bank AG, Hermann J. Merkens, informed the Supervisory Board and the other members of the Management Board on 8 November 2020 that for health reasons, he would not be able to perform his duties as member and Chairman of the Management Board for an expected period of three to four months. The other members of the Management Board assumed Mr Merkens' portfolio of responsibilities based on the substitution regulations in place with immediate effect. This relates primarily to Marc Hess, who, in addition to his role as Chief Financial Officer, assumed responsibility for Group Strategy, Group Communications and Governmental Affairs and Investor Relations/Sustainability, and Thomas Ortmanns, who, in addition to his role as Chief Digitalisation Officer, assumed responsibility for Group Human Resources & Infrastructure and Corporate Affairs, including the Legal department.

Increase in share deferral

For the ordinary members of the Management Board, the share deferral portion of the variable remuneration has been increased from 30 % to 35 %. The share of cash deferral has been reduced from 30 % to 25 % in turn. This increases the proportion of variable remuneration attributable to share-based payment to a total of 55 %, which already takes effect for the 2020 financial year. This adjustment has not yet been made for Mr Merkens due to his leave of absence.

Target achievement in the 2020 financial year

Target achievement

Due to the Covid-19-related low level of Group target achievement for the reporting year 2020, target achievement for individual Management Board members was significantly reduced, to approximately 50 %. Given the three-year target measurement period, this will also have a negative impact upon variable remuneration for the two subsequent

%		Hermann J. Merkens	Marc Hess	Dagmar Knopek	Christiane Kunisch-Wolff	Thomas Ortmanns	Christof Winkelmann
2020	Group targets	20.0	20.0	20.0	20.0	20.0	20.0
	Sectional targets	110.0	110.0	110.0	110.0	110.0	110.0
	Individual targets	120.0	130.0	120.0	120.0	130.0	120.0
	Target achievement for 2020	**50.0**	**51.6**	**50.0**	**50.0**	**51.6**	**50.0**
Overall target achievement for 2020, based on a three-year observation period		**71.7**	**72.9**	**70.6**	**71.2**	**72.1**	**71.7**
Amount of variable remuneration (€)		**895,626**	**568,231**	**550,680**	**555,360**	**562,380**	**558,871**

years. Likewise, the overall target achievement level for 2020 – on a three-year basis – also comprises target achievement levels for the two previous years, leading to a level of approximately 70 % for each member of the Management Board.

Group performance targets 2020

Group performance is calculated by multiplying the target achievement level for an earnings target with a risk-adjusting indicator. At the beginning of the year, consolidated operating profit before taxes of € 215 million and a target RWA level of € 17.2 billion based on Basel IV (fully phased-in) – as a risk-adjusting indicator – were set as the earnings target for 100 % target achievement. The target RWA level was achieved. However, the Covid-19 pandemic – and the precautionary measures taken in response – resulted in the Group reporting negative consolidated operating profit. The Supervisory Board has made allowances for these extraordinary developments by applying the "modifier", using the maximum adjustment level of 20 percentage points to ensure appropriate recognition of the Management Board's actual performance despite the Covid-19 pandemic, which was outside of their control.

Sectional and individual targets 2020

Specific sectional and individual targets were defined for each Management Board member. Whilst the individual targets reflect the individual contributions of each Management Board member, the sectional targets are meant to reflect the target achievement of the respective Management Board member's overall area of responsibility. Thus, the strategic initiatives and measures defined and implemented in the respective area of responsibility are the main basis for determining sectional targets. Furthermore, various ESG targets (derived from the business strategy) have been agreed upon on both levels. The measurement of the individual contribution is based, among other things, on the "risk culture report", which assesses the supervisory authorities' expectations regarding managers as role models, the personal responsibility of employees, the benefits of open, critical and constructive communication spanning all hierarchical levels and divisions, and the appropriate incentive effect of monetary and non-monetary instruments.

The target achievement levels for the sectional and individual contributions made by the individual members of the Management Board resulted from the following main reasons:

Hermann-Josef Merkens

Aareal Bank's effectiveness was strengthened through the further process-oriented alignment of the Bank's organisational structure and processes, as well as measures to optimise the integrated Group management approach. The results of the employee survey conducted in 2019 were implemented systematically and, in particular, progress was made in rejuvenating Aareal Bank by recruiting more young professionals. Cross-sectional ESG opportunity and risk management was established, and Aareal Bank's ESG measures initiated were positioned in the capital markets, which was reflected in positive external ESG ratings.

With regard to Hermann J. Merkens's individual contribution, the Supervisory Board recognised the fact that the projects and tasks assigned to him as part of the Aareal Next Level strategic framework were implemented despite the Covid-19 pandemic, while at the same time, the culture of discussion was promoted as a key outcome of the employee survey, and the sale of a minority stake in Aareon was successfully executed with his intensive involvement.

Even though Mr Merkens was unable to contribute to achievement of his targets during his time of absence, given the temporary nature of his absence during 2020, this only had a minor impact on target measurement.

Marc Hess

Aareal Bank's funding structure was optimised, allowing the Bank to maintain sufficient liquidity and capital resources at all times, even in the face of increased lending and the Covid-19 pandemic. In addition, Aareal Bank shaped its ESG profile, allowing the Bank to exploit more favourable funding terms, and to achieve higher allocations for bond issues of public-sector entities in some cases. The organisation's cost control and effectiveness have also been strengthened.

The projects and tasks assigned to him as part of the Aareal Next Level strategic framework were implemented despite the Covid-19 pandemic and the culture of discussion was promoted at the same time as a key outcome of the employee survey. Hermann Merkens's responsibilities for Group Strategy, Group Communications and Governmental Affairs and Investor Relations/Sustainability were continued successfully by Marc Hess in Mr Merkens's absence – in particular, the review of the strategic programme (which had been commenced) against the backdrop of the Covid-19 pandemic (the so-called 360-degree review) was completed.

Dagmar Knopek
The reduction in the Bank's non-core assets exceeded the planned level. In order to make lending more effective, Dagmar Knopek ensured, in particular, that processes were digitalised further. Transparency was enhanced in the property portfolio with regard to various ESG criteria, and this was reflected in lending processes.

The credit portfolio and the NPL portfolio were managed appropriately in the context of the Covid-19 pandemic, in particular thanks to cooperation between different divisions as promoted by Dagmar Knopek.

Christiane Kunisch-Wolff
The frequent adoption of new regulatory requirements, which were introduced even more frequently due to the Covid-19 pandemic, was anticipated and implemented at an early stage. In particular, this strengthened the adequacy and effectiveness of the risk management and internal control systems with regard to information security risks, cyber resilience, ESG, IT stability, sanctions as well as money laundering within the limits of the cost budget earmarked for this purpose.

Christiane Kunisch-Wolff ensured that immediate changes were made to risk and monitoring systems to deal with the Covid-19 pandemic, while intensively promoting their ongoing digital development. Thanks to increased transparency, the management of the Bank by the Management Board was optimised. She served as a role model regarding the benefits of a positive and constructive discussion culture in her direct contact with managers and non-managers alike. Ms Kunisch-Wolff successfully assumed Mr Merkens's responsibility for Group Audit during his absence.

Thomas Ortmanns
When it comes to responsibility for business divisions, the sectional contribution is measured primarily based on key operating figures. Even though Aareon's planned adjusted EBITDA for 2020 was not fully achieved, due to Covid-19, significant strategic product enhancements (including Virtual Assistant, Predictive Maintenance, Smart Platform) were implemented whilst clearly remaining below the cost budget that had been set. This is reflected, among other things, in increased revenue generated with digital products, despite Covid-19.

The projects and tasks assigned to him as part of the Aareal Next Level strategic framework were implemented despite the Covid-19 pandemic and the culture of discussion was promoted at the same time as a key outcome of the employee survey. The partial sale of Aareon AG was successfully supported. Hermann Merkens's responsibilities for Group Human Resources & Infrastructure and Corporate Affairs, including the Legal department, were continued successfully during his absence. Mr Ortmanns ensured that sufficient IT stability was ascertained at all times, despite a large number of employees working from home, and the availability of IT capacities for the digital further development of Aareal Bank Group's products and processes thanks to his intensive personal commitment. In addition, Thomas Ortmanns very successfully chaired the Pandemic Committee, which managed the internal response to the Covid-19 pandemic efficiently and, in doing so, made a significant contribution to protecting the workforce.

Christof Winkelmann
The portfolio targets were all achieved or exceeded. In particular, growth in those property markets that are relevant to Aareal Bank was achieved in spite of the Covid-19 pandemic, while the syndication ratio was increased as planned and new products,

such as green lending products, were developed at the same time.

The increased flexibility in business activities already achieved in recent years allowed the portfolio to be readjusted during the year, in particular to increase the logistics property type. With his intensive involvement, contact with Aareal Bank's clients was intensified and they were supported in their response to the Covid-19 pandemic. Christof Winkelmann played a key role in promoting the close coordination between Aareal Bank Group employees that is necessary for management purposes. He assumed the function of membership on the Supervisory Board of Aareal Estate AG in Mr Merkens's absence, as well as various communications tasks.

No penalty-triggering events

In addition, compliance with governance provisions, i. e., with internal and external rules, as well as with the corporate values determined in Aareal Bank Group's Code of Conduct, is assessed within the scope of the annual penalty review. No penalty-triggering events were found.

Other information

No severance payments were agreed with Management Board members in the last financial year.

What is more, the annual backtesting of past target achievement did not rewveal any indications requiring a decision on a subsequent adjustment to the variable remuneration and a possible clawback via clawback provisions agreed in the service contract.

Total remuneration

In accordance with German commercial law in conjunction with GAS 17, the following table shows fixed and other remuneration for members of the Management Board, variable remuneration determined for the respective financial year (total amount, plus a breakdown into its components), as well as the total target achievement levels, as determined by the Supervisory Board.

€	Year	Fixed remuneration	Variable remuneration						Ancillary benefits	Total remuneration
			Cash component		Share-based component		Target achievement level	Total		
			Cash bonus	Cash deferral[1]	Share bonus	Share deferral[1]				
Hermann J. Merkens	2020	1,425,000	179,125	268,688	179,125	268,688	71.7 %	895,626	69,680	2,390,306
	2019	1,425,000	257,825	386,738	257,825	386,738	103.1 %	1,289,126	36,079	2,750,205
Marc Hess[2]	2020	900,000	113,646	142,058	113,646	198,881	72.9 %	568,231	100,791	1,569,022
	2019	900,000	157,638	236,457	157,638	236,457	101.1 %	788,190	39,855	1,728,045
Dagmar Knopek	2020	900,000	110,136	137,670	110,136	192,738	70.6 %	550,680	38,959	1,489,639
	2019	900,000	156,671	235,006	156,671	235,006	100.4 %	783,354	56,012	1,739,366
Christiane Kunisch-Wolff	2020	900,000	111,072	138,840	111,072	194,376	71.2 %	555,360	38,965	1,494,325
	2019	859,957	153,754	230,631	153,754	230,631	102.2 %	768,770	34,797	1,663,524
Thomas Ortmanns	2020	900,000	112,476	140,595	112,476	196,833	72.1 %	562,380	38,598	1,500,978
	2019	900,000	159,245	238,867	159,245	238,867	102.1 %	796,224	40,678	1,736,902
Christof Winkelmann	2020	900,000	111,774	139,718	111,774	195,605	71.7 %	558,871	34,886	1,493,757
	2019	802,000	146,776	220,165	146,776	220,165	103.3 %	733,882	38,245	1,574,127
Total	**2020**	**5,925,000**	**738,229**	**967,569**	**738,229**	**1,247,121**	**71.7 %**	**3,691,148**	**321,879**	**9,938,027**
	2019	**5,786,957**	**1,031,909**	**1,547,864**	**1,031,909**	**1,547,864**	**102.1 %**	**5,159,546**	**245,666**	**11,192,169**

[1] The deferrals shown are subject to the criteria on retention of variable remuneration components and penalty criteria, as set out above.
[2] The increase in ancillary benefits for Marc Hess in 2020 is mainly due to the one-off effect of security expenses incurred in the 2020 reporting year.

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. Payments to former Management Board members of Aareal Bank AG and their surviving dependants totalled € 1.7 million (2019: € 2.3 million).

(Virtual) shareholdings of Management Board members and share-based remuneration

Within Aareal Bank's remuneration system for Management Board members, the reference value for 100 % target achievement is slightly below the respective basic salary. Given that 50 % of variable remuneration is disbursed in the form of virtual shares, Management Board members typically earn virtual shares amounting to more than 100 % of their fixed annual salary at the latest after three years of service. Provided that they also earn variable remuneration in subsequent years, the equivalent value of the virtual shares will not fall below this 100% threshold until the end of their term on the Management Board.

The following table shows the portion of the variable component attributable to share-based remuneration arrangements as well as the corresponding number of virtual shares granted in 2020 and 2019, respectively – as well as the number of virtual shares already held as at the reporting date.

		Share-based remuneration		Total quantity of virtual shares held (31 Dec)
	Year	Value (€)	Quantity (number)[1]	Quantity (number)
Hermann J. Merkens	2020	447,813	22,906	47,218
	2019	644,563	25,357	58,753
Mark Hess	2020	312,527	15,986	6,502
	2019	394,095	15,503	1,405
Dagmar Knopek	2020	302,874	15,492	27,916
	2019	391,677	15,408	35,689
Christiane Kunisch-Wolff	2020	305,448	15,624	19,405
	2019	384,385	15,121	18,504
Thomas Ortmanns	2020	309,309	15,821	28,007
	2019	398,112	15,661	35,942
Christof Winkelmann	2020	307,379	15,723	17,805
	2019	366,941	14,435	15,751
Total	**2020**	**1,985,350**	**101,552**	**146,853**
	2019	**2,579,773**	**101,485**	**166,044**

[1] The stated number of virtual shares granted for 2020 is a preliminary figure, based on the price of Aareal Bank AG's share on 31 December 2020 (€ 19.55). The final conversion rate may only be determined after publication of preliminary results for 2020. The stated number of virtual shares granted for 2019 differs from the previous year's figure since the former was calculated using a final conversion rate of € 25.42.

Target remuneration granted

The following table shows the target remuneration (fixed annual salary and variable remuneration based on a 100 % target achievement) for the year under review, in accordance with sections 4.2.4 and 4.2.5 of the German Corporate Governance Code in the version dated 7 February 2017. In addition, the defined maximum remuneration is shown as an absolute upper limit pursuant to section 87a (1) 1 of the AktG.

Remuneration granted	Hermann J. Merkens – Chairman of the Management Board			
	2019	2020	2020 (min)[1]	2020 (max)[2]
€				
Fixed remuneration	1,425,000	1,425,000	1,425,000	1,425,000
Ancillary benefits	36,079	69,680	69,680	69,680
Total	**1,461,079**	**1,494,680**	**1,494,680**	**1,494,680**
One-year variable remuneration	250,000	179,125	–	375,000
Multi-year variable remuneration				
Cash deferral 2020 (March 2026)	–	268,688	–	562,500
Share bonus 2020 (March 2021)	–	179,125	–	375,000
Share deferral 2020 (March 2026)	–	268,688	–	562,500
Cash deferral 2019 (March 2025)	375,000	–	–	–
Share bonus 2019 (March 2020)	250,000	–	–	–
Share deferral 2019 (March 2025)	375,000	–	–	–
Total	**1,250,000**	**895,626**	**–**	**1,875,000**
Benefit expense[3]	788,303	864,322	864,322	864,322
Total remuneration	**3,499,382**	**3,254,628**	**2,359,002**	**4,234,002**

Remuneration granted	Mark Hess			
	2019	2020	2020 (min)[1]	2020 (max)[2]
€				
Fixed remuneration	900,000	900,000	900,000	900,000
Ancillary benefits	39,855	100,791	100,791	100,791
Total	**939,855**	**1,000,791**	**1,000,791**	**1,000,791**
One-year variable remuneration	156,000	113,646	–	234,000
Multi-year variable remuneration				
Cash deferral 2020 (March 2026)	–	142,058	–	292,500
Share bonus 2020 (March 2021)	–	113,646	–	234,000
Share deferral 2020 (March 2026)	–	198,881	–	409,500
Cash deferral 2019 (March 2026)	234,000	–	–	–
Share bonus 2019 (March 2020)	156,000	–	–	–
Share deferral 2019 (March 2026)	234,000	–	–	–
Total	**780,000**	**568,231**	**–**	**1,170,000**
Benefit expense[3]	519,026	637,516	637,516	637,516
Total remuneration	**2,238,881**	**2,206,538**	**1,638,307**	**2,808,307**

[1] Minimum amount of the remuneration component granted in the year under review
[2] Maximum amount of the remuneration component granted in the year under review
[3] Benefit expense refers to the service cost pursuant to IAS 19. The figures for 2019 were adjusted accordingly to reflect the service cost pursuant to IAS 19 for 2019.

Remuneration granted	Dagmar Knopek			
€	2019	2020	2020 (min)[1]	2020 (max)[2]
Fixed remuneration	900,000	900,000	900,000	900,000
Ancillary benefits	56,012	38,959	38,959	38,959
Total	**956,012**	**938,959**	**938,959**	**938,959**
One-year variable remuneration	156,000	110,136	–	234,000
Multi-year variable remuneration				
Cash deferral 2020 (March 2026)	–	137,670	–	292,500
Share bonus 2020 (March 2021)	–	110,136	–	234,000
Share deferral 2020 (March 2026)	–	192,738	–	409,500
Cash deferral 2019 (March 2025)	234,000	–	–	–
Share bonus 2019 (March 2020)	156,000	–	–	–
Share deferral 2019 (March 2025)	234,000	–	–	–
Total	**780,000**	**550,680**	**–**	**1,170,000**
Benefit expense3)	395,582	429,474	429,474	429,474
Total remuneration	**2,131,594**	**1,919,113**	**1,368,433**	**2,538,433**

Remuneration granted	Christiane Kunisch-Wolff			
€	2019	2020	2020 (min)[1]	2020 (max)[2]
Fixed remuneration	859,957	900,000	900,000	900,000
Ancillary benefits	34,797	38,965	38,965	38,965
Total	**894,754**	**938,965**	**938,965**	**938,965**
One-year variable remuneration	150,400	111,072	–	234,000
Multi-year variable remuneration				
Cash deferral 2020 (March 2026)	–	138,840	–	292,500
Share bonus 2020 (March 2021)	–	111,072	–	234,000
Share deferral 2020 (March 2026)	–	194,376	–	409,500
Cash deferral 2019 (March 2025)	225,600	–	–	–
Share bonus 2019 (March 2020)	150,400	–	–	–
Share deferral 2019 (March 2025)	225,600	–	–	–
Total	**752,000**	**555,360**	**–**	**1,170,000**
Benefit expense3)	460,018	557,884	557,884	557,884
Total remuneration	**2,106,772**	**2,052,209**	**1,496,849**	**2,666,849**

[1] Minimum amount of the remuneration component granted in the year under review
[2] Maximum amount of the remuneration component granted in the year under review
[3] Benefit expense refers to the service cost pursuant to IAS 19. The figures for 2019 were adjusted accordingly to reflect the service cost pursuant to IAS 19 for 2019.

Remuneration granted	Thomas Ortmanns			
	2019	**2020**	**2020 (Min)[1]**	**2020 (Max)[2]**
€				
Fixed remuneration	900,000	900,000	900,000	900,000
Ancillary benefits	40,678	38,598	38,598	38,598
Total	**940,678**	**938,598**	**938,598**	**938,598**
One-year variable remuneration	156,000	112,476	–	234,000
Multi-year variable remuneration				
Cash deferral 2020 (March 2026)	–	140,595	–	292,500
Share bonus 2020 (March 2021)	–	112,476	–	234,000
Share deferral 2020 (March 2026)	–	196,833	–	409,500
Cash deferral 2019 (March 2025)	234,000	–	–	–
Share bonus 2019 (March 2020)	156,000	–	–	–
Share deferral 2019 (March 2025)	234,000	–	–	–
Total	**780,000**	**562,380**	**–**	**1,170,000**
Benefit expense[3]	574,053	431,854	431,854	431,854
Total remuneration	**2,294,731**	**1,932,832**	**1,370,452**	**2,540,452**

Remuneration granted	Christof Winkelmann			
	2019	**2020**	**2020 (Min)[1]**	**2020 (Max)[2]**
€				
Fixed remuneration	802,000	900,000	900,000	900,000
Ancillary benefits	38,245	34,886	34,886	34,886
Total	**840,245**	**934,886**	**934,886**	**934,886**
One-year variable remuneration	142,115	111,774	–	234,000
Multi-year variable remuneration				
Cash deferral 2020 (March 2026)	–	139,718	–	292,500
Share bonus 2020 (March 2021)	–	111,774	–	234,000
Share deferral 2020 (March 2026)	–	195,605	–	409,500
Cash deferral 2019 (March 2025)	213,173	–	–	–
Share bonus 2019 (March 2020)	142,115	–	–	–
Share deferral 2019 (March 2025)	213,173	–	–	–
Total	**710,576**	**558,871**	**–**	**1,170,000**
Benefit expense[3]	509,514	720,696	720,696	720,696
Total remuneration	**2,060,335**	**2,214,453**	**1,655,582**	**2,825,582**

[1] Minimum amount of the remuneration component granted in the year under review
[2] Maximum amount of the remuneration component granted in the year under review
[3] Benefit expense refers to the service cost pursuant to IAS 19. The figures for 2019 were adjusted accordingly to reflect the service cost pursuant to IAS 19 for 2019.

Remuneration paid

The following table shows the remuneration disbursed in the year under review, as defined in sections 4.2.4 and 4.2.5 of the German Corporate Governance Code in the version dated 7 February 2017. It also outlines disbursements under variable remuneration components related to multiple years which expired during the year under review:

Remuneration paid	Hermann J. Merkens Chairman of the Management Board		Marc Hess		Dagmar Knopek		Christiane Kunisch-Wolff	
	2020	2019	2020	2019	2020	2019	2020	2019
€								
Fixed remuneration	1,425,000	1,425,000	900,000	900,000	900,000	900,000	900,000	859,957
Ancillary benefits	69,680	36,079	100,791	39,855	38,959	56,012	38,965	34,797
Total	**1,494,680**	**1,461,079**	**1,000,791**	**939,855**	**938,959**	**956,012**	**938,965**	**894,754**
One-year variable remuneration	257,825	304,248	157,638	40,329	156,671	164,256	153,754	139,085
Multi-year variable remuneration	–	–	–	–	–	–	–	–
Cash deferral 2016 (April 2020)	191,250	–	–	–	107,503	–	68,511	–
Cash deferral 2017 (April 2020)	173,238	–	–	–	98,993	–	79,194	–
Cash deferral 2018 (April 2020)	91,274	–	8,642	–	49,277	–	41,725	–
Share bonus 2016 (April 2020)	269,482	–	–	–	151,478	–	96,536	–
Share bonus 2018 (April 2020)	269,383	–	35,707	–	145,433	–	123,146	–
Share deferral 2014 (April 2020)	66,766	–	–	–	66,607	–	–	–
Share deferral 2015 (April 2020)	139,985	–	–	–	99,373	–	–	–
Share deferral 2016 (April 2020)	135,307	–	–	–	76,057	–	48,470	–
Cash deferral 2015 (April 2019)	–	152,530	–	–	–	108,278	–	–
Cash deferral 2016 (April 2019)	–	190,450	–	–	–	107,054	–	68,224
Cash deferral 2017 (April 2019)	–	172,613	–	–	–	98,638	–	78,910
Share bonus 2015 (April 2019)	–	312,384	–	–	–	221,754	–	–
Share deferral 2013 (April 2019)	–	101,264	–	–	–	59,071	–	–
Share deferral 2014 (April 2019)	–	74,734	–	–	–	74,557	–	–
Share deferral 2015 (April 2019)	–	157,145	–	–	–	111,553	–	–
Dividends	–	128,964	–	2,950	–	78,046	–	41,361
Total	**1,594,510**	**1,594,332**	**201,987**	**43,279**	**951,392**	**1,023,207**	**611,336**	**327,580**
Benefit expense[1)]	864,322	788,303	637,516	519,026	429,474	395,582	557,884	460,018
Total remuneration	**3,953,512**	**3,843,714**	**1,840,294**	**1,502,160**	**2,319,825**	**2,374,801**	**2,108,185**	**1,682,352**

[1)] Benefit expense refers to the service cost pursuant to IAS 19. The figures for 2019 were adjusted accordingly to reflect the service cost pursuant to IAS 19 for 2019.

Remuneration paid	Thomas Ortmanns		Christof Winkelmann		Dr Wolf Schumacher[2]	
	2020	2019	2020	2019	2020	2019
€						
Fixed remuneration	900,000	900,000	900,000	802,000	–	–
Ancillary benefits	38,598	40,678	34,886	38,245	–	–
Total	**938,598**	**940,678**	**934,886**	**840,245**	**–**	**–**
One-year variable remuneration	159,245	173,856	146,776	139,085	–	–
Multi-year variable remuneration	–	–	–	–	–	–
Cash deferral 2016 (April 2020)	108,151	–	43,099	–	–	–
Cash deferral 2017 (April 2020)	97,784	–	80,161	–	–	–
Cash deferral 2018 (April 2020)	52,157	–	41,725	–	–	–
Share bonus 2016 (April 2020)	152,392	–	60,728	–	–	–
Share bonus 2018 (April 2020)	153,933	–	123,146	–	–	–
Share deferral 2014 (April 2020)	66,238	–	–	–	116,563	–
Share deferral 2015 (April 2020)	98,774	–	–	–	128,954	–
Share deferral 2016 (April 2020)	76,516	–	30,492	–	–	–
Cash deferral 2015 (April 2019)	–	107,626	–	–	–	140,510
Cash deferral 2016 (April 2019)	–	107,669	–	42,918	–	–
Cash deferral 2017 (April 2019)	–	97,434	–	79,874	–	–
Share bonus 2015 (April 2019)	–	220,419	–	–	–	287,767
Share deferral 2013 (April 2019)	–	101,264	–	–	–	170,844
Share deferral 2014 (April 2019)	–	74,144	–	–	–	130,475
Share deferral 2015 (April 2019)	–	110,882	–	–	–	144,761
Dividends	–	78,565	–	35,240	–	31,001
Total	**965,190**	**1,071,859**	**526,127**	**297,117**	**245,517**	**905,358**
Benefit expense[1]	431,854	574,053	720,696	509,514	–	–
Total remuneration	**2,335,642**	**2,586,590**	**2,181,709**	**1,646,876**	**245,517**	**905,358**

[1] Benefit expense refers to the service cost pursuant to IAS 19. The figures for 2019 were adjusted accordingly to reflect the service cost pursuant to IAS 19 for 2019.
[2] Dr Wolf Schumacher resigned with effect from 30 September 2015.

Pensions

	2020			2019		
	Pension claims p.a.[1]	Balance of pension obligations (IFRS) as at 31 Dec 2020	Increase of pension obligations (IFRS) in 2020	Pension claims p.a.[1]	Balance of pension obligations (IFRS) as at 31 Dec 2019	Increase of pension obligations (IFRS) in 2019
000's €						
Hermann J. Merkens	396	11,426	1,859	371	9,567	2,297
Marc Hess	62	1,776	873	35	902	754
Dagmar Knopek	145	3,992	702	127	3,290	780
Christiane Kunisch-Wolff	97	2,769	771	75	1,998	826
Thomas Ortmanns	308	9,237	1,270	294	7,967	1,610
Christof Winkelmann	121	4,314	1,649	92	2,664	1,436
Total	**1,129**	**33,514**	**7,124**	**994**	**26,388**	**7,703**

[1] The pension claims mentioned refer to old-age pension earned as at 31 December of the year under review, based on the grants made by the Bank, at the applicable retirement age.

Service cost (in accordance with IFRSs) incurred in the 2020 financial year in connection with the pension claims of members of the Management Board totalled € 4.0 million (2019: € 3.6 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 € 8.4 million in the year under review (2019: € 10.3 million). The total amount of pension obligations is € 70.1 million (2019: € 61.8 million). Of that amount, € 36.6 million relates to former members of the Management Board and their surviving dependants (2019: € 35.4 million).

Remuneration system for members 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. Remuneration for the services of the Supervisory Board members comprises exclusively fixed remuneration, plus an attendance fee. Where membership in the Supervisory Board falls short of an entire financial year, said remuneration shall be paid on a pro rata temporis basis. Furthermore, the Supervisory Board members will be reimbursed for their expenses. Any value-added tax invoiced will also be deemed to be a refundable expense.

Remuneration of the Supervisory Board comprises the following.

The remuneration for any financial year shall be due and payable one month after the end of the respective financial year. The members of the Supervisory Board are also included in a D&O (directors' and officers') liability insurance policy maintained by the Bank in an appropriate amount with a deductible of 10 %.

Remuneration element	Description	Structure
Fixed remuneration	Remuneration for activities on the Supervisory Board; Depending on the role of the respective Supervisory Board member (e.g. Chairman)	– € 50,000 p.a. per Supervisory Board member – € 150,000 p.a. for the Chairman – € 75,000 p.a. for the Deputy Chairman
Committee remuneration	Remuneration for activities and duties on the Supervisory Board committees also depends on the role of the respective Supervisory Board member in the respective committee (e.g. a committee chairman)	– € 20,000 p.a. each for membership in the Risk Committee and/or the Audit Committee – € 40,000 p.a. each for the chairmanship in the two committees – € 15,000 p.a. each for membership in other committees – € 30,000 p.a. each for the chairmanship in other committees
Attendance fees	Remuneration for participation in Supervisory Board meetings and on the committees of the Supervisory Board	– € 1,000 per meeting

Supervisory Board remuneration

€	Year	Fixed remuneration	Attendance fees	Total remuneration
Marija Korsch Chairman	2020	265,000	55,000	320,000
	2019	265,000	37,000	302,000
Richard Peters Deputy Chairman (since 27 May 2020)	2020	114,903	44,000	158,903
	2019	100,000	25,000	125,000
Prof. Dr Stephan Schüller Deputy Chairman (until 27 May 2020)	2020	51,042	19,000	70,042
	2019	125,000	23,000	148,000
Klaus Novatius Deputy Chairman	2020	105,000	37,000	142,000
	2019	105,000	21,000	126,000
Jana Brendel (since 27 May 2020)	2020	50,528	14,000	64,528
	2019	–	–	–
Christof von Dryander (since 27 May 2020)	2020	59,444	25,000	84,444
	2019	–	–	–
Thomas Hawel	2020	65,000	22,000	87,000
	2019	65,000	13,000	78,000
Petra Heinemann-Specht	2020	81,889	29,000	110,889
	2019	70,000	15,000	85,000
Jan Lehmann (since 27 May 2020)	2020	38,639	12,000	50,639
	2019	–	–	–
Dr Hans-Werner Rhein (until 27 May 2020)	2020	34,708	17,000	51,708
	2019	85,000	21,000	106,000
Sylvia Seignette	2020	90,000	24,000	114,000
	2019	90,000	15,000	105,000
Elisabeth Stheeman [1]	2020	85,000	28,000	113,000
	2019	85,000	19,000	104,000
Hans-Dietrich Voigtländer	2020	115,000	38,000	153,000
	2019	115,000	25,000	140,000
Prof. Dr Hermann Wagner	2020	118,917	37,000	155,917
	2019	110,000	21,000	131,000
Beate Wollmann (until 27 May 2020)	2020	28,583	12,000	40,583
	2019	70,000	15,000	85,000
Total	**2020**	**1,303,653**	**413,000**	**1,716,653**
	2019	**1,285,000**	**250,000**	**1,535,000**

[1] Income tax plus solidarity surcharge for the Supervisory Board member subject to limited tax liability was declared pursuant to section 50a (1) no. 4 of the German Income Tax Act (Einkommensteuergesetz – "EStG"), and paid to the German Central Tax Office (Bundeszentralamt für Steuern, BZSt).

Remuneration system for employees

When it comes to the structure of the remuneration system for employees, a general distinction is made between three groups of employees. First of all, Aareal Bank has employees whose remuneration is governed by collective agreements. Then, there are employees whose remuneration is not governed by collective agreements. These employees who are not covered by collective agreements are then split into two further groups. First, there are those employees whose duties have a material impact on the overall risk profile of Aareal Bank (risk takers) or of Aareal Bank Group (Group risk takers). The variable remuneration paid to these "risk takers" is subject to very stringent regulatory requirements. The other employees who are not covered by collective agreements and are not risk takers either are not subject to these provisions and make up the third group.

The remuneration system for the Management Board and the remuneration system for employees are closely aligned, aside from regulatory requirements. Consistency between the systems is achieved, in particular, by using the Group component in the structure of the variable remuneration system, such that both the Management Board and employees (not covered by collective agreements) are set targets based on the Group performance criteria. In general, the targets set for the employees are derived from those set for the members of the Management Board, meaning that, as well as the structure of the two systems being consistent, the actual content of the targets set is also cascaded throughout the entire workforce from the strategic Group targets.

The report below starts by explaining the remuneration system for risk takers and then addresses the differences compared with the other groups.

Remuneration system for risk takers

In order to identify those employees who are classed as "risk takers", Aareal Bank carries out an annual independent risk analysis, identifying the employees in question based on a uniform set of criteria whilst taking regulatory requirements into account.

The remuneration system for risk takers is subject to the same basic conditions as the remuneration system for Management Board members, and is also aligned with the business and risk strategy of Aareal Bank AG and Aareal Bank Group respectively. As is the case with the Management Board remuneration, risk takers receive both fixed and variable remuneration. The fixed component comprises a fixed annual salary and ancillary benefits.

Performance-related variable remuneration

Remuneration parameters and target level weighting

As with the Management Board members, the variable remuneration is measured based on targets derived from the corporate strategy. One difference compared with the Management Board system is that the assessment period for the target achievement is one year. The targets set for risk takers are split into three components that are added together, as is the case for the remuneration paid to the Management Board: a Group component, an organisational unit component (referring to the organisational unit that the risk taker works for) and an individual component (individual target achievement). The performance of the organisational unit for divisions allocated to Sales is measured using the Structured Property Financing segment operating result, as well as in terms of risk weighted assets. The performance of the Housing Industry division is measured by reference to the segment operating result of the Consulting/Services Bank (as of 1 January 2021: Banking & Digital Solutions) segment. The central staff functions and control units, as well as the Treasury division, are measured based on their respective cost target. The remuneration system also takes account of the risk taker's position in the organisation's hierarchy, reflecting the influence that he/she can exert over the Group's/Bank's success. This results in differences in the weighting attached to the three additive components depending on an individual's responsibility within the Company: The Group component payable to risk takers assigned to the management level below the Management Board (Managing Directors) is 35 %. By contrast, it is 25 % for the other risk takers. For further information on the individual targets and possible resulting KPIs, we refer to the information on Management Board remuneration.

Deferred disbursement, through retention of variable remuneration components and virtual shares

To ensure that the remuneration system provides long-term incentives, the initial value for variable remuneration – as determined according to the principles set out above – is mostly paid out on a deferred basis after the end of the financial year. The payout terms are based on those that apply to the Management Board remuneration system but once again vary depending on the risk taker's position within the organisational structure.

60 % of the variable remuneration paid to risk takers on the Managing Director level is subject to a five-year deferral period. 50 % each of deferred and non-deferred components are converted into virtual shares that are held for a minimum period of one year. Unlike with the Management Board remuneration system, risk takers can, however, opt to select when they want their virtual shares to be converted into cash after the end of the one-year holding period, selecting a conversion date that falls within a period of up to three years.

By contrast, 40 % of the variable remuneration paid to the other risk takers is subject to deferral over a period of three years.

All other aspects relating to the calculation of virtual shares are explained in the section on the Management Board remuneration system.

Ex-post review of target achievement and behaviour of the risk takers

As in the Management Board remuneration system, the original target achievement level is back-tested and, where appropriate, reduced before virtual shares are paid out/granted. Penalty-triggering events can also result in reductions or in the forfeiture of the variable remuneration entitlement in full and, as a result, also in variable remuneration that has already been paid out being clawed back. Details can be found in the information on the Management Board remuneration system.

Remuneration system for employees who are not classed as risk takers

Aareal Bank AG is a member in Germany of the Arbeitgeberverband des privaten Bankgewerbes e.V. (association of employers in private banking) and bound by the collective agreements for private banks. Variable remuneration for employees not classified as risk takers is split into two components, too: the Group component (25 % of target variable remuneration) and the individual component (75 % of target variable remuneration). This means that the variable remuneration of all employees is directly linked to Aareal Bank Group's performance, and the employees are directly involved in reaching the communicated targets. The individual component paid to those employees whose remuneration is governed by a collective agreement is based on an annual appraisal. The initial value for measuring the variable remuneration corresponds to 0.75 gross monthly salaries for employees covered by a collective agreement. The individual component paid to those employees who are not covered by a collective agreement is based on contractually agreed target-variable remuneration and is measured based on an annual overall appraisal that also takes the target achievement level for the individual targets that have been set for the employee in question into account.

Restrictions and link to risk-bearing capacity for all employee remuneration systems

All employee remuneration systems feature provisions corresponding to those found in the Management Board remuneration system regarding the impact of special external conditions (modifiers). In cases involving risk takers, the ban on hedging also applies. There are, however, differences with regard to the caps and the safeguarding of the risk-bearing capacity. The contracts of employment with those employees below Management Board level do not include contractual provisions on severance pay.

Caps and proportion of variable remuneration

The Group component and – for risk takers – the organisational component are capped at 150 % in the target achievement level. The individual targets are capped at a target achievement level of 200 %. If the individual target achievement level is 0 %, no variable remuneration is paid at all. Performance of virtual shares is capped at 300 %.

In order to comply with the requirements set out in section 25a (5) of the KWG, the reference value for the variable remuneration in cases involving a target achievement level of 100 % generally corresponds to a maximum of 50 % of the fixed remuneration. This means that, even if an employee achieves the maximum target achievement level, the variable remuneration does not exceed the fixed remuneration. Consequently, if an employee receives fixed annual remuneration of € 80,000, for example, the reference value for the variable remuneration paid out if that employee achieves 100 % target achievement is limited to a maximum of € 40,000. It is very common, however, for variable remuneration to account for a smaller proportion of an employee's total remuneration. Furthermore, it has been ensured in line with regulatory requirements that the variable remuneration for control unit employees amounts to no more than one-third of total remuneration.

In 2014, the Annual General Meeting of Aareal Bank AG approved exemptions from this 1:1 rule for certain groups of employees. In order to ensure that the remuneration paid by Aareal Bank AG and its international subsidiaries is competitive in an international comparison, employees working in international sales at Aareal Bank AG, as well as executives and employees working for the subsidiaries Aareal Capital Corporation, New York, and Aareal Bank Asia Ltd., Singapore, have to be paid remuneration in line with local market standards. This applies to fewer than 25 positions.

Reporting on quantitative disclosure requirements

This report only covers the qualitative disclosure requirements regarding employee remuneration set out in Article 450 of the EU's Capital Requirements Regulation 2013/575 (CRR) and section 16 InstVergV. The quantitative disclosure requirements relating to the provisions set out above are published in a separate report entitled "Disclosure of Remuneration Indicators", which can be found on the website of Aareal Bank AG. This report is made available within six months of the end of the financial year: www.aareal-bank.com/en/investors-portal/finance-information/regulatory-disclosures/archive/2020/.

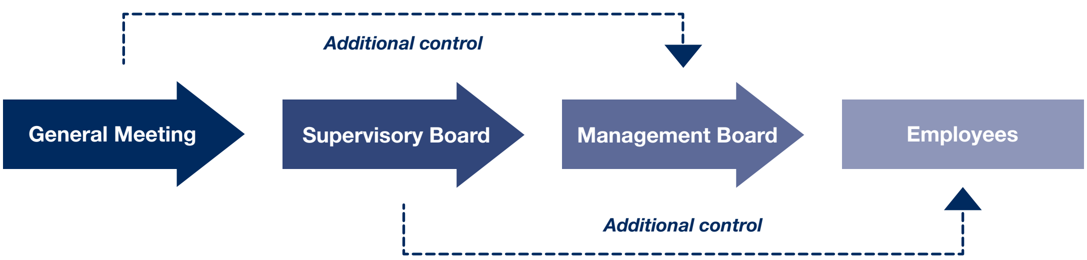
Remuneration governance

Governance of Supervisory Board remuneration

The role of the Annual General Meeting

Given the Supervisory Board's role as a supervisory body, remuneration for its members must not provide any incentives which would counter this surveillance function. The Annual General Meeting

Determination and control of remuneration systems



(AGM) determines the remuneration of the Supervisory Board, in Aareal Bank AG's Memorandum and Articles of Association; the AGM therefore also resolves on any adjustments to Supervisory Board remuneration (cf. Article 9 (4) and (5) of the Memorandum and Articles of Association).

In the implementation of the Second Shareholder Rights Directive in the German Public Limited Companies Act (AktG), as of the first ordinary Annual General Meeting following the 2020 financial year, the AGM will need to discuss Supervisory Board remuneration at least every four years, even without any concrete proposals for amendments, and will need to resolve whether it still approves it.

The role of the Supervisory Board

The Supervisory Board shall review the appropriateness of remuneration for its members at least once a year. Every four years, it shall retain an external remuneration advisor to obtain an opinion as to the appropriateness of its remuneration – and especially, on whether remuneration is in line with common practice and comparable. The Supervisory Board shall present the results of this review as part of its report to the AGM. Where appropriate, the Supervisory Board will prepare recommendations for adjustments to its remuneration, and will submit them to shareholders at the next AGM.

Governance of Management Board remuneration

The role of the Supervisory Board

The Supervisory Board shall act in the Company's interests; accordingly, it shall ensure that Management Board remuneration is geared towards the Company's sustainable development (cf. section 87 of the AktG). The Supervisory Board decides on Management Board remuneration, monitors appropriateness, defines targets for determining variable remuneration, and decides on target achievement. During the following years, the Supervisory Board reviews, within the framework of backtesting/ penalty reviews, whether variable remuneration determined originally must be adjusted or reclaimed (clawback).

As part of examining appropriateness of Management Board remuneration, the Supervisory Board shall review whether the remuneration system for the Management Board (as well as the corresponding targets for Management Board members derived therefrom) is consistent with the Company's business and risk strategies, the objectives derived from these strategies, the corresponding risk management, as well as with the defined risk appetite and the corporate values. As further elements of this examination of appropriateness, a vertical comparison with the average remuneration of relevant employees and the top management level below the Management Board is to be carried out, as well as a horizontal comparison with the remuneration of management board members of comparable enterprises. These components reflect the orientation of Management Board remuneration towards sustainable Company development, meaning that remuneration is aligned with the long-term interests of Aareal Bank's stakeholders.

When taking decisions concerning the structure of the remuneration system for the Management Board, the Supervisory Board shall take the views of Aareal Bank AG's relevant shareholders and of proxy advisors into account.

The role of the Remuneration Control Committee

The Remuneration Control Committee supports the Supervisory Board in its monitoring duties and prepares the plenary meeting's resolutions concerning remuneration. The Committee monitors the appropriateness of the structure of Management Board remuneration, proposes targets for variable remuneration and for target achievement at the end of the year, and also monitors the levels of target achievement during the course of each year. Moreover, the Committee assesses the effects of the remuneration systems on the Group's risk, capital and liquidity management. In the run-up to determining remuneration, in cooperation with the Audit Committee, it reviews whether there are any backtesting or penalty-triggering events which may result in a reduction of variable remuneration.

The role of the Risk Committee

The duties of the Risk Committee with regard to remuneration are unaffected by the assessment by the Remuneration Control Committee, as set out above. The Risk Committee verifies whether the incentives created by the remuneration system take the Company's risk, capital and liquidity structure into account, as well as the probability and timing of income.

The role of the Audit Committee

Circumstances where variable remuneration may be reduced may occur where Management Board members fail to fulfil any of their duties, or where they breach external or internal requirements. To the extent that any such events have occurred, these are identified in the reports prepared by Compliance, addressed to the Audit Committee as well as to the plenary meeting of the Supervisory Board. Internal conduct rules are also defined in a Code of Conduct which must be presented to the Audit Committee at least once a year.

The role of the Annual General Meeting

In accordance with the German Act Implementing the Second Shareholder Rights Directive (ARUG II), the remuneration system for Management Board members is submitted to the Annual General Meeting for approval at least every four years and in the event of significant changes (Say-on-Pay). The remuneration system will be presented to the 2021 Annual General Meeting for the first time in line with these provisions.

Governance of staff remuneration

The role of the Management Board

The Management Board is responsible for structuring the remuneration system for employees. As an element of appropriate and effective risk management, staff remuneration is monitored as to whether it is consistent with the corporate and risk culture, and with Aareal Bank's risk appetite. Especially with respect to the remuneration of material risk takers, the Management Board will take care to adjust remuneration parameters to such employees' influence on the Bank's risk exposure.

The role of the Supervisory Board/ the Remuneration Control Committee/ the Risk Committee

The Supervisory Board and its Remuneration Control Committee monitor the structure of staff remuneration. In this context, the Remuneration Control Committee also assesses the criteria for, and the actual selection of, Aareal Bank Group's material risk takers. Together with the Risk Committee, and in line with the rules for Management Board remuneration, the Remuneration Control Committee monitors whether the remuneration system for employees is consistent with the Company's business and risk strategies, the objectives derived from these strategies, its risk appetite and the risk management.

Further information on the Supervisory Board and its committees

The composition and responsibilities of the Supervisory Board committees, and of the plenary meeting, are described in the Corporate Governance Statement/the Corporate Governance Report and in the Notes to the consolidated financial statements.

The Supervisory Board presents the remuneration-related activities of its plenary meetings and of its committees as part of its report to the AGM. This report also provides details regarding the number of meetings, and on the participation of the members of the committees and the Supervisory Board.

The role of the Remuneration Officer

Following consultation of the Supervisory Board, the Management Board of Aareal Bank AG shall appoint a Remuneration Officer in order to ensure appropriate, sustained and effective monitoring of staff remuneration. Aareal Bank has appointed a Remuneration Officer, to carry out duties in accordance with section 24 of the InstVergV. These duties include supporting the Supervisory Board and the Remuneration Control Committee in structuring and monitoring the remuneration system. The Remuneration Officer is obliged to respond to queries of the Remuneration Control Committee's Chairman.

The Remuneration Officer reports on the appropriate structure of the remuneration systems for employees in the form of a Remuneration Report at least once a year. Due to the responsibility of monitoring the appropriateness of the remuneration systems on a continuing basis, the Remuneration Officer is being included in the conceptional new drafting (and future development), as well as in the application of the remuneration systems. In particular, the Remuneration Officer plays an active part in the process for the determination of the total amount available for variable remuneration, the annual review of penalty rules, the regular (at least spot checks) review of appropriate compliance structures, the monitoring of the hedging ban (and potential violations), the drafting of the annual remuneration report (pursuant to section 16 of the InstVergV in connection with Article 450 of the CRR) as well as the review of the risk taker analysis.

Involvement of external advisors

In order to review the appropriateness of the Supervisory Board remuneration, an external remuneration advisor is engaged at least every four years to prepare an opinion as to the appropriateness of this remuneration – and especially, on whether this remuneration is in line with common practice and is comparable.

In addition, a horizontal comparison of the remuneration paid to Aareal Bank's Management Board members with suitable peer companies is carried out by an external remuneration advisor to review the appropriateness of the Management Board emuneration. The composition of the peer groups is reviewed on a regular basis by the remuneration advisor as part of the appropriateness review process.

The Remuneration Control Committee and the Supervisory Board are advised by hkp/// within this context. The Bank also seeks advice from the law firm Freshfields Bruckhaus Deringer on matters relating to remuneration law.

Takeover Disclosures in Accordance with Section 315a (1) of the German Commercial Code (HGB)

Composition of subscribed capital, and rights and obligations attached to shares

The composition of Aareal Bank AG's subscribed capital is shown in the Note "Equity" to the consolidated 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 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 German Public Limited Companies Act (Aktiengesetz – "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 Note "Disclosures pursuant to section 160 (1) no. 8 of the AktG".

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 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 31 May 2017 resolved to authorise the Management Board to increase, on one or more occasions, the Company's share capital, subject to the approval of the Supervisory Board, by up to a maximum total amount of € 89,785,830 by issuance of new shares for contribution in cash or in kind; the Management Board is also authorised, within defined limits, to disapply pre-emptive rights, given the fulfilment of certain conditions. This authorisation will expire on 30 May 2022. 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 share capital – including treasury shares and any shares issued during the term of this authorisation, under the authorisation under agenda item no. 6 of the Annual General Meeting held on 21 May 2014. The authorised capital has not been utilised to date.

Conditional capital

Based on a resolution passed by the General Meeting on 22 May 2019, the Management Board was authorised to issue, on one or more occasions until 21 May 2024, profit-participation certificates with a limited or unlimited term for contribution in cash or in kind of up to € 900,000,000. The profit-participation certificates must be structured in such a way that the funds paid upon issuance are eligible as regulatory capital pursuant to the legal regulations applicable as at the time of issuance. Profit-articipation certificates and other hybrid promissory note loans to be issued according to this authorisation shall be connected with conversion rights, entitling or compelling, in accordance with their respective conditions, the holder to purchase Company shares. Conversion rights or obligations may be attached exclusively to bearer no-par value shares and are limited to a maximum amount of € 71,828,664.00 of the Company's share capital. The sum of shares to be issued so as to service conversion or option rights or conversion obligations from profit-participation certificates or hybrid promissory note loans issued pursuant to this authorisation, including shares issued during validity of this authorisation as a result of another authorisation (especially from the Authorised Capital 2017), may not exceed an amount of € 71,828,664.00 (which equals approx. 40 % of the current share capital). Subject to the approval of the Supervisory Board, the Management Board may exclude shareholders' pre-emptive rights in relation to the profit-participation rights in certain cases.

Accordingly, the Company's share capital is subject to a conditional capital increase not exceeding € 71,828,664.00 by issuance of up to 23,942,888 new no-par value bearer shares ("Conditional Capital 2019"). The purpose of the conditional capital increase is to grant shares to holders or creditors of convertible bonds issued in accordance with the aforementioned authorisation. The new no-par value bearer shares may only be issued at a conversion price in line with the resolution passed by the Gen-eral Meeting on 22 May 2019. The conditional capital increase shall only be carried out insofar as conversion rights are exercised or as conversion obligations from such convertible bonds are fulfilled or as the Company makes use of alternative performance and insofar as no cash compensation is granted or treasury shares are used to service the rights. The new shares shall 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 rights or the fulfilment of conversion obligations. The Management Board is authorised to determine the details of the conditional capital increase. The Management Board is also authorised to determine the further contents of share rights and the terms governing the issuance of shares, subject to the approval of the Supervisory Board.

Authorisation to purchase treasury shares

The General Meeting authorised the Management Board by way of a resolution dated 27 May 2020, 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 purchase or prior to assuming a purchase obligation by more than 10%. This authorisation expires on 26 May 2025. 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.

Furthermore, the Management Board was authorised by means of a resolution of the General Meeting held on 27 May 2020, pursuant to section 71 (1) no. 8 of the AktG, to purchase treasury shares in a volume of up to 10 % of the share capital for any permitted purposes. This authorisation expires on 26 May 2025. Such purchases may be effected via stock exchanges or public purchase offers made to all shareholders, taking into account the prices as specified in the respective Annual General Meeting's resolution, which are in turn based on the Company's stock exchange share price. This authorisation may be exercised – also by direct or indirect subsidiaries of Aareal Bank AG – in full or in part, on one or more occasions.

Subject to the approval of the Supervisory Board, the shares acquired under this or an earlier authorisation may be sold outside stock exchanges and without an offer to all shareholders, thereby excluding shareholders' pre-emptive rights, provided that the shares sold do not exceed the threshold value of 10% of the Company's share capital and that the issue price is not significantly lower than the stock exchange price, or if the sale of such shares is made against contribution in kind, or if the shares are given to the holders of conversion or option rights, even if they had been issued by subsidiaries. The treasury shares may also be given to the holders of conversion or option rights in lieu of new shares from a contingent capital increase. The shares can also be withdrawn, without such a withdrawal or its implementation requiring a further resolution by the General Meeting.

The Management Board was also authorised to effect the acquisition of treasury shares by using put or call options. However, any and all share purchases involving the use of derivatives shall be limited to a maximum threshold value of 5 % of the Company's share capital. In addition, any acquisition of shares shall count towards the 10 % threshold for the authorisation to acquire treasury shares. Where treasury shares are acquired using equity derivatives, the shareholders' right to enter into any option transactions with the Company is excluded in analogous application of section 186 (3) sentence 4 of the AktG.

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.

Combined Separate Non-Financial Report

The Combined Separate Non-Financial Report pursuant to sections 289b (3) and 315b (3) of the HGB has been published on the Company's website, on www.aareal-bank.com/en/responsibility/reporting-on-our-progress/.

Corporate Governance Statement

Since Aareal Bank AG is the only listed Group entity, and also the Group's parent undertaking, only one Corporate Governance Statement will be issued.

The full Corporate Governance Statement pursuant to sections 289f and 315d of the HGB is publicly available on the Company's website (www.aareal-bank.com/en/about-us/corporate-governance/), and in the "Transparency" section of the Group Annual Report.

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

Consolidated Financial Statements

Contents II

Consolidated Financial Statements
Statement of Comprehensive Income
Income Statement

€ mn	Note	1 Jan - 31 Dec 2020	1 Jan - 31 Dec 2019
Interest income from financial instruments (ac and fvoci)		720	889
Interest income from financial instruments (fvpl)		34	44
Market-driven modification gains		0	0
Interest expenses for financial instruments (ac)		75	111
Interest expenses for financial instruments (fvpl)		166	289
Market-driven modification losses		1	0
Net interest income	31	**512**	**533**
Loss allowance excluding credit-driven net modification gain or loss		343	85
Credit-driven net modification gain or loss		1	5
Loss allowance	32	**344**	**90**
Commission income		283	279
Commission expenses		49	50
Net commission income	33	**234**	**229**
Net gain or loss on the derecognition of financial assets (ac)		19	31
Net gain or loss on the derecognition of financial liabilities (ac)		7	3
Net gain or loss on the derecognition of financial assets (fvoci)		2	30
Net derecognition gain or loss	34	**28**	**64**
Net gain or loss from financial instruments (fvpl)	35	-32	1
Net gain or loss from hedge accounting	36	6	-4
Net gain or loss from investments accounted for using the equity method	37	1	1
Administrative expenses	38	469	488
Net other operating income/expenses	39	-11	2
Operating profit		**-75**	**248**
Income taxes	40	-6	85
Consolidated net income		**-69**	**163**
Consolidated net income attributable to non-controlling interests		5	2
Consolidated net income attributable to shareholders of Aareal Bank AG		-74	161
Earnings per share (EpS)			
Consolidated net income attributable to shareholders of Aareal Bank AG [1)]		-74	161
of which: allocated to ordinary shareholders		-90	145
of which: allocated to AT1 investors		16	16
Earnings per ordinary share (€)	41	-1.50	2.42
Earnings per AT1 unit (€)	41	0.16	0.16

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

Statement of Comprehensive Income

Reconciliation from Consolidated Net Income to Total Comprehensive Income

€ mn	1 Jan - 31 Dec 2020	1 Jan - 31 Dec 2019
Consolidated net income	**-69**	**163**
Items that will not be reclassified subsequently to profit or loss		
Changes in the reserve from remeasurements of defined benefit plans	**-29**	**-43**
Remeasurements of defined benefit plans	-43	-62
Taxes on remeasurements of defined benefit plans	14	19
Changes in the reserve from the measurement of equity instruments (fvoci)	**0**	**-4**
Gains and losses from equity instruments (fvoci)	0	-4
Reclassifications to retained earnings from equity instruments (fvoci)	–	–
Taxes on gains and losses from equity instruments (fvoci)	0	0
Items that are reclassified subsequently to profit or loss		
Changes in the reserve from the measurement of debt instruments (fvoci)	**5**	**-32**
Gains and losses from debt instruments (fvoci)	9	-16
Reclassifications to the income statement from debt instruments (fvoci)	-2	-30
Taxes on gains and losses from debt instruments (fvoci)	-2	14
Changes in the reserve from foreign currency basis spreads	**-11**	**-6**
Gains and losses from foreign currency basis spreads	-16	-9
Reclassifications to the income statement from foreign currency basis spreads	–	–
Taxes on gains and losses from foreign currency basis spreads	5	3
Changes in currency translation reserves	**-13**	**3**
Gains and losses from translating foreign operations' financial statements	-5	2
Reclassifications to the income statement from translating foreign operations’ financial statements	–	–
Taxes on gains and losses arising from translating foreign operations’ financial statements	-8	1
Other comprehensive income	**-48**	**-82**
Total comprehensive income	**-117**	**81**
Total comprehensive income attributable to non-controlling interests	5	2
Total comprehensive income attributable to shareholders of Aareal Bank AG	-122	79

Statement of Financial Position

€ mn	Note	31 Dec 2020	31 Dec 2019
Assets			
Financial assets (ac)	42	**37,999**	**33,972**
Cash funds (ac)	10	4,744	1,494
Loan receivables (ac)	11	27,277	25,783
Money market and capital market receivables (ac)	12	5,884	6,618
Receivables from other transactions (ac)	14	94	77
Loss allowance (ac)	43	-592	-386
Financial assets (fvoci)	44	**3,672**	**3,420**
Money market and capital market receivables (fvoci)	12	3,667	3,415
Equity instruments (fvoci)	13	5	5
Financial assets (fvpl)	45	**3,167**	**2,979**
Loan receivables (fvpl)	11	856	1,050
Money market and capital market receivables (fvpl)	12	93	135
Positive market value of designated hedging derivatives (fvpl)	15	1,431	1,380
Positive market value of other derivatives (fvpl)	16	787	414
Investments accounted for using the equity method	17, 46	13	8
Intangible assets	18, 47	207	175
Property and equipment	19, 48	289	311
Income tax assets	20, 49	116	30
Deferred tax assets	21, 50	176	168
Other assets	22, 51	431	460
Total		**45,478**	**41,137**
Equity and liabilities			
Financial liabilities (ac)	52	**39,823**	**35,332**
Money market and capital market liabilities (ac)	23	28,206	24,526
Deposits from the housing industry (ac)	24	10,592	9,744
Liabilities from other transactions (ac)	25	86	94
Subordinated liabilities (ac)	26	939	968
Financial liabilities (fvpl)	53	**1,906**	**2,165**
Negative market value of designated hedging derivatives (fvpl)	15	1,298	1,341
Negative market value of other derivatives (fvpl)	16	608	824
Provisions	27, 54	583	581
Income tax liabilities	55	20	44
Deferred tax liabilities	21, 56	36	19
Other liabilities	28, 57	143	135
Equity	29, 58	**2,967**	**2,861**
Subscribed capital		180	180
Capital reserves		721	721
Retained earnings		1,902	1,812
AT1 bond		300	300
Other reserves		-197	-154
Non-controlling interests		61	2
Total		**45,478**	**41,137**

Statement of Changes in Equity

€ mn	Subscribed capital	Capital reserves	Retained earnings	AT1 bond	Other reserves: Reserve from remeasurements of defined benefit plans	Other reserves: Reserve from the measurement of equity instruments (fvoci)	Other reserves: Reserve from the measurement of debt instruments (fvoci)	Other reserves: Reserve from changes in the value of foreign currency basis spreads	Other reserves: Currency translation reserve	Total	Non-controlling interests	Equity
Equity as at 1 Jan 2020	**180**	**721**	**1,812**	**300**	**-141**	**-4**	**7**	**-15**	**-1**	**2,859**	**2**	**2,861**
Total comprehensive income for the period	–	–	-74	**–**	-29	0	5	-11	-13	**-122**	5	**-117**
Payments to non-controlling interests	–	–	–	**–**	–	–	–	–	–	**–**	-2	**-2**
Dividends	–	–	–	**–**	–	–	–	–	–	**–**	–	**–**
AT1 coupon	–	–	-16	**–**	–	–	–	–	–	**-16**	–	**-16**
Changes in ownership interests in subsidiaries	–	–	180	**–**	4	–	–	–	1	**185**	56	**241**
Equity as at 31 Dec 2020	**180**	**721**	**1,902**	**300**	**-166**	**-4**	**12**	**-26**	**-13**	**2,906**	**61**	**2,967**

€ mn	Subscribed capital	Capital reserves	Retained earnings	AT1 bond	Other reserves: Reserve from remeasurements of defined benefit plans	Other reserves: Reserve from the measurement of equity instruments (fvoci)	Other reserves: Reserve from the measurement of debt instruments (fvoci)	Other reserves: Reserve from changes in the value of foreign currency basis spreads	Other reserves: Currency translation reserve	Total	Non-controlling interests	Equity
Equity as at 1 Jan 2019	**180**	**721**	**1,793**	**300**	**-98**	**–**	**39**	**-9**	**-4**	**2,922**	**2**	**2,924**
Total comprehensive income for the period	–	–	161	**–**	-43	-4	-32	-6	3	**79**	2	**81**
Payments to non-controlling interests	–	–	–	**–**	–	–	–	–	–	**–**	-2	**-2**
Dividends	–	–	-126	**–**	–	–	–	–	–	**-126**	–	**-126**
AT1 coupon	–	–	-16	**–**	–	–	–	–	–	**-16**	–	**-16**
Changes in ownership interests in subsidiaries	–	–	–	**–**	–	–	–	–	–	**–**	–	**–**
Equity as at 31 Dec 2019	**180**	**721**	**1,812**	**300**	**-141**	**-4**	**7**	**-15**	**-1**	**2,859**	**2**	**2,861**

Statement of Cash Flows

€ mn	Cash flow 1 Jan - 31 Dec 2020	Cash flow 1 Jan - 31 Dec 2019
Consolidated net income	**-69**	**163**
Additions to and reversals of loss allowances	348	94
Amortisation, depreciation, impairment and write-ups of non-current assets	45	46
Other non-cash changes	-117	170
Gains/losses on the disposal of non-current assets	-8	-3
Other adjustments	-569	-530
Adjusted consolidated net income	**-370**	**-60**
Changes in financial assets (ac) (excluding cash funds)	-641	1,119
Changes in financial assets (fvoci)	-151	927
Changes in financial assets (fvpl)	-104	36
Changes in other assets	-46	-142
Changes in financial liabilities (ac) (excluding subordinated capital)	4,297	-1,795
Changes in financial liabilities (fvpl)	-435	34
Changes in provisions	-70	-74
Changes in other liabilities	-4	2
Income taxes paid/income tax refunds	16	-72
Interest received	790	778
Interest paid	-273	-268
Cash flow from operating activities	**3,009**	**485**
Proceeds from the disposal of equity instruments and investments accounted for using the equity method	0	0
Payments for the acquisition of equity instruments and investments accounted for using the equity method	-4	1
Proceeds from the disposal of property and equipment and intangible assets	40	21
Payments for the acquisition of property and equipment and intangible assets	-41	-33
Effect of changes in reporting entity structure	0	0
Cash flow from investing activities	**-5**	**-11**
Dividends paid and AT1 coupon payments	-16	-141
Changes in subordinated liabilities	24	-102
Changes due to other funding activities	238	-2
Cash flow from financing activities	**246**	**-245**
Cash and cash equivalents as at 1 January	**1,494**	**1,265**
Cash flow from operating activities	3,009	485
Cash flow from investing activities	-5	-11
Cash flow from financing activities	246	-245
Cash and cash equivalents as at 31 December	**4,744**	**1,494**

Notes
Basis of Accounting

Aareal Bank AG is a public limited company incorporated under German law, with its registered office in Paulinenstrasse 15, 65189 Wiesbaden, Germany. Aareal Bank AG is the parent company of an international property finance and services group, and registered under no. HRB 13184 in the Commercial Register at the Wiesbaden local court (Amtsgericht Wiesbaden, Germany).

As a listed public limited company, Aareal Bank AG has prepared its consolidated financial statements for the financial year ended on 31 December 2020 in accordance with International Financial Reporting Standards (IFRSs) applicable within the European Union (EU) as at the reporting date, in connection with the provisions pursuant to section 315e of the German Commercial Code (Handelsgesetzbuch – "HGB"). The reporting currency is the euro (€). In addition, the consolidated financial statements were prepared using the European Single Electronic Format pursuant to Commission Delegated Regulation (EU) No. 2019/815 as amended (i.e. in the XHTML format) and were complemented with tags based on Inline XBRL technology.

The Management Board approved the consolidated financial statements for publication on 2 March 2021; they will be published in the German Federal Gazette.

Accounting Policies

(1) Accounting standards

Recognition and measurement within Aareal Bank Group are based on accounting policies applied consistently throughout the Group. The consolidated financial statements are prepared on a going concern basis.

We apply accounting policies – and the presentation of financial statements – consistently, in order to ensure the comparability of financial statements over time.

Information is presented in accordance with the principle of materiality. Minor differences may occur regarding the figures stated, due to rounding.

The Bank observes the general prohibition of setting off assets against liabilities. To the extent that the criteria of IAS 12.74 are met, deferred tax assets and deferred tax liabilities are offset. If the requirements set out in IAS 32.42 are met, financial assets and liabilities are reported on a net basis.

Income and expenses are recognised on an accrual basis and recorded in the income statement in the period to which they relate.

Interest income and expenses are recognised using the effective interest method. In the case of impaired receivables, interest income and expenses are recognised only on the basis of the net carrying amount. Interest from derivatives designated for hedge accounting and economic hedging relationships is included in net interest income. Interest from derivative hedging instruments is shown under interest from financial instruments (ac and fvoci), while interest from economic hedging relationships is reported under interest from financial instruments (fvpl). We provide specific information on negative interest from financial assets or positive interest from financial liabilities in the Notes, under net interest income. These assets and liabilities are deposits as well as money market and securities repurchase transactions. The interest benefit from the ECB's Targeted Longer-Term Refinancing Operations (TLTRO) is recognised if there is reasonable certainty that it will be granted.

Dividend income is recognised when there is a corresponding legal title.

Commission income and expenses include revenue from the provision of goods or services in the ordinary course of business. This mainly refers to IT consulting projects, trainings, licence and maintenance agreements and hosting or outsourcing services.

The presentation of the financial position and the financial performance in the consolidated financial statements depends on the recognition and measurement methods underlying the preparation of the financial statements, as well as on estimates and assumptions made by the management in relation to uncertain future events. Any assessments required for recognition and measurement are prepared in line with the relevant accounting standards. Estimates and assumptions are based on historical experience and other factors, such as planning and current expectations and forecasts with respect to the occurrence of future events. The estimates and assessments themselves as well as the underlying assessment factors and estimation techniques are reviewed regularly and compared with actual outcome. In our view, the parameters used are relevant and reasonable.

The most significant estimates and assumptions of the management primarily refer to the calculation of provisions, allowances for credit losses and provisions in the lending business, the measurement of goodwill, property and tax assets and liabilities. We refer to the item-specific disclosures in this section for information related to the estimates and assumptions actually made within the context of recognition and measurement.

An asset is recognised in the statement of financial position when it is probable that an associated future economic benefit will flow to the Company and the asset can be measured reliably.

A liability is recognised if it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and when the settlement amount of the liability can be measured with sufficient reliability.

(2) Changes in accounting policies

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

- **IAS 1 Definition of Material (IAS 8)**
  The amendments were issued to refine the definition of the term "material" and to harmonise the various definitions in the Conceptual Framework and in the standards.

- **IFRS 3 Definition of a Business**
  The objective of the amendments is to resolve cases of doubt that arise when a company determines whether it has acquired a business or a group of assets. The problems result from the fact that the accounting policies for goodwill, the acquisition costs and deferred taxes in case of the acquisition of a business differ from those applicable to the purchase of a group of assets.

The new and revised standards and interpretations did not have material consequences for the consolidated financial statements of Aareal Bank Group.

Until 31 December 2020, the following financial reporting standards (IASs/IFRSs) and interpretations (IFRICs) had been published by the International Accounting Standards Board (IASB) and endorsed by the EU Commission:

New International Financial Reporting Standards/Interpretations		Issued	Endorsed	Effective date
IFRS 17	Insurance Contracts	May 2017		Financial years beginning on or after 1 January 2022
ED/2019/7	General Presentation and Disclosures	December 2019		Pending

Revised International Financial Reporting Standards		Issued	Endorsed	Effective date
IFRS 16	Covid-19-Related Rent Concessions	May 2020	October 2020	Financial years beginning on or after 1 June 2020
IFRS 9, IFRS 7	Interest Rate Benchmark Reform (Phase 2)	August 2020	January 2021	Financial years beginning on or after 1 January 2021
IFRS 3	Reference to the Conceptual Framework	May 2020		Financial years beginning on or after 1 January 2022
IAS 37	Onerous Contracts – Costs of Fulfilling a contract	May 2020		Financial years beginning on or after 1 January 2022
IAS 16	Property, Plant and Equipment	May 2020		Financial years beginning on or after 1 January 2022
	Annual Improvements 2018–2020	May 2020		Financial years beginning on or after 1 January 2022
IAS 1	Classification of Liabilities as Current or Non-current	May 2020		Financial years beginning on or after 1 January 2023
ED/2020/4	Lease Liability in a Sale and Leaseback	November 2020		Pending

- **IFRS 17 Insurance Contracts**
  The standard governs the accounting for insurance contracts. IFRS 17 replaces the previously applicable interim standard IFRS 4. The new standard applies to insurance contracts, reinsurance contracts as well as investment contracts with discretionary participation features. In accordance with IFRS 17, insurance contracts are generally measured using the general measurement model. Under this model, the fulfilment cash flows and the contractual service margin are determined upon initial recognition for a group of insurance contracts. Depending on what any changes in underlying parameters refer to, subsequent measurement affects either insurance revenue or insurance finance income or expenses, or the contractual service margin may have to be adjusted which will affect the income statement only in later periods.

- **Covid-19-related rent concessions**
  The amendments grant lessees an exemption from the assessment as to whether rent concessions granted due to the Covid-19 pandemic (such as rent free periods or temporary rent reductions) constitute a lease modification. If an entity elects to apply this exemption, rent concessions have to be accounted for as if they did not represent modifications of the lease agreement. The changes apply to rent concessions which lead to a reduction of the rental payments due on or before 30 June 2021. In the 2020 financial year, Aareal Bank Group decided to opt for an early application of these standards.

- **IFRS 9 / IFRS 7 Interest Rate Benchmark Reform (Phase 2)**
  The second phase of the standard amendments as a result of the effects of the IBOR reform refers to the period when the existing interest rate benchmarks are replaced. Apart from hedge accounting requirements, the amendments concern practical expedients regarding the recognition of modifications of financial instruments and other disclosure requirements.

  The effects of the IBOR reform are analysed and monitored, and any resulting new requirements are implemented, as part of a separate project. The transition of the collateralisation of centrally settled derivatives as well as the transition of the discounting of the derivatives to the new interest rate benchmarks were made in July (for EUR) and October 2020 (for USD), respectively. The transition of collateral agreements of OTC derivatives and of the discounting of the derivatives was implemented gradually on a case-by-case basis in accordance with the bilateral agreements between the counterparties from the second half of 2020. Any existing hedging relationships did not have to be discontinued.

The necessary adjustments of the new business to the new interest rate benchmarks are currently being implemented so that, depending on the progress of implementation, the first transactions can already be made using the new interest rate benchmarks. The existing transactions will be changed starting in 2021 on a currency-by-currency basis. Therefore, there have not yet been any changes of the contractual cash flows due to the changes to the new interest rate benchmarks, which means that there neither have been any modifications. Overall, we do not expect any material effects from transition. To the extent that transactions are concluded using the new interest rate benchmarks and/or existing transactions are changed to refer to such new benchmarks, this will be taken into account as part of the risk management strategy.

- **IFRS 3 Reference to the Conceptual Framework**
  The amendments result in an update of IFRS 3 pursuant to which the standard now refers to the Conceptual Framework 2018 and no longer to the Conceptual Framework 1989. Moreover, two additions were made. In terms of the identification of liabilities that an acquirer has assumed in a business combination, the acquirer has to apply the provisions set out in IAS 37 or IFRIC 21 (instead of those included in the Conceptual Framework) for transactions and similar events that are within the scope of IAS 37 or IFRIC 21. Moreover, the explicit statement that contingent assets acquired in a business combination shall not be recognised was included.

- **IAS 37 Onerous Contracts – Costs of Fulfilling a Contract**
  The amendments determine that the "cost of fulfilling a contract" comprises the "costs that relate directly to a contract". Such costs may either be incremental costs of fulfilling that contract (for example, direct labour and materials) or an allocation of other costs that relate directly to fulfilling contracts (for example, an allocation of the depreciation charge for an item of property, plant and equipment used in fulfilling that contract).

- **IAS 16 Property, Plant & Equipment: Proceeds before Intended Use**
  As a result of the amendments, it is now prohibited to deduct income from the cost of an item of property, plant and equipment that results from selling any goods produced while such item of property, plant and equipment is being brought to the location and condition necessary for it to be capable of operating in the manner intended by the management. Instead, an entity recognises the proceeds from such disposals and the costs for the production of these goods under operating profit. As before, costs for test runs carried out to test whether the item of property, plant and equipment is working properly are an example for directly attributable costs.

- **Annual Improvements 2018 – 2020**
  Improvements to IFRS 1, IFRS 9, IFRS 16 and IAS 41

- **IAS 1 Classifications of Liabilities as Current or Non-Current**
  The amendments to IAS 1 are meant to clarify the classification of liabilities as current or non-current. In future, only rights that exist as at the end of the reporting period shall be relevant for the classification of a liability. In addition, further guidance as to the interpretation of the criterion "right to defer settlement for at least twelve months" as well as explanations regarding settlement characteristics were included.

With the exception of the standard amendments with respect to Covid-19-related rent concessions, Aareal Bank Group did not opt for early application of these standards in 2020, which are required to be applied in future financial years.

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

(3) Consolidation

Consolidation principles

The consolidated financial statements of Aareal Bank Group include all subsidiaries which are controlled directly or indirectly by Aareal Bank AG. Aareal Bank controls an investee when it has the power to direct the investee's relevant activities, has an exposure or rights to variable returns from its involvement with the investee and has the ability to use its power over the investee to affect the amount of such returns. If control is exercised via voting rights, Aareal Bank assumes that a parent-subsidiary relationship exists if more than half of the voting rights are held directly or indirectly. In cases where voting rights are not conclusive in determining control relationships, other factors are used to assess whether Aareal Bank Group has the power over the company. For this purpose, an assessment is made of the following: purpose and design of an investee, what are the relevant activities of the company, what is the decision-making process in relation to these relevant activities and whether Aareal Bank, by virtue of its rights, currently has the ability to direct these relevant activities. In addition, we assess whether Aareal Bank Group exercises control as principal or as agent or whether a third party acts as agent for the Group. If the assessment shows that Aareal Bank has the sole power over an investee and additionally has the ability to use its power over the investee to affect the amount of the investor's returns, the investee is included in the consolidated financial statements.

Consolidation of a subsidiary begins from the date the Group obtains significant influence (full consolidation). Subsidiaries are deconsolidated when there is no longer the ability to exercise significant influence.

Any non-controlling interests resulting from full consolidation are shown in the statement of financial position, as a separate item of equity. This also applies to a partial disposal without the loss of control over the subsidiary (sale of a non-controlling interest).

Initial consolidation of an entity in the event of an acquisition is based on the purchase method, in accordance with IFRS 3, whereby remeasured amounts must be used when recognising assets and liabilities (including any hidden reserves and hidden encumbrances) of an entity to be consolidated. This may lead to the recognition of new assets and liabilities (including contingent liabilities) that were previously not reported in the statement of financial position of the company to be consolidated. Any excess of acquisition cost over the Group's interest in the fair value of net assets is recognised as (positive) goodwill. Any negative goodwill determined during this comparison is charged against income.

Intragroup transactions, balances and results of transactions between Group entities are eliminated. Accounting policies applied by subsidiaries were amended for the purpose of preparing consolidated financial statements to the extent required to ensure consistent accounting throughout the Group.

Joint arrangements are defined as contractual arrangements where two or more parties carry out business activities that are subject to joint control. Joint control only exists when the decisions about the relevant activities require unanimous consent of the parties sharing control. In general, a distinction is made between joint operations and joint ventures. The parties to a joint operation that have joint control have the rights to the assets, and the obligations for the liabilities, relating to the arrangement. Assets and obligations, as well as revenue and expenses are carried on a pro-rata basis. A joint venture is a joint arrangement whereby the parties that have joint control of the arrangement have rights to the net assets of the arrangement. Interests in joint ventures are measured using the equity method.

Associates are companies in which the Group has an equity interest and may exercise significant influence, without having control. Significant influence is deemed to exist when an investor holds 20%-50% of the voting rights of a company. Associates are also measured using the equity method.

In accordance with the equity method, the Group's share in the profit or loss of associates and joint ventures is recognised in the consolidated income statement from the date of acquisition and is included in the carrying amount of the equity investment, taking into account interim distributions. Further information on investments accounted for using the equity method is included in Note (46).

Associates and joint ventures are no longer accounted for using the equity method from the date when Aareal Bank loses significant influence over the company or when joint control ends.

As at the reporting date, Aareal Bank was not exposed to material limitations as regards the access to, or use of, assets of the Group and as regards the settlement of liabilities of the Group.

Reporting entity structure

As at 31 December 2020, the reporting entity structure comprised 68 companies (2019: 65), including Aareal Bank AG as well as 59 (2019: 59) subsidiaries, one joint arrangement (2019: one) and seven associates (2019: four). The additions were offset by mergers/integrations of existing subsidiaries so that the total number of subsidiaries remains unchanged over the previous year.

During the reporting period, CalCon Group and Tintoretto Rome S.r.l., which originated from an Italian lending exposure, were added to the reporting entity structure. Moreover, an investment in the start-up objego – a joint venture with ista Deutschland GmbH which provides software to private landlords with up to 250 units, allowing them to manage their rented apartments in an efficient and straightforward manner – was acquired. There were no other material changes to the reporting entity structure.

Aareon acquired the business operations of CalCon Holding GmbH and its subsidiaries within the scope of an asset deal, effective 1 January 2020. In Germany and Austria, the takeover encompassed 100% of the capital, and a 83.33% stake in Romania. CalCon is a provider of digital solutions for structural condition assessment, requirements assessment, and maintenance planning in Germany and Austria. The purchase price consists of a fixed price paid of € 20 million, plus a contingent purchase price to be determined by comparing realised to planned EBIT for the years 2020 and 2021. The fair value of the contingent purchase price amounted to € 4 million at the time of acquisition and was measured on the assumption of 100% target achievement. The maximum contingent purchase price is € 6 million, with the fair value of the assets and liabilities measured at € 11 million. The acquisition resulted in goodwill of € 13 million, including potential market value effects and synergies. The acquisition complements our Aareon Smart World product portfolio and provides potential for business with public-sector entities and the commercial property sector in Germany and Austria.

On 23 December 2020, Aareon signed an agreement for the acquisition of 100% of the shares in Arthur Online Ltd. The company was acquired with effect from 29 January 2021. The purchase price exclusively comprised a fixed price of € 19 million, which was paid by means of a cash consideration of € 17 million and a consideration in kind in the amount of € 2 million in return for granting shares in Aareon AG within the context of a capital increase. The preliminary fair value of the assets and liabilities amounts to € 5 million. The acquisition results in a preliminary goodwill of € 14 million. With this acquisition, Aareon enters into the business field of small and medium-sized property managers in the UK. This presents Aareon with additional growth potentials.

Note (89) "List of Shareholdings" includes an overview of the Group companies.

(4) Currency translation

Individual line items in the financial statements of each Group entity are measured on the basis of the currency of the primary economic environment the respective entity operates in ("functional currency"). The consolidated financial statements are prepared in euro, being both the functional and the reporting currency.

Monetary assets and liabilities denominated in a foreign currency, unsettled cash market/spot transactions and non-monetary items measured at fair value are all translated to the functional currency on the basis of the ECB reference rate prevailing on the balance sheet date. Non-monetary items measured at amortised cost are translated using historical rates. Foreign exchange forward transactions are measured at the forward exchange rate prevailing on the balance sheet date.

Currency translation adjustments on monetary assets and liabilities must be recognised in income. Depending on the relevant measurement category, currency translation adjustments on non-monetary items are either recognised directly in equity (in the currency translation reserves), or recognised in the income statement (in net gain or loss from transactions measured at fair value).

Financial statements of consolidated subsidiaries, which are presented in a currency other than the euro, are translated at the ECB reference rate prevailing at the reporting date (statement of financial position) and at (monthly) average rates (income statement). Translation differences are recognised in equity, in the currency translation reserves.

(5) Revenue recognition

Aareal Bank Group recognises revenue in the banking business as well as in the area of Consulting/Services. Revenue recognition in the banking business mainly refers to the provision of loans, the administration of syndicated loans or the provision of payment systems for the property and energy industries. Aareal Bank Group recognises revenue in the same period in which the services are provided. When contracts comprise various performance obligations, each of the performance obligations are priced separately. Mostly, fixed fees are agreed. Commissions from the lending and other banking business mainly arise over a specified period of time. The customer obtains control over the service while Aareal Bank is providing the service. The agreed transaction price is invoiced to the customer on a pro-rata basis as at the end of an agreed period (normally monthly or quarterly). The Bank recognises the invoiced amount as revenue when it is entitled to a consideration in an amount that directly corresponds to the value of the services already provided. Invoiced amounts are payable immediately in the agreed amounts. Since the service has already been provided at the time the invoice is issued, an unconditional right to consideration arises, and a receivable due from the customer is recorded.

In the Consulting/Services division, Aareal Bank Group earns revenue mainly from the country-specific ERP business in the property industry, from the marketing of digital solutions and other additional products and services such as insurance management, IT outsourcing, solutions for the energy industry and integrated payment systems. In this context, services are provided within the framework of licence agreements, maintenance agreements, consulting and training projects as well as hosting from the exclusive Aareon Cloud.

Licence revenue is deemed to be realised when there is an agreement signed by both parties without a right of rescission, the product has been delivered in its entirety (e.g. via licence keys), the licence fee is fixed, and payment is probable. Thus, the customer obtains control over the right-of-use asset transferred. The payment is made primarily after the licence agreement has been concluded or after successful implementation of the software with a credit term of several days. Revenue is accrued as a contract asset until the implementation is completed. After that, the amount is recognised as a trade receivable.

The recognition of maintenance as well as hosting and outsourcing services is made on a pro-rata basis over the contractual service period. Hosting solutions are billed monthly and recorded as sales revenue. A large portion of the customers pays its maintenance and hosting fees in advance for a specified period (not more than one year). The advance payments that refer to performance obligations that have not yet been satisfied are accrued as contract liabilities and released on a pro-rata basis as the services are provided in future. The customer obtains the benefits from the service and uses the service at the same time as it is provided.

Consulting and training services are recognised in income when the service has been provided. In addition, the Group provides implementation services as part of projects. This involves the generation or enhancement of assets for the customers over which they obtain control. Revenue recognition as well as the recognition of the contract asset are based on the progress towards complete satisfaction which is normally measured using input methods. The progress of the projects is determined by comparing the contract costs incurred with the expected contract costs for the project. Customers make advance payments in relation to the long-term services provided by Aareon. These are offset against the related contract assets, or reported under contract liabilities if the advance payment received exceeds the contract asset. Provisions are recognised for anticipated losses from such services in the period in which they are caused, to the extent that there is no assets item.

Standardised contracts are concluded within Aareal Bank Group for the vast majority of contracts with customers. This does not involve costs of obtaining a contract. In addition, there are no material amounts of variable consideration for the various services. The customers are not granted significant financing components.

(6) Leases

A lease is a contract or a part of a contract that conveys the right to control the use of an identified asset for a period of time in exchange for consideration.

In accordance with IFRS 16, a lessee has to recognise a liability for lease payments as well as an asset for the right to use the underlying asset during the lease term. The practical relief provided for by the IFRS 16 as regards short-term lease agreements and low-value leased assets is made use of. The lease liabilities include the present value of the lease payments to be made over the lease term. Lease payments may comprise:

- fixed payments less any lease incentives receivable,
- variable lease payments that depend on an index or interest rate,
- amounts expected to be payable under residual value guarantees,
- the exercise price of a purchase option if the exercise of the option is reasonably certain, and
- payments of penalties for terminating the lease if terminating the lease is reasonably certain.

To determine the present value, the lease payments are discounted using the interest rate implicit in the lease. If such rate cannot be determined, discounting is based on Aareal Bank Group's incremental borrowing rate for the corresponding maturity band and the corresponding currency. The lease term is determined as the non-cancellable period of a lease, taking into account both extension options and termination options if it is reasonably certain that such options are exercised.

The right-of-use asset is measured upon initial measurement at cost which comprises the following amounts:

- the amount of the lease liability,
- any lease payments made to the lessor at or before the commencement date, less any lease incentives received,
- any initial direct costs, and
- asset retirement obligations.

These items are re-measured at amortised cost. The right-of-use assets are depreciated on a straight-line basis over the lease term.

Aareal Bank Group does not apply the IFRS 16 rules to leases where the Bank acts as the lessee involving intangible assets. If contracts include both lease components and non-lease components, the practical expedient as provided for by the standard not to separate these components is made use of.

Aareal Bank Group also acts as lessor, in which case a distinction has to be made between operating and finance leases. The basis for this classification is the extent to which the risks and rewards incidental to ownership of an underlying asset are attributable to either the lessor or the lessee. If a substantial portion of the risks and rewards remain with the lessor, the lease is classified as an operating lease. Where substantially all risks and rewards are transferred to the lessee, the lease is classified as a finance lease.

The major rental contracts of Aareal Bank Group as lessor are operating leases and mainly refer to let property. They are reported in the statement of financial position under other assets. Lease contracts are entered into individually and include various terms and conditions.

In the case of operating leases, the leased asset continues to be recognised as an asset at amortised cost. The lease payments received are reported in the income statement in net other operating income/expenses.

In the case of finance leases, Aareal Bank Group derecognises the carrying amount of the leased asset as at the commencement date and recognises a receivable at an amount equal to the net investment in the lease. Any gains or losses on disposal are recognised in the income statement.

For subsequent measurement, interest income from the lease receivable is recognised and the net investment in the lease is reduced by the lease payments received. Any impairment resulting from these lease receivables are included in the loss allowance in accordance with IFRS 9.

(7) Consolidated statement of cash flows

Aareal Bank Group's statement of cash flows records cash flows pertaining to the areas of operating activities, investing activities and financing activities for the period under review. The starting point of the consolidated statement of cash flows is the amount of cash and cash equivalents, consisting of cash on hand, balances with central banks as well as public-sector debt instruments and bills of exchange eligible for refinancing at central banks.

The definition of the term "operating activities" is consistent with the composition of the operating profit in the statement of comprehensive income. Cash flows from investing activities include proceeds from and payments for property and equipment, intangible assets, equity instruments and investments. Cash flows from financing activities include cash flows from transactions with providers of equity and subordinated capital.

(8) Determination of fair value

The determination of fair value is governed by IFRS 13 and applies to both financial instruments and non-financial assets or liabilities. In accordance with IFRS 13.9, the fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction under current market conditions at the measurement date. The determination of the fair value is based on the principal market for the asset or liability or, in the absence of a principal market, the most advantageous market for the asset or liability. Another factor to be taken into account is whether Aareal Bank can enter into a transaction for the relevant asset or liability at the price in that market at the measurement date. The principal market is the market with the greatest volume and the highest level of activity for the asset or liability to which Aareal Bank has access. The most advantageous market is the market that maximises the amount that would be received to sell the asset, or minimises the amount that would be paid to transfer the liability.

Fair value hierarchy

In accordance with IFRS 13.72 et seqq., the fair value determination is based on the fair value hierarchy pursuant to which the inputs used are classified into various hierarchy levels on the basis of their respective market proximity and objectivity. The fair value of assets and liabilities is allocated to Level 1 of the fair value hierarchy if it is determined on the basis of unadjusted qualifying prices in active markets for identical assets or liabilities. Fair values determined using inputs other than qualifying prices included within Level 1 that are observable for the financial instrument, either directly or indirectly, are included in Level 2 of the fair value hierarchy. Fair values determined using valuation techniques where one or more material inputs are not based on observable market data are assigned to Level 3 of the fair value hierarchy. The estimation uncertainties as regards fair value measurement increase the higher the level is.

Measurement methods

The property and public-sector loans included in loan receivables are measured using the discounted cash flow method for the purpose of the determination of fair value. Discounting of future cash flows of a transaction is based on transaction-specific risk-adjusted interest rates. These are derived on the basis of a virtually risk-free market interest rate for each currency depending on the relevant term, taking into account add-ons for risks specific to the counterparty as well as credit costs. In the case of loans subject to fixed interest rates, the contractually agreed payments are used as future cash flows. The future cash flows for floating-rate loans are derived using the future forward interest rates, taking into account the relevant spread for customer-specific terms and conditions. In the case of defaulted loans, future cash flows are reduced by the expected losses. Debt securities and promissory note loans for which no current market price is available in an active market are measured through an analysis of future payments using the fully-capitalised earnings value approach, where the inputs are based on observable market data to the extent possible. These approaches include the discounted cash flow (DCF) method which is used to determine the present value of contractual cash flows until the expected end of the term. The present value is determined based on the benchmark curve applicable for the relevant market, taking into account mark-ups based on credit quality and liquidity. The valuation model used for options included in the transaction is the commonly used Black-Scholes model or numerical procedures.

In the case of unquoted financial investments in equity instruments, the costs of acquisition may also be the best estimate of fair value.

The fair value of OTC derivatives is determined on the basis of sector-specific standardised measurement models, such as the present value method or option pricing models. These techniques are based on inputs of active markets, such as interest rates, yield curves and credit spreads. The fair value of foreign exchange forwards is generally based on current forward exchange rates quoted on active markets. Since the derivatives are part of highly effective collateral agreements (Credit Support Annex to the ISDA Master Agreement and Collateral Annex to the German Master Agreement on Financial Derivatives Transactions) which are each subject to a master collateralisation agreement, measurement adjustments to reflect any potential counterparty credit risk or own credit risk (CVA and DVA) are not required for reasons of materiality. Nevertheless, with respect to defaulted property loans, receivables arising from associated derivatives are taken into account in the determination of loss allowances. The Bank uses the overnight interest rate swap curve (OIS curve) for the measurement of derivatives secured by cash collateral.

Amortised cost is an adequate estimate of fair value for cash funds, other loan receivables as well as short-term money market receivables and liabilities.

(9) Recognition and measurement of financial instruments

Pursuant to IAS 32, a financial instrument is any contract that gives rise to a financial asset at one contracting party and a financial liability or equity instrument at another contracting party.

Recognition

Financial instruments (including derivative financial instruments) must be recognised if the reporting entity has become a party to the contractual provisions of such financial instruments. Trade date and settlement date are not the same for regular way purchases and sales of financial assets. Such regular way purchases and sales may be accounted for either at trade date or at settlement date. At Aareal Bank Group, financial instruments (fvpl) are recognised at the trade date, while all other financial instruments are recognised at the settlement date.

Financial instruments have to be derecognised when the contractual rights to the cash flows from the financial asset expire or an entity transfers the financial asset, including substantially all its risks and rewards. The modification of the contractual terms may also result in the derecognition of a financial instrument and the recognition of a new financial instrument.

If only a portion of risks and rewards is transferred and a portion of control is retained, the financial asset is recognised only to the extent of its continuing involvement. The extent of the continuing involvement corresponds to the extent to which the Company is exposed to changes in the value of the financial asset. A financial liability is derecognised when it is extinguished, i.e. when the obligation specified in the contract is discharged.

Modification

As a matter of principle, a modification is defined as any change made to existing terms of a loan agreement or a contractual adjustment during the loan or contract term. This applies regardless of the reasons for the modification (credit-driven or market-driven). Contractual adjustments may either lead to the derecognition of the "old" and the recognition of a "new" asset when such adjustments are substantial to the extent that they, in essence, constitute a new asset (hereinafter referred to as "substantial modification") or to the recalculation of the carrying amount and the recognition of a net modification gain or loss, when such adjustments constitute an adjustment of an existing asset (hereinafter referred to as "non-substantial modification").

The contractual adjustments subject to modifications may generally be caused by the borrower's credit quality and solvency (credit-driven modifications) or the granting of more favourable terms and conditions in an existing contract or the adjustment of the framework for financings as a result of changes in the customer's financing needs (market-driven modifications).

Both substantial and non-substantial modifications have an impact on profit or loss.

The amount of net modification gains or losses arising from non-substantial modifications is determined by the difference of the gross carrying amounts before and after the modification. Net modification gains or losses arising from market-driven modifications are recognised in net interest income, while credit-driven modifications are reported in the loss allowance. Subsequently, the changes in the carrying amount of the receivable is amortised over the remaining term of the receivable and recorded in net interest income.

In the case of a substantial modification, the old asset has to be derecognised, and a new asset has to be recognised. The difference of the gross carrying amounts before and after the modification is reported as net derecognition gain or loss after utilisation of the existing loss allowance in the case of market-driven modifications. This also comprises the extension of terms of loans that are not subject to an impaired credit quality. The derecognition and new recognition of the loan results in a new significance level being determined for a later migration in Stage 2. In the case of credit-driven modifications, a loss allowance is recorded prior to derecognition in an amount that covers the entire difference between the old carrying amount and the fair value determined at the time of initial recognition.

Measurement

Upon initial recognition, financial instruments are measured at fair value, for subsequent measurement at ac or fvoci (cf. section Classification), in each case plus any transaction costs.

Subsequent measurement of financial assets is based on the classification of the financial instrument. Depending on the classification, financial assets are measured at amortised cost, at fair value through other comprehensive income or at fair value through profit or loss. Investments in equity instruments are measured at fair value through profit or loss, unless an irrevocable election is made at initial recognition to present subsequent changes in fair value in other comprehensive income. Within Aareal Bank Group, this election is exercised as a rule due to the investment characteristics of the equity instruments.

Financial liabilities are measured at amortised cost.

In addition, financial assets and liabilities may be designated as at fair value through profit or loss if certain prerequisites are met. Aareal Bank Group does not make use of this option.

Classification

The classification, i.e. the determination of the measurement category of a financial asset, is to be assessed on the basis of two criteria. The objective criterion refers to the contractual design as to whether the payments solely represent payments of interest and principal on the principal amount outstanding (SPPI = solely payments of principal and interest). Relevant criteria were defined that are reviewed at initial recognition. For example, this may be financings with a primary investment risk or contractually agreed payments that depend on the borrower's economic performance. The subjective classification criterion refers to the business model, i.e. the aim that a company pursues for a group of assets.

Subsequent measurement has to be based on amortised cost (ac) when the financial instrument is held in order to collect contractual cash flows (business model "Hold") and additionally the contractual cash flows represent solely payments of principal and interest, i.e. are SPPI compliant. This classification category is used for a large portion of the lending and securities business.

Subsequent measurement at fair value, with changes in fair value being recognised initially directly in equity and subsequently reclassified to profit or loss (so-called recycling) (fair value through other comprehensive income (fvoci)), has to be made when financial instruments are SPPI compliant and are held either to collect contractual cash flows or to be sold (business model "Hold & Sell").

Subsequent measurement at fair value, with changes in fair value being recognised through profit or loss (fvpl), has to be made if the financial instrument is not SPPI compliant or cannot be allocated to one of the two business models mentioned above. The latter is the case for example when there is the purpose of selling such financial instruments in the near term due to syndication covenants.

Loss allowance

Loss allowances are based on the internal staging and expected credit loss (ECL/EL) model of Aareal Bank. For this purpose, financial instruments measured at amortised cost and at fair value through other comprehensive income as well as loan commitments and financial guarantees are allocated to various stages at both initial recognition and subsequent measurement. The related loss allowances are recognised in the amount of the twelve-month or the lifetime expected credit loss.

Stage 1: All financial instruments without impairment trigger are allocated to this stage at initial recognition. If the credit risk is not significantly increased, the financial instrument has to remain in Stage 1 for subsequent measurement. Loss allowances are recognised in the amount of the losses expected for the following twelve months and interest income is calculated on the basis of the gross carrying amount, applying the effective interest method. Loss allowances have to be recognised on a present value basis.

Stage 2: All financial instruments where credit risk has increased significantly since initial recognition are allocated to this stage. Loss allowances are recognised in the amount of the losses expected for the entire remaining term of the instrument and interest income is calculated on the basis of the gross carrying amount, applying the effective interest method. Loss allowances have to be recognised on a present value basis. The significant increase in credit risk for the allocation to Stage 2 is determined using the so-called bank-internal expected downgrade staging model and taking into consideration quantitative and qualitative criteria such as the credit rating of the customer, the intensity of customer handling, the existence of forbearance measures and/or payment defaults. If the significant increase in credit risk no longer applies, the financial instrument is re-transferred to Stage 1. A description of the credit risk methods and systems in place at Aareal Bank AG is presented in the Risk Report as part of the Group Management Report.

Stage 3: This stage includes all financial instruments where there is objective evidence of impairment (impairment trigger or credit impaired). Loss allowances are recognised in the amount of the losses of the lifetime expected credit loss, and interest income is calculated on the basis of the net carrying amount (i.e. gross carrying amount less loss allowance) using the effective interest method. The lifetime expected credit loss in Stage 3 is determined as the difference between the gross carrying amount and the present value of expected future cash flows (discounted using the original effective interest). If the impairment triggers no longer apply, the financial instrument is re-transferred to Stage 1 or 2.

POCI (purchased or originated credit impaired): This category includes all financial instruments that were subject to an impairment trigger at initial recognition. The loss allowance is recorded in the amount of the lifetime expected credit loss.

The expected credit loss is generally determined by Aareal Bank using a model-based procedure where, depending on the stage, one- or multi-year parameters are used. The calculation of the expected loss in Stage 1 and of lifetime expected credit loss in Stage 2 is based on the one-year or lifetime probability of default (PD), respectively, the loss given default (LGD), the expected exposure at default (EAD), a discount factor (DF) and the expected contractual term. Current and expected country-specific economic conditions such as the GDP, long-term interest rates and unemployment rate are included in the LGD by means of a scenario-weighted market value forecast. This probability-weighted scenario mix reflects the uncertainties as to how the Covid-19 pandemic will develop further and supplements our baseline scenario (swoosh) with the addition of divergent developments over an observation period of three years. When accounting for Covid-19-related adjustments to rules set out in loan agreements, we have used as guidelines the recommendations made by the IASB, and by relevant regulatory authorities such as the EBA, the ECB and ESMA – with the objective of providing a realistic assessment of expected losses. As at 31 December 2020, we assume recovery to kick in later (compared to expectations in the third quarter of 2020) due to the pandemic developments. These prospective changes in estimates result in such Covid-19-related liquidity measures no longer being of a temporary nature, but lead to a significant deterioration of credit quality in general. The assumption that no significant decrease in credit quality has occurred is only made in exceptional cases when this is justified based on supportable information.

A period of not more than twelve months is assessed for Stage 1, while the expected contractual term of the financial instrument has to be taken into account for Stages 2 and 3 (and, in addition, the expected term for repayment of the financial instrument in Stage 3).

The expected loss in Stage 3 is usually determined on the basis of individually estimated cash flows (ECF procedure) in three probability-weighted scenarios. The amount of the loss allowance is determined as being the difference between the carrying amount of the asset and the present value of the expected future cash flows, discounted using the original effective interest rate applicable at initial recognition or after the most recent interest rate adjustment in the case of variable-rate financial instruments (taking into account cash flows from realisation of collateral provided). Collateral is largely provided in the form of land charges or mortgages; these are measured at fair value of the respective scenario which is generally based on either the income capitalisation approach or the discounted cash flow method. Impairment triggers are strong indications for a decline of the borrower's credit quality, arrears, external expert opinions as well as further indications that not all interest and principal payments can be made as contractually agreed.

The loss allowance for debt instruments measured at amortised cost is reported in the item "Loss allowance (ac)", for debt instruments measured at fair value through other comprehensive income in the item "Reserve from the measurement of debt instruments (fvoci)" and for loan commitments and financial guarantees under provisions. Debt instruments reported under POCI are accounted for on a net basis, i. e. without any loss allowance. Changes in loss allowance are reflected by increasing or decreasing the carrying amount through other loss allowance.

If the receivables are not recoverable, the corresponding loss allowance is utilised and the receivable is derecognised. Direct write-offs are not made.

The loss allowance for receivables from other transactions is determined using a simplified procedure in the amount of the lifetime expected credit losses.

Hedging relationships

The risk management strategy set out in the Risk Report of the Group Management Report is the basis for the recognition of hedging relationships. At Aareal Bank Group, risks from value fluctuations are hedged in the case of transactions not measured at fair value through profit or loss. In this context, the risks from hedged items are intended to be offset by entering into hedging derivatives where the fair value changes have the opposite direction compared to those of the hedged item. Average prices of the hedges are not relevant for risk management. Hedging relationships are not recorded for transactions that are measured at fair value through profit or loss. The results from economic hedging relationships are offset in net gain or loss from transactions measured at fair value.

Hedge accounting in accordance with IFRS 9 distinguishes various forms of hedging relationships.

Fair value hedges are used to hedge hedged items against fair value changes resulting from changes in interest rates or from changes in interest and exchange rates that are determined accordingly as hedged risk. At Aareal Bank Group, property loans, securities and promissory note loans are typically hedged using interest rate swaps and cross-currency swaps. The derivatives used for hedging are accounted for at fair value through profit or loss. The offsetting fair value changes of the hedged item resulting from the hedged risk are also recognised through profit or loss. The proportion of the fair value changes of the hedged item not attributable to the hedged risk is accounted for in line with the classification of the hedged item. A fully effective hedging relationship results in offsetting measurement results. The hedging relationship may result in adjustments in the carrying amount of the underlying transaction. Such adjustments will only be recognised in income at the end of the transaction term.

Hedges of a net investment in a foreign operation are used to hedge currency risks arising on the translation of the net assets of foreign Group companies. The effective portion of measurement gains or losses from derivative hedging instruments is recognised directly in equity in the currency translation reserve. The ineffective portion of the hedging derivative's fair value changes have to be recognised in the income statement. The gain or loss on the hedging derivative relating to the effective portion of the hedge that has been recognised directly in equity shall be recognised in profit or loss on disposal of the foreign operation. Any translation differences resulting from the translation of an entity with a different functional currency into the Group currency also have to be recognised directly in equity in the currency translation reserve; they will be reclassified to the income statement upon disposal of the foreign operation.

The effectiveness of hedging relationships is reviewed by way of a forward-looking sensitivity analysis regarding the hedged risks. Factors which may lead to ineffectiveness include the term of transactions or payment dates, or diverging market conventions for underlying transactions and related hedges which affect the relevant measurement parameters (e.g. discounting using an OIS rate). Currency basis spreads are accounted for as hedging costs, with fair value changes of this element recognised in other comprehensive income. In the event of any changes to hedging relationships occurring in the course of risk management, the hedge ratio of existing hedges and/or hedged items is adjusted accordingly.

(10) Cash funds

Cash funds include cash on hand and balances with central banks. Cash funds are exclusively allocated to the measurement category "ac".

(11) Loan receivables

The item "Loan receivables" comprises property loans, public-sector loans and other loan receivables, including deferred interest. Loan receivables can be allocated to all measurement categories. At present, they are allocated to the ac and fvpl measurement categories. The portion of loan commitments not disbursed is reported as contingent liabilities.

(12) Money market and capital market receivables

The item "Money market and capital market receivables" comprises money market receivables, promissory note loans and debt securities, including deferred interest. Money market and capital market receivables may generally be allocated to all measurement categories.

(13) Equity instruments

This item includes unconsolidated equity instruments. They are allocated to the measurement category ”fvoci”.

(14) Receivables from other transactions

The item ”Receivables from other transactions” comprises trade receivables and other financial receivables. Receivables from other transactions are exclusively allocated to the measurement category ”ac”.

(15) Positive market value of designated hedging derivatives / Negative market value of designated hedging derivatives

The items ”Positive market value of designated hedging derivatives” and ”Negative market value of designated hedging derivatives” include derivatives with positive or negative market values from fair value hedges, cash flow hedges and hedges of a net investment in a foreign operation, including deferred interest. Derivatives are exclusively allocated to the measurement category ”fvpl”. The basis for the recognition of hedging relationships is described in the chapter ”Recognition and measurement of financial instruments” in this section. Effects from the measurement of these derivatives are reported in the item ”Net gain or loss from hedge accounting”, together with the effects from the measurement of the transactions.

(16) Positive market values of other derivatives / Negative market value of other derivatives

Derivative financial instruments that are not part of recognised hedging relationships are reported in Aareal Bank Group under positive or negative market values of other derivatives. They are mainly used to hedge economic market price risks. Derivatives are exclusively allocated to the measurement category ”fvpl”. Results from the measurement and the termination of the derivatives are reported in the item ”Net gain or loss from financial instruments (fvpl)”. Interest received or paid in connection with these derivatives is also recorded generally in the item ”Net gain or loss from financial instruments (fvpl)”. Interest received or paid for derivatives entered into for hedging purposes which, however, do not meet the hedge accounting criteria, is reported in net interest income. Effects from the measurement of these derivatives are reported in the item ”Net gain or loss from financial instruments (fvpl)”, together with the effects from the measurement of the transactions.

(17) Investments accounted for using the equity method

The item “Investments accounted for using the equity method” includes shares in companies where Aareal Bank Group can exercise significant influence (associates) as well as shares in joint ventures.

Investments in associates included in this item are recognised at cost when the significant influence arises, and subsequently carried at amortised cost whereby, in particular, the share of results of operations of any financial year is recognised in income.

The equity method applied to the major associates was based on the most recent available financial statements.

(18) Intangible assets

The item "Intangible assets" consists of proprietary software, goodwill and other intangible assets such as purchased software and licences.

Intangible assets (except goodwill) are carried at cost, less accumulated amortisation and any impairment losses.

Research costs incurred in connection with software development are expensed as they are incurred. Development costs are capitalised from the time when the software development can be regarded as completed from a technical perspective, and several other conditions are fulfilled. They are amortised on a straight-line basis, using an estimated economic life of generally five years. Purchased software is also deemed to have a limited useful life. Amortisation is recognised in administrative expenses.

Goodwill is defined as the excess of the cost of acquisition over the fair value of the Group's interest in the net assets of an acquired entity, at the time of acquisition (positive difference). Goodwill is carried at historical cost less accumulated impairments. Any negative goodwill arising upon acquisition is immediately recognised in income.

In case the annual impairment test (which must be carried out at least on an annual basis) shows that there are indications of impairment of intangible assets (as set out in IAS 36) and that the recoverable amount is lower than the carrying amount of the asset concerned, the asset is written down through profit or loss, to the estimated recoverable amount.

If it is impossible to estimate the recoverable amount for a specific asset, the recoverable amount of the cash-generating unit that the asset belongs to must be determined. A cash-generating unit is the smallest identifiable group of assets that generates cash inflows that are largely independent of the cash inflows from other assets or groups of assets. Aareal Bank Group defines cash-generating units either on the basis of a single subsidiary or on product level. The recoverable amount of an asset or a cash-generating unit is the higher of fair value less costs to sell and value in use. Value in use is the present value of future cash flows expected to arise from the continuing use of an asset or cash-generating unit. Future cash flows are determined based on medium-term projections. The present value of the future cash flows is determined using discount factors which are in line with the risks involved. Accordingly, the recognition of intangible assets and the impairment test are also subject to estimation uncertainties.

(19) Property and equipment

Property and equipment includes owner-occupied land and buildings as well as office furniture and equipment, and their right-of-use assets. Property and equipment also includes a hotel operated by Aareal Bank. Property and equipment is measured at cost, less accumulated depreciation, impairment losses, and write-downs. Depreciation, impairment losses, and write-downs are reported under administrative expenses, while those of the owner-operated hotel are shown in net other operating income/expenses.

Owner-occupied buildings reported under property and equipment are depreciated on a straight-line basis, over a period of 25 to 50 years. Owner-occupied land is not depreciated. Please refer to the explanations in the Notes on other assets for the accounting method to be applied for land and buildings which are not owner-occupied. Office furniture and equipment items are depreciated using the straight-line method, applying the following periods:

	Depreciation period
Other property and equipment	
IT equipment	3-7 years
Other office furniture and equipment	5-13 years

Tenant improvements are depreciated based on the principles applicable for the relevant building.

For details on recognising impairments as defined in IAS 36, please refer to the explanations in the Note on intangible assets in this section.

Gains and losses upon disposal of property and equipment are recognised in income (in net other operating income/expenses).

The costs to purchase property and equipment in the amount of up to € 250.00 (low-value assets) are expensed as they are incurred.

Any items of property and equipment with a cost of more than € 250.00 net, but not exceeding € 1,000.00, can be combined in a collective account for the year, which is then depreciated on a straight-line basis over a period of five years.

(20) Income tax assets/income tax liabilities

The measurement of uncertain tax positions is made using the best estimate of the expenditure required to settle the obligation (most likely amount). In contrast, measurement is based on the expected value if this helps to achieve a more precise estimate.

(21) Deferred tax assets/deferred tax liabilities

Deferred tax assets are recognised when they are deemed recoverable. The recoverability is assessed using tax planning (internal assessment) on the basis of medium-term Group planning. Accordingly, deferred tax assets are only recognised to the extent that we deem it probable that future taxable profits will be available against which the temporary differences and tax loss carryforwards can be utilised. In this context, the matters underlying the deferred tax items were subjected to a maturity analysis. Deferred taxes are calculated on the basis of country- and company-specific tax rates expected to apply at the time of the realisation of temporary differences and set-off against loss carryforwards.

Deferred tax assets and deferred tax liabilities are offset in accordance with IAS 12.74 when there is a legally enforceable right to set off current tax assets against current tax liabilities and when the deferred tax assets and the deferred tax liabilities relate to income taxes levied by the same taxation authority on either the same taxable entity or tax group.

We generally assume that the deferred tax items are of a long-term nature. The remaining maturity or the time of the expected realisation is long-term when there is more than one year between the reporting date and the maturity date.

(22) Other assets

The item ”Other assets” includes, amongst other things, properties and contract assets. Properties reported under other assets are intended for short-term disposal. They are measured at the lower of cost or net realisable value, in accordance with IAS 2, and therefore are subject to estimation uncertainties.

(23) Money market and capital market liabilities

The item ”Money market and capital market liabilities” comprises money market liabilities, mortgage Pfandbriefe, registered public-sector Pfandbriefe, promissory note loans and other debt securities, including deferred interest. Money market and capital market liabilities are allocated to the measurement category ”ac”.

(24) Deposits from the housing industry

The item ”Deposits from the housing industry” includes deposits payable on demand and term deposits, including deferred interest. Deposits from the housing industry are allocated to the measurement category ”ac”.

(25) Liabilities from other transactions

The item ”Liabilities from other transactions” comprises trade payables and other financial liabilities. Liabilities from other transactions are exclusively allocated to the measurement category ”ac”.

(26) Subordinated liabilities

Subordinated funds raised do not provide for any early repayment obligation. In the event of liquidation or insolvency, claims on interest and principal from these liabilities are subordinated to the claims of all other creditors, which are not subordinated themselves. Subordinated liabilities are allocated to the measurement category ”ac”.

(27) Provisions

The item ”Provisions” comprises provisions for pensions and similar obligations, provisions for staff expenses and non-staff operating costs, provisions for risks related to unrecognised items in the lending business, provisions for legal or tax risks, as well as other provisions. Provisions are recognised when there is a present legal or constructive obligation towards third parties arising from a past event, the outflow of resources to meet this obligation is probable and the amount of the obligation can be reliably estimated. The measurement of provisions is made using the best estimate of the expenditure required to settle the obligation (most likely amount). In the context of acquisitions in accordance with IFRS 3, contingent liabilities were also recognised at their fair value (expected value). These are released when the reasons for their recognition cease to exist.

Measurement is subject to several uncertainties and often requires significant estimates made by the management in relation to various factors that may not apply subsequently. The final amount of the liabilities may deviate significantly from the measurement previously made in accounting. For example, the outcome of individual legal proceedings may not be predicted with certainty.

If utilisation from the obligation is not expected in the short term, i.e. within twelve months, the provision will be recognised at present value.

Provisions for pensions and similar obligations

Aareal Bank Group maintains various pension plans as defined in IAS 19. For the purpose of reporting pension obligations, IAS 19 makes a distinction between defined contribution plans and defined benefit plans.

Under defined contribution plans, an enterprise pays fixed contributions into a separate entity or a fund and will have no legal or constructive obligation to pay further contributions if the fund does not hold sufficient assets to pay all employee benefits relating to employee service in the current and prior periods. Contributions paid to the statutory pension insurance scheme are also classified as defined contribution plans. The contributions paid to a defined contribution plan are recorded as staff expenses.

Defined benefit obligations are all pension obligations that do not meet the criteria of a defined contribution obligation. The amount of obligations usually depends on one or several factors, including age, length of service, and salary.

The Group's obligations under defined benefit plans are recognised as a provision in the consolidated statement of financial position. These are based on general works agreements on an employee pension scheme, individual agreements with executive staff as well as individual agreements concluded with the members of the Company's senior management. Projected economic and demographic developments as well as salary trends must be applied to the calculation of the provisions. Calculating the amount of provisions in the Group is based on actuarial opinions which are prepared by external actuaries on the basis of Aareal Bank-specific and Group-wide standardised parameters.

Provisions for pensions and similar obligations under defined benefit plans are determined in accordance with IAS 19 on the basis of the projected unit credit method; the various defined benefit plans are measured separately. The fair value of the plan assets is deducted from the present value of the pension obligation, taking into account, if applicable, the rules for the asset ceiling in relation to a surplus of plan assets over the benefit obligation. The resulting amount represents the net defined benefit liability (provision) or the net defined benefit asset. Net interest expense in the financial year is determined by applying the discount rate calculated at the beginning of the financial year to the net liability calculated as at that date. The discount rate used to determine the present value of the obligation is based on the capital market rate of high quality corporate bonds with comparable maturities at the reporting date. Determination is based on the GlobalRate:Link method by Willis Towers Watson. The data basis consists of corporate bonds recorded by Bloomberg which have a rating of at least "AA" and are denominated in the same currency as the underlying pension obligation. As a result of market distortions, Bloomberg adjusted the composition of the bonds during the reporting year. This adjustment was also applied by Willis Towers Watson in the derivation of interest as part of the GlobalRate:Link method. Without the transition, the obligation would have been approximately € 37 million higher as at year-end, and other comprehensive income would have been reduced by the same amount. Actuarial gains and losses (remeasurements), which – in connection with the amount of obligations – arise on changes in expectations regarding life expectancy, pension increases, salary development and discount rate compared to the estimation made at the beginning of the period or compared to the actual trend during the period, are recorded in other comprehensive income in the item "Changes in the reserve from remeasurements of defined benefit plans". Actuarial gains and losses (remeasurements) recorded in other comprehensive income may not be reclassified subsequently to profit or loss (recycling). Differences between the expected return on plan assets, determined at the beginning of the period using the then applicable discount rate, and the actual return on plan assets (remeasurement) at the end of the period are also recognised in other comprehensive income. Actuarial gains and losses as well as the difference between expected and actual return on plan assets are included in other reserves. They are reported separately in the statement of changes in equity. Thus, the recognition of pension obligations is based on estimates which are subject to uncertainty.

Share-based payment

Aareal Bank Group maintains share-based payment plans subject to cash settlement in accordance with IFRS 2. We refer to our comments in Note (79) to the consolidated financial statements, which include a detailed description of the plans and their scope as well as information on the valuation model applied and the effects of share-based payments on the Group's financial position and performance.

Provisions for obligations arising from share-based remuneration plans are recognised under administrative expenses, in the amount of the fair value of the relevant obligation as at the reporting date.

(28) Other liabilities

The item "Other liabilities" includes, among other things, contract liabilities, deferred income and liabilities from other taxes.

(29) Equity

The item "Equity" comprises subscribed capital, capital reserves, retained earnings and other reserves. Other reserves include the reserve from remeasurements of defined benefit plans, the reserves from the measurement of equity and debt instrument at fair value through other comprehensive income, the reserve from changes in the value of foreign currency basis spreads and currency translation reserve. In addition, the item "Equity" includes non-controlling interests as well as the so-called Additional Tier 1 bond (AT1 bond). The AT1 bond is classified as equity since there is neither an obligation to repay the bond nor is there an obligation for ongoing debt service (payment of a dividend). The transaction costs directly attributable to the issue of the AT1 bond as well as dividends paid are deducted directly from equity, net of taxes.

(30) Financial guarantee contracts

A financial guarantee contract is a contract that requires the issuer to make specified payments to reimburse the holder for a loss that it incurs because a specified debtor fails to make payment when due. A guarantor recognises a financial guarantee contract as a liability at the date of addition, using the fair value of the guarantee obligation. The obligation is subsequently measured at the greater of the impaired amount and the original amount, less any accumulated amortisation. Within Aareal Bank Group, financial guarantee contracts are presented based on the present value of the claim resulting from the future premium payments of the holder, and offset with the obligation for the guarantee (net basis).

Notes to the Statement of Comprehensive Income

(31) Net interest income

€ mn	1 Jan - 31 Dec 2020	1 Jan - 31 Dec 2019
Interest income from financial assets (ac and fvoci)	674	875
Loan receivables	677	865
Money market and capital market receivables	-3	10
Interest income from financial liabilities (ac)	46	14
Money market and capital market liabilities	31	6
Deposits from the housing industry	15	8
Interest income from financial instruments (fvpl)	34	44
Loan receivables	18	26
Money market and capital market receivables	4	6
Other derivatives	12	12
Market-driven modification gains	0	0
Total interest and similar income	**754**	**933**
Interest expenses from financial liabilities (ac)	57	99
Money market and capital market liabilities	33	73
Deposits from the housing industry	1	1
Liabilities from other transactions	1	2
Subordinated liabilities	22	23
Interest expenses from financial assets (ac)	18	12
Cash funds	15	9
Money market and capital market receivables	3	3
Interest expenses for financial instruments (fvpl)	166	289
Other derivatives	166	289
Market-driven modification losses	1	0
Total interest and similar expenses	**242**	**400**
Total	**512**	**533**

At € 512 million, net interest income was down on the previous year (€ 533 million), mainly due to a decline in the loan and securities portfolios in the course of the year. This was attributable to the previous year's accelerated de-risking involving defaulted loans, a larger exposure to a single borrower and securities in Italy, as well as to lower new business, on account of Covid-19. In line with portfolio growth, net interest income rose again at the end of the year and also includes a pro rata interest benefit from the TLTRO programme.

Within the framework of the ECB's longer-term refinancing operations (TLTROs), Aareal Bank raised funds in the amount of € 4.3 billion in the financial year under review. Apart from the favourable refinancing rate, the ECB grants interest benefits as part of its monetary policy measures when Aareal Bank's net lending volume in the euro area has increased between 31 March 2020 and 31 March 2021. Based on its new business and portfolio planning, Aareal expects to receive these interest benefits. The interest benefit is recognised on a straight-line basis over its reference period as a result of its features. Aareal Bank reports the pro rata interest income of € 11 million within interest income from money market liabilities and expects an interest benefit in the same amount for 2021. The negative base interest rate on the funding transaction is offset by the interest rate bonus.

(32) Loss allowance

€ mn	1 Jan - 31 Dec 2020	1 Jan - 31 Dec 2019
Additions	380	206
Reversals	33	118
Recoveries on loans and advances previously written off	4	3
Loss allowance – other items	–	0
Credit-driven net modification gain or loss	1	5
Total	**344**	**90**

Loss allowance of € 344 million (2019: € 90 million) was recognised, largely due to the adverse economic effects related to the Covid-19 pandemic.

Based on the extended and further tightened global lockdown measures, the Bank has generally classified all loans for which liquidity support measures (payment deferrals and liquidity facilities) were granted as Stage 2 as at 31 December 2020 and recognised loss allowance in the amount of the losses expected for the entire remaining term. The assumption that no significant decrease in credit quality has occurred is only made in exceptional cases when this is justified based on supportable information. Stage 3 loss allowance increased due to new loan defaults; causes for increases with respect of existing exposures included a deterioration of market values, particularly affecting shopping centres in the UK and individual exposures in the US. The scope of current valuation reviews within the portfolio particularly affected by the Covid-19 pandemic (including property types such as retail, hotels, and student housing) for the purpose of year-end valuation covered this portfolio almost completely; external valuations accounted for approximately 85 % of the lending volume. Overall, the valuation reviews were in line with our expectations from the third quarter of 2020, except for a few NPL cases. No management overlay was required by the year-end. Moreover, the accelerated de-risking burdened the loss allowance in the second quarter with € 9 million.

The recognition of loss allowances and the collateral values is based on the expected recovery of our "swoosh" scenario. The scenario is based on the following macro-economic factors:

%	2020	2021	2022	2023
'Swoosh' scenario				
Gross domestic product (year-on-year change in %)				
Euro zone	-7.1	4.2	4.9	2.2
US	-3.5	4.2	3.4	2.0
UK	-10.3	4.5	6.4	2.3
Unemployment (%)				
Euro zone	8.0	9.1	8.4	7.9
US	8.1	6.2	5.2	4.7
UK	6.1	7.4	5.5	4.6
Portfolio-weighted property price development (2020 basis = 100 %)		104.2	107.5	108.2

We expect the market values of commercial properties to remain stable over the next few years. All in all, commercial properties should have reached or overcome the performance low. Considering the assumed recovery, most commercial properties should return to their pre-crisis values in the years to come. With a view to retail properties, we expect the situation to ease more slowly, as the structural change in buying behaviour is having a dampening effect on the outlook of value-driving rental revenues, depending on location and segment. Also depending on location and segment, we see hotel properties recovering in the years to come. As travel activities gradually increase, we expect a recovery at least to pre-crisis levels. We expect a similar development for student housing activities, where demand should pick up thanks to international students. We expect the values of office properties to rise slower compared to the previous year, due to the Covid-19 pandemic. Logistics properties continue to be assessed positively, as we expect the trend of rising market values of these properties to prevail. Individual properties may generally deviate from this estimate, depending on the different regional economic impacts of the Covid-19 pandemic.

The Stage 1 and 2 loss allowances are calculated using the probability of default (PD) and the loss given default (LGD) based on models and largely depends on the market value of the properties. In case of an increase/decrease of the market value by 5 % at year-end, the loss allowance would have decreased/increased by a low double-digit million euro amount. This calculation includes the so-called quantitative stage transfer to Stage 2 based on the so-called expected downgrade model, but does not include qualitative criteria for a significant increase in credit risk.

Please also refer to our explanations in Note (62).

(33) Net commission income

€ mn	1 Jan - 31 Dec 2020	1 Jan - 31 Dec 2019
Commission income from		
ERP products (incl. add-on products)	179	183
Digital solutions	61	51
Banking business and other activities	43	45
Total commission income	**283**	**279**
Commission expenses for		
Purchased services	45	44
Banking business and other activities	4	6
Total commission expenses	**49**	**50**
Total	234	229

Despite Covid-19, net commission income increased to € 234 million (2019: € 229 million) on the back of the higher sales revenue at Aareon and in the Consulting/Services Bank segment.

Commission income from ERP products and digital solutions includes € 21 million of licence revenue (2019: € 22 million) recognised at a point in time. In the reporting period, revenue of € 1 million (2019: € 1 million) was recorded attributable to performance obligations of earlier periods.

The net amount of commission income and commission expenses from financial assets and financial liabilities not measured at fair value amounts to € 10 million (2019: € 13 million).

(34) Net derecognition gain or loss

€ mn	1 Jan - 31 Dec 2020	1 Jan - 31 Dec 2019
Net gain or loss on the derecognition of financial assets (ac)		
Loan receivables	22	32
Money market and capital market receivables	-3	-1
Net gain or loss on the derecognition of financial liabilities (ac)		
Money market and capital market liabilities	7	3
Net gain or loss on the derecognition of financial assets (fvoci)		
Money market and capital market receivables	2	30
Total	**28**	**64**

The net derecognition gain of € 28 million (2019: € 64 million) was attributable to market-driven effects from early loan repayments, and to repurchases in the Treasury business within the scope of market support. The higher figure for the previous year reflected structural adjustments to our securities portfolio following the acquisition of former Düsseldorfer Hypothekenbank AG (Düsselhyp).

(35) Net gain or loss from financial instruments (fvpl)

€ mn	1 Jan - 31 Dec 2020	1 Jan - 31 Dec 2019
Net gain or loss from loan receivables	-35	-14
Net gain or loss from money market and capital market receivables	-3	4
Net gain or loss from other derivatives	4	13
Currency translation	2	-2
Total	**-32**	**1**

The net loss from financial instruments was also burdened by Covid-19, and amounted to € 32 million (2019: profit of € 1 million). The decline was largely due to credit-risk induced measurement losses of defaulted property loans, which are reflected in the net gain or loss from financial instruments (fvpl) as the SPPI criterion is not met.

(36) Net gain or loss from hedge accounting

€ mn	1 Jan - 31 Dec 2020	1 Jan - 31 Dec 2019
Ineffective portion of fair value hedges	6	-4
Ineffective portion of net investment hedges	0	0
Total	**6**	**-4**

(37) Net gain or loss from investments accounted for using the equity method

In the past financial year, there was a net gain from investments accounted for using the equity method of € 1 million (2019: € 1 million); this was also in line with the pro-rata results from joint ventures and associates.

(38) Administrative expenses

€ mn	1 Jan - 31 Dec 2020	1 Jan - 31 Dec 2019
Staff expenses	286	295
Wages and salaries	224	237
Social security contributions	37	35
Pensions	25	23
Other administrative expenses	142	152
Depreciation, amortisation and impairment of property and equipment and intangible assets	41	41
Total	**469**	**488**

Administrative expenses declined to € 469 million (2019: € 488 million) in spite of rising expenses in connection with Aareon's growth, also due to cost savings incurred in connection with the Covid-19 pandemic. The previous year's figure still included running costs and integration expenses in the amount of € 11 million incurred in conjunction with the integration of Düsselhyp.

Staff expenses include contributions to defined contribution plans in the amount of € 16 million (2019: € 15 million).

Other administrative expenses include administrative costs for research and development in relation to existing and new functions and products not eligible for capitalisation in the amount of € 34 million (2019: € 29 million).

This item also includes the total fees charged by the auditor of the consolidated financial statements in the financial year 2020, which consists of the following sub-items:

€ 000's	1 Jan - 31 Dec 2020	1 Jan - 31 Dec 2019
Auditing fees	4,056	3,987
Other assurance services	173	144
Tax advisory services	2	3
Other services	102	356
Total	**4,333**	**4,490**

Other assurance services include the review in accordance with the German Securities Trading Act (WpHG), the bank levy, software confirmations, comfort letters and the review of the separate combined non-financial report. Tax advisory services refer to general tax advice. Other services primarily include regulatory advice.

(39) Net other operating income/expenses

€ mn	1 Jan - 31 Dec 2020	1 Jan - 31 Dec 2019
Income from properties	20	43
Income from the reversal of provisions	11	2
Income from goods and services	0	0
Other operating income	32	23
Total other operating income	**63**	**68**
Expenses for properties	57	40
Expenses for other taxes	6	4
Other operating expenses	11	22
Total other operating expenses	**74**	**66**
Total	**-11**	**2**

Income from properties declined, mainly due to the shutdown of our hotel operations following the Covid-19 pandemic. In addition, a provision from a sale of a property was reversed. Other operating income also includes further non-recurring effects of € 20 million (2019: € 5 million). These non-recurring effects comprise the sale of the operating property of the Rome branch, the transfer of the custody operations and the reversal of a guarantee obligation from a property held by the Bank. Expenses for properties increased due to Covid-19 as a result of write-downs on properties held by the Bank in the amount of € -33 million.

(40) Income taxes

€ mn	1 Jan - 31 Dec 2020	1 Jan - 31 Dec 2019
Current income taxes	-15	76
Deferred taxes	9	9
Total	**-6**	**85**

The capitalisation of deferred taxes had a positive impact on income tax expenses.

The differences between calculated and reported income taxes are presented in the following reconciliation:

€ mn	1 Jan – 31 Dec 2020	1 Jan – 31 Dec 2019
Operating profit (before income taxes)	-75	248
Expected tax rate	31.7 %	31.7 %
Calculated income taxes	**-24**	**79**
Reconciliation to reported income taxes		
Different foreign tax burden	-1	-2
Tax attributable to tax-exempt income	-3	–
Tax attributable to non-deductible expenses	19	24
Remeasurement of deferred taxes	-7	–
Taxes for previous years	9	-16
Other tax effects	1	–
Reported income taxes	**-6**	**85**
Effective tax rate	8 %	34 %

(41) Earnings per share

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

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

Notes to the Statement of Financial Position

(42) Financial assets (ac)

€ mn	31 Dec 2020	31 Dec 2019
Cash funds (ac)	**4,744**	**1,494**
Cash on hand	0	0
Balances with central banks	4,744	1,494
Loan receivables (ac)	**27,277**	**25,783**
Property loans	26,852	25,333
Public-sector loans	360	398
Other loan receivables	65	52
Money market and capital market receivables (ac)	**5,884**	**6,618**
Money market receivables	1,029	1,363
Promissory note loans	1,714	1,823
Bonds	3,141	3,432
Receivables from other transactions (ac)	**94**	**77**
Trade receivables	40	37
Other financial receivables	54	40
Total	**37,999**	**33,972**

(43) Loss allowance (ac)

31 December 2020

€ mn	Stage 1	Stage 2	Stage 3	Receivables from other transactions (ac)	Total loss allowance (ac)
Balance as at 1 January	**22**	**16**	**345**	**3**	**386**
Additions	23	72	279	3	**377**
Utilisation	0	–	129	1	**130**
Reversals	12	9	11	–	**32**
Transfer to Stage 1	0	0	-	–	**–**
Transfer to Stage 2	-14	16	-2	–	**–**
Transfer to Stage 3	0	-17	17	–	**–**
Interest rate effect	–	–	5	–	**5**
Currency adjustments	0	-1	-7	-1	**-9**
Changes in the basis of consolidation	–	–	-5	–	**-5**
Balance as at 31 December	**19**	**77**	**492**	**4**	**592**

The loss allowance for financial assets measured at amortised cost refers to loan receivables, money and capital market receivables as well as receivables from other transactions (largely trade receivables) that are measured at amortised cost.

A detailed breakdown of loss allowance by classes of financial assets is disclosed in Note (62) in the chapter "Notes related to financial instruments".

31 December 2019

€ mn	Stage 1	Stage 2	Stage 3	Receivables from other transactions (ac)	Total loss allowance (ac)
Balance as at 1 January	**34**	**22**	**519**	**2**	**577**
Additions	13	7	184	2	**206**
Utilisation	–	–	237	1	**238**
Reversals	25	15	74	0	**114**
Transfer to Stage 1	1	-1	–	–	**–**
Transfer to Stage 2	-2	7	-5	–	**–**
Transfer to Stage 3	0	-4	4	–	**–**
Interest rate effect	–	–	21	–	**21**
Currency adjustments	1	0	3	0	**4**
Changes in the basis of consolidation	–	–	-70	–	**-70**
Balance as at 31 December	**22**	**16**	**345**	**3**	**386**

(44) Financial assets (fvoci)

€ mn	31 Dec 2020	31 Dec 2019
Money market and capital market receivables (fvoci)	**3,667**	**3,415**
Bonds	3,667	3,415
Equity instruments (fvoci)	**5**	**5**
Equities and other non-fixed income securities	0	0
Other investments	5	5
Total	**3,672**	**3,420**

(45) Financial assets (fvpl)

€ mn	31 Dec 2020	31 Dec 2019
Loan receivables (fvpl)	**856**	**1,050**
Property loans	852	1,050
Other loan receivables	4	–
Money market and capital market receivables (fvpl)	**93**	**135**
Promissory note loans	89	94
Bonds	–	38
Fund units	4	3
Positive market value of designated hedging derivatives (fvpl)	**1,431**	**1,380**
Positive market value of fair value hedges	1,343	1,374
Positive market value of net investment hedges	88	6
Positive market value of other derivatives (fvpl)	**787**	**414**
Positive market value of economic hedging derivatives	578	238
Positive market value of miscellaneous derivatives	209	176
Total	**3,167**	**2,979**

(46) Investments accounted for using the equity method

Aareal Bank holds interests in seven associates (2019: four) and one joint arrangement (2019: one) that are accounted for using the equity method. The sum total of the carrying amounts of the equity investments amounted to € 13 million (2019: € 8 million).

(47) Intangible assets

€ mn	31 Dec 2020	31 Dec 2019
Goodwill	102	89
Proprietary software	55	37
Other intangible assets	50	49
Total	**207**	**175**

Goodwill is entirely attributable to the Consulting/Services Bank and Aareon segments and can be allocated to the following business divisions:

€ mn	31 Dec 2020 Goodwill	31 Dec 2019 Goodwill
Consulting/Services Bank		
Germany	4	4
Aareon		
DACH	48	35
International Business	50	50
Total	**102**	**89**

The increase in goodwill is attributable to the acquisition of CalCon Group.

Goodwill is generally tested for impairment in the fourth quarter of each year. The basis for the valuation is the present value of future cash flows (value in use), which are determined using medium-term projections. In this context, the projected pre-tax cash flows determined on the basis of the three-year plan are used. Accordingly, there is an individual planning of revenue and expense items within the first three years. The parameters underlying the major assumptions are based on internal and external factors as well as on past experience. The major basis is the previous year's planning. Revenue projections are largely subject to assumptions in relation to migration plans, new business, as well as renewals of contracts and follow-up business with existing customers. At the same time, these represent the key sources for estimation uncertainty. Regular sales revenues, such as maintenance and fees from transactions with existing customers, are normally not subject to major estimation uncertainty. The projections for cost of materials are derived from revenue projections. The projections for staff expenses predominantly take into account the number of employees, as well as wage and salary trends. Other costs are projected based on the previous year's figures, taking into account known one-off effects. Estimation uncertainties in relation to costs arise as a result of unplanned price increases or unforeseeable one-off effects. In principle, estimation uncertainty increases if assumptions are made further into the future. Cash flows beyond the four-year horizon are determined by way of a perpetual annuity.

The present values of future cash flows were determined on the basis of a risk-adequate discount factor of 7.62 % for the Aareon segment and of 5.82 % after taxes for the Consulting/Services Bank segment. The discount factor is calculated based on a risk-free basic interest rate of -0.03 % plus a company-specific risk premium of 7.5 %, multiplied with a beta factor of 1.02 for the Aareon segment and of 0.78 for the Consulting/Services Bank segment. Due to the uncertainty surrounding the planning beyond the three-year horizon and our cautious view of the market environment, the growth rate is limited to 2 %. The recoverable amounts show an excess compared to the carrying amounts: even if the above-mentioned material assumptions were to change (such as a 1.0 % increase in the risk-adequate discount factor, a 5.0 % decline in the EBIT included in the cash flow projections, or a decrease in the growth rate to 1 %), this would not result in a specific impairment loss. There was no need to recognise impairment losses in the year under review.

Intangible assets developed as follows:

	2020				2019			
€ mn	Goodwill	Proprietary software	Other intangible assets	Total	Goodwil	Proprietary software	Other intangible assets	Total
Cost								
Balance as at 1 January	**142**	**111**	**119**	**372**	**138**	**106**	**103**	**347**
Additions	–	22	12	**34**	–	11	13	**24**
Transfers	–	2	-8	**-6**	–	–	–	**–**
Disposals	15	1	3	**19**	0	6	2	**8**
Changes in the basis of consolidation	13	–	13	**26**	4	–	5	**9**
Currency translation differences	0	0	–	**–**	0	0	0	**0**
Balance as at 31 December	**140**	**134**	**133**	**407**	**142**	**111**	**119**	**372**
Amortisation and impairment losses								
Balance as at 1 January	**53**	**74**	**70**	**197**	**53**	**74**	**62**	**189**
Amortisation and impairment losses	–	9	18	**27**	–	6	9	**15**
of which: impairment losses	–	–	–	**–**	–	–	–	**–**
Transfers	–	-3	-2	**-5**	–	–	–	**–**
Disposals	15	1	3	**19**	–	6	1	**7**
Currency translation differences	0	0	0	**0**	–	0	0	**0**
Balance as at 31 December	**38**	**79**	**83**	**200**	**53**	**74**	**70**	**197**
Carrying amount as at 1 January	**89**	**37**	**49**	**175**	**85**	**32**	**41**	**158**
Carrying amount as at 31 December	**102**	**55**	**50**	**207**	**89**	**37**	**49**	**175**

(48) Property and equipment

€ mn	31 Dec 2020	31 Dec 2019
Land and buildings and construction in progress	260	277
Office furniture and equipment	29	34
Total	**289**	**311**

The effects of the Covid-19 pandemic required an impairment review as regards our hotel business. No impairments were required in addition to depreciation.

Property and equipment developed as follows:

	2020			2019		
€ mn	Land and buildings and construction in progress	Office furniture and equipment	Total	Land and buildings and construction in progress	Office furniture and equipment	Total
Cost						
Balance as at 1 January	**371**	**87**	**458**	**389**	**82**	**471**
Additions	5	10	**15**	20	11	**31**
Transfers	-3	-1	**-4**	-1	–	**-1**
Disposals	15	6	**21**	37	6	**43**
Changes in the basis of consolidation	4	0	**4**	–	0	**0**
Currency translation differences	-2	0	**-2**	0	0	**0**
Balance as at 31 December	**360**	**90**	**450**	**371**	**87**	**458**
Amortisation and impairment losses						
Balance as at 1 January	**94**	**53**	**147**	**95**	**46**	**141**
Amortisation and impairment losses	17	13	**30**	19	12	**31**
of which: impairment losses	–	–	**–**	–	–	**–**
Write-ups	1	–	**1**	–	–	**–**
Transfers	-2	0	**-2**	1	–	**1**
Disposals	7	5	**12**	21	5	**26**
Changes in the basis of consolidation	–	–	**–**	–	0	**0**
Currency translation differences	-1	0	**-1**	0	0	**0**
Balance as at 31 December	**100**	**61**	**161**	**94**	**53**	**147**
Carrying amount as at 1 January	**277**	**34**	**311**	**230**	**30**	**260**
Carrying amount as at 31 December	**260**	**29**	**289**	**277**	**34**	**311**

(49) Income tax assets

Income tax assets in a total amount of € 116 million as at 31 December 2020 (2019: € 30 million) include € 20 million (2019: € 17 million) expected to be realised after a period of more than twelve months.

(50) Deferred tax assets

When recognising deferred taxes, claims and liabilities arising vis-à-vis the same tax authority, which may be netted and paid in one amount, were offset in the amount of € 405 million (2019: € 495 million).

Deferred tax assets were recognised in relation to the following items of the statement of financial position:

€ mn	31 Dec 2020	31 Dec 2019
Financial assets (ac)	4	53
Financial assets (fvpl)	–	1
Property and equipment	0	2
Other assets	0	0
Financial liabilities (ac)	451	466
Financial liabilities (fvpl)	5	27
Provisions	113	105
Other liabilities	0	0
Tax loss carryforwards	8	9
Deferred tax assets	**581**	**663**

Of the deferred taxes on loss carryforwards, an amount of € 2 million (2019: € 2 million) is attributable to foreign permanent establishments. The existing loss carryforwards may be carried forward for an unlimited period. Deferred taxes on losses carried forward were recognised to the extent that they are expected to be realised within the next five years.

The deferred tax assets not recognised or not subject to valuation adjustments amount to € 80 million (2019: € 82 million).

Deferred tax assets in the amount of € 76 million (2019: € 70 million) were reported under other reserves.

(51) Other assets

€ mn	31 Dec 2020	31 Dec 2019
Properties	326	337
Contract assets	19	25
Miscellaneous	86	98
Total	**431**	**460**

Property holdings increased as a result of the acquisition of a property SPV from an Italian lending exposure.

The effects of the Covid-19 pandemic required a valuation review as regards properties held by the Bank. Write-downs of € 33 million were recognised. In addition, costs for value-enhancing measures were capitalised.

(52) Financial liabilities (ac)

€ mn	31 Dec 2020	31 Dec 2019
Money market and capital market liabilities (ac)	**28,206**	**24,526**
Money market liabilities	8,717	3,566
Promissory note loans	4,077	4,797
Mortgage Pfandbriefe	9,755	10,820
Public-sector Pfandbriefe	1,971	2,585
Other debt securities	3,686	2,758
Other financial liabilities	0	0
Deposits from the housing industry (ac)	**10,592**	**9,744**
Payable on demand	8,426	7,694
Term deposits	2,166	2,050
Liabilities from other transactions (ac)	**86**	**94**
Trade payables	13	20
Other liabilities	73	74
Subordinated liabilities (ac)	**939**	**968**
Total	39,823	35,332

Money-market liabilities increased due to entering into targeted longer-term refinancing operations (TLTROs).

The changes in subordinated liabilities in the amount of € -29 million (2019: € -76 million) consist of € -23 million (2019: € -77 million) related to cash payments of principal as well as an amount of € -6 million (2019: € 1 million) related to non-cash changes in fair value and changes of accrued interest.

(53) Financial liabilities (fvpl)

€ mn	31 Dec 2020	31 Dec 2019
Negative market value of designated hedging derivatives (fvpl)	**1,298**	**1,341**
Negative market value of fair value hedges	1,298	1,327
Negative market value of net investment hedges	–	14
Negative market value of other derivatives (fvpl)	**608**	**824**
Negative market value of economic hedging derivatives	128	422
Negative market value of miscellaneous derivatives	480	402
Total	1,906	2,165

(54) Provisions

€ mn	31 Dec 2020	31 Dec 2019
Provisions for pensions and similar obligations	474	428
Provisions for unrecognised lending business	4	2
Other provisions and contingent liabilities	105	151
Total	**583**	**581**

A detailed breakdown of the provisions for unrecognised lending business by classes of financial assets is disclosed in Note (62) in the chapter "Notes related to financial instruments".

Provisions for pensions and similar obligations

The pension obligations result mainly from retirement benefit plans maintained at Aareal Bank, Aareon, BauGrund and Westdeutsche Immobilien Servicing (former WestImmo), which are classified as defined contribution plans or defined benefit plans in accordance with IAS 19.

Aareal Bank contributed assets held to cover existing pension obligations into a Contractual Trust Arrangement (CTA). This is to ensure improved insolvency protection of the pension claims as a result of the limited protection provided by the German Pension Guarantee Association (Pensionssicherungsverein; PSVaG). For this purpose, a bilateral trust was agreed between Aareal Bank AG (trustor) and Aareal Pensionsverein e.V. as legally independent third party (trustee). The trustee is registered in the Register of Associations at the Wiesbaden District Court.

The trustee holds in trust the special fund for the trustor (administrative trust). Simultaneously, but senior to the administrative trust, the trustee holds the special fund for all beneficiaries on trust to secure the recorded entitlements (security trust).

The security trust is established in the interest of the beneficiaries by way of a genuine agreement for the benefit of third parties (section 328 (1) of the German Civil Code (Bürgerliches Gesetzbuch – "BGB")). On the basis of this security trust, the beneficiaries may request from the trustee that the trustee holds and manages this special fund pursuant to the regulations of this trust agreement for the purpose of securing the recorded entitlements. Upon the occurrence of an insured event, the beneficiaries may, based on the security trust, request from the trustee that the trustee satisfies their recorded entitlements pursuant to the regulations of this trust agreement out of the special fund.

The Bank is the economic beneficiary of the assets. The assets are managed by HSBC INKA in a special fund under German investment law ("Spezialfonds"). Based on an investment guideline, HSBC INKA takes investment decisions for staff pensions. A joint investment committee was established, comprising staff from HSBC INKA and Aareal Bank. The Bank transfers new assets to be invested to Aareal Pensionsverein e.V. on an annual basis, which in turn acquires additional units in the special fund. The fund manager invests interest income during the course of the year.

The Bank has taken out reinsurance policies for a portion of the benefit entitlements of active members of the Management Board and former Management Board members. These policies were also transferred to Aareal Pensionsverein e.V. on a trust basis. The Bank provides corresponding funds for contribution paid to these policies.

Transferring assets to Aareal Pensionsverein e.V. on the one hand secures benefit entitlements and claims under occupational pension schemes, and on the other hand creates plan assets within the meaning of IAS 19 which may be offset with benefit obligations of the trustor.

Brief description of the material pension plans

DePfa Bank Betriebsvereinbarung dated 14 December 1999 (BV 97)

BV 97 applies for new joiners since 1 January 1997. The following benefits are granted after a waiting period of five pensionable service years: old-age pension after completing the 65th year of age (also after any previous disability), early old-age pension, disability pension until completing the 65th year of age, as well as widow(er)'s pension.

The Bank shall grant its employees a basic pension from own contributions and additional benefits in the form of corresponding individual agreements on deferred compensation. The basic pension for the pensionable service period is calculated based on an annual benefit expense of 3.5 % for portions of the pensionable income below the contribution ceiling and 10 % for portions of pensionable income above the contribution ceiling. The employer contributions thus calculated as well as the contributions from deferred compensation are contributed into a CTA at the end of each financial year. The benefit assets, including any allocated surpluses, bear interest at a rate of at least 4 %. The annual benefit payments are calculated based on an annuitisation of the benefit assets upon occurrence of the insured event, using a fixed annuitisation table.

The pensionable service period is deemed to be the period from completing the 20th year of age to completing the 65th year of age. Pensionable income is the gross remuneration received within one year. Any actuarial deductions upon claiming old-age pensions before completing the 65th year of age are taken into account through an annuitisation of the benefit assets. The widow(er)'s pension amounts to 60 % of the employee pension. The Bank increases the current benefit payments annually by 1 %; there is no obligation to provide for an inflation adjustment.

Management Board

The six Management Board members receive their benefits based on individual commitments (a total of eight individual benefit commitments).

Two individual benefit commitments are aligned to fixed annual employer contributions, which are paid to the relevant benefit account and bear interest at a rate of 4 %. In the event of payment of early retirement, disability or death benefits, non-recurring contribution and interest payments are made directly; leading to the level of benefits that would be achieved if the employment relationship would continue until the retirement age on which the awards are based. The benefit assets are translated into a lifelong old-age or disability pension upon the occurrence of an insured event, using actuarial principles. The annuitisation factor was fixed for the time of the retirement age underlying the awards. Annuitisation is based on biometric principles and a notional interest rate of 4 % p.a. and takes into account a pension increase of 2 % p.a. The widow pension amounts to 60 % of the beneficiary's pension entitlement. The current benefit payments are adjusted based on the development of standard wages within the private banking sector.

Six individual benefit commitments are aligned to the fixed annual employer contributions and the amounts from deferred compensation, which are paid to the relevant benefit account and bear interest at a rate of 4 %. In the case of disability or death, the existing benefit assets are increased by the sum total of the amounts that would have been credited in future (up to a maximum contribution period of ten years) for each full calendar year prior to turning 62 or 63. The benefit assets and the assets from deferred compensation are translated into a lifelong old-age or disability pension upon the occurrence of an insured event, using actuarial principles. Annuitisation is based on biometric principles and a notional interest rate of 4 % p.a. and takes into account a guaranteed pension increase of 1 % p. a. The widow pension amounts to 60 % of the beneficiary's pension entitlement. The current benefit payments are increased annually by 1 %; there is no obligation to provide for an inflation adjustment. The old-age pension benefits based on two of these individual commitments were secured through reinsurance policies. These reinsurance policies include benefits in the case of disability or death.

DePfa Bank Dienstvereinbarung dated 30 December 1955 (DePfa 55)

DePfa 55 is a pay-related benefit commitment for new entrants before 31 December 1988. It provides for benefit payments after completing the 65th year of age after a waiting period of five service years and benefits paid in case of occupational incapacity (disability) as well as benefits for surviving dependants, each in form of a monthly annuity.

The amount of the entitlement is based on the following increases: 5% of the last annual salary for the first five service years each, 2 % of the last annual salary for the next 20 service years each, and 1 % of the last annual salary for any following service year, up to a maximum percentage of 75 % of the last annual salary after 35 service years. The widow(er)'s pension amounts to 60 % of the old-age or disability pension. Benefits paid by social security insurance and VBL/Gerling are charged to the benefit entitlements. DePfa 55 does not include any provision allowing for an early payout of old-age pensions or for an adjustment of current benefit payments.

These commitments are based on final salary. The obligation resulting from the respective benefit commitment is therefore very sensitive to unexpected salary changes.

Current benefits are not subject to a fixed adjustment rate; therefore, the adjustment is made pursuant to section 16 of the German Occupational Pensions Act (BetrAVG). Accordingly, an inflation adjustment has to be made every three years given an appropriate economic situation of the Bank. Changes in inflation and, hence, pension increases have an impact on the benefit volume as regards these commitments.

BauBoden agreement dated 1 July 1968 (BauBoden 68)

This agreement applies to employees after completing their 18th year of age who were employed by the Bank on 1 January 1967 or joined the Bank not later than on 31 December 1983. The following benefits are granted after a waiting period of ten service years: old-age pension after completing the 65th year of age, early old-age pension, (total) occupational incapacity pension as well as widow(er)'s pension.

Benefits consist of an overall pension, comprising the statutory pension insurance scheme, the additional pension insurance scheme at VBL or BVV (which is taken into account), or the group insurance contracts and the bank subsidy. The overall pension amounts to 55 % of the pensionable salary after ten years of service. The overall pension is increased by 1 % of the pensionable salary for any further service year, up to the maximum rate of 75 %. The pensionable salary is the last monthly gross salary received during service.

No actuarial deductions are made upon claiming old-age pensions before completing the 65th year of age. The widow(er)'s pension amounts to 60 % of the bank subsidy. The current pension payments are adjusted pursuant to section 16 of the German Occupational Pensions Act (Betriebsrentengesetz; "BetrAVG").

These commitments are based on final salary. The obligation resulting from the respective benefit commitment is therefore very sensitive to unexpected salary changes.

Current benefits are not subject to a fixed adjustment rate; therefore, the adjustment is made pursuant to section 16 of the German Occupational Pensions Act (BetrAVG). Accordingly, an inflation adjustment has to be made every three years given an appropriate economic situation of the Bank. Changes in inflation and, hence, pension increases have an impact on the benefit volume as regards these commitments.

BauBoden agreement dated 12 December 1984 (BauBoden 84) and DePfa Bank Versorgungsordnung dated 28 November 1990 (DePfa 90)

BauBoden 84 applies to employees who joined the Company after 31 December 1983 and have completed their 20th year of age. DePfa 90 applies to employees who joined the Company after 31 December 1988. The following benefits are granted after a waiting period of ten service years: old-age pension and early old-age pension, (total) occupational incapacity pension as well as widow(er)'s pension.

The benefit entitlements of the employees vest after completing their 65th year of age. The amount of the monthly pension entitlement is calculated for each pensionable service year (up to a maximum of 40 service years) as follows: 0.6 % of pensionable salary up to the contribution ceiling, 2 % of the portion of pensionable salary exceeding the contribution ceiling, with pensionable salary and contribution ceiling being calculated using the average for the last twelve months. Benefits paid by BVV are charged to the benefit entitlements under BauBoden 84.

The Bank does not make any actuarial deductions upon claiming early old-age pensions. The widow(er)'s pension amounts to 60 % of the entitlements to benefit payments. The current pension payments are adjusted pursuant to section 16 of the BetrAVG.

These commitments are based on final salary. The obligation resulting from the respective benefit commitment is therefore very sensitive to unexpected salary changes.

Current benefits are not subject to a fixed adjustment rate; therefore, the adjustment is made pursuant to section 16 of the BetrAVG. Accordingly, an inflation adjustment has to be made every three years given an appropriate economic situation of the Bank. Changes in inflation and, hence, pension increases have an impact on the benefit volume as regards these commitments.

AHB – General works agreement on additional pension benefits (company pension scheme) of former Corealcredit

The pension benefits to former employees of Allgemeine Hypothekenbank AG, whose employment relationship began prior to 1 January 1994, are governed by the additional benefit arrangement dated 29 August 1995 on the basis of the complementing general works agreement dated 7 March 1995.

This benefit commitment is based on aggregate benefits derived from pension benefits for civil servants. After a waiting period of five years of service, the aggregate benefit rate is 50 % of pensionable income.

For each year after completing the 37th year of age, the aggregate benefit rate increases by 1 % of pensionable income, up to a maximum 75 % of pensionable income. The entitlement amounts to at least 65 % of pensionable income in the case of (total) occupational incapacity and 75 % of pensionable income in the case of workplace accidents. Pensionable income is the annual income (calculated on the basis of 14 monthly salaries), divided by 12.

The pension benefits of the statutory pension insurance and the BVV, which are based on mandatory contributions, are taken into account in the pension determined as described. To that extent, the benefit obligation directly depends on the development of the level of pensions from the statutory pension insurance on the one hand and from the BVV on the other.

As a result of the German Pension Reform Act of 1992 and the associated cuts in statutory pension insurance, the pension scheme was restructured in 1995. The main pillar of the new structure is the limitation of the Bank's deficiency guarantee for the declining level of statutory pensions due to deduction factors applied at early retirement (Rentenzugangsfaktor) and the lower adjustment of the pension value. Accordingly, the Bank continues to assume the deficiency guarantee on a pro-rata basis for the periods of service until the restructuring on 31 December 1995 in relation to the deduction factors applied at early retirement and for the reduced level of the current pension value (net adjustment factor). The reduction in the level of statutory pensions that occurred during the service periods from the restructuring date until retirement is taken into account at the expense of the beneficiary.

From the start of retirement, the AHB pension is decoupled from the development of the statutory pension and the BVV pension already prior to the restructuring since only the AHB pension is adjusted for inflation on an annual basis.

Accordingly, the obligation for the pension commitment during the qualification period is, on the one hand, directly dependent upon the development of the statutory pension and the BVV pension. On the other hand, it is fully dependent upon salary development for all years of service, even including past service. The volume of the obligation also depends upon the fluctuation of inflation and hence pension increases.

Rheinboden Hypothekenbank AG – pension scheme in the version dated 1 December 1991 of former Corealcredit

The former employees of Rheinboden Hypothekenbank AG are entitled to old-age and disability pensions as well as surviving dependant's benefits in accordance with the pension schemes in the version dated 1 December 1991.

The monthly benefits for employees who commenced service prior to 1 October 1978 amount to 5 % of pensionable remuneration (most recent monthly salary based on collective or individual agreements) after ten service years and increase by 0.5 % of pensionable remuneration for each service year, up to 14 % of pensionable remuneration after 15 service years. The monthly benefit entitlement increases by 0.3 % of pensionable remuneration for any additional service years, up to a maximum of 20 %. The BVV benefits are taken into account in such entitlement to the extent that these are based on employer contributions.

The benefits for employees who commenced service after 30 September 1978 amount to 0.15% of pensionable remuneration up to the contribution ceiling as well as 1.5% of pensionable remuneration above the contribution ceiling for each year of service between the 25th and 65th year of age. The maximum number of recognisable service years is 35.

The old-age pension under the Rheinboden pension schemes is paid after completing the 65th year of age or upon commencement of old-age pension under the statutory pension insurance scheme (full pension). In case of early retirement, the benefits are subject to deductions of 0.3% per month of early retirement prior to the age of 65 as a partial compensation for the additional costs associated with early retirement. The surviving dependant's benefits amount to 60% of the employee's pension entitlement for widow(er)s as well as 15% for half-orphans and 20% for orphans, however, in aggregate not exceeding the amount of the employee's pension entitlement.

Supplementary individual contractual arrangements were agreed with individual pensioners and leavers with vested benefits for the purpose of the transition from the old to the new Rheinboden pension scheme and the application of the BVV benefits.

In addition, individual contractual commitments apply to former management board members and general managers – currently pensioners and one leaver with vested benefits.

The adjustment of current pensions on the basis of the Rheinboden commitments is performed on the basis of the inflation allowance set out in section 16 of the German Occupational Pensions Act (BetrAVG), with the exception of a small group of approximately ten pensioners where adjustment is made pursuant to the collective agreement for banks.

WestImmo – Pension fund rules dated 1 October 1995

The pension fund rules dated 1 October 1995 represent a defined contribution scheme. The following benefits are paid after a waiting period of five year of service: old-age pension, early old-age pension, (total) occupational incapacity pension as well as widow(er)'s and orphan's pension.

The amount of the old-age pension, the early old-age pension and the (total) occupational incapacity pension is calculated based on the sum of the pension components earned during the pensionable service period. If the pensionable service period exceeds 40 years, the monthly pension is calculated based on the sum of the highest 40 pension components earned during the pensionable service period. The amount of one pension component is derived from multiplying the reference contribution (since 2020: € 302), the personal earnings relation (relation between pensionable income and contribution ceiling of the German statutory pension insurance; earnings components above the contribution ceiling are weighted with a factor of 3.75) and the annuitisation factor in the relevant age pursuant to the annuitisation table. The amount of the early old-age pension is reduced by 0.5% for each month in which annuity is paid prior to completing the 65th year of age. The widow(er)'s pension entitlement amounts to 60%.

If necessary, the determination of the amount of pension obligations is based on the following actuarial assumptions applied consistently throughout the Group:

	31 Dec 2020	31 Dec 2019
Calculation method	Projected unit credit method	Projected unit credit method
Calculation basis	Actuarial tables issued by K. Heubeck in 2018	Actuarial tables issued by K. Heubeck in 2018
Actuarial assumptions (in %)		
Interest rate used for valuation	0.74	1.09
Development of salaries	2.00	2.00
Pension increase	1.49	1.53
Rate of inflation	1.75	1.75
Staff turnover rate	3.00	3.00

Development of net pension liabilities:

€ mn	Present value of pension obligations	Fair value of plan assets	Net pension liability
Balance as at 1 January 2020	**526**	**-98**	**428**
Pension expense	**19**	**-1**	**18**
Current service cost	14	–	14
Net interest cost	5	-1	4
Payments	**-9**	**-6**	**-15**
Pension benefits paid	-13	1	-12
Employer's contributions	–	-3	-3
Contributions made by beneficiaries of defined benefit plans	4	-4	0
Remeasurements	**44**	**-1**	**43**
due to experience adjustments	4	–	4
due to changes in financial assumptions	40	–	40
due to changes in demographic assumptions	0	–	0
Difference between actual return and return calculated using an internal rate of interest (plan assets)	–	-1	-1
Balance as at 31 December 2020	**580**	**-106**	**474**

€ mn	Present value of pension obligations	Fair value of plan assets	Net pension liability
Balance as at 1 January 2019	**448**	**-86**	**362**
Pension expense	**20**	**-1**	**19**
Current service cost	12	–	12
Net interest cost	8	-1	7
Payments	**-8**	**-7**	**-15**
Pension benefits paid	-12	1	-11
Employer's contributions	–	-4	-4
Contributions made by beneficiaries of defined benefit plans	4	-4	0
Remeasurements	**66**	**-4**	**62**
due to experience adjustments	0	–	0
due to changes in financial assumptions	66	–	66
due to changes in demographic assumptions	0	–	0
Difference between actual return and return calculated using an internal rate of interest (plan assets)	–	-4	-4
Balance as at 31 December 2019	**526**	**-98**	**428**

The weighted duration of pension liabilities is 20.1 years as at 31 December 2020 (2019: 19.8 years).

Expected maturities of the defined benefit obligation (DBO):

€ mn	31 Dec 2020	31 Dec 2019
Up to 1 year	14	13
Between 1 year and 5 years	60	58
Between 5 years and 10 years	86	83
Total	**160**	**154**

Contributions in the amount of € 16 million are expected to be paid in the financial year 2021 (2020: € 14 million).

Sensitivity of the defined benefit obligation (DBO) compared to the central actuarial assumptions

Based on the qualitative plan description, the valuation parameters significant for calculating the amount of the obligation were derived and corresponding calculations were made as regards sensitivity:

		Defined benefit obligation 2020	Change	Defined benefit obligation 2019	Change
		€ mn	%	€ mn	%
Present value of obligations		**580**		**526**	
Interest rate used for valuation	Increase by 1.0 percentage points	478	-17	436	-17
	Decrease by 1.0 percentage points	714	23	644	23
Development of salaries	Increase by 0.5 percentage points	591	2	536	2
	Decrease by 0.5 percentage points	569	-2	515	-2
Pension increase	Increase by 0.25 percentage points	588	2	533	2
	Decrease by 0.25 percentage points	571	-1	517	-2
Life expectancy	Increase by 1 year	611	6	553	5
	Decrease by 1 year	547	-6	497	-5

The sensitivity analysis takes into account, in each case, the change of an assumption, while the other assumptions remain unchanged compared to the original calculation, i.e. any potential correlation effects between the individual assumptions are not taken into consideration.

Plan assets can be broken down as follows:

	31 Dec 2020	31 Dec 2019
€ mn		
Cash	0	0
Investment funds	73	68
Reinsurance	33	30
Total	**106**	**98**

Apart from the usual actuarial risks, the risks associated with defined benefit obligations primarily relate to financial risks in connection with plan assets. Amongst others, these may include counterparty credit risks and market price risks. These risks are taken into account in the risk management of Aareal Bank Group. The measurement of investment funds has to be allocated to Level 2 of the fair value hierarchy.

Other provisions

Other provisions developed as follows:

€ mn	Provisions for staff expenses and non-staff operating costs	Provisions for legal and tax risks	Other provisions	Total
Carrying amount as at 1 Jan 2020	**118**	**9**	**24**	**151**
Additions	42	0	3	**45**
Utilisation	47	0	9	**56**
Reversals	21	6	4	**31**
Interest	0	–	0	**0**
Reclassifications	-1	-1	0	**-2**
Changes in the basis of consolidation	–	–	0	**0**
Exchange rate fluctuations	-2	–	0	**-2**
Carrying amount as at 31 Dec 2020	**89**	**2**	**14**	**105**

€ mn	Provisions for staff expenses and non-staff operating costs	Provisions for legal and tax risks	Other provisions	Total
Carrying amount as at 1 Jan 2019	**128**	**10**	**14**	**152**
Additions	54	1	14	**69**
Utilisation	52	1	6	**59**
Reversals	8	1	5	**14**
Interest	0	0	0	**0**
Reclassifications	-4	–	0	**-4**
Changes in the basis of consolidation	0	0	7	**7**
Exchange rate fluctuations	0	–	0	**0**
Carrying amount as at 31 Dec 2019	**118**	**9**	**24**	**151**

Other provisions of € 105 million include € 21 million expected to be realised after a period exceeding twelve months (2019: € 27 million).

Provisions for staff expenses and non-staff operating costs refer to personnel provisions in the amount of € 65 million (2019: € 94 million) and provisions for non-staff operating costs in the amount of € 24 million (2019: € 24 million). Personnel provisions consist of, among other things, provisions for bonuses (cash and share-based), partial retirement, severance pay and existing working hours accounts; Provisions for staff expenses include € 8 million in provisions for severance pay and for partial retirement (2019: € 20 million). Provisions for non-staff operating expenses mainly include provisions for professional and legal advice.

(55) Income tax liabilities

Income tax liabilities in a total amount of € 20 million as at 31 December 2020 (2019: € 44 million) include € 7 million (2019: € 12 million) expected to be realised after a period of more than twelve months.

(56) Deferred tax liabilities

When recognising deferred taxes, claims and liabilities arising vis-à-vis the same tax authority, which may be netted and paid in one amount, were offset in the amount of € 405 million (2019: € 495 million).

Deferred tax liabilities were recognised in relation to the following items of the statement of financial position:

€ mn	31 Dec 2020	31 Dec 2019
Financial assets (ac)	368	429
Financial assets (fvoci)	43	54
Financial assets (fvpl)	7	9
Intangible assets	12	12
Property and equipment	8	6
Other assets	2	4
Provisions	–	0
Other liabilities	0	0
Deferred tax liabilities	**441**	**514**

(57) Other liabilities

€ mn	31 Dec 2020	31 Dec 2019
Lease liabilities	82	84
Deferred income	1	1
Liabilities from other taxes	35	35
Contract liabilities	20	15
Miscellaneous	5	0
Total	**143**	**135**

An amount of € 14 million (2019: € 10 million) of the contract liabilities was recorded in profit or loss in the current reporting period.

(58) Equity

€ mn	31 Dec 2020	31 Dec 2019
Subscribed capital	180	180
Capital reserves	721	721
Retained earnings	1,902	1,812
AT1 bond	300	300
Other reserves		
Reserve from remeasurements of defined benefit plans	-166	-141
Reserve from the measurement of equity instruments (fvoci)	-4	-4
Reserve from the measurement of debt instruments (fvoci)	12	7
Reserve from foreign currency basis spreads	-26	-15
Currency translation reserves	-13	-1
Non-controlling interests	61	2
Total	**2,967**	**2,861**

The sale of a 30 per cent minority stake in Aareon to Advent was completed on 31 October 2020. The financial terms of the disposal are based on an enterprise value for Aareon of approximately € 960 million. This corresponds to an equity value of approximately € 860 million, leading to a purchase price for the 30 per cent stake of € 258 million, which was paid in cash. The sales proceeds (excluding transaction costs and taxes) were recognised directly in equity, increasing retained earnings; non-controlling interests now also include Advent's stake. Retained earnings also increased due to the fact that no dividend was paid for the previous year.

The item "Reserve from the measurement of debt instruments (fvoci)" includes loss allowance of € 0 million (2019: € 0 million).

Subscribed capital

Aareal Bank AG's subscribed capital amounted to € 180 million as at the reporting date (2019: € 180 million). It is divided into 59,857,221 notional fully-paid no-par value shares ("unit shares") with a notional value of € 3 per share. The shares are bearer shares. Each share carries one vote. There are no pre-emptive rights or constraints with respect to dividend payouts.

Treasury shares

The General Meeting authorised the Management Board by way of a resolution dated 27 May 2020, pursuant to section 71 (1) no. 7 of the German Stock Corporation Act (Aktiengesetz – "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 purchase or prior to assuming a purchase obligation by more than 10%. This authorisation expires on 26 May 2025. 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 given day.

Furthermore, the Management Board was authorised by means of a resolution of the General Meeting held on 27 May 2020, pursuant to section 71 (1) no. 8 of the AktG, to purchase treasury shares in a volume of up to 10 % of the share capital for any permitted purposes. This authorisation expires on 26 May 2025. Shares may be acquired via the stock exchange or by means of a public offer to buy directed at all shareholders, and at purchase prices stipulated in the authorisation and based on the prevailing market price of the Company's shares. This authorisation may be exercised – also by the direct or indirect subsidiaries of Aareal Bank AG – in full or in part, on one or more occasions.

The shares acquired in accordance with this or an earlier authorisation may be sold, subject to Supervisory Board approval, outside the stock exchange and without an offer directed at all shareholders, subject to the exclusion of shareholders' pre-emptive rights, when the shares sold do not exceed 10 % of the share capital and the issue price is not significantly below the prevailing stock exchange price or in the event of a sale against contributions in kind, or when the shares sold are used to service rights from convertible bonds or bonds with warrants. This also applies to shares issued by subsidiaries. The treasury shares may also be given to the holders of conversion or option rights in lieu of new shares from a contingent capital increase. The shares can also be withdrawn, without such a withdrawal or its implementation requiring a further resolution by the General Meeting.

The Management Board was also authorised to effect the acquisition of treasury shares by using put or call options. Any acquisition of shares using derivatives is limited to 5 % of share capital. In addition, any acquisition of shares shall count towards the 10 % threshold for the authorisation for the acquisition of treasury shares. Where treasury shares are acquired using equity derivatives, the shareholders' right to enter into any option transactions with the Company is excluded in analogous application of section 186 (3) sentence 4 of the AktG.

Authorised capital

Aareal Bank has authorised capital pursuant to the resolution by the Annual General Meeting held on 31 May 2017. 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 2017) by issuance of new no-par value bearer shares for contribution in cash or in kind, subject to the approval of the Supervisory Board; this authority will expire on 30 May 2022. 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 203 (1) and (2) and section 186 (3) sentence 4 of the AktG, shall not exceed 10 % of the issued share capital at the time said authorisation comes into effect or – if lower – at the time it 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 10 % of the issued 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.

e) in the event of a capital increase against contributions in kind for the purpose of acquiring companies, divisions of companies or interests in companies or other assets.

The above authorisation for the exclusion of shareholders' subscription rights in the case of capital increases against contributions in cash or in kind is limited to a total of 20 % of the share capital; this limit may be exceeded neither at the time said authorisation comes into effect, nor at the time it is exercised. The above-mentioned 20 % threshold shall furthermore include treasury shares which are sold to the exclusion of shareholders' subscription rights during the validity of this authorisation as well as such shares which are issued to service debt securities, provided that the debt securities were issued to the exclusion of shareholders' subscription rights during the validity of this authorisation due to the authorisation under agenda item 6 of the Annual General Meeting on 21 May 2014. When a new authorisation for the exclusion of shareholders' subscription rights is resolved after the reduction and said new authorisation comes into effect, the upper limit, reduced in accordance with the above-mentioned requirements, shall be increased again to the amount permitted by the new authorisation, with a maximum total of 20 % of the share capital in accordance with the above-mentioned requirements.

The authorised capital has not yet been utilised.

Conditional capital

Based on a resolution passed by the General Meeting on 22 May 2019, the Management Board was authorised to issue, on one or more occasions until 21 May 2024, profit-participation certificates with a limited or unlimited term for contribution in cash or in kind of up to € 900,000,000. The profit-participation certificates must be constructed in such a way that the funds paid for them after issuance can be recognised as banking regulatory capital pursuant to the legal regulations applicable as at the time of issuance. Profit-participation certificates and other hybrid promissory note loans to be issued according to this authorisation shall be connected with conversion rights, entitling or compelling, in accordance with their respective conditions, the holder to purchase Company shares. Conversion rights or obligations may be attached exclusively to bearer no-par value shares and are limited to a maximum amount of € 71,828,664.00 of the Company's share capital. The sum of shares to be issued so as to service conversion or option rights or conversion obligations from profit-participation certificates or hybrid promissory note loans issued pursuant to this authorisation, including shares issued during validity of this authorisation as a result of another authorisation (especially from the Authorised Capital 2017), may not exceed an amount of € 71,828,664.00 (which equals approx. 40 % of the current share capital). Subject to the approval of the Supervisory Board, the Management Board may exclude shareholders' pre-emptive rights in relation to the profit-participation rights in certain cases.

Accordingly, the Company's share capital is subject to a conditional capital increase not exceeding € 71,828,664.00 by issuance of up to 23,942,888 new no-par value bearer shares ("Conditional Capital 2019"). The purpose of the conditional capital increase is to grant shares to holders or creditors of convertible bonds issued in accordance with the aforementioned authorisation. The new no-par value bearer shares may only be issued at a conversion price in line with the resolution passed by the General Meeting on 22 May 2019. The conditional capital increase shall only be carried out insofar as conversion rights are exercised or as conversion obligations from such convertible bonds are fulfilled or as the Company makes use of alternative performance and insofar as no cash compensation is granted or treasury shares are used to service the rights. The new shares shall 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 rights or the fulfilment of conversion obligations The Management Board is authorised to determine the details of the conditional capital increase. The Management Board is also authorised to determine the further contents of share rights and the terms governing the issuance of shares, subject to the approval of the Supervisory Board.

To date, the Conditional Capital has not yet been utilised.

Capital reserves

The capital reserves contain premiums received upon the issuance of shares. Costs incurred within the framework of a capital increase reduce capital reserves.

Retained earnings

Retained earnings are comprised of statutory reserves (pursuant to section 150 of the AktG) of € 5 million (2019: € 5 million) and of other retained earnings of € 1,897 million (2019: € 1,807 million).

Additional Tier 1 bond (AT1 bond)

On 13 November 2014, the Management Board issued notes in an aggregate nominal amount of € 300 million with a denomination of € 200,000 and an initial interest rate of 7.625 %, based on the authorisation granted by the Annual General Meeting on 21 May 2014.

The notes bear interest of 7.625 % p.a. from the interest commencement date to 30 April 2020. The rate of interest for any interest period commencing on or after 30 April 2020 shall be equal to the reference rate (one-year EUR swap rate) determined on the relevant interest determination date plus a margin of 7.18 % p.a.

The notes constitute unsecured and subordinated obligations of the issuer.

Upon the occurrence of a trigger event, the redemption amount and the principal amount of each note shall be reduced by the amount of the relevant write-down. The write-down shall be effected pro rata with all other Additional Tier 1 instruments within the meaning of the CRR, the terms of which provide for a write-down upon the occurrence of the trigger event. A trigger event occurs if the Common Equity Tier 1 capital ratio, pursuant to Article 92 (1) (a) CRR or a successor provision, and determined on a consolidated basis, falls below 7.0 %. After a write-down has been effected, the principal amount and the redemption amount of each note, unless previously redeemed or repurchased and cancelled, may be written up in each of the financial years of the issuer subsequent to such write-down until the full initial principal amount has been reached.

The notes may be redeemed, in whole but not in part, at any time at the option of the issuer, subject to the prior consent of the competent supervisory authority, upon not less than 30 and not more than 60 days' prior notice of redemption at their redemption amount (taking into account a potential write-down) together with interest accrued until the redemption date (to the extent that interest payment is not cancelled or ruled out in accordance with the terms and conditions of the notes), when the tax or regulatory reasons set out in the terms and conditions of the notes apply. The issuer may also redeem the notes, in whole but not in part, at any time, subject to the prior consent of the competent supervisory authority, upon not less than 30 days' notice of redemption with effect as at 30 April 2020 for the first time and, thereafter, with effect as at each interest payment date at their redemption amount together with interest (if any) accrued to the redemption date.

Distributions

Aareal Bank intends to pay a dividend in a total amount of € 1.50 per share in 2021 for the financial year 2020. This is subject to the relevant supervisory and regulatory requirements. The payout would need to be made in two steps.

In compliance with the requirements published by the European Central Bank (ECB) on 15 December 2020, the Management Board proposes to the Annual General Meeting on 18 May 2021 that the net retained profit of € 89,785,831.50 for the financial year 2020, as reported under the German Commercial Code (HGB), be used to distribute a dividend of € 0.40 per share (€ 23,942,888.40 in total) and to transfer the remaining amount (€ 65,842,943.10) to profits carried forward. Depending on further economic developments, regulatory requirements, the Bank's capital position and its risk situation, a subsequent Annual General Meeting, which could possibly take place during the fourth quarter of 2021, could then decide on the distribution of the profit initially carried forward as a dividend of € 1.10 per share.

No dividends were distributed in 2020. The Annual General Meeting of Aareal Bank AG held on 27 May 2020 resolved that Aareal Bank AG's net retained profit of € 119,714,442.00 for the financial year 2019, as reported under the German Commercial Code (HGB), be transferred in full to other retained earnings.

Previously, following a request issued by the European Central Bank, dated 27 March 2020, to refrain from paying out any dividends at least until 1 October 2020 due to the Covid-19 pandemic, having conducted a detailed review – and diverging from the proposal for the appropriation of profits as published in the financial statements 2019 – the Management Board and the Supervisory Board resolved to propose to the Annual General Meeting that no dividends be distributed for the 2019 financial year, as an exceptional measure to strengthen the Bank's capital base, and that net retained profit be transferred in full to other retained earnings. On 28 July 2020, the ECB extended its request until 1 January 2021.

In addition, on 30 April 2021, the Management Board will resolve on a distribution in relation to the AT1 instruments, pursuant to the terms and conditions of the notes.

Notes to Financial Instruments

A detailed description of the system in place at Aareal Bank Group to measure, limit, and manage risks throughout Aareal Bank Group is presented in the Risk Report as part of the Group Management Report. The disclosures on the description and the extent of the risks arising from financial instruments in accordance with IFRS 7 are included (in part) in the Risk Report.

(59) Net gains/losses of financial instruments by category

The following overview shows the net gains or net losses from financial instruments in accordance with the classification and measurement categories of financial assets and liabilities (from which the results are generated):

€ mn	1 Jan - 31 Dec 2020	1 Jan - 31 Dec 2019
Net gain or loss from financial assets (ac)	-322	-63
Net gain or loss from financial liabilities (ac)	7	4
Net gain or loss from financial assets (fvoci) recognised in other comprehensive income	9	-16
Net gain or loss from financial assets (fvoci) transferred to the income statement	2	30
Net gain or loss from equity instruments (fvoci)	0	-4
Net gain or loss from financial instruments (fvpl)	-32	1
Net gain or loss from financial guarantee contracts and loan commitments	-2	3

The net results include measurement gains and losses, realised gains/losses on disposal, subsequent recoveries on loans and advances previously written off in relation to all financial instruments of the respective measurement category. The net gain or loss from financial instruments (fvpl) also comprises the net gain or loss from currency translation.

The hedge result from hedged items is aggregated with the hedge result from derivative hedging instruments in one line item and amounted to € 6 million (2019: € -4 million) in the year under review. Moreover, the change in the reserve from foreign-currency basis spreads amounted to € -16 million (2019: € -9 million).

(60) Fair value hierarchy in accordance with IFRS 13

The carrying amounts of financial instruments held by Aareal Bank Group which are reported at fair value in the statement of financial position are presented in the following table according to the three-tier fair value hierarchy pursuant to IFRS 13.72 et seq. The presentation is made for each class of financial instrument.

31 December 2020

€ mn	Total fair value	Fair value level 1	Fair value level 2	Fair value level 3
Financial assets (fvoci)	**3,672**	**3,667**	**3**	**2**
Money market and capital market receivables (fvoci)	3,667	3,667	–	–
Equity instruments (fvoci)	5	–	3	2
Financial assets (fvpl)	**3,167**	**0**	**2,307**	**860**
Loan receivables (fvpl)	856	–	–	856
Money market and capital market receivables (fvpl)	93	0	89	4
Positive market value of designated hedging derivatives (fvpl)	1,431	–	1,431	–
Positive market value of other derivatives (fvpl)	787	–	787	–
Financial liabilities (fvpl)	**1,906**	**–**	**1,906**	**–**
Negative market value of designated hedging derivatives (fvpl)	1,298	–	1,298	–
Negative market value of other derivatives (fvpl)	608	–	608	–

31 December 2019

€ mn	Total fair value	Fair value level 1	Fair value level 2	Fair value level 3
Financial assets (fvoci)	**3,420**	**3,415**	**3**	**2**
Money market and capital market receivables (fvoci)	3,415	3,415	–	–
Equity instruments (fvoci)	5	–	3	2
Financial assets (fvpl)	**2,979**	**0**	**1,926**	**1,053**
Loan receivables (fvpl)	1,050	–	–	1,050
Money market and capital market receivables (fvpl)	135	0	132	3
Positive market value of designated hedging derivatives (fvpl)	1,380	–	1,380	–
Positive market value of other derivatives (fvpl)	414	–	414	–
Financial liabilities (fvpl)	**2,165**	**0**	**2,165**	**–**
Negative market value of designated hedging derivatives (fvpl)	1,341	–	1,341	–
Negative market value of other derivatives (fvpl)	824	0	824	–

The fair values of loan receivables recognised at fair value in the statement of financial position that are assigned to Level 3 of the fair value hierarchy developed as follows during the period under review:

Loan receivables (fvpl)

€ mn	2020	2019
Fair value as at 1 January	**1,050**	**711**
Change in measurement	**-36**	**-18**
Portfolio changes		
Additions	175	924
Derecognition	333	567
Deferred interest	0	0
Fair value as at 31 December	**856**	**1,050**

Receivables held in the Bank's portfolio contributed € -21 million to the net gain or loss from loan receivables (fvpl) (2019: € -18 million).

Regarding loan receivables (fvpl), the add-ons for risks specific to the counterparty represent the material input parameter not observable in the market. Regarding the non-defaulted loans, an increase/decrease by 1 % would lead to a decrease/increase of the fair value by approximately € 22 million (2019: approximately € 31 million).

The fair values of financial instruments held by Aareal Bank Group which are reported at amortised cost in the statement of financial position are presented in the following table according to the three-tier fair value hierarchy pursuant to IFRS 13.72 et seq. The presentation is made for each class of financial instrument:

31 December 2020

€ mn	Total fair value	Fair value level 1	Fair value level 2	Fair value level 3
Financial assets (ac)	**37,655**	**2,827**	**7,813**	**27,015**
Cash funds (ac)	4,744	–	4,744	–
Loan receivables (ac)	26,952	–	1	26,951
Money market and capital market receivables (ac)	5,869	2,827	3,041	1
Receivables from other transactions (ac)	90	–	27	63
Financial liabilities (ac)	**40,033**	**1,855**	**38,064**	**114**
Money market and capital market liabilities (ac)	28,371	1,545	26,798	28
Deposits from the housing industry (ac)	10,592	–	10,592	–
Liabilities from other transactions (ac)	86	–	0	86
Subordinated liabilities (ac)	984	310	674	–

31 December 2019

€ mn	Total fair value	Fair value level 1	Fair value level 2	Fair value level 3
Financial assets (ac)	**33,899**	**3,059**	**4,951**	**25,889**
Cash funds (ac)	1,494	–	1,494	–
Loan receivables (ac)	25,850	–	2	25,848
Money market and capital market receivables (ac)	6,481	3,059	3,422	–
Receivables from other transactions (ac)	74	–	33	41
Financial liabilities (ac)	**35,477**	**1,854**	**33,486**	**137**
Money market and capital market liabilities (ac)	24,610	1,533	23,034	43
Deposits from the housing industry (ac)	9,744	–	9,744	–
Liabilities from other transactions (ac)	94	–	0	94
Subordinated liabilities (ac)	1,029	321	708	–

(61) Comparison of carrying amounts and fair values of financial instruments

The fair values of financial instruments are compared with their carrying amounts (including loss allowance) in the following table. The presentation is made for each class of financial instrument:

€ mn	31 Dec 2020 Carrying amount	31 Dec 2020 Fair value	31 Dec 2019 Carrying amount	31 Dec 2019 Fair value
Financial assets (ac)	**37,407**	**37,655**	**33,586**	**33,899**
Cash funds (ac)	4,744	4,744	1,494	1,494
Loan receivables (ac)	26,695	26,952	25,403	25,850
Money market and capital market receivables (ac)	5,879	5,869	6,615	6,481
Receivables from other transactions (ac)	89	90	74	74
Financial assets (fvoci)	**3,672**	**3,672**	**3,420**	**3,420**
Money market and capital market receivables (fvoci)	3,667	3,667	3,415	3,415
Equity instruments (fvoci)	5	5	5	5
Financial assets (fvpl)	**3,167**	**3,167**	**2,979**	**2,979**
Loan receivables (fvpl)	856	856	1,050	1,050
Money market and capital market receivables (fvpl)	93	93	135	135
Positive market value of designated hedging derivatives (fvpl)	1,431	1,431	1,380	1,380
Positive market value of other derivatives (fvpl)	787	787	414	414

>

€ mn	31 Dec 2020 Carrying amount	31 Dec 2020 Fair value	31 Dec 2019 Carrying amount	31 Dec 2019 Fair value
Financial liabilities (ac)	**39,823**	**40,033**	**35,332**	**35,477**
Money market and capital market liabilities (ac)	28,206	28,371	24,526	24,610
Deposits from the housing industry (ac)	10,592	10,592	9,744	9,744
Liabilities from other transactions (ac)	86	86	94	94
Subordinated liabilities (ac)	939	984	968	1,029
Financial liabilities (fvpl)	**1,906**	**1,906**	**2,165**	**2,165**
Negative market value of designated hedging derivatives (fvpl)	1,298	1,298	1,341	1,341
Negative market value of other derivatives (fvpl)	608	608	824	824

(62) Disclosures on credit risk

For information on risk management practice and input factors, please refer to the chapter "Credit default risk" in the Risk Report included in the Management Report.

The following overviews present the loss allowance and the provisions for credit risks per stage and separately by product groups.

Loss allowance (ac)

2020

€ mn	Balance as at 1 January	Additions	Utilisation	Reversals	Transfer to Stage 1	Transfer to Stage 2	Transfer to Stage 2	Interest effect	Currency adjustment	Changes in the basis of consolidation	Balance as at 31 December
Stage 1	**22**	**23**	**0**	**12**	**0**	**-14**	**0**	**–**	**0**	**–**	**19**
Loan receivables (ac)	21	23	0	12	0	-14	0	–	0	–	18
Money market and capital market receivables (ac)	1	0	–	0	0	0	–	–	0	–	1
Stage 2	**16**	**72**	**–**	**9**	**0**	**16**	**-17**	**–**	**-1**	**–**	**77**
Loan receivables (ac)	14	69	–	9	0	15	-17	–	-1	–	71
Money market and capital market receivables (ac)	2	3	–	0	0	1	–	–	–	–	6
Stage 3	**345**	**279**	**129**	**11**	**–**	**-2**	**17**	**5**	**-7**	**-5**	**492**
Loan receivables (ac)	345	279	129	11	–	-2	17	5	-7	-5	492
Receivables from other transactions	**3**	**3**	**1**	**0**	**–**	**–**	**–**	**–**	**-1**	**–**	**4**
Total	386	377	130	32	–	–	–	5	-9	-5	592

2019

€ mn	Balance as at 1 January	Additions	Utilisation	Reversals	Transfer to Stage 1	Transfer to Stage 2	Transfer to Stage 3	Interest effect	Currency adjustment	Changes in the basis of consolidation	Balance as at 31 December
Stage 1	**34**	**13**	**–**	**25**	**1**	**-2**	**0**	**–**	**1**	**–**	**22**
Loan receivables (ac)	33	12	–	24	1	-2	0	–	1	–	21
Money market and capital market receivables (ac)	1	1	–	1	0	–	–	–	0	–	1
Stage 2	**22**	**7**	**–**	**15**	**-1**	**7**	**-4**	**–**	**0**	**–**	**16**
Loan receivables (ac)	12	7	–	7	-1	7	-4	–	0	–	14
Money market and capital market receivables (ac)	10	–	–	8	0	–	–	–	–	–	2
Stage 3	**519**	**184**	**237**	**74**	**0**	**-5**	**4**	**21**	**3**	**-70**	**345**
Loan receivables (ac)	519	184	237	74	0	-5	4	21	3	-70	345
Receivables from other transactions	**2**	**2**	**1**	**0**	**–**	**–**	**–**	**–**	**0**	**–**	**3**
Total	577	206	238	114	–	–	–	21	4	–70	386

The loss allowance for financial assets (ac) is reported in the item "Loss allowance (ac)" on the assets side of the statement of financial position.

Loss allowance in the reserve from the measurement of debt instruments (fvoci)

The loss allowance for debt instrument (fvoci) amounts to € 0 million (2019: € 0 million) and is reported on the equity and liabilities side of the statement of financial position under other reserves.

Provisions for unrecognised lending business

2020

€ mn	Provisions as at 1 January	Additions	Utilisation	Reversals	Transfer to Stage 1	Transfer to Stage 2	Transfer to Stage 3	Interest effect	Currency adjustment	Provisions as at 31 December
Stage 1	2	1	–	1	0	0	–	–	0	2
Stage 2	0	2	–	0	0	0	–	–	0	2
Stage 3	0	–	0	0	–	–	–	–	–	0
Total	2	3	0	1	–	–	–	–	0	4

2019

€ mn	Provisions as at 1 January	Additions	Utilisation	Reversals	Transfer to Stage 1	Transfer to Stage 2	Transfer to Stage 3	Interest effect	Currency adjustment	Provisions as at 31 December
Stage 1	2	1	–	1	0	–	–	–	0	2
Stage 2	0	0	–	0	0	–	–	–	0	0
Stage 3	3	–	–	3	–	–	–	–	0	0
Tiotal	5	1	–	4	–	–	–	–	0	2

The provisions for unrecognised lending business refer to loan commitments and contingent liabilities and are reported on the equity and liabilities side of the statement of financial position under provisions.

No impaired financial assets were recognised for the first time in the financial year 2020, nor were assets acquired within the context of the realisation of collateral.

Credit quality of financial receivables from other transactions

Financial receivables from other transactions are subject to credit risk. Of the receivables from other transactions in the amount of € 94 million (2019: € 77 million), € 86 million (2019: € 66 million) were neither overdue nor impaired, € 2 million (2019: € 5 million) were overdue but not impaired and € 6 million (2019: € 6 million) were impaired.

(63) Reconciliation of gross carrying amounts of financial assets

The following tables show the development of the gross carrying amounts of financial assets that are subject to the impairment rules and to which the loss allowance mentioned above can be attributed.

Financial assets (ac) 2020

€ mn	Gross carrying amount as at 1 Jan	Additions	Disposals	Transfer to Stage 1	Transfer to Stage 2	Transfer to Stage 3	Impairment and reversals of impairment	Net modification gain or loss	Currency and other changes	Gross carrying amount as at 31 Dec
Loan receivables (ac)	**25,783**	**9,881**	**7,745**	**–**	**–**	**–**	**-118**	**-1**	**-523**	**27,277**
Stage 1	23,923	9,709	7,071	163	-6,704	-90	–	0	-612	19,318
Stage 2	916	172	459	-163	6,704	-750	–	0	-10	6,410
Stage 3	944	0	215	–	0	840	-118	-1	99	1,549
POCI	–	–	–	–	–	–	–	–	–	–
Money market and capital market receivables (ac)	**6,618**	**633**	**1,347**	**–**	**–**	**–**	**–**	**–**	**-20**	**5,884**
Stage 1	6,493	633	1,278	–	-494	–	–	–	-26	5,328
Stage 2	125	–	69	–	494	–	–	–	6	556
Receivables from other transactions (ac)	**77**	**57**	**40**	**–**	**–**	**–**	**–**	**–**	**0**	**94**
Total	32,478	10,571	9,132	–	–	–	-118	-1	-543	33,255

Financial assets (ac) 2019

€ mn	Gross carrying amount as at 1 Jan	Additions	Disposals	Transfer to Stage 1	Transfer to Stage 2	Transfer to Stage 3	Impairment and reversals of impairment	Net modification gain or loss	Currency and other changes	Gross carrying amount as at 31 Dec
Loan receivables (ac)	**26,795**	**10,567**	**12,082**	**–**	**–**	**–**	**-229**	**-5**	**737**	**25,783**
Stage 1	24,422	10,476	10,997	86	-726	-57	–	–	719	23,923
Stage 2	786	78	287	-86	728	-307	–	-5	9	916
Stage 3	1,587	13	798	–	-2	364	-229	–	9	944
POCI	–	–	–	–	–	–	–	–	–	–
Money market and capital market receivables (ac)	**6,578**	**1,360**	**1,440**	**–**	**–**	**–**	**–**	**–**	**120**	**6,618**
Stage 1	5,773	1,359	1,302	548	–	–	–	–	115	6,493
Stage 2	805	1	138	-548	–	–	–	–	5	125
Receivables from other transactions (ac)	**64**	**58**	**44**	**–**	**–**	**–**	**–**	**–**	**-1**	**77**
Total	33,437	11,985	13,566	–	–	–	-229	-5	856	32,478

Financial assets (fvoci) 2020

€ mn	Gross carrying amount as at 1 Jan	Additions	Disposals	Transfer to Stage 1	Transfer to Stage 2	Transfer to Stage 3	Impairment and reversals of impairment	Net modification gain or loss	Currency and other changes	Gross carrying amount as at 31 Dec
Money market and capital market receivables (fvoci)	**3,415**	**869**	**620**	**–**	**–**	**–**	**–**	**–**	**3**	**3,667**
Stage 1	3,415	869	620	–	–	–	–	–	3	3,667
Equity instruments (fvoci)	**5**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**0**	**5**
Stage 1	5	–	–	–	–	–	–	–	0	5
Total	3,420	869	620	–	–	–	–	–	3	3,672

Financial assets (fvoci) 2019

€ mn	Gross carrying amount as at 1 Jan	Additions	Disposals	Transfer to Stage 1	Transfer to Stage 2	Transfer to Stage 3	Impairment and reversals of impairment	Net modification gain or loss	Currency and other changes	Gross carrying amount as at 31 Dec
Money market and capital market receivables (fvoci)	**4,443**	**1,028**	**1,842**	**–**	**–**	**–**	**–**	**–**	**-214**	**3,415**
Stage 1	4,443	1,028	1,842	–	–	–	–	–	-214	3,415
Equity instruments (fvoci)	**7**	**1**	**–**	**–**	**–**	**–**	**–**	**–**	**-3**	**5**
Stage 1	7	1	–	–	–	–	–	–	-3	5
Total	4,450	1,029	1,842	–	–	–	–	–	-217	3,420

Please refer to the presentation of the items of the statement of financial position in the section "Notes to the statement of financial position" for information on maximum credit risk exposure since the carrying amount corresponds to the maximum credit risk exposure of Aareal Bank as at the balance sheet date, for both items that are subject to the impairment rules and for financial assets that are not subject to the impairment rules. The collateral received is described in the Report on the Economic Position and in the Risk Report as part of the Group Management Report.

As at the current and the previous year's reporting dates, no receivables from the lending business that were written off during the reporting year, were still part of foreclosure proceedings.

(64) Modification effects

If modifications are made to financial assets during the contract term leading to changes in the contractual cash flows and if these changes are not that extensive that the financial asset is derecognised and a new asset is recognised, such modifications are non-substantial modifications. Following a non-substantial modification, the carrying amount of a financial asset is remeasured and a net modification gain or loss is recorded in net interest income or in the loss allowance.

The following table shows the amortised cost before modification of financial assets that were subject to non-substantial modifications in the reporting period as well as the related modification gain or loss.

	2020			2019		
	Stage 1	Stage 2	Stage 3	Stage 1	Stage 2	Stage 3
€ mn						
Amortised cost before modification	283	1,689	264	284	82	–
Net gain or loss on modification	0	0	-1	0	-5	–
Amortised cost after modification	**283**	**1,689**	**263**	**284**	**77**	**–**

During the financial year, no receivables from the lending business were reclassified from Stage 2 or Stage 3 to Stage 1, which had been modified since they were first classified as Stage 2 or Stage 3 receivables (2019: € – million).

(65) Offsetting financial instruments

Financial assets and financial liabilities are offset and the net amount is presented in the statement of financial position when currently there is a legally enforceable right to set off the recognised amounts, and when the Bank intends either to settle on a net basis – or to realise the asset and settle the liability simultaneously. The following overviews show whether and to what extent financial instruments were actually offset as at the current reporting date. The tables also include disclosures on financial instruments that are part of an enforceable master netting or similar arrangement that do not meet the criteria for offsetting in the statement of financial position.

Financial assets

31 December 2020

€ mn	Gross carrying amounts of recognised financial assets	Gross carrying amounts of offset amounts	Net carrying amount reported in the statement of financial position	Financial liabilities which were not subject to offsetting	Collateral received	Remaining net amount
Derivatives	2,245	–	2,245	1,058	1,280	-93
Reverse repos	–	–	–	–	–	–
Total	**2,245**	**–**	**2,245**	**1,058**	**1,280**	**-93**

31 December 2019

€ mn	Gross carrying amounts of recognised financial assets	Gross carrying amounts of offset amounts	Net carrying amount reported in the statement of financial position	Financial liabilities which were not subject to offsetting	Collateral received	Remaining net amount
Derivatives	1,800	–	1,800	1,065	658	77
Reverse repos	–	–	–	–	–	–
Total	**1,800**	**–**	**1,800**	**1,065**	**658**	**77**

Financial liabilities

31 December 2020

€ mn	Gross carrying amounts of recognised financial liabilities	Gross carrying amounts of offset amounts	Net carrying amount reported in the statement of financial position	Financial assets which were not subject to offsetting	Collateral provided	Remaining net amount
Derivatives	1,906	–	1,906	1,058	852	-4
Repos	–	–	–	–	–	–
Total	**1,906**	**–**	**1,906**	**1,058**	**852**	**-4**

31 December 2019

€ mn	Gross carrying amounts of recognised financial liabilities	Gross carrying amounts of offset amounts	Net carrying amount reported in the statement of financial position	Financial assets which were not subject to offsetting	Collateral provided	Remaining net amount
Derivatives	2,174	–	2,174	1,065	1,077	32
Repos	–	–	–	–	–	–
Total	**2,174**	**–**	**2,174**	**1,065**	**1,077**	**32**

To reduce counterparty risk, Aareal Bank Group concludes standardised master agreements for financial derivatives and securities repurchase agreements, such as the ISDA Master Agreement, the German Master Agreement on Financial Derivatives or the Master Agreement for Securities Repurchase Transactions. In addition, Aareal Bank enters into collateral agreements (Credit Support Annex to the ISDA Master Agreement and Collateral Annex to the German Master Agreement on Financial Derivatives) in which a mutual collateralisation of all claims between the contracting parties is agreed and which include netting arrangements.

The master agreements for financial derivatives used by Aareal Bank include netting arrangements at a single transaction level (so-called "payment netting"), which provide for a netting of payments when both parties need to make payments in the same currency on the same date, as set out in the contract. Aareal Bank does not offset financial derivatives according to the rules related to payment netting, as the transactions are not settled on a net basis. Aareal Bank Group has not entered into arrangements providing for netting of derivatives across several transactions.

For securities repurchase transactions (repo), depending on the counterparty, payment or delivery netting is made. In line with the rules set out in the master agreement for repo transactions, payments or deliveries of securities may be offset when both counterparties have to make payments in the same currency on the same date, or have to deliver securities of the same type. Transactions effected on the basis of the master agreement for repo transactions generally meet the offsetting requirements of IAS 32.

(66) Assets provided or accepted as collateral

Assets provided as collateral

Aareal Bank Group has provided financial assets as collateral for its liabilities (including TLTRO) or contingent liabilities. The following overview shows the carrying amount of the collateral provided and the items of the statement of financial position in which they are reported.

	31 Dec 2020	31 Dec 2019
€ mn		
Money market and capital market receivables (ac, fvoci and fvpl)	5,729	1,434
Receivables from other transactions (ac)	30	26
Total	**5,759**	**1,460**

The protection buyer has no right to sell or re-pledge any of financial assets pledged as collateral (2019: € – million). There is a fully cash-collateralised and irrevocable payment obligation in the amount of € 30 million (2019: € 26 million) from the bank levy and also for the deposit guarantee scheme of German banks. This obligation is reported under receivables from other transactions (ac).

Assets accepted as collateral

Aareal Bank Group accepts financial assets as collateral. These assets may be sold or pledged without the collateral owner being in default. No fixed-income securities were accepted as collateral for repo transactions as at the reporting date (2019: € – million).

Collateral is provided and accepted predominantly on the basis of standardised agreements on securities repurchase transactions and on the collateralisation of forward transactions.

(67) Transfer of financial assets without derecognition

Aareal Bank Group sells securities subject to a take-back requirement as borrower within the framework of genuine repurchase agreements. Within the scope of such agreements, securities were transferred to lenders without resulting in the securities being derecognised since Aareal Bank Group retains the substantial risks and rewards from the securities. The risks to which Aareal Bank Group is still exposed comprise the default risk, the interest rate risk and other price risks. The equivalent values received as collateral during the transfer of securities are accounted as money-market receivables or liabilities. Within the context of securities repurchase transactions, the unrestricted title and the unrestricted power of disposition is transferred to the lender upon delivery of the securities. The lender has the right to sell or pledge these securities, however, he is required to retransfer securities of the same type and in the same amount as at the repurchase date.

As in the previous year, no securities were part of repurchase agreements as at the balance sheet date.

(68) Derivative financial instruments

The following table shows positive and negative market values (including pro-rata interest) of all derivative financial instruments by hedge and risk types:

	Fair value as at 31 Dec 2020		Fair value as at 31 Dec 2019	
€ mn	positive	negative	positive	negative
Fair value hedge derivatives	**1,343**	**1,298**	**1,374**	**1,327**
Interest rate risk	1,343	1,267	1,374	1,294
Interest rate swaps	1,343	1,267	1,374	1,294
Interest rate and currency risk	–	31	–	33
Cross-currency swaps	–	31	–	33
Hedge of net investments	**88**	**–**	**6**	**14**
Currency risk	88	–	6	14
Cross-currency swaps	88	–	6	14
Other derivatives	**787**	**608**	**414**	**824**
Interest rate risk	209	503	182	427
Interest rate swaps	208	502	181	426
Swaptions	–	–	–	–
Caps, floors	1	1	1	1
Interest rate and currency risk	578	105	232	397
Spot and forward foreign exchange transactions	7	7	4	21
Cross-currency swaps	571	98	228	376
Total	**2,218**	**1,906**	**1,794**	**2,165**

Derivatives have been entered into with the following counterparties:

	Fair value as at 31 Dec 2020		Fair value 31 Dec 2019	
€ mn	positive	negative	positive	negative
OECD banks and central governments	2,132	1,853	1,701	2,164
Companies and private individuals	86	53	93	1
Total	**2,218**	**1,906**	**1,794**	**2,165**

The following overview shows the cash flows of derivative financial instruments by risk types, based on the contractual maturity. The amounts shown in the table represent the contractually agreed future undiscounted cash flows.

31 December 2020

€ mn	Up to 3 months	3 months to 1 year	1 year to 5 years	more than 5 years	Total
Interest rate risk					
Interest rate swaps					
Cash inflows	107	286	745	166	**1,304**
Cash outflows	119	224	676	127	**1,146**
Caps, floors					
Cash inflows	0	0	1	0	**1**
Cash outflows	0	0	1	0	**1**
Interest rate and currency risk					
Spot and forward foreign exchange transactions					
Cash inflows	1,808	132	–	–	**1,940**
Cash outflows	1,808	132	–	–	**1,940**
Cross-currency swaps					
Cash inflows	200	2,101	9,298	54	**11,653**
Cash outflows	212	2,033	9,118	–	**11,363**
Total cash inflows	**2,115**	**2,519**	**10,044**	**220**	**14,898**
Total cash outflows	**2,139**	**2,389**	**9,795**	**127**	**14,450**

31 December 2019

€ mn	Up to 3 months	3 months to 1 year	1 year to 5 years	more than 5 years	Total
Interest rate risk					
Interest rate swaps					
Cash inflows	135	381	1,015	264	**1,795**
Cash outflows	134	264	853	277	**1,528**
Caps, floors					
Cash inflows	0	0	1	0	**1**
Cash outflows	0	0	1	0	**1**
Interest rate and currency risk					
Spot and forward foreign exchange transactions					
Cash inflows	2,210	274	–	–	**2,484**
Cash outflows	2,226	273	–	–	**2,499**
Cross-currency swaps					
Cash inflows	897	1,048	8,484	–	**10,429**
Cash outflows	949	1,211	9,041	53	**11,254**
Total cash inflows	**3,242**	**1,703**	**9,500**	**264**	**14,709**
Total cash outflows	**3,309**	**1,748**	**9,895**	**330**	**15,282**

The procedure for measuring and monitoring liquidity risk is described in the Risk Report, part of the Group Management Report.

(69) Disclosures on hedging relationships

Disclosures on hedging derivatives

The following tables show designated hedging derivatives separately for each type of hedging relationship, risk category and product type:

Positive market value of designated hedging derivatives

€ mn	Carrying amount 31 Dec 2020	Nominal amount 31 Dec 2020	Fair value change 1 Jan – 31 Dec 2020	Carrying amount 31 Dec 2019	Nominal amount 31 Dec 2019	Fair value change 1 Jan – 31 Dec 2019
Fair value hedges						
Interest rate risk						
Interest rate swaps	1,343	16,694	181	1,374	17,915	423
Hedge of net investments						
Currency risk						
Cross-currency swaps	88	1,027	0	6	518	0
Total	**1,431**	**17,721**	**181**	**1,380**	**18,433**	**423**

Negative market value of designated hedging derivatives

€ mn	Carrying amount 31 Dec 2020	Nominal amount 31 Dec 2020	Fair value change 1 Jan – 31 Dec 2020	Carrying amount 31 Dec 2020	Nominal amount 31 Dec 2019	Fair value change 1 Jan – 31 Dec 2019
Fair value hedges						
Interest rate risk						
Interest rate swaps	1,267	14,609	189	1,294	12,186	256
Interest rate and currency risk						
Cross-currency swaps	31	111	3	33	118	5
Hedge of net investments						
Currency risk						
Cross-currency swaps	–	–	–	14	597	0
Total	**1,298**	**14,720**	**192**	**1,341**	**12,901**	**261**

The following overview presents the nominal amounts of the hedging derivatives by maturities:

31 December 2020

€ mn	Up to 3 months	3 months to 1 year	1 year to 5 years	More than 5 years	Total
Fair value hedges					
Interest rate risk					
Interest rate swaps	1,301	4,730	17,656	7,617	**31,304**
Interest rate and currency risks					
Cross-currency swaps	–	–	111	–	**111**
Hedge of net investments					
Currency risk					
Cross-currency swaps	55	421	551	–	**1,027**
Total nominal amounts	**1,356**	**5,151**	**18,318**	**7,617**	**32,442**

Aareal Bank applies the standard amendments from the first part of the effects of the interest rate benchmark reform (IBOR reform) on financial reporting in the period prior to the replacement of an existing interest rate benchmark. The uncertainties refer to the hedging of changes in fair value from interest rate risk. This applies to variable reference rates with terms of one to six months for the currencies AUD, CAD, DKK, EUR, GBP, SEK and USD. Of the total amount of € 32.4 billion, € 6.0 billion is linked to non-euro reference interest rates. Aareal Bank Group still does not expect the changes from the IBOR reform (Phase 1) to require the discontinuation of hedging relationships.

31 December 2019

€ mn	Up to 3 months	3 months to 1 year	1 year to 5 years	More than 5 years	Total
Fair value hedges					
Interest rate risk					
Interest rate swaps	843	3,512	17,999	7,747	**30,101**
Interest rate and currency risks					
Cross-currency swaps	–	–	118	–	**118**
Hedge of net investments					
Currency risk					
Cross-currency swaps	184	218	713	–	**1,115**
Total nominal amounts	**1,027**	**3,730**	**18,830**	**7,747**	**31,334**

Disclosures on hedged items

Hedged items of fair value hedges

The following tables show hedged items separately for each type of hedging relationship and risk category:

	Active hedging relationships			Discontinued hedging relationships
€ mn	Carrying amount 31 Dec 2020	Accumulated hedge adjustment 31 Dec 2020	Change in hedged fair values 1 Jan - 31 Dec 2020	Balance of hedge adjustments 31 Dec 2020
Interest rate risk				
Loan receivables (ac)	7,045	224	168	58
Money market and capital market receivables (ac)	2,990	701	10	165
Money market and capital market receivables (fvoci)	3,534	148	18	2
Money market and capital market liabilities (ac)	19,433	1,086	82	46
Subordinated liabilities (ac)	818	45	-6	3
Interest rate and currency risk				
Money market and capital market receivables (ac)	160	49	3	–

	Active hedging relationships			Discontinued hedging relationships
€ mn	Carrying amount 31 Dec 2019	Accumulated hedge adjustment 31 Dec 2019	Change in hedged fair values 1 Jan - 31 Dec 2019	Balance of hedge adjustments 31 Dec 2019
Interest rate risk				
Loan receivables (ac)	6,539	94	77	70
Money market and capital market receivables (ac)	2,538	520	44	22
Money market and capital market receivables (fvoci)	3,236	209	-121	48
Money market and capital market liabilities (ac)	18,653	1,025	176	59
Subordinated liabilities (ac)	841	51	2	4
Interest rate and currency risk				
Money market and capital market receivables (ac)	164	46	5	–

Hedge of net investments

The change in value of currency-hedged net investments in foreign operations amounted to € 93 million (2019: € -10 million) in the financial year under review. The balance of the hedging reserve (net) stood at € 68 million (2019: € -20 million) at year-end.

Net gain or loss from hedge accounting

Fair value hedges

The net gain or loss from hedge accounting include the following ineffective portions of fair value hedges by risk categories:

€ mn	1 Jan-31 Dec 2020	1 Jan-31 Dec 2019
Interest rate risks	6	-4
Interest rate and currency risks	0	0
Total	**6**	**-4**

Hedge of net investments

The ineffective portion of currency-hedged net investments in foreign operations amounted to € 0 million (2019: € 0 million), reported in net gains or losses from hedge accounting. No amounts were reclassified from the reserve for currency-hedged net investments to the income statement.

(70) Maturities of financial liabilities

The following overview shows the future undiscounted cash flows of non-derivative financial liabilities and of loan commitments.

Maturities as at 31 December 2020

€ mn	Payable on demand	Up to 3 months	3 months to 1 year	1 year to 5 years	More than 5 years	Total
Money market and capital market liabilities (ac)	1,444	1,427	6,898	10,924	8,476	**29,169**
Deposits from the housing industry (ac)	8,428	2,166	–	–	–	**10,594**
Subordinated liabilities (ac)	–	17	22	445	550	**1,034**
Financial liabilities from other transactions (ac)	85	–	1	–	–	**86**
Lease liabilities	–	3	10	34	36	**83**
Financial guarantees	160	–	–	–	2	**162**
Loan commitments	1,258	–	–	–	–	**1,258**

Maturities as at 31 December 2019

€ mn	Payable on demand	Up to 3 months	3 months to 1 year	1 year to 5 years	More than 5 years	Total
Money market and capital market liabilities (ac)	845	1,486	4,181	10,307	9,608	**26,427**
Deposits from the housing industry (ac)	7,696	2,050	–	–	–	**9,746**
Subordinated liabilities (ac)	–	17	43	454	588	**1,102**
Financial liabilities from other transactions (ac)	91	0	2	0	–	**93**
Lease liabilities	–	3	9	33	40	**85**
Financial guarantees	154	–	–	–	2	**156**
Loan commitments	1,205	–	–	–	–	**1,205**

The Risk Report, part of the Group Management Report, includes a detailed description of the liquidity risk associated with financial liabilities.

Segment Reporting

(71) Operating segments of Aareal Bank

Aareal Bank prepares its segment reporting in accordance with IFRS 8 Operating Segments.

In accordance with the "management approach" set out in IFRS 8, the segment report discloses, on a segment-specific basis, financial information which is relevant for internal control of an entity and which is also used by such entity's management to make decisions on the allocation of resources as well as to measure the financial performance of segments.

As explained in the Group Management Report 2019, Aareal Bank's management system was revised in the course of the "Aareal Next Level" strategic development at the turn of the year 2019. The previous Consulting/Services segment was split into the Consulting/Services Bank and Aareon segments, in order to sharpen the independent profiles of the individual business activities and to enhance transparency. The previous year's figures were adjusted accordingly. Whilst the structure of the existing Structured Property Financing segment remained unchanged in principle, the name of the former Consulting/Services Bank segment was changed to Banking & Digital Solutions at the turn of the year as part of the strategic review.

Two changes were necessary as part of the further development of the management system. A review of our liquidity model conducted during the fourth quarter of 2019 had shown that a higher share of deposits from the housing industry is available to the Bank for an extended period of time, as a replacement for unsecured placements on the capital markets. This resulted in lower unsecured funding requirements (and to a corresponding relief on income), as well as a change in intra-segment charges. A similar effect applied to the interest rate on residual deposits; this rate was also raised as part of modelling changes. In the current (as well as in the expected) interest rate environment, backing this residual interest rate using fixed-income assets gives rise to interest income as well as typing up RWAs; these effects were allocated to the Consulting/Services Bank segment from the effective date of this change on 1 January 2020. For management purposes, the calculation of allocated equity was changed for all segments, applying the regulatory calculation method. Reported equity on the statement of financial position differs from this. Other reserves were now also included when calculating allocated equity at Group level. RoE before taxes was thus also changed accordingly. The previous year's figures were adjusted accordingly.

Three operating segments were defined within Aareal Bank in line with internal management reporting, based on the organisational structure established according to the various products and services offered.

The **Structured Property Financing segment** comprises the property financing and refinancing activities. In this segment, Aareal Bank facilitates property investments for its domestic and international clients, and is active in this respect in Europe, North America and Asia-Pacific. It offers commercial property financing solutions, especially for office buildings, hotels, retail, logistics and residential properties. Its particular strength lies in its success in 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 and retail properties and hotels. This enables Aareal Bank to offer tailor-made financing concepts that meet the special requirements of its 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 (German covered bonds), which account for a major share of the Bank's long-term funding. The AAA rating of the Pfandbriefe additionally confirms the quality of the cover assets pool. To cater to a broad investor base, Aareal Bank covers a wide range of other refinancing tools, including promissory notes and debt securities. Depending on market conditions, the Bank places large-sized public issues or private placements. 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.

In the **Consulting/Services Bank segment,** Aareal Bank Group offers services, products and solutions to the housing and commercial property industries to optimise digital payment, electronic banking and cash management processes. Aareal Bank distributes BK01, the leading procedure in the German housing and property management sector for the automated settlement of mass payments. The procedure is integrated in licensed bookkeeping systems. Therefore, customers in Germany may process their payment transactions and account management from the administration software employed. Apart from the German residential and commercial property sector, the German energy and waste disposal industry is a second important customer group of the segment. This enables the offer of further products, facilitating the cross-sector cooperation of target groups and realising synergy effects via end-to-end digital processes. The use of the payment transaction products of Aareal Bank generates deposits that contribute significantly to Aareal Bank Group's refinancing base.

As part of the **Aareon segment,** the Aareon sub-group offers the IT systems and advisory business for the housing and commercial property sector. Aareon offers its customers reliable, pioneering solutions in the fields of consulting, software and services to optimise IT-supported business processes in the digital age. The ERP (Enterprise Resource Planning) systems, which are tailored to the needs of the respective market, may be supplemented by further digital solutions for purposes of process optimisation. The majority of these integrated systems forms the digital ecosystem "Aareon Smart World". It connects property companies with customers, employees and business partners as well as technical "equipment" in apartments and buildings. Aareon Smart World can be used to restructure and optimise processes. The applications help to reduce costs, enable the creation of new business models by providing links between all participants and offer more ease-of-use in the dialogue between tenants and employees of the housing industry.

Aareon offers software solutions both in Germany and abroad that may be used in various types of operating environments: in-house services, hosting and Software as a Service (SaaS) from the exclusive Aareon Cloud. Data from Aareon's Cloud Computing is held in Aareon's certified data-processing centre in Mainz, which guarantees data security and protection at the highest level. Following successful advice, implementation and training, customers usually opt for a maintenance model covering regular support services.

Income and expenses within Aareal Bank are predominantly attributable to transactions with third parties, and are directly allocated to the responsible business segment. Revenue from transactions between Aareal Bank's segments was not generated in a significant amount. Therefore, we elected not to distinguish between internal and external revenue in the following disclosures. Administrative expenses not directly attributable to any of the business segments are segmented in line with the internal cost allocation, based on the principle of causation.

The results of the business segments are measured by the operating profit and the return on equity (RoE). RoE, which indicates a segment's profitability, is calculated as the ratio of the segment's operating result (after non-controlling interests and after AT1 interest) to the portion of equity allocated to that segment on average. Allocated equity is calculated on the basis of the capital requirements pursuant to Basel IV.

(72) Segment results

€ mn	Structured Property Financing		Consulting/ Services Bank		Aareon		Consolidation/ Reconciliation		Aareal Bank Group	
	1 Jan – 31 Dec 2020	1 Jan – 31 Dec 2019	1 Jan – 31 Dec 2020	1 Jan – 31 Dec 2019	1 Jan – 31 Dec 2020	1 Jan – 31 Dec 2019	1 Jan – 31 Dec 2020	1 Jan – 31 Dec 2019	1 Jan – 31 Dec 2020	1 Jan – 31 Dec 2019
Net interest income	474	549	39	-15	-1	-1	0	0	512	533
Loss allowance	344	90	0	0	0	0			344	90
Net commission income	8	10	26	23	213	208	-13	-12	234	229
Net derecognition gain or loss	28	64							28	64
Net gain or loss from financial instruments (fvpl)	-32	1	0		0	0			-32	1
Net gain or loss from hedge accounting	6	-4							6	-4
Net gain or loss from investments accounted for using the equity method	2	1			-1	0			1	1
Administrative expenses	227	254	68	73	188	173	-14	-12	469	488
Net other operating income/expenses	-14	-1	0		4	3	-1	0	-11	2
Operating profit	**-99**	**276**	**-3**	**-65**	**27**	**37**	**0**	**0**	**-75**	**248**
Income taxes	-14	95	-1	-21	9	11			-6	85
Consolidated net income	**-85**	**181**	**-2**	**-44**	**18**	**26**	**0**	**0**	**-69**	**163**
Consolidated net income attributable to non-controlling interests	0	0	0	0	5	2			5	2
Consolidated net income attributable to shareholders of Aareal Bank AG	-85	181	-2	-44	13	24	0	0	-74	161
Allocated equity[1]	1,849	1,878	199	195	32	42	442	399	2,522	2,514
RoE before taxes (%)[2]	-6.6	13.5	-1.7	-33.4	68.2	83.4			-4.1	8.9
Employees (average)	**785**	**796**	**385**	**390**	**1,745**	**1,605**			**2,915**	**2,791**
Segment assets	**34,101**	**30,012**	**10,997**	**10,771**	**380**	**354**			**45,478**	**41,137**

[1] For management purposes, the calculation of allocated equity was changed for all segments, applying the regulatory calculation method. Reported equity on the statement of financial position differs from this. Other reserves are now also included when calculating allocated equity at Group level. RoE before taxes is thus also changed accordingly. The previous year's figures were adjusted accordingly. Aareon's RoE before taxes was influenced by the sale of the minority stake. As from the second quarter of 2020, consolidated net income attributable to non-controlling interests was increased. Aareon's total equity as disclosed in the statement of financial position declined to € 140 million.
[2] The allocation of earnings is based on the assumption that net interest payable on the AT1 bond is recognised on an accrual basis.

Commission income from contracts with clients is allocated to the segments as follows:

	Structured Property Financing		Consulting/ Services Bank		Aareon		Consolidation/ Reconciliation		Aareal Bank Group	
	1 Jan – 31 Dec 2020	1 Jan – 31 Dec 2019	1 Jan – 31 Dec 2020	1 Jan – 31 Dec 2019	1 Jan – 31 Dec 2020	1 Jan – 31 Dec 2019	1 Jan – 31 Dec 2020	1 Jan – 31 Dec 2019	1 Jan – 31 Dec 2020	1 Jan – 31 Dec 2019
€ mn										
ERP products (incl. add-on products)					197	201	-18	-18	179	183
Digital solutions					61	51			61	51
Banking business and other activities	11	13	32	32	0	0			43	45
Total	**11**	**13**	**32**	**32**	**258**	**252**	**-18**	**-18**	**283**	**279**

(73) Income by geographical markets

	2020	2019
€ mn		
Germany	505	563
Rest of Europe	142	160
North America	90	99
Asia/Pacific	6	5
Total	**743**	**827**

Income includes net interest income (excluding loss allowance), net commission income, net gain or loss on derecognition and net gain or loss from financial instruments (fvpl). Allocation to geographical markets is based on the registered office or domicile of the Group company or branch office.

Other Notes

(74) Assets and liabilities in foreign currency

Foreign currency assets

€ mn	31 Dec 2020	31 Dec 2019
USD	11,092	11,264
GBP	4,279	4,271
CAD	1,291	1,357
SEK	862	701
CHF	313	364
DKK	59	117
Others	459	256
Total	**18,355**	**18,330**

Foreign currency liabilities

€ mn	31 Dec 2020	31 Dec 2019
USD	11,106	11,230
GBP	4,359	4,262
CAD	1,289	1,349
SEK	855	701
CHF	311	365
DKK	59	119
Others	452	248
Total	**18,431**	**18,274**

(75) Subordinated assets

In the event of insolvency or liquidation of the issuer, subordinated assets are those subordinate to the claims of all other creditors. Subordinated assets amounted to € 350 million in the financial year 2020 (2019: € – million).

(76) Leases

Leases where the Bank acts as the lessee

The following overview shows the movements in the right-of-use assets from leases where Aareal Bank Group acts as the lessee.

	2020			2019		
€ mn	Right-of-use assets in land and buildings	Right-of-use assets in office furniture and equipment	Total	Right-of-use assets in land and buildings	Right-of-use assets in office furniture and equipment	Total
Cost						
Balance as at 1 January	**69**	**7**	**76**	**64**	**6**	**70**
Additions	5	4	**9**	17	5	**22**
Transfers	-2	0	**-2**	-1	–	**-1**
Amortisation and impairment losses	5	2	**7**	9	4	**13**
Disposals	2	3	**5**	2	0	**2**
Changes in the basis of consolidation	4	–	**4**	–	–	**–**
Currency translation differences	-2	0	**-2**	0	–	**0**
Balance as at 31 December	**67**	**6**	**73**	**69**	**7**	**76**

Right-of-use assets are recognised under property and equipment.

Aareal Bank Group primarily rents properties which are, in some cases, subject to longer-term rental agreements with extension options of up to ten years where the exercise is reasonably certain. The leases are not subject to material residual value guarantees.

The entire cash outflows from leases where Aareal Bank Group is the lessee in the current period amount to € 14 million (2019: € 16 million) as at the reporting date.

Expenses and income from Aareal Bank Group include the following amounts from leases with Aareal Bank Group as the lessee in the 2020 financial year:

€ mn	31 Dec 2020	31 Dec 2019
Interest expenses for lease liabilities	2	2
Expenses for short-term leases	2	2
Expenses for low-value leases	1	0
Income from the sublease of right-of-use assets	1	0

In addition, the operating property of the Rome branch, which is held by a subsidiary, was sold as part of a sale and leaseback transaction, resulting in gain of € 8 million.

In the financial year 2020, no material variable lease payments were agreed upon.

The future undiscounted cash flows from lease liabilities based on their maturities are disclosed in the Note "Maturities of financial liabilities".

Leases where the Bank acts as the lessor

Aareal Bank Group acts as lessor as regards the lease of property. The material rental contracts are classified as operating leases. Properties leased by the Group are reported under the item "Other assets". Not all properties reported under the item "Other assets" are currently let. The risks of these properties are included in property risk management.

Income from operating leases amounted to € 9 million (2019: € 12 million) in the year under review. It is recognised in the income statement on a straight-line basis over the lease term.

The following overview shows the future undiscounted payments under operating leases based on their maturities where Aareal Bank Group acts as the lessor.

€ mn	31 Dec 2020	31 Dec 2019
Up to 1 year	6	8
Longer than 1 year, and up to 5 years	14	17
Longer than 5 years	6	4
Total minimum lease payments	**26**	**29**

(77) Contingent liabilities and loan commitments

€ mn	31 Dec 2020	31 Dec 2019
Contingent liabilities	163	157
Loan commitments	1,258	1,205
of which: irrevocable	896	881

Contingent liabilities include irrevocable payment obligations regarding the bank levy and the liability to the deposit guarantee scheme of German banks. These and the values reported under loan commitments given represent the maximum default risk to which Aareal Bank Group is exposed at the end of the reporting period.

Furthermore, the Bank is involved in legal disputes. Based on a legal analysis, successful outcome of these disputes is more likely than not. Essentially, these are legal disputes with borrowers (or former borrowers) who claim damages against the Bank. These are included in the table above, with a probability-weighted amount of € 92 million (2019: € 99 million), but have not been recognised as liabilities.
We estimate the maximum default risk in the low triple-digit million range. The duration of proceedings depends on the complexity of each individual litigation, and the legal remedies available in each case. Likewise, the final amount in the event of defeat may vary considerably, depending upon the duration of proceedings and the legal remedies. Refunds of litigation costs are possible. Accordingly, the recognition of contingent liabilities is also subject to estimation uncertainties.

(78) Regulatory capital and capital management

As regards meeting minimum capital ratios, Aareal Bank Group has to comply with the capital adequacy requirements set out in the Capital Requirements Regulation (CRR), the Capital Requirements Directive IV (CRD IV), the German Banking Act (Kreditwesengesetz, KWG) and the German Solvency Regulation (Solvabilitätsverordnung, SolvV). This requires Aareal Bank to comply with a Total SREP Capital Requirement (TSCR) in 2021 of 10.25 % (2020: 10.25 %). This comprises an additional own funds requirement (Pillar 2 Requirements – P2R) of 2.25 %, which has to be maintained of at least 56.25 % in Common Equity Tier 1 capital and 75 % of Tier 1 capital. Taking into account the capital conservation buffer of 2.5 % and the countercyclical capital buffer of 0.0 % (2020: 0.2 %), both of which have to be maintained in the form of Common Equity Tier 1 capital, the Overall Capital Requirement (OCR) of Aareal Bank in 2021 amounts to 12.75 % (2020: 12.9 %).

The objectives of capital management are optimising the capital base as well as an efficient capital allocation to the individual business areas in terms of risk and income. Aareal Bank has defined the CET1 ratio (Basel IV (phased-in)) as a key management indicator, subject to further regulatory changes. The capital ratios are managed through the generation of profits, an active dividend policy, optimisation of the capital structure, and an efficient management of risk assets.

Within the context of capital management, projections are made on a regular basis showing the changes of the individual capital components and risk-weighted assets, as well as the resulting capital ratios. This is reported regularly to the Management Board within the framework of management reporting. The strategic allocation of capital to the individual business segments is incorporated in the Group's annual overall planning process.

Aareal Bank Group's regulatory capital[1] [2] are composed of the following:

€ mn	31 Dec 2020[2]	31 Dec 2019[1]
Tier 1 capital (T1)		
Subscribed capital and capital reserves	900	900
Eligible retained earnings	1,782	1,653
Accumulated other comprehensive income	-180	-133
Amounts to be deducted from CET 1 capital	-216	-229
Total Common Equity Tier 1 (CET 1) capital	**2,286**	**2,191**

>

[1] 31 December 2019: excluding dividends for 2019 (in line with original proposal for appropriation of profits) and incorporating the pro-rata accrual of net interest payable on the AT1 bond.

[2] 31 December 2020: including dividends for 2019 (in line with initial proposal on the appropriation of profits) less a proposed dividend distribution of € 1.50 per share in 2021, and incorporating the pro-rata accrual of net interest payable on the AT1 bond. The 2021 dividend payment of € 1.50 for 2020 would need to be made in two steps. In compliance with the requirements published by the European Central Bank (ECB) on 15 December 2020, the distributable amount is calculated at € 0.40 per share. The Management Board plans to submit a corresponding proposal for the appropriation of profits to the ordinary Annual General Meeting in May 2021. Depending on further economic developments, regulatory requirements, the Bank's capital position and its risk situation, an extraordinary Annual General Meeting, which could possibly take place during the fourth quarter of 2021, could then decide on the intended remaining payout of € 1.10 per share.

€ mn	31 Dec 2020[2)]	31 Dec 2019[1)]
AT1 bond	300	300
Sum total of Additional Tier 1 (AT1) capital	**300**	**300**
Sum total of Tier 1 capital (T1)	**2,586**	**2,491**
Tier 2 (T2) capital		
Subordinated liabilities	752	830
Other	57	22
Sum total of Tier 2 capital (T2)	**809**	**852**
Total capital (TC)	**3,395**	**3,343**

1) 31 December 2019: excluding dividends for 2019 (in line with original proposal for appropriation of profits) and incorporating the pro-rata accrual of net interest payable on the AT1 bond.

2) 31 December 2020: including dividends for 2019 (in line with initial proposal on the appropriation of profits) less a proposed dividend distribution of € 1.50 per share in 2021, and incorporating the pro-rata accrual of net interest payable on the AT1 bond. The 2021 dividend payment of € 1.50 for 2020 would need to be made in two steps. In compliance with the requirements published by the European Central Bank (ECB) on 15 December 2020, the distributable amount is calculated at € 0.40 per share. The Management Board plans to submit a corresponding proposal for the appropriation of profits to the ordinary Annual General Meeting in May 2021. Depending on further economic developments, regulatory requirements, the Bank's capital position and its risk situation, an extraordinary Annual General Meeting, which could possibly take place during the fourth quarter of 2021, could then decide on the intended remaining payout of € 1.10 per share.

The regulatory measurement of risk-weighted assets (RWA)[3)] in the area of credit risks is based on both the Advanced Internal Ratings Based Approach (AIRBA) and on the standardised approach (CRSA). RWA as at 31 December 2020 can be broken down as follows:

€ mn	Risk-weighted assets (RWA) 31 Dec 2020	Minimum capital requirements 31 Dec 2020	Risk-weighted assets (RWA) 31 Dec 2019	Minimum capital requirements 31 Dec 2019
Credit risk	**9,886**	**791**	**8,774**	**702**
Credit Risk Standard Approach (CRSA)	416	33	595	48
Advanced IRB (AIRB) approach	8,795	704	7,388	591
Equity under the IRB approach based on the simple risk-weighted approach	675	54	791	63
Counterparty credit risk	**517**	**41**	**486**	**39**
Mark to market	288	23	283	23
Risk exposure amount from contributions to the default fund of a central counterparty	5	0	0	0
Credit Valuation Adjustment	224	18	203	16
Market risk	**87**	**7**	**61**	**5**
Operational risk	**1,236**	**99**	**1,489**	**119**
Basic indicator approach	29	2	44	4
Standard approach	1,207	97	1,445	116
Other receivables (e.g. deferred tax assets)	**412**	**33**	**385**	**31**
Total	**12,138**	**971**	**11,195**	**896**

3) From 30 September 2020, the "CRR Quick Fix" has also been taken into consideration.

(79) Additional disclosures to the Remuneration Report

Management Board

In the financial year 2020, the Management Board's total remuneration amounted to € 10 million (2019: € 11 million), of which € 4 million (2019: € 5 million) referred to variable components.

Payments to former Management Board members and their surviving dependants totalled € 2 million in 2020 (2019: € 2 million).

The pension obligations to former members of the Management Board and their surviving dependants amounted to a total of € 37 million as at 31 December 2020 (2019: € 35 million).

Supervisory Board

The total remuneration of members of the Supervisory Board for the financial year 2020 amounted to € 2 million (2019: € 2 million). The remuneration for any financial year shall be due and payable one month after the end of the respective financial year.

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.

Total remuneration of executives in key positions is analysed below:

€ 000's	31 Dec 2020	31 Dec 2019
Short-term benefits	8,193	8,600
Post-employment benefits	7,125	7,704
Other long-term benefits	967	1,548
Termination benefits	–	–
Share-based remuneration	1,985	2,580
Total	**18,270**	**20,432**

Provisions for pension obligations concerning key executives totalled € 34 million as at 31 December 2020 (2019: € 26 million).

Disclosures on share-based remuneration

Valuation model and valuation assumptions

The obligations resulting from share-based payment arrangements as at 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 Euribor swap rate applicable as at the relevant balance sheet date, depending on the term.

Amount of cash-settled share-based payment transactions

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

Quantity (number)	2020	2019
Balance (outstanding) as at 1 January	**699,743**	**656,900**
Granted during the reporting period	313,908	276,782
Expired during the reporting period	–	–
Exercised during the reporting period	310,090	233,939
Balance (outstanding) as at 31 December	**703,561**	**699,743**
of which: exercisable	–	–

The fair value of the virtual shares granted during the reporting period amounted to € 6 million (2019: € 8 million) as at the balance sheet date.

The virtual shares exercised during the reporting period were converted at a weighted average price of the Aareal Bank AG share of € 25.38 (2019: € 28.70).

Impact on financial performance

The total amount recognised as income from share-based payment transactions during the financial year 2020 was € 2 million (2019: total expense of € 10 million). The portion of the total income attributable to members of the Management Board amounted to € 1 million (2019: total expense of € 3 million) and can be broken down to the individual members of the Management Board as follows:

€[1]	2020	2019
Hermann J. Merkens	-448,770	820,318
Marc Hess	192,192	395,408
Dagmar Knopek	-223,382	564,712
Christiane Kunisch-Wolff	-61,132	466,764
Thomas Ortmanns	-223,978	574,412
Christof Winkelmann	-31,042	435,043

[1] Negative amounts indicate income; positive amounts indicate expenses.

In addition, € 0 million (2019: € 0 million) was expensed for former members of the Management Board.

The intrinsic value of the virtual shares exercisable at the reporting date amounted to € 0 million (2019: € 0 million), since there were no exercisable virtual shares at that date. The obligation from share-based payment transactions as at 31 December 2020 amounted to € 19 million (2019: € 30 million). It is reported in the statement of financial position in the line item “Provisions”.

(80) Related party disclosures in accordance with IAS 24

The group of related parties of Aareal Bank Group comprises the members of management or supervisory bodies of Aareal Bank AG (see preceding note) and close members of these persons' families. The group of companies related to Aareal Bank Group consists of the companies set out in Note 89 "List of Shareholdings". Intra-group receivables and liabilities, as well as consolidated income and expenses, are not shown here.

The following list provides an overview of the balances of existing transactions with related parties:

€ mn	31 Dec 2020	31 Dec 2019
Management Board	–	–
Supervisory Board	–	–
Other related parties	20	16
Total	**20**	**16**

The item "Other related parties" includes a loan of € 16 million which was provided to our investee Mount Street Group Limited on an arm's length basis, as well as a loan of € 4 million to Aareon's equity companies, which was also provided on an arm's length basis. Moreover, there is a receivable in the amount of € 0.5 million due from the BauGrund/TREUREAL syndicate.

In addition, there were no further significant transactions within the meaning of IAS 24.

(81) Events after the reporting date

There were no material events after the end of the reporting period which would have to be reported here.

(82) Contingencies

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.

(83) Disclosures pursuant to section 160 (1) no. 8 of the AktG

Pursuant to the German Securities Trading Act (WpHG), any investor whose shareholding in a listed company reaches, exceeds or falls short of certain threshold values in terms of voting rights (whether by purchase, sale or by any other means) must notify the Company and the German Federal Financial Supervisory Authority. The lowest threshold for this notification requirement is 3 %. 100 % of Aareal Bank AG shares are held in free float.

As at 31 December 2020, we were aware of the following shareholders holding a share in the voting rights of at least 3 % pursuant to section 33 (1) of the WpHG:

	Location	Total[1]	Threshold reached on (according to notification)
Responsible entity			
Deka	Frankfurt	9.60 %	22 May 2018
Morgan Stanley[1]	Wilmington	7.53 %	25 September 2020
VBL[2]	Karlsruhe	6.50 %	3 February 2015
Igor Kuzniar	Zug	5.06 %	23 April 2020
Teleios Global Opportunities Master Fund Ltd[3]	George Town		
Allianz Global Investors	Frankfurt	4.99 %	2 October 2019
Dimensional Fund	Austin	4.93 %	7 April 2020
Klaus Umek (Petrus Advisers Ltd.)	London	4.21 %	31 July 2020
JPMorgan Investment Management Inc.[4]	Wilmington	3.07 %	13 November 2018
JPMorgan Chase Bank[4]	Columbus		
JPMorgan Asset Management (UK)[4]	London		
Janus Henderson Group plc	Saint Helier	3.00 %	4 September 2020

[1] Shares are held in safe custody by Morgan Stanley, i. e. are part of the trading book. Nevertheless, the shareholding had to be notified as the 5 % threshold was exceeded.
[2] Shares are managed by Deka and are therefore included in Deka's holding.
[3] Shares are also attributed to Igor Kuzniar and therefore correspond to his shareholding.
[4] Holdings of these three companies are attributed to each other.

(84) Declaration of Compliance in accordance with section 161 of the AktG

The Management Board and the Supervisory Board issued the Declaration of Compliance as stipulated in section 161 of the AktG, and made this Declaration available to shareholders. It is available to the public on the Company's website on www.aareal-bank.com/en/about-us/corporate-governance/declaration-of-compliance/.

(85) Employees

The number of Aareal Bank Group employees is shown below:

	31 Dec 2020[1]	Average 1 Jan - 31 Dec 2020[2]	31 Dec 2019[1]	Average 1 Jan - 31 Dec 2019[2]
Salaried employees	2,817	2,751	2,640	2,641
Executives	165	164	148	150
Total	**2,982**	**2,915**	**2,788**	**2,791**
of which: part-time employees	584	567	556	564

[1] This number does not include 35 employees of the hotel business (31 December 2019: 45 employees).
[2] This number does not include 52 employees of the hotel business (1 January to 31 December 2019: 180 employees).

(86) Nature and extent of interests in unconsolidated structured entities

In accordance with IFRS 12.24, the nature and extent of interests in unconsolidated structured entities as well as the nature of, and changes in, the risks associated with such interests have to be disclosed in the consolidated financial statements. An interest in a structured entity arises from a contractual and/or non-contractual involvement which entitles the Group to receive variable returns from the relevant activities of the structured entity. Examples for this are equity or debt instruments of structured entities or the provision of financing, collateral and guarantees to structured entities.

Structured entities are companies where voting rights or similar rights are not the dominant factor to assess control of the company. The relevant activities of structured entities are directed by means of contractual arrangements; any voting rights relate to administrative tasks only. Structured entities are characterised by features or attributes such as restricted activities, a narrow and well-defined objective and/or insufficient equity. In addition, structured entities may relate to financings in the form of multiple contractually linked instruments to investors that create concentrations of credit or other risks. Examples of structured entities are securitisation vehicles, asset-backed financings and some investment funds.

Aareal Bank Group mainly interacts with structured entities such as open-ended property funds and leased property companies. In this context, the Group provides financing to structured entities in the form of loans or guarantees. In the following table, strategic investments made by the Group are shown under "Other". The leased property companies were established by third parties for the financing of particular transactions and have the legal form of a German private limited company with a limited liability company as general partner (GmbH & Co KG). In the year under review and the previous year, Aareal Bank Group did not provide any non-contractual support for unconsolidated structured entities.

To the extent that this is relevant, the following table shows the carrying amounts of assets and liabilities recognised by Aareal Bank Group as at the reporting date as well as the existing off-balance sheet risk exposures that relate to unconsolidated structured entities. The carrying amounts of the assets and off-balance sheet items correspond to the Group's maximum loss exposure from interests in unconsolidated structured entities (without taking into account collateral). The size of the structured entities was determined on the basis of the net fund assets for open-ended property funds and other vehicles and on the basis of total assets for leased property companies.

31 December 2020

€ mn	Open-ended property funds	Leased property companies	Other	Total
Assets				
Loan receivables	31	17	4	**52**
Off-balance sheet exposures				
Loan commitments and guarantees (nominal value)	–	–	2	**2**
Size range of structured units	**€ 267 mn – € 1,053 mn**	**€ 4 mn – € 47 mn**	**€ 1 mn – € 18 mn**	

31 December 2019

€ mn	Open-ended property funds	Leased property companies	Other	Total
Assets				
Loan receivables	31	17	3	**51**
Off-balance sheet exposures				
Loan commitments and guarantees (nominal value)	–	–	2	**2**
Size range of structured units	**€ 167 mn – € 896 mn**	**€ 5 mn – € 47 mn**	**€ 1 mn – € 11 mn**	

(87) Disclosures on material non-controlling interests

The disposal of a minority stake of 30 % of the shares held in Aareon AG to Advent International, which was announced within the context of the strategic initiatives and measures as part of "Aareal Next Level", was completed on 31 October 2020. Voting rights are attached to the shares. Consolidated net income attributable to the non-controlling interest amounted to € 5 million. Aareon's segment assets (before consolidation) amount to € 380 million, comprising € 173 million in intangible assets, € 72 million in property and equipment, and € 92 million in financial assets. Assets are backed by equity of € 201 million. In addition, there are lease liabilities of € 62 million and € 54 million in provisions. For further details, please refer to the explanations in relation to the Aareon segment.

(88) Country-by-Country Reporting

The disclosure requirements refer to information on registered office, revenue, profit or loss, taxes on profit or loss, received government assistance as well as wage and salary earners of Aareal Bank AG, together with its foreign branches and domestic and foreign subsidiaries included in the reporting entity-structure, prior to consolidation.

For this purpose, the Bank's entities – subsidiaries as well as Aareal Bank AG's foreign branches – are allocated to our three business segments, Structured Property Financing, Consulting/Services Bank and Aareon.

Aareal Bank defines the branch offices' operating profit, which is used as a proxy for revenue, as the sum of the following consolidated income statement items (in accordance with IFRSs):

- Net interest income before loss allowance
- Net commission income
- Net derecognition gain or loss
- Net gain or loss from financial instruments (fvpl)
- Net gain or loss from hedge accounting
- Net gain or loss from investments accounted for using the equity method
- Net other operating income/expenses

Taxes disclosed are tax expenses in accordance with IFRSs.

The number of wage and salary earners relates to average full-time equivalent staff employed during the financial year.

The following overview shows all countries where Aareal Bank AG has offices, including foreign branches and subsidiaries. Please refer to the list of shareholdings as regards the allocation of individual subsidiaries to the relevant country of domicile. Aareal Bank AG's foreign branches are located in France, Ireland, Italy, Poland, Sweden and the UK.

2020

	Revenues	Profit/loss before taxes	Taxes on profit or loss	Number of wage and salary earners
	€ mn	€ mn	€ mn	Full-time equivalents
Structured Property Financing segment	**466**	**-99**	**-14**	**752**
Belgium	0	0	–	–
France	8	5	1	7
Germany	330	-40	1	660
Ireland	2	0	0	1
Italy	-12	-13	5	28
Poland	8	5	0	5
Singapore	5	3	0	6
Sweden	2	0	1	3
United Kingdom	46	-32	-23	6
US	83	-27	1	36
Consolidation	-6	–	–	–
Consulting/Services Bank segment	**57**	**-3**	**-1**	**265**
Germany	65	-3	-1	265
Consolidation	-8	–	–	–
Aareon segment	**215**	**27**	**9**	**1,595**
Finland	1	0	–	3
France	28	7	2	206
Germany	132	16	6	871
Netherlands	31	4	1	275
Norway	2	1	–	7
Romania	–	–	–	18
Sweden	10	-1	0	94
United Kingdom	11	0	–	121
Consolidation	–	–	–	–
Total	**738**	**-75**	**-6**	**2,612**

Government assistance was not received in the financial year 2020.

Aareal Bank Group's return on assets, calculated as the ratio of net profit to total assets, was -0.16 % as at the record date.

The previous Consulting/Services segment was split into the Consulting/Services Bank and Aareon segments in the financial year 2020. The previous year's figures were adjusted accordingly.

2019

	Revenues	Profit/loss before taxes	Taxes on profit or loss	Number of wage and salary earners
	€ mn	€ mn	€ mn	Full-time equivalents
Structured Property Financing segment	**612**	**276**	**95**	**804**
Belgium	1	1	–	–
France	6	1	1	7
Germany	419	223	70	710
Ireland	1	2	0	1
Italy	50	-62	0	31
Poland	9	5	2	5
Singapore	4	3	0	5
Spain	–	0	–	–
Sweden	4	2	1	3
United Kingdom	8	5	–	7
USA	118	96	21	35
Consolidation	-8	–	–	–
Consulting/Services Bank segment	**4**	**-65**	**-21**	**268**
Germany	8	-65	-21	268
Consolidation	-4	–	–	–
Aareon segment	**210**	**37**	**11**	**1,488**
Finland	–	0	–	3
France	28	7	3	193
Germany	129	23	8	819
Netherlands	32	6	–	266
Norway	3	3	0	5
Sweden	7	-2	0	78
United Kingdom	11	0	0	124
Consolidation	–	–	–	–
Total	**826**	**248**	**85**	**2,560**

(89) List of shareholdings

The list of shareholdings is prepared pursuant to section 313 (2) of the HGB. The disclosures in relation to the companies' equity and earnings are retrieved from the financial statements based on the respective local financial reporting principles.

31 December 2020

No.	Company name	Registered office	Shareholding	Equity	Results
			%	€ mn	€ mn
1	Aareal Bank AG	Wiesbaden			
	I. Fully-consolidated subsidiaries				
2	Aareal Bank Asia Ltd.	Singapore	100.0	SGD 28.3 mn	SGD 6.4 mn [1]
3	Aareal Beteiligungen AG	Frankfurt	100.0	167.0	0.0 [3]
4	Aareal Capital Corporation	Wilmington	100.0	USD 993.8 mn	USD 2.1 mn [4]
5	Aareal Estate AG	Wiesbaden	100.0	2.9	0.0 [3]
6	Aareal First Financial Solutions AG	Mainz	100.0	6.4	0.7 [3]
7	Aareal Gesellschaft für Beteiligungen und Grundbesitz Erste mbH & Co. KG	Wiesbaden	94.9	2.8	0.1 [1]
8	Aareal Holding Realty LP	Wilmington	100.0	USD 240.2 mn	USD -0.2 mn [4]
9	Aareal Immobilien Beteiligungen GmbH	Wiesbaden	100.0	437.1	0.0 [3]
10	Aareon AG	Mainz	70.0	170.7	11.2 [1]
11	Aareon Deutschland GmbH	Mainz	100.0	34.7	0.0 [3]
12	Aareon Finland Oy	Helsinki	100.0	0.2	-0.3 [2]
13	Aareon France S.A.S.	Meudon-la Forêt	100.0	10.5	4.5 [2]
14	Aareon Nederland B.V.	Emmen	100.0	28.4	2.2 [2]
15	Aareon Norge AS	Oslo	100.0	NOK 10.6 mn	NOK 4.9 mn [2]
16	Aareon Planungs- und Bestandsentwicklungs GmbH	Mainz	100.0	-0.3	-0.3 [1]
17	Aareon RELion GmbH	Augsburg	100.0	1.4	0.3 [1]
18	Aareon Sverige AB	Mölndal	100.0	SEK 57.8 mn	SEK 0.7 mn [2]
19	Aareon UK Ltd.	Coventry	100.0	GBP 4.8 mn	GBP 0.4 mn [2]
20	AV Management GmbH	Mainz	100.0	0.4	0.0 [3]
21	BauContact Immobilien GmbH	Wiesbaden	100.0	14.1	1.0 [1]
22	BauGrund Immobilien-Management GmbH	Bonn	100.0	0.5	0.0 [3]
23	BauGrund Solida Immobilien GmbH	Frankfurt	100.0	0.1	0.0 [1]
24	BauGrund TVG GmbH	Munich	100.0	0.1	0.0 [1]
25	BauSecura Versicherungsmakler GmbH	Hamburg	51.0	4.3	4.1 [1]
26	BVG – Grundstücks- und Verwertungsgesellschaft mit beschränkter Haftung	Frankfurt	100.0	152.3	0.0 [3]
27	CalCon Austria GmbH	Vienna	100.0	0.4	0.2 [1]
28	CalCon Deutschland GmbH	Munich	100.0	1.9	-0.4 [1]
29	CalCrom S.R.L.	Iasi	83.3	0.1	0.0 [1]
30	Cave Nuove S.p.A.	Rome	100.0	-36.6	-5.1 [1]
31	DBB Inka	Dusseldorf	100.0	100.2	0.1
32	Deutsche Bau- und Grundstücks-Aktiengesellschaft	Berlin	100.0	1.0	-0.9 [1]
33	Deutsche Structured Finance GmbH	Wiesbaden	100.0	2.5	-0.5 [1]

[1] Preliminary figures as at 31 December 2020; [2] Equity and results as at 31 December 2019;
[3] Profit and loss transfer agreement/control and profit transfer agreement; [4] Disclosures in accordance with IFRSs

>

No.	Company name	Registered office	Shareholding	Equity	Results
			%	€ mn	€ mn
34	DSF Flugzeugportfolio GmbH	Wiesbaden	100.0	0.0	0.0 [3]
35	DHB Verwaltungs AG	Wiesbaden	100.0	5.1	0.0 [3]
36	FIRE B.V.	Utrecht	60.0	0.0	0.0 [2]
37	GEV Besitzgesellschaft mbH	Wiesbaden	100.0	3.0	0.0 [3]
38	GEV Beteiligungsgesellschaft mbH	Wiesbaden	100.0	0.1	0.0 [1]
39	GVN-Grundstücks- und Vermögensverwaltungs-gesellschaft mit beschränkter Haftung	Frankfurt	100.0	0.2	0.0 [3]
40	IV Beteiligungsgesellschaft für Immobilieninvestitionen mbH	Wiesbaden	100.0	2.5	0.0 [1]
41	Izalco Spain S.L.	Madrid	100.0	10.3	-1.2 [1]
42	Jomo S.p.r.l.	Brussels	100.0	26.6	0.2 [1]
43	La Sessola Holding GmbH	Wiesbaden	100.0	86.6	0.0 [1]
44	La Sessola S.r.l.	Rome	100.0	90.7	-10.0 [1]
45	La Sessola Service S.r.l.	Rome	100.0	4.1	-4.4 [1]
46	Manager Realty LLC	Wilmington	100.0	USD 0.0 mn	USD 0.0 mn [4]
47	Mercadea S.r.l.	Rome	100.0	7.3	8.0 [1]
48	Mirante S.r.l.	Rome	100.0	4.6	-0.2 [1]
49	Northpark Realty LP	Wilmington	100.0	USD 93.8 mn	USD -32.8 mn [4]
50	Participation Achte Beteiligungs GmbH	Wiesbaden	100.0	3.3	0.0 [3]
51	Participation Elfte Beteiligungs GmbH	Wiesbaden	100.0	0.0	0.0 [3]
52	Participation Zehnte Beteiligungs GmbH	Wiesbaden	100.0	0.0	0.0 [3]
53	phi-Consulting GmbH	Bochum	100.0	0.2	0.0 [3]
54	Pisana S.p.A.	Rome	100.0	-6.0	-0.8 [1]
55	plusForta GmbH	Dusseldorf	100.0	0.2	0.0 [3]
56	Terrain-Aktiengesellschaft Herzogpark	Wiesbaden	100.0	4.7	0.0 [3]
57	Terrain Beteiligungen GmbH	Wiesbaden	94.0	59.0	1.4 [1]
58	Tintoretto Rome S.r.l.	Rome	100.0	2.5	-0.3 [1]
59	Westdeutsche Immobilien Servicing AG	Mainz	100.0	50.1	0.0 [3]
60	WP Galleria Realty LP	Wilmington	100.0	USD 136.3 mn	USD -1.8 mn [4]
	II. Joint arrangements				
61	Konsortium BauGrund/TREUREAL[5]	Bonn	50.0	0.0	-0.1 [1]
	III. Associates				
62	DSF PP Justizzentrum Thüringen GmbH & Co. KG	Bremen	48.4	0.3	0.0 [2]
63	Ecaria GmbH	Berlin	20.0	0.0	-0.1 [1]
64	Mount Street Group Limited	London	20.0	GBP -4.5 mn	GBP -6.2 mn [1]
65	objego GmbH	Essen	40.0	3.6	-2.5 [1]
66	OFI Group GmbH	Frankfurt	35.8	0.0	-1.3 [1]
67	Refurbio GmbH	Berlin	18.4	0.0	-0.1 [1]
68	Westhafen Haus GmbH & Co. Projektentwicklungs KG	Frankfurt	25.0	0.0	0.0 [2]
	IV. Other enterprises				
69	blackprint Booster Fonds International GmbH & Co. KG	Frankfurt	49.9	0.8	0.0 [2]
70	PropTech1 Fund I GmbH & Co. KG	Berlin	18.6	25.8	-0.9 [1]

[1] Preliminary figures as at 31 December 2020; [2] Equity and results as at 31 December 2019;
[3] Profit and loss transfer agreement/control and profit transfer agreement; [4] Disclosures in accordance with IFRSs [5] Joint operation

(90) Executive Bodies of Aareal Bank AG

The members of the Management Board and the Supervisory Board disclose their offices held, in accordance with the requirements set out in section 285 of the HGB and Article 435 (2) of Regulation (EU) No 575/2013, in conjunction with the EBA Guidelines on disclosure requirements under Part Eight of the CRR (EBA/GL/2016/11) and the EBA Guidelines on the assessment of the suitability of members of the management body and key function holders (EBA/GL/2017/12).

Composition of Supervisory Board's committees

Executive and Nomination Committee	
Marija Korsch	Chairman
Richard Peters	Deputy Chairman
Christof von Dryander	
Klaus Novatius	
Prof. Dr Hermann Wagner	

Remuneration Control Committee	
Marija Korsch	Chairman
Christof von Dryander	Deputy Chairman
Klaus Novatius	
Richard Peters	
Hans-Dietrich Voigtländer	

Risk Committee	
Sylvia Seignette	Chairman
Elisabeth Stheeman	Deputy Chairman
Jana Brendel	
Petra Heinemann-Specht	
Marija Korsch	
Prof. Dr Hermann Wagner	

Audit Committee	
Prof. Dr Hermann Wagner	Chairman
Hans-Dietrich Voigtländer	Deputy Chairman
Christof von Dryander	
Petra Heinemann-Specht	
Marija Korsch	
Richard Peters	

Technology and Innovation Committee	
Hans-Dietrich Voigtländer	Chairman
Jana Brendel	Deputy Chairman
Thomas Hawel	
Marija Korsch	
Jan Lehmann	
Elisabeth Stheeman	

Supervisory Board

Marija Korsch, Chairman of the Supervisory Board
Former partner of Bankhaus Metzler seel. Sohn & Co. Holding AG

Aareal Bank AG	Chairman of the Supervisory Board
Just Software AG	Member of the Supervisory Board
Nomura Financial Products Europe GmbH	Member of the Supervisory Board
(Offices held at other listed companies)	
Instone Real Estate Group N.V.	Member of the Supervisory Board
(Non-commercial mandates)	
FAZIT – Stiftung Gemeinnützige Verlagsgesellschaft mbH	Shareholder and member of the Advisory Board
Städelsches Kunstinstitut und Städtische Galerie	Member of the Administration
Gesellschaft der Freunde der Alten Oper Frankfurt e.V.	Deputy Chairman of the Management Board
Stiftung Centrale für private Fürsorge	Chairman of the Foundation's Executive Board
Institut für Bank- und Finanzgeschichte	Member of the Board of Trustees

Richard Peters, Deputy Chairman of the Supervisory Board
President and Chairman of the Management Board of Versorgungsanstalt des Bundes und der Länder

Aareal Bank AG	Deputy Chairman of the Supervisory Board
(Non-commercial mandates)	
VBLV e.V.	Chairman of the Management Board

>

Klaus Novatius*, Deputy Chairman of the Supervisory Board
Aareal Bank AG

Aareal Bank AG	Deputy Chairman of the Supervisory Board	

Jana Brendel
Chief Information Officer 1&1 Telecommunication SE

Aareal Bank AG	Member of the Supervisory Board	since 27 May 2020

Christof von Dryander
Senior Counsel (retired Partner), Cleary Gottlieb Steen & Hamilton LLP

Aareal Bank AG	Member of the Supervisory Board	since 27 May 2020
DWS Investment GmbH	Deputy Chairman of the Supervisory Board	
(Non-commercial mandates)		
Deutsche Bank Stiftung	Member of the Board	
Die Steinhausen-Stiftung	Member of the Board	
Frankfurter Bachkonzerte e.V.	Member of the Board	
Rotary Club Bad Homburg v.d.H.	Member of the Board	

Thomas Hawel*
Aareon Deutschland GmbH

Aareal Bank AG	Member of the Supervisory Board	
Aareon Deutschland GmbH (office held with Aareal Bank Group)	Deputy Chairman of the Supervisory Board	

Petra Heinemann-Specht*
Aareal Bank AG

Aareal Bank AG	Member of the Supervisory Board	

Jan Lehmann*
Aareon Deutschland GmbH

Aareal Bank AG	Member of the Supervisory Board	since 27 May 2020
Aareon Deutschland GmbH (office held with Aareal Bank Group)	Member of the Supervisory Board	

Sylvia Seignette, Chair of the Risk Committee
Former CEO for Germany and Austria, Crédit Agricole CIB (formerly Calyon)

Aareal Bank AG	Member of the Supervisory Board	

Elisabeth Stheeman
External Member of the Financial Policy Committee and the Financial Market Infrastructure Board, Bank of England, Prudential Regulation Authority

Aareal Bank AG	Member of the Supervisory Board	
(Offices held at other listed companies)		
Edinburgh Investment Trust Plc	Member of the Board of Directors	

Hans-Dietrich Voigtländer, Chair of the Technology and Innovation Committee
Associate Partner at BDG Innovation + Transformation GmbH & Co. KG

Aareal Bank AG	Member of the Supervisory Board	

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

Prof. Dr Hermann Wagner, Chairman of the Audit Committee
German Chartered Accountant, tax consultant

Aareal Bank AG	Member of the Supervisory Board	
btu beraterpartner Holding AG	Member of the Supervisory Board	until 6 April 2020
Squadra Immobilien GmbH & Co. KGaA	Chairman of the Supervisory Board	
(Offices held at other listed companies)		
PEH Wertpapier AG	Member of the Supervisory Board	
Capsensixx AG (subsidiary of PEH Wertpapier AG)	Member of the Supervisory Board	since 13 October 2020
Corestate Capital Holding S.A.	Deputy Chairman of the Supervisory Board	since 30 November 2020
Consus Real Estate AG ("Scale" segment of the Regulated Unofficial Market)	Member of the Supervisory Board	until 31 December 2020

(retired members)

Prof. Dr Stephan Schüller
Businessman; former spokesman of the General Partners of Bankhaus Lampe KG

Aareal Bank AG		until 27 May 2020

Dr Hans-Werner Rhein
German Lawyer (Rechtsanwalt)

Aareal Bank AG	Member of the Supervisory Board	until 27 May 2020

Beate Wollmann*
Aareon Deutschland GmbH

Aareal Bank AG	Member of the Supervisory Board	until 27 May 2020

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

Management Board

Hermann Josef Merkens, Chairman of the Management Board (CEO)
Group Strategy, Group Communications & Governmental Affairs, Group Human Resources & Infrastructure, Investor Relations (incl. Sustainability), Group Audit, Corporate Affairs (Legal, Board Office and Organisation Management)

Familienstiftung Becker & Kries	Member of the Board of Trustees	
(Offices held at companies of Aareal Bank Group)		
Aareal Estate AG	Chairman of the Supervisory Board	
Aareal Capital Corporation	Chairman of the Board of Directors	
Aareon AG	Deputy Chairman of the Supervisory Board	
Aareal Beteiligungen AG	Chairman of the Supervisory Board	

Marc Hess, Member of the Management Board (CFO)
Finance & Controlling, Treasury

(Offices held at companies of Aareal Bank Group)		
Aareon AG	Member of the Supervisory Board	
Aareal Beteiligungen AG	Member of the Supervisory Board	since 12 November 2020

>

Dagmar Knopek, Member of the Management Board (CLO)
Group Chief Lending Office (Credit Management, Workout, Valuation & Research)

HypZert GmbH	Chairman of the Supervisory Board

Christiane Kunisch-Wolff, Member of the Management Board (CRO)
Group Chief Risk Office (Risk Controlling, NFR, Compliance, Information Security & Data Protection, Regulatory Affairs)

Thomas Ortmanns, Member of the Management Board (CDO)
Group Business Consulting Services, Aareon, Group Technology

(Offices held at companies of Aareal Bank Group)

Aareon AG	Chairman of the Supervisory Board

Christof Winkelmann, Member of the Management Board (CMO)
Group Real Estate Structured Finance

(Offices held at companies of Aareal Bank Group)

Aareal Bank Asia Limited	Chairman of the Board of Directors	
Aareal Capital Corporation	Member of the Board of Directors	
La Sessola Service S.r.l.	Member of the Management Board	
La Sessola S.r.l.	Member of the Management Board	
Aareal Estate AG	Member of the Supervisory Board	since 3 December 2020

Wiesbaden, 2 March 2021

The Management Board

Hermann J. Merkens
(absent due to illness)

Marc Hess

Dagmar Knopek

Christiane Kunisch-Wolff

Thomas Ortmanns

Christof Winkelmann

Independent Auditors' Report

The following copy of the auditor's report also includes a "Report on the audit of the electronic renderings of the financial statements and the management report prepared for disclosure purposes in accordance with § 317 Abs. 3b HGB" ("Separate report on ESEF conformity"). The subject matter (ESEF documents to be audited) to which the separate report on ESEF conformity relates is not attached. The audited ESEF documents can be inspected in or retrieved from the Federal Gazette

To Aareal Bank AG, Wiesbaden

Report on the Audit of the Consolidated Financial Statements and of the Group Management Report

Audit Opinions

We have audited the consolidated financial statements of Aareal Bank AG, Wiesbaden, and its subsidiaries (the Group), which comprise the statement of financial position as at 31 December 2020, and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the financial year from 1 January through 31 December 2020 and notes to the consolidated financial statements, including a summary of significant accounting policies. In addition, we have audited the group management report of Aareal Bank AG for the financial year from 1 January to 31 December 2020. In accordance with the German legal requirements, we have not audited the content of those parts of the group management report listed in the "Other Information" section of our auditor's report.

In our opinion, on the basis of the knowledge obtained in the audit,

- the accompanying consolidated financial statements comply, in all material respects, with the IFRSs as adopted by the EU, and the additional requirements of German commercial law pursuant to § (Article) 315e Abs. (paragraph) 1 HGB (Handelsgesetzbuch: German Commercial Code) and, in compliance with these requirements, give a true and fair view of the assets, liabilities, and financial position of the Group as at 31 December 2020, and of its financial performance for the financial year from 1 January to 31 December 2020, and

- the accompanying group management report as a whole provides an appropriate view of the Group's position. In all material respects, this group management report is consistent with the consolidated financial statements, complies with German legal requirements and appropriately presents the opportunities and risks of future development. Our audit opinion on the group management report does not cover the content of those parts of the group management report listed in the "Other Information" section of our auditor's report.

Pursuant to § 322 Abs. 3 Satz (sentence) 1 HGB, we declare that our audit has not led to any reservations relating to the legal compliance of the consolidated financial statements and of the group management report.

Basis for the Audit Opinions

We conducted our audit of the consolidated financial statements and of the group management report in accordance with § 317 HGB and the EU Audit Regulation (No. 537/2014, referred to subsequently as "EU Audit Regulation") in compliance with German Generally Accepted Standards for Financial Statement Audits promulgated by the Institut der Wirtschaftsprüfer (Institute of Public Auditors in Germany) (IDW). We performed the audit of the consolidated financial statements in supplementary compliance with the International Standards on Auditing (ISAs). Our responsibilities under those requirements, principles and standards are further described in the "Auditor's Responsibilities for the Audit of the Consolidated Financial Statements and of the Group Management Report" section of our auditor's report. We are independent of the group entities in accordance with the requirements of European law and German commercial and professional law, and we have fulfilled our other German professional responsibilities in accordance with these requirements. In addition, in accordance with Article 10 (2) point (f) of the EU Audit Regulation, we declare that we have not provided non-audit services prohibited under Article 5 (1) of the EU Audit Regulation. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions on the consolidated financial statements and on the group management report.

Key Audit Matters in the Audit of the Consolidated Financial Statements

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the consolidated financial statements for the financial year from 1 January to 31 December 2020. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our audit opinion thereon; we do not provide a separate audit opinion on these matters.

In our view, the matters of most significance in our audit were as follows:

❶ Valuation of real estate loans in default
❷ Recoverability of properties acquired from previous loan exposures as reported under the property, plant and equipment and other assets balance sheet items

Our presentation of these key audit matters has been structured in each case as follows:

① Matter and issue
② Audit approach and findings
③ Reference to further information

Hereinafter we present the key audit matters:

❶ Valuation of real estate loans in default

① In the consolidated financial statements of Aareal Bank AG, € 1,5 billion in loans secured by real estate which met the definition for default applied by the bank in accordance with Article 178 of Regulation (EU) No 575/2013 (Capital Requirements Regulation, CRR) are reported as at 31 December 2020 (hereinafter referred to as "real estate loans in default"). The loan exposures in default are classified as stage 3 in accordance with IFRS 9. As of 31 December 2020, risk provisions totaling

€ 492 million were recognized to reflect them. The difficult macro-economic situation resulting from the global Covid-19 pandemic has affected borrowers and the real estate financed by Aareal Bank AG mostly on a non-recourse basis to differing degrees. As a result of this, certain types of properties (in particular hotels, shopping centers and student housing) in certain countries were affected by significant depreciation in the value of the financed properties. In instances where individual borrowers experienced additional payment difficulties over extended periods, this resulted in default within the meaning of Article 178 CRR. Aareal Bank AG analyzes its borrowers' financial circumstances, including based on the financial overviews, business and liquidity plans and lease overviews provided, and reviews the market values of the corresponding collateral, generally at least once per year. In order to account for the volatility caused by the pandemic, analyses and reviews were carried out mainly in the final months of the 2020 financial year. In the majority of cases, Aareal Bank AG obtains external valuations to determine the market values of the properties used as collateral. Property market values are calculated by appraisers in each case as the present values of future cash flows using the discounted cash flow method, with the appraisers deriving the assumptions about future cash flows that can be generated by the property using the information and business plans provided by the borrowers as well as their marked assessment, or determined on the basis of floor area-related comparative values. In addition, the appraisers assess the general conditions of the properties, existing opportunities and risks and the situation on the location and property type-specific real estate market in order to determine appropriate discount rates and benchmark yields. Based on the overall circumstances affecting the respective loan exposures, Aareal Bank AG then assesses whether the conditions under which a default is defined pursuant to Article 178 CRR are met. Specific valuation allowances are recognized for individual loans in default. In calculating the specific valuation allowance for real estate loans in default, the executive directors, taking into account external appraisals, make assumptions relating to cash flows, completion and realization, as well as estimates relating to the likelihood of scenarios occurring. Since even relatively small changes in these assumptions have a significant influence on the associated collateral value and the measurements of the loans and advances are subject to uncertainties in this regard, this matter was of particular significance in the context of our audit.

② As part of our audit we evaluated, inter alia, the statements in the available documentation for a risk-focused sample of loan exposures with respect to the borrower's financial circumstances, the recoverability of the related collateral and the application of the definition of default applied by the Bank. We evaluated the valuations performed by the appraisers and their review by Aareal Bank AG in terms of their suitability, up-to-dateness and methodology, as well as the transparency of the value calculation. At the same time, we gained an understanding of the original data, value parameters and assumptions on which the valuations and their review by Aareal Bank AG were based, evaluated these critically and assessed whether they were within a justifiable range. In individual cases, we sought to discuss individual aspects affecting the valuation with the appraisers. In addition, we based our assessment of the executive directors' assumptions concerning cash flow, completion and realization on general and sector-specific market expectations as well as on documentation and explanations from the executive directors about expected cash inflows and outflows as well as assumptions concerning the probability of scenarios. Furthermore, we examined the relevant credit processes in the Aareal Bank AG's internal control in terms of the appropriateness of their design, and tested their effectiveness. Based on the available information and taking into account the particular economic environment resulting from the Covid-19 pandemic, our audit found that the assumptions made by the executive directors in testing the real estate loans in default for impairment, and the processes applied, are justifiable.

③ Please refer to sections 9, 32, 43 and 62 of the notes for information on the risk provisions.

❷ Recoverability of properties acquired from previous loan exposures as reported under the property, plant and equipment and other assets balance sheet items

① In the consolidated financial statements of Aareal Bank AG, real estate acquired from former loan exposures amounting to € 124 million are reported under the "Property and equipment" balance sheet item and € 326 million are reported under the "Other assets" balance sheet item at 31 December 2020. The properties were acquired by the Aareal Bank AG through fully consolidated real estate special purpose entities. Aareal Bank AG tests the properties acquired from former credit exposures at least once a year for impairment using external valuations. The market values of the properties are calculated in each case as the present values of future cash flows using the discounted cash flow method, with the appraisers deriving the assumptions about future cash flows using the information and projections provided by the executive directors and their market assessment, or determined on the basis of floor area-related comparative values. In addition, the appraisers assessed the general conditions of the properties, existing opportunities and risks and the situation on the location and property type-specific real estate market in order to determine appropriate discount rates and benchmark yields. In addition, the executive directors made assumptions relating to completion, leasing and marketing measures taking into account the external appraisals. Since even relatively small changes in these assumptions have a significant influence on the market values of the properties, and the measurements are subject to estimation uncertainties, this matter was of particular significance in the context of our audit.

② As part of our audit, we particularly evaluated the valuations performed by the external appraisers in terms of their up-to-dateness and methodology, as well as the transparency of the value calculation. At the same time we gained an understanding of the material original data, value parameters and assumptions on which the valuations were based, evaluated these critically and assessed whether they were within a justifiable range. In this context we involved our own real estate experts. In addition, we based our assessment of the cash flow, completion, leasing and marketing assumptions made by the executive directors on, inter alia, a comparison with general and sector-specific market expectations as well as on documentation and explanations from the executive directors about expected cash flows. Furthermore, we evaluated the classification of the properties and, therwith, the respective accounting policies to be applied under IAS 2 and IAS 16. Based on the available information and taking into account the particular economic environment resulting from the Covid-19 pandemic, our audit found that the material assumptions made by the executive directors for testing the impairment of the properties acquired from former loan exposures and the classifications applied are justifiable.

③ We refer to the Company's disclosures on property, plant and equipment and other assets contained in notes 19, 22, 48 and 51 in the notes to the consolidated financial statements.

Other Information

The executive directors are responsible for the other information. The other information comprises the following non-audited parts of the group management report:

- the statement on corporate governance pursuant to § 289f HGB and § 315d HGB included in section "Corporate Governance Statement" of the group management report
- the separate non-financial report pursuant to § 289b Abs. 3 HGB and § 315b Abs. 3 HGB

The other information comprises further the remaining parts of the annual report – excluding cross-references to external information – with the exception of the audited consolidated financial statements, the audited group management report and our auditor's report.

Our audit opinions on the consolidated financial statements and on the group management report do not cover the other information, and consequently we do not express an audit opinion or any other form of assurance conclusion thereon.

In connection with our audit, our responsibility is to read the other information and, in so doing, to consider whether the other information

- is materially inconsistent with the consolidated financial statements, with the group management report or our knowledge obtained in the audit, or
- otherwise appears to be materially misstated.

If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of the Executive Directors and the Supervisory Board for the Consolidated Financial Statements and the Group Management Report

The executive directors are responsible for the preparation of the consolidated financial statements that comply, in all material respects, with IFRSs as adopted by the EU and the additional requirements of German commercial law pursuant to § 315e Abs. 1 HGB and that the consolidated financial statements, in compliance with these requirements, give a true and fair view of the assets, liabilities, financial position, and financial performance of the Group. In addition, the executive directors are responsible for such internal control as they have determined necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, the executive directors are responsible for assessing the Group's ability to continue as a going concern. They also have the responsibility for disclosing, as applicable, matters related to going concern. In addition, they are responsible for financial reporting based on the going concern basis of accounting unless there is an intention to liquidate the Group or to cease operations, or there is no realistic alternative but to do so.

Furthermore, the executive directors are responsible for the preparation of the group management report that as a whole provides an appropriate view of the Group's position and is, in all material respects, consistent with the consolidated financial statements, complies with German legal requirements, and appropriately presents the opportunities and risks of future development. In addition, the executive directors are responsible for such arrangements and measures (systems) as they have considered necessary to enable the preparation of a group management report that is in accordance with the applicable German legal requirements, and to be able to provide sufficient appropriate evidence for the assertions in the group management report.

The supervisory board is responsible for overseeing the Group's financial reporting process for the preparation of the consolidated financial statements and of the group management report.

Auditor's Responsibilities for the Audit of the Consolidated Financial Statements and of the Group Management Report

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and whether the group management report as a whole provides an appropriate view of the Group's position and, in all material respects, is consistent with the consolidated financial statements and the knowledge obtained in the audit, complies with the German legal requirements and appropriately presents the opportunities and risks of future development, as well as to issue an auditor's report that includes our audit opinions on the consolidated financial statements and on the group management report.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with § 317 HGB and the EU Audit Regulation and in compliance with German Generally Accepted Standards for Financial Statement Audits promulgated by the Institut der Wirtschaftsprüfer (IDW) and supplementary compliance with the ISAs will always detect a material misstatement Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements and this group management report.

We exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements and of the group management report, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our audit opinions. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal controls.

- Obtain an understanding of internal control relevant to the audit of the consolidated financial statements and of arrangements and measures (systems) relevant to the audit of the group management report in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an audit opinion on the effectiveness of these systems.

- Evaluate the appropriateness of accounting policies used by the executive directors and the reasonableness of estimates made by the executive directors and related disclosures.

- Conclude on the appropriateness of the executive directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in the auditor's report to the related disclosures in the consolidated financial statements and in the group management report or, if such disclosures are inadequate, to modify our respective audit opinions. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to be able to continue as a going concern.

- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements present the underlying transactions and events in a manner that the consolidated financial statements give a true and fair view of the assets, liabilities, financial position and financial performance of the Group in compliance with IFRSs as adopted by the EU and the additional requirements of German commercial law pursuant to § 315e Abs. 1 HGB.

- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express audit opinions on the consolidated financial statements and on the group management report. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinions.

- Evaluate the consistency of the group management report with the consolidated financial statements, its conformity with German law, and the view of the Group's position it provides.

- Perform audit procedures on the prospective information presented by the executive directors in the group management report. On the basis of sufficient appropriate audit evidence we evaluate, in particular, the significant assumptions used by the executive directors as a basis for the prospective information and evaluate the proper derivation of the prospective information from these assumptions. We do not express a separate audit opinion on the prospective information and on the assumptions used as a basis. There is a substantial unavoidable risk that future events will differ materially from the prospective information.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with the relevant independence requirements, and communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, the related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter.

Other Legal and Regulatory Requirements

Assurance Report in Accordance with § 317 Abs. 3b HGB on the Electronic Reproduction of the Consolidated Financial Statements and the Group Management Report Prepared for Publication Purposes

Reasonable Assurance Conclusion

We have performed an assurance engagement in accordance with § 317 Abs. 3b HGB to obtain reasonable assurance about whether the reproduction of the consolidated financial statements and the group management report (hereinafter the "ESEF documents") contained in the attached electronic file Aareal Bank_AG_KA+KLB_ESEF-2020-12-31.zip and prepared for publication purposes complies in all material respects with the requirements of § 328 Abs. 1 HGB for the electronic reporting format ("ESEF format").

In accordance with German legal requirements, this assurance engagement only extends to the conversion of the information contained in the consolidated financial statements and the group management report into the ESEF format and therefore relates neither to the information contained within this reproduction nor to any other information contained in the above-mentioned electronic file.

In our opinion, the reproduction of the consolidated financial statements and the group management report contained in the above-mentioned attached electronic file and prepared for publication purposes complies in all material respects with the requirements of § 328 Abs. 1 HGB for the electronic reporting format. We do not express any opinion on the information contained in this reproduction nor on any other information contained in the above-mentioned electronic file beyond this reasonable assurance conclusion and our audit opinion on the accompanying consolidated financial statements and the accompanying group management report for the financial year from 1 January to 31 December 2020 contained in the "Report on the Audit of the Consolidated Financial Statements and on the Group Management Report" above.

Basis for the Reasonable Assurance Conclusion

We conducted our assurance engagement on the reproduction of the consolidated financial statements and the group management report contained in the above-mentioned attached electronic file in accordance with § 317 Abs. 3b HGB and the Exposure Draft of IDW Assurance Standard: Assurance in Accordance with § 317 Abs. 3b HGB on the Electronic Reproduction of Financial Statements and Management Reports Prepared for Publication Purposes (ED IDW AsS 410) and the International Standard on Assurance Engagements 3000 (Revised). Accordingly, our responsibilities are further described below in the "Group Auditor's Responsibilities for the Assurance Engagement on the ESEF Documents" section. Our audit firm has applied the IDW Standard on Quality Management: Requirements for Quality Management in the Audit Firm (IDW QS 1).

Responsibilities of the Executive Directors and the Supervisory Board for the ESEF Documents

The executive directors of the Company are responsible for the preparation of the ESEF documents including the electronic reproduction of the consolidated financial statements and the group management report in accordance with § 328 Abs. 1 Satz 4 Nr. 1 HGB and for the tagging of the consolidated financial statements in accordance with § 328 1 Satz 4 Nr. 2 HGB.

In addition, the executive directors of the Company are responsible for such internal control as they have considered necessary to enable the preparation of ESEF documents that are free from material noncompliance with the requirements of § 328 Abs. 1 HGB for the electronic reporting format, whether due to fraud or error.

The executive directors of the Company are also responsible for the submission of the ESEF documents together with the auditor's report and the attached audited consolidated financial statements and audited group management report as well as other documents to be published to the operator of the German Federal Gazette (Bundesanzeiger).

The Supervisory board is responsible for overseeing the preparation of the ESEF documents as part of the financial reporting process.

Group Auditor's Responsibilities for the Assurance Engagement on the ESEF Documents

Our objective is to obtain reasonable assurance about whether the ESEF documents are free from material non-compliance with the requirements of § 328 Abs. 1 HGB, whether due to fraud or error. We exercise professional judgment and maintain professional skepticism throughout the assurance engagement. We also:

- Identify and assess the risks of material non-compliance with the requirements of § 328 Abs. 1 HGB, whether due to fraud or error, design and perform assurance procedures responsive to those risks, and obtain assurance evidence that is sufficient and appropriate to provide a basis for our assurance conclusion.
- Obtain an understanding of internal control relevant to the assurance engagement on the ESEF documents in order to design assurance procedures that are appropriate in the circumstances, but not for the purpose of expressing an assurance conclusion on the effectiveness of these controls.
- Evaluate the technical validity of the ESEF documents, i.e., whether the electronic file containing the ESEF documents meets the requirements of the Delegated Regulation (EU) 2019/815 in the version applicable as at the balance sheet date on the technical specification for this electronic file.
- Evaluate whether the ESEF documents enables a XHTML reproduction with content equivalent to the audited consolidated financial statements and to the audited group management report.
- Evaluate whether the tagging of the ESEF documents with Inline XBRL technology (iXBRL) enables an appropriate and complete machine-readable XBRL copy of the XHTML reproduction.

Further Information pursuant to Article 10 of the EU Audit Regulation

We were elected as group auditor by the annual general meeting on 27 May 2020. We were engaged by the supervisory board on 2 June 2020. We have been the group auditor of Aareal Bank AG, Wiesbaden, and its legal predecessors without interruption since the financial year 1976.

We declare that the audit opinions expressed in this auditor's report are consistent with the additional report to the audit committee pursuant to Article 11 of the EU Audit Regulation (long-form audit report).

German Public Auditor Responsible for the Engagement

The German Public Auditor responsible for the engagement is Christian F. Rabeling.

Frankfurt/Main, 3 March 2021

PricewaterhouseCoopers GmbH
Wirtschaftsprüfungsgesellschaft

sgd. Ralf Schmitz	**sgd. Christian F. Rabeling**
Wirtschaftsprüfer	**Wirtschaftsprüfer**
(German Public Auditor)	**(German Public Auditor)**

Responsibility Statement

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

Wiesbaden, 2 March 2021

The Management Board

Hermann J. Merkens
(absent due to illness)

Marc Hess

Dagmar Knopek

Dagmar Knopek

Christiane K.-Wolff

Christiane Kunisch-Wolff

Thomas Ortmanns

Thomas Ortmanns

Christof Winkelmann

Christof Winkelmann

Responsible and transparent corporate governance is of great importance to Aareal Bank AG, and is considered the essence of prudent commercial conduct by both the Management Board and the Supervisory Board.

Transparency

Corporate Governance Statement pursuant to Sections 289f and 315d of the German Commercial Code (HGB) / Corporate Governance Report

Declaration of Compliance in accordance with Section 161 of the AktG

The Management Board and Supervisory Board of Aareal Bank AG declare, in accordance with section 161 of the AktG, that:

1. Aareal Bank AG has complied with the recommendations of the Government Commission "German Corporate Governance Code" (as amended and published in the German Federal Gazette on 24 April 2017) – except for the restriction set out below – since the last Declaration of Compliance was issued in December 2019:

   Pursuant to section 25d of the German Banking Act (Kreditwesengesetz – "KWG"), the Executive and Nomination Committee of Aareal Bank AG's Supervisory Board is required to assume additional tasks which are not supposed to be prepared by shareholder representatives on the Supervisory Board alone. Hence, the Executive and Nomination Committee also includes employee representative members, in contravention of the recommendation in section 5.3.3 of the German Corporate Governance Code (the "Code"). However, the Committee will ensure that the nomination of candidates for election by the Annual General Meeting will be determined exclusively by shareholder representatives on the Committee.

2. Since 20 March 2020, all recommendations of the Government Commission "German Corporate Governance Code" (as amended and published in the German Federal Gazette on 20 March 2020) have been complied with – except for the restriction set out below:

   Pursuant to recommendation G. 10 sentence 2, Management Board members shall have access to granted long-term variable remuneration components only after a period of four years. In contrast to the draft version dated 22 May 2019, the Government Commission refrained from defining the term "long-term variable remuneration" in its final version.

   According to the definition in the version dated 22 May 2019, typical performance indicators for long-term variable remuneration were, inter alia, "long-term financial success (profitability and growth with multiple-year measurement basis), non-financial success as prerequisite for subsequent financial success […], implementation of the corporate strategy [etc.]."

   Within Aareal Bank's remuneration system, all targets are derived from the strategy and measured over a period of three years. In line with the definition provided in the draft version dated 22 May 2019, Aareal Bank's entire variable remuneration would classify as long-term. The three-year target determination yields an imputed amount of which only 20 % is paid out directly, whereas the remaining 80 % is paid out in several tranches and over a period of six years.

This means that most of the long-term variable remuneration is accessible at the earliest after four years and at the latest after nine years, thus complying with the Code's draft version. However, in the absence of the definition having been adopted and the associated imprecise recommendation it is not clear whether Aareal Bank's remuneration structure meets the Code expectations. As a result, and as a precautionary measure, we declare a deviation from rec-ommendation G. 10 sentence 2.

Wiesbaden, December 2020

The Management Board

Hermann J. Merkens
(absent due to illness)

Marc Hess

Dagmar Knopek

Christiane Kunisch-Wolff

Thomas Ortmanns

Christof Winkelmann

For the Supervisory Board

Marija Korsch (Chairman)

Corporate Governance at Aareal Bank Group

Aareal Bank Group is managed by the parent company Aareal Bank AG. Aareal Bank is a listed bank, which by virtue of being classified as "significant", is supervised directly by the European Central Bank. Although the Management Board and the Supervisory Board of Aareal Bank AG are required to observe a large number of specific corporate governance rules, their common understanding does not end at compliance with these rules. They also discuss on a regular basis the application of voluntary standards that are recommended by the Code, the supervisory authorities, Aareal Bank shareholders or due to international best practice, or that arise for the Supervisory Board and the Management Board in their day-to-day work.

The top priority of the Management Board and the Supervisory Board is to act in the interests of the Company and hence to meet their responsibility vis-à-vis the employees, customers, shareholders and the public alike.

Disclosures regarding Corporate Governance standards

To discharge its responsibility, senior management aligns corporate governance with legal and regulatory rules, as well as a comprehensive set of internal rules and regulations, which provide concrete guidance on the conduct and processing of the Bank's business, in line with our ethical responsibility. These documents comprise the Memorandum and Articles of Association, the Rules of Procedure for the Supervisory Board and the Management Board, the strategies, the Risk Appetite Framework, the Internal Governance Policy, and the Code of Conduct; all members of staff have access to the documents, via common internal communications channels such as the Bank's Intranet. Memorandum and Articles of Association, Code of Conduct, and Rules of Procedure for the Supervisory Board are also accessible via Aareal Bank's website.

Aligning with the German Corporate Governance Code's guiding principle

The Management Board and the Supervisory Board follow their own value structure and that of Aareal Bank, as well as the "honourable businessperson" concept and the German Corporate Governance Code's principles of good corporate governance. The Declaration of Compliance pursuant to section 161 of the AktG lays out to what extent the recommendations were complied with, or shall be complied with.

Furthermore, since 1 January 2021 the Management Board and Supervisory Board have also reported whether they comply with the Code's suggestions, stating the reasons for failing to do so if applicable. Other than the following exception/restriction, the Management Board and the Supervisory Board comply with the suggestions:

- Contrary to the suggestion made in G. 14 of the Code, Management Board members' service contracts continue to contain rules governing severance pay in the event of a change of control. Any severance payment made shall not exceed twice the annual remuneration (severance cap) and shall not constitute remuneration for more than the remaining term of the employment contract.

- In line with D. 8 sentence 2, participation in Supervisory Board meetings by video or telephone conference should not be the rule. To protect Supervisory Board members, employees and Management Board members of Aareal Bank from a potential SARS-CoV-2 infection, most Supervisory Board meetings in 2020 were held virtually. As soon as developments concerning the coronavirus pandemic reasonably allow it, the Supervisory Board intends to resume personal attendance for members at meetings.

According to Code recommendation F. 4, companies shall specify, in the Corporate Governance Statement, what Code recommendations were not applicable due to overriding legal stipulations.

- This applies to Code recommendation D. 5, according to which the Nomination Committee shall be composed exclusively of shareholder representatives. The Nomination Committee of a credit institution is regulated separately in the KWG. Pursuant to section 25d of the KWG, the Nomination Committee of Aareal Bank AG's Supervisory Board is required to assume additional tasks which are not supposed to be prepared by shareholder representatives on the Supervisory Board alone. Hence, the Executive and Nomination Committee of Aareal Bank AG also includes employee representative members. However, the Committee will ensure that the nomination of candidates for election by the Annual General Meeting will be determined exclusively by shareholder representatives on the Committee.

Sustainability approach

Contributing to sustainable economic development is a priority for Aareal Bank Group. As a partner to the property industry, Aareal Bank Group is thus pursuing a business strategy appropriate to the requirements of the sector and the stakeholders. The Group is aware of the responsibility associated with its sustainability mission statement and the need to focus on the needs of society, and aims to preserve the foundations on which future generations can base and shape their lives.

The sustainability mission statement, which is supported by an integrated sustainability management system, is an integral part of the corporate strategy, providing a summary of the corporate responsibility principles of Aareal Bank Group that are aligned with our objective of doing business sustainably:

- Our thinking is integrated and future-oriented, taking ethical, societal and ecological topics into account.

- We analyse trends holistically, evaluate the resulting opportunities and risks, and align our forward-looking sustainability programme with this.

- We focus on all relevant stakeholder groups, seek to engage in active dialogue with them in a variety of ways and show how we make use of the insights we have gained.

- We make sure that business decisions take account of ecological, social and governance factors, and communicate our progress and the challenges we face transparently and credibly.

- We set priorities and implement our decisions, thereby reinforcing corporate sustainability values such as reliability, innovative ability, integrity and compliance, our appeal as an employer, and an emphasis on building and maintaining high-trust client relationships.

In doing so, we are guided by national and international frameworks, we commit to initiatives or have joined organisations that represent generally accepted ethical standards and whose values we share. Relevant organisations here include:

- United Nations Global Compact
- International Labor Organization
- German Corporate Governance Code
- Diversity Charter
- Work-Care Balance Charter

At an organisational level, Aareal Bank Group has assigned responsibility for sustainability management to the Chairman of the Management Board. In this way, Aareal Bank Group emphasises the strategic importance of sustainability for its corporate philosophy and steers its practical implementation at the highest level. Established now since 2012, the Sustainability Committee supports the Management Board in the ongoing development of the sustainability programme and in coordinating the Group-wide sustainability activities. It includes representatives from all key divisions.

Further details can be found in the latest Sustainability Report: www.aareal-bank.com/en/investors-portal/finance-information/sustainability-reports/archive

Code of Conduct

We believe that the principles of integrity and responsible conduct must be observed by the members of the Management Board and the Supervisory Board, and by all our employees across the Company, regardless of their functions and duties. Our internal Code of Conduct therefore contains binding rules governing the legal and ethical conduct of employees vis-à-vis clients, business partners, and colleagues. Aareal Bank Group's efforts in this context are also motivated by the desire to affirm and further strengthen the confidence placed by stakeholders – our clients, investors, and staff: www.aareal-bank.com/fileadmin/downloadlist/DAM_Content/Code_of_Conduct_en.pdf

Principles of diversity

The Management Board and the Supervisory Board are openly committed to diversity throughout the entire Aareal Bank Group.

Aareal Bank defines diversity as:

- The appreciation that every individual is unique, and the respect for this uniqueness
- 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.

The goals are to promote Aareal Bank Group's image as a modern employer, to strengthen employee commitment and increase employee motivation, to ensure skills and competencies are fostered individually in a way that promotes employee performance, to react to demographic change and an ageing workforce, and to take into account individual circumstances and stages of life.

In order to highlight the significance of diversity, and to 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 the German industry in 2006) in 2013.

Aareal Bank employs people from more than 30 different countries. At Aareal Bank's foreign locations, we take care to ensure that positions are primarily filled by local staff if possible. Aareal Bank Group attaches great importance to the equal treatment of women and men, whether in the context of filling vacant positions, with regard to continuous professional development, or in terms of remuneration. Specifically, any vacancies below senior executive level are generally published throughout the Company, in the form of job advertisements that all members of staff – male or female – may apply for. When setting the remuneration of employees, we do not differentiate by gender but rely exclusively on aspects such as qualification, professional experience or training.

In accordance with the German Act on Equal Participation of Men and Women in Executive Positions in the Private and Public Sector (Gesetz für die gleichberechtigte Teilhabe von Frauen und Männern an Führungspositionen in der Privatwirtschaft und im öffentlichen Dienst), the Management Board sets specific targets – including concrete implementation deadlines – for the share of women holding executive positions on the first two management levels below the Management Board of Aareal Bank AG. On the first management level below the Management Board, by 30 June 2022 at least 13.5 % of executive positions are to be held by women; on 31 December 2020, the share of female managers on this level was 14.7 % (2019: 16.2 %). On the second management level below the Management Board, by 30 June 2022 at least 21.1 % of executive positions are to be held by women; on 31 December 2020, the share of female managers on this level was 23.1 % (2019: 23.7 %).

Across Aareal Bank Group, the share of women in executive positions stood at 24.6 % (2019: 23.8 %); at Aareal Bank AG, it was 21.6 % (2019: 21.9 %), and at Aareon, it was 25.5 % (2019: 24.1 %), with women accounting for 37.6 % of Aareal Bank Group's entire workforce as at 31 December 2020

(2019: 36.8 % – Aareal Bank AG: 42.5 % (2019: 41.9 %); Aareon: 34.4 % (2019: 33.1 %).

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

Inclusion

Severely disabled persons made up 5 % of Aareal Bank's staff base in 2020 (2019: 4.8 %). This employee group is represented in the Group's German entities by a disability representative.

Working practices of the Management Board and the Supervisory Board

The Management Board is responsible for managing the Company and for its strategic orientation, material transactions and proper organisation. This also includes the implementation of effective monitoring systems. It focuses its business activities upon the Company's long-term and sustainable development. Its decisions incorporate the long-term consequences of its actions and are guided by the ethical principles of Aareal Bank Group (see relevant corporate governance principles).

Supervisory Board

The Supervisory Board exercises its control using different instruments. On the one hand, it sets out the reporting requirements of the Management Board in its internal Rules of Procedure, to ensure comprehensive and prompt reporting. These reports include the financial reports prior to being published, the reports of Internal Audit, Risk Controlling and Compliance, as well as the external auditor's reports. It also determines the transactions of the Management Board in its internal Rules of Procedure, where its approval is required.

Furthermore, the Supervisory Board contributes to the sustainable success of Aareal Bank Group – in the interest of investors, clients, staff, and the general public – by selecting suitable Management Board members (as set out in the Guidelines for the Selection of Members of the Supervisory Board and Management Board), a Management Board remuneration system which is aligned with the Company's long-term and sustainable interests (as set out in the Remuneration Report), and the effective supervision of this remuneration system.

The Supervisory Board has established five committees in order to perform its supervisory duties in an efficient manner: the Executive and Nomination Committee, the Remuneration Control Committee, the Risk Committee, the Audit Committee, and the Technology and Innovation Committee. An overview of the respective committee members can be found in the Notes: www.aareal-bank.com/en/investors-portal/finance-information/financial-reports/archive

Executive and Nomination Committee

The Executive and Nomination Committee prepares the plenary meetings of the Supervisory Board, together with proposed resolutions. In particular, it supports the Supervisory Board in advising and monitoring the strategy via a regular strategy dialogue. The Committee's area of responsibility also includes assessing the internal condition of the Group, corporate governance, and issues concerning personnel planning for the Management Board (also regarding the contracts with individual Management Board members, based on the remuneration system prepared by the Remuneration Control Committee and adopted by the plenary meeting of the Supervisory Board). The Executive and Nomination Committee compiles profiles defining the requirements for members of the Management Board and the Supervisory Board and supports the Supervisory Board in selecting suitable candidates, considering personal and professional requirements as well as its targets for the composition of both bodies, including the diversity concept. Based on an at least annual evaluation, it determines the extent to which the members of the Management Board or Supervisory Board have a need for further training, or whether other adjustments are required. Furthermore, the Executive and Nomination Committee monitors, and resolves if necessary, decision proposals regarding loans to senior managers and other related party transactions. The Executive and Nomination Committee is also responsible for the assessment and handling of conflicts of interest in line with the Conflicts of Interest Policy.

The Executive and Nomination Committee, excluding the employee representatives, discusses the nomination of shareholder representatives for election by the Annual General Meeting.

Remuneration Control Committee

The Remuneration Control Committee monitors whether the structure of the remuneration systems for Management Board members and employees is appropriate, taking into account the impact of remuneration systems on Aareal Bank's overall risk profile. The Remuneration Control Committee prepares corresponding proposals concerning remuneration (including for members of the Management Board) for the plenary meeting of the Supervisory Board. The Remuneration Control Committee receives the information provided by Aareal Bank's Remuneration Officer, as well as the information on the remuneration system intended for disclosure. For further details, please refer to the section on remuneration governance in the Remuneration Report.

Risk Committee

The Risk Committee deals with all material types of risk Aareal Bank is exposed to in its business activities. Along with the Supervisory Board in its entirety, it is also the recipient of the risk reports (please refer to the Risk Report). The material risk types comprise financial and non-financial types of risk alike, including IT-related risks. The Committee is also responsible for reviewing the contents of the risk strategies in accordance with the MaRisk, for checking conformity with the business strategy, and preparing the corresponding resolutions of the Supervisory Board. It furthermore advises the Management Board on how to design an appropriate and effective risk management system, making sure that the Bank's risk-bearing capacity is adequate. To achieve this, the Committee monitors the Management Board, especially as regards determining risk appetite and the corresponding limits.

Audit Committee

The Audit Committee is concerned with all accounting issues, as well as regarding the audit of Aareal Bank AG and Aareal Bank Group. The Committee is responsible for the preparation and conduct of the audit of the financial statements and the consolidated financial statements; it prepares the decisions to be taken by the Supervisory Board on the basis of the Committee's analysis of the external auditors' reports. For this purpose, the Committee reports to the plenary meeting of the Supervisory Board on the results of its analysis and the assessments derived. Preparing the audit of the financial statements also comprises the preparations for instructing the external auditors (by virtue of the corresponding resolution passed by the Annual General Meeting), verifying the independence of the external auditors, including the approval of permissible non-audit services, negotiating the auditors' fees, determining focal points of the audit, and regularly selecting new external auditors. The Audit Committee also discusses quarterly and half-yearly financial reports with the Management Board, and obtains the external auditors' report on their review of the half-yearly report. Furthermore, the Audit Committee is responsible for examining the projections submitted by the Management Board. In addition, Compliance and Internal Audit address their reports to the Committee. The Committee is also responsible for monitoring the effectiveness of the internal control and monitoring system.

Technology and Innovation Committee

The Committee deals with issues concerning information technology used within the Company, and with issues related to IT products created and distributed by Aareal Bank Group entities. This comprises the Bank's as well as Aareon's products. As part of these duties, the Committee monitors the implementation of Aareal Bank Group's digitalisation strategy which calls not only for a technical transformation, but also for modern and agile working practices and project methods.

Working relationship between the Management Board and Supervisory Board

The working relationship between Management Board and Supervisory Board is characterised by trust and a constructive, yet critical dialogue – during Supervisory Board meetings and outside of them. Discussions during meetings are held in an adequate and target-oriented working atmosphere. Meetings also take place without the Management Board present, for example when talking about personnel matters, Management Board remuneration, evaluation results, and individual business-related or strategic aspects.

Outside meetings, it is mainly the Chairman of the Supervisory Board and committee chairmen that communicate with the competent Management Board members. The Chairman of the Supervisory Board regularly discusses questions regarding the strategy, business development, risk situation, risk management, compliance, as well as personnel- and remuneration-related matters with the Chairman of the Management Board. The Chairman of the Risk Committee goes into detail – especially with the Chief Risk Officer – on topics such as risk situation, risk management, and risk strategies. The Chairman of the Audit Committee also regularly exchanges views with the Chief Risk Officer, but also with the Chief Financial Officer and the external auditors; finally, the Chairman of the Technology and Innovation Committee keeps in touch with the Chief Digitalisation Officer outside meetings. The chairmen inform the other Supervisory Board members about the key points of these discussions at the next committee meeting.

Communications

Aareal Bank assigns great importance to extensive communications with all of the Bank's stakeholders. It has set itself the target of actively, transparently and openly communicating with all stakeholders, taking into account the interests of all stakeholders.

All press releases, ad-hoc disclosures, corporate presentations, as well as annual, sustainability and quarterly reports published by Aareal Bank are available on the Bank's website to any interested person, and may be downloaded from there. In addition, the financial calendar is updated regularly, and provides information about upcoming events.

Aareal Bank publishes details on its financial position and performance five times annually. On these occasions, the Management Board gives a personal account of results, within the scope of press and analysts' conferences, as well as issuing press releases.

All information can be found on Aareal Bank's website: www.aareal-bank.com/en/investors-portal/

Relationship to shareholders

To facilitate direct communication, Aareal Bank has set up a separate division within its organisation, which serves as a first point of contact for shareholders, other investors and analysts. The contact persons in Investor Relations can be found on the Aareal Bank website www.aareal-bank.com/en/investors-portal/equity-investors/contact/

Aareal Bank addresses shareholders and other stakeholders in a targeted manner via roadshow activities, actively seeking their opinions. The Chairman of the Supervisory Board is also available for talks with shareholders and other stakeholders, using her own roadshow activities to gather external opinions on the Bank's governance.

The Bank also holds an ordinary Annual General Meeting once a year. Shareholders are thus given the opportunity to actively participate in the development of the Company.

At the Annual General Meeting, the shareholders decide, in particular, on the formal approval of the members of the Supervisory Board and Management Board for the financial year under review, on the appropriation of any net retained profit, amendments to the Memorandum and Articles of Association, and authorisations on capital adjustments. The Annual General Meeting also elects the external auditors for the Company and decides who joins the Supervisory Board as shareholder representative.

The Company's shareholders may submit statements or proposals in writing, by fax or e-mail, to the Company. They may also request to speak at the Annual General Meeting. The shareholders may also submit counter or supplemental motions to the agenda items at the Annual General Meeting, so that they participate in structuring and influencing the meeting. The Management Board and the Supervisory Board refer to shareholders' comments made during the general debate, or to motions submitted by shareholders in advance, to respond to questions, or to comment on other contributions.

In certain situations, such as the current pandemic, the aforementioned may be legally limited or adapted to allow for an Annual General Meeting to take place adjusted to the respective situation.

Guidelines regarding the Selection of Members of the Management Board and the Supervisory Board

The Supervisory Board of Aareal Bank AG is satisfied that the Management Board and the Supervisory Board are adequately staffed, if all members are in a position to perform their duties (professional qualification), commit the time necessary to perform these and possess the integrity to be guided by the ethical principles of Aareal Bank when performing their duties (with respect to personal reliability, including conflicts of interest and independence aspects). The composition of the Supervisory Board and the Management Board, respectively, shall facilitate, in its entirety, cooperation and the widest possible diversity of opinions and knowledge (the concept of diversity).

The Supervisory Board has defined concrete requirements and processes to incorporate these criteria for the evaluation of Management Board and Supervisory Board members, as well as when selecting candidates for appointment to the Management Board, or for shareholder representatives to the Supervisory Board. When establishing these processes, it has taken into account the legal requirements of the German Public Limited Companies Act (Aktiengesetz – "AktG"), the German Banking Act (Kreditwesengesetz – "KWG") and of the German Corporate Governance Code. In addition, the regulatory guidelines of the European Central Bank and the European Banking Authority on adequacy and internal governance are also incorporated, as are corporate governance guidelines of consultants on share voting rights and major shareholders that are relevant to Aareal Bank. Besides the Supervisory Board, the European Central Bank also reviews the suitability of the respective candidates prior to taking up their duties, using the so-called "fit & proper" assessment.

Personal reliability

The principles of personal reliability apply equally for all members of the Management Board and the Supervisory Board. All members of the Management Board and the Supervisory Board should demonstrate honesty, integrity and independence of mind. They should live by the ethical principles of Aareal Bank, as set out in the Code of Conduct, and commit sufficient time to perform their duties. The Supervisory Board calculates the time commitment of every member of the Management Board and the Supervisory Board, and reviews on an annual basis whether they also dedicate sufficient time to exercising the mandate. In this connection, the Supervisory Board takes care to ensure compliance with the requirements for the maximum number of additional offices, pursuant to sections 25c (2) and 25d (3) of the KWG.

Conflicts of interest & independence

Acting in the interests of the Company means being able to make significant judgements unbiased by considerations irrelevant to the matter at hand. The Supervisory Board therefore attaches particular importance to the handling and disclosure of conflicts of interest or potential conflicts of interest that could, for example, call into question the independence of the Supervisory Board.

In its Conflicts of Interest Policy, the Supervisory Board has laid down procedures on how to prevent or handle potential conflicts of interest affecting members of the Management Board or the Supervisory Board. Specifically, the Policy provides that individual Management Board and Supervisory Board members must establish transparency even where there is only a potential conflict of interest. The members of the Supervisory Board and the Management Board have declared in writing that no conflicts of interest pursuant to recommendation E. 1 of the German Corporate Governance Code arose during the financial year under review. Any individual whose circumstances may give rise to a material conflict of interest that cannot be mitigated will be ineligible as a candidate.

The Supervisory Board also determines when the independence of one of its members is not ensured and carries out an annual review of whether the independence of individual members is no longer ensured, or may be compromised. In the event of the following circumstances, the Supervisory Board generally assumes that independence is not ensured:

- At the commencement of the fourth term of office as a member of the Supervisory Board of Aareal Bank AG ("general limitation to a member's maximum term of office"). The term of office begins with the election by the Annual General Meeting, excluding any judicial appointments.

- The period between membership in Aareal Bank AG's Management Board and membership in the Supervisory Board is less than five years.

- The period between being a senior manager at the first management level below the Management Board and membership in the Supervisory Board of Aareal Bank AG is less than three years.

- The period between working as or on behalf of a material consultant, auditor, or other service provider or client of Aareal Bank and membership in the Supervisory Board of Aareal Bank AG is less than three years.

- A Supervisory Board member is simultaneously associated with a major competitor, as a staff member, member of the Management or Supervisory Board; consultants to major competitors may also not be considered independent.

Furthermore, all Supervisory Board members are subject to the statutory limitations laid out in section 100 (2) nos. 2 to 4 of the AktG. Unlike the criteria listed above, the statutory limitations are mandatory, which means that they prevent the nomination of a potential candidate, or require the resignation of the affected board member.

Effective 31 December 2019, the Supervisory Board believes, taking the above criteria into account, that all shareholder representatives (Marija Korsch, Jana Brendel, Christof von Dryander, Richard Peters, Sylvia Seignette, Elisabeth Stheeman, Dietrich Voigtländer and Prof. Dr Hermann Wagner) are independent.

Professional qualification

Every member of an executive body must possess the knowledge, ability and experience to properly perform their duties. This means that they must at least be able to understand and assess the Company's material business activities and the associated material risks, the control and monitoring system established in this regard, as well as the corresponding accounting and financial reporting systems. This also requires being familiar with the underlying material legal requirements. The members of the Management Board are responsible for the duties of the entire Management Board as well as those of the sections assigned to them. Each member of the Supervisory Board must be in a position to perform the duties incumbent on the Supervisory Board in its entirety.

When chairing a committee, Supervisory Board members should possess extensive expertise in the topics covered by that committee. The Chairman of the Audit Committee, for example, must be an expert on financial reporting issues and internal control and monitoring systems, while the Chairman of the Risk Committee must be an expert in monitoring risks. Both committee chairmen may not hold the position of Chairman of the Supervisory Board.

Overall, with regard to its collective composition, the Supervisory Board further decided that the following additional expertise be adequately represented:

- Experience in sectors and financial markets which are material to Aareal Bank Group
- Digitalisation and transformation
- Strategic planning
- Design and assessment of risk management systems, internal control systems and corporate governance frameworks
- Accounting and audit matters

The curricula vitae of the members of the Management Board: www.aareal-bank.com/en/about-us/company-profile/the-management-board/ and the members of the Supervisory Board: www.aareal-bank.com/en/about-us/company-profile/supervisory-board/ can be found on the website.

Concept of diversity

In principle, the Management Board and the Supervisory Board pursue the objective in their bodies of ensuring maximum variety with regard to gender, age, internationality and professional diversity. Where there are several suitable candidates, further selection takes these aspects into account, to draw together the broadest possible spectrum of different perceptions in the interest of making the best possible decision for Aareal Bank. The Management Board ensures that these aspects of diversity are also taken into consideration at the management levels it controls, to facilitate succession oriented around this concept of diversity (please refer to relevant management duties/diversity). The Supervisory Board has set individual objectives for the aforementioned diversity aspects, for both itself and the Management Board, the implementation of which it presents annually. It understands these objectives as being minimum objectives; there is no reason why they cannot be exceeded.

Gender diversity

In accordance with the German Act on Equal Participation of Men and Women in Executive Positions in the Private and Public Sector, the Supervisory Board sets specific targets – including concrete implementation deadlines – for the share of female members on the Supervisory Board and the Management Board. Likewise, the Management Board defines such targets for the first two management levels below the Management Board. On the Supervisory Board, by 30 June 2022 at least 25 % of positions are to be held by women. The status quo is 41.66 %, unchanged from the previous year. On the Management Board, by 30 June 2022 at least 20 % of positions are to be held by women. The status quo is 33.33 %, unchanged from the previous year. Therefore, the minimum objectives set by the Supervisory Board have been achieved.

Age diversity

The Supervisory Board has set out targets for the age structure of the Management Board and the Supervisory Board, in order to safeguard the continuous development of both executive bodies. At the time of (re)election to the Supervisory Board, candidates should be less than 70 years old. Furthermore, the Supervisory Board should not consist exclusively of members who are older than 60 years. Members of the Management Board should not exceed the upper age limit of 65 years while serving on the Management Board. These objectives are currently met.

International profile

In addition, given Aareal Bank's international business activities, the Supervisory Board has set itself and the Management Board the goal of having the broadest possible international experience, which can be proven by foreign nationality or considerable professional experience gained in another country. For the Management Board, the figure is currently at 33 %, unchanged from the previous year, whilst the figure has increased to 33 % (2019: 25 %) for the Supervisory Board.

Diversity of professional skills

The Supervisory Board pursues the objective of maximum professional diversity when selecting the members of the Management Board and the Supervisory Board. However, the demanding professional requirements for members of the management board and the supervisory board of so-called "significant credit institutions" limit the opportunities for achieving this objective: for instance, regulatory rules require in principle that the members of the Management Board have extensive experience in the lending business and in risk management. In accordance with section 100 (5) of the AktG, the Management Board members in their entirety shall be familiar with the sector in which the Company operates. The Supervisory Board's aim of ensuring that not all members have gained most of their professional experience at a credit institution is currently met.

Election periods and dates ("staggered board")

To avoid a simultaneous outflow of considerable know-how, the Supervisory Board has set different election dates at which decisions are made about three groups of Supervisory Board members. The terms of office of Ms Korsch, Mr von Dryander, Mr Peters, and Ms Seignette run until the ordinary Annual General Meeting in 2023. All the other shareholder representatives' terms of office do not expire before the ordinary Annual General Meeting in 2024. Shareholder representatives' terms of office are only four years long, as a result of which a new resolution concerning some of the shareholder representatives must be taken at the latest every three years, bringing with it a possibility of renewing the Supervisory Board.

The terms of office for employee representatives continue to run for five years: the current representatives are therefore in office until the ordinary Annual General Meeting in 2025.

Regular evaluation of suitability and performance

The Executive and Nomination Committee evaluates the Management Board and Supervisory Board at least once a year. The evaluation consists of two components: the suitability test and the efficiency test. The evaluation is supported by external partners.

Within the scope of the evaluation, the Committee checks whether the Management Board and Supervisory Board members possess the necessary personal and professional requirements on the one hand, and whether requirements for the collective composition, including skills profiles and diversity concepts, are fulfilled on the other hand. Should this not be the case, the Executive and Nomination Committee submits proposals to the Supervisory Board as to how individual or collective suitability can be achieved. The Executive and Nomination Committee also assesses future trends and developments, and, at a minimum, suggests adequate training programmes for the two bodies, enabling them to deal with such trends and developments. This applies, for example, to information on digitalisation and on sustainability and non-financial risks (cf. the Report of the Supervisory Board), tailored to the needs of the Management Board and Supervisory Board.

Furthermore, the Executive and Nomination Committee takes the structure, size, composition, and performance of both bodies into consideration, including the results of a benchmark comparison conducted precisely for this reason. The assessment of structure, size, and composition is not restricted to the bodies as such, but also includes the Supervisory Board committees; it comprises an efficiency and effectiveness review of the cooperation within the Supervisory Board, between the committees and with the plenary meeting of the Supervisory Board, as well as between the committees, the Supervisory Board and the Management Board.

In addition to the regular annual evaluation, event-driven assessments may be conducted, should, for example, suspicions arise regarding insufficient individual or collective suitability, or should adequate composition of the Management Board and/or the Supervisory Board need to be reviewed due to a change in strategy.

Succession planning

The Executive and Nomination Committee is responsible for the succession planning of the Management Board and the shareholder representatives on the Supervisory Board. On an annual basis, the Committee reviews the established competence profile, and whether this is compatible with Aareal Bank's business and risk strategies, proposing any necessary adjustments. Furthermore, the Committee reviews, as part of the annual evaluation, whether the current members of the Management and Supervisory Boards fulfil the presently applicable criteria, taking the latest amendments into account. If this is not the case, the Committee suggests measures to the Supervisory Board to ensure that all criteria are fulfilled going forward. Such measures may include continuing education courses for individual or multiple Management or Supervisory Board members as well as changes in the composition of the Management or Supervisory Board.

Furthermore, at the beginning of every year, the Executive and Nomination Committee discusses personnel decisions due within the next two years, such as projected retirements, potential re-appointments, etc. Therefore, if the re-appointment of a Management or Supervisory Board member is not an option, the Executive and Nomination Committee concerns itself with a suitable successor more than one year in advance.

If changes in the composition of the Management or Supervisory Board have to be made, the Executive and Nomination Committee aims to fulfil the personal criteria, while at the same time promoting the fulfilment of the goals established in terms of board composition (collective competence profile and diversity). Succession planning for the Management Board is made in close cooperation with the Chairman of the Management Board. The Executive and Nomination Committee considers both internal and external candidates.

Aareal Bank has taken various measures to be able to respond to short-term personnel fluctuations (for example, due to resignation for personal reasons), and to identify suitable internal successors. For instance, the Bank can provide tailor-made development measures to senior managers in order to fundamentally prepare them to become a member of the Management Board. This includes, in particular, business development, risk management and accounting know-how as well as leadership skills. In addition, all Management Board members have first- and second-level responsibilities. This means that if the Management Board member with first-level responsibility is not available, his/her duties will be assumed by the respective Management Board member with second-level responsibility.

As a general rule, every competence required for the activities of Aareal Bank's Supervisory Board and its committees is represented by at least two Supervisory Board members. Hence, the Audit Committee comprises not only the respective Chair as a financial expert, but also at least one other person holding the same qualifications. In addition, in order to make sure there is a quorum even in the event of short-term changes in the composition of the respective committee, every committee comprises more than three members.

Composition of the Management Board and Supervisory Board

The members of the Supervisory Board and its committees, the respective chairmen and members of the Management Board and their relevant areas of responsibility, are presented below. As per the Supervisory Board's decision, the Management Board is comprised of six members. The Supervisory Board appoints one of the members as Chairman of the Management Board. In accordance with Aareal Bank AG's Memorandum and Articles of Association, the Supervisory Board consists of twelve members. Once elected by the Annual General Meeting, the members of the Supervisory Board elect a Chairman and two Deputy Chairmen from amongst them, for the duration of their term of office. Eight members are elected by shareholders at the Annual General Meeting. Four members are elected by employees, through the Group Works Council.

The committees comprise at least four members, while the Audit Committee and the Risk Committee comprise six members. The Chairman of the Supervisory Board belongs to every committee and assumes the position of risk management expert in the Remuneration Control Committee. According to the provisions of recommendation D. 4 of the German Corporate Governance Code as well as Aareal Bank's Guidelines for the selection of members of the Management Board and the Supervisory Board, the Audit Committee and the Risk Committee are chaired by independent experts. Additionally, care is also taken to avoid any interlinking of the committee members' positions, to ensure the mutual exchange of information.

Purchase or sale of the Company's shares

In 2020, members of the Company's executive bodies did not carry out any transactions involving the Company's shares, which would have required publication in accordance with the requirements of Article 19 of the EU Market Abuse Regulation (596/2014/EU), in conjunction with section 26 of the German Securities Trading Act (Wertpapierhandelsgesetz – "WpHG"). As set out on Aareal Bank AG's website, only one transaction by a family member of a Supervisory Board member took place. At the end of the financial year, aggregate shareholdings of members of executive bodies in the Company's shares were less than 1% of the issued share capital of Aareal Bank AG.

Please refer to Aareal Bank's website under www.aareal-bank.com/en/about-us/corporate-governance/managers-transactions/ for the notifications.

Accounting policies

Aareal Bank AG prepares the Group's accounts according to the International Financial Reporting Standards (IFRSs) as applicable in the European Union. The single-entity financial statements of Aareal Bank AG are prepared in accordance with the provisions of the German Commercial Code (Handelsgesetzbuch – "HGB"). The Management Board prepares the financial statements and management reports of Aareal Bank AG and Aareal Bank Group. The external auditors submit their report on the audit of the financial statements and the consolidated financial statements to the Supervisory Board, which also monitors their independence. The fees paid to the external auditors are shown in Note (38) to the financial statements. Permissible non-audit services provided by the external auditors must be approved beforehand by the Audit Committee of the Supervisory Board.

PricewaterhouseCoopers GmbH Wirtschaftsprüfungsgesellschaft (PwC), the auditors of the 2020 financial statements – as elected by the Annual General Meeting 2020 and instructed accordingly by the Supervisory Board – have exercised their audit activities under the management of Messrs Ralf Schmitz and Christian Rabeling. In line with the audit firm's internal regulations, their staff members rotate their audit mandates periodically – every five year in this case.

Mr Schmitz has audited Aareal Bank since 2018; Mr Rabeling, the responsible auditor, since 2019.

Please note that, due to the statutory rotation of external auditors, this was the final time (for now) that PricewaterhouseCoopers GmbH were appointed as external auditors for Aareal Bank AG.

Report of the Supervisory Board of Aareal Bank AG, Wiesbaden

Dear shareholders,

This annual report reflects the different ways in which the events of last year concern us all and led to diverse restrictions and new situations for you, dear shareholders, and for the companies and hence for Aareal Bank. In addition, Aareal Bank finds itself in a special situation due to the ill health of Hermann Merkens, our Chairman of the Management Board. Nonetheless, Aareal Bank can be proud of how superbly its management and employees have mastered these changes. This allowed the Bank to continue its operating business activities unrestricted during the lockdown in spring 2020, with virtually all of its staff working from home. The Management Board and the Works Council ensured well in advance that the Bank's workforce was sufficiently mobile. Regardless of this development, Aareal Bank has continued to operate successfully in its markets. It also conducted the sale of a partial stake in Aareon, among other things.

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 about 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 was also informed about compliance within the Company on a regular basis, and it received the reports prepared by Internal Audit. The Supervisory Board also received comprehensive reports on the development of the business segments, and on operative and strategic planning. Against the backdrop of the Covid-19 pandemic, the scope of reporting and the frequency with which we held meetings were intensified significantly. The Supervisory Board was involved in all material decisions made by Aareal Bank Group, also – and in particular – in monitoring the Aareal Next Level strategic framework and the event-driven review against the background of the Covid-19 pandemic and the process for the sale of a minority stake in Aareon AG. 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 in due time, and a decision taken. In cases where resolutions needed to be passed in periods between scheduled Supervisory Board meetings, such resolutions were passed by way of circulation or via conference calls or video calls.

Furthermore, between the individual meetings of the Supervisory Board, the Chairman of the Management Board, or his deputies, kept the Chairman of the Supervisory Board informed, on a continuous and regular basis, on all material developments of the Company. The Chairman of the Management Board, or his deputies, maintained close contact with the Chairman of the Supervisory Board, in order to discuss key issues and important decisions personally. The Chairman of the Supervisory Board then proceeded to inform the other Supervisory Board members of these discussions at the following Supervisory Board meetings. Due to Hermann Merkens's absence due to illness, discussions have since been held with his deputies on the Management Board, Marc Hess and Thomas Ortmanns.

Discussions were also held – on a weekly basis initially, then every two weeks and now monthly – between Aareal Bank's management and the Chairman of the Supervisory Board, the Risk Committee and the Audit Committee about the impact of the Covid-19 pandemic and how Aareal Bank was dealing with it. The chairmen of the Supervisory Board, and of the Risk Committee and the Audit Committee, also held various talks with the banking regulator's Joint Supervisory Team and presented the Supervisory Board's intensified corporate governance. The chairmen reported on the aforementioned discussions in their respective committees, in line with their respective areas of responsibility.

Activities of the Plenary Meeting of the Supervisory Board

Eighteen plenary meetings of the Supervisory Board were held in the year under review, also due to the developments arising from the global Covid-19 pandemic. During these meetings, the members of the Supervisory Board received the submitted reports and documents, as well as oral explanations, which were discussed in detail. Economic and market developments, also in view of and particularly against the background of the Covid-19 pandemic, the still large number of related adjustments to regulatory requirements, and the ongoing progress made in implementing the Aareal Next Level strategic programme were focal points of the work and reporting in all scheduled meetings.

This also included the measures taken by the Bank to counter these market developments. During the 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, Consulting/Services Bank and Aareon segments, focusing in particular on current economic developments. In addition, the Supervisory Board was informed about the business development of the entire Aareal Bank Group. At regular intervals, the Supervisory Board was informed of the Bank's liquidity status and the related steps taken by the Bank's Treasury division. The Management Board also reported regularly on the quality of the property financing portfolio against the background of market trends in the various property markets, with a particular emphasis placed on the effects of the Covid-19 pandemic. Within the scope of reporting, the regular reports prepared by the control functions – including Risk Controlling, Compliance, Internal Audit, Information Security & Data Protection, the Remuneration Officer, and Human Resources – were presented and discussed. At each plenary meeting of the Supervisory Board, the committee chairmen reported on the committee meetings that had taken place in the meantime.

The focal points of the individual meetings are outlined below.

- In two meetings in **January 2020,** the Supervisory Board addressed strategic questions and associated communications. It discussed the Aareal Next Level strategic programme, which was subsequently approved by the Management Board and communicated to the capital market.

- During its meeting at the **beginning of the year,** the Supervisory Board dealt with the Bank's dividend policy, the individual Management Board members' target achievement in the past financial year, and the setting of targets for the new financial year. Preparations were also made for the election of members to the Supervisory Board at the Annual General Meeting in May. Deliberations on the Supervisory Board elections continued during another meeting in March, together with the feedback and implementation proposals from the corporate governance roadshow. The Management Board members' targets were also dealt with.

- In the **March 2020** meeting, the Supervisory Board dealt in detail with the financial statements and consolidated financial statements presented for the 2019 financial year, and with the auditors' report. The relevant facts were presented in the Supervisory Board report for the previous year. Furthermore, the Supervisory Board discussed the non-financial report 2019 and the results of the audit going hand in hand with it, to obtain limited assurance. Another issue covered during the March meeting included preparations for the Annual General Meeting in May 2020. This comprised resolution proposals for the agenda of the Annual General Meeting, including the proposal for the appropriation of profit and the proposal regarding the selection of external auditors and election of Supervisory Board members. At the March meeting, the Management Board also presented the strategies pursuant to Minimum Requirements for Risk Management ("MaRisk") applicable to the Group in detail. According to their respective responsibilities, the strategies had previously been presented to the Executive and Nomination Committee, the Risk Committee, and the Audit Committee, and finally to the Supervisory Board, to subsequently be discussed with the Management Board in depth. The annual report submitted by Internal Audit, and their audit planning for the upcoming financial year as well as their mid-term plans were also discussed during the meeting. The Supervisory Board also concerned itself with the internal governance and the remuneration systems for employees and Management Board members; it came to the conclusion that the Company's remuneration systems are appropriate.

- During three meetings in **April 2020,** alongside discussions concerning Aareal Bank's first virtual Annual General Meeting, the Supervisory Board addressed in particular the agenda items of the Annual General Meeting, including the final proposal for candidates to be elected to the Supervisory Board, the introduction of different terms of office for Supervisory Board members, the handling of the supervisory authorities' recommendation on dividend policy, and the proposal on the appointment of the external auditors. External legal advisors were consulted, in particular with regard to the moratorium on dividend payments. The Supervisory Board agreed to permanently reduce the terms of office of Supervisory Board members to four years, and at the same time to introduce elections at different points in time. The Supervisory Board candidates especially strengthened the digitalisation and banking expertise on the Supervisory Board. As reported in the previous year, PricewaterhouseCoopers GmbH Wirtschaftsprüfungsgesellschaft, Frankfurt/Main, was proposed for the last time for the audit of the 2020 financial statements and the consolidated financial statements, due to the rotation requirements that are in place. KPMG AG Wirtschaftsprüfungsgesellschaft, Berlin, was proposed for any review of additional financial information after 31 December 2020 and up to the 2021 Annual General Meeting. In addition, the meeting in April also dealt with the already extended reporting on the effects of the Covid-19 pandemic.

- The launch of a process to sell a minority stake in Aareon was on the agenda of the Supervisory Board's first meeting in **May 2020.** The Supervisory Board's second meeting in May, which was held immediately after the Annual General Meeting, started with a review of the Annual General Meeting of Aareal Bank AG preceding the meeting. Following the conclusion of the Supervisory Board elections, the meeting also covered the election of the Chairman and Deputy Chairman of the Supervisory Board and its committees.

- Two Supervisory Board meetings were held in **June 2020.** These addressed the impact of the Covid-19 pandemic on Group planning and the intra-year forecast, including the assumed scenarios, and the Supervisory Board's governance. Organisational issues were also covered.

- The two-day Supervisory Board meeting in **July 2020** was held to comprehensively discuss Aareal Bank Group's strategy and refinements thereon, as well as to receive the Management Board's regular report. Issues concerning coping with the situation surrounding the Covid-19 pandemic were also added to this year's agenda. The Supervisory Board talked about the presented strategic initiatives and options with the Management Board in considerable depth and detail. Within this context, adjustments made to material risk documents were also presented and discussed.

- The meeting in **August 2020** dealt exclusively with the sale of a minority stake in Aareon AG. During the **September 2020** meeting, current questions concerning strategic initiatives, including a progress report on their implementation, were presented and discussed, in addition to the regular reports. Besides an update on Covid-19, these questions dealt with Aareon and Advent subsequent to the signing of the sale of a minority stake in August 2020, with the share price and shareholder structure, M&A and capital management, as well as with ESG topics. In this context, the event-driven review of the business and risk strategies, including the Risk Appetite Framework, were also discussed with the Supervisory Board.

- In the two meetings convened in **November 2020,** the Supervisory Board addressed the illness of the Chairman of the Management Board, Hermann J. Merkens. Based on consultations, all measures were agreed upon that would allow his responsibilities to be continued without interruption during the substitution phase. Since his absence as Chairman of the Management Board, the Supervisory Board convened on a weekly basis until year-end and, in coordination with Marc Hess and Thomas Ortmanns, is convinced of the Management Board's capacity to act. The Supervisory Board also dealt with the proposal to appoint a new Compliance Officer and approved the proposal.

- In the **December 2020** meeting, the Management Board prepared and presented the Corporate Governance Report, including the Corporate Governance Statement and the Declaration of Compliance. The latter was resolved and subsequently published on Aareal Bank AG's website. Furthermore, the annual review was carried out concerning Rules of Procedure for the Management Board and Supervisory Board, the individual and collective suitability and efficiency of the Management Board and Supervisory Board (annual evaluation), the review processes, and the Conflict of Interest Policy for members of the Company's executive bodies. The Supervisory Board discussed the results of the evaluation in detail and will incorporate the findings into its work. The Supervisory Board also concerned itself with the Management Board's preliminary target achievement 2020 and approved the targets for 2021.

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 members of the plenary meeting in detail.

To the extent that any Supervisory Board decisions were taken by way of circulation, the Supervisory Board received a report by the Management Board on the implementation of such decisions taken previously, at the subsequent Supervisory Board meeting.

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.

Activities of Supervisory Board Committees

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

Executive and Nomination Committee:

The Executive and Nomination Committee of the Supervisory Board convened for eleven meetings in the year under review. The Committee prepared the plenary meetings of the Supervisory Board in all its meetings and discussed Aareal Bank Group's strategic development with the Management Board at regular intervals. Regarding the agenda items within the responsibility of the Supervisory Board, the Committee convened without the Management Board. These meetings particularly included discussions regarding suitability requirements for Management Board and Supervisory Board members, the processes for reviewing these requirements, the targets for the composition of both executive bodies, and the results of the annual evaluation of Management Board and Supervisory Board. Consultations were also held in the year under review on the shareholder representatives nominated for election to the Supervisory Board. The Management Board was not present at these meetings.
As provided for in the Supervisory Board's Rules of Procedure, the employee representatives on the committee had no right to vote on this issue.

- At the meeting in **February 2020,** the Executive and Nomination Committee dealt with the Company's dividend policy and the selection of candidates for election to the Supervisory Board.

- The meetings in **March 2020** were used to continue selecting candidates and hence to prepare for the Annual General Meeting in May 2020. Information was also provided on the corporate governance roadshow held by the Chairman of the Supervisory Board. This comprised the resolution proposals for the agenda of the Annual General Meeting plus the introduction of different terms of office for Supervisory Board members. The meetings also dealt with any pending appointments to the Management Board in the next financial year, and thus with the topic of succession planning.

- The meetings in **April 2020** were also concerned with further preparations for the Annual General Meeting and corporate governance topics, including in particular discussions regarding the ECB's recommendation on the dividend policy. In **May 2020,** the Executive and Nomination Committee discussed in detail with the Management Board the current plans in relation to Aareon.

- The **June 2020** meeting was used to prepare for the Supervisory Board's strategy meeting. An intense discussion as regards the processes for the Management Board's general succession planning was also held. The Supervisory Board also advised on regulatory changes and the regular changes in the German Corporate Governance Code (GCGC) and their relevance for Aareal Bank.

- In **August 2020,** the sale of a minority stake in Aareon was discussed in detail with the Executive and Nomination Committee.

- The Executive and Nomination Committee meeting in **September 2020** was held to prepare for this year's evaluation and the selection of external auditors to this end. In addition, the strategy dialogue for the second half of the year 2020 was discussed. Current corporate governance developments and the implementation of the relevant changes in the GCGC were also advised on. As proposed by the GCGC, the Chairman of the Supervisory Board held an appropriate number of talks with investors in the year under review, exchanging views with them on Aareal Bank's corporate governance and informing Board members concerning the contents of these talks in subsequent meetings (see "Shareholder communication" below for details on the topics).

- At the **December 2020** meeting, the Executive and Nomination Committee carried out the annual review of the Rules of Procedure for the Management Board and Supervisory Board, the individual and collective suitability and efficiency of the Management Board and Supervisory Board (annual evaluation), the respective review processes, and the Conflict of Interest Policy for members of the Company's executive bodies – also considering the results of the written survey directed at all Management Board and Supervisory Board members regarding potential conflicts of interest in the past financial year. The members of the Management Board and Supervisory Board have declared in writing that no conflicts of interest within the meaning of the GCGC arose during the financial year under review.

Risk Committee:

The Risk Committee held six meetings during the year under review. It regularly discussed reports on the Bank's risk situation, which were submitted and explained by the Management Board. The risk reporting structure and frequency was extended with supplementary reports, relating specifically to the impact of the Covid-19 pandemic. 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, as well as reputational and IT risks. The Committee was also engaged with the analysis of Aareal Bank's risk-bearing capacity and its capital ratios. Also, detailed reports were provided regarding the Bank's liquidity status and management as well as its funding. Risks from existing investments, as well as all additional material risks were also presented.

The Risk Committee concerned itself with Aareal Bank's strategies and the derived sub-risk strategies, as well as with the risk management system. The Management Board also submitted detailed reports to the Risk 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. Within the scope of risk reporting, significant exposures were discussed in detail, and measures for the reduction of high-risk exposures presented and consulted within the Committee. The Risk Committee received a report on recovery planning and other risk management measures, which included preparations for the UK's exit from the EU after the end of the transition period on 31 December 2020 and the related ongoing consultations about an agreement between the UK and the European Union. The Management Board also informed the Risk Committee about all completed, ongoing and scheduled audits by the supervisory authorities at each Risk Committee meeting. In addition to regular reporting on the risk situation at each meeting, the following meetings had additional focal points on certain topics: The impact of current Covid-19 pandemic-related developments on the individual types of risk were examined in all meetings since March 2020.

- The Risk Committee meeting held in **March 2020** dealt with the results of the risk management system review performed by the external auditors, the supervisory authorities' focus in the 2020 financial year and other regulatory publications and amendments.

- In **April 2020,** the Risk Committee mainly addressed the non-financial risks of Aareal Bank Group, the risk culture report and specific credit risk management aspects.

- In **June 2020,** it dealt with the regular reporting as well as with the yearly reports of the individual risk management functions.

- At the **September 2020** meeting, the Management Board informed the Risk Committee about current recovery planning. Another focal point was the event-driven review of the business and risk strategies, in light of the Covid-19 pandemic.

- At the meeting in **October 2020,** individual aspects of the event-driven review of the risk strategies were dealt with in more detail, including the specific emphasis on the credit processes due to the Covid-19 pandemic. Issues concerning data and information security were also addressed.

- In its meeting in **December 2020,** the Risk Committee discussed the results of the Bank's annual risk inventory. The Committee monitored the terms in the client business, based on the business model and risk structure of the Bank, supported the Remuneration Control Committee in evaluating the effects of the remuneration systems on the Bank's risk, capital and liquidity situation, and checked whether the remuneration systems are aligned with the Bank's sustainable development and business strategy. Within this context, the Risk Committee also ensured that the derived risk strategies and the remuneration strategy are in line. The meeting in December also served to comprehensively review ESG risks, and the measures that are in place to manage these risks.

The Committee also concerned itself in all meetings with the banking and regulatory environment, focusing on current topics such as individual risk types during individual meetings. Furthermore, the Risk Committee dealt with the audits performed by the supervisory authorities, the findings these audits yielded, and the authorities' recommendations on risk-related topics in all meetings.

Audit Committee:

The Audit Committee held eight meetings during the year under review.

In accordance with the requirements of the GCGC, during its meetings in May, August and November 2020, the Audit Committee discussed with the Management Board the quarterly results to be published. Furthermore, the current status and planning of key management indicators in the financial year, and current reviews and projects at Aareal Bank were reported upon at the Audit Committee meetings. In its meetings, the Committee received reports submitted by Internal Audit and the Bank's Compliance Officer, requesting and receiving detailed explanations, and duly noting both reports. The Committee was also informed about the work carried out by Internal Audit and of the audit planning. The Head of Internal Audit attended all meetings, unless these were exclusively for the purpose of presenting the preliminary quarterly figures. The Committee dealt with the measures the Management Board had taken to address the findings identified by external auditors, Internal Audit and supervisory authorities, and had the Management Board report on the status and progress of their rectification. External auditor representatives, too, attended all meetings, excluding the agenda items regarding the assessment of financial statements auditing and the proposal for new external auditors. A regular update on the status of already approved and expected non-audit services provided by the external auditors was given at all meetings. The 70 % limit of approved non-audit services in relation to planned audit services was neither reached nor exceeded at any time. The latest impact of the Covid-19 pandemic on Aareal Bank Group's figures, including the underlying scenarios, have been discussed at all meetings since March 2020. The external auditor's assessment of this was also sought on several occasions.

- At its **February 2020** meeting, the preliminary figures for the 2019 financial year were submitted to the Audit Committee, and the dividend policy was discussed, among other things. In addition, the annual report 2019 and the audit planning of Internal Audit were presented.

- In **March 2020,** the Committee received the external auditors' report on the audit of the financial and consolidated financial statements for the 2019 financial year, and discussed the results with the auditors in detail. The Committee members discussed the contents of the audit reports provided; they formed their own judgement of the audit results on the basis of these reports, and by way of meetings held with the external auditors. Furthermore, the Chairman of the Audit Committee informed the meeting about his discussions with the external auditors outside the meetings. Without the external auditors being present, the Audit Committee discussed the agenda items regarding the assessment of financial statements auditing and the proposal for the external auditors for the 2020 financial year. As reported in the previous year, PricewaterhouseCoopers GmbH Wirtschaftsprüfungsgesellschaft, Frankfurt/Main, was proposed for the last time for the audit of the 2020 financial statements and the consolidated financial statements. The Committee also concerned itself with Aareal Bank Group's Sustainability Report and the audit undertaken to obtain limited assurance for this report. The report on compliance-related issues was also discussed.

- At its meeting in **May 2020,** the Audit Committee discussed the focal audit points determined by the Supervisory Board for the 2020 financial year.

- The compliance-related reporting, including the annual review of the Code of Conduct, was continued at the meeting in **June 2020.**

- In **August 2020,** the Audit Committee meeting focused on the interim financial report as at 30 June 2020, including the results of its review, and the approach for the audit of the financial statements and consolidated financial statements.

- The meeting in **September 2020** focused on the discussion of the impact of the Covid-19 pandemic on Group planning and the intra-year forecast, including the assumed scenarios, as well as the progress in preparing for the implementation of the requirements of the benchmark reform.

- At its **November 2020** meeting, the Audit Committee dealt with the preliminary figures for the financial year as at 30 September 2020.

- In its meeting in **December 2020,** the Audit Committee discussed the medium-term Group planning in detail with the Management Board. The external auditors also informed the committee about the results of the audit of the organisation of the lending business. The Audit Committee was also informed by the Management Board about the structure of sustainability reporting for the 2020 financial year. Furthermore, the Committee was regularly informed about the risk management system and the review of the Internal Control System, in accordance with legal requirements; it duly acknowledged the reports, following discussion.

Remuneration Control Committee:

The Remuneration Control Committee held eight meetings during the year under review. The Remuneration Officer, who attended every meeting, supported the Supervisory Board and the Remuneration Control Committee throughout the year under review.

Pursuant to the requirement set out in section 25d (12) of the KWG, which is reflected in the Rules of Procedure of Aareal Bank's Supervisory Board, the Management Board does not attend Remuneration Control Committee meetings which deal with Management Board remuneration. In the 2020 financial year, the Remuneration Control Committee held four meetings without the Management Board, and four with it.

During its six meetings, the Remuneration Control Committee discussed issues concerning the Bank's remuneration systems and all related matters, fulfilling its original assignment. For this purpose, and to the extent considered necessary, external legal and remuneration advisors were retained to provide support. The Committee supported the plenary meeting of the Supervisory Board in monitoring the inclusion of internal control units and of all other material divisions in designing the remuneration systems, and assessed the effects of the remuneration systems on the Bank's risk, capital and liquidity situation. Moreover, the Remuneration Control Committee supported the Supervisory Board with all issues related to the remuneration of the Management Board. As a rule, support was provided to the Supervisory Board by preparing the corresponding recommendations.

- At the beginning of the year under review, the Committee dealt with the Management Board's target achievement for the 2019 financial year and with determining the Management Board targets for 2020.

- In **March 2020,** the Committee finalised the assessment of the appropriate structure of the remuneration systems for the Management Board and employees. The results of the penalty review for employees and the Management Board were also presented, as was the review of the overall amount of variable remuneration as to legal permissibility, pursuant, inter alia, to section 7 of the InstVergV.

- The Remuneration Control Committee meeting in **June 2020** focused on the completed implementation of the comments which the supervisory authorities had made regarding the remuneration system, as well as on how Covid-19 impacted on the remuneration of the Management Board and employees.

- The Remuneration Control Committee continued its deliberations about the impact of Covid-19 on the remuneration of the Management Board and employees in **September 2020** and **November 2020.**

- In the two meetings in **December 2020,** the Remuneration Control Committee dealt with the Management Board's preliminary target achievement for 2020 and determined the Management Board targets for 2021. Regulatory issues were also discussed.

Technology and Innovation Committee:

The Technology and Innovation Committee convened for four scheduled meetings in the year under review, during which the Committee discussed the implementation and further development of the digitalisation strategy, market trends, technological developments and innovation trends in detail, especially with a view to clients of the Consulting/Services Bank and Aareon segments. Potential business opportunities arising from the growing digitalisation of business processes – and how these can be put to use by Aareal Bank Group, and especially for its clients – were explained by the employees of the Bank and respective subsidiaries responsible for the development, among others.

Further key aspects of regular discussions were issues relating to the security and flexibility of IT systems provided and used within the Bank, as well as the current realignment of banking systems and successes already achieved here, such as the introduction of S4/HANA and the associated adjustments to the new requirements in the areas of accounting, regulation, and cybersecurity. The IT strategy, budget planning and the monitoring and progress of important IT projects were also discussed.

Member of the Supervisory Board	Participation in plenary meetings	Quota	Participation in committee meetings	Quota	Number of meetings attended / number of meetings*
Marija Korsch	18/18	100%	37/37	100%	55/55
Richard Peters	18/18	100%	26/26	100%	44/44
Klaus Novatius*	18/18	100%	19/19	100%	37/37
Jana Brendel	8/9	89%	6/7	86%	14/16
Thomas Hawel*	18/18	100%	4/4	100%	22/22
Petra Heinemann-Specht*	18/18	100%	11/11	100%	29/29
Jan Lehmann*	9/9	100%	3/3	100%	12/12
Dr Hans-Werner Rhein	9/9	100%	8/8	100%	17/17
Prof. Dr Stephan Schüller	9/9	100%	10/11	91%	19/20
Sylvia Seignette	18/18	100%	6/6	100%	24/24
Elisabeth Stheeman	18/18	100%	10/10	100%	28/28
Hans-Dietrich Voigtländer	18/18	100%	20/20	100%	38/38
Christof von Dryander	9/9	100%	16/16	100%	25/25
Prof. Dr Hermann Wagner	18/18	100%	19/19	100%	37/37
Beate Wollmann*	9/9	100%	3/3	100%	12/12

* Plenary and committee meetings; ** Employee representative

External experts were invited to the meetings for selected topics, to present current developments from an independent perspective, and to discuss their potential impact on Aareal Bank, or how they can be taken on board by the Bank.

Attendance of Supervisory Board members at plenary and committee meetings:

Where members of the Supervisory Board were unable to attend a meeting, they announced their absence in advance, giving reasons. Attendance of Supervisory Board members at meetings is shown in the table below.

Financial Statements and Consolidated Financial Statements

The Supervisory Board instructed PricewaterhouseCoopers GmbH Wirtschaftsprüfungsgesellschaft, Frankfurt/Main, who were elected as auditors by the Annual General Meeting 2020, with the audit of the financial statements and the consolidated 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 GmbH Wirtschaftsprüfungsgesellschaft audited the financial statements prepared in accordance with the German Commercial Code ("HGB") and the consolidated financial statements prepared in accordance with IFRSs, as well as the Management Report and the Group Management Report. Based on the results of their audit, PricewaterhouseCoopers GmbH Wirtschaftsprüfungsgesellschaft issued an unqualified audit opinion for the financial statements and consolidated financial statements.

All members of the Supervisory Board received the audit reports, including all annexes thereto, in good time before the meeting during which the financial statements and the consolidated financial statements were discussed. Having examined the documents provided, the Supervisory Board members formed their own judgement of the audit results. The external auditor representatives attended the meeting of the Supervisory Board, during which the financial statements and consolidated financial statements were discussed, and gave a detailed account of the results of their audit. The representatives of PricewaterhouseCoopers GmbH Wirtschaftsprüfungsgesellschaft were then 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, the consolidated financial statements as well as the Group Management Report prepared in accordance with IFRSs, the proposal of the Management Board regarding the appropriation of profit, and the audit reports, were all examined in detail. No objections were raised to the audit results. In its meeting on 25 March 2021, the Supervisory Board approved the results of the audit. The Supervisory Board thus confirmed the financial statements of Aareal Bank AG (in accordance with the HGB), and approved the consolidated financial statements (in accordance with IFRSs). The Supervisory Board examined and discussed with the Management Board its proposal regarding the appropriation of profit. On the basis of this discussion, the Supervisory Board endorsed the proposal for the appropriation of profit submitted by the Management Board, which is oriented on the ECB's recommendations.

Non-financial Report

The Audit Committee and the Supervisory Board concerned themselves with sustainability issues and related reporting during their meetings on 19 and 24 March 2020, 23 September 2020 and on 10 and 16 December 2020.

Moreover, during its meeting on 23 March 2021, the Audit Committee of the Supervisory Board discussed the separate combined non-financial report for 2020 and the result of PricewaterhouseCoopers's audit of that report. Representatives of the external auditors attended this Audit Committee meeting and reported on material results of their commercial review in accordance with ISAE 3000 (revised), undertaken to obtain limited assurance for this report. They answered supplementary questions from Committee members. The Audit Committee conducted a plausibility check of the audit results submitted by PricewaterhouseCoopers, and presented its assessment of the non-financial report (and its analysis of PricewaterhouseCoopers's audit results) to the Supervisory Board. The Audit Committee also issued a recommendation to the Supervisory Board to concur with the results of the audit conducted by PricewaterhouseCoopers. The Supervisory Board followed this recommendation; in its meeting on 25 March 2021, it summarised its examination by stating that it had no objections concerning the non-financial report and the results of the audit conducted by PricewaterhouseCoopers.

Communication with Shareholders

In her function as Chairman of the Supervisory Board, Ms Korsch held discussions with shareholder representatives concerning corporate governance at Aareal Bank. Ms Korsch presented the topics within the responsibility of the Supervisory Board, such as the composition of the Management Board and the Supervisory Board, the remuneration systems for Management Board and Supervisory Board members, the role of the Supervisory Board in the strategy development and implementation process as well as its involvement in environmental, social and governance (ESG) matters, the election of the auditor and succession planning.

Personnel matters

The following personnel changes were made to the Supervisory Board during the reporting period: Six shareholder representatives – Elisabeth Stheeman, Sylvia Seignette, Dietrich Voigtländer, Prof. Dr Hermann Wagner, Jana Brendel and Christof von Dryander – were elected to the Supervisory Board. Prof. Dr Stephan Schüller and Dr Hans Werner

Rhein resigned from the Supervisory Board at the Annual General Meeting.

We would like to thank Prof. Dr Stephan Schüller and Dr Hans Werner Rhein for their enriching and constructive cooperation on the Supervisory Board of Aareal Bank.

Employee representative Ms Beate Wollmann resigned from the Supervisory Board at the Annual General Meeting. The Supervisory Board would also like to express its thanks for her outstanding commitment and constructive work. She is succeeded by Jan Lehmann, who was appointed by Aareon as employee representative to the Supervisory Board.

No personnel changes were made with regard to the Management Board in 2020.

Due to the illness of the Chairman of the Management Board, Hermann J. Merkens, the Executive and Nomination Committee and the plenary meeting convened to discuss the situation and take measures to ensure the management's operational capacity. Taking the situation into account, the already communicated substitutional regulations were put into effect.

The Supervisory Board sincerely regrets that Mr Merkens is currently unable to perform his duties for health-related reasons, and wish him a swift recovery.

On 12 March 2021, Mr Merkens announced that his absence due to ill health will last longer than originally expected and communicated on 8 November 2020. Whether and when Mr Merkens will be able to return to his duties cannot be reliably predicted at this point. The substitution regulations described will remain in force. Due to the uncertainties surrounding the recovery of Mr Merkens, the Supervisory Board has decided to expedite the search for a successor, which it has initiated as a precautionary measure, alongside an analysis of the size and composition of the Management Board, as communicated during the annual press conference on 24 February 2021.

Training and Continuous Professional Development

The Supervisory Board members made use of the training and continuous professional development measures offered and required for their task at their own account. Aareal Bank AG supported them in an appropriate manner. An internal introductory programme, specifically aligned to the members newly elected to the Supervisory Board by the Annual General Meeting 2020, was conducted and external training measures structured and provided, to familiarise them with their new role and hence with the mandate. These measures included individual continuous professional development and information events organised by the external auditor elected by the Annual General Meeting.

Aareal Bank's onboarding process for new members of the Company's executive bodies aims to impart deeper knowledge of the business specifics, the strategy, risk management, accounting, and material legal provisions of Aareal Bank. Alongside external training and continuous professional development measures, more than 20 internal discussions were held with the heads of division of the internal control units, of Finance & Controlling, Group Strategy, the business divisions, the Chairman of the Management Board of Aareon AG, and with the Management Board members and chairmen of the Supervisory Board committees. To ensure the transition to the Supervisory Board work runs as seamlessly as possible, this onboarding process started already before the candidates were elected by the Annual General Meeting, while respecting confidentiality measures. Comprehensive knowledge about Aareal Bank was imparted before the candidates elected by the Annual General Meeting attended their first committee meetings.

Furthermore, continuous professional development measures take place on a regular basis within the course of Supervisory Board meetings. This is typically a two-stage process. In a first meeting, trends or legal or regulatory changes in particular are reported on in the abstract, and their impact on Aareal Bank Group outlined. The specific implementation is presented in a next meeting. Adjustments made during the year are referred to in later reports. The committees also address relevant topics in more depth in their own meetings. In 2020, these included for example two meetings of the Risk Committee with an in-depth analysis of current regulatory developments and of reporting and monitoring instruments that were expanded specifically due to the Covid-19 pandemic. The requirements for addressing non-financial risks and their treatment at Aareal Bank Group represented another focal point.

In addition to its regular meetings, the Supervisory Board convened for a separate informational meeting, during which auditors Pricewaterhouse-Coopers provided detailed information on current changes and deliberations within the regulatory and legal framework, as well as on the potential impact of such trends upon Aareal Bank.

In conclusion, the Supervisory Board would like to thank the Management Board and all of the Group's employees for the dedication, tremendous commitment and flexibility they have shown during the past 2020 financial year. With this continued commitment, strong motivation and persistence, all Group employees have not only contributed to the Company's seamless transition to working from home, allowing day-to-day operations to continue unrestricted. They have also successfully handled the special challenges, while at the same time setting the course for the future, for example, with the important work carried out on the IT infrastructure under special circumstances. This visibly demonstrated the great team spirit that defines Aareal Bank.

Frankfurt/Main, March 2021

For the Supervisory Board

Marija Korsch

Marija Korsch (Chairman)

Offices

Wiesbaden Head Office

Aareal Bank AG
Paulinenstrasse 15
65189 Wiesbaden, Germany
Phone: +49 611 3480
Fax: +49 611 3482549

Structured Property Financing

Dublin
Torquay Road
Foxrock Village
Dublin D18 A2N7, Ireland
Phone: +353 1 6369220
Fax: +353 1 6702785

Istanbul
Ebulula Mardin Caddesi
Maya Meridyen Iş Merkezi
D:2 Blok · Kat. 11
34335 Akatlar-Istanbul, Turkey
Phone: +90 212 3490200
Fax: +90 212 3490299

London
6th Floor, 6,7,8 Tokenhouse Yard
London EC2R 7AS, UK
Phone: +44 20 74569200
Fax: +44 20 79295055

Madrid
Paseo de la Castellana, 41, 4º
28046 Madrid, Spain
Phone: +34 915 902420
Fax: +34 915 902436

Moscow
Business Centre ”Mokhovaya“
4/7 Vozdvizhenka Street
Building 2
125009 Moscow, Russia
Phone: +7 499 2729002
Fax: +7 499 2729016

New York
Aareal Capital Corporation
360 Madison Avenue, 18th Floor
New York, NY 10017, USA
Phone: +1 212 5084080
Fax: +1 917 3220285

Paris
29 bis, rue d'Astorg
75008 Paris, France
Phone: +33 1 44516630
Fax: +33 1 42662498

Rome
Via Mercadante, 12/14
00198 Rome, Italy
Phone: +39 06 83004200
Fax: +39 06 83004250

Singapore
Aareal Bank Asia Limited
3 Church Street
17-03 Samsung Hub
Singapore 049483, Singapore
Phone: +65 6372 9750
Fax: +65 6536 8162

Stockholm
Norrmalmstorg 14
11146 Stockholm, Sweden
Phone: +46 8 54642000
Fax: +46 8 54642001

Warsaw
RONDO 1 · Rondo ONZ 1
00-124 Warsaw, Poland
Phone: +48 22 5380060
Fax: +48 22 5380069

Wiesbaden
Paulinenstrasse 15
65189 Wiesbaden, Germany
Phone: +49 611 3482950
Fax: +49 611 3482020

Aareal Estate AG
Paulinenstrasse 15
65189 Wiesbaden, Germany
Phone: +49 611 3482446
Fax: +49 611 3483587

Banking & Digital Solutions

Aareal Bank AG
Banking & Digital Solutions
Paulinenstrasse 15
65189 Wiesbaden, Germany
Phone: +49 611 3482967
Fax: +49 611 3482499

Banking & Digital Solutions
Berlin Branch
SpreePalais
Anna-Louisa-Karsch-Strasse 2
10178 Berlin, Germany
Phone: +49 30 88099444
Fax: +49 30 88099470

Banking & Digital Solutions
Essen Branch
Alfredstrasse 220
45131 Essen, Germany
Phone: +49 201 81008100
Fax: +49 201 81008200

Banking & Digital Solutions
Rhine-Main Branch
Paulinenstrasse 15
65189 Wiesbaden, Germany
Hotline: +49 611 3482000
Fax: +49 611 3483002

Aareal First Financial Solutions AG
Isaac-Fulda-Allee 6
55124 Mainz, Germany
Phone: +49 6131 4864500
Fax: +49 6131 486471500

Deutsche Bau- und Grundstücks-Aktiengesellschaft
Lievelingsweg 125
53119 Bonn, Germany
Phone: +49 228 5180
Fax: +49 228 518298

plusForta GmbH
Talstrasse 24
40217 Düsseldorf, Germany
Phone: +49 211 5426830
Fax: +49 211 54268330

Aareon

Aareon AG
Isaac-Fulda-Allee 6
55124 Mainz, Germany
Phone: +49 6131 3010
Fax: +49 6131 301419

Glossary

Ad-hoc disclosure
Pursuant to Article 17 of the MAR (Market Abuse Regulation), issuers of financial instruments are obliged to publish any information that may have an impact on the price of these instruments without delay. This obligation is discharged using so-called ”ad-hoc” disclosures which may relate to the issuer's financial position and performance, or to its general business operations. The ad-hoc disclosure obligation applies in Germany as well as in other major financial centres; it is designed to prevent insider trading.

Advanced Internal Ratings-Based Approach (AIRBA)
Under the ”Advanced Approach”, banks are allowed to use their internal rating procedures to gain an assessment of the credit quality for the supervisory measurement of risk-weighted assets (RWAs).

Associated enterprise (associate)
An enterprise which is accounted for in the consolidated financial statements using the equity method (as opposed to full or partial consolidation), over whose business or financial policies an entity included in the consolidated financial statements exercises significant influence.

Basel III/IV
”Basel III” denotes the regulatory framework for banks, promulgated by the Basel Committee on Banking Supervision at the Bank for International Settlements (BIS) with the objective of stabilising the banking sector. The Basel III regulations, finalised in December 2017, are generally known as ”Basel IV”.

Bonds
Generic term for fixed-income securities or debt securities.

Capital ratios
Common Equity Tier 1 ratio (CET 1 ratio) =

$$\frac{\text{Common Equity Tier 1 (CET 1)}}{\text{Total risk exposure amount (RWAs)}} \times 100\,\%$$

Tier 1 ratio (T1 ratio) =

$$\frac{\text{Tier 1 capital (T1)}}{\text{Total risk exposure amount (RWAs)}} \times 100\,\%$$

Total capital ratio (TC ratio) =

$$\frac{\text{Total capital (TC)}}{\text{Total risk exposure amount (RWAs)}} \times 100\,\%$$

Commercial Mortgage Backed Securities (CMBS)
Bonds backed by loans collateralised by commercial and multi-family properties.

Consolidated statement of cash flows
Statement showing the cash flows an enterprise has generated and used during a financial year, from its operating, investment and financing activities, together with the cash and cash equivalents at the beginning and end of the financial year.

Corporate governance
Corporate governance denotes the legal and factual framework for the management and governance of enterprises. The recommendations of the German Corporate Governance Code safeguard transparency and are designed to strengthen confidence in good and responsible corporate governance. They predominantly serve to protect shareholders' interests.

Cost/Income ratio (CIR)
Financial indicator expressing the ratio of expenses to income within a given reporting period.

CIR =

$$\frac{\text{Administrative expenses}}{\begin{array}{c}\text{Net interest income + net commission income}\\ \text{+ net derecognition gain/loss + net gain/loss from financial}\\ \text{instruments fvpl + net gain/loss from hedge accounting}\\ \text{+ net gain/loss from investments accounted for using the}\\ \text{equity method + net other operating income/expenses}\end{array}}$$

In line with common practice in the banking sector, bank levy and contributions to the deposit guarantee scheme are not included in administrative expenses.

Covered bonds
”Covered” bonds is a generic term for debt securities covered by collateral. In Germany, covered bonds are mainly issued in the form of ”Pfandbriefe”

pursuant to the German Pfandbrief Act (PfandBG), which provides a legal framework for collateralisation (assets eligible for Pfandbrief cover include mortgages and public-sector loans).

Credit Risk Standard Approach (CRSA)
The CRSA is applied, provided no advanced approach (AIRBA) to assess the credit risk exposure exists, or has been approved.

Deferred taxes
Income taxes payable or receivable in the future, due to temporary differences between the carrying amounts of assets and liabilities in the IFRS statement of financial position and the tax accounts. At the time of recognition, deferred tax assets or liabilities do not yet constitute any actual claims on, or liabilities to the tax authorities.

Derivatives
Derivatives – which include all types of forwards, futures, options and swaps – are financial instruments whose value is derived from the price (and/or the price fluctuations) of an underlying instrument, such as equities, bonds or currencies.

Earnings per share (EpS)
Earnings per ordinary share: financial indicator expressing the ratio of net income after non-ontrolling interest income to the average number of common shares outstanding.

$$\text{Earnings per share} = \frac{\text{Operating profit/loss ./. income taxes ./. consolidated net income attributable to non-controlling interests ./. AT1 coupon (net)}}{\text{Number of common shares}}$$

EBIT margin

$$\text{BIT margin} = \frac{\text{EBIT (operating profit before interests)}}{\text{Sales revenues}}$$

Effective interest method
Method for amortising the mark-up/mark-down between cost and the nominal value (premium/discount), using the effective yield of a financial asset or liability.

Equity method
Method for measuring shareholdings in enterprises on whose business policy the reporting entity has significant influence ("associates"). When applying the equity method, the associate's pro-rata net income/loss is recognised in the carrying amount of the shareholding; any distributions are recognised via a corresponding pro-rata reduction in the carrying amount.

EURIBOR
European Interbank Offered Rate – the interest rate at which prime European banks offer euro deposits (with fixed terms of one week, and between one and twelve months) to one another.

Fair value
The fair value is the amount for which an asset can be exchanged (or a liability settled) between knowledgeable, willing parties in an arm's length transaction; this is often identical to the market price.

Fair value hedge
Using a swap to hedge the market risk of a balance sheet item with a fixed interest rate (e.g. a receivable or a security); this is measured at fair value.

Financial assets (fvoci)
Financial assets measured at fair value, whose change in value is recognised directly in equity via other reserves (fvoci = fair value through other comprehensive income).

Financial assets/liabilities (ac)
Financial instruments measured by applying the effective interest method at amortised cost (ac = amortised cost). The financial instrument is measured at the amount at which it was initially recognised, minus principal repayments, plus or minus the cumulative amortisation of any premium or discount, and minus any reduction for impairment or non-collectability. The effective interest method amortises the mark-up/mark-down between cost and nominal value (premium/discount) over a residual term.

Financial assets/liabilities (fvpl)
Financial instruments measured at fair value, whose change in value is recognised in income (fvpl = fair value through profit or loss).

Financial instruments
Generic term for loans extended and other receivables, fixed-income securities, equities, shareholdings, liabilities, and derivatives.

FX
Abbreviation for foreign exchange.

Goodwill
The amount which the buyer of an enterprise pays over the fair value of assets less liabilities (the net asset value), taking expected future income into account (the fully-capitalised earnings value).

Hedge accounting
Concept describing the recognition (or other form of accounting) of two or more financial instruments, which together form a hedging relationship. In this context, the relationship between these contracts is based on the equal and opposite specification of contractual elements giving rise to risks (usually financial risks). Given these specifications, such agreements can be used to partially or fully offset and neutralise risks. In the context of hedge accounting, one of the contracts involved (specifically, the contract establishing the risk(s) concerned) is referred to as the ”underlying transaction”, and the other contract (the one entered into to hedge the risk(s) of the underlying transaction) as the ”hedge transaction” or just ”hedge”.

Impairment
An impairment within the scope of determining loss allowance.

International Financial Reporting Standards (IASs/IFRSs)
IFRSs comprise International Accounting Standards (IASs) and interpretations issued by the Standing Interpretations Committee, as well as International Financial Reporting Standards (IFRSs) and related interpretations published by the International Accounting Standards Board (IASB).

LIBOR
London Interbank Offered Rate; the interest rate at which prime London banks offer deposits to one another.

Liquidity Coverage Ratio (LCR)
A Basel III indicator designed to assess liquidity risk.

Loan-to-value ratio (LTV)
The ratio of loan amount to property value, in the context of property loans.

MDAX
The MDAX® mid-cap index comprises the shares of 60 companies from traditional sectors listed in Deutsche Börse’s Prime Standard segment that, in terms of market capitalisation and exchange turnover, rank immediately below the companies included in the DAX® blue-chip index.

Minimum Requirements for Risk Management (MaRisk)
The Minimum Requirements for Risk Management in Banks (MaRisk) are binding requirements for the structure of risk management in German banks, as promulgated by the German Federal Financial Supervisory Authority (BaFin).

Money and capital markets
Markets for short, medium- and long-term investments and borrowing in different forms, such as debt securities or promissory note loans.

Mortgage Pfandbriefe
Debt securities issued by Pfandbrief issuers (Pfandbrief banks), which are collateralised by mortgages with a maximum mortgage lending value ratio of 60 %.

Option
The right to buy or sell a specific asset.

Other Comprehensive Income (OCI)
Other reserves. Equity sub-item, in which the following effects are recognised directly: the reserve from remeasurements of defined benefit plans, the reserve from the measurement of equity and debt instruments at fair value through other com-

prehensive income, the hedging reserve, the reserve from changes in the value of foreign currency basis spreads, and the currency translation reserve.

Over the counter (OTC)
Financial markets term for off-exchange trading between market participants.

Present value
The present value of a future cash flow, determined by discounting all future cash flows (inflows and outflows) to today's date.

Profit-participation rights
Profit-participation rights are a hybrid of equity and debt. Their creditors' rights are subordinated to those of other creditors, whilst their interest claim takes precedence over the profit entitlements of shareholders.

Public-Sector Pfandbriefe
Debt securities issued by Pfandbrief issuers (Pfandbrief banks), which are collateralised by claims against the public sector.

Purchased or originated credit impaired (POCI)
Financial assets which had already defaulted at the time of acquisition.

Repo or reverse repo transaction (repurchase transaction)
Short-term money-market transaction collateralised by securities.

Return on equity (RoE)
Financial indicator expressing the ratio of net income (or pre-tax profit, for example) to average equity over the period. RoE expresses the return on the capital employed by the company (and its owners/shareholders).

$$\text{RoE before taxes} = \frac{\text{Operating profit ./. consolidated net income attributable to non-controlling interests ./. AT1 coupon}}{\text{Average equity (IFRS) excluding non-controlling interests, other reserves, AT1 bond and dividends}}$$

$$\text{RoE after taxes} = \frac{\text{Operating profit ./. income taxes ./. consolidated net income attributable to non-controlling interests ./. AT1 coupon (net)}}{\text{Average equity (IFRS) excluding non-controlling interests, other reserves, AT1 bond and dividends}}$$

Risk-weighted assets (RWAs)
Risk-weighted assets are determined by multiplying the exposure value of a counterparty credit risk position with the risk weight assigned to the borrower.

Segment reporting
Shows financial information of segments which are material for management, and their contribution to the consolidated net income.

Swap
Generic term for contracts to exchange cash flows, such as the exchange of fixed-rate and variable-rate cash flows in the same currency (interest rate swap), or the exchange of cash flows and/or nominal amounts in different currencies (cross-currency swap).

Swaption
Option to enter into a swap agreement: the right to enter into a swap at a specific point in time, at interest rates and terms agreed upon at the outset.

Value-at-risk (VaR)
Method to quantify risks: it measures the maximum potential future loss which will not be exceeded within a defined period, and given a certain probability.

Financial Calendar

11 May 2021	Publication of results as at 31 March 2021
18 May 2021	Annual General Meeting
12 August 2021	Publication of results as at 30 June 2021
11 November 2021	Publication of results as at 30 September 2021

Imprint

Contents:
Aareal Bank AG, Group Communications
Concept/Text editor Magazine "New perspectives":
Commpark, Liederbach am Taunus
Concept/Design Magazine "New perspectives":
LIGALUX GmbH, Hamburg
Concept/Design Digital Annual Report:
die firma . experience design GmbH, Wiesbaden
Layout Annual Report:
S/COMPANY · Die Markenagentur GmbH, Fulda
Photographs:
© istockphoto / CHUNYIP WONG (p. 5);
Easyturn (p. 10+11); StockByM (p. 13); Rawpixel (p. 12+13);
Danila Shtantsov (p. 16); Diversity Studio (p. 20+21);
ollo (p. 22+23); shironosov (p. 22); baranozdemir (p. 25);
stockfour (p. 25); pixelfit (p. 26); Volodymyr Kalyniuk (p. 26);
nd3000 (p. 28+29); nimis69 (p. 30); IGphotography (p. 31);
fizkes (p. 32, 38, 48+49, 52); stockfour (p. 34); lechatnoir (p. 34);
golero (p. 36); Maryna Andriichenko (p. 41); anyaberkut (p. 44, 47);
StockRocket (p. 47); AvigatorPhotographer (p. 52)
© gettyimages / Westend61 (p. 11, 18); Alexander Spatari (p. 22)
© Adobe Stock / olezzo (p. 50+51)
© Andreas Schlote (p. 17, 37, 48+49)
© Sören Kunz (illustrations p. 8, 23, 24, 26+27, 30+31,
33, 35, 39, 41, 42+43, 46, 50+51, 53, 54+55, 58)
© Uwe Nölke (p. 58)
© Carolin Kuhaupt (p. 32, 40)
© Jörg Puchmüller (p. 42)
© Aareal Bank AG (p. 51)
© Aareal Bank AG/Pond5 (p. 6)

Use this QR code to access the online version of our Group Annual Report 2020:
ar2020.aareal-bank.com

Aareal Bank AG
Investor Relations
Paulinenstrasse 15 · 65189 Wiesbaden, Germany
Phone: +49 611 348 3009
Fax: +49 611 348 2637

www.aareal-bank.com

Aareal Bank Group

03/2021

Aareal

YOUR COMPETITIVE ADVANTAGE.